

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2023

OR

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

For the transition period from to

Commission File Number: 001-40526

CONFLUENT, INC.

(Exact Name of Registrant as Specified in its Charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

**899 W. Evelyn Avenue
Mountain View, California**

(Address of principal executive offices)

47-1824387

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

94041

(Zip Code)

Registrant's telephone number, including area code: (800) 439-3207

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Class A Common Stock, par value \$0.00001 per share	CFLT	The Nasdaq Stock Market LLC (Nasdaq Global Select Market)

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

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

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

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

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

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

As of July 26, 2023, there were 211,915,403 shares of the registrant's Class A common stock and 90,506,212 shares of the registrant's Class B common stock, each with a par value of \$0.00001 per share, outstanding.

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SPECIAL NOTE ABOUT FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements about us and our industry that involve substantial risks and uncertainties. All statements other than statements of historical fact contained in this Quarterly Report on Form 10-Q, including statements regarding our future results of operations and financial condition, business strategy and plans, and objectives of management for future operations, are forward-looking statements. In some cases, you can identify forward-looking statements because they contain words such as “anticipate,” “believe,” “contemplate,” “continue,” “could,” “estimate,” “expect,” “intend,” “may,” “plan,” “potential,” “predict,” “project,” “should,” “target,” “toward,” “will,” “would,” or the negative of these words or other similar terms or expressions. These forward-looking statements include, but are not limited to, statements concerning the following:

- our expectations regarding our revenue, revenue mix, expenses, and other results of operations;
- our ability to acquire new customers and successfully retain existing customers;
- our ability to increase consumption of our offering and expand features and functionalities;
- our ability to achieve or sustain our margins and profitability;
- the impact of, and our ability to operate our business and effectively manage our growth under evolving and uncertain macroeconomic conditions, such as high inflation and recessionary environments;
- future investments in our business, our anticipated capital expenditures, and our estimates regarding our capital requirements;
- the costs and success of our sales and marketing efforts and our ability to promote our brand;
- our growth strategies;
- the estimated addressable market opportunity;
- our reliance on key personnel and our ability to identify, recruit, and retain skilled personnel;
- our ability to effectively manage our growth, including international expansion;
- our ability to protect our intellectual property rights and any costs associated therewith;
- the effects of the COVID-19 pandemic or other public health crises;
- our ability to compete effectively with existing competitors and new market entrants; and
- the growth rates of the markets in which we compete.

We caution you that the foregoing list may not contain all of the forward-looking statements made in this Quarterly Report on Form 10-Q.

Forward-looking statements are based on our management’s beliefs and assumptions and on information currently available. These forward-looking statements are subject to a number of known and unknown risks, uncertainties and assumptions, including risks described in the section titled “Risk Factors” and elsewhere in this Quarterly Report on Form 10-Q. Other sections of this Quarterly Report on Form 10-Q may include additional factors that could harm our business and financial performance. Moreover, we operate in a very competitive and rapidly changing environment. New risk factors emerge from time to time, and it is not possible for our management to predict all risk factors nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ from those contained in, or implied by, any forward-looking statements.

You should not rely upon forward-looking statements as predictions of future events. We cannot assure you that the events and circumstances reflected in the forward-looking statements will be achieved or occur. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance, or achievements. Except as required by law, we undertake no obligation to update publicly any forward-looking statements for any reason after the date of this report or to conform these statements to actual results or to changes in our expectations. You should read this Quarterly Report on Form 10-Q and the documents that we reference in this Quarterly Report on Form 10-Q and have filed as exhibits to this report with the understanding that our actual future results, levels of activity, performance, and achievements may be materially different from what we expect. We qualify all of our forward-looking statements by these cautionary statements.

In addition, statements that “we believe” and similar statements reflect our beliefs and opinions on the relevant subject. These statements are based upon information available to us as of the filing date of this Quarterly Report on Form 10-Q, and while we believe such information forms a reasonable basis for such statements, such information may be limited or incomplete, and our statements should not be read to indicate that we have conducted an exhaustive inquiry into, or review of, all potentially available relevant information. These statements are inherently uncertain and investors are cautioned not to unduly rely upon these statements.

Where You Can Find More Information

Investors and others should note that we may announce material business and financial information to our investors using our Investor Relations website (investors.confluent.io), our filings with the Securities and Exchange Commission (“SEC”), webcasts, press releases, public conference calls, and blogs published on our website. We use these mediums, including our website, to communicate with investors and the general public about our company, our products, and other issues. It is possible that the information that we make available on our website may be deemed to be material information. We therefore encourage investors and others interested in our company to review the information that we make available on our website.

We also use our Twitter, LinkedIn, and Facebook accounts as a means of disclosing material non-public information and for complying with our disclosure obligations under Regulation FD. The information we post through these social media channels may be deemed material. Accordingly, investors should monitor these accounts, in addition to following our SEC filings, webcasts, press releases, public conference calls, and blogs published on our website. This list may be updated from time to time. The information we post through these channels is not a part of this Quarterly Report on Form 10-Q. These channels may be updated from time to time on our investor relations website.

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS (UNAUDITED)

Confluent, Inc.
Condensed Consolidated Balance Sheets
(in thousands, except share and per share data)
(unaudited)

	June 30, 2023		December 31, 2022
ASSETS			
Current assets:			
Cash and cash equivalents	\$ 312,643	\$	435,781
Marketable securities	1,534,912		1,491,044
Accounts receivable, net	188,705		178,188
Deferred contract acquisition costs	39,180		35,883
Prepaid expenses and other current assets	64,218		57,229
Total current assets	2,139,658		2,198,125
Property and equipment, net	43,599		29,089
Operating lease right-of-use assets	11,870		29,478
Goodwill and intangible assets, net	45,814		-
Deferred contract acquisition costs, non-current	67,533		68,401
Other assets, non-current	19,166		19,756
Total assets	\$ 2,327,640	\$	2,344,849
LIABILITIES AND STOCKHOLDERS' EQUITY			
Current liabilities:			
Accounts payable	\$ 2,459	\$	21,439
Accrued expenses and other liabilities	112,495		105,331
Operating lease liabilities	7,618		7,375
Deferred revenue	300,786		290,185
Total current liabilities	423,358		424,330
Operating lease liabilities, non-current	21,394		25,136
Deferred revenue, non-current	27,187		32,644
Convertible senior notes, net	1,086,389		1,084,500
Other liabilities, non-current	7,926		8,762
Total liabilities	1,566,254		1,575,372
Commitments and contingencies (Note 9)			

	June 30, 2023	December 31, 2022
Stockholders' equity:		
Preferred stock, par value of \$0.00001 per share; 10,000,000 shares authorized as of June 30, 2023 and December 31, 2022; 0 shares issued and outstanding as of June 30, 2023 and December 31, 2022	-	-
Class A common stock, par value of \$0.00001 per share; 1,000,000,000 shares authorized as of June 30, 2023 and December 31, 2022; 210,903,270 and 172,483,134 shares issued and outstanding as of June 30, 2023 and December 31, 2022, respectively	2	2
Class B common stock, par value of \$0.00001 per share; 500,000,000 shares authorized as of June 30, 2023 and December 31, 2022; 90,774,951 and 116,901,046 shares issued and outstanding as of June 30, 2023 and December 31, 2022, respectively	1	1
Additional paid-in capital	2,228,574	1,980,335
Accumulated other comprehensive loss	(9,806)	(9,456)
Accumulated deficit	(1,457,385)	(1,201,405)
Total stockholders' equity	761,386	769,477
Total liabilities and stockholders' equity	\$ 2,327,640	\$ 2,344,849

See accompanying notes to the condensed consolidated financial statements.

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2023	2022	2023	2022
Revenue:				
Subscription	\$ 176,488	\$ 127,018	\$ 337,055	\$ 240,938
Services	12,797	12,389	26,532	24,608
Total revenue	189,285	139,407	363,587	265,546
Cost of revenue:				
Subscription	44,188	35,608	87,093	69,211
Services	13,732	13,901	28,971	26,075
Total cost of revenue	57,920	49,509	116,064	95,286
Gross profit	131,365	89,898	247,523	170,260
Operating expenses:				
Research and development	85,677	64,472	170,567	122,133
Sales and marketing	127,770	112,754	256,394	219,456
General and administrative	36,343	29,979	71,698	57,460
Restructuring and other related charges	943	-	34,325	-
Total operating expenses	250,733	207,205	532,984	399,049
Operating loss	(119,368)	(117,307)	(285,461)	(228,789)
Other income, net	17,610	1,186	32,795	370
Loss before income taxes	(101,758)	(116,121)	(252,666)	(228,419)
Provision for income taxes	1,667	1,510	3,314	2,199
Net loss	\$ (103,425)	\$ (117,631)	\$ (255,980)	\$ (230,618)
Net loss per share, basic and diluted	\$ (0.35)	\$ (0.42)	\$ (0.87)	\$ (0.84)
Weighted-average shares used to compute net loss per share, basic and diluted	297,827,200	278,268,980	294,862,197	275,593,362

See accompanying notes to the condensed consolidated financial statements.

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2023	2022	2023	2022
Net loss	\$ (103,425)	\$ (117,631)	\$ (255,980)	\$ (230,618)
Other comprehensive loss, net of tax:				
Net unrealized loss on marketable securities	(5,574)	(4,005)	(1,415)	(8,717)
Net unrealized gain on derivative instruments	222	-	1,065	-
Other comprehensive loss, net of tax	(5,352)	(4,005)	(350)	(8,717)
Total comprehensive loss	\$ (108,777)	\$ (121,636)	\$ (256,330)	\$ (239,335)

See accompanying notes to the condensed consolidated financial statements.

Confluent, Inc.
Condensed Consolidated Statements of Stockholders' Equity
(in thousands, except share data)
(unaudited)

Three Months Ended June 30, 2023							
	Class A and Class B Common Stock			Additional Paid-In Capital	Accumulated Other Comprehensive Loss	Accumulated Deficit	Total Stockholders' Equity
	Shares	Amount					
Balances as of April 1, 2023	295,378,610	\$ 3	\$ 2,103,262	\$ (4,454)	\$ (1,353,960)	\$ 744,851	
Vesting of early exercised options	-	-	629	-	-	629	
Issuance of common stock upon exercise of vested options	3,645,882	-	26,714	-	-	26,714	
Vesting of restricted stock units	2,653,729	-	-	-	-	-	
Stock-based compensation	-	-	97,969	-	-	97,969	
Other comprehensive loss, net of tax	-	-	-	(5,352)	-	(5,352)	
Net loss	-	-	-	-	(103,425)	(103,425)	
Balances as of June 30, 2023	301,678,221	\$ 3	\$ 2,228,574	\$ (9,806)	\$ (1,457,385)	\$ 761,386	
Three Months Ended June 30, 2022							
	Class A and Class B Common Stock			Additional Paid-In Capital	Accumulated Other Comprehensive Loss	Accumulated Deficit	Total Stockholders' Equity
	Shares	Amount					
Balances as of April 1, 2022	278,036,762	\$ 3	\$ 1,703,449	\$ (5,542)	\$ (861,841)	\$ 836,069	
Issuance of common stock upon early exercise of unvested options	14,584	-	-	-	-	-	
Repurchases of unvested options	(121,867)	-	-	-	-	-	
Vesting of early exercised options	-	-	3,093	-	-	3,093	
Issuance of common stock upon exercise of vested options	2,610,173	-	8,634	-	-	8,634	
Vesting of restricted stock units	873,994	-	-	-	-	-	
Stock-based compensation	-	-	70,464	-	-	70,464	
Other comprehensive loss, net of tax	-	-	-	(4,005)	-	(4,005)	
Net loss	-	-	-	-	(117,631)	(117,631)	
Balances as of June 30, 2022	281,413,646	\$ 3	\$ 1,785,640	\$ (9,547)	\$ (979,472)	\$ 796,624	

Six Months Ended June 30, 2023							
	Class A and Class B Common Stock		Additional Paid-In Capital	Accumulated Other Comprehensive Loss	Accumulated Deficit	Total Stockholders' Equity	
	Shares	Amount					
Balances as of January 1, 2023	289,384,180	\$ 3	\$ 1,980,335	\$ (9,456)	\$ (1,201,405)	\$ 769,477	
Repurchases of unvested options	(30,828)	-	-	-	-	-	
Vesting of early exercised options	-	-	1,904	-	-	1,904	
Issuance of common stock upon exercise of vested options	7,241,647	-	47,983	-	-	47,983	
Vesting of restricted stock units	4,368,636	-	-	-	-	-	
Issuance of common stock under employee stock purchase plan	714,586	-	17,172	-	-	17,172	
Stock-based compensation	-	-	181,180	-	-	181,180	
Other comprehensive loss, net of tax	-	-	-	(350)	-	(350)	
Net loss	-	-	-	-	(255,980)	(255,980)	
Balances as of June 30, 2023	301,678,221	\$ 3	\$ 2,228,574	\$ (9,806)	\$ (1,457,385)	\$ 761,386	

Six Months Ended June 30, 2022							
	Class A and Class B Common Stock		Additional Paid-In Capital	Accumulated Other Comprehensive Loss	Accumulated Deficit	Total Stockholders' Equity	
	Shares	Amount					
Balances as of January 1, 2022	271,801,882	\$ 3	\$ 1,599,962	\$ (830)	\$ (748,854)	\$ 850,281	
Issuance of common stock upon early exercise of unvested options	59,185	-	-	-	-	-	
Repurchases of unvested options	(130,845)	-	-	-	-	-	
Vesting of early exercised options	-	-	8,794	-	-	8,794	
Issuance of common stock upon exercise of vested options	7,636,738	-	25,039	-	-	25,039	
Vesting of restricted stock units	1,311,869	-	-	-	-	-	
Issuance of common stock under employee stock purchase plan	734,817	-	22,485	-	-	22,485	
Stock-based compensation	-	-	129,360	-	-	129,360	
Other comprehensive loss, net of tax	-	-	-	(8,717)	-	(8,717)	
Net loss	-	-	-	-	(230,618)	(230,618)	
Balances as of June 30, 2022	281,413,646	\$ 3	\$ 1,785,640	\$ (9,547)	\$ (979,472)	\$ 796,624	

See accompanying notes to the condensed consolidated financial statements.

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

	Six Months Ended June 30,	
	2023	2022
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	\$ (255,980)	\$ (230,618)
Adjustments to reconcile net loss to cash used in operating activities:		
Depreciation and amortization	6,378	3,060
Net (accretion) amortization of (discounts) premiums on marketable securities	(19,721)	236
Amortization of debt issuance costs	1,889	1,883
Amortization of deferred contract acquisition costs	21,537	17,395
Non-cash operating lease costs	2,184	4,475
Lease abandonment charges	15,667	-
Stock-based compensation, net of amounts capitalized	171,448	126,235
Deferred income taxes	10	26
Other	851	559
Changes in operating assets and liabilities, net of effects of a business combination:		
Accounts receivable	(11,293)	(12,462)
Deferred contract acquisition costs	(23,966)	(22,723)
Prepaid expenses and other assets	(6,057)	(20,121)
Accounts payable	(18,720)	7,452
Accrued expenses and other liabilities	7,552	1,756
Operating lease liabilities	(3,754)	(4,910)
Deferred revenue	5,143	39,254
Net cash used in operating activities	<u>(106,832)</u>	<u>(88,503)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Capitalization of internal-use software costs	(9,886)	(4,765)
Purchases of marketable securities	(999,764)	(1,167,362)
Maturities of marketable securities	975,383	370,659
Purchases of property and equipment	(1,355)	(2,071)
Cash paid for a business combination, net of cash acquired	(45,802)	-
Net cash used in investing activities	<u>(81,424)</u>	<u>(803,539)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from issuance of common stock upon exercise of vested options	48,272	24,383
Proceeds from issuance of common stock upon early exercise of unvested options	-	416
Repurchases of unvested options	(223)	(695)
Payments of debt issuance costs for convertible senior notes	-	(786)
Proceeds from issuance of common stock under employee stock purchase plan	17,172	22,485
Net cash provided by financing activities	<u>65,221</u>	<u>45,803</u>
Effect of exchange rate changes on cash, cash equivalents, and restricted cash	(103)	(26)
Net decrease in cash, cash equivalents, and restricted cash	<u>(123,138)</u>	<u>(846,265)</u>
Cash, cash equivalents, and restricted cash at beginning of period	435,781	1,376,682
Cash, cash equivalents, and restricted cash at end of period	<u>\$ 312,643</u>	<u>\$ 530,417</u>

	Six Months Ended June 30,	
	2023	2022
Reconciliation of cash, cash equivalents, and restricted cash within the condensed consolidated balance sheets to the amounts shown above:		
Cash and cash equivalents	\$ 312,643	\$ 529,667
Restricted cash included in other assets, current	-	750
Total cash, cash equivalents, and restricted cash	<u>\$ 312,643</u>	<u>\$ 530,417</u>
Supplementary cash flow disclosures:		
Cash paid for:		
Income taxes	\$ 3,979	\$ 2,225
Non-cash investing and financing activities:		
Stock-based compensation capitalized as internal-use software costs	\$ 9,732	\$ 3,125
Vesting of early exercised stock options	\$ 1,904	\$ 8,794

See accompanying notes to the condensed consolidated financial statements.

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

1. Organization and Description of Business

Description of Business

Confluent, Inc. (“Confluent” or the “Company”) created a data infrastructure platform focused on data in motion. Confluent’s platform allows customers to connect their applications, systems, and data layers and can be deployed either as a self-managed software offering, Confluent Platform, or as a fully-managed cloud-native software-as-a-service (“SaaS”) offering, Confluent Cloud. Confluent also offers professional services and education services. The Company was incorporated in the state of Delaware in September 2014 and is headquartered in California with various other global office locations.

2. Basis of Presentation and Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) and applicable rules and regulations of the U.S. Securities and Exchange Commission (“SEC”) regarding interim financial reporting. Certain information and note disclosures normally included in the financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. Therefore, these condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes included in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2022, as filed with the SEC on February 28, 2023 (the “Annual Report”).

In management’s opinion, the unaudited condensed consolidated financial statements have been prepared on a basis consistent with the annual consolidated financial statements and reflect all adjustments, which include only normal recurring adjustments, necessary for the fair statement of the Company’s financial position as of June 30, 2023 and the results of operations and cash flows for the three and six months ended June 30, 2023 and 2022. The results of operations for the three and six months ended June 30, 2023 are not necessarily indicative of the results to be expected for the full year or any other future interim or annual period.

The condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

Reclassifications

Certain amounts in the prior year condensed consolidated financial statements have been reclassified to conform to the presentation of the current year consolidated financial statements. These reclassifications had no effect on consolidated net loss, stockholders’ equity, or cash flows as previously reported.

Use of Estimates

The preparation of the condensed consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Such estimates include, but are not limited to, the standalone selling price for each distinct performance obligation included in customer contracts, deferred contract acquisition costs and their period of benefit, valuation of stock-based awards, the fair value of acquired intangible assets, capitalization and estimated useful life of internal-use software, the incremental borrowing rate used to measure operating lease liabilities, and accounting for income taxes.

The Company bases its estimates on historical and anticipated results, trends, and various other assumptions that it believes are reasonable under the circumstances. Estimates and assumptions about future events and their effects, including the impact of global macroeconomic conditions, cannot be determined with certainty and therefore require the exercise of judgment. Actual results could differ from those estimates and any such differences may be material to the Company's condensed consolidated financial statements.

Significant Accounting Policies

Other than the policies described below, there were no significant changes to the Company's significant accounting policies disclosed in "Note 2 – Basis of Presentation and Summary of Significant Accounting Policies" of the Company's Annual Report.

Business Combinations

When the Company acquires a business, the purchase consideration is allocated to the tangible and intangible assets acquired and liabilities assumed at their estimated acquisition date fair values. The excess of the purchase consideration over the fair value of assets acquired and liabilities assumed, if any, is recorded as goodwill. Determining the fair value of intangible assets requires the use of estimates including, but not limited to, time and resources required to recreate the assets acquired. The Company's estimates of fair value are based upon assumptions believed to be reasonable, but which are inherently uncertain and unpredictable and, as a result, actual results may differ from estimates. During the measurement period, which may be up to one year from the acquisition date, the Company may record adjustments to the fair values of assets acquired and liabilities assumed, with the corresponding offset to goodwill. Upon the conclusion of the measurement period, any subsequent adjustments are recorded in the condensed consolidated statement of operations.

Impairment of Goodwill, Intangible Assets, and Other Long-Lived Assets

The Company evaluates the recoverability of long-lived assets, including property and equipment, operating lease right-of-use assets, and acquired intangible assets, for possible impairment whenever events or circumstances indicate that the carrying amount of such assets may not be fully recoverable. Recoverability of these assets is measured by a comparison of the carrying amounts to the undiscounted future cash flows the assets are expected to generate. If the carrying amount exceeds the undiscounted future cash flows, the carrying amount of such assets is reduced to fair value. There were no impairment charges related to long-lived assets during the three and six months ended June 30, 2023 and 2022.

Goodwill is not amortized but rather tested for impairment at least annually or whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Goodwill impairment is recognized when the quantitative assessment results in the carrying value of the reporting unit exceeding its fair value, in which case an impairment charge is recorded to the extent the carrying value exceeds the fair value, limited to the amount of goodwill. There were no goodwill impairment charges during the three and six months ended June 30, 2023.

Recent Accounting Pronouncements

Recently Adopted Accounting Pronouncements

Acquired Contract Assets and Contract Liabilities: In October 2021, the FASB issued ASU No. 2021-08, *Business Combinations (Topic 805): Accounting for Contract Assets and Contract Liabilities from Contracts with Customers*, which requires contract assets and contract liabilities acquired in a business combination to be recognized and measured by the acquirer on the acquisition date in accordance with ASC 606, *Revenue from Contracts with Customers*, as if it had originated the contracts. This guidance is effective for the Company for the year beginning January 1, 2023. The Company adopted this guidance as of January 1, 2023 on a prospective basis and the adoption did not have a material impact on its condensed consolidated financial statements.

3. Marketable Securities

The following tables summarize the fair values of the Company's marketable securities (in thousands):

	June 30, 2023			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. treasury securities	\$ 924,413	\$ 28	\$ (4,706)	\$ 919,735
U.S. agency obligations	412,422	-	(3,891)	408,531
Corporate notes and bonds	170,102	1	(1,693)	168,410
Commercial paper	38,290	1	(55)	38,236
Total marketable securities	<u>\$ 1,545,227</u>	<u>\$ 30</u>	<u>\$ (10,345)</u>	<u>\$ 1,534,912</u>

	December 31, 2022			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. treasury securities	\$ 1,033,587	\$ 68	\$ (4,072)	\$ 1,029,583
U.S. agency obligations	273,804	17	(3,570)	270,251
Corporate notes and bonds	160,208	9	(2,375)	157,842
Commercial paper	33,526	-	(158)	33,368
Total marketable securities	<u>\$ 1,501,125</u>	<u>\$ 94</u>	<u>\$ (10,175)</u>	<u>\$ 1,491,044</u>

The following tables summarize the fair values and unrealized losses of the Company's marketable securities, classified by the length of time that the securities have been in a continuous unrealized loss position (in thousands):

	June 30, 2023					
	Less than 12 Months		12 Months or Greater		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. treasury securities	\$ 786,455	\$ (3,844)	\$ 51,480	\$ (862)	\$ 837,935	\$ (4,706)
U.S. agency obligations	353,803	(2,960)	52,728	(931)	406,531	(3,891)
Corporate notes and bonds	108,503	(1,174)	58,505	(519)	167,008	(1,693)
Commercial paper	20,286	(55)	-	-	20,286	(55)
Total	\$ 1,269,047	\$ (8,033)	\$ 162,713	\$ (2,312)	\$ 1,431,760	\$ (10,345)

	December 31, 2022					
	Less than 12 Months		12 Months or Greater		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. treasury securities	\$ 566,093	\$ (2,892)	\$ 167,817	\$ (1,180)	\$ 733,910	\$ (4,072)
U.S. agency obligations	201,846	(2,014)	51,595	(1,556)	253,441	(3,570)
Corporate notes and bonds	90,287	(1,259)	65,579	(1,116)	155,866	(2,375)
Commercial paper	33,368	(158)	-	-	33,368	(158)
Total	\$ 891,594	\$ (6,323)	\$ 284,991	\$ (3,852)	\$ 1,176,585	\$ (10,175)

The Company does not intend to sell these securities and it is more likely than not that the Company will hold these securities until maturity or a recovery of the cost basis. The Company determined that the decline in fair value of these securities was not due to credit-related factors, and no allowance for expected credit losses was recorded as of June 30, 2023 and 2022. Realized gains and losses were not material for the three and six months ended June 30, 2023 and 2022.

The following table summarizes the contractual maturities of the Company's marketable securities (in thousands):

	June 30, 2023	
	Amortized Cost	Fair Value
Due within one year	\$ 1,121,569	\$ 1,115,659
Due after one year through five years	423,658	419,253
Total	\$ 1,545,227	\$ 1,534,912

4. Fair Value of Financial Instruments

The following tables summarize the Company's financial assets and liabilities that are measured at fair value on a recurring basis (in thousands):

	June 30, 2023		
	Level 1	Level 2	Total
Assets:			
Cash equivalents:			
Money market funds	\$ 246,569	\$ -	\$ 246,569
Commercial paper	-	4,964	4,964
Marketable securities:			
U.S. treasury securities	-	919,735	919,735
U.S. agency obligations	-	408,531	408,531
Corporate notes and bonds	-	168,410	168,410
Commercial paper	-	38,236	38,236
Derivative instruments:			
Foreign currency forward contracts	-	2,032	2,032
Total assets	\$ 246,569	\$ 1,541,908	\$ 1,788,477
Liabilities:			
Derivative instruments:			
Foreign currency forward contracts	\$ -	\$ 605	\$ 605
Total liabilities	\$ -	\$ 605	\$ 605
December 31, 2022			
	Level 1	Level 2	Total
Assets:			
Cash equivalents:			
Money market funds	\$ 367,699	\$ -	\$ 367,699
U.S. treasury securities	-	12,971	12,971
U.S. agency obligations	-	2,000	2,000
Marketable securities:			
U.S. treasury securities	-	1,029,583	1,029,583
U.S. agency obligations	-	270,251	270,251
Corporate notes and bonds	-	157,842	157,842
Commercial paper	-	33,368	33,368
Derivative instruments:			
Foreign currency forward contracts	-	672	672
Total assets	\$ 367,699	\$ 1,506,687	\$ 1,874,386
Liabilities:			
Derivative instruments:			
Foreign currency forward contracts	\$ -	\$ 19	\$ 19
Total liabilities	\$ -	\$ 19	\$ 19

The Company classifies its highly liquid money market funds within Level 1 of the fair value hierarchy because they are valued based on quoted market prices in active markets. The Company classifies its U.S. treasury securities, U.S. agency obligations, corporate notes and bonds, commercial paper, and foreign currency forward contracts within Level 2 of the fair value hierarchy because they are valued using inputs other than quoted prices that are directly or indirectly observable in the market, including readily available pricing sources for the identical underlying security that may not be actively traded. There were no transfers of financial instruments between valuation levels during the three and six months ended June 30, 2023 and 2022.

As of June 30, 2023 and December 31, 2022, the total estimated fair value of the Company's 0% convertible senior notes due 2027 was \$913.2 million and \$837.3 million, respectively. The fair value was determined based on the quoted price of the convertible senior notes in an inactive market on the last trading day of the reporting period and is classified within Level 2 of the fair value hierarchy. See Note 8 for further information on the Company's convertible senior notes.

5. Derivative Instruments and Hedging

In December 2022, the Company began entering into foreign currency forward contracts to manage its exposure to certain foreign currency exchange risks. Derivative instruments that hedge the exposure to variability in expected future cash flows are designated as cash flow hedges. The Company records changes in the fair value of these derivatives as a component of accumulated other comprehensive income (loss) ("AOCI") and subsequently reclassifies the related gains or losses into cost of revenue or operating expense in the same period, or periods, during which the hedged transaction affects earnings. Derivative instruments that hedge the exposure to variability in the fair value of assets or liabilities are not designated as hedges for financial reporting purposes. The Company records changes in the fair value of these derivatives in other income (expense), net in the condensed consolidated statements of operations. The Company's derivative instruments generally have maturities of 13 months or less. The Company does not use derivative instruments for trading or speculative purposes.

The following table summarizes the notional amounts of the Company's derivative instruments (in thousands):

	June 30, 2023	December 31, 2022
Foreign currency forward contracts designated as hedging instruments	\$ 60,517	\$ 96,097
Foreign currency forward contracts not designated as hedging instruments	86,645	-
Total derivative instruments	\$ 147,162	\$ 96,097

The Company has master netting agreements with each of its counterparties, which permit net settlement of multiple, separate derivative contracts with a single payment. The Company does not have collateral requirements with any of its counterparties. Although the Company is allowed to present the fair value of derivative instruments on a net basis according to master netting arrangements, the Company has elected to present its derivative instruments on a gross basis in the condensed consolidated financial statements. The following table summarizes the fair value of the Company's derivative instruments on the condensed consolidated balance sheets (in thousands):

	Balance Sheet Location	June 30, 2023	December 31, 2022
Derivative Assets:			
Foreign currency forward contracts designated as hedging instruments	Prepaid expenses and other current assets	\$ 819	\$ 672
Foreign currency forward contracts not designated as hedging instruments	Prepaid expenses and other current assets	1,213	-
Total derivative assets		\$ 2,032	\$ 672
Derivative Liabilities:			
Foreign currency forward contracts designated as hedging instruments	Accrued expenses and other liabilities	\$ 279	\$ 19
Foreign currency forward contracts not designated as hedging instruments	Accrued expenses and other liabilities	326	-
Total derivative liabilities		\$ 605	\$ 19

The following table presents the activity of foreign currency forward contracts designated as hedging instruments and the impact of these derivatives on AOCI (in thousands):

	Three Months Ended June 30, 2023		Six Months Ended June 30, 2023	
Beginning balance	\$	1,024	\$	653
Net gain recognized in other comprehensive income		222		1,065
Net gain reclassified from AOCI to earnings		(706)		(1,178)
Ending balance	\$	540	\$	540

As of June 30, 2023, net unrealized gains included in the balance of accumulated other comprehensive loss related to foreign currency forward contracts designated as hedging instruments was \$0.5 million, all of which the Company expects to reclassify from accumulated other comprehensive loss into earnings over the next 12 months.

The following table summarizes the effect of foreign currency forward contracts on the condensed consolidated statements of operations (in thousands):

	Three Months Ended June 30, 2023		Six Months Ended June 30, 2023	
	Derivatives Designated as Hedging Instruments	Derivatives Not Designated as Hedging Instruments	Derivatives Designated as Hedging Instruments	Derivatives Not Designated as Hedging Instruments
Cost of revenue - subscription	\$ 89	\$ -	\$ 133	\$ -
Cost of revenue - services	60	-	108	-
Research and development	140	-	199	-
Sales and marketing	318	-	581	-
General and administrative	99	-	157	-
Other income, net	-	11	-	87
Total gains recognized in earnings	\$ 706	\$ 11	\$ 1,178	\$ 87

6. Balance Sheet Components

Property and Equipment, Net

The cost and accumulated depreciation and amortization of property and equipment were as follows (in thousands):

	June 30, 2023		December 31, 2022	
Computers, equipment, and software	\$	9,862	\$	8,794
Furniture and fixtures		903		977
Leasehold improvements		380		458
Capitalized internal-use software costs		32,725		25,639
Construction in progress		17,935		5,404
Property and equipment, at cost	\$	61,805	\$	41,272
Less: Accumulated depreciation and amortization		(18,206)		(12,183)
Property and equipment, net	\$	43,599	\$	29,089

Depreciation and amortization expense was \$3.2 million and \$1.8 million for the three months ended June 30, 2023 and 2022, respectively, and \$6.2 million and \$3.1 million for the six months ended June 30, 2023 and 2022, respectively.

