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ANNUAL REPORT

2016





To Our Stockholders,

I'm very proud of our achievements in 2016 and look forward with tremendous enthusiasm toward the opportunities for even more progress in the future. We not only achieved record revenue in 2016 but, as promised, we achieved non-GAAP profitability during the year. We maintained our relentless focus on executing our plan for strategic growth and profitability. Our success was a testament to the diligence and execution of our leadership teams; the drive and expertise of our employees; and the passion and dedication of our customers.

#### Financial Highlights

- Grew revenue 16% over 2015 to reach a record \$230 million
- Reduced GAAP loss by over 47% to \$20.9 million in 2016 compared to \$40.0 million in 2015
- Achieved non-GAAP profitability goal in Q3
- Grew deferred revenue 28% year-over-year to \$92.9 million
- Generated almost \$19 million in cash flow from operations
- Increased cash, cash equivalents and marketable securities to \$114 million; up \$16 million from 2015

#### Corporate & Product Accomplishments

- Launched A10 Thunder TPS 14045, the industry's most powerful DDoS protection solution and best-selling product in A10 history
- Introduced A10 Thunder SSLi as a standalone encryption, decryption and inspection solution
- Released Thunder Convergent Firewall for service providers, cloud providers and large enterprises
- Acquired Appcito, which accelerated the launch of our cloud-native A10 Lightning Application Delivery Service (ADS) and expansion of the A10 Harmony™ platform
- Broadened the A10 Thunder ADC lineup with six new fourth-generation products, including the industry's fastest ADC (as of April 2016)
- Added bare metal capabilities for A10 Thunder ADC to give customers more software deployment options
- Announced partnerships with Cisco and Cylance

We believe our success in 2016 will serve as a springboard for accelerating the execution of our A10 Harmony vision, which helps organizations centrally manage secure application services across any combination of clouds and traditional data centers. As cloud, software and security trends evolve, A10's value to customers and footprint will continue to expand. I am pleased with the strides we have made to meaningfully grow our security portfolio and offer compelling solutions to very complex threats that our customers face.

We believe there is an opportunity to boldly stand out from competitors. We understand customer challenges. We see opportunity to help customers holistically manage traditional and cloud application environments in a distinct way compared to competitors and we deliver versatile, powerful solutions to help them do it.

Looking forward, to continue to foster our growth and create value for our customers, employees and stockholders, we plan to continue to optimize our business strategies, execute our technology roadmaps, evolve our product offerings, expand our partnerships and strengthen our channel. We believe A10 is well-positioned to take full advantage of market opportunities. With solid execution, I am confident that we will have another tremendous year.

Sincerely,

Lee Chen

Founder, CEO and President



[Please see statement regarding forward looking statements on the following page](#)

## Forward Looking Statements

This letter contains “forward-looking statements,” including statements regarding our ability to increase revenue, improve gross margins, grow our business and anticipated benefits from new platform and product introductions. Forward-looking statements are subject to known and unknown risks and uncertainties and are based on assumptions that may prove to be incorrect, which could cause actual results to differ materially from those expected or implied by the forward-looking statements. Factors which may cause actual results to differ include the continued market adoption of our products, our ability to successfully anticipate market needs and opportunities, our ability to further penetrate our existing customer base, our ability to displace existing products in established markets, our ability to expand our leadership position in next-generation application delivery and server load balancing solutions, our ability to timely and effectively scale and adapt our existing technology, the effects of increased competition in our market and our ability to compete effectively, our timely development of new products and features, any loss or delay of expected purchases by our largest end-customers, our ability to attract and retain new end-customers, continued growth in markets relating to network security, our ability to hire, retain and motivate qualified personnel, the ability of our sales team to execute well, our ability to shorten our close cycles, the ability for our channel partners to sell our products, our ability to achieve or maintain profitability while continuing to invest in our sales, marketing and research and development teams, variations in product mix or geographic locations of our sales, fluctuations in currency exchange rates, and risks associated with our significant presence in international markets. More information about potential factors that could affect the company's business and financial results is included in our annual report on Form 10-K filed with the SEC on February 23, 2017. This filing is available on the SEC's website at [www.sec.gov](http://www.sec.gov) and the company's website. All forward-looking statements in this letter are based on information available to the company as of the date hereof. We disclaim any obligation to update information contained in these forward-looking statements whether as a result of new information, future events, or otherwise.



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

**Form 10-K**

(Mark One)

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the fiscal year ended December 31, 2016  
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: 001-36343

**A10 NETWORKS, INC.**  
(Exact Name of Registrant as Specified in its Charter)

Delaware  
(State or Other Jurisdiction of Incorporation or Organization)

20-1446869  
(I.R.S. Employer Identification No.)

3 West Plumeria Drive, San Jose, California 95134  
(Address of Principal Executive Offices, including zip code)  
(408) 325-8668  
(Registrant's Telephone Number, Including Area Code)

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

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, \$.00001 Par Value	New York Stock Exchange

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

None.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K, or any amendment to this Form 10-K.

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

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

(Do not check if a smaller reporting company)

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

The aggregate market value of the registrant's common stock held by non-affiliates of the registrant as of June 30, 2016 (the last business day of the registrant's most recently completed second fiscal quarter) was approximately \$288.7 million, based upon the closing sale price of such stock on the New York Stock Exchange. For purposes of this disclosure, shares of common stock held or controlled by executive officers and directors of the registrant and by persons who hold more than 5% of the outstanding shares of common stock have been treated as shares held by affiliates. However, such treatment should not be construed as an admission that any such person is an "affiliate" of the registrant. The registrant has no non-voting common equity.

As of February 13, 2017 the number of outstanding shares of the registrant's common stock, par value \$0.00001 per share, was 68,346,582.

**DOCUMENTS INCORPORATED BY REFERENCE**

As noted herein, the information called for by Part III is incorporated by reference to specified portions of the Registrant's definitive proxy statement to be filed in conjunction with the Registrant's 2017 Annual Meeting of Stockholders, which is expected to be filed not later than 120 days after the Registrant's fiscal year ended December 31, 2016.

**A10 NETWORKS, INC.**  
**ANNUAL REPORT ON FORM 10-K**  
**FOR THE YEAR ENDED DECEMBER 31, 2016**  
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## FORWARD-LOOKING STATEMENTS

*This Annual Report on Form 10-K contains forward-looking statements made pursuant to the provisions of Section 21E of the Securities Exchange Act of 1934. These forward-looking statements are based on management's current expectations and beliefs, including estimates and projections about our industry. The following discussion and analysis contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The words "believe," "may," "will," "potentially," "estimate," "continue," "anticipate," "intend," "could," "would," "project," "plan" "expect," and similar expressions that convey uncertainty of future events or outcomes are intended to identify forward-looking statements.*

*These forward-looking statements include, but are not limited to, statements concerning the following:*

- our ability to maintain an adequate rate of revenue growth;*
- our ability to successfully anticipate market needs and opportunities;*
- our business plan and our ability to effectively manage our growth;*
- loss or delay of expected purchases by our largest end-customers;*
- our ability to attract and retain end-customers;*
- our ability to further penetrate our existing customer base;*
- our ability to displace existing products in established markets;*
- our ability to expand our leadership position in next-generation application delivery and server load balancing solutions;*
- continued growth in markets relating to network security;*
- our ability to timely and effectively scale and adapt our existing technology;*
- our ability to innovate new products and bring them to market in a timely manner;*
- our ability to expand internationally;*
- the effects of increased competition in our market and our ability to compete effectively;*
- the effects of seasonal trends on our results of operations;*
- our expectations concerning relationships with third parties;*
- the attraction and retention of qualified employees and key personnel;*
- our ability to achieve or maintain profitability while continuing to invest in our sales, marketing and research and development teams;*
- variations in product mix or geographic locations of our sales;*
- fluctuations in currency exchange rates;*
- increased cost requirements of being a public company and future sales of substantial amounts of our common stock in the public markets;*
- the cost and potential outcomes of existing and future litigation;*
- our ability to maintain, protect, and enhance our brand and intellectual property;*
- future acquisitions of or investments in complementary companies, products, services or technologies; and*
- our ability to effectively integrate operations of entities we have acquired or may acquire.*

*These forward-looking statements are subject to a number of risks, uncertainties, and assumptions, including those described in Item 1A Risk Factors and elsewhere in this Annual Report on Form 10-K. Moreover, we operate in a very competitive and rapidly changing environment, and new risks emerge from time to time. It is not possible for our management to predict all risks, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements we may make. In light of these risks, uncertainties, and assumptions, the forward-looking events and circumstances discussed in this Annual Report on Form 10-K may not occur and actual results could differ materially and adversely from those anticipated or implied in the forward-looking statements.*