Accrued Expenses and Other Liabilities

Accrued expenses and other liabilities consisted of the following (in thousands):

	June 30, 2023	December 31, 2022
Accrued compensation and benefits	\$ 47,353	\$ 27,799
Accrued expenses	16,266	16,798
Accrued payroll taxes	12,314	10,349
Employee contributions under employee stock purchase plan	11,233	15,283
Accrued commissions	9,354	18,058
Other liabilities	15,975	17,044
Total accrued expenses and other liabilities	\$ 112,495	\$ 105,331

7. Business Combination, Goodwill, and Intangible Assets**Business Combination**

In January 2023, the Company acquired all outstanding shares of immerok GmbH (“Immerok”), an Apache Flink stream processing managed services company, for purchase consideration of \$54.9 million in cash. The Company acquired Immerok primarily for its talent and developed technology. The Company also entered into holdback agreements with certain employees of Immerok, pursuant to which the Company will pay up to an aggregate of \$52.3 million in cash. The vesting and payout of the holdback is subject to continued employment and achievement of certain milestones over three years, and is recorded as post-combination compensation expense within operating expenses over the requisite service period for accounting purposes. During the three and six months ended June 30, 2023, the Company recognized compensation expense of \$4.3 million and \$8.7 million, respectively, related to the holdback agreements.

In allocating the purchase consideration, the Company preliminarily recorded \$9.1 million of cash acquired, \$2.6 million as a developed technology intangible asset, to be amortized on a straight-line basis over an estimated useful life of five years, and \$43.5 million of goodwill. The goodwill is primarily attributed to the assembled workforce and expected synergies arising from the acquisition, and is not deductible for income tax purposes. The Company may continue to adjust the preliminary purchase price allocation after obtaining more information primarily relating to deferred income taxes and residual goodwill through the measurement period, no more than one year from the date of acquisition.

Transaction costs associated with the acquisition incurred during the three and six months ended June 30, 2023 were not material and were recorded as general and administrative expenses in the condensed consolidated statements of operations. The results of operations of Immerok included in the Company’s condensed consolidated financial statements since the date of acquisition were not material. Pro forma results of operations have not been presented because they were not material to the condensed consolidated results of operations.

Goodwill

Goodwill as of June 30, 2023 was \$43.5 million. No goodwill was recorded as of December 31, 2022.

Intangible Assets, Net

Intangible assets, net consisted of the following (in thousands):

	June 30, 2023		
	Gross	Accumulated Amortization	Net
Developed technology	\$ 2,556	\$ (240)	\$ 2,316
Total	<u>\$ 2,556</u>	<u>\$ (240)</u>	<u>\$ 2,316</u>

Amortization expense was not material for the three and six months ended June 30, 2023.

As of June 30, 2023, future amortization expense is expected to be as follows (in thousands):

Year Ending December 31,	Amount
Remainder of 2023	\$ 258
2024	513
2025	511
2026	511
2027	511
Thereafter	12
Total	<u>\$ 2,316</u>

8. Convertible Senior Notes

In December 2021, the Company issued \$1.1 billion aggregate principal amount of 0% convertible senior notes due 2027 (the “2027 Notes”), including the exercise in full of the initial purchasers’ option to purchase up to an additional \$100.0 million principal amount of the 2027 Notes, in a private placement to qualified institutional buyers pursuant to Rule 144A under the Securities Act. The 2027 Notes are general unsecured obligations of the Company and will mature on January 15, 2027, unless earlier converted, redeemed, or repurchased. The 2027 Notes do not bear regular interest, and the principal amount of the 2027 Notes will not accrete. Special interest, if any, is payable semiannually in arrears on January 15 and July 15 of each year, beginning on July 15, 2022 (if and to the extent that special interest is then payable on the 2027 Notes). No special interest has been paid in connection with the 2027 Notes to date. The total net proceeds from the offering, after deducting initial purchasers’ discounts and debt issuance costs, were \$1,080.5 million.

The initial conversion rate is 9.9936 shares of the Company’s Class A common stock per \$1,000 principal amount of 2027 Notes (equivalent to an initial conversion price of approximately \$100.06 per share of the Company’s Class A common stock), subject to adjustment as set forth in the indenture governing the 2027 Notes (the “Indenture”). The 2027 Notes are convertible at the option of the holders at any time prior to the close of business on the business day immediately preceding October 15, 2026, only under the following conditions:

- (1) during any calendar quarter commencing after the calendar quarter ending on March 31, 2022 (and only during such calendar quarter), if the last reported sale price of the Company's Class A common stock for at least 20 trading days (whether or not consecutive) during a period of 30 consecutive trading days ending on, and including, the last trading day of the immediately preceding calendar quarter is greater than or equal to 130% of the conversion price for the 2027 Notes on each applicable trading day;
- (2) during the five business day period after any ten consecutive trading day period (the "measurement period") in which the trading price per \$1,000 principal amount of the 2027 Notes for each trading day of the measurement period was less than 98% of the product of the last reported sale price of the Company's Class A common stock and the conversion rate for the 2027 Notes on each such trading day;
- (3) if the Company calls such 2027 Notes for redemption, at any time prior to the close of business on the scheduled trading day immediately preceding the redemption date, but only with respect to the 2027 Notes called (or deemed called) for redemption; or
- (4) upon the occurrence of specified corporate events as set forth in the Indenture.

On or after October 15, 2026, until the close of business on the second scheduled trading day immediately preceding the maturity date, holders of the 2027 Notes may convert all or any portion of their 2027 Notes at any time, at the option of the holder regardless of the foregoing conditions. Upon conversion, the Company may satisfy its conversion obligation by paying or delivering, as the case may be, cash, shares of Class A common stock or a combination of cash and shares of Class A common stock, at the Company's election, in the manner and subject to the terms and conditions provided in the Indenture. In addition, following certain corporate events that occur prior to the maturity date of the 2027 Notes or if the Company delivers a notice of redemption in respect of the 2027 Notes, the Company will, under certain circumstances, increase the conversion rate of the 2027 Notes for a holder who elects to convert its 2027 Notes in connection with such a corporate event or convert its 2027 Notes called (or deemed called) for redemption in connection with such notice of redemption, as the case may be.

During the three months ended June 30, 2023, the conditions allowing holders of the 2027 Notes to convert have not been met. The 2027 Notes were therefore not convertible and were classified as long-term debt on the Company's condensed consolidated balance sheets as of June 30, 2023 and December 31, 2022.

The Company may not redeem the 2027 Notes prior to January 20, 2025. The Company may redeem for cash all or any portion of the 2027 Notes (subject to the certain limitations described in the Indenture), at its option, on or after January 20, 2025, if the last reported sale price of the Company's Class A common stock has been at least 130% of the conversion price for the 2027 Notes then in effect for at least 20 trading days (whether or not consecutive) during any 30 consecutive trading day period (including the last trading day of such period) ending on, and including, the trading day immediately preceding the date on which the Company provides notice of redemption at a redemption price equal to 100% of the principal amount of the 2027 Notes to be redeemed, plus accrued and unpaid special interest, if any, to, but excluding, the redemption date. If the Company redeems less than all of the outstanding 2027 Notes, at least \$100.0 million aggregate principal amount of 2027 Notes must be outstanding and not subject to redemption as of, and after giving effect to, delivery of the relevant notice of redemption. No sinking fund is provided for the 2027 Notes.

The Company incurred \$19.5 million of debt issuance costs related to the 2027 Notes. These costs are amortized to interest expense included within other (income) expense, net on the condensed consolidated statements of operations over the contractual term of the 2027 Notes at an effective interest rate of 0.35%. Amortization of debt issuance costs was \$1.0 million and \$0.9 million for the three months ended June 30, 2023 and 2022, respectively, and \$1.9 million for both the six months ended June 30, 2023 and 2022.

The net carrying amount of the 2027 Notes was as follows (in thousands):

	June 30, 2023	December 31, 2022
Principal	\$ 1,100,000	\$ 1,100,000
Unamortized debt issuance costs	(13,611)	(15,500)
Net carrying amount	<u>\$ 1,086,389</u>	<u>\$ 1,084,500</u>

Capped Calls

In connection with the pricing of the 2027 Notes and the exercise in full by the initial purchasers of their option to purchase additional 2027 Notes, the Company entered into capped call transactions with certain of the initial purchasers of the 2027 Notes or their respective affiliates and other financial institutions (the “Capped Calls”). The Capped Calls each have an initial strike price of approximately \$100.06 per share, subject to certain adjustments, which corresponds to the initial conversion price of the 2027 Notes. The Capped Calls have initial cap prices of \$138.02 per share, subject to certain adjustments. The Capped Calls associated with the 2027 Notes cover, subject to anti-dilution adjustments, approximately 11.0 million shares of the Company’s Class A common stock. The Capped Calls are expected generally to reduce the potential dilution to the Company’s Class A common stock upon any conversion of the 2027 Notes and/or offset any cash payments the Company is required to make in excess of the principal amount of converted 2027 Notes, as the case may be, with such reduction and/or offset subject to a cap based on the cap price. For accounting purposes, the Capped Calls are separate transactions and not part of the terms of the 2027 Notes. As these transactions meet certain accounting criteria, the Capped Calls are recorded in stockholders’ equity and are not accounted for as derivatives. The cost of \$91.0 million incurred to purchase the Capped Calls was recorded as a reduction to additional paid-in capital and will not be remeasured.

9. Commitments and Contingencies

Leases

The Company has entered into non-cancelable operating leases, primarily for the rent of office space expiring at various dates through 2029. Certain lease agreements contain an option for the Company to renew the lease for a term of up to five years or an option to terminate the lease early within three years of lease termination. The Company considers these options in determining the lease term and minimum lease payments on a lease-by-lease basis. None of the Company’s lease agreements contain any material non-lease components, material residual value guarantees, or material restrictive covenants.

In 2019, the Company was issued a letter of credit of \$8.2 million for its office space in Mountain View, California. No draws have been made under the letter of credit as of June 30, 2023 and December 31, 2022.

In addition, the Company subleased certain floors of its unoccupied office space that expired at various dates in 2022. Sublease income was recorded as a reduction of lease expense and was not material for the three and six months ended June 30, 2022.

During the six months ended June 30, 2023, the Company ceased use of certain leased office space. The Company accelerated amortization of the related operating lease right-of-use assets and recognized \$15.7 million of lease abandonment charges within restructuring and other related charges in the condensed consolidated statements of operations. See Note 12 for further information on the Company’s restructuring actions.

Purchase Obligations

During the six months ended June 30, 2023, the Company entered into an amended third-party infrastructure agreement that includes a non-cancelable commitment of \$140.0 million payable over the next five years through June 2028. There were no other material changes to the Company’s purchase obligations from those disclosed in the Company’s Annual Report.

Legal Matters

From time to time, the Company has become involved in claims and other legal matters arising in the ordinary course of business. The Company investigates these claims as they arise. As of June 30, 2023 and December 31, 2022, the Company is not aware of any matters that would individually or taken together have a material adverse effect on the Company’s results of operations, financial position, or cash flows.

Indemnification

The Company enters into indemnification provisions under its agreements with other companies in the ordinary course of business, including customers, business partners, landlords, and certain third-party vendors. Under these arrangements, the Company agrees to indemnify, hold harmless, and reimburse the indemnified party for certain losses suffered or incurred by the indemnified party resulting from certain Company activities. The terms of these indemnification agreements are generally perpetual. The maximum potential amount of future payments the Company could be required to make under these agreements is not determinable. As of June 30, 2023 and December 31, 2022, the Company has not incurred material costs to defend lawsuits or settle claims related to these indemnification agreements. The Company maintained commercial general liability insurance and product liability insurance during the three and six months ended June 30, 2023 and 2022 to offset certain of the Company's potential liabilities under these indemnification provisions.

The Company also indemnifies certain of its officers, directors, and certain key employees while they are serving in good faith in their respective capacities. As of June 30, 2023 and December 31, 2022, the Company has not incurred material costs to defend lawsuits or settle claims related to these indemnification agreements.

10. Revenue**Disaggregation of Revenue**

The following table sets forth revenue disaggregated by geographic markets based on the location of the customer and by subscription and service categories (dollars in thousands):

	Three Months Ended June 30,				Six Months Ended June 30,			
	2023		2022		2023		2022	
Geographic markets:								
United States	\$ 113,910	60 %	\$ 87,556	63 %	\$ 217,852	60 %	\$ 166,548	63 %
International	75,375	40 %	51,851	37 %	145,735	40 %	98,998	37 %
Total revenue	<u>\$ 189,285</u>	<u>100 %</u>	<u>\$ 139,407</u>	<u>100 %</u>	<u>\$ 363,587</u>	<u>100 %</u>	<u>\$ 265,546</u>	<u>100 %</u>
Subscriptions and services:								
Confluent Platform - License	\$ 20,544	11 %	\$ 19,568	14 %	\$ 39,532	11 %	\$ 38,515	15 %
Confluent Platform - PCS ⁽¹⁾	72,366	38 %	60,470	43 %	140,307	39 %	116,530	44 %
Confluent Cloud	83,578	44 %	46,980	34 %	157,216	43 %	85,893	32 %
Subscription	176,488	93 %	127,018	91 %	337,055	93 %	240,938	91 %
Services	12,797	7 %	12,389	9 %	26,532	7 %	24,608	9 %
Total revenue	<u>\$ 189,285</u>	<u>100 %</u>	<u>\$ 139,407</u>	<u>100 %</u>	<u>\$ 363,587</u>	<u>100 %</u>	<u>\$ 265,546</u>	<u>100 %</u>

⁽¹⁾ PCS refers to post-contract customer support, maintenance, and upgrades.

Remaining Performance Obligations ("RPO")

RPO represent the amount of contracted future revenue that has not yet been recognized as of the end of each period, including both deferred revenue that has been invoiced and non-cancelable committed amounts that will be invoiced and recognized as revenue in future periods. RPO exclude pay-as-you-go arrangements. As of June 30, 2023, the Company's RPO was \$791.4 million, approximately 65% of which is expected to be recognized as revenue over the next 12 months and the substantial majority of the remainder in the next 13 to 36 months.

Deferred Revenue

Deferred revenue, including current and non-current balances as of June 30, 2023 and December 31, 2022 was \$328.0 million and \$322.8 million, respectively. For the six months ended June 30, 2023 and 2022, revenue recognized from deferred revenue at the beginning of the year was \$199.9 million and \$152.7 million, respectively.

Accounts Receivable, Net

The unbilled receivables balance included in accounts receivable, net on the condensed consolidated balance sheets was \$54.5 million and \$51.3 million as of June 30, 2023 and December 31, 2022, respectively.

The Company's allowance for expected credit losses was not material as of June 30, 2023 and December 31, 2022. Additions to and write-offs against the allowance for expected credit losses were not material for the three and six months ended June 30, 2023 and 2022.

Deferred Contract Acquisition Costs

The following table summarizes the activity of deferred contract acquisition costs (in thousands):

	Six Months Ended June 30,	
	2023	2022
Beginning balance	\$ 104,284	\$ 78,824
Capitalization of contract acquisition costs	23,966	22,723
Amortization of deferred contract acquisition costs	(21,537)	(17,395)
Ending balance	<u>\$ 106,713</u>	<u>\$ 84,152</u>

11. Stockholders' Equity**Preferred Stock**

In connection with the IPO, the Company's amended and restated certificate of incorporation became effective, which authorized the issuance of 10,000,000 shares of undesignated preferred stock with a par value of \$0.00001 per share with rights and preferences, including voting rights, designated from time to time by the board of directors.

Common Stock

The Company has two classes of common stock: Class A common stock and Class B common stock. In connection with the IPO, the Company's amended and restated certificate of incorporation authorized the issuance of 1,000,000,000 shares of Class A common stock and 500,000,000 shares of Class B common stock. The shares of Class A common stock and Class B common stock are identical, except with respect to voting, converting, and transfer rights. Each share of Class A common stock is entitled to one vote. Each share of Class B common stock is entitled to ten votes. Class A and Class B common stock have a par value of \$0.00001 per share and are referred to as common stock throughout the notes to the condensed consolidated financial statements, unless otherwise noted. Holders of common stock are entitled to receive any dividends as may be declared from time to time by the board of directors.

Each share of Class B common stock is convertible at any time at the option of the holder into one share of Class A common stock. Any holder's shares of Class B common stock will convert automatically to Class A common stock, on a one-to-one basis, upon the following: (i) sale or transfer of such share of Class B common stock, except for permitted transfers as described in the amended and restated certificate of incorporation; (ii) the death or incapacity of the Class B common stockholder (or nine months after the date of the death or incapacity if the stockholder is one of the Company's founders); and (iii) on the final conversion date, defined as the earliest of (a) the date fixed by our board of directors that is no less than 61 days and no more than 180 days following the date on which the outstanding shares of Class B common stock represent less than 10% of the then outstanding shares of Class A and Class B common stock; (b) the last trading day of the fiscal year following the tenth anniversary of the Company's IPO; or (c) the date specified by a vote of the holders of a majority of the outstanding shares of Class B common stock, voting as a single class.

Common Stock Reserved for Future Issuance

The Company has reserved the following shares of common stock for future issuance:

	June 30, 2023	December 31, 2022
2014 Stock Plan:		
Options outstanding	36,444,774	45,276,579
Restricted stock units outstanding	1,479,976	2,224,138
2021 Equity Incentive Plan:		
Options outstanding	22,500	22,500
Restricted stock units outstanding	23,828,489	17,729,318
Remaining shares available for future issuance	39,666,627	33,300,077
2021 Employee Stock Purchase Plan	8,673,168	6,493,913
Total	110,115,534	105,046,525

Equity Incentive Plans

In September 2014, the Company’s board of directors adopted and the Company’s stockholders approved the 2014 Stock Plan (the “2014 Plan”). The 2014 Plan was also amended and restated in March 2021 and June 2021. Under the 2014 Plan, the board of directors may grant stock options and other equity-based awards to eligible employees, directors, and consultants. The 2014 Plan was terminated in June 2021 in connection with the IPO, but continues to govern the terms of outstanding awards that were granted prior to the termination of the 2014 Plan. No further equity awards will be granted under the 2014 Plan. With the establishment of the 2021 Equity Incentive Plan (the “2021 Plan”), upon the expiration, forfeiture, cancellation, or reacquisition of any shares of Class B common stock underlying outstanding stock-based awards granted under the 2014 Plan, an equal number of shares of Class A common stock will become available for grant under the 2021 Plan. Equity-based awards granted under the 2014 Plan and the 2021 Plan generally vest over four years. All stock option grants expire ten years from the date of grant.

In April 2021, the Company’s board of directors adopted, and in June 2021, the Company’s stockholders approved, the 2021 Plan, which became effective at the time of the execution of the underwriting agreement related to the Company’s IPO. The 2021 Plan provides for the grant of incentive stock options, nonqualified stock options, stock appreciation rights, restricted stock awards, restricted stock units (“RSUs”) awards, performance awards, and other forms of awards to employees, directors, and consultants, including employees and consultants of the Company’s affiliates. A total of 25,812,876 shares of the Company’s Class A common stock have been reserved for future issuance under the 2021 Plan in addition to (i) the shares that remained available for grant of future awards under the 2014 Plan at the time the 2021 Plan became effective, (ii) shares underlying outstanding stock awards granted under the 2014 Plan that expire, or are forfeited, cancelled, or reacquired, as described above, and (iii) any automatic increases in the number of shares of Class A common stock reserved for future issuance under this plan.

In April 2021, the Company’s board of directors adopted, and in June 2021, the Company’s stockholders approved, the 2021 Employee Stock Purchase Plan (the “2021 ESPP”), which became effective at the time of the execution of the underwriting agreement related to the Company’s IPO. The 2021 ESPP authorizes the issuance of shares of Class A common stock pursuant to purchase rights granted to employees. A total of 5,162,575 shares of the Company’s Class A common stock have been reserved for future issuance under the 2021 ESPP, in addition to any automatic increases in the number of shares of Class A common stock reserved for future issuance under this plan.

Except for the initial offering period, the 2021 ESPP provides for 12-month offering periods beginning February 16 and August 16 of each year, and each offering period consists of two six-month purchase periods. The initial offering period began on June 24, 2021 and ended on August 15, 2022. The initial offering consisted of two purchase periods, with the first purchase period ending on February 15, 2022 and the second purchase period ending on August 15, 2022. The price at which Class A common stock is purchased under the 2021 ESPP is equal to 85% of the lesser of (1) the fair market value of the Company’s Class A common stock on the offering date or (2) the fair market value of the Company’s Class A common stock on the purchase date.

The 2021 ESPP offers a rollover feature pursuant to which, if the fair market value of a share of Class A common stock on the first trading day of a new purchase period is lower than the fair market value on the offering date, that offering period will terminate and participants will be automatically enrolled in a new 12-month offering period. In February 2023, an ESPP rollover occurred because the Company's closing stock price on the first trade date of the new purchase period was below the closing stock price on the offering date. This triggered a new 12-month offering period and resulted in immaterial incremental stock-based compensation expense to be recognized over the remaining requisite service period.

Equity Awards Outstanding

The following table summarizes stock equity award activity and activity regarding shares available for grant under the 2014 Plan and the 2021 Plan:

	Equity Awards Outstanding				
	Shares Available for Grant	Outstanding Stock Options	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in thousands)
Balance as of January 1, 2023	33,300,077	45,299,079	\$ 7.76	6.99	\$ 657,307
Increase in authorized shares	14,469,209	-	\$ -		
Stock options exercised	-	(7,241,647)	\$ 6.63		
Stock options forfeited or expired	1,590,158	(1,590,158)	\$ 12.26		
Repurchases of unvested common stock	30,828	-	\$ -		
RSUs granted	(12,019,143)	-	\$ -		
RSUs forfeited or cancelled	2,295,498	-	\$ -		
Balance as of June 30, 2023	<u>39,666,627</u>	<u>36,467,274</u>	\$ 7.78	6.58	\$ 1,004,232
Vested as of June 30, 2023		<u>25,354,766</u>	\$ 6.44	6.33	\$ 732,274
Vested and expected to vest as of June 30, 2023		<u>36,467,274</u>	\$ 7.78	6.58	\$ 1,004,232

Aggregate intrinsic value represents the difference between the exercise price of the options to purchase common stock and the estimated fair value of the Company's common stock. The intrinsic value of options exercised was \$144.7 million and \$284.4 million for the six months ended June 30, 2023 and 2022, respectively. No options were granted during the six months ended June 30, 2023 and 2022.

Early Exercised Options

All stock option holders have the right to exercise unvested options, which are subject to a repurchase right held by the Company at the original exercise price in the event of voluntary or involuntary termination of employment of the stockholder. As of June 30, 2023 and December 31, 2022, there were 284,550 and 578,119 shares that had been early exercised and were subject to repurchase, respectively. The proceeds related to early exercised options are recorded as liabilities within accrued expenses and other liabilities and other liabilities, non-current on the condensed consolidated balance sheets until the options vest, at which point they are reclassified to equity. As of June 30, 2023 and December 31, 2022, the liabilities for early exercised options subject to repurchase were \$2.3 million and \$4.0 million, respectively.

Shares issued for early exercised options are included in issued and outstanding shares as they are legally issued and outstanding, but are not deemed outstanding for accounting purposes until the shares vest.

RSUs

The following table summarizes RSU activity under the 2014 Plan and the 2021 Plan:

	RSUs Outstanding	
	Number of Shares	Weighted-Average Grant Date Fair Value
Unvested balance as of January 1, 2023	19,953,456	\$ 33.18
RSUs granted	12,019,143	\$ 23.96
RSUs vested	(4,368,636)	\$ 30.51
RSUs forfeited or cancelled	(2,295,498)	\$ 33.52
Unvested balance as of June 30, 2023	25,308,465	\$ 29.23

Stock-Based Compensation Expense

Total stock-based compensation expense was as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2023	2022	2023	2022
Cost of revenue - subscription	\$ 6,914	\$ 6,018	\$ 13,242	\$ 11,331
Cost of revenue - services	3,125	2,328	5,902	4,190
Research and development	35,420	25,337	65,435	45,422
Sales and marketing	32,889	24,746	61,376	45,808
General and administrative	13,811	10,437	25,493	19,484
Stock-based compensation, net of amounts capitalized	\$ 92,159	\$ 68,866	\$ 171,448	\$ 126,235
Capitalized stock-based compensation	5,810	1,598	9,732	3,125
Total stock-based compensation	\$ 97,969	\$ 70,464	\$ 181,180	\$ 129,360

As of June 30, 2023, there was \$779.7 million of unrecognized stock-based compensation expense, which is expected to be recognized over a weighted-average period of 2.3 years.

12. Restructuring and Other Related Charges

In January 2023, the Company approved restructuring actions (the “Restructuring Plan”) to adjust its cost structure and real estate footprint. The Restructuring Plan includes a reduction of approximately 8% of the Company’s global workforce as of December 31, 2022. During the three and six months ended June 30, 2023, the Company recorded restructuring and other related charges of \$0.9 million and \$34.3 million, respectively, consisting of \$0.9 million and \$18.7 million related to employee transition and severance payments, employee benefits, and related facilitation costs, respectively, and nil and \$15.7 million of lease abandonment charges, respectively. The Restructuring Plan was substantially completed as of June 30, 2023.

The following table summarizes the Company’s liability for restructuring-related employee termination benefits included in accrued expenses and other current liabilities on the condensed consolidated balance sheets (in thousands):

	Employee Termination Benefits	
Balance as of January 1, 2023	\$	-
Restructuring charges		18,658
Cash payments		(16,756)
Balance as of June 30, 2023	\$	1,902

13. Income Taxes

The Company computes its provision for (benefit from) income taxes for interim periods by applying its estimated annual effective tax rate to year-to-date loss or income for includable jurisdictions before income taxes from recurring operations and adjusting for discrete tax items arising in that interim period.

The Company’s provision for income taxes was \$1.7 million and \$1.5 million for the three months ended June 30, 2023 and 2022, respectively, and \$3.3 million and \$2.2 million for the six months ended June 30, 2023 and 2022, respectively, primarily due to foreign and state income taxes. The Company provides a valuation allowance on its U.S. and U.K. deferred tax assets.

14. Net Loss Per Share

For periods in which there were shares of Class A and Class B common stock outstanding, the rights, including the liquidation and dividend rights, of the holders of Class A and Class B common stock were identical, except with respect to voting, converting, and transfer rights. As the liquidation and dividend rights were identical for Class A and Class B common stock, the undistributed earnings were allocated on a proportionate basis and the resulting net loss per share would, therefore, be the same for both Class A and Class B common stock on an individual or combined basis.

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2023	2022	2023	2022
	Class A and Class B Common Stock		Class A and Class B Common Stock	
Numerator:				
Net loss	\$ (103,425)	\$ (117,631)	\$ (255,980)	\$ (230,618)
Denominator:				
Weighted-average shares used to compute net loss per share, basic and diluted	297,827,200	278,268,980	294,862,197	275,593,362
Net loss per share, basic and diluted	\$ (0.35)	\$ (0.42)	\$ (0.87)	\$ (0.84)

The following outstanding potentially dilutive shares were excluded from the computation of diluted net loss per share for the periods presented because the impact of including them would have been anti-dilutive:

	June 30, 2023	June 30, 2022
Stock options	36,467,274	51,921,878
Unvested early exercised stock options	284,550	1,079,122
RSUs	25,308,465	17,167,218
ESPP	1,553,885	758,398
Shares issuable upon conversion of the 2027 Notes	10,992,960	10,992,960
Total	74,607,134	81,919,576

The Company calculates the potential dilutive effect of its 2027 Notes under the if-converted method. Under this method, diluted net loss per share is determined by assuming that all of the 2027 Notes were converted into shares of the Company's Class A common stock at the beginning of the reporting period.

In connection with the issuance of the 2027 Notes, the Company entered into Capped Calls, which are not included for purposes of calculating the number of diluted weighted-average shares outstanding, as their effect would have been anti-dilutive. The Capped Calls are expected to partially offset the potential dilution to the Company's Class A common stock upon any conversion of the 2027 Notes.

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our unaudited condensed consolidated financial statements and related notes appearing elsewhere in this Quarterly Report on Form 10-Q and our audited consolidated financial statements and the related notes and the discussion under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations" for the fiscal year ended December 31, 2022 included in the Company's Annual Report on Form 10-K for the year ended December 31, 2022 filed with the Securities and Exchange Commission ("SEC") on February 28, 2023 (the "Annual Report"). This discussion, particularly information with respect to our future results of operations or financial condition, business strategy and plans, and objectives of management for future operations, includes forward-looking statements that involve risks and uncertainties as described under the heading "Special Note About Forward-Looking Statements" in this Quarterly Report on Form 10-Q. You should review the disclosure under the heading "Risk Factors" in this Quarterly Report on Form 10-Q for a discussion of important factors that could cause our actual results to differ materially from those anticipated in these forward-looking statements. Unless the context otherwise requires, all references in this Quarterly Report on Form 10-Q to "we," "us," "our," "our company," and "Confluent" refer to Confluent, Inc. and its consolidated subsidiaries. Unless otherwise indicated, references to our "common stock" include our Class A common stock and Class B common stock.

Overview

Confluent is on a mission to set data in motion. We were founded in 2014 to pioneer this fundamentally new category of data infrastructure designed to connect all the applications, systems, and data layers of a company around a real-time central nervous system. This new data infrastructure software has emerged as one of the most strategic parts of the next-generation technology stack, and using this stack to harness data in motion is critical to the success of every modern company as they strive to compete and win in the digital-first world. Prior to Confluent, our founders created the open source software project Apache Kafka, a technology that has been central to enabling data in motion. Since our founding, we have heavily invested in product development to build a complete, cloud-native platform for data in motion.

Confluent is designed to act as the nexus of real-time data, from every source, allowing it to stream across the organization and enabling applications to harness it to power real-time customer experiences and data-driven business operations. Our offering enables organizations to deploy production-ready applications that span across cloud environments and data centers, while scaling elastically with enhanced features for security, compliance, and governance. Our platform provides the capabilities to fill the structural, operational, and engineering gaps required for businesses to fully realize the power of data in motion. We enable software developers to easily build their initial applications to harness data in motion, and enable large, complex enterprises to make data in motion core to everything they do. As organizations mature in their adoption cycle, we enable them to quickly, securely, and reliably build more and more applications that take advantage of data in motion. The results have a dual effect: businesses continuously improve their ability to provide better customer experiences and concurrently drive data-driven business operations. We believe that Confluent, over time, will become the central nervous system for modern digital enterprises, providing ubiquitous real-time connectivity and powering real-time applications across the enterprise.

We generate our revenue primarily from the sale of subscriptions to our offering that can be deployed in two different ways. Confluent Platform is an enterprise-ready, self-managed software offering that can be deployed in our customers' on-premise, private cloud, and public cloud environments. Confluent Cloud is a fully-managed, cloud-native software-as-a-service ("SaaS") offering available on all of the leading cloud providers. Confluent Platform and Confluent Cloud can be leveraged independently or together, spanning the various public cloud, private cloud, and on-premise environments in which our customers operate.

Confluent Platform customers receive access to our proprietary features and various tiers of customer support. Our Confluent Platform subscriptions primarily have one-year terms and are generally billed annually in advance. Confluent Cloud customers may purchase subscriptions either without a minimum commitment contract on a month-to-month basis, which we refer to as pay-as-you-go, or under a usage-based minimum commitment contract of at least one year in duration, in which customers commit to a fixed minimum monetary amount at specified per-usage rates. Pay-as-you-go customers are billed, and revenue from them is recognized, based on usage. Customers with usage-based minimum commitments are typically billed annually in advance or monthly in arrears, and we recognize revenue from such subscriptions based on usage by the customer. As a result, our revenue may fluctuate from period to period due to varying patterns of customer consumption.