*The forward-looking statements in this report speak only as of the time they are made and do not necessarily reflect our outlook at any other point in time. We undertake no obligation to update publicly any forward-looking statements, whether as a result of new information, future event, or for any other reason. However, readers should carefully review the risk factors set forth in other reports or documents we file from time to time with the Securities and Exchange Commission.*

*As used herein, "A10 Networks," the "Company," "we," "our," and similar terms include A10 Networks, Inc. and its subsidiaries, unless the context indicates otherwise.*



## PART I.

### ITEM 1. BUSINESS

#### Overview

We are a leading provider of software and hardware solutions designed to address our customers' needs for secure application services. Our solutions enable our customers to secure and optimize the performance of their data center and cloud applications and secure their users, applications and infrastructure from internet, web and network threats at scale. We deliver a broad portfolio of hardware, software, and cloud offerings to our customers. These solutions are designed to give customers the visibility, performance, and security their applications need across both on-premise and cloud environments to produce greater agility for their businesses. Our customers include cloud providers, web-scale companies, service providers, government organizations and enterprises.

#### Industry Trends & Market Drivers

Applications are critical to our customers' business operations. How safely and efficiently their applications perform dictates how their businesses perform; how they compete, how they grow and how they stand out. The applications networking industry is experiencing dynamic shifts in the way applications are developed, delivered, monetized, and protected. Our corporate positioning and strategy are aimed at addressing these evolving needs of our customers. As an industry, we are all facing key trends, such as the following:

***Increased Adoption of Cloud Applications.*** For decades, businesses operated with applications based in physical, appliance-based data centers. While these traditional applications remain central to businesses around the world, a new genre of cloud-based applications is emerging, presenting new opportunities and challenges. Some of these challenges relate to how a business effectively manages secure application services across various data centers and cloud type - whether private, public or hybrid clouds. Over time, more and more applications may be born in the cloud. Also some applications that existed in traditional data centers may migrate to clouds as well. We believe businesses will need solutions that bridge both traditional and cloud-based application environments and centrally manage all secure application services holistically. We believe the confluence of addressing visibility, performance, and security needs for businesses' critical applications presents significant risks and opportunities for many organizations.

***Increased Network Complexity and New Infrastructure Paradigms.*** For years now, our industry has deliberated and innovated new ways of creating more efficient, automated information technology ("IT") infrastructures. In the past, applications were forced to comply with the way networks were architected and innovated. Now IT vendors may increasingly build networks to conform to applications. As a result, traditional IT vendors may need to shift from hardware-centric models to software-defined approaches to improve agility for critical applications, and subsequently their business operations. Ensuring product portfolios adapt and diversify to include traditional hardware as well as newer software and cloud-based offerings are key factors determining future market leadership and competitive landscapes.

***Rapid Growth of Internet-Connected Devices and the Exhaustion of the Existing IP Address Space.*** The rapid growth of mobile and other internet-connected devices threatens to overwhelm the current Internet Protocol ("IP") addressing scheme, IPv4. This "Internet of Things" trend, combined with mobility and widespread access to the internet globally, all feed each other. To support the continuing and rapid growth of internet-connected devices, application networking technology plays a significant role in managing two internet connection standards simultaneously, extending the viability of IPv4 while enabling customers to move to IPv6. As new trends like 5G emerge in coming years, the need for IPv4 preservation and IPv6 transition may increase in importance.

***The Rise of DDoS Attacks.*** Cyber criminals such as hacktivists, amateur hackers, and foreign military and intelligence organizations target data centers of every type. Attack types continue to diversify. Distributed Denial of Service ("DDoS") attacks are prominent examples and are increasing in notoriety. They are increasing in volume, attack vectors and regularity. A DDoS attacker seeks to render a target network or website unavailable by orchestrating coordinated attacks from massive worldwide networks of compromised endpoints, called botnets. Compromised endpoints can be computing devices or Internet of Things-driven devices like video cameras. Any internet-connected device can be compromised and utilized as part of a botnet. In September 2016, a DDoS attack registered more than 600 Gbps. Days later, a new DDoS attack reached more than 1 Tbps in size, the largest volumetric attack reported publicly by that year's end. Businesses increasingly seek to rely on DDoS protection solutions to enhance protection of their business operations and brand.