We are focused on the acquisition of new customers and expanding within our current customers. Our go-to-market model benefits from our self-service motions driven by our cloud-native platform offerings, our widespread mindshare among developers through Apache Kafka, community downloads, and our enterprise sales force. We are able to acquire new customers through seamless and frictionless self-service cloud adoption and free cloud trials, as well as community downloads. For example, after users get started with our free cloud trial, they can easily convert to become paying customers either online on a pay-as-you-go model or with a minimum commitment contract. Once customers see the benefits of our platform for their initial use cases, they often expand into other use cases and lines of business, divisions, and geographies. Our deep technical expertise, coupled with our product capabilities and laser focus on customer outcomes, enable us to form strategic partnerships with our customers to guide and accelerate this journey. This expansion often generates a natural network effect in which the value of our platform to a customer increases as more use cases are adopted, more users and teams are onboarded, more applications and systems are connected, and more data is added. We had approximately 4,830 and 4,120 customers as of June 30, 2023 and June 30, 2022, respectively, representing year-over-year growth of 17%. We have experienced significant growth, with revenue of \$189.3 million and \$139.4 million for the three months ended June 30, 2023 and 2022, respectively, representing year-over-year growth of 36%, and revenue of \$363.6 million and \$265.5 million for the six months ended June 30, 2023 and 2022, respectively, representing year-over-year growth of 37%.

Business and Macroeconomic Conditions

Our business and financial condition have been, and we believe will continue to be, impacted by adverse and uncertain macroeconomic conditions, including higher inflation, higher interest rates, bank failures and related uncertainty, supply chain challenges, fluctuations or volatility in capital markets or foreign currency exchange rates, and geopolitical events such as the ongoing conflict between Russia and Ukraine. In particular, we have experienced in certain instances, and we believe we will continue to experience, longer sales cycles or generally increased scrutiny on IT spending from existing and potential customers due to macroeconomic uncertainty. We cannot be certain how long these uncertain macroeconomic conditions and the resulting effects on our industry, our business strategy, and customers will persist. To navigate the current economic environment and its effects, we have taken actions to streamline our operating expenses by adjusting our cost structure and real estate footprint, including a workforce reduction in January 2023, while prudently investing in growth.

The full extent to which uncertain macroeconomic conditions and other factors discussed above will directly or indirectly impact our business, results of operations, cash flows, and financial condition remains uncertain and cannot be accurately predicted. We will continue to monitor and evaluate the actual and potential impacts of general macroeconomic conditions and related factors on our business and operations.

Key Factors Affecting Our Performance

Developing Innovative, Market-Leading Offerings and Expanding Developer Mindshare

We are focused on delivering market-leading offerings. We believe it is critical for us to maintain our product leadership position and further increase the strength of our brand and reputation to drive revenue growth. We launched Confluent Cloud, our cloud-native SaaS offering, in 2017 to capitalize on the existing demand for a fully-managed cloud service for Apache Kafka. Confluent Cloud has grown rapidly since launch, as organizations have been making significant investments in digital infrastructure with the goal of both driving efficiencies across their businesses, and better leveraging the data that powers their processes and customer experiences. In addition, we continue to release new product enhancements and features to simplify application development and real-time analytics and enhance security and data governance. We intend to invest efficiently in our engineering capabilities, including through acquisitions, and marketing activities to maintain our strong position within the developer community. Our results of operations may fluctuate as we make these investments to drive increased customer adoption and usage.

Increasing Adoption of Confluent Cloud

We believe our cloud-native Confluent Cloud offering represents an important growth opportunity for our business. Organizations are increasingly looking for a fully-managed offering to seamlessly leverage data in motion across a variety of environments. In some cases, customers that have been self-managing deployments through Confluent Platform subsequently have become Confluent Cloud customers. We offer customers a free cloud trial and a pay-as-you-go arrangement to encourage adoption and usage over time. We will continue to leverage our cloud-native differentiation to drive our growth. We expect Confluent Cloud's contribution to our subscription revenue to increase over time. Our Confluent Cloud revenue represented 44% and 34% of our total revenue for the three months ended June 30, 2023 and 2022, respectively, and 43% and 32% for the six months ended June 30, 2023 and 2022, respectively. As we recognize revenue from Confluent Cloud based on usage, our revenue and results of operations may fluctuate from period to period due to varying patterns of customer consumption and adoption trends.

Growing Our Customer Base

We are intensely focused on continuing to grow our customer base. We have invested and will continue to invest in our sales and marketing efforts, including pipeline generation and execution, and developer community outreach, which are critical to driving customer acquisition. We historically focused on large enterprise customers with significant expansion opportunities and built a go-to-market motion around this approach. As we grew our cloud offering and created more self-serve opportunities, we have significantly broadened our reach of customers and are able to attract a greater array of customers. This is evidenced by our significant increase in customer count in recent years, driven by Confluent Cloud customers. Our ability to attract new customers will depend on a number of factors, including our success in recruiting and scaling our sales and marketing organization, our ability to accelerate ramp time of our sales force, expansion and refinement of our go-to-market strategies to reach additional customer opportunities, the impact of marketing efforts to enhance our brand and educate potential customers about the benefits of our offering compared to alternatives for data in motion, our ability to grow and harness our partner ecosystem, macroeconomic uncertainty and challenges, and competitive dynamics in our target markets. We had approximately 4,830 and 4,120 customers as of June 30, 2023 and June 30, 2022, respectively, spanning organizations of all sizes and industries. Our customer count treats affiliated entities with the same parent organization as a single customer and includes pay-as-you-go customers.

Retaining and Expanding Revenue from Existing Customers

Our business model is driven by customer renewals and increasing existing customer subscriptions over time, referred to as land-and-expand. We believe we have significant opportunities to increase our revenue as customers expand their use of our offering in connection with migrating more data to the public cloud, identifying new use cases, and realizing the benefits of data in motion. Our ability to retain and expand revenue from existing customers, including through increased consumption of our offering and contractual commitments, will depend on a number of factors, including market acceptance of our offering compared to data-in-motion alternatives, such as Apache Kafka, customer satisfaction with our subscriptions and services, competition, pricing, economic conditions, and overall changes in our customers' spending levels, including effects on consumption growth rates, among other things.

Investing in Growth and Scaling our Business

We believe our market opportunity is significant, and we are focused on continuing to make disciplined investments in our long-term revenue and profitability potential. We believe it is critical to scale across all organizational functions, including our sales and marketing organization, in order to capture this opportunity. Investments we make in our sales and marketing organization will occur in advance of experiencing the benefits from such investments, and it may be difficult for us to determine if we are efficiently allocating resources within the organization. Our revenue growth potential is dependent on the effectiveness of such investments and the continued refinement of our go-to-market strategies. To navigate more challenging macroeconomic conditions, we intend to take a disciplined approach in investing to grow our business to take advantage of our expansive market opportunity while also optimizing for improvements in profitability, margins, and cash flow, including by streamlining our operating expenses.

Key Business Metrics

We monitor the key business metrics set forth below to help us evaluate our business and growth trends, establish budgets, measure our performance, and make strategic decisions. The calculation of the key metrics discussed below may differ from other similarly titled metrics used by other companies, securities analysts, or investors.

Remaining Performance Obligations (“RPO”)

RPO represents the amount of contracted future revenue that has not yet been recognized as of the end of each period, including both deferred revenue that has been invoiced and non-cancelable committed amounts that will be invoiced and recognized as revenue in future periods. RPO excludes pay-as-you-go arrangements.

RPO as a metric is not necessarily indicative of future revenue growth because it does not account for the actual timing of customers’ consumption or future expansion. RPO may also fluctuate due to a number of factors, including the timing of renewals, average contract terms, seasonality, and dollar amount of customer contracts. Due to these factors, it is important to review RPO in conjunction with revenue and other financial measures disclosed elsewhere in this Quarterly Report on Form 10-Q. Our RPO was \$791.4 million and \$591.3 million as of June 30, 2023 and 2022, respectively.

Customers with \$100,000 or Greater in Annual Recurring Revenue (“ARR”)

We define ARR as (1) with respect to Confluent Platform customers, the amount of revenue to which our customers are contractually committed over the following 12 months assuming no increases or reductions in their subscriptions, and (2) with respect to Confluent Cloud customers, the amount of revenue that we expect to recognize from such customers over the following 12 months, calculated by annualizing actual consumption of Confluent Cloud in the last three months of the applicable period, assuming no increases or reductions in usage rate. Services arrangements are excluded from the calculation of ARR. Large customer relationships lead to scale and operating leverage in our business model. Compared with smaller customers, large customers present a greater opportunity for us because they have larger budgets, greater potential for migrating more applications over time, and a wider range of potential use cases for data in motion. As a measure of our ability to scale with our customers and attract large enterprises to our offering, we count the number of customers that contributed \$100,000 or greater in ARR as of period end. Our customer count may also fluctuate due to acquisitions, consolidations, spin-offs, and other market activity. We had 1,144 and 862 customers with \$100,000 or greater in ARR as of June 30, 2023 and 2022, respectively.

From time to time, we may adjust our methodology for calculating ARR. Prior to the first quarter of 2023, ARR with respect to Confluent Cloud customers excluded pay-as-you-go arrangements and was based on contractual commitments over the following 12 months, regardless of actual consumption. We adjusted our methodology for calculating ARR commencing with the first quarter of 2023 to incorporate actual consumption of Confluent Cloud and applied this change retroactively. We believe this change better aligns with how our management assesses ARR internally and better reflects actual customer behavior over time as Confluent Cloud’s contribution to our subscription revenue increases over time. We expect this change to have a positive impact on customers with \$100,000 or greater in ARR, including in prior periods, as Confluent Cloud customers may be ramping their consumption more quickly than their contractual commitments. However, with this change, we may experience more volatility in ARR as our customers’ consumption trends may vary significantly across periods. Refer to the section titled “Risk Factors—Risks Related to Our Business and Operations—We expect fluctuations in our financial results and key metrics, making it difficult to project future results, and if we fail to meet the expectations of securities analysts or investors with respect to our results of operations, our stock price and the value of your investment could decline.”

Dollar-Based Net Retention Rate (“NRR”)

We calculate our dollar-based NRR as of a period end by starting with the ARR from the cohort of all customers as of 12 months prior to such period end, or Prior Period Value. We then calculate the ARR from these same customers as of the current period end, or Current Period Value, and divide the Current Period Value by the Prior Period Value to arrive at our dollar-based NRR. The dollar-based NRR includes the effect, on a dollar-weighted value basis, of our Confluent Platform subscriptions that expand, renew, contract, or attrit. The dollar-based NRR also includes the effect of annualizing actual consumption of Confluent Cloud in the last three months of the applicable period, but excludes ARR from new customers in the current period. Our dollar-based NRR is subject to adjustments for acquisitions, consolidations, spin-offs, and other market activity. We believe that our dollar-based NRR provides useful information about the evolution of our existing customers and our future growth prospects. Our dollar-based NRR was over 130% as of June 30, 2023, demonstrating our ability to expand within existing customers. However, our methodology for calculating ARR may result in increased volatility in NRR as our customers’ consumption trends may vary significantly across quarters. Refer to the section titled “Risk Factors—Risks Related to Our Business and Operations—We expect fluctuations in our financial results and key metrics, making it difficult to project future results, and if we fail to meet the expectations of securities analysts or investors with respect to our results of operations, our stock price and the value of your investment could decline.”

Components of Results of Operations

Revenue

We derive revenue primarily from subscriptions and, to a lesser extent, services.

Subscription Revenue. Our subscription revenue consists of revenue from term-based licenses and post-contract customer support, maintenance, and upgrades, referred to together as PCS, which we refer to as Confluent Platform, and our SaaS offering, which we refer to as Confluent Cloud. We recognize a portion of the revenue from our term-based license subscriptions at a point in time, upon delivery and transfer of control of the underlying license to the customer, which is typically the effective start date. Revenue from PCS, which represents a substantial majority of the revenue from our term-based license subscriptions, is recognized ratably over the contract term. The substantial majority of our revenue from Confluent Cloud for the three and six months ended June 30, 2023 and 2022 was based on usage-based minimum commitments and is recognized on a usage basis, as usage represents a direct measurement of the value to the customer of the subscription transferred as of a particular date relative to the total value to be delivered over the term of the contract. Our subscriptions primarily have terms of one to three years, and are generally non-cancelable and non-refundable. We also provide pay-as-you-go arrangements, which consist of month-to-month SaaS contracts. These arrangements have historically represented an immaterial portion of our subscription revenue.

Services Revenue. Services revenue consists of revenue from professional services and education services, which are generally sold on a time-and-materials basis. Revenue for professional services and education services is recognized as these services are delivered.

We expect our total revenue may vary from period to period based on, among other things, the timing and size of new subscriptions, the rate of customer renewals and expansions, fluctuations in customer consumption of and adoption trends for our usage-based offering, delivery of professional services, ramp time and productivity of our salesforce, the impact of significant transactions, and seasonality.

Cost of Revenue

Cost of Subscription Revenue. Cost of subscription revenue primarily includes personnel-related costs, including salaries, bonuses, benefits, and stock-based compensation, for employees associated with customer support and maintenance, third-party cloud infrastructure costs, amortization of internal-use software and acquired intangible assets, and allocated overhead costs for information technology, facilities, recruiting, and business systems. We expect our cost of subscription revenue to increase in absolute dollars as our subscription revenue increases.

Cost of Services Revenue. Cost of services revenue primarily includes personnel-related costs, including salaries, bonuses, benefits, and stock-based compensation, for employees associated with our professional services and education services, costs of third-party consultants and partners who supplement our services delivery team, and allocated overhead. We expect our cost of services revenue to increase in absolute dollars as our services revenue increases.

Gross Profit and Gross Margin

Gross Profit. Gross profit represents revenue less cost of revenue.

Gross Margin. Gross margin, or gross profit as a percentage of revenue, has been and will continue to be affected by a variety of factors, including the average sales price of our subscriptions and services, changes in our revenue mix, including the mix of revenue between our Confluent Platform, Confluent Cloud, and service offerings, timing and amount of usage of third-party cloud infrastructure resources, and infrastructure optimization. We expect our gross margin to fluctuate over time depending on the factors described above.

Operating Expenses

Our operating expenses consist of research and development, sales and marketing, general and administrative expenses, and restructuring and other related charges. Personnel-related costs are the most significant component of each category of operating expenses. Operating expenses also include allocated overhead costs for information technology, facilities, recruiting, and business systems.

Research and Development. Research and development expenses consist primarily of personnel-related costs, including salaries, bonuses, benefits, and stock-based compensation, net of capitalized amounts, third-party cloud infrastructure expenses incurred in developing our offering, software and subscription services dedicated for use by our research and development organization, contractor and professional services fees, and allocated overhead. We expect our research and development expenses will continue to increase in absolute dollars as our business grows and we continue to invest in our offering.

Sales and Marketing. Sales and marketing expenses consist primarily of personnel-related costs, including salaries, sales commissions, bonuses, benefits, and stock-based compensation, amortization of deferred contract acquisition costs, which primarily consist of sales commissions and the associated payroll taxes, conferences, costs related to marketing programs, travel-related costs, and allocated overhead. Marketing programs consist of advertising, events, corporate communications, and brand-building and developer-community activities. We expect our sales and marketing expenses will increase in absolute dollars over time and continue to be our largest operating expense for the foreseeable future as we invest in our sales and marketing efforts.

General and Administrative. General and administrative expenses consist primarily of personnel-related costs, including salaries, bonuses, benefits, and stock-based compensation for administrative functions including finance, human resources, and legal, professional fees, software and subscription services dedicated for use by our general and administrative functions, and allocated overhead. We expect our general and administrative expenses will increase in absolute dollars over time as we continue to invest in the growth of our business and incur costs associated with being a publicly traded company.

Restructuring and Other Related Charges. Restructuring and other related charges consist of personnel-related costs, including employee transition and severance payments, employee benefits, and related facilitation costs, as well as lease abandonment charges.

Other Income (Expense), Net

Other income (expense), net consists primarily of interest earned on our cash equivalents and marketable securities, amortization of premiums and accretion of discounts on marketable securities, interest expense from amortization of debt issuance costs, gains and losses from foreign currency transactions, and realized gains and losses on marketable securities.

Provision for (Benefit from) Income Taxes

Provision for (benefit from) income taxes consists primarily of income taxes in certain foreign and U.S. state jurisdictions in which we conduct business. We maintain a full valuation allowance against our U.S. and U.K. deferred tax assets because we have concluded that it is more likely than not that the deferred tax assets will not be realized.

Results of Operations

The following table sets forth our condensed consolidated statements of operations data for the periods presented:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2023	2022	2023	2022
	(in thousands)			
Revenue:				
Subscription	\$ 176,488	\$ 127,018	\$ 337,055	\$ 240,938
Services	12,797	12,389	26,532	24,608
Total revenue	189,285	139,407	363,587	265,546
Cost of revenue:				
Subscription ⁽¹⁾⁽²⁾	44,188	35,608	87,093	69,211
Services ⁽¹⁾⁽²⁾	13,732	13,901	28,971	26,075
Total cost of revenue	57,920	49,509	116,064	95,286
Gross profit	131,365	89,898	247,523	170,260
Operating expenses:				
Research and development ⁽¹⁾⁽²⁾	85,677	64,472	170,567	122,133
Sales and marketing ⁽¹⁾⁽²⁾	127,770	112,754	256,394	219,456
General and administrative ⁽¹⁾⁽²⁾	36,343	29,979	71,698	57,460
Restructuring and other related charges	943	-	34,325	-
Total operating expenses	250,733	207,205	532,984	399,049
Operating loss	(119,368)	(117,307)	(285,461)	(228,789)
Other income, net	17,610	1,186	32,795	370
Loss before income taxes	(101,758)	(116,121)	(252,666)	(228,419)
Provision for income taxes	1,667	1,510	3,314	2,199
Net loss	\$ (103,425)	\$ (117,631)	\$ (255,980)	\$ (230,618)

⁽¹⁾ Includes stock-based compensation expense as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2023	2022	2023	2022
	(in thousands)			
Cost of revenue - subscription	\$ 6,914	\$ 6,018	\$ 13,242	\$ 11,331
Cost of revenue - services	3,125	2,328	5,902	4,190
Research and development	35,420	25,337	65,435	45,422
Sales and marketing	32,889	24,746	61,376	45,808
General and administrative	13,811	10,437	25,493	19,484
Total stock-based compensation expense	\$ 92,159	\$ 68,866	\$ 171,448	\$ 126,235

⁽²⁾ Includes employer taxes on employee stock transactions as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2023	2022	2023	2022
	(in thousands)			
Cost of revenue - subscription	\$ 265	\$ 70	\$ 586	\$ 403
Cost of revenue - services	128	80	218	157
Research and development	1,306	342	2,975	1,381
Sales and marketing	1,488	1,048	2,571	1,728
General and administrative	412	130	912	440
Total employer taxes on employee stock transactions	\$ 3,599	\$ 1,670	\$ 7,262	\$ 4,109

The following table sets forth our condensed consolidated statements of operations data expressed as a percentage of revenue for the periods indicated:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2023	2022	2023	2022
Revenue:				
Subscription	93%	91%	93%	91%
Services	7	9	7	9
Total revenue	100	100	100	100
Cost of revenue:				
Subscription	23	26	24	26
Services	7	10	8	10
Total cost of revenue	31	36	32	36
Gross profit	69	64	68	64
Operating expenses:				
Research and development	45	46	47	46
Sales and marketing	68	81	71	83
General and administrative	19	22	20	22
Restructuring and other related charges	0	0	9	0
Total operating expenses	132	149	147	150
Operating loss	(63)	(84)	(79)	(86)
Other income, net	9	1	9	0
Loss before income taxes	(54)	(83)	(69)	(86)
Provision for income taxes	1	1	1	1
Net loss	(55)%	(84)%	(70)%	(87)%

Note: Certain figures may not sum due to rounding.

Comparison of the Three Months Ended June 30, 2023 and 2022
Revenue

	Three Months Ended June 30,		Change	
	2023	2022	\$	%
	(in thousands, except percentages)			
Subscription	\$ 176,488	\$ 127,018	\$ 49,470	39%
Services	12,797	12,389	408	3%
Total revenue	\$ 189,285	\$ 139,407	\$ 49,878	36%

Subscription revenue increased by \$49.5 million during the three months ended June 30, 2023 compared to the three months ended June 30, 2022. The increase in revenue was primarily from sales to existing customers and the remaining increase was attributable to sales to new customers. Sales to new customers represent the revenue recognized from customers acquired in the 12 months prior to June 30, 2023. A further indication of our ability to expand from existing customers is through our dollar-based net retention rate of over 130% as of June 30, 2023. Confluent Platform and Confluent Cloud contributed 53% and 47% of our subscription revenue during the three months ended June 30, 2023, respectively, compared to 63% and 37% during the three months ended June 30, 2022, respectively.

Services revenue increased by \$0.4 million during the three months ended June 30, 2023 compared to the three months ended June 30, 2022 primarily due to an increase in delivery of professional services.

Cost of Revenue, Gross Profit, and Gross Margin

	Three Months Ended June 30,		Change	
	2023	2022	\$	%
	(in thousands, except percentages)			
Cost of revenue				
Subscription	\$ 44,188	\$ 35,608	\$ 8,580	24%
Services	13,732	13,901	(169)	(1)%
Total cost of revenue	\$ 57,920	\$ 49,509	\$ 8,411	17%
Gross profit	\$ 131,365	\$ 89,898	\$ 41,467	46%

	Three Months Ended June 30,	
	2023	2022
Gross margin		
Subscription	75%	72%
Services	(7)%	(12)%
Total gross margin	69%	64%

Cost of subscription revenue increased by \$8.6 million during the three months ended June 30, 2023 compared to the three months ended June 30, 2022. This increase was primarily due to an increase of \$4.8 million in third-party cloud infrastructure costs and an increase of \$3.2 million in personnel-related costs and allocated overhead costs driven by increased headcount.

Cost of services revenue decreased by \$0.2 million during the three months ended June 30, 2023 compared to the three months ended June 30, 2022. This decrease was primarily due to a decrease of \$1.5 million in costs for third-party contractors and partners who supplement our services delivery team, offset by an increase of \$1.5 million in personnel-related costs and allocated overhead costs driven by increased headcount.

Our subscription gross margin increased primarily due to economies of scale resulting from increased efficiency and optimization of our infrastructure, offset by a change in our revenue mix toward Confluent Cloud which has a lower gross margin. Our services gross margin increased primarily due to an increase in services revenue and a decrease in costs for third-party contractors.

Research and Development

	Three Months Ended June 30,		Change	
	2023	2022	\$	%
	(in thousands, except percentages)			
Research and development	\$ 85,677	\$ 64,472	\$ 21,205	33%
Percentage of revenue	45%	46%		

Research and development expenses increased by \$21.2 million during the three months ended June 30, 2023 compared to the three months ended June 30, 2022. This increase was primarily due to an increase of \$15.9 million in personnel-related costs and allocated overhead costs and an increase of \$3.8 million in acquisition-related compensation costs. The increase in personnel-related costs was mainly driven by increased headcount and an increase of \$10.1 million in stock-based compensation expense, net of amounts capitalized.

Sales and Marketing

	Three Months Ended June 30,		Change	
	2023	2022	\$	%
	(in thousands, except percentages)			
Sales and marketing	\$ 127,770	\$ 112,754	\$ 15,016	13%
Percentage of revenue	68%	81%		

Sales and marketing expenses increased by \$15.0 million during the three months ended June 30, 2023 compared to the three months ended June 30, 2022. This increase was primarily due to an increase of \$13.7 million in personnel-related costs and allocated overhead costs and an increase of \$2.1 million in amortization of deferred contract acquisition costs. The increase in personnel-related costs was mainly driven by increased headcount and an increase of \$8.1 million in stock-based compensation expense.

General and Administrative

	Three Months Ended June 30,		Change	
	2023	2022	\$	%
	(in thousands, except percentages)			
General and administrative	\$ 36,343	\$ 29,979	\$ 6,364	21%
Percentage of revenue	19%	22%		

General and administrative expenses increased by \$6.4 million during the three months ended June 30, 2023 compared to the three months ended June 30, 2022. This increase was primarily due to an increase of \$5.9 million in personnel-related costs and allocated overhead costs. The increase in personnel-related costs was mainly driven by increased headcount and an increase of \$3.4 million in stock-based compensation expense.

Restructuring and Other Related Charges

	Three Months Ended June 30,		Change	
	2023	2022	\$	%
	(in thousands, except percentages)			
Restructuring and other related charges	\$ 943	\$ -	\$ 943	100%
Percentage of revenue	0%	0%		

Restructuring and other related charges increased by \$0.9 million during the three months ended June 30, 2023 compared to the three months ended June 30, 2022 primarily due to our restructuring actions to adjust cost structure. See Note 12 to our condensed consolidated financial statements for further information.

Other Income (Expense), Net

	Three Months Ended June 30,		Change	
	2023	2022	\$	%
	(in thousands, except percentages)			
Other income, net	\$ 17,610	\$ 1,186	\$ 16,424	1385%

Other income, net increased by \$16.4 million during the three months ended June 30, 2023 compared to the three months ended June 30, 2022 primarily due to higher yields on marketable securities.

Provision for (Benefit from) Income Taxes

	Three Months Ended June 30,		Change	
	2023	2022	\$	%
	(in thousands, except percentages)			
Loss before income taxes	\$ (101,758)	\$ (116,121)	\$ 14,363	(12)%
Provision for income taxes	1,667	1,510	157	10%
Effective tax rate	(1.6)%	(1.3)%		

The provision for income taxes during the three months ended June 30, 2023 and 2022 were primarily driven by foreign and state income taxes.

We maintain a full valuation allowance on our U.S. and U.K. deferred tax assets. Our effective tax rate may fluctuate to the extent the mix of earnings fluctuates between jurisdictions with different tax rates.

Comparison of the Six Months Ended June 30, 2023 and 2022
Revenue

	Six Months Ended June 30,		Change	
	2023	2022	\$	%
	(in thousands, except percentages)			
Subscription	\$ 337,055	\$ 240,938	\$ 96,117	40%
Services	26,532	24,608	1,924	8%
Total revenue	\$ 363,587	\$ 265,546	\$ 98,041	37%

Subscription revenue increased by \$96.1 million during the six months ended June 30, 2023 compared to the six months ended June 30, 2022. The increase in revenue was primarily from sales to existing customers and the remaining increase was attributable to sales to new customers. Sales to new customers represent the revenue recognized from customers acquired in the 12 months prior to each discrete quarter end within the six months ended June 30, 2023. A further indication of our ability to expand from existing customers is through our dollar-based net retention rate of over 130% as of June 30, 2023. Confluent Platform and Confluent Cloud contributed 53% and 47% of our subscription revenue during the six months ended June 30, 2023, respectively, compared to 64% and 36% during the six months ended June 30, 2022, respectively.

Services revenue increased by \$1.9 million during the six months ended June 30, 2023 compared to the six months ended June 30, 2022 primarily due to an increase in delivery of professional services.

Cost of Revenue, Gross Profit, and Gross Margin

	Six Months Ended June 30,		Change	
	2023	2022	\$	%
	(in thousands, except percentages)			
Cost of revenue				
Subscription	\$ 87,093	\$ 69,211	\$ 17,882	26%
Services	28,971	26,075	2,896	11%
Total cost of revenue	\$ 116,064	\$ 95,286	\$ 20,778	22%
Gross profit	\$ 247,523	\$ 170,260	\$ 77,263	45%

	Six Months Ended June 30,	
	2023	2022
Gross margin		
Subscription	74%	71%
Services	(9)%	(6)%
Total gross margin	68%	64%

Cost of subscription revenue increased by \$17.9 million during the six months ended June 30, 2023 compared to the six months ended June 30, 2022. This increase was primarily due to an increase of \$10.0 million in third-party cloud infrastructure costs and an increase of \$8.0 million in personnel-related costs and allocated overhead costs. The increase in personnel-related costs was mainly driven by increased headcount and an increase of \$1.9 million in stock-based compensation expense.

Cost of services revenue increased by \$2.9 million during the six months ended June 30, 2023 compared to the six months ended June 30, 2022. This increase was primarily due to an increase of \$4.5 million in personnel-related costs and allocated overhead costs driven by increased headcount, offset by a decrease of \$1.5 million in costs for third-party contractors and partners who supplement our services delivery team. The increase in personnel-related costs included an increase of \$1.7 million in stock-based compensation expense.

Our subscription gross margin increased primarily due to economies of scale resulting from increased efficiency and optimization of our infrastructure, offset by a change in our revenue mix toward Confluent Cloud which has a lower gross margin. Our services gross margin decreased primarily due to personnel-related costs, including stock-based compensation expense, growing at a higher rate than services revenue.

Research and Development

	Six Months Ended June 30,		Change	
	2023	2022	\$	%
	(in thousands, except percentages)			
Research and development	\$ 170,567	\$ 122,133	\$ 48,434	40%
Percentage of revenue	47%	46%		

Research and development expenses increased by \$48.4 million during the six months ended June 30, 2023 compared to the six months ended June 30, 2022. This increase was primarily due to an increase of \$34.6 million in personnel-related costs and allocated overhead costs and an increase of \$11.5 million in acquisition-related compensation costs. The increase in personnel-related costs was mainly driven by increased headcount and an increase of \$20.0 million in stock-based compensation expense, net of amounts capitalized.

Sales and Marketing

	Six Months Ended June 30,		Change	
	2023	2022	\$	%
	(in thousands, except percentages)			
Sales and marketing	\$ 256,394	\$ 219,456	\$ 36,938	17%
Percentage of revenue	71%	83%		

Sales and marketing expenses increased by \$36.9 million during the six months ended June 30, 2023 compared to the six months ended June 30, 2022. This increase was primarily due to an increase of \$30.9 million in personnel-related costs and allocated overhead costs and an increase of \$4.1 million in amortization of deferred contract acquisition costs. The increase in personnel-related costs was mainly driven by increased headcount and an increase of \$15.6 million in stock-based compensation expense.

General and Administrative

	Six Months Ended June 30,		Change	
	2023	2022	\$	%
	(in thousands, except percentages)			
General and administrative	\$ 71,698	\$ 57,460	\$ 14,238	25%
Percentage of revenue	20%	22%		

General and administrative expenses increased by \$14.2 million during the six months ended June 30, 2023 compared to the six months ended June 30, 2022. This increase was primarily due to an increase of \$11.2 million in personnel-related costs and allocated overhead costs and an increase of \$1.2 million in professional services fees. The increase in personnel-related costs was mainly driven by increased headcount and an increase of \$6.0 million in stock-based compensation expense.

Restructuring and Other Related Charges

	Six Months Ended June 30,		Change	
	2023	2022	\$	%
	(in thousands, except percentages)			
Restructuring and other related charges	\$ 34,325	\$ -	\$ 34,325	100%
Percentage of revenue	9%	0%		

Restructuring and other related charges increased by \$34.3 million during the six months ended June 30, 2023 compared to the six months ended June 30, 2022 primarily due to our restructuring actions to adjust cost structure and real estate footprint. See Note 12 to our condensed consolidated financial statements for further information.

Other Income (Expense), Net

	Six Months Ended June 30,		Change	
	2023	2022	\$	%
	(in thousands, except percentages)			
Other income, net	\$ 32,795	\$ 370	\$ 32,425	8764%

Other income, net increased by \$32.4 million during the six months ended June 30, 2023 compared to the six months ended June 30, 2022 primarily due to higher yields on marketable securities.

Provision for (Benefit from) Income Taxes

	Six Months Ended June 30,		Change	
	2023	2022	\$	%
	(in thousands, except percentages)			
Loss before income taxes	\$ (252,666)	\$ (228,419)	\$ (24,247)	11%
Provision for income taxes	3,314	2,199	1,115	51%
Effective tax rate	(1.3)%	(1.0)%		

The provision for income taxes during the six months ended June 30, 2023 and 2022 were primarily driven by foreign and state income taxes.

We maintain a full valuation allowance on our U.S. and U.K. deferred tax assets. Our effective tax rate may fluctuate to the extent the mix of earnings fluctuates between jurisdictions with different tax rates.

Liquidity and Capital Resources

To date, we have financed operations primarily through proceeds received from issuances of equity and debt securities and payments received from our customers. In June 2021, our initial public offering resulted in proceeds of \$786.6 million, net of underwriting discounts and commissions. In December 2021, we issued \$1.1 billion aggregate principal amount of 0% convertible senior notes due 2027 (the "2027 Notes") in a private placement to qualified institutional buyers pursuant to Rule 144A under the Securities Act. The net proceeds from the issuance of the 2027 Notes, after deducting the initial purchasers' discounts and commissions and debt issuance costs, were \$1,080.5 million.

As of June 30, 2023, our principal sources of liquidity were cash, cash equivalents, and marketable securities totaling \$1,847.6 million. Our cash, cash equivalents, and marketable securities consist of bank deposits, money market funds, corporate notes and bonds, commercial paper, U.S. agency obligations, and U.S. treasury securities. We believe that existing cash, cash equivalents, marketable securities, and cash flow from operations will be sufficient to fund our short-term and long-term operating and capital needs, including our purchase obligations primarily related to our non-cancelable agreements for third-party cloud infrastructure, and operating lease commitments primarily related to our office space.

We have generated significant operating losses and negative cash flows from operations. As of June 30, 2023, we had an accumulated deficit of \$1,457.4 million. We may require additional capital resources to execute strategic initiatives to grow our business. Our future capital requirements will depend on many factors including our growth rate, the timing and extent of spending to support development efforts, the expansion of sales and marketing and international operations, and the continuing market acceptance of our subscriptions and services. We may be required to seek additional equity or debt financing. In the event that additional financing is required from outside sources, we may not be able to raise it on terms acceptable to us or at all. If we are unable to raise additional capital when desired, our business, results of operations, and financial condition would be adversely affected.

The following table summarizes our cash flows for the periods presented:

	Six Months Ended June 30,	
	2023	2022
	(in thousands)	
Net cash used in operating activities	\$ (106,832)	\$ (88,503)
Net cash used in investing activities	\$ (81,424)	\$ (803,539)
Net cash provided by financing activities	\$ 65,221	\$ 45,803

Cash Flows from Operating Activities

We generally invoice our customers annually in advance for our term-based licenses and typically annually in advance or monthly in arrears for our SaaS offering. Our largest source of operating cash is payments received from our customers. We have in the past and expect in the future to experience seasonality, with the fourth quarter historically being our strongest quarter for sales to customers as a result of large enterprise buying patterns. Accordingly, the operating cash flow benefit from increased collections from our customers generally occurs in the subsequent quarter after billing. We expect seasonality, timing of billings, and collections from our customers to have a material impact on our cash flow from operating activities from period to period. Our primary uses of cash from operating activities are for personnel-related expenses, third-party cloud infrastructure costs, sales and marketing expenses, and overhead expenses.

Cash used in operating activities of \$106.8 million for the six months ended June 30, 2023 primarily consisted of our net loss of \$256.0 million, adjusted for non-cash charges of \$200.2 million, and net cash outflows of \$51.1 million from changes in our operating assets and liabilities, net of the effects of a business combination. Our non-cash charges included \$171.4 million of stock-based compensation expense, net of amounts capitalized, \$21.5 million of amortization of deferred contract acquisition costs, \$15.7 million of lease abandonment charges, and \$6.4 million of depreciation and amortization of property equipment and acquired intangible assets, partially offset by \$19.7 million of net accretion of discounts and amortization of premiums on marketable securities. The main drivers of the changes in operating assets and liabilities, net of the effects of a business combination, were a \$24.0 million increase in deferred contract acquisition costs due to our increased sales, an \$18.7 million decrease in accounts payable due to timing of payments, and a \$11.3 million increase in accounts receivable due to overall growth of our sales, partially offset by a \$7.6 million increase in accrued expenses and other liabilities due to the timing of accruals and payments.

Cash used in operating activities of \$88.5 million for the six months ended June 30, 2022 primarily consisted of our net loss of \$230.6 million, adjusted for non-cash charges of \$153.9 million, and net cash outflows of \$11.8 million from changes in our operating assets and liabilities. Our non-cash charges included \$126.2 million of stock-based compensation expense, net of amounts capitalized, \$17.4 million of amortization of deferred contract acquisition costs, and \$4.5 million of non-cash operating lease costs. The main drivers of the changes in operating assets and liabilities were a \$22.7 million increase in deferred contract acquisition costs due to our increased sales, a \$20.1 million increase in prepaid expenses and other assets primarily driven by prepaid third-party cloud infrastructure, and a \$12.5 million increase in accounts receivable due to overall growth of our sales and our expanding customer base, partially offset by a \$39.3 million increase in deferred revenue corresponding with our increased sales.

Cash Flows from Investing Activities

Cash used in investing activities of \$81.4 million for the six months ended June 30, 2023 was primarily due to purchases of marketable securities of \$999.8 million, cash paid for a business combination, net of cash acquired of \$45.8 million, and capitalized internal-use software development costs of \$9.9 million, partially offset by maturities of marketable securities of \$975.4 million.

Cash used in investing activities of \$803.5 million for the six months ended June 30, 2022 was primarily due to purchases of marketable securities of \$1,167.4 million and capitalized internal-use software development costs of \$4.8 million, partially offset by maturities of marketable securities of \$370.7 million.

Cash Flows from Financing Activities

Cash provided by financing activities of \$65.2 million for the six months ended June 30, 2023 was primarily due to \$48.3 million in proceeds from the issuance of common stock upon exercises of stock options and \$17.2 million in proceeds from the issuance of common stock under our employee stock purchase plan.

Cash provided by financing activities of \$45.8 million for the six months ended June 30, 2022 was primarily due to \$24.8 million in proceeds from the issuance of common stock upon exercises of stock options, and \$22.5 million in proceeds from the issuance of common stock under our employee stock purchase plan.

Critical Accounting Estimates

Our condensed consolidated financial statements and the related notes thereto included elsewhere in this Quarterly Report on Form 10-Q are prepared in accordance with generally accepted accounting principles in the United States, or U.S. GAAP. The preparation of these condensed consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, costs and expenses, and related disclosures. We evaluate our estimates and assumptions on an ongoing basis. Our estimates are based on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. Actual results could differ significantly from the estimates made by management. To the extent that there are differences between our estimates and actual results, our financial condition, results of operations, and cash flows will be affected.

There have been no material changes to our critical accounting estimates as compared to those described in “Management’s Discussion and Analysis of Financial Condition and Results of Operations” set forth in our Annual Report.

Recent Accounting Pronouncements

See Note 2, *Basis of Presentation and Summary of Significant Accounting Policies*, to our condensed consolidated financial statements included elsewhere in this Quarterly Report on Form 10-Q for recent accounting pronouncements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

Market risk represents the risk of loss that may impact our financial position due to adverse changes in financial market prices and rates. We have operations both within the United States and internationally, and we are exposed to market risk in the ordinary course of our business.

Interest Rate Risk

As of June 30, 2023, we had \$1,847.6 million of cash, cash equivalents, and marketable securities in a variety of securities, including money market funds, corporate notes and bonds, commercial paper, U.S. agency obligations, and U.S. treasury securities. Our cash, cash equivalents, and marketable securities are held for working capital purposes. We do not enter into investments for trading or speculative purposes. The effect of a hypothetical 10% relative change in interest rates would not have a material impact on the fair value of our cash equivalents and marketable securities as of June 30, 2023.

In December 2021, we issued \$1.1 billion aggregate principal amount of 0% convertible senior notes due 2027 (the “2027 Notes”) in a private placement to qualified institutional buyers pursuant to Rule 144A under the Securities Act. The fair value of the 2027 Notes are subject to market risk and other factors due to the conversion feature. The fair value of the 2027 Notes will generally increase as our Class A common stock price increases, and will generally decrease as our Class A common stock price declines. The market value changes affect the fair value of the 2027 Notes, but do not impact our financial position, cash flows or results of operations due to the fixed nature of the debt obligation. Additionally, we carry the 2027 Notes at face value less unamortized debt issuance costs on our condensed consolidated balance sheet, and we present the fair value for required disclosure purposes only.

Foreign Currency Risk

Our reporting currency and the functional currency of our wholly-owned foreign subsidiaries is the U.S. dollar. All of our sales contracts are denominated in U.S. dollars, and therefore our revenue is not currently subject to significant foreign currency risk. A portion of our operating expenses is incurred outside the United States and denominated in foreign currencies and is subject to fluctuations due to changes in foreign exchange rates.

To reduce the impact of foreign currency fluctuations, we established a hedging program in December 2022. See Note 5 to our condensed consolidated financial statements for additional information. Our hedging program reduces but does not eliminate the impact of currency exchange rate movements.

The effect of a hypothetical 10% relative change in foreign exchange rates, after considering our hedging program, would not have a material impact on our financial condition, results of operations, or cash flows for the periods presented. As our international operations grow, we will continue to reassess our approach to manage our risk relating to fluctuations in foreign exchange rates.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q. The term “disclosure controls and procedures,” as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to provide reasonable assurance that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company’s management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this Quarterly Report on Form 10-Q, our disclosure controls and procedures were effective at the reasonable assurance level.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting identified in connection with the evaluation required by Rule 13a-15(d) and 15d-15(d) of the Exchange Act that occurred during the period covered by this Quarterly Report on Form 10-Q that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Inherent Limitations on Effectiveness of Controls

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

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

From time to time, we have been and will continue to be subject to legal proceedings and claims. We are not presently a party to any legal proceedings that, if determined adversely to us, would individually or taken together have a material adverse effect on our business, results of operations, financial condition, or cash flows. Defending such proceedings is costly and can impose a significant burden on management and employees. The results of any current or future litigation cannot be predicted with certainty, and regardless of the outcome, litigation can have an adverse impact on us because of defense and settlement costs, diversion of management resources, and other factors.

ITEM 1A. RISK FACTORS

Investing in our Class A common stock involves a high degree of risk. You should consider and read carefully all of the risks and uncertainties described below, as well as other information included in this Quarterly Report on Form 10-Q, including our consolidated financial statements and related notes appearing elsewhere in this Quarterly Report on Form 10-Q, before making an investment decision. The risks described below are not the only ones we face. The occurrence of any of the following risks or additional risks and uncertainties not presently known to us or that we currently believe to be immaterial could materially and adversely affect our business, financial condition, or results of operations. In such case, the trading price of our Class A common stock could decline, and you may lose some or all of your original investment. You should not interpret our disclosure of any of the following risks to imply that such risks have not already materialized.

Risk Factors Summary

Below is a summary of the principal factors that make an investment in our Class A common stock speculative or risky:

- Our recent rapid growth may not be indicative of our future growth. Our rapid growth also makes it difficult to evaluate our future prospects and may increase the risk that we will not be successful.
- We have a history of operating losses and may not achieve or sustain profitability in the future. In particular, we have limited experience operating our business at current scale under economic conditions characterized by high inflation or in recessionary or uncertain economic environments.
- Macroeconomic uncertainty, unfavorable conditions in our industry or the global economy, including those caused by the ongoing conflict between Russia and Ukraine, reductions in information technology spending, or inflation, have impacted and may continue to impact our ability to grow our business and negatively affect our results of operations.
- Actions that we are taking to restructure our business in alignment with our strategic priorities may not be as effective as anticipated.
- We derive substantially all of our revenue from our data-in-motion offering. Failure of our offering to satisfy customer demands or achieve continued market acceptance over competitors, including open source alternatives, would harm our business, results of operations, financial condition, and growth prospects.
- We intend to continue investing significantly in Confluent Cloud, and if it fails to achieve further market adoption, our growth, business, results of operations, and financial condition could be harmed.
- Failure to effectively develop and expand our sales and marketing capabilities or improve the productivity of our sales and marketing organization could harm our ability to expand our potential customer and sales pipeline, increase our customer base, and achieve broader market acceptance of our offering.
- If we are unable to attract new customers or expand our potential customer and sales pipeline, our business, financial condition, and results of operations will be adversely affected.
- Our business depends on our existing customers renewing their subscriptions and usage-based minimum commitments, purchasing additional subscriptions and usage-based minimum commitments, and expanding their use of our offering.
- If we fail to maintain and enhance our brand, including among developers, our ability to expand our customer base will be impaired and our business, financial condition, and results of operations may suffer.
- The markets in which we participate are competitive, and if we do not compete effectively, our business, financial condition, and results of operations could be harmed.

- If we or third parties with whom we work experience a security breach, or if the confidentiality, integrity, or availability of our information technology, software, services, communications, or data is compromised, our offering may be perceived as not being secure, our reputation may be harmed, demand for our offering may be reduced, proprietary data and information, including source code, could be, and has in the past been, exfiltrated, and we may incur significant liabilities.
- We rely on third-party providers of cloud-based infrastructure to host Confluent Cloud. Any failure to adapt our offering to evolving network architecture technology, disruption in the operations of these third-party providers, limitations on capacity or use of features, or interference with our use could adversely affect our business, financial condition, and results of operations.
- We expect fluctuations in our financial results and key metrics, making it difficult to project future results, and if we fail to meet the expectations of securities analysts or investors with respect to our results of operations, our stock price and the value of your investment could decline.
- The dual class structure of our common stock as contained in our amended and restated certificate of incorporation has the effect of concentrating voting control with those stockholders who held our stock prior to the IPO, including our executive officers, employees, and directors and their affiliates, and limiting your ability to influence corporate matters, which could adversely affect the trading price of our Class A common stock.

Risks Related to Our Business and Operations

Our recent rapid growth may not be indicative of our future growth. Our rapid growth also makes it difficult to evaluate our future prospects and may increase the risk that we will not be successful.

Our revenue was \$585.9 million, \$387.9 million, and \$236.6 million for the years ended December 31, 2022, 2021, and 2020, respectively and \$363.6 million and \$265.5 million for the six months ended June 30, 2023 and 2022, respectively. You should not rely on the revenue growth of any prior period as an indication of our future performance. Our revenue growth rate has declined from time to time, and may decline in the future, as a result of a variety of factors, including our focus on operating efficiency and margin improvement, the effectiveness of our sales and marketing strategies and function, our ability to continue gaining market acceptance of our offering, macroeconomic challenges and uncertainty, increased competition, and changes to technology. Overall growth of our revenue depends on a number of factors, including our ability to:

- market and price our offering effectively so that we are able to attract new customers and expand sales to our existing customers;
- invest in the growth of our business while adjusting our cost structure to focus on operating efficiency and improved margins;
- successfully develop a substantial customer and sales pipeline for our products;
- expand the features and functionality of our offering to enable additional use cases for our customers;
- continue investing in our sales and marketing function to support our growth, and reduce the time for new sales personnel to achieve desired productivity levels;
- extend our product leadership to expand our addressable market;
- differentiate our offering from open source alternatives and products offered by our competitors;
- maintain and expand the rates at which new customers purchase and existing customers renew subscriptions and committed use of our offering and increase consumption of our offering, including in light of the evolving macroeconomic environment;
- provide our customers with support that meets their needs;

- expand our partner ecosystem, including with major cloud providers, independent software vendors (ISVs), and regional and global systems integrators;
- increase awareness of our brand on a global basis to successfully compete with other companies; and
- expand to new international markets and grow within existing markets.

We may not successfully accomplish any of these objectives, and as a result, it is difficult for us to forecast our future results of operations. If the assumptions that we use to plan our business are incorrect or change in reaction to changes in our market, or if we are unable to maintain consistent revenue or revenue growth, our stock price could be volatile, and it may be difficult to achieve and maintain profitability. As a result of our rapid revenue growth in prior periods, we expect our revenue growth rate to decline in future periods. You should not rely on our revenue for any prior quarterly or annual periods as any indication of our future revenue or revenue growth.

In addition, we expect to continue to expend substantial financial and other resources on:

- expansion and enablement of our sales, services, and marketing organization to increase brand awareness and drive adoption of our offering;
- product development, including investments in our product development team and the development of new products and new features and functionality for our offering to expand use cases and provide feature parity across third-party public cloud platforms, as well as investments in further differentiating our existing offering;
- our cloud infrastructure technology, including systems architecture, scalability, availability, performance, and security;
- technology and sales channel partnerships, including cloud marketplaces;
- international expansion;
- acquisitions or strategic investments; and
- general administration, including increased legal and accounting expenses associated with being a public company.

These investments may not result in increased revenue in our business. If we are unable to maintain or increase our revenue at a rate sufficient to offset the expected increase in our costs, our business, financial position and results of operations will be harmed, and we may not be able to achieve or maintain profitability. Additionally, we may encounter unforeseen operating expenses, difficulties, complications, delays, and other unknown factors that may result in losses in future periods. If our revenue does not meet our expectations in future periods, our business, financial position, and results of operations may be harmed.

We have a history of operating losses and may not achieve or sustain profitability in the future.

We have experienced net losses in each period since inception. We generated a net loss of \$452.6 million, \$342.8 million, and \$229.8 million for the years ended December 31, 2022, 2021, and 2020, respectively and \$256.0 million and \$230.6 million for the six months ended June 30, 2023 and 2022, respectively. As of June 30, 2023, we had an accumulated deficit of \$1,457.4 million. While we have experienced significant revenue growth in recent periods, we are not certain whether or when we will obtain or maintain a high enough volume of sales or level of market acceptance to achieve or maintain profitability in the future. Our revenue growth rate has declined, and may continue to decline for a number of reasons, particularly during times of macroeconomic uncertainty, resulting in a more challenging environment for acquiring new customers and maintaining existing customers as well as shifts in priorities toward operating efficiencies and margin improvements. We also expect our costs and expenses to increase in future periods, which could negatively affect our future results of operations if our revenue does not increase. In particular, we intend to continue to expend significant funds to further develop our offering, including by introducing new offerings and features and functionality, and to expand our sales, marketing, and services teams to drive new customer adoption, expand the use of our offering by existing customers, support international expansion, and implement additional systems and processes to effectively scale operations. We will also face increased compliance costs associated with growth, the planned expansion of our customer base and pipeline, international expansion, and being a public company. In addition, Confluent Cloud operates on public cloud infrastructure provided by third-party vendors, and our costs and gross margins are significantly influenced by the prices we are able to negotiate with these public cloud providers, which in many cases are also our competitors. To the extent we are able to successfully increase the percentage of our revenue attributable to Confluent Cloud, we may incur increased costs related to our public cloud contracts, which would negatively impact our gross margins. Our efforts to grow our business may be costlier than we expect, or the rate of our growth in revenue may be slower than we expect, and we may not be able to increase our revenue enough to offset our increased operating expenses. In addition, our efforts and investments to implement systems and processes to scale operations may not be sufficient or may not be appropriately executed. As a result, we may incur significant losses in the future for a number of reasons, including the other risks described herein, and unforeseen expenses, difficulties, complications or delays, and other unknown events. If we are unable to achieve and sustain profitability, the value of our business and Class A common stock may significantly decrease.

We have a limited operating history, which makes it difficult to forecast our future results of operations.

We were founded in 2014. As a result of our limited operating history, our ability to accurately forecast our future results of operations is limited and subject to a number of uncertainties, including our ability to plan for and model future growth. Our historical revenue growth should not be considered indicative of our future performance. In particular, we have limited experience operating our business at current scale under economic conditions characterized by high inflation or in recessionary or uncertain economic environments. We recently also undertook an internal restructuring, including a reduction in force, and increased focus on operating efficiencies and margin improvements. Further, we have experienced, and in future periods, may continue to experience, slower revenue growth or our revenue could decline for a number of reasons, including shifts in our offering and revenue mix, slowing demand for our offering, increasing competition, decreased productivity of our sales and marketing organization and effectiveness of our sales and marketing efforts to acquire new customers, retain existing customers or expand existing subscriptions and usage-based minimum commitments, strategic focus on operating efficiencies and margin improvements, changing technology, a decrease in the growth of our overall market, our failure, for any reason, to continue to take advantage of growth opportunities, or our failure to adapt and respond to inflationary factors affecting our business or future economic recessions. We have also encountered, and will continue to encounter, risks and uncertainties frequently experienced by growing companies in rapidly changing industries, such as the risks and uncertainties described in this Quarterly Report. If our assumptions regarding these risks and uncertainties and our future revenue growth are incorrect or change, or if we do not address these risks successfully, our operating and financial results could differ materially from our expectations, and our business could suffer.

Macroeconomic uncertainty, unfavorable conditions in our industry or the global economy, including those caused by the ongoing conflict between Russia and Ukraine, reductions in information technology spending, or inflation, have impacted, and may continue to impact our ability to grow our business and negatively affect our results of operations.

Global business activities face widespread macroeconomic uncertainties, and our results of operations may vary based on the impact of changes in our industry or the global economy on us or our customers and potential customers. Negative conditions in the general economy both in the United States and abroad, including conditions resulting from changes in gross domestic product growth, financial and credit market fluctuations, inflation and efforts to control further inflation, including rising interest rates, bank failures, international trade relations, political turmoil, natural catastrophes, warfare, and terrorist attacks on the United States, Europe, the Asia Pacific region, including Japan, or elsewhere, could cause a decrease in business investments by existing or potential customers, including spending on information technology, and negatively affect the growth of our business. As an example, in the United States, capital markets have experienced and continue to experience volatility and disruption. Furthermore, inflation rates in the United States have recently increased to levels not seen in decades resulting in federal action to increase interest rates, affecting capital markets. In addition to the foregoing, adverse developments that affect financial institutions, transactional counterparties or other third parties, such as bank failures, or concerns or speculation about any similar events or risks, could lead to market-wide liquidity problems, which in turn may cause third parties, including customers, to become unable to meet their obligations under various types of financial arrangements as well as general disruptions or instability in the financial markets. Such economic volatility could adversely affect our business, financial condition, results of operations and cash flows, and future market disruptions could negatively impact us. In particular, we have experienced and may continue to experience longer sales cycles for new customers and existing customer expansions, reduced contract sizes or generally increased scrutiny on IT spending and budgets from existing and potential customers, due in part to the effects of macroeconomic uncertainty and challenges and the geopolitical situation in Ukraine. These customer dynamics may persist in the future, even if macroeconomic conditions improve, and to the extent there is a sustained general economic downturn, a recession, or other period when IT budgets are growing at a slower rate or contracting growth, these customer dynamics may be exacerbated. These customer dynamics have had and may continue to have negative impacts on our revenue, business, and results of operations and have resulted and may in the future result in strategic changes in our focus on growth versus operating efficiency, margin improvements, and profitability. For example, we recently adjusted our cost structure and reduced our overall headcount. Competitors, many of whom are larger and have greater financial resources than we do, may respond to challenging market conditions by lowering prices in an attempt to attract our customers, which may require us to respond in kind and may negatively impact our existing customer relationships and new customer acquisition strategy. In addition, the increased pace of consolidation in certain industries may result in reduced overall spending on our offering. We cannot predict the timing, strength, or duration of any economic slowdown, instability, or recovery, generally or within any particular industry.

Actions that we are taking to restructure our business in alignment with our strategic priorities may not be as effective as anticipated.

In January 2023, we commenced certain restructuring actions, or the Restructuring Plan, designed to adjust our cost structure and real estate footprint. We may encounter challenges in the execution of these efforts, and these challenges could impact our financial results.

Although we believe that the Restructuring Plan will reduce operating costs and improve operating margins, we cannot guarantee that the Restructuring Plan will achieve or sustain the targeted benefits, or that the benefits, even if achieved, will be adequate to meet our long-term profitability and operational expectations. As a result of these actions, we will incur additional costs in the near term, including cash expenditures for employee transition, notice period and severance payments, employee benefits, and related facilitation costs. Additional risks associated with the continuing impact of the Restructuring Plan include employee attrition beyond our intended reduction in force and adverse effects on employee morale (which may also be further exacerbated by actual or perceived declining value of equity awards), diversion of management attention, adverse effects to our reputation as an employer (which could make it more difficult for us to hire new employees in the future), and potential failure or delays to meet operational and growth targets due to the loss of qualified employees. If we do not realize the expected benefits of our Restructuring Plan on a timely basis or at all, our business, results of operations and financial condition could be adversely affected.

We derive substantially all of our revenue from our data-in-motion offering. Failure of our offering to satisfy customer demands or achieve continued market acceptance over competitors, including open source alternatives, would harm our business, results of operations, financial condition, and growth prospects.

We derive and expect to continue to derive substantially all of our revenue from sales of, and additional services related to, our data-in-motion offering. We have directed, and intend to continue to direct, a significant portion of our financial and operating resources to developing more features and functionality for such offering. Our growth will depend in large part on enabling additional use cases for our customers after they initially adopt our offering, ranging from industry-specific use cases to use cases generated by the network effects of connecting multiple applications within an enterprise. In addition, the success of our business is substantially dependent on the actual and perceived viability, benefits, and advantages of our offering as a preferred platform for data in motion, particularly when compared to open source alternatives developed internally by customers. As such, market adoption of our offering is critical to our continued success. Demand for our offering is affected by a number of factors, including increased market acceptance of our offering by existing customers and potential new customers, effectiveness of our sales and marketing strategy and team, the extension of our offering to new applications and use cases, the timing of development and release of new offerings by us and our competitors, technological change, growth or contraction of the market in which we compete, and customer information technology spending budgets, which may be reduced during periods of high inflation or in recessionary or uncertain economic environments and may be impacted by geopolitical events such as the ongoing conflict between Russia and Ukraine. Failure to successfully address these factors, satisfy customer demands, achieve continued market acceptance over competitors, including open source alternatives, and achieve growth in sales of our offering would harm our business, results of operations, financial condition, and growth prospects.

We have historically derived a substantial portion of our revenue from Confluent Platform, and any loss in market acceptance or reduction in sales of Confluent Platform would harm our business, results of operations, financial condition, and growth prospects.

While our revenue mix has increasingly shifted toward Confluent Cloud, our business remains substantially dependent on Confluent Platform, our enterprise-ready, self-managed software offering. Confluent Platform contributed 61% and 73% of our subscription revenue for the years ended December 31, 2022 and 2021, respectively and 53% and 64% of our subscription revenue for the six months ended June 30, 2023 and 2022, respectively. We expect to continue to rely on customer adoption and expansion of Confluent Platform as a component of our future growth. In particular, we are dependent on Confluent Platform serving as a fundamental self-managed, data-in-motion offering to generate wide-ranging use cases for our customers and increase our dollar-based net retention rate with existing customers. If we experience loss in market acceptance, reduced customer renewals or new customer adoption, or limited use case expansion among existing customers of Confluent Platform, our growth, business, financial condition, and results of operations may be harmed.

We intend to continue investing significantly in Confluent Cloud, and if it fails to achieve further market adoption, our growth, business, results of operations, and financial condition could be harmed.

We intend to continue investing significantly in developing and growing Confluent Cloud as a fully-managed, cloud-native service. We have less experience marketing, determining pricing for, and selling Confluent Cloud. As a result, our shifts in sales strategy focused on customer acquisition for Confluent Cloud could result in near term fluctuations in our financial results as compared to prior periods, particularly if previous Confluent Platform customers shift to Confluent Cloud, given that subscriptions to Confluent Cloud have historically had a lower average price compared to subscriptions to Confluent Platform. Our sales strategy for Confluent Cloud also involves landing customers at low entry points, including starting with our free Confluent Cloud trial and pay-as-you-go, which have no commitments. There can be no assurance that such customers will enter into usage-based minimum commitments with us, expand their existing commitments, or ramp their usage of Confluent Cloud. In addition, there can be no assurance as to the length of time required to attain substantial market adoption of Confluent Cloud, if at all. The growth rate of our Confluent Cloud revenue may also fluctuate over time, including due to the usage-based nature of Confluent Cloud and customer adoption trends. To expand our potential customer and sales pipeline for Confluent Cloud, we will need to increase brand awareness, cultivate relationships with potential customers in key industries and sectors, rapidly convert the sales pipeline into new customers and continue to expand and improve the productivity of our sales and marketing organization. To increase market adoption and expand the customer base for Confluent Cloud, we have also been targeting the commercial customer segment, comprised of small to medium-sized companies, including early-stage companies, as part of our overall sales and marketing strategy for Confluent Cloud. These customers typically demand faster deployment of Confluent Cloud within their organizations and prioritize ease of use. In addition, the sales cycle for these customers is typically shorter, requiring accelerated ramp time of our sales force and higher velocity marketing strategies. We have also historically targeted larger enterprise customers as part of our overall sales and marketing strategy, which we refine from time to time, partly due to the relative size and complexity of such customers and the efforts needed to expand their usage of Confluent Cloud. If we are unsuccessful in these and our other efforts to drive market adoption of and expand the customer base for Confluent Cloud, or if we do so in a way that is not profitable, fails to compete successfully against our current or future competitors, or fails to adequately differentiate Confluent Cloud from open source alternatives, our growth, business, results of operations, and financial condition could be harmed.

We may not be able to successfully manage our growth, and if we are not able to grow efficiently, our business, financial condition, and results of operations could be harmed.

As usage and adoption of our offering grows, we will need to devote additional resources to improving our offering's capabilities, features, and functionality. In addition, we will need to appropriately scale our internal business operations and our services organization to serve our growing customer base. Any failure of or delay in these efforts could result in impaired product performance and reduced customer satisfaction, resulting in decreased sales to new customers, lower dollar-based net retention rates, or the issuance of service credits or requested refunds, which would hurt our revenue growth and our reputation. Further, any failure in optimizing the costs associated with our third-party cloud services as we scale could negatively impact our gross margins. Our expansion efforts will be expensive and complex, and require the dedication of significant management time and attention. We could also face inefficiencies, vulnerabilities or service disruptions as a result of our efforts to scale our internal infrastructure, which may result in extended outages, loss of customer trust, and harm to our reputation. We cannot be sure that the expansion of and improvements to our internal infrastructure will be effectively implemented on a timely basis, if at all, and such failures could harm our business, financial condition, and results of operations.

The markets in which we participate are competitive, and if we do not compete effectively, our business, financial condition, and results of operations could be harmed.

Our platform for data in motion combines and expands upon functionality from numerous traditional product categories, and hence we compete in each of these categories with products from a number of different vendors. Our primary competition, especially on-premise, is internal IT teams that develop data infrastructure software using open source software, including Apache Kafka. Our principal competitors in the cloud are the well-established public cloud providers that compete in their respective clouds. These enterprises are developing and have released managed service offerings for real-time data ingestion and data streaming, such as Azure Event Hubs (Microsoft Corporation), Amazon Kinesis, Amazon MSK, and Google Cloud Pub/Sub and Dataflow. On premise, there are a number of vendors with legacy products that have pivoted into this space including Cloudera Dataflow, TIBCO Messaging, and Red Hat AMQ Streams.

We currently offer Confluent Cloud on the public clouds provided by AWS, Azure, and GCP, which are also some of our primary actual and potential competitors. There is risk that one or more of these public cloud providers could use their respective control of their public clouds to embed innovations or privileged interoperating capabilities in competing products, bundle competing products, provide us unfavorable pricing, leverage their public cloud customer relationships to exclude us from opportunities, and treat us and our customers differently with respect to terms and conditions or regulatory requirements compared to similarly situated customers. In addition, if public cloud providers develop a data-in-motion offering that operates across multiple public clouds or on premise, we would face increased competition from these providers. Further, they have the resources to acquire or partner with existing and emerging providers of competing technologies and thereby accelerate adoption of those competing technologies. All of the foregoing could make it difficult or impossible for us to provide subscriptions and services that compete favorably with those of the public cloud providers.

With the introduction of new technologies, market entrants, and open source alternatives, including those based on Apache Kafka, we expect that the competitive environment will remain intense going forward. Because Apache Kafka is open source and there are few technological barriers to entry into the open source market, it may be relatively easier for competitors, some of which may have greater resources than we have, to enter our markets and develop data-in-motion alternatives based on Apache Kafka. In addition, the data infrastructure market is large and continues to grow rapidly, and our future success will depend in part on differentiating our offering from open source alternatives, including Apache Kafka, and other data-in-motion offerings. If we are unable to sufficiently differentiate our offering from Apache Kafka, other offerings based on or derived from Apache Kafka, or other data-in-motion offerings, we may not be successful in achieving market acceptance of our offering, which would limit our growth and future revenue. Some existing and prospective customers may elect to use certain of our data-in-motion platform functions under free-to-use licenses, which can reduce demand for our offering. Such existing or prospective customers may also have reservations about utilizing proprietary software like our offering and may instead opt to use solely open source software based on the perception that this will lower long-term costs and reduce dependence on third-party vendors. In addition, our existing customers have chosen or could in the future choose to develop similar capabilities in-house and strengthen their use of open source software, rather than continue to purchase our offering.

Some of our actual and potential competitors have been acquired by other larger enterprises and have made or may make acquisitions or may enter into partnerships or other strategic relationships that may provide more comprehensive offerings than they individually had offered or achieve greater economies of scale than us. Any trend toward industry consolidation may negatively impact our ability to successfully compete and may impose pressure on us to engage in similar strategic transactions, including acquisitions, which would be costly and may divert management's attention. In addition, new entrants not currently considered to be competitors may enter the market through acquisitions, partnerships, or strategic relationships. As we look to market and sell our offering and platform capabilities to potential customers with existing solutions, we must convince their internal stakeholders that the capabilities of our offering are superior to their current solutions.

We compete on the basis of a number of factors, including:

- ease of deployment, integration, and use;

- enterprise-grade data in motion;
- the cloud-native capabilities of our offering;
- the ability to operate at scale and offer elasticity, end-to-end security, and reliability;
- the completeness of our offering, including as a complete platform for data in motion, and our ability to offer rich SQL-based stream processing, integrated governance capabilities, and connectors to existing applications and IT and cloud infrastructure;
- the availability of our offering, including in multiple public clouds, and for use in private clouds and in on-premise data centers;
- quality of professional services and customer support;
- price and total cost of ownership;
- flexible pricing, such as pay-as-you-go delivery;
- sales and marketing productivity and expertise;
- brand recognition and reputation; and
- adherence to industry standards and certifications.

Our competitors vary in size and in the breadth and scope of the products offered. Many of our competitors and potential competitors have greater name recognition, longer operating histories, more established customer relationships and installed customer bases, larger marketing budgets and greater resources than we do. Further, other potential competitors not currently offering competitive solutions may expand their offerings to compete with our existing and new offering and platform capabilities. Additionally, our current and potential competitors may establish cooperative relationships among themselves or with third parties that may further enhance their resources and offerings in our addressable market. Our competitors may be able to respond more quickly and effectively than we can to new or changing opportunities, technologies, standards, and customer requirements. An existing competitor or new entrant could introduce new technology that reduces demand for our offering. In addition to product and technology competition, we face pricing competition. Some of our competitors offer their solutions at a lower price, which has resulted in, and may continue to result in, pricing pressures.

For all of these reasons, we may not be able to compete successfully against our current or future competitors, and this competition could result in the failure of our offering to continue to achieve or maintain market acceptance, any of which would harm our business, results of operations, and financial condition.

We expect fluctuations in our financial results and key metrics, making it difficult to project future results, and if we fail to meet the expectations of securities analysts or investors with respect to our results of operations, our stock price and the value of your investment could decline.

Our results of operations and key metrics, including RPO, ARR, NRR and customers with \$100,000 or greater in ARR, have fluctuated in the past and are expected to fluctuate in the future due to a variety of factors, many of which are outside of our control. As a result, our past results may not be indicative of our future performance and period-over-period comparisons of our operating results and key metrics may not be meaningful or accurately measure our business. In addition to the other risks described herein, factors that may affect our results of operations include the following:

- changes in our revenue mix as Confluent Cloud’s contribution to subscription revenue increases over time, and related changes in revenue recognition;
- changes in actual and anticipated growth rates of our revenue, customers, and key operating metrics, including due to changes in methodology for calculating certain of our key operating metrics;
- strategic shifts in focus on growth versus operating efficiency and profitability;
- fluctuations in demand for or pricing of our offering;
- fluctuations in usage of Confluent Cloud under usage-based minimum commitments and pay-as-you-go arrangements;
- our ability to attract new customers;
- our ability to retain our existing customers, particularly large customers, and secure renewals of subscriptions and usage-based minimum commitments, as well as the timing of customer renewals or non-renewals;
- customer retention rates and the pricing and quantity of subscriptions renewed, as well as our ability to accurately forecast customer expansions and renewals;
- downgrades in customer subscriptions;
- customers and potential customers opting for alternative products, including developing their own in-house solutions or opting to use only the free version of our offering;
- timing and amount of our investments to expand the capacity of our third-party cloud service providers;
- seasonality in sales, customer implementations, results of operations (including Confluent Cloud revenue), and remaining performance obligations, or RPO;
- investments in new offerings, features, and functionality;
- fluctuations or delays in development, release, or adoption of new features and functionality for our offering;
- delays in closing sales, including the timing of renewals, which may result in revenue being pushed into the next quarter, particularly because a large portion of our sales occur toward the end of each quarter;
- fluctuations or delays in purchasing decisions by existing or future customers, including due to geopolitical or economic conditions such as inflation or in anticipation of new offerings or enhancements by us or our competitors;
- changes in customers’ budgets and in the timing of their budget cycles and purchasing decisions, including due to macroeconomic factors and currency exchange rate fluctuations;

- our ability to control costs, including hosting costs associated with Confluent Cloud and our operating expenses, and to realize operating efficiencies in connection with the Restructuring Plan;
- the amount and timing of payment for operating expenses, particularly research and development and sales and marketing expenses, including commissions;
- timing of hiring personnel for our research and development and sales and marketing organizations;
- the amount and timing of non-cash expenses, including stock-based compensation expense and other non-cash charges;
- the amount and timing of costs associated with recruiting, educating, and integrating new employees and retaining and motivating existing employees;
- the effects of acquisitions and their integration;
- general geopolitical or economic conditions, both domestically and internationally, as well as economic conditions specifically affecting industries in which our customers participate;
- fluctuations in foreign currency exchange rates;
- the impact of new accounting pronouncements;
- changes in revenue recognition policies that impact our subscriptions and services revenue;
- changes in regulatory or legal environments that may cause us to incur, among other things, expenses associated with compliance;
- the impact of changes in tax laws or judicial or regulatory interpretations of tax laws, which are recorded in the period such laws are enacted or interpretations are issued and may significantly affect the effective tax rate of that period;
- health epidemics or pandemics, such as the COVID-19 pandemic;
- changes in the competitive dynamics of our market, including consolidation among competitors or customers; and
- significant security breaches of, technical difficulties with, or interruptions to, the delivery and use of our offering.

The calculation methodology of our key metrics, including adjustments in methodologies from time to time, may also result in fluctuations in period-over-period results that may not be indicative of our long-term performance or that result in differing interpretations of trends in our business. For example, commencing with the first quarter of 2023, we began calculating ARR with respect to Confluent Cloud customers by annualizing actual consumption of Confluent Cloud in the last three months of the applicable period, which impacted our methodology for NRR and customers over \$100,000 in ARR as well. See the section titled “Management’s Discussion and Analysis of Financial Condition and Results of Operations–Key Business Metrics.” While we believe this change in ARR methodology better aligns with how our management assesses ARR internally and better reflects actual customer behavior, it assumes Confluent Cloud consumption trends over 12-month periods based on three months of actual consumption, which does not account for future fluctuations and unpredictability in consumption rates or reflect trends in the growth or contraction of subscriptions over time. Further, we have experienced fluctuations in NRR and, as Confluent Cloud’s contribution to our revenue continues to increase, we may continue to experience increased volatility in NRR as our customers’ consumption trends may vary significantly across quarters for various reasons, including due to uncertainty in expected consumption ramp of a customer as well as factors outside our control such as macroeconomic uncertainty and its effects on customers’ IT spending and customers’ organizational and business changes. As a result, our short-term NRR trends may be less indicative of longer-term timing and pace of Confluent Cloud customer expansion.

Any of these and other factors, or the cumulative effect of some of these factors, may cause our results of operations to vary significantly. If our quarterly results of operations fall below the expectations of investors and securities analysts who follow our stock, the price of our Class A common stock could decline substantially, and we could face costly lawsuits, including securities class action suits.

Our revenue mix may result in fluctuations in our results across periods, making it difficult to assess our future growth.

Our revenue mix is varied based on the revenue recognition principles applicable to our offering. We recognize a portion of revenue from sales of subscriptions to Confluent Platform up front when our term-based license is delivered. The remainder, constituting post-contract customer support, maintenance, and upgrades, referred to together as PCS, comprises the substantial majority of the revenue and is recognized ratably over the subscription term. Customers may use Confluent Cloud either without a minimum commitment contract, which we refer to as pay-as-you-go, or on a usage-based minimum commitment contract of at least one year in duration. Pay-as-you-go customers are billed, and revenue from them is recognized, based on usage. Customers with usage-based minimum commitments are billed annually in advance or monthly in arrears, and we recognize revenue from such subscriptions based on usage by the customer. Historically, our Confluent Cloud sales have been individually smaller, with varied usage levels from such customers over time, which may continue as we target the commercial customer segment as part of our sales strategy for Confluent Cloud. However, larger Confluent Cloud sales, including those with terms over one year, may also result in greater variations in usage levels due to the timing and size of those commitments. In addition, we have experienced and expect to continue experiencing an increased contribution from Confluent Cloud to our revenue mix. Macroeconomic impacts have caused, and may continue to cause, longer sales cycles compared to prior periods. As a result, there may be fluctuations in revenue period over period as revenue is dependent on varying patterns of customer consumption and timing of sales of Confluent Platform, which can result in larger upfront revenue recognition upon delivery of the term-based licenses, as well as revenue mix. In addition, we may experience fluctuations in margins as a result of high cloud infrastructure costs resulting from increased Confluent Cloud sales. Future fluctuations in our revenue and results across periods, including due to further changes in our revenue mix, may make it difficult to assess our future growth and performance.

Downturns or upturns in our sales may not be immediately reflected in our financial position and results of operations.

We recognize a significant portion of our revenue ratably over the term of Confluent Platform subscriptions. As a result, any decreases in new subscriptions or renewals in any one period may not immediately be fully reflected as a decrease in revenue for that period but would negatively affect our revenue in future quarters, even though such a decrease would be reflected in certain of our key metrics as of the end of such period, including RPO. This also makes it difficult for us to rapidly increase our revenue through the sale of additional subscriptions in any period, as revenue is recognized over the term of the subscription. In addition, fluctuations in usage under our usage-based Confluent Cloud offering or monthly subscriptions for our pay-as-you-go offering could affect our revenue on a period-over-period basis. If our quarterly results of operations fall below the expectations of investors and securities analysts who follow our stock, the price of our Class A common stock would decline substantially, and we could face costly lawsuits, including securities class actions.

Seasonality may cause fluctuations in our sales, results of operations, and remaining performance obligations.

Historically, we have experienced seasonality in RPO and new customer bookings, as we typically sell a higher percentage of subscriptions to new customers and renewal subscriptions with existing customers in the fourth quarter of the year. We believe that this results from the procurement, budgeting and deployment cycles of many of our customers, particularly our enterprise customers. We expect that this seasonality will continue to affect our bookings, RPO, and results of operations in the future and might become more pronounced as we continue to target larger enterprise customers.

If we fail to adapt and respond effectively to rapidly changing technology, evolving industry standards, changing regulations, or to changing customer needs, requirements, or preferences, our offering may become less competitive.

Our ability to attract new users and customers and increase revenue from existing customers depends in large part on our ability to enhance, improve, and differentiate our existing offering, increase adoption and usage of our offering, and introduce new offerings and capabilities. The market in which we compete is relatively new and subject to rapid technological change, evolving industry standards, and changing regulations, as well as changing customer needs, requirements, and preferences. The success of our business will depend, in part, on our ability to adapt and respond effectively to these changes on a timely basis. Because the market for our offerings is relatively new, it is difficult to predict customer adoption, increased customer usage and demand for our offering, the size and growth rate of this market, the entry of competitive products, or the success of existing competitive products. If we are unable to enhance our offering and keep pace with rapid technological change, or if new technologies emerge that are able to deliver competitive products at lower prices, more efficiently, more conveniently or more securely than our offering, our business, financial condition, and results of operations could be adversely affected.

To remain competitive, we need to continuously modify and enhance our offering to adapt to changes and innovation in existing and new technologies. We expect that we will need to continue to differentiate our data-in-motion platform capabilities, as well as expand and enhance our platform to support a variety of adjacent use cases. This development effort will require significant engineering, sales, and marketing resources. Any failure to effectively offer solutions for these adjacent use cases could reduce customer demand for our offering. Further, our offering must also integrate with a variety of network, hardware, mobile, cloud, and software platforms and technologies, and we need to continuously modify and enhance our offering to adapt to changes and innovation in these technologies. This development effort may require significant investment in engineering, support, marketing, and sales resources, all of which would affect our business and results of operations. Any failure of our offering to operate effectively with widely adopted, future data infrastructure platforms, applications, and technologies would reduce the demand for our offering. In addition, the landscape of data and infrastructure will be impacted by the adoption of artificial intelligence in ways that are currently unforeseeable and that could have significant risks and opportunities for our business. If we are unable to respond to evolving customer needs, requirements, or preferences in a cost-effective manner, our offering may become less marketable and less competitive or obsolete, and our business, financial condition, and results of operations could be adversely affected.

The market for our offering may develop more slowly or differently than we expect.

It is difficult to predict customer adoption rates and demand for our offering, the entry of competitive products or the future growth rate and size of the data infrastructure market. The expansion of this market depends on a number of factors, including the cost, performance, and perceived value associated with data infrastructure platforms as an alternative or supplement to legacy systems such as traditional databases, as well as the ability of platforms for data in motion to address heightened data privacy and security concerns. If we have a security incident or third-party cloud service providers experience security incidents, loss of customer data, disruptions in delivery or other similar problems, which is an increasing focus of the public and investors in recent years, the market for products as a whole, including our offering, may be negatively affected. In addition, many of our potential customers have made significant investments in alternative data infrastructure platforms and may be unwilling to invest in new products, such as our offering. If data-in-motion technology does not continue to achieve market acceptance, or there is a reduction in demand caused by a lack of customer acceptance, technological challenges, weakening economic conditions, data privacy and security concerns, governmental regulation, competing technologies and products, decreases in information technology spending or otherwise, the market for our offering might not continue to develop or might develop more slowly than we expect, which would adversely affect our business, financial condition, and results of operations.

The competitive position of our offering depends in part on its ability to operate with third-party products and services, including those of our partners, and if we are not successful in maintaining and expanding the compatibility of our offering with such products and services, our business may be harmed.

The competitive position of our offering depends in part on its ability to operate with products and services of third parties, including software companies, software services, and infrastructure, and our offering must be continuously modified and enhanced to adapt to changes in hardware, software, networking, browser, and database technologies. In the future, one or more technology companies, whether our partners or otherwise, may choose not to support the operation of their software, software services, and infrastructure with our offering, or our offering may not support the capabilities needed to operate with such software, software services, and infrastructure. In addition, to the extent that a third party were to develop software or services that compete with ours, that provider may choose not to support our offering. We intend to facilitate the compatibility of our offering with various third-party software, software services, and infrastructure offerings by maintaining and expanding our business and technical relationships. If we are not successful in achieving this goal, our business, financial condition, and results of operations may be harmed.

If we are unable to successfully manage the growth of our professional services business and improve our margins from these services, our business, financial condition, and results of operations will be harmed.

Our professional services business, which engages with customers to help them in their strategy, architecture, and adoption of a platform for data in motion, has grown as we have scaled our business. We believe our investment in professional services facilitates the adoption of our offering, especially with larger customers. As a result, our sales efforts have focused on marketing our offering to larger customers, rather than the profitability of our professional services business. If we are unable to successfully manage the growth of this business and improve our profit margin from these services, our business, financial condition, and results of operations will be harmed.

We face risks associated with the growth of our business with certain heavily regulated industry verticals.

We market and sell our offering to customers in heavily regulated industry verticals, including the banking and financial services industries. As a result, we face additional regulatory scrutiny, risks, and burdens from the governmental entities and agencies which regulate those industries. Selling to and supporting customers in heavily regulated verticals and expanding in those verticals will continue to require significant resources, and there is no guarantee that such efforts will be successful or beneficial to us. If we are unable to successfully maintain or expand our market share in such verticals, or cost-effectively comply with governmental and regulatory requirements applicable to our activities with customers in such verticals, our business, financial condition, and results of operations may be harmed.

Sales to government entities are subject to a number of challenges and risks.

We sell to U.S. Federal, state, and local government customers, as well as foreign and governmental agency customers, generally through resellers. Sales to such entities, whether direct or indirect, are subject to a number of challenges and risks. Selling to such entities can be highly competitive, expensive, and time-consuming, often requiring significant upfront time and expense without any assurance that these efforts will generate a sale. Contracting with certain federal government entities or resellers to such entities requires additional compliance from us and our offering, and if we fail to achieve compliance with these standards and requirements, we may be disqualified from selling our offering to such governmental entities, or be at a competitive disadvantage, which would harm our business, operating results, and financial condition. Government contracting requirements may also change and in doing so restrict our ability to sell into the government sector until we have obtained any required government certifications. Further, achieving and maintaining government certifications, such as U.S. Federal Risk and Authorization Management Program (FedRAMP) authorization for Confluent Cloud, may require significant upfront cost, time, and resources. If we do not obtain U.S. FedRAMP authorization for Confluent Cloud, we will not be able to sell Confluent Cloud, directly or indirectly, to certain Federal government and other public sector customers as well as private sector customers that require such certification for their intended use cases, which could harm our growth, business, and results of operations. This may also harm our competitive position against larger enterprises whose competitive offerings are FedRAMP authorized. Further, there can be no assurance that we will secure commitments or contracts with government entities even following such certifications, which could harm our margins, business, financial condition, and results of operations. Government demand and payment for our offering are affected by public sector budgetary cycles and funding authorizations, with funding reductions or delays adversely affecting public sector demand for our offering.

Further, governmental entities or resellers to such entities may demand contract terms that differ from our standard arrangements and are less favorable than terms agreed with private sector customers. Such entities or resellers may have statutory, contractual or other legal rights to terminate contracts with us or our partners for convenience or for other reasons. Any such termination may adversely affect our ability to contract with other government customers as well as our reputation, business, financial condition, and results of operations. In addition, compliance with requirements applicable to suppliers to the Federal government, including contractual requirements, regulations, and Executive Orders, may require us to change certain of our operations and involve significant effort and expense, which could harm our margins, business, financial condition, and results of operations. Governments and whistleblowers routinely investigate and audit government contractors' administrative processes and compliance with applicable legal requirements. An unfavorable investigation or audit could result in the government refusing to continue buying our subscriptions, a reduction of revenue, suspension or debarment from government contracting, or fines or civil or criminal liability if the audit uncovers improper or illegal activities, including under the False Claims Act, which could adversely affect our results of operations and reputation.

Our customers also include certain non-U.S. governments, to which government procurement law risks similar to those present in U.S. government contracting also apply, particularly in certain emerging markets where our customer base is less established. In addition, compliance with complex regulations and contracting provisions in a variety of jurisdictions can be expensive and consume significant management resources. In certain jurisdictions, our ability to win business may be constrained by political and other factors unrelated to our competitive position in the market. Each of these difficulties could harm our business and results of operations.

Acquisitions, strategic investments, joint ventures, or alliances could be difficult to identify, pose integration challenges, divert the attention of management, disrupt our business and culture, dilute stockholder value, and adversely affect our business, financial condition, and results of operations.

We have in the past and may in the future seek to acquire or invest in businesses, joint ventures, products and platform capabilities, technologies, or technical know-how that we believe could complement or expand our platform capabilities, enhance our technical capabilities, or otherwise offer growth opportunities. Further, the proceeds we received from the IPO and our convertible notes offering increase the likelihood that we will devote resources to exploring larger and more complex acquisitions and investments than we have previously attempted. Any such acquisition or investment may divert the attention of management and cause us to incur various expenses in identifying, investigating, and pursuing suitable opportunities, whether or not the transactions are completed, and may result in unforeseen operating difficulties and expenditures. In particular, we may encounter difficulties assimilating or integrating the businesses, technologies, products and platform capabilities, personnel, or operations of any acquired companies, particularly if the key personnel of an acquired company choose not to work for us, their software is not easily adapted to work with our platform, or we have difficulty retaining the customers of any acquired business due to changes in ownership, management or otherwise. These transactions may also disrupt our business, divert our resources, and require significant management attention that would otherwise be available for development of our existing business. We may also have difficulty establishing our company values with personnel of acquired companies, which may negatively impact our culture and work environment. Any such transactions that we are able to complete may not result in any synergies or other benefits we had expected to achieve, which could result in impairment charges that could be substantial. In addition, we may not be able to find and identify desirable acquisition targets or business opportunities or be successful in entering into an agreement with any particular strategic partner. These transactions could also result in dilutive issuances of equity securities or the incurrence of debt, which could adversely affect our results of operations. In addition, if the resulting business from such a transaction fails to meet our expectations, our business, financial condition, and results of operations may be adversely affected or we may be exposed to unknown risks or liabilities.

We may require additional capital to support the growth of our business, and this capital might not be available on acceptable terms, if at all.

We have funded our operations since inception primarily through equity and debt financings and sales of our offering. While we have taken steps aimed at improving our operating efficiency, including our recent Restructuring Plan, we cannot be certain when or if our operations will generate sufficient cash to fully fund our ongoing operations or the growth of our business. We intend to continue to make investments to support our business, which may require us to engage in equity or debt financings to secure additional funds. Additional financing may not be available on terms favorable to us, if at all, particularly during times of market volatility and general economic instability. If adequate funds are not available on acceptable terms, we may be unable to invest in future growth opportunities, which could harm our business, results of operations, and financial condition. If we incur additional debt, the debt holders, together with holders of our outstanding convertible notes, would have rights senior to holders of common stock to make claims on our assets, and the terms of any future debt could restrict our operations, including our ability to pay dividends on our common stock. Furthermore, if we issue additional equity securities, including through future issuances of equity-linked or derivative securities, our existing stockholders could experience further dilution, and the new equity securities could have rights senior to those of our common stock. Because our decision to issue securities in the future will depend on numerous considerations, including factors beyond our control, we cannot predict or estimate the amount, timing, or nature of any future issuances of debt or equity securities. As a result, our stockholders bear the risk of future issuances of debt or equity securities reducing the value of our Class A common stock and diluting their interests.

Investors' and other stakeholders' expectations of our performance relating to environmental, social and governance factors may impose additional costs and expose us to new risks.

There is an increasing focus from certain investors, customers, employees, and other stakeholders concerning environmental, social and governance matters, or ESG. Some investors may use these non-financial performance factors to guide their investment strategies and, in some cases, may choose not to invest in us if they believe our policies and actions relating to ESG are inadequate. We may face reputational damage in the event that we do not meet the ESG standards set by various constituencies.

As ESG best practices and reporting standards continue to develop, we may incur increasing costs relating to ESG monitoring and reporting and complying with ESG initiatives. For example, the SEC has recently proposed climate change and ESG reporting requirements, which, if approved, would increase our compliance costs. We may also face greater costs to comply with new ESG standards or initiatives in the European Union. In 2022, we published our first ESG Report, which describes the measurement of our greenhouse gas emissions for 2021 and our efforts to achieve carbon neutrality. In addition, our ESG Report provides highlights of how we are supporting our global workforce and our governance practices. Our disclosures on these matters, or a failure to meet evolving stakeholder expectations for ESG practices and reporting, may potentially harm our reputation and customer relationships. Due to new regulatory standards and market standards, certain new or existing customers, particularly those in the European Union, may impose stricter ESG guidelines or mandates for, and may scrutinize relationships more closely with, their counterparties, including us, which may lengthen sales cycles or increase our costs.

Furthermore, if our competitors' ESG performance is perceived to be better than ours, potential or current investors may elect to invest with our competitors instead. In addition, in the event that we communicate certain initiatives or goals regarding ESG matters, we could fail, or be perceived to fail, in our achievement of such initiatives or goals, or we could be criticized for the scope of such initiatives or goals. If we fail to satisfy the expectations of investors, customers, employees and other stakeholders or our initiatives are not executed as planned, our business, financial condition, results of operations, and prospects could be adversely affected.

The COVID-19 pandemic has had, and could in the future have, an adverse impact on our business, operations, and the markets and communities in which we, our partners, and customers operate.

The COVID-19 pandemic has caused disruptions to our business operations, and could have an adverse impact on our business and operations in the future. The extent of the impact of the COVID-19 pandemic on our customers and our customers' evolving response to the COVID-19 pandemic is difficult to assess or predict, and we may be unable to accurately forecast our revenues or financial results. Our results of operations could be below our forecasts, which could adversely affect our results of operations, disappoint analysts and investors, and/or cause our stock price to decline.

Starting in March 2020, we temporarily required employees to work remotely, and we suspended most travel by our employees. We implemented a vaccine mandate for our U.S. employees, where permissible with local, state and federal laws, and most of our employees have the flexibility to work remotely with our "remote first" work policy, which we announced in late 2021 and continue to maintain. For activities that may be conducted remotely, there is no guarantee that we will be as effective while working remotely. Because our team is dispersed, some employees have experienced, and may continue to experience, less capacity to work due to increased personal obligations (such as childcare, eldercare, or caring for family who become sick). Decreased effectiveness and availability of our team could adversely affect our results due to slow-downs in our sales cycles and recruiting and onboarding efforts, delays in our entry into customer contracts, delays in addressing performance issues, delays in product development, delays and inefficiencies among various operational aspects of our business, including our financial organization, or other decreases in productivity that could seriously harm our business. While these actions caused minor disruptions in our business and operations to date, such actions and any future similar actions could impact our competitive positioning, ability to attract and retain customers, and our growth, business, and revenue.

The global impact of the COVID-19 pandemic continues to evolve, and we will continue to monitor the situation closely. The ultimate impact of the COVID-19 pandemic, a similar health epidemic or other global health emergency, is highly uncertain and subject to change. We do not yet know the full extent of potential delays or impacts on our business, operations, ability to access capital, or the global economy as a whole, including due to future waves of outbreak or new variant strains of the virus which may require re-closures or other preventative measures. While the spread of COVID-19 may be contained or mitigated, there is no guarantee that a future outbreak of this or any other widespread epidemics will not occur, or that the global economy will recover, either of which could harm our business.

Risks Related to Cybersecurity

If we, or third parties upon which we rely, experience a security incident comprising the confidentiality, integrity, or availability of our information technology, software, services, communications, or data, we could experience adverse consequences resulting from such compromise, including but not limited to, reputational harm, a reduction in the demand for our offering, regulatory investigations or actions, litigation, fines and penalties, disruptions of our business operations, or other adverse consequences.

In the ordinary course of our business, we and the third parties upon which we rely, may process sensitive data, which may include personal information and our or our customers' or other third parties' sensitive, proprietary, and confidential information. As a result, we and the third parties upon which we rely, face a variety of evolving threats, which could cause security incidents. Security incidents that compromise the confidentiality, integrity, and availability of this information could result from cyber-attacks, computer viruses (such as worms, spyware, or other malware), social engineering (including phishing), ransomware, supply chain attacks, denial of service attacks, credential harvesting or stuffing, efforts by individuals or groups of hackers and sophisticated organizations, including state-sponsored organizations, errors or malfeasance of our personnel, including personnel who have authorized access to our systems and/or information, and security vulnerabilities in the software or systems on which we rely, including third-party systems. In particular, severe ransomware attacks, including those perpetrated by organized criminal threat actors, nation-states, and nation-state-supported actors, are becoming increasingly prevalent and severe and can lead to significant interruptions in our operations, loss of information and income, reputational harm, and diversion of funds. In addition, if our personnel access authorization policies for our systems and/or information are too permissive, we may be subject to heightened risk of security incidents due to errors or malfeasance from our personnel. Extortion payments may alleviate the negative impact of a ransomware attack, but we may be unwilling or unable to make such payments due to, for example, applicable laws or regulations prohibiting such payments.

Some threat actors now engage and are expected to continue to engage in cyber-attacks, including without limitation nation-state actors for geopolitical reasons and in conjunction with military conflicts and defense activities. During times of war and other major conflicts, we and the third parties upon which we rely may be vulnerable to a heightened risk of these attacks, including retaliatory cyber-attacks, that could materially disrupt our systems and operations, supply chain, and ability to produce, sell and distribute our services.

Additionally, certain functional areas of our workforce remain in a remote work environment and outside of our corporate network security protection boundaries, which imposes additional risks to our business, including increased risk of industrial espionage, phishing, and other cybersecurity attacks, including those that are state-sponsored or politically motivated, and unauthorized access to or dissemination of sensitive, proprietary, or confidential information. Future acquisitions could also expose us to additional cybersecurity risks and vulnerabilities from any newly acquired information technology infrastructure.

In addition, our reliance on third-party service providers could introduce new cybersecurity risks and vulnerabilities, including supply-chain attacks, and other threats to our business operations. We rely on third parties to operate our critical business systems and process the sensitive, proprietary, and confidential information that we own, process, or control, including customer information and proprietary data and information, including source code. Our ability to monitor these third parties' information security practices is limited, and these third parties may not have adequate security measures and could experience a security incident that compromises the confidentiality, integrity, or availability of the systems they operate for us or the information they process on our behalf. If our third-party service providers experience a security incident or other interruption, we could experience adverse consequences. While we may be entitled to damages if our third-party service providers fail to satisfy their data privacy or security-related obligations to us, any award may be insufficient to cover our damages, or we may be unable to recover such award. In addition, supply-chain attacks have increased in frequency and severity, and we cannot guarantee that third parties' infrastructure in our supply chain or our third-party partners' supply chains have not been compromised.

Cybercrime and hacking techniques are constantly evolving, and we or third parties who we work with may be unable to anticipate attempted security breaches, react in a timely manner, or implement adequate preventative measures, particularly given increasing use of hacking techniques designed to circumvent controls, avoid detection, and remove or obfuscate forensic artifacts. These risks are likely to increase as we continue to grow and process, control, store, and transmit increasingly large amounts of data.

While we have taken steps designed to protect the confidentiality, integrity, and availability of our systems and the sensitive, proprietary, and confidential information that we own, process, or control, our security measures or those of our third-party vendors may not be able to anticipate or implement effective preventive and remedial measures against all data privacy and security threats. No security solution, strategy, or measures can address all possible security threats or block all methods of penetrating a network or otherwise perpetrating a security incident. For example, we and our third-party providers have been and may in the future be compromised by the aforementioned or similar threats, and result in unauthorized, unlawful, or accidental processing of our information, or vulnerabilities in the products or systems upon which we rely. For example, beginning in January 2021, a malicious third party gained unauthorized access to a third-party vendor, Codecov, that provides a software code testing tool, potentially affecting more than a thousand of Codecov's customers, or Codecov Breach. In April 2021, we were notified that we had been impacted by the Codecov Breach. Through our investigations, we determined that the attackers leveraged a vulnerability in Codecov's software to gain access to credentials in our development environment, and thereby obtained unauthorized read-only access to, and copied to overseas IP addresses, the private Github repositories containing our source code and certain internal-use documents containing references to certain customers and other customer-related attributes. Upon learning of the breach, we took action to revoke Codecov's access and discontinued our use of the Codecov service, rotated all of our credentials identified as exposed by the Codecov Breach to prevent further unauthorized access, enhanced monitoring of our environment, and engaged a third-party forensics firm to assist in our investigation, response, and impact mitigation. We did not find any evidence of access to any customer data sent through or stored in our products, nor did we find any evidence that the attackers modified any of our source code or uploaded any malware or any other malicious code to our system. However, the full extent of the impact of this incident on our operations, products, or services may not be known for some time, and we cannot assure you that there will be no further impact in the future. This incident or any future incidents relating to the Codecov Breach could result in the use of exfiltrated source code to attempt to identify vulnerabilities in our offering, future ransomware or social engineering attacks, reduced market acceptance of our offering, injury to our reputation and brand, legal claims against us, and the diversion of our resources.

In addition, we do not control the content that our customers transmit, process, and maintain using our offering. If our customers use our offering for the transmission or storage of personal information and our security measures are, or are believed to have been, breached, our business may suffer, and we could incur significant liability.

If we, or a third party upon whom we rely, experience a security incident that results in the compromise of the confidentiality, integrity, or availability of our systems or the sensitive, proprietary, or confidential information that we own, process, or control, or the perception that one has occurred, this could result in a loss of customer confidence in the security of our platform and damage to our brand, reduce the demand for our offering, disrupt business operations, result in the exfiltration of proprietary data and information, including source code, require us to spend material resources to investigate or correct the incident and to prevent future security incidents, expose us to legal liabilities, including litigation, regulatory enforcement (including investigations, fines, penalties, audits, and inspections), additional oversight, restrictions or bans on processing personal information, indemnity obligations, claims by our customers or other relevant parties that we have failed to comply with contractual obligations to implement specified security measures, and adversely affect our business, financial condition, and results of operations.

We cannot assure you that the limitations of liability in our contracts would be enforceable or adequate or would otherwise protect us from such liabilities or damages. Applicable data privacy and security obligations may also require us to notify relevant stakeholders of security incidents. Such notifications are costly, and the notifications or the failure to comply with such requirements could lead to material adverse impacts such as negative publicity, loss of customer confidence in our services or security measures, investigations, and private or government claims.

In addition to experiencing a security incident, third parties may gather, collect, or infer sensitive information about us from public sources, data brokers, or other means that reveals competitively sensitive details about our organization and could be used to undermine our competitive advantage or market position. Additionally, sensitive information of the Company or our customers could be leaked, disclosed, or revealed as a result of or in connection with our employees', personnel's, or vendors' use of generative AI technologies.

Additionally, we cannot be certain that our insurance coverage will be adequate or otherwise protect us with respect to claims, expenses, fines, penalties, business loss, data loss, litigation, regulatory actions, or other impacts arising out of security incidents, particularly if we experience an event that impacts multiple customers, that such coverage will continue to be available on acceptable terms or at all, or that such coverage will pay future claims. Any of these results could adversely affect our business, financial condition, and results of operations.

Real or perceived errors, failures, bugs, or defects in our offering could adversely affect our reputation and harm our business.

Our offering and platform for data in motion are complex and, like all software, may contain undetected defects or errors. We are continuing to evolve the features and functionality of our data-in-motion platform through updates and enhancements, and as we do so, we may introduce additional defects or errors that may not be detected until after deployment by our customers. In addition, if our platform is not implemented or used correctly or as intended, inadequate performance and disruptions in service may result. Moreover, if we acquire companies or integrate into our platform technologies developed by third parties, we may encounter difficulty in incorporating the newly-obtained technologies into our platform and maintaining the quality standards that are consistent with our reputation. Since our customers use our platform for data in motion for important aspects of their business, any actual or perceived errors, defects, bugs, or other performance problems could damage our customers' businesses. Any defects or errors in our data-in-motion platform, or the perception of such defects or errors, could result in a loss of, or delay in, market acceptance of our offering, loss of existing or potential customers, and delayed or lost revenue and could damage our reputation and our ability to convince enterprise users of the benefits of our offering.

In addition, errors in our data-in-motion platform could cause system failures, loss of data or other adverse effects for our customers that may assert warranty and other claims for substantial damages against us. Although our agreements with our customers typically contain provisions that seek to limit our exposure to such claims, it is possible that these provisions may not be effective or enforceable under the laws of some jurisdictions. While we seek to insure against these types of claims, our insurance policies may not adequately limit our exposure to such claims. These claims, even if unsuccessful, could be costly and time consuming to defend and could harm our business, financial condition, results of operations, and cash flows.

Interruptions or performance problems associated with our offering may adversely affect our business, financial condition, and results of operations.

Our continued growth depends in part on our ability to provide a consistently reliable platform for data in motion. If we are unable to do so due to vulnerabilities in programming, coding errors, outages caused by our platform's complexity or scale or due to disruptions in cloud services, or because the systems complexity and scale result in extended outages, we may experience a loss of customers, lost or delayed market acceptance of our offering, delays in payment to us by customers, injury to our reputation and brand, legal claims against us, and the diversion of our resources.

It may become increasingly difficult to maintain and improve the performance of Confluent Cloud as our customer base grows and Confluent Cloud becomes more complex. We may experience disruptions, outages, and other performance problems in Confluent Cloud due to a variety of factors, including infrastructure changes, introductions of new functionality, human or software errors, denial of service attacks, issues with third-party cloud hosting providers, or other security-related incidents. In addition, to the extent that we do not effectively address capacity constraints, upgrade our systems as needed, and continually develop our technology and network architecture to accommodate actual and anticipated changes in technology, our business, financial condition, and results of operations may be adversely affected.

We are subject to increasingly stringent and evolving U.S. and foreign laws, regulations, rules, contractual obligations, policies, and other requirements related to data privacy and security. Our actual or perceived failure to comply with such obligations could lead to regulatory investigations or actions, litigation, fines and penalties, disruptions of our business operations, reputational harm, or otherwise harm our business.

In the ordinary course of our business, we collect, receive, store, generate, use, transfer, disclose, make accessible, protect, secure, dispose of, transmit, share, and process sensitive, proprietary, confidential, and regulated information, including personal information, trade secrets, intellectual property, and other business information, that belongs to us or that we may handle on behalf of others such as our customers. As such, we, our customers, and third parties upon which we rely, are subject to numerous evolving and increasingly stringent foreign and domestic laws and requirements relating to data privacy and security that are increasing the cost and complexity of operating our business. These requirements may also include regulations, guidance, industry standards, policies, contractual obligations, external and internal policies and procedures, and other obligations related to data privacy and security.

In the United States, federal, state, and local governments have enacted numerous data privacy and security laws, including data breach notification laws, personal information privacy laws, health information privacy laws, consumer protection laws (e.g., Section 5 of the Federal Trade Commission Act), other similar laws (e.g., wiretapping laws). For example, the California Consumer Privacy Act, or CCPA, imposes several obligations on covered businesses, including requiring specific disclosures in privacy notices related to a business's collection, use, and sharing of personal information, implementing new operational practices, and honoring requests from California residents to exercise certain privacy rights related to their personal information. The CCPA contains civil potential penalties for noncompliance of up to \$7,500 per violation and allows private litigants affected by certain data breaches to recover significant statutory damages. In addition, the California Privacy Rights Act of 2020, or CPRA, which became effective January 1, 2023, expands the CCPA's requirements including by applying to personal information of business representatives and employees and establishing a new California Privacy Protection Agency to implement and enforce the law. Other states, such as Virginia and Colorado, have also passed comprehensive data privacy and security laws, and similar laws are being considered in several other states, as well as at the federal and local levels. These developments may further complicate compliance efforts and may increase legal risk and compliance costs for us and the third parties upon whom we rely. Additionally, pursuant to various data privacy and security laws and other obligations, we may be required to obtain certain consents to process personal information. Our inability or failure to do so could result in adverse consequences.

Foreign laws relating to data privacy and security are also undergoing a period of rapid change and have become more stringent in recent years. For example, the General Data Protection Regulation, or EU GDPR, applies in the European Union, or EU, and by virtue of section 3 of the European Union (Withdrawal) Act 2018, the United Kingdom GDPR, or UK GDPR, applies in the UK. Under the EU GDPR, noncompliant companies face fines of up to the greater of 20 million Euros or 4% of their global annual revenues for major violations and up to the greater of £17.5m or up to 4% of annual global revenues in respect of the UK GDPR. In addition to the foregoing, a breach of the EU GDPR or UK GDPR could result in regulatory investigations, reputational damage, potential bans on processing of personal information, private litigation, and/or other corrective action, such as class actions brought by classes of data subjects or by consumer protection organizations authorized at law to represent their interests. Laws in EU member states and the UK also impose restrictions on direct marketing communications and the use of cookies and similar technologies online, and a new regulation proposed in the EU called the e-Privacy Regulation may make such restrictions more stringent.

Furthermore, European data privacy and security laws, including the EU GDPR and UK GDPR, generally restrict the transfer of personal information from the European Economic Area, or EEA, and the UK to countries that are not generally considered by some data protection authorities as providing an adequate level of data protection. Swiss laws contain similar data transfer restrictions. The European Commission recently released updated Standard Contractual Clauses and the EU-U.S. Data Privacy Framework, mechanisms to transfer personal information outside of the EEA, which impose additional obligations for cross-border data transfers. Although there are currently various mechanisms available to transfer data from Europe, such as the Standard Contractual Clauses, the EU-U.S. Data Privacy Framework, and the UK's International Data Transfer Agreement/Addendum, the mechanisms are subject to legal challenges and there is no assurance that we can satisfy or rely on these mechanisms to lawfully transfer personal information to the United States. Countries outside of Europe have enacted or are considering similar cross-border data transfer restrictions and laws requiring local data residency and restricting cross-border data transfer, which could increase the cost and complexity of doing business. If we cannot implement a valid mechanism for cross-border personal information transfers, we may face increased risk of regulatory actions, penalties, and data processing restrictions or bans. For example, in May 2023, the Irish Data Protection Commission determined that a major social media company's use of the Standard Contractual Clauses was insufficient and levied a 1.2 billion Euro fine against the company and prohibited the company from transferring personal information to the United States. Evolving cross-border data transfer requirements may also result in reduced demand for our services and require us to increase our data processing capabilities and other operations in Europe at significant expense.

Data privacy and security laws are also becoming more stringent beyond Europe. For example, in Canada, the Personal Information Protection and Electronic Documents Act, and various related provincial laws, as well as Canada's Anti-Spam Legislation, may apply to our operations. We also target customers in Asia and have operations in China, Japan, and Singapore and may be subject to new and emerging data privacy and security regimes in Asia, including China's Personal Information Protection Law, Japan's Act on the Protection of Personal Information, and Singapore's Personal Data Protection Act.

We may also be bound by contractual obligations related to data privacy and security, and our efforts to comply with such obligations may not be successful. For example, data privacy laws including the GDPR and CCPA increasingly require companies to impose specific contractual restrictions on their service providers or processors. In addition, customers that may use certain of our offerings to process protected health information may require us to sign business associate agreements that subject us to the data privacy and security requirements under the U.S. Health Insurance Portability and Accountability Act of 1996 and the U.S. Health Information Technology for Economic and Clinical Health Act, or HIPAA, as well as state laws that govern the data privacy and security of health information. Our customers' increasing data privacy and security requirements also increase the cost and complexity of ensuring that the third parties we rely on to operate our business and deliver our services can meet these standards. If we or our vendors are unable to meet our customers' demands or comply with the increasingly stringent legal or contractual requirements they impose on us relating to data privacy and security, including requirements based on updated Standard Contractual Clauses, we may face increased legal liability, customer contract terminations and reduced demand for our services.

Our employees and personnel may use generative artificial intelligence, or AI, technologies to perform their work, and the disclosure and use of personal information in such technologies is subject to various data privacy and security laws and obligations. Governments have passed and are likely to pass additional laws regulating generative AI. Our use of this technology could result in additional compliance costs and regulatory investigations and actions. If we are unable to use generative AI, it could make our business less efficient and result in competitive disadvantages.

Finally, we may publish privacy policies, marketing material, and other documentation or statements regarding our collection, use, disclosure, and other processing of personal information. Although we endeavor to adhere to these policies, statements, and documentation, we, and the third parties on which we rely, may at times fail to do so or may be perceived to have failed to do so. Such failures could subject us to regulatory enforcement action as well as costly legal claims by affected individuals or our customers.

The number and scope of obligations related to data privacy and security are quickly changing. Preparing for and attempting to comply with these obligations requires significant resources and, potentially, changes to our technologies, systems, and practices and those of any third parties that process personal data on our behalf. We strive to comply with applicable data privacy and security laws and requirements, but we cannot fully determine the impact that current or future such laws and requirements may have on our business or operations. Such laws or requirements may be inconsistent from one jurisdiction to another, subject to differing interpretations, and courts or regulators may deem our efforts to comply as insufficient. If we, or the third parties we rely on to operate our business and deliver our services, fail to comply, or are perceived as failing to comply, with our legal or contractual obligations relating to data privacy and security, or our policies and documentation relating to personal information, we could face governmental enforcement action; litigation with our customers, individuals or others; fines and civil or criminal penalties for us or company officials; obligations to cease offering our services or to substantially modify them in ways that make them less effective in certain jurisdictions; negative publicity and harm to our brand and reputation; and reduced overall demand for our services. Such developments could adversely affect our business, financial condition, and results of operations.

Risks Related to Our Sales and Marketing Efforts and Brand

Failure to effectively develop and expand our sales and marketing capabilities or improve the productivity of our sales and marketing organization could harm our ability to expand our potential customer and sales pipeline, increase our customer base, and achieve broader market acceptance of our offering.

Our ability to increase our customer base, achieve broader market adoption and acceptance of our offering, and expand our potential customer and sales pipeline and brand awareness will depend to a significant extent on our ability to expand and improve the productivity and effectiveness of our sales and marketing organization. We plan to continue expanding our direct sales force, both domestically and internationally. We also plan to dedicate significant resources to sales and marketing programs, including to decrease the time required for our sales personnel to achieve desired productivity levels. Historically, newly hired sales personnel have needed several quarters to achieve desired productivity levels. While our recent Restructuring Plan is expected to streamline sales and marketing spend, we expect to continue investing significant financial and other resources in our sales and marketing efforts, which will result in increased costs and impact our margins and results of operations. Our revenue growth rate, business, and results of operations have from time to time been harmed and may in the future be harmed if our sales and marketing efforts fail to successfully expand our potential customer and sales pipeline and existing customer engagement with our offering, including through increasing brand awareness, new customer acquisition, and market adoption of our offering, particularly for Confluent Cloud. In addition, we may not achieve anticipated revenue growth from investing in our sales force if we are unable to hire, develop, integrate, and retain talented and effective sales personnel, if our new and existing sales personnel, on the whole, are unable to achieve desired productivity levels in a reasonable period of time or at all, or if our sales and marketing programs are not effective.

If we fail to maintain and enhance our brand, including among developers, our ability to expand our customer base will be impaired and our business, financial condition, and results of operations may suffer.

We believe that maintaining and enhancing the Confluent brand, including among developers, is important to support the marketing and sale of our existing and future offerings to new customers and expansion of sales to existing customers. We believe that the importance of brand recognition will increase as competition in our market increases. In particular, we believe that enhancing the Confluent brand will be critical to the growth and market adoption and acceptance of Confluent Cloud due to the presence of open source alternatives, competing large public cloud providers with widespread name recognition, such as AWS, Azure, and GCP, and other data infrastructure platforms. Software developers, including those within our customers' IT departments, are often familiar with our underlying technology and value proposition. We rely on their continued adoption of our offering to evangelize on our behalf within their organizations and increase reach and mindshare within the developer community. Actions that we have taken in the past or may take in the future with respect to Apache Kafka or our community license, including the development and growth of our proprietary offering, may be perceived negatively by the developer community and harm our reputation. Successfully maintaining and enhancing our brand will depend largely on the effectiveness of our marketing efforts, our ability to provide reliable products that continue to meet the needs of our customers at competitive prices, our ability to maintain our customers' trust, our ability to continue to develop new functionality and use cases, our ability to successfully differentiate our offering and its capabilities from competitive products, including open source alternatives, and our ability to increase our reach and mindshare in the developer community. Our brand promotion activities may not generate customer awareness or yield increased revenue, and even if they do, any increased revenue may not offset the expenses we incur in building our brand. If we fail to successfully promote and maintain our brand, our business, financial condition, and results of operations may suffer.

We have a limited history with pricing models for our offering, and we may need to adjust the pricing terms of our offering, which could have an adverse effect on our revenue and results of operations.

We have limited experience with respect to determining the optimal prices for our offering, and, in particular, we have limited experience pricing our offering under economic conditions characterized by high inflation or in recessionary or uncertain economic environments. We have changed our pricing model from time to time and expect to continue to do so in the future. For example, in late 2019, we transitioned the primary purchase model for Confluent Cloud from a defined configuration paid annually in advance to a model based on actual monthly usage and committed annual spend. We also expect to continue providing additional features and functionality for our offering as we work toward expanding applications and use cases for our offering, which will require us to continuously evaluate optimal pricing for our offering. If we do not optimally adjust pricing for our offering, our revenue and margins as well as future customer acquisitions may be negatively impacted. As the markets for our offering mature, as macroeconomic conditions evolve, or as new competitors introduce new products or services that compete with ours, we may be unable to attract new customers at the same price or on the same terms. Moreover, enterprise customers may demand greater price concessions, or we may be unable to increase prices to offset increases in costs, including hosting costs associated with Confluent Cloud and increases related to inflationary pressures. However, our historical data and operating experience may be insufficient to adequately inform our future pricing strategies for changing market environments. As a result, in the future we may be required to reduce our prices or increase our discounting, which could adversely affect our revenue, gross margin, profitability, financial position, and cash flow.

Sales to enterprise customers involve risks that may not be present or that are present to a lesser extent with respect to sales to smaller organizations.

As of June 30, 2023 and December 31, 2022, we had 1,144 customers and 1,015 customers with \$100,000 or greater in ARR, respectively. See the section titled “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Key Business Metrics” for a description of ARR. Sales to enterprise customers and large organizations involve risks that may not be present or that are present to a lesser extent with sales to smaller customers, including the commercial customer segment. These risks include longer sales cycles, more complex customer requirements, substantial upfront sales costs and less predictability in completing some of our sales. For example, enterprise customers may require considerable time to evaluate and test our offering and those of our competitors prior to making a purchase decision and placing an order. A number of factors influence the length and variability of our sales cycle, including the need to educate potential customers about the uses and benefits of our offering, the discretionary nature of purchasing and budget cycles, macroeconomic uncertainty and challenges and resulting increased IT spending scrutiny, heightened security and data privacy requirements, and the competitive nature of evaluation and purchasing approval processes. Since the process for deployment, configuration and management of our offering is complex, we are also often required to invest significant time and other resources to train and familiarize potential customers with our offering. Customers may engage in extensive evaluation, testing, and quality assurance work before making a purchase commitment, which increases our upfront investment in sales, marketing, and deployment efforts, with no guarantee that these customers will make a purchase or increase the scope of their subscriptions. In certain circumstances, an enterprise customer’s decision to use our offering may be an organization-wide decision, and therefore, these types of sales require us to provide greater levels of education regarding the use and benefits of our offering. As a result, the length of our sales cycle, from identification of the opportunity to deal closure, has varied, and may continue to vary, significantly from customer to customer, with sales to large enterprises and organizations typically taking longer to complete. Moreover, large enterprise customers often begin to deploy our offering on a limited basis but nevertheless demand configuration, integration services, and pricing negotiations, which increase our upfront investment in the sales effort with no guarantee that these customers will deploy our offering widely enough across their organization to justify our substantial upfront investment.

Given these factors, it is difficult to predict whether and when a sale will be completed and when revenue from a sale will be recognized due to the variety of ways in which customers may purchase our offering. This may result in lower than expected revenue in any given period, which would have an adverse effect on our business, results of operations, and financial condition.

Our estimates of market opportunity and forecasts of market growth may prove to be inaccurate, and even if the market in which we compete achieves the forecasted growth, our business could fail to grow at similar rates, if at all.

Our estimates of market opportunity and forecasts of market growth may prove to be inaccurate. Market opportunity estimates and growth forecasts are subject to significant uncertainty and are based on assumptions and estimates that may not prove to be accurate, including due to the risks described in this Quarterly Report. Even if the market in which we compete achieves the forecasted growth, our business could fail to grow at similar rates, if at all.

The variables that go into the calculation of our market opportunity are subject to change over time, and there is no guarantee that any particular number or percentage of addressable users or companies covered by our market opportunity estimates will purchase our offering at all or generate any particular level of revenue for us.

Any expansion in our market depends on a number of factors, including the cost, performance, and perceived value associated with our platform for data in motion and those of our competitors. Even if the market in which we compete meets our size estimates and growth forecasts, our business could fail to grow at similar rates, if at all. Our growth is subject to many factors, including our success in implementing our business strategy, which is subject to many risks and uncertainties.

Risks Related to Our Customers

If we are unable to attract new customers or expand our potential customer and sales pipeline, our business, financial condition, and results of operations will be adversely affected.

To increase our revenue, we must continue to generate market acceptance of our brand and attract new customers and expand our potential customer and sales pipeline. Our success will depend to a substantial extent on the widespread adoption of our offering as an alternative to competing solutions, including open source alternatives. In addition, as our market matures, our offering evolves, and competitors introduce lower cost or differentiated products that compete with our offering, our ability to sell our offering could be impaired. Similarly, our sales efforts could be adversely impacted if customers or users within these organizations perceive that features incorporated into competitive products reduce the need for our offering or if they prefer to purchase competing products that are bundled together with other types of products, such as data infrastructure platforms offered by public cloud providers. Our existing sales and marketing strategies for new customer acquisition may also be unsuccessful. For example, we offer free, limited evaluation and developer usage of Confluent Platform and free introductory usage of Confluent Cloud to encourage awareness, usage, familiarity, and adoption, and a pay-as-you-go arrangement for Confluent Cloud without minimum usage commitments. If we are unable to successfully convert these free users into paying customers, or convert pay-as-you-go customers into customers with usage-based minimum commitments, we will not realize the intended benefits of this marketing and adoption strategy. As a result of these and other factors, we may be unable to attract new customers or expand our potential customer and sales pipeline, which may have an adverse effect on our business, financial condition, and results of operations.

Our business depends on our existing customers renewing their subscriptions and usage-based minimum commitments, purchasing additional subscriptions and usage-based minimum commitments, and expanding their use of our offering.

Our future success depends in part on our ability to expand our customers' use of our offering into additional use cases, our customers renewing their subscriptions and usage-based minimum commitments, and our ability to develop our offering for additional use cases and applications. The terms of our subscriptions and usage-based minimum commitments are primarily one year in duration. Our customers have no obligation to renew after the expiration of the applicable term. In order for us to maintain or improve our results of operations, it is important that our customers enter into relationships with us that increase in value over time, and renew and expand their subscriptions with us, including through the use of our offering for additional use cases and applications. Although we seek to increase our revenue through expanded use of our offering by customers in additional use cases, we may not be successful in such efforts. Our dollar-based net retention rate has historically declined or fluctuated, and may further decline or fluctuate, as a result of a number of factors, including loss of one or more customers, the timing and size of any such losses, business strength or weakness of our customers, customer usage of our offering, customer satisfaction with the capabilities of our offering and our level of customer support, our prices, the capabilities and prices of competing products, decisions by customers to use open source alternatives, mergers and acquisitions affecting our customer base, the effects of global economic conditions, including increased interest rates and inflation, currency exchange rate fluctuations, or reductions in our customers' spending on IT solutions or their spending levels generally. In addition, as some customers transition from Confluent Platform to Confluent Cloud, our dollar-based net retention rate may decline or fluctuate, at least in the short term, as those customers replace subscriptions to Confluent Platform with usage-based minimum commitments. Historically, some of our customers have elected not to renew their subscriptions with us for a variety of reasons, including as a result of competing products, internally developed or managed solutions, including those based on Apache Kafka or other open source alternatives, mergers and acquisitions of our customers, and global economic conditions. These factors may also be exacerbated if our customer base of larger enterprises continues to grow, which may require increasingly sophisticated and costly sales efforts, if large enterprises further develop internal capabilities, and if a recessionary or uncertain economic environment negatively impacts our customer base's information technology budgets. In addition, a strengthening of the U.S. dollar could increase the real cost of our offering to our customers outside of the United States, which could result in loss of customers or reduced usage of our offering. If our customers do not renew their subscriptions and/or usage-based minimum commitments, expand their use of our offering, and purchase additional products from us, our revenue may decline and our business, financial condition, and results of operations may be harmed.

If we or any of our partners fail to offer high-quality support, our reputation could suffer.

Our customers rely on our or our channel partners' support personnel to resolve issues and realize the full benefits that our offering provides. High-quality support is also important for the continuation and expansion of our relationships with existing customers. The importance of these support functions will increase as we expand our business and pursue new customers. In certain cases when we provide our offering for sale by channel partners as part of their value-added offerings, our partners may be responsible for providing support and support personnel for our customers. We often have limited to no control or visibility in such cases. If we or such partners do not help our customers quickly resolve issues and provide effective ongoing support, our ability to maintain and expand our sales to existing and new customers could suffer, and our reputation with existing or potential customers could suffer.

Incorrect implementation or use of our offering, or our customers' failure to update Confluent Platform, could result in customer dissatisfaction and negatively affect our reputation, business, operations, financial results, and growth prospects.

Our offering is often used for and within large scale, complex IT environments. Our customers and some partners require education and experience in the proper use of and the benefits that can be derived from our offering to maximize their potential. If users of our offering do not implement, use, or update our offering correctly or as intended, then inadequate performance and/or security vulnerabilities may result. Because our customers rely on our offering to manage a wide range of operations, the incorrect implementation or use of our offering, or our self-managed customers' failure to update Confluent Platform, or our failure to train customers on how to use our offering productively may result in customer dissatisfaction, and negative publicity, and may adversely affect our reputation and brand. Our failure to effectively provide education and implementation services to our customers could result in lost opportunities for follow-on sales to these customers and decrease subscriptions by new customers, which would adversely affect our business and growth prospects.

Indemnity provisions in various agreements to which we are party potentially expose us to substantial liability for infringement, misappropriation, or other violation of intellectual property rights, data protection, and other losses.

Certain of our agreements with our customers and other third parties include indemnification provisions under which we agree to indemnify or otherwise be liable to them for losses suffered or incurred as a result of claims of infringement, misappropriation or other violation of intellectual property rights, data protection, compliance with laws, damages caused by us to property or persons, or other liabilities relating to or arising from our software, services, platform, our acts or omissions under such agreements, or other contractual obligations. From time to time, our customers and other third parties have requested, and may in the future request, us to indemnify them for such claims or liabilities. In certain circumstances, our agreements provide for uncapped indemnity liability for certain intellectual property infringement claims. Large indemnity payments could harm our business, financial condition, and results of operations. Although we attempt to contractually limit our liability with respect to such indemnity obligations, we are not always successful and may still incur substantial liability related to them, and we may be required to cease use of or modify certain functions of our offering as a result of any such claims. Any dispute with a customer or other third party with respect to such obligations could have adverse effects on our relationship with such customer or other third party and other existing or prospective customers, reduce demand for our subscriptions and services and adversely affect our business, financial condition, and results of operations. In addition, although we carry general liability insurance, our insurance may not be adequate to indemnify us for all liability that may be imposed or otherwise protect us from liabilities or damages with respect to claims alleging unauthorized access to or disclosure of customer data, and any such coverage may not continue to be available to us on acceptable terms or at all.

We typically provide service-level commitments under our customer agreements. If we fail to meet these commitments, we could face customer terminations, a reduction in renewals, and damage to our reputation, which would lower our revenue and harm our business, financial condition, and results of operations.

Our agreements with our customers contain uptime and response service-level commitments. If we fail to meet these commitments, we could face customer terminations or a reduction in renewals, which could significantly affect both our current and future revenue. Any service-level commitment failures could also damage our reputation. In addition, if we are unable to meet the stated uptime requirements described in our Confluent Cloud agreements, we may be contractually obligated to provide these customers with service credits, which could significantly affect our revenue in the periods in which the failure occurs and the credits are applied. Any of these outcomes or failures could also adversely affect our business, financial condition, and results of operations.

Risks Related to Our Intellectual Property

We use third-party open source software in our offering, which could negatively affect our ability to sell our offering or subject us to litigation or other actions.

We use third-party open source software in our offering, most significantly Apache Kafka and including Apache Flink, and we expect to continue to incorporate such open source software in our offering in the future. Many open source software licenses, including the Apache License, Version 2.0, state that any work of authorship licensed under it may be reproduced and distributed provided that certain conditions are met. However, we may be subject to suits by parties claiming ownership rights in what we believe to be permissively licensed open source software or claiming non-compliance with the applicable open source licensing terms. It is possible that a court would hold the Apache License, Version 2.0 to be unenforceable or that someone could assert a claim for proprietary rights in a program developed and distributed under it. Any ruling by a court that this license is not enforceable, or that open source components of our offering may not be reproduced or distributed, may negatively impact our distribution or development of all or a portion of our offering.

In addition, some open source licenses require end-users who distribute or make available across a network software and services that include open source software to make available all or part of such software, which in some circumstances could include valuable proprietary code. While we employ practices designed to monitor our compliance with the licenses of third-party open source software and protect our valuable proprietary source code, we may inadvertently use third-party open source software in a manner that is inconsistent with our applicable policies, or that exposes us to claims of non-compliance with the terms of their licenses, including claims of intellectual property rights infringement or breach of contract. Furthermore, there exists today an increasing number of types of open source software licenses, almost none of which have been tested in courts of law to provide guidance of their proper legal interpretations. From time to time, there have been claims challenging the ownership rights in open source software against companies that incorporate it into their offerings, and the licensors of such open source software provide no warranties or indemnities with respect to such claims. As a result, we and our customers could be subject to lawsuits or threats of lawsuits by parties claiming ownership rights in what we believe to be permissively licensed open source software. Resulting litigation could be costly for us to defend and harm our reputation, business, financial condition, and results of operations. If our activities were determined to be out of compliance with the terms of any applicable “copyleft” open source licenses, we may be required to publicly release certain portions of our proprietary source code for no cost, we could face an injunction for our offering, and we could also be required to expend substantial time and resources to re-engineer some or all of our software.

We also regularly contribute source code under open source licenses and have made some of our own software available under open source or source-available licenses, and we include third-party open source software in our offering. Because the source code for any software we contribute to open source projects, including Apache Kafka and Apache Flink, or distribute under open source or source-available licenses is publicly available, our ability to protect our intellectual property rights with respect to such source code may be limited or lost entirely, and we may be limited in our ability to prevent our competitors or others from using such contributed source code. While we have policies in place that govern such submissions, there is a risk that employees may submit proprietary source code or source code embodying our intellectual property, in either case, not intended to be distributed in such a manner, to such open source projects. In addition, the use of third-party open source software may expose us to greater risks than the use of third-party commercial software because open source licensors generally do not provide warranties or controls on the functionality or origin of the software. Use of open source software may also present additional security risks because the public availability of such software may publicize vulnerabilities or otherwise make it easier for hackers and other third parties to determine how to compromise our platform or the systems of our customers who are running our offering. Any of the foregoing could be harmful to our business, results of operations or financial condition, and could help our competitors develop products and services that are similar to or better than ours.

Our offering has evolved from Apache Kafka, Apache Flink and other open source software, which are widely available, and therefore, we do not own the exclusive rights to the use of Apache Kafka, Apache Flink and other open source software, nor are we able to control the evolution, enhancement, and maintenance of Apache Kafka, Apache Flink and other open source software.

The technology underlying our offering has evolved from certain open source software, such as Apache Kafka and Apache Flink, and as a result we cannot exclude other companies from adopting and modifying certain common elements of our software and that of such open source software. With open source software, competitors can also develop competing products without the amount of overhead and lead time required for traditional proprietary software development. In addition, if competing products are also based on or compatible with Apache Kafka or Apache Flink, existing customers may also be able to easily transfer their applications to competing products. Competitors with greater resources than ours or members of the Apache Kafka or Apache Flink communities may create similar or superior offerings, or modify Apache Kafka or Apache Flink with different, superior features, and could make such products available to the public free of charge. Our competitors or members of the open source community may also develop a new open source project or a closed-source proprietary product that is similar to or superior to Apache Kafka or Apache Flink in terms of features or performance, in turn gaining popularity or replacing Apache Kafka as the new standard for data-in-motion technology among developers and other users. As a result, the future of Apache Kafka, Apache Flink and other open source software could change dramatically and such change in trajectory, use and acceptance in the marketplace and resulting competitive pressure could result in reductions in the prices we charge for our offering, loss of market share, and adversely affect our business operations and financial outlook. Additionally, the development and growth of our proprietary offering may result in the perception within the open source community of a diminution of our commitment to Apache Kafka, Apache Flink and other open source platforms. Such perceptions may negatively affect our reputation within the developer community, which may adversely affect market acceptance and future sales of our offering.

Any failure to obtain, maintain, protect, or enforce our intellectual property and proprietary rights could impair our ability to protect our proprietary technology and our brand.

Our success depends to a significant degree on our ability to obtain, maintain, protect and enforce our intellectual property rights, including our proprietary technology, know-how, and our brand. We rely on a combination of trademarks, trade secrets, patents, copyrights, service marks, contractual restrictions, and other intellectual property laws and confidentiality procedures to establish and protect our proprietary rights. However, the steps we take to obtain, maintain, protect, and enforce our intellectual property rights may be inadequate. We will not be able to protect our intellectual property rights if we are unable to enforce our rights or if we do not detect unauthorized use of our intellectual property rights. If we fail to protect our intellectual property rights adequately, our competitors may gain access to our proprietary technology and develop and commercialize substantially identical products, services, or technologies. In addition, defending our intellectual property rights might entail significant expense. Any patents, trademarks or other intellectual property rights that we have or may obtain may be challenged or circumvented by others or invalidated or held unenforceable through administrative process, including re-examination, *inter partes* review, interference and derivation proceedings, and equivalent proceedings in foreign jurisdictions (e.g., opposition proceedings), or litigation.

We have a limited patent portfolio. Even if we continue to seek patent protection in the future, we may be unable to obtain or maintain patent protection for our technology. In addition, our issued patents or any patents issued from future patent applications or licensed to us in the future may not provide us with competitive advantages or may be successfully challenged by third parties. There may be issued patents of which we are not aware, held by third parties that, if found to be valid and enforceable, could be alleged to be infringed by our current or future technologies or offerings. There also may be pending patent applications of which we are not aware that may result in issued patents, which could be alleged to be infringed by our current or future technologies or offerings. Furthermore, legal standards relating to the validity, enforceability, and scope of protection of intellectual property rights are uncertain. Despite our precautions, it may be possible for unauthorized third parties to copy our offering and use information that we regard as proprietary to create products that compete with ours. Patent, trademark, copyright, and trade secret protection may not be available to us in every country in which our offering is available.

The value of our intellectual property could diminish if others assert rights in or ownership of our trademarks and other intellectual property rights, or trademarks that are similar to our trademarks. We may be unable to successfully resolve these types of conflicts to our satisfaction. In some cases, litigation or other actions may be necessary to protect or enforce our trademarks and other intellectual property rights. Furthermore, third parties may assert intellectual property claims against us, and we may be subject to liability, required to enter into costly license agreements, or required to rebrand our offering or prevented from selling our offering if third parties successfully oppose or challenge our trademarks or successfully claim that we infringe, misappropriate or otherwise violate their trademarks or other intellectual property rights. In addition, the laws of some foreign countries may not be as protective of intellectual property rights as those in the United States, and mechanisms for enforcement of intellectual property rights may be inadequate. As we expand our international activities, our exposure to unauthorized copying and use of our offering and proprietary information will likely increase. Moreover, policing unauthorized use of our technologies, trade secrets, and intellectual property may be difficult, expensive, and time-consuming, particularly in foreign countries where the laws may not be as protective of intellectual property rights as those in the United States and where mechanisms for enforcement of intellectual property rights may be weak. Accordingly, despite our efforts, we may be unable to prevent third parties from infringing upon, misappropriating or otherwise violating our intellectual property rights.

We enter into confidentiality and invention assignment agreements with our employees and consultants and enter into confidentiality agreements with other third parties, including suppliers and other partners. However, we cannot guarantee that we have entered into such agreements with each party that has or may have had access to our proprietary information, know-how, and trade secrets. Moreover, no assurance can be given that these agreements will be effective in controlling access to, distribution, use, misuse, misappropriation, reverse engineering, or disclosure of our proprietary information, know-how, and trade secrets. Further, these agreements may not prevent our competitors from independently developing technologies that are substantially equivalent or superior to our offering and platform capabilities. These agreements may be breached, and we may not have adequate remedies for any such breach. Additionally, as a result of the Codecov Breach, certain of our proprietary data and information, including source code, was exfiltrated. This and any future similar incidents may lead to unauthorized use of our intellectual property rights by third parties. Third parties with access to our exfiltrated source code may also glean insights into our proprietary architecture by examining structural elements of the source code. Due to the nature of this incident, our ability to enforce our rights against such unauthorized users may be limited or not possible.

In order to protect our intellectual property rights, we may be required to spend significant resources to monitor and protect such rights. Litigation may be necessary in the future to enforce our intellectual property rights and to protect our trade secrets. Litigation brought to protect and enforce our intellectual property rights could be costly, time-consuming, and distracting to management, and could result in the impairment or loss of portions of our intellectual property. Further, our efforts to enforce our intellectual property rights may be met with defenses, counterclaims, and countersuits attacking the validity and enforceability of our intellectual property rights, and if such defenses, counterclaims, or countersuits are successful, we could lose valuable intellectual property rights. Our inability to protect our proprietary technology against unauthorized copying or use, as well as any costly litigation or diversion of our management's attention and resources, could delay further sales or the implementation of our offering and platform capabilities, impair the functionality of our offering and platform capabilities, delay introductions of new solutions, result in our substituting inferior or more costly technologies into our offering, or injure our reputation.

We may become subject to intellectual property disputes, which are costly and may subject us to significant liability and increased costs of doing business.

Our success depends, in part, on our ability to develop and commercialize our offering without infringing, misappropriating or otherwise violating the intellectual property rights of third parties. However, we may not be aware that our offering is infringing, misappropriating or otherwise violating third-party intellectual property rights, and such third parties may bring claims alleging such infringement, misappropriation or violation. Lawsuits are time-consuming and expensive to resolve, and they divert management's time and attention. The software industry is characterized by the existence of a large number of patents, copyrights, trademarks, trade secrets, and other intellectual and proprietary rights. Companies in the software industry are often required to defend against litigation claims based on allegations of infringement, misappropriation or other violations of intellectual property rights. Our technologies may not be able to withstand any third-party claims against their use. In addition, many companies have the capability to dedicate substantially greater resources to enforce their intellectual property rights and to defend claims that may be brought against them. We do not currently have a large patent portfolio, which could prevent us from deterring patent infringement claims through our own patent portfolio, and our competitors and others may now and in the future have significantly larger and more mature patent portfolios than we have. Any litigation may also involve patent holding companies or other adverse patent owners that have no relevant product revenue, and therefore, our patent applications may provide little or no deterrence as we would not be able to assert them against such entities or individuals. If a third party is able to obtain an injunction preventing us from accessing such third-party intellectual property rights, or if we cannot license or develop alternative technology for any infringing aspect of our business, we would be forced to limit or stop sales of our offering or cease business activities related to such intellectual property. Although we carry general liability insurance, our insurance may not cover potential claims of this type or may not be adequate to indemnify us for all liability that may be imposed. We cannot predict the outcome of lawsuits and cannot ensure that the results of any such actions will not have an adverse effect on our business, financial condition or results of operations. Any intellectual property litigation to which we might become a party, or for which we are required to provide indemnification, may require us to do one or more of the following:

- cease selling or using offerings that incorporate the intellectual property rights that we allegedly infringe, misappropriate or violate;
- make substantial payments for legal fees, settlement payments, or other costs or damages;
- obtain a license, which may not be available on reasonable terms or at all, to sell or use the relevant technology; or
- redesign the allegedly infringing offerings to avoid infringement, misappropriation or violation, which could be costly, time-consuming, or impossible.

Even if the claims do not result in litigation or are resolved in our favor, these claims, and the time and resources necessary to resolve them, could divert the resources of our management and harm our business and results of operations. Moreover, there could be public announcements of the results of hearings, motions or other interim proceedings or developments, and if securities analysts or investors perceive these results to be negative, it could have a substantial adverse effect on the price of our Class A common stock. We expect that the occurrence of infringement claims is likely to grow as the market for our platform for data in motion and our offering grows. Accordingly, our exposure to damages resulting from infringement claims could increase, and this could further exhaust our financial and management resources.

Risks Related to Our Dependence on Third Parties

We rely on third-party providers of cloud-based infrastructure to host Confluent Cloud. Any failure to adapt our offering to evolving network architecture technology, disruption in the operations of these third-party providers, limitations on capacity or use of features, or interference with our use could adversely affect our business, financial condition, and results of operations.

We outsource all of the infrastructure relating to Confluent Cloud to AWS, Azure, and GCP, as selected by our customers. Customers of our Confluent Cloud service need to be able to access our service at any time, without interruption or degradation of performance, and we provide them with service-level commitments with respect to uptime. Our Confluent Cloud service depends on the ability of the cloud infrastructure hosted by these third-party providers to allow for our customers' configuration, architecture, features, and interconnection specifications, as well as secure the information stored in these virtual data centers, which is transmitted through third-party internet service providers. Any limitation on the capacity of our third-party hosting providers, including due to technical failures, natural disasters, fraud, or security attacks, could impede our ability to onboard new customers or expand the usage of our existing customers, which could adversely affect our business, financial condition, and results of operations. In addition, our third-party cloud service providers run their own platforms that we access, and we are, therefore, vulnerable to service interruptions at these providers. Any incident affecting our providers' infrastructure, including any incident that may be caused by cyber-attacks, natural disasters, fire, flood, severe storm, earthquake, power loss, telecommunications failures, terrorist or other attacks, and other similar events beyond our control could negatively affect our Confluent Cloud service. In some instances, we may not be able to identify the cause or causes of these performance problems within a period of time acceptable to our customers. A prolonged service disruption affecting our service for any of the foregoing reasons would negatively impact our ability to serve our customers and could damage our reputation with current and potential customers, expose us to liability, cause us to lose customers or otherwise harm our business. We may also incur significant costs for using alternative equipment or taking other actions in preparation for, or in reaction to, events that damage the third-party cloud services we use. Features and functionality for Confluent Cloud may also not be available on the same basis or at all on one or more infrastructure platforms, which may hinder adoption of Confluent Cloud, reduce usage, and harm our brand, business, and results of operations. Additionally, such third-party providers either have, or may develop competing products to Confluent Cloud, which may impact our ability to partner with them effectively. Any of the above circumstances or events may harm our reputation, cause customers to stop using our products, impair our ability to increase revenue from existing customers, impair our ability to grow our customer base, and otherwise harm our business, results of operations, and financial condition.

In the event that our service agreements with our third-party cloud service providers are terminated or amended, or there is a lapse of service, elimination of services or features that we utilize, interruption of internet service provider connectivity or damage to such facilities, access to Confluent Cloud could be interrupted and result in significant delays and additional expense as we arrange or create new facilities and services or re-architect our Confluent Cloud service for deployment on a different cloud infrastructure service provider, which could adversely affect our business, financial condition, and results of operations. To the extent that we do not effectively anticipate capacity demands, upgrade our systems as needed, and continually develop our technology and network architecture to accommodate actual and anticipated changes in technology, our business and results of operations may be adversely affected.

If we are unable to develop and maintain successful relationships with partners to distribute our products and generate sales opportunities, our business, results of operations, and financial condition could be harmed.

We have established, and intend to continue seeking opportunities for, partnership arrangements with certain channel partners to distribute our products and generate sales opportunities, particularly internationally. We believe that continued growth in our business is dependent upon identifying, developing, and maintaining strategic relationships with our existing and potential channel partners that can drive revenue growth in more geographies and market segments, particularly for government customers, and provide additional features and functionality to our customers. Our agreements with our existing channel partners are non-exclusive, meaning our channel partners may offer customers the products of several different companies, including products that compete with ours. They may also cease marketing our products with limited or no notice and with little or no penalty. We expect that any additional channel partners we identify and develop will be similarly non-exclusive and not bound by any requirement to continue to market our products. As our channel partnerships come to an end or terminate, we may be unable to renew or replace them on comparable terms, or at all. In addition, winding down channel partnerships can result in additional costs, litigation, and negative publicity. If we fail to identify additional channel partners in a timely and cost-effective manner, or at all, or are unable to assist our current and future channel partners in independently distributing and deploying our products, our business, results of operations, and financial condition could be harmed. When we enter into channel partnerships, our partners may be required to undertake some portion of sales, marketing, implementation services, engineering services, support services, or software configuration that we would otherwise provide, including due to regulatory constraints. In such cases, our partner may be less successful than we would have otherwise been absent the arrangement and our ability to influence, or have visibility into, the sales, marketing, and related efforts of our partners may be limited. Further, if our channel partners do not effectively market and sell our products, or fail to meet the needs of our customers, our reputation and ability to grow our business may also be harmed.

We depend and rely on SaaS technologies from third parties to operate our business, and interruptions or performance problems with these technologies may adversely affect our business and results of operations.

We rely on hosted SaaS applications from third parties in order to operate critical functions of our business, including enterprise resource planning, order management, billing, project management, human resources, technical support, and accounting and other operational activities. If these services become unavailable due to extended outages, interruptions or because they are no longer available on commercially reasonable terms, our expenses could increase, our ability to manage finances could be interrupted and our processes for managing sales of our offering and supporting our customers could be impaired until equivalent services, if available, are identified, obtained, and implemented, all of which could adversely affect our business and results of operations.

Risks Related to Our Employees and Culture

We rely on the performance of highly skilled personnel, including senior management and our engineering, services, sales and technology professionals. If we are unable to retain or motivate key personnel or hire, retain and motivate qualified personnel, our business will be harmed.

We believe our success has depended, and continues to depend, on the efforts and talents of our senior management team, particularly Jay Kreps, our Chief Executive Officer and co-founder, as well as our other key employees in the areas of research and development and sales and marketing.

From time to time, there may be changes in our executive management team or other key employees resulting from the hiring or departure of these personnel. Our executive officers and certain other key employees are generally employed on an at-will basis, which means that these personnel could terminate their employment with us at any time. The loss of one or more of our executive officers, or the failure by our executive team to effectively work with our employees and lead our company, could harm our business. We also are dependent on the continued service of our existing software engineers because of the complexity of our offering.

In addition, to execute our growth plan, we must attract and retain highly qualified personnel. Competition for these personnel is intense, especially for engineers experienced in designing and developing cloud-based infrastructure products and for experienced sales professionals. If we are unable to attract such personnel at appropriate locations, we may need to hire in new regions, which may add to the complexity and costs of our business operations. From time to time, we have experienced, and we expect to continue to experience, difficulty in hiring and retaining employees with appropriate qualifications, which may be exacerbated by the Restructuring Plan and any similar future actions. Many of the companies with which we compete for experienced personnel have greater resources than we have. Further, inflationary pressures, or stress over economic, geopolitical, or pandemic-related events such as those the global market is currently experiencing, may result in employee attrition. If we hire employees from competitors or other companies, their former employers may attempt to assert that these employees or we have breached certain legal obligations, resulting in a diversion of our time and resources. In addition, prospective and existing employees often consider the value of the equity awards they receive in connection with their employment. If the actual or perceived value of our equity awards declines, experiences significant volatility, or increases such that prospective employees believe there is limited upside to the value of our equity awards, it may adversely affect our ability to recruit and retain key employees. Additionally, in order to retain our existing employees and manage potential attrition, including as a result of stock price decreases and continued market volatility that impact the actual or perceived value of our equity awards, we have issued and may in the future issue additional equity awards, which could negatively impact our results of operations. If we fail to attract new personnel or fail to retain and motivate our current personnel, our business and future growth prospects would be harmed.

Our company values have contributed to our success. If we cannot maintain these values as we grow, we could lose certain benefits we derive from them, and our employee turnover could increase, which could harm our business.

We believe that our company values have been and will continue to be a key contributor to our success. Despite the Restructuring Plan, we expect to continue to hire across our business in a disciplined manner to support future growth initiatives. Our headcount growth may result in changes to certain employees' adherence to our core company values. If we do not continue to maintain our adherence to our company values as we grow, including through any future acquisitions or other strategic transactions, we may experience increased turnover in a portion of our current employee base and may not continue to be successful in hiring future employees. Moreover, many of our employees may be eligible to receive significant proceeds from the sale of Class A common stock in the public markets. This may lead to higher employee attrition rates. If we do not replace departing employees on a timely basis, our business and growth may be harmed.

Risks Related to Our International Operations

If we are not successful in expanding our operations and customer base internationally, our business and results of operations could be negatively affected.

A component of our growth strategy involves the further expansion of our operations and customer base internationally. Customers outside the United States generated 40% and 38% of our revenue for the six months ended June 30, 2023, and the year ended December 31, 2022, respectively. We are continuing to adapt to and develop strategies to expand in international markets, but there is no guarantee that such efforts will have the desired effect. For example, we anticipate that we will need to establish relationships with new channel partners in order to expand into certain countries, and if we fail to identify, establish, and maintain such relationships, we may be unable to execute on our expansion plans. As of June 30, 2023, approximately 40% of our full-time employees were located outside of the United States, with 8% of our full-time employees located in the UK. We expect that our international activities will continue to grow for the foreseeable future as we continue to pursue opportunities in existing and new international markets, which will require significant dedication of management attention and financial resources. If we invest substantial time and resources to further expand our international operations and are unable to do so successfully and in a timely manner, our business and results of operations will suffer.

We are subject to risks inherent in international operations that can harm our business, results of operations, and financial condition.

Our current and future international business and operations involve a variety of risks, including:

- slower than anticipated availability and adoption of cloud infrastructure or cloud-native products by international businesses;
- changes in a specific country's or region's political or economic conditions, including in the UK as a result of Brexit;
- the need to adapt and localize our offering for specific countries;
- greater difficulty collecting accounts receivable and longer payment cycles;
- potential changes in trade relations, regulations, or laws;
- unexpected changes in laws, regulatory requirements, or tax laws;
- interest rates, as well as changes in existing and expected interest rates, which may vary across the jurisdictions in which we do business;
- more stringent regulations relating to data privacy, security, and data localization requirements and the unauthorized use of, or access to, commercial and personal information;
- differing and potentially more onerous labor regulations, especially in Europe, where labor laws are generally more advantageous to employees as compared to the United States, including deemed hourly wage and overtime regulations in these locations;
- challenges inherent in efficiently managing, and the increased costs associated with, an increased number of employees over large geographic distances, including the need to implement appropriate systems, policies, benefits, and compliance programs that are specific to each jurisdiction;
- potential changes in laws, regulations, and costs affecting our UK operations and local employees due to Brexit;
- difficulties in managing a business in new markets with diverse cultures, languages, customs, legal systems, alternative dispute systems, and regulatory systems;

- increased travel, real estate, infrastructure, and legal compliance costs associated with international operations;
- currency exchange rate fluctuations and the resulting effect on our revenue and expenses, and challenges to international customers due to a rise in the value of the U.S. dollar;
- the cost and risk of entering into hedging transactions;
- limitations on our ability to reinvest earnings from operations in one country to fund the capital needs of our operations in other countries;
- laws and business practices favoring local competitors or general market preferences for local vendors;
- limited or insufficient intellectual property protection or difficulties obtaining, maintaining, protecting, or enforcing our intellectual property rights, including our trademarks and patents;
- political instability, economic sanctions, terrorist activities, or international conflicts, including the ongoing conflict between Russia and Ukraine, which have impacted and may continue to impact the operations of our business or the businesses of our customers;
- inflationary pressures, such as those the global market is currently experiencing, which have increased and may continue to increase costs for certain services;
- health epidemics or pandemics, such as the COVID-19 pandemic;
- actual or perceived risk of economic recession;
- exposure to liabilities under anti-corruption and anti-money laundering laws, including the U.S. Foreign Corrupt Practices Act, or FCPA, U.S. bribery laws, the UK Bribery Act, and similar laws and regulations in other jurisdictions; and
- adverse tax burdens and foreign exchange controls that could make it difficult to repatriate earnings and cash.

The occurrence of any one of these risks could harm our international business and, consequently, our results of operations. Additionally, operating in international markets requires significant management attention and financial resources. We cannot be certain that the investment and additional resources required to operate in other countries will produce desired levels of revenue or profitability.

We are exposed to fluctuations in currency exchange rates, which could negatively affect our results of operations.

Our subscriptions and services are billed in U.S. dollars, and therefore, our revenue is not subject to foreign currency risk. However, a strengthening of the U.S. dollar could increase the real cost of our offering to our customers outside of the United States, which could adversely affect our results of operations. In addition, an increasing portion of our operating expenses are incurred outside the United States. These operating expenses are denominated in foreign currencies and are subject to fluctuations due to changes in foreign currency exchange rates. We currently hedge a portion of operating expenses denominated in certain currencies against foreign currency exchange rate fluctuations. If we are not able to successfully hedge against the risks associated with fluctuations in these currencies or if we do not hedge a sufficient portion of such operating expenses, our financial condition and results of operations could be adversely affected.

Risks Related to Our Tax, Legal, and Regulatory Environment

We are subject to governmental export and import controls that could impair our ability to compete in international markets or subject us to liability if we violate the controls.

Our offering is subject to U.S. export controls, including the Export Administration Regulations, and we incorporate encryption technology into our offering. Our offering and the underlying technology may be exported outside of the United States only with the required export authorizations, including by license, a license exception, or other appropriate government authorizations, including the filing of an encryption classification request or self-classification report, as applicable.

Furthermore, we are required to comply with economic and trade sanctions laws and regulations administered by governments where our offering is provided, including the U.S. government (including regulations administered and enforced by the Office of Foreign Assets Control of the U.S. Treasury Department and the U.S. Department of State). For example, following Russia's invasion of Ukraine, the United States and other countries imposed economic sanctions and severe export control restrictions against Russia and Belarus, and the United States and other countries could impose wider sanctions and export restrictions and take other actions should the conflict further escalate. These economic and trade sanctions prohibit or restrict the shipment of most products and services to embargoed jurisdictions or sanctioned parties, unless required export authorizations are obtained. Obtaining the necessary export license or other authorization for a particular sale may be time-consuming and may result in the delay or loss of sales opportunities.

While we have taken certain precautions to prevent our offering from being provided in violation of export control and sanctions laws, and are in the process of enhancing our policies and procedures relating to export control and sanctions compliance, our products may have been in the past, and could in the future be, provided inadvertently in violation of such laws. Violations of U.S. sanctions or export control regulations can result in significant fines or penalties and possible incarceration for responsible employees and managers.

If our channel partners fail to obtain appropriate import, export, or re-export licenses or permits, we may also be adversely affected through reputational harm, as well as other negative consequences, including government investigations and penalties.

Also, various countries, in addition to the United States, regulate the import and export of certain encryption and other technology, including import and export licensing requirements, and have enacted laws that could limit our ability to distribute our offering or could limit our end-customers' ability to implement our offering in those countries. Additionally, export restrictions recently imposed on Russia and Belarus specifically limit the export of encryption software to these locations. Changes in our offering or future changes in export and import regulations may create delays in the introduction of our offering in international markets, prevent our end-customers with international operations from deploying our offering globally or, in some cases, prevent the export or import of our offering to certain countries, governments or persons altogether. From time to time, various governmental agencies have proposed additional regulation of encryption technology. Any change in export or import regulations, economic sanctions or related legislation, increased export and import controls, or change in the countries, governments, persons or technologies targeted by such regulations, could result in decreased use of our offering by, or in our decreased ability to export or sell our offering to, existing or potential end-customers with international operations. Any decreased use of our offering or limitation on our ability to export or sell our offering would adversely affect our business, results of operations, and growth prospects.

We are subject to anti-corruption, anti-bribery, anti-money laundering, and similar laws, and non-compliance with such laws can subject us to criminal or civil liability and harm our business, financial condition, and results of operations.

We are subject to the FCPA, U.S. domestic bribery laws, the UK Bribery Act, and other anti-corruption and anti-money laundering laws in the countries in which we conduct activities. Anti-corruption and anti-bribery laws have been enforced aggressively in recent years and are interpreted broadly to generally prohibit companies, their employees, and their third-party intermediaries from authorizing, offering, or providing, directly or indirectly, improper payments or benefits to recipients in the public or private sector. As we increase our international sales and business and sales to the public sector, we may engage with business partners and third-party intermediaries to market our offering and to obtain necessary permits, licenses, and other regulatory approvals. In addition, we or our third-party intermediaries may have direct or indirect interactions with officials and employees of government agencies or state-owned or affiliated entities. We can be held liable for the corrupt or other illegal activities of these third-party intermediaries, our employees, representatives, contractors, partners, and agents, even if we do not explicitly authorize such activities.

While we have policies and procedures to address compliance with such laws, our employees and agents may take actions in violation of our policies and applicable law, for which we may be ultimately held responsible. As we increase our international sales and business, our risks under these laws may increase.

Detecting, investigating and resolving actual or alleged violations of anti-corruption laws can require a significant diversion of time, resources, and attention from senior management. In addition, noncompliance with anti-corruption, anti-bribery or anti-money laundering laws could subject us to whistleblower complaints, investigations, sanctions, settlements, prosecution, enforcement actions, fines, damages, other civil or criminal penalties or injunctions, suspension, or debarment from contracting with certain persons, reputational harm, adverse media coverage, and other collateral consequences. If any subpoenas or investigations are launched, or governmental or other sanctions are imposed, or if we do not prevail in any possible civil or criminal proceeding, our business, financial condition, and results of operations could be harmed. In addition, responding to any action will likely result in a materially significant diversion of management's attention and resources and significant defense costs and other professional fees.

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

The future success of our business, and particularly Confluent Cloud, depends upon the continued use of the internet as a primary medium for commerce, communication, and business applications. Federal, state or foreign government bodies or agencies have in the past adopted, and may in the future adopt, laws or regulations affecting the use of the internet as a commercial medium. Changes in these laws or regulations could require us to modify our software in order to comply with these changes. In addition, government agencies or private organizations may begin to impose taxes, fees or other charges for accessing the internet or commerce conducted via the internet. These laws or charges could limit the growth of internet-related commerce or communications generally, resulting in reductions in the demand for internet-based solutions such as ours.

In addition, the use of the internet as a business tool could be adversely affected due to delays in the development or adoption of new standards and protocols to handle increased demands of internet activity, security, reliability, cost, ease of use, accessibility, and quality of service. The performance of the internet and its acceptance as a business tool have been adversely affected by "ransomware," "viruses," "worms," "malware," "phishing attacks," "data breaches," and similar malicious programs, behavior, and events, and the internet has experienced a variety of outages and other delays as a result of damage to portions of its infrastructure. If the use of the internet is adversely affected by these issues, demand for our subscription offering and related services could suffer.

Our international operations may subject us to greater than anticipated tax liabilities.

We are expanding our international operations to better support our growth into international markets. Our corporate structure and associated transfer pricing policies contemplate future growth in international markets, and consider the functions, risks, and assets of the various entities involved in intercompany transactions. The amount of taxes we pay in different jurisdictions may depend on the application of the tax laws of various jurisdictions, including the United States, to our international business activities, changes in tax rates, new or revised tax laws or interpretations of existing tax laws and policies, and our ability to operate our business in a manner consistent with our corporate structure and intercompany arrangements. The taxing authorities of the jurisdictions in which we operate may challenge our methodologies for pricing intercompany transactions pursuant to our intercompany arrangements or disagree with our determinations as to the income and expenses attributable to specific jurisdictions. If such a challenge or disagreement were to occur, and our position was not sustained, we could be required to pay additional taxes, interest, and penalties, which could result in one-time tax charges, higher effective tax rates, reduced cash flows, and lower overall profitability of our operations. Our financial statements could fail to reflect adequate reserves to cover such a contingency.

Changes in tax laws or tax rulings could harm our financial position, results of operations and cash flows.

The tax regimes we are subject to or operate under, including income and non-income taxes, are unsettled and may be subject to significant change. Changes in tax laws, regulations, or rulings, or changes in interpretations of existing laws and regulations, could materially affect our financial position and results of operations. Many countries in Europe, as well as a number of other countries and organizations, including the Organization for Economic Cooperation and Development and the European Commission, have recently proposed, recommended, or (in the case of countries) enacted or otherwise become subject to changes to existing tax laws or new tax laws that could significantly increase our tax obligations in the countries where we do business or require us to change the manner in which we operate our business. These proposals, recommendations and enactments include changes to the existing framework in respect of income taxes, as well as new types of non-income taxes (such as taxes based on a percentage of revenue), which could apply to our business. If U.S. or other foreign tax authorities change applicable tax laws or successfully challenge how or where our profits are currently recognized, our overall taxes could increase, and our business, financial condition or results of operations may be adversely impacted. These proposals, recommendations and enactments include changes to the existing framework in respect of income taxes, as well as new types of non-income taxes (such as taxes based on a percentage of revenue or taxes applicable to digital services), which could apply to our business. Due to the large and expanding scale of our international business activities, these types of changes to the taxation of our activities could increase our worldwide effective tax rate, increase the amount of taxes imposed on our business, and harm our financial position. Such changes may also apply retroactively to our historical operations and result in taxes greater than the amounts estimated and recorded in our financial statements. Any of these outcomes could harm our financial position and results of operations.

We could be required to collect additional sales taxes or be subject to other tax liabilities that may increase the costs our customers would have to pay for our offering and adversely affect our results of operations.

An increasing number of states have considered or adopted laws that impose tax collection obligations on out-of-state companies. Online sellers can be required to collect sales and use tax despite not having a physical presence in the buyer's state. States or local governments may interpret existing laws, or have adopted or may adopt new laws, requiring us to calculate, collect and remit taxes on sales in their jurisdictions. A successful assertion by one or more taxing jurisdictions requiring us to collect taxes where we presently do not do so, or to collect more taxes in a jurisdiction in which we currently do collect some taxes, could result in substantial tax liabilities, including taxes on past sales, as well as penalties and interest. The imposition by state or local governments of sales tax collection obligations on out-of-state sellers also could create additional administrative burdens for us, put us at a competitive disadvantage if they do not impose similar obligations on our competitors, and decrease our future sales, which could have a material adverse effect on our business and results of operations.

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

As of December 31, 2022, we had net operating loss (NOL) carryforwards for federal and state income tax purposes of \$1,283.0 million and \$689.3 million, respectively, which may be available to offset taxable income in the future. A portion of the NOLs begin to expire in various years beginning in 2034 for federal purposes and 2025 for state purposes if not utilized. The remaining portion of these federal NOLs are carried forward indefinitely. Of the federal net operating loss carryforwards, approximately 97% can be carried forward indefinitely, but are limited to 80% of annual taxable income. In addition, as of December 31, 2022, we had foreign NOL carryforwards of \$60.8 million which can be carried forward indefinitely. A lack of future taxable income would adversely affect our ability to utilize these NOLs before they expire.

In general, under Section 382 of the Internal Revenue Code of 1986, as amended, or the Code, a corporation that undergoes an “ownership change” (as defined under Section 382 of the Code and applicable Treasury Regulations) is subject to limitations on its ability to utilize its pre-change NOLs to offset future taxable income. We may experience a future ownership change under Section 382 of the Code that could affect our ability to utilize the NOLs to offset our income. Furthermore, our ability to utilize NOLs of companies that we have acquired or may acquire in the future may be subject to limitations. There is also a risk that due to regulatory changes, such as suspensions on the use of NOLs or other unforeseen reasons, our existing NOLs could expire or otherwise be unavailable to reduce future income tax liabilities, including for state tax purposes. For these reasons, we may not be able to utilize a material portion of the NOLs reflected on our balance sheet, even if we attain profitability, which could potentially result in increased future tax liability to us and could adversely affect our results of operations and financial condition.

Changes in our effective tax rate or tax liability may have an adverse effect on our results of operations.

We are subject to income taxes in the United States and various foreign jurisdictions. The determination of our worldwide provision for income taxes and other tax liabilities requires significant judgment by management, and there are many transactions where the ultimate tax determination is uncertain. We believe that our provision for income taxes is reasonable, but the ultimate tax outcome may differ from the amounts recorded in our consolidated financial statements and may materially affect our financial results in the period or periods in which such outcome is determined.

Our effective tax rate could increase due to several factors, including:

- changes in the relative amounts of income before taxes in the various jurisdictions in which we operate that have differing statutory tax rates;
- changes in tax laws, tax treaties, and regulations or the interpretation of them, including the Tax Act;
- changes to our assessment about our ability to realize our deferred tax assets that are based on estimates of our future results, the prudence and feasibility of possible tax planning strategies, and the economic and political environments in which we do business;
- the effects of acquisitions and their integrations;
- the outcome of current and future tax audits, examinations or administrative appeals; and
- limitations or adverse findings regarding our ability to do business in some jurisdictions.

Any of these developments could adversely affect our results of operations.

Risks Related to Our Accounting Policies and Internal Controls

Our reported financial results may be adversely affected by changes in generally accepted accounting principles (“GAAP”) in the United States.

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

If our estimates or judgments relating to our critical accounting policies prove to be incorrect, our results of operations could be adversely affected.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in our consolidated financial statements and accompanying notes appearing elsewhere in this Quarterly Report. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, as provided in the section titled “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies and Estimates.” The results of these estimates form the basis for making judgments about the carrying values of assets, liabilities and equity, and the amount of revenue and expenses that are not readily apparent from other sources. Significant estimates and judgments involve revenue recognition, deferred contract costs, and the valuation of our stock-based compensation awards, among others. Our results of operations may be adversely affected if our assumptions change or if actual circumstances differ from those in our assumptions, which could cause our results of operations to fall below the expectations of securities analysts and investors, resulting in a decline in the market price of our Class A common stock.

We are obligated to develop and maintain proper and effective internal control over financial reporting, and any failure to maintain the adequacy of these internal controls may adversely affect investor confidence in our company and, as a result, the value of our Class A common stock.

We are required, pursuant to Section 404 of the Sarbanes-Oxley Act, or Section 404, to furnish a report by management on, among other things, the effectiveness of our internal control over financial reporting. This assessment includes disclosure of any material weaknesses identified by our management in our internal control over financial reporting. In addition, our independent registered public accounting firm is required to attest to the effectiveness of our internal control over financial reporting. The process of compiling the system and process documentation necessary to perform the evaluation required under Section 404 is costly and challenging. We have established an internal audit group, and as we continue to grow, we may hire additional accounting and financial staff with appropriate public company experience and technical accounting knowledge.

During the evaluation and testing process of our internal controls, if we identify one or more material weaknesses in our internal control over financial reporting, we will be unable to certify that our internal control over financial reporting is effective. We cannot assure you that there will not be material weaknesses in our internal control over financial reporting in the future. Failure to maintain internal control over financial reporting, including historical or future control deficiencies, could severely inhibit our ability to accurately report our financial condition or results of operations. If we are unable to conclude that our internal control over financial reporting is effective, or if our independent registered public accounting firm determines we have a material weakness in our internal control over financial reporting, we could lose investor confidence in the accuracy and completeness of our financial reports, the market price of our Class A common stock could decline, and we could be subject to sanctions or investigations by the SEC or other regulatory authorities. Failure to remedy any material weakness in our internal control over financial reporting, or to implement or maintain other effective control systems required of public companies, could also restrict our future access to the capital markets.

Risks Related to Ownership of Our Class A Common Stock

The dual class structure of our common stock as contained in our amended and restated certificate of incorporation has the effect of concentrating voting control with those stockholders who held our stock prior to the IPO, including our executive officers, employees, and directors and their affiliates, and limiting your ability to influence corporate matters, which could adversely affect the trading price of our Class A common stock.

Our Class B common stock has 10 votes per share, and our Class A common stock has one vote per share. As of June 30, 2023, stockholders who hold shares of Class B common stock, including our executive officers and directors and their affiliates, together hold approximately 81.1% of the voting power of our outstanding capital stock, and our Chief Executive Officer, Mr. Kreps, beneficially owns approximately 8.6% of our outstanding classes of common stock as a whole, but controls approximately 22.4% of the voting power of our outstanding common stock. As a result, our executive officers, directors, and other affiliates and potentially our Chief Executive Officer on his own have significant influence over our management and affairs and over all matters requiring stockholder approval, including election of directors and significant corporate transactions, such as a merger or other sale of the company or our assets, for the foreseeable future. Even if Mr. Kreps is no longer employed with us, he will continue to have the same influence over matters requiring stockholder approval.

In addition, the holders of Class B common stock collectively will continue to be able to control all matters submitted to our stockholders for approval even if their stock holdings represent less than 50% of the outstanding shares of our common stock. Because of the 10-to-1 voting ratio between our Class B common stock and Class A common stock, the holders of our Class B common stock collectively will continue to control a majority of the combined voting power of our common stock even when the shares of Class B common stock represent as little as 10% of all outstanding shares of our Class A common stock and Class B common stock. This concentrated control will limit your ability to influence corporate matters for the foreseeable future, and, as a result, the market price of our Class A common stock could be adversely affected.

Future transfers or voluntary conversions by holders of shares of Class B common stock will generally result in those shares converting to shares of Class A common stock, which will have the effect, over time, of increasing the relative voting power of those holders of Class B common stock who retain their shares in the long term. Certain permitted transfers, as specified in our amended and restated certificate of incorporation, will not result in shares of Class B common stock automatically converting to shares of Class A common stock, including certain estate planning transfers as well as transfers to our founders or our founders' estates or heirs upon death or incapacity of such founder. If, for example, Mr. Kreps (or family trusts to which he were to transfer shares of Class B common stock) retain a significant portion of his holdings of Class B common stock for an extended period of time, he (or such trusts) could, in the future, control a majority of the combined voting power of our Class A common stock and Class B common stock. As a board member, Mr. Kreps owes a fiduciary duty to our stockholders and must act in good faith in a manner he reasonably believes to be in the best interests of our stockholders. As a stockholder, Mr. Kreps is entitled to vote his shares in his own interests, which may not always be in the interests of our stockholders generally.

FTSE Russell does not allow most newly public companies utilizing dual or multi-class capital structures to be included in its indices, including the Russell 2000. Also, in 2017, MSCI, a leading stock index provider, opened public consultations on its treatment of no-vote and multi-class structures and temporarily barred new multi-class listings from certain of its indices; however, in October 2018, MSCI announced its decision to include equity securities "with unequal voting structures" in its indices and to launch a new index that specifically includes voting rights in its eligibility criteria. Under the announced policies, our dual class capital structure makes us ineligible for inclusion in certain indices, and as a result, mutual funds, exchange-traded funds, and other investment vehicles that attempt to passively track these indices will not be investing in our stock. In addition, we cannot assure you that other stock indices will not take similar actions. Given the sustained flow of investment funds into passive strategies that seek to track certain indices, exclusion from certain stock indices would likely preclude investment by many of these funds and would make our Class A common stock less attractive to other investors. As a result, the trading price, volume, and liquidity of our Class A common stock could be adversely affected.

Our stock price may be volatile, and the value of our Class A common stock may decline.

The market price of our Class A common stock may be highly volatile and may fluctuate or decline substantially as a result of a variety of factors, some of which are beyond our control, including:

- actual or anticipated fluctuations in our financial condition or results of operations, including due to fluctuations in usage of Confluent Cloud and strategic shifts in our focus on growth versus operating efficiency, margin improvement, and profitability;
- variance in our financial performance, including sales growth and operating margins, from our forecasts or the expectations of securities analysts;
- changes in our revenue mix;
- changes in the pricing of our offering;
- changes in our projected operating and financial results;
- changes in laws or regulations applicable to our offering;
- seasonality in sales, customer implementations, results of operations, and RPO;
- announcements by us or our competitors of significant business developments, acquisitions, or new offerings;
- significant data breaches, disruptions to or other incidents involving our offering;
- our involvement in litigation or regulatory actions;
- future sales of our Class A common stock and Class B common stock by us or our stockholders;
- changes in senior management or key personnel;
- the trading volume of our Class A common stock;
- financial results, changes in operating performance and stock market valuations of technology companies in our industry segment, including our partners and competitors;
- changes in the anticipated future size and growth rate of our market; and
- general political, social, economic and market conditions, in both domestic and our foreign markets, including effects of increased interest rates, inflationary pressures, bank failures and macroeconomic uncertainty and challenges; and
- actual or perceived risk of economic recession.

Broad market and industry fluctuations, as well as general economic, political, regulatory and market conditions, may also negatively impact the market price of our Class A common stock. In addition, technology stocks have historically experienced high levels of volatility. In the past, companies that have experienced volatility in the market price of their securities have been subject to securities class action litigation. We may be the target of this type of litigation in the future, which could result in substantial expenses and divert our management's attention.

We have broad discretion in the use of the net proceeds to us from our IPO and our convertible notes offering and may not use them effectively.

We have broad discretion in the application of the net proceeds to us from our IPO and our convertible notes offering. Because of the number and variability of factors that will determine our use of the net proceeds from our IPO and convertible notes offering, our ultimate use may vary substantially from our currently intended use. Investors will need to rely on the judgment of our management with respect to the use of proceeds. Pending use, we may invest the net proceeds from our IPO and our convertible notes offering in short-term, investment-grade, interest-bearing securities, such as money market funds, corporate notes and bonds, certificates of deposit, commercial paper, and guaranteed obligations of the U.S. government that may not generate a high yield for our stockholders. If we do not use the net proceeds that we received in our IPO or convertible notes offering effectively, our business, financial condition, results of operations, and prospects could be harmed, and the market price of our Class A common stock could decline.

Future sales of our Class A common stock in the public market could cause the market price of our Class A common stock to decline.

Sales of a substantial number of shares of our Class A common stock in the public market, or the perception that these sales might occur, could depress the market price of our Class A common stock and could impair our ability to raise capital through the sale of additional equity securities. Many of our equity holders who held our capital stock prior to completion of the IPO have substantial unrecognized gains on the value of the equity they hold based on recent market prices of our shares of Class A common stock, and therefore, they may take steps to sell their shares or otherwise secure the unrecognized gains on those shares. We are unable to predict the timing of or the effect that such sales may have on the prevailing market price of our Class A common stock.

Additionally, the conversion of some or all of the notes may dilute the ownership interests of our stockholders. Upon conversion of the notes, we have the option to pay or deliver, as the case may be, cash, shares of our Class A common stock, or a combination of cash and shares of our Class A common stock. If we elect to settle our conversion obligation in shares of our Class A common stock or a combination of cash and shares of our Class A common stock, any sales in the public market of our Class A common stock issuable upon such conversion could adversely affect prevailing market prices of our Class A common stock. In addition, the existence of the notes may encourage short selling by market participants because the conversion of the notes could be used to satisfy short positions, or anticipated conversion of the notes into shares of our Class A common stock could depress the price of our Class A common stock.

In addition, as of June 30, 2023, up to 37,924,750 shares of our Class B common stock and up to 23,850,989 shares of our Class A common stock may be issued upon exercise of outstanding stock options or vesting and settlement of outstanding RSUs, and 48,339,795 shares of our Class A common stock are available for future issuance under our 2021 Plan and our 2021 ESPP, and will become eligible for sale in the public market to the extent permitted by the provisions of various vesting schedules, exercise limitations and Rule 144 and Rule 701 under the Securities Act. In addition, certain of our employees may elect to automatically convert their shares of Class B common stock upon receipt following exercise or settlement of equity awards, as applicable. We have registered all of the shares of Class A common stock and Class B common stock issuable upon exercise of outstanding options and all of the shares of Class A common stock issuable upon vesting and settlement of restricted stock units, as well as other equity incentive awards we may grant in the future for public resale under the Securities Act. Shares of Class A common stock will become eligible for sale in the public market to the extent such options are exercised and restricted stock units settle, subject to compliance with applicable securities laws. Our 0% convertible senior notes due 2027 will also become convertible at the option of the holders, subject to certain limitations and restrictions prior to October 15, 2026. If these additional shares of Class A common stock are sold, or if it is perceived that they will be sold, in the public market, the trading price of our Class A common stock could decline.

Further, certain holders of our outstanding common stock, including our founders and entities affiliated with our founders and certain of our directors, have rights, subject to some conditions, to require us to file registration statements covering the sale of their shares or to include their shares in registration statements that we may file for ourselves or other stockholders.

Our issuance of additional capital stock in connection with financings, acquisitions, investments, our equity incentive plans or otherwise will dilute all other stockholders.

We expect to issue additional capital stock in the future that will result in dilution to all other stockholders. We expect to grant equity awards to employees, officers and directors under our equity incentive plans. We may also raise capital through equity financings in the future. As part of our business strategy, we may acquire or make investments in companies, products or technologies and issue equity securities to pay for any such acquisition or investment. Any such issuances of additional capital stock may cause stockholders to experience significant dilution of their ownership interests and the per share value of our Class A common stock to decline.

We do not intend to pay dividends for the foreseeable future and, as a result, your ability to achieve a return on your investment will depend on appreciation in the price of our Class A common stock.

We have never declared or paid any cash dividends on our capital stock, and we do not intend to pay any cash dividends in the foreseeable future. Any determination to pay dividends in the future will be at the discretion of our board of directors. Accordingly, you may need to rely on sales of our Class A common stock after price appreciation, which may never occur, as the only way to realize any future gains on your investment.

We incur significant costs as a result of operating as a public company, and our management is required to devote substantial time to compliance with our public company responsibilities and corporate governance practices.

As a public company, we incur significant legal, accounting, and other expenses that we did not incur as a private company. We expect such expenses to further increase now that we are no longer an “emerging growth company” as defined in the JOBS Act. The Sarbanes-Oxley Act, the Dodd-Frank Wall Street Reform and Consumer Protection Act, the listing requirements of the Nasdaq Global Select Market, and other applicable securities rules and regulations impose various requirements on public companies. Our management and other personnel devote a substantial amount of time to compliance with these requirements. Moreover, these rules and regulations have increased our legal and financial compliance costs and will make some activities more time-consuming and costly. We cannot predict or estimate the amount of additional costs we will incur as a public company or the specific timing of such costs.

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

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

- authorize our board of directors to issue, without further action by the stockholders, shares of undesignated preferred stock with terms, rights, and preferences determined by our board of directors that may be senior to our Class A common stock;
- require that any action to be taken by our stockholders be effected at a duly called annual or special meeting and not by written consent;
- specify that special meetings of our stockholders can be called only by our board of directors, the chairperson of our board of directors, our chief executive officer, or our president (in the absence of a chief executive officer);
- establish an advance notice procedure for stockholder proposals to be brought before an annual meeting, including proposed nominations of persons for election to our board of directors;
- establish that our board of directors is divided into three classes, with each class serving three-year staggered terms;
- prohibit cumulative voting in the election of directors;
- provide that our directors may be removed for cause only upon the vote of the holders of at least a majority of our outstanding shares of voting stock;
- provide that vacancies on our board of directors may be filled only by the affirmative vote of a majority of directors then in office, even though less than a quorum, or by a sole remaining director; and
- require the approval of our board of directors or the holders of at least 66 2/3% of the voting power of our outstanding shares of voting stock to amend our bylaws and certain provisions of our certificate of incorporation.

These provisions may frustrate or prevent any attempts by our stockholders to replace or remove our current management by making it more difficult for stockholders to replace members of our board of directors, which is responsible for appointing the members of our management. In addition, because we are incorporated in Delaware, we are governed by the provisions of Section 203 of the Delaware General Corporation Law, which generally, subject to certain exceptions, prohibits a Delaware corporation from engaging in any of a broad range of business combinations with any “interested” stockholder for a period of three years following the date on which the stockholder became an “interested” stockholder. Any of the foregoing provisions could limit the price that investors might be willing to pay in the future for shares of our Class A common stock, and they could deter potential acquirers of our company, thereby reducing the likelihood that holders of our Class A common stock would receive a premium for their shares of our Class A common stock in an acquisition.

Our amended and restated certificate of incorporation designates the Court of Chancery of the State of Delaware and the federal district courts of the United States of America as the exclusive forums for certain disputes between us and our stockholders, which restricts our stockholders' ability to choose the judicial forum for disputes with us or our directors, officers, or employees.

Our amended and restated certificate of incorporation provides that the Court of Chancery of the State of Delaware (or, if and only if the Court of Chancery of the State of Delaware lacks subject matter jurisdiction, any state court located within the State of Delaware or, if and only if all such state courts lack subject matter jurisdiction, the federal district court for the District of Delaware) is the sole and exclusive forum for the following types of actions or proceedings under Delaware statutory or common law: (i) any derivative action or proceeding brought on our behalf; (ii) any action or proceeding asserting a claim of breach of a fiduciary duty owed by any of our current or former directors, officers, or other employees to us or our stockholders, or any action asserting a claim for aiding and abetting such breach of fiduciary duty; (iii) any action or proceeding asserting a claim against us or any of our current or former directors, officers or other employees arising out of or pursuant to any provision of the Delaware General Corporation Law, our amended and restated certificate of incorporation or our amended and restated bylaws; (iv) any action or proceeding to interpret, apply, enforce or determine the validity of our amended and restated certificate of incorporation or our amended and restated bylaws (including any right, obligation, or remedy thereunder); (v) any action or proceeding as to which the Delaware General Corporation Law confers jurisdiction to the Court of Chancery of the State of Delaware; and (vi) any action or proceeding asserting a claim against us or any of our current or former directors, officers, or other employees that is governed by the internal affairs doctrine, in all cases to the fullest extent permitted by law and subject to the court's having personal jurisdiction over the indispensable parties named as defendants. This provision does not apply to suits brought to enforce a duty or liability created by the Exchange Act or any other claim for which the federal courts have exclusive jurisdiction. In addition, to prevent having to litigate claims in multiple jurisdictions and the threat of inconsistent or contrary rulings by different courts, among other considerations, our amended and restated certificate of incorporation provides that, unless we consent in writing to the selection of an alternative forum, to the fullest extent permitted by law, the federal district courts of the United States of America are the exclusive forum for resolving any complaint asserting a cause of action arising under the Securities Act, including all causes of action asserted against any defendant named in such complaint. For the avoidance of doubt, this provision is intended to benefit and may be enforced by us, our officers and directors, the underwriters to any offering giving rise to such complaint, and any other professional entity whose profession gives authority to a statement made by that person or entity and who has prepared or certified any part of the documents underlying the offering. However, as Section 22 of the Securities Act creates concurrent jurisdiction for federal and state courts over all suits brought to enforce any duty or liability created by the Securities Act or the rules and regulations thereunder, there is uncertainty as to whether a court would enforce such provision. Our amended and restated certificate of incorporation further provides that any person or entity holding, owning or otherwise acquiring any interest in any of our securities shall be deemed to have notice of and consented to these provisions. Investors also cannot waive compliance with the federal securities laws and the rules and regulations thereunder.

These choice of forum provisions may limit a stockholder's ability to bring a claim in a judicial forum that it finds favorable for disputes with us or our directors, officers, or other employees. While the Delaware courts have determined that such choice of forum provisions are facially valid, a stockholder may nevertheless seek to bring such a claim arising under the Securities Act against us, our directors, officers, or other employees in a venue other than in the federal district courts of the United States of America. In such instance, we would expect to vigorously assert the validity and enforceability of the exclusive forum provisions of our amended and restated certificate of incorporation. This may require significant additional costs associated with resolving such action in other jurisdictions and we cannot assure you that the provisions will be enforced by a court in those other jurisdictions. If a court were to find either exclusive-forum provision in our amended and restated certificate of incorporation to be inapplicable or unenforceable in an action, we may incur further significant additional costs associated with resolving the dispute in other jurisdictions, all of which could harm our business.

Risks Related to Our Convertible Senior Notes

We may not have the ability to raise the funds necessary to settle conversions of the notes in cash or to repurchase the notes upon a fundamental change, and our future debt may contain limitations on our ability to pay cash upon conversion or repurchase of the notes.

Holders of the notes have the right, subject to certain conditions and limited exceptions, to require us to repurchase all or a portion of their notes upon the occurrence of a fundamental change at a fundamental change repurchase price equal to 100% of the principal amount of the notes to be repurchased, plus accrued and unpaid special interest. In addition, upon conversion of the notes, unless we elect to deliver solely shares of our Class A common stock to settle such conversion (other than paying cash in lieu of delivering any fractional share), we will be required to make cash payments in respect of the notes being converted. However, we may not have enough available cash or be able to obtain financing at the time we are required to make repurchases of notes surrendered therefor or pay cash with respect to notes being converted. In addition, our ability to repurchase the notes or to pay cash upon conversions of the notes may be limited by law, by regulatory authority or by agreements governing our future indebtedness. Our failure to repurchase notes at a time when the repurchase is required by the indenture or to pay any cash payable on future conversions of the notes as required by the indenture would constitute a default under the indenture. A default under the indenture governing the notes or the fundamental change itself could also lead to a default under agreements governing our future indebtedness. If the repayment of the related indebtedness were to be accelerated after any applicable notice or grace periods, we may not have sufficient funds to repay the indebtedness and repurchase the notes or make cash payments upon conversions thereof.

The conditional conversion feature of the notes, if triggered, may adversely affect our financial condition and operating results.

In the event the conditional conversion feature of the notes is triggered, holders of notes will be entitled to convert their notes at any time during specified periods at their option. If one or more holders elect to convert their notes, unless we elect to satisfy our conversion obligation by delivering solely shares of our Class A common stock (other than paying cash in lieu of delivering any fractional share), we would be required to settle a portion or all of our conversion obligation through the payment of cash, which could adversely affect our liquidity. In addition, even if holders do not elect to convert their notes, we could be required under applicable accounting rules to reclassify all or a portion of the outstanding principal of the notes as a current rather than long-term liability, which would result in a material reduction of our net working capital.

Certain provisions in the indenture governing the notes may delay or prevent an otherwise beneficial takeover attempt of us.

Certain provisions in the indenture governing the notes may make it more difficult or expensive for a third party to acquire us. For example, the indenture governing the notes generally requires us to repurchase the notes for cash upon the occurrence of a fundamental change and, in certain circumstances, to increase the conversion rate for a holder that converts its notes in connection with a make-whole fundamental change. A takeover of us may trigger the requirement that we repurchase the notes and/or increase the conversion rate, which could make it costlier for a potential acquirer to engage in such takeover. Such additional costs may have the effect of delaying or preventing a takeover of us that would otherwise be beneficial to investors.

General Risk Factors

Any future litigation against us could be costly and time-consuming to defend.

We may become subject to legal proceedings and claims that arise in the ordinary course of business, including but not limited to, intellectual property claims, including trade secret misappropriation and breaches of confidentiality terms, alleged breaches of non-competition or non-solicitation terms, or employment claims made by our current or former employees. Litigation might result in substantial costs and may divert management's attention and resources, which might seriously harm our business, financial condition, and results of operations. Insurance might not cover such claims, might not provide sufficient payments to cover all the costs to resolve one or more such claims, and might not continue to be available on terms acceptable to us. A claim brought against us that is uninsured or underinsured could result in unanticipated costs, potentially harming our business, financial position, and results of operations.

If securities or industry analysts do not publish research or publish unfavorable or inaccurate research about our business, the market price and trading volume of our Class A common stock could decline.

The market price and trading volume of our Class A common stock is heavily influenced by the way analysts interpret our financial information and other disclosures. We do not have control over these analysts. If industry analysts cease coverage of us, our stock price would be negatively affected. If securities or industry analysts do not publish research or reports about our business, downgrade our Class A common stock, or publish negative reports about our business, our stock price would likely decline. If one or more of these analysts cease coverage of us or fail to publish reports on us regularly, demand for our Class A common stock could decrease, which might cause our stock price to decline and could decrease the trading volume of our Class A common stock.

Our business could be disrupted by catastrophic events.

Occurrence of any catastrophic event, including earthquake, fire, flood, tsunami, or other weather event, power loss, telecommunications failure, software or hardware malfunction, cyber-attack, war, or terrorist attack, explosion, or pandemic could impact our business. In particular, our corporate headquarters are located in the San Francisco Bay Area, a region known for seismic activity, and are thus vulnerable to damage in an earthquake. Our insurance coverage may not compensate us for losses that may occur in the event of an earthquake or other significant natural disaster. Additionally, we rely on third-party cloud providers and enterprise applications, technology systems, and our website for our development, marketing, operational support, hosted services, and sales activities. In the event of a catastrophic event, we may be unable to continue our operations and may endure system interruptions, reputational harm, delays in our product development, lengthy interruptions in our services, and security incidents, all of which could have an adverse effect on our future results of operations. If we are unable to develop adequate plans to ensure that our business functions continue to operate during and after a disaster and to execute successfully on those plans in the event of a disaster or emergency, our business would be harmed.

Climate change may have an impact on our business.

While we seek to mitigate our business risks associated with climate change (such as drought, wildfires, hurricanes, increased storm severity and sea level rise), we recognize that there are inherent climate-related risks wherever business is conducted. Our primary locations may be vulnerable to the adverse effects of climate change. For example, certain of our offices have experienced, and are projected to continue to experience, climate-related events at an increasing frequency, including drought, heat waves, wildfires and resultant air quality impacts and power shutoffs associated with wildfire prevention. Changing market dynamics, global policy developments and the increasing frequency and impact of extreme weather events on critical infrastructure in the U.S. and elsewhere have the potential to disrupt our business, the business of our third-party suppliers and the business of our customers, and may cause us to experience losses and additional costs to maintain or resume operations. In addition, we may be subject to increased regulations, reporting requirements, standards or expectations regarding the environmental impacts of our business.

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

(a) Recent Sales of Unregistered Securities.

None.

(b) Use of Proceeds.

On June 28, 2021, we closed our initial public offering of 23,000,000 shares of Class A common stock at an offering price of \$36.00 per share, resulting in aggregate gross proceeds to us of \$828.0 million, before deducting underwriting discounts and commissions and offering expenses. All of the shares issued and sold in our initial public offering were registered under the Securities Act pursuant to a registration statement on Form S-1, as amended (File No. 333-256693), which was declared effective by the SEC on June 23, 2021. There has been no material change in the planned use of proceeds from our initial public offering from those disclosed in our final prospectus for our initial public offering dated as of June 23, 2021 and filed with the SEC pursuant to Rule 424(b)(4) on June 25, 2021.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

None.

ITEM 5. OTHER INFORMATION

During the three months ended June 30, 2023, no director or officer of the Company adopted or terminated a “Rule 10b5-1 trading arrangement” or “non-Rule 10b5-1 trading arrangement,” as each term is defined in Item 408(a) of Regulation S-K.

ITEM 6. EXHIBITS

Exhibit Number	Description	Form	File No.	Exhibit	Filing Date	Filed Herewith
3.1	Amended and Restated Certificate of Incorporation of Confluent, Inc.	8-K	001-40526	3.1	6-28-2021	
3.2	Amended and Restated Bylaws of Confluent, Inc.	10-Q	001-40526	3.2	5-3-2023	
31.1	Certification of Principal Executive Officer pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.					X
31.2	Certification of Principal Financial Officer pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.					X
32.1*	Certification of Principal Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.					X
32.2*	Certification of Principal Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.					X
101.INS	Inline XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document.					X
101.SCH	Inline XBRL Taxonomy Extension Schema Document.					X
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document.					X
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document.					X
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase Document.					X
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase Document.					X
104	Cover Page Interactive Data File (formatted as inline XBRL and contained in Exhibits 101).					X

* The certifications furnished in Exhibits 32.1 and 32.2 hereto are deemed to accompany this Quarterly Report on Form 10-Q and are not deemed “filed” for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section, nor shall they be deemed incorporated by reference into any filing under the Securities Act or the Exchange Act, irrespective of any general incorporation language contained in such filing.

SIGNATURES

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

Date: August 2, 2023

CONFLUENT, INC.

By: /s/ Edward Jay Kreps

Name: Edward Jay Kreps

Title: Chief Executive Officer
(Principal Executive Officer)

By: /s/ Steffan Tomlinson

Name: Steffan Tomlinson

Title: Chief Financial Officer
(Principal Financial Officer)

By: /s/ Ying Christina Liu

Name: Ying Christina Liu

Title: Chief Accounting Officer
(Principal Accounting Officer)

**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER PURSUANT TO
RULES 13a-14(a) AND 15d-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934,
AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Edward Jay Kreps, certify that:

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

Date: August 2, 2023

By: /s/ Edward Jay Kreps
 Name: Edward Jay Kreps
 Title: Chief Executive Officer
 (Principal Executive Officer)

**CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER PURSUANT TO
RULES 13a-14(a) AND 15d-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934,
AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Steffan Tomlinson, certify that:

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

Date: August 2, 2023

By: _____ /s/ Steffan Tomlinson
Name: Steffan Tomlinson
Title: Chief Financial Officer
(Principal Financial Officer)

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

In connection with the Quarterly Report of Confluent, Inc. (the “Company”) on Form 10-Q for the period ended June 30, 2023 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”); and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 2, 2023

By:	_____/s/ Edward Jay Kreps
Name:	Edward Jay Kreps
Title:	Chief Executive Officer (Principal Executive Officer)

This certification accompanies the Form 10-Q to which it relates, is not deemed filed with the Securities and Exchange Commission and is not to be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Exchange Act (whether made before or after the date of the Form 10-Q), irrespective of any general incorporation language contained in such filing.

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

In connection with the Quarterly Report of Confluent, Inc. (the "Company") on Form 10-Q for the period ended June 30, 2023 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"); and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 2, 2023

By: _____ /s/ Steffan Tomlinson
Name: Steffan Tomlinson
Title: Chief Financial Officer
(Principal Financial Officer)

This certification accompanies the Form 10-Q to which it relates, is not deemed filed with the Securities and Exchange Commission and is not to be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Exchange Act (whether made before or after the date of the Form 10-Q), irrespective of any general incorporation language contained in such filing.