***Rapid growth of SSL, encrypted applications, and hidden threats.*** Many applications use the Secure Sockets Layer ("SSL") protocol. Cyber criminals exploit the protocol to hide malicious malware within encrypted channels and carry out attacks against businesses and users. This malicious trend drives demand for greater visibility within SSL-encrypted channels. Businesses need a way to efficiently decrypt traffic. They need an effective way to inspect, identify, and remediate malicious traffic. Also they need to re-encrypt traffic and deliver it quickly to its destination. Conducting this process without placing a "security performance tax" on the application delivery is a critical requirement.

## ***Need for Advanced Secure Application Service Solutions***

In order to address these challenges, advanced and integrated solutions for managing secure application services across businesses' application environments are needed. Of the many solution requirements needed, some of the more critical include:

***Ability to Centrally Manage Traditional and Cloud Environments.*** As more applications are born in the cloud, and they operate alongside traditional applications supported by on-premise and appliance-based data centers, application delivery and security solutions will be called upon to span traditional and cloud-based environments. In doing so, solutions must centrally control and manage secure application services across any combination of traditional data centers and clouds. To support data centers and different cloud types, solutions require a variety of form factors; hardware, software (i.e. virtual, bare metal) and cloud-based offerings.

***Clear Visibility and Sophisticated Analytics.*** The effectiveness of application performance and security depends greatly on the level of visibility a business has into its application traffic. That visibility must be able to span any number of data centers and cloud types to ensure a holistic view into security threats and performance issues affecting applications. The deeper and clearer the visibility, the better the analytics and actionable information that can be applied to enhancing application performance and protection. Secure application service solutions must be driven by solid visibility and per-app analytics.

***Ability to Scale.*** Performance and security at scale are paramount in today's dynamic application environments. Solutions need to analyze application traffic quickly and enhance performance and security in traditional and cloud-based application environments in a centrally managed manner.

***Sophisticated Security Functionality.*** Secure application service solutions must detect and mitigate sophisticated cyber security threats, such as malicious threats hiding in encrypted traffic and DDoS attacks. In order to defend against the rising volume of sophisticated cyber-attacks, solutions require exceptional performance and scale without dramatically increasing footprint and total cost of ownership.

## **Our Product Portfolio**

Our portfolio seeks to address many of the aforementioned challenges and solution requirements. The portfolio consists of six advanced application delivery and security products.

- 1) Application Delivery Controllers ("ADC")
- 2) Lightning Application Delivery Service ("Lightning ADS")
- 3) Carrier Grade Network Address Translation ("CGN")
- 4) Threat Protection System ("TPS")
- 5) SSL Insight ("SSLi")
- 6) Convergent Firewall ("CFW")

They are available in a variety of form factors, such as optimized hardware appliances, bare metal software, virtual appliances, and cloud-native software. These choices make our portfolio among the most comprehensive in the industry.

The following is an overview of our portfolio:

- 1) *Application Delivery Controller.* Thunder ADC provides advanced server load balancing, including global server load balancing, high availability, aFleX scripting, aVCS, ADP virtualization delivery for multi-tenancy, SSL, acceleration, SSL intercept, caching and compression, web application firewall, domain name server application firewall and others. ADCs are typically deployed in front of a server farm within a data center, including web, application and database servers.
- 2) *Lightning Application Delivery Service.* Lightning ADS allows us to service growing demand for ADC functionality in the cloud, increasing the agility and reducing costs for our customers. Introduced after the acquisition of Appcito, Inc. ("Appcito") in 2016, Lightning ADS is a cloud-native software-as-a-service ("SaaS") platform designed to boost the delivery and security of applications and microservices across public, private and hybrid clouds, enabling "ADC-as-a-service." Central to the Lightning ADS, is the SaaS based A10 Lightning Controller, which provides central management, policy configuration, and a big data repository and analytics engine.

- 3) *Carrier Grade Networking*. Thunder CGN extends the life of increasingly scarce IPv4 address blocks and their associated infrastructure using Carrier-Grade NAT (“CGNAT” or “CGN”), and also provides migration solutions to the IPv6 addressing standard. Our CGN solution is typically deployed in service provider networks to provide standards-compliant address and protocol translation services between varying types of IP addresses. It is considered an industry-leading product and has been successfully implemented in many large service providers around the world.
- 4) *Threat Protection System*. Thunder TPS solution provides high-volume, large-scale protection for our customers’ networks and server resources against massive DDoS attacks. TPS is typically deployed at the perimeter of customer networks to protect their internal network resources from large-scale, volumetric and multi-vector attacks from distributed networks of compromised machines, commonly referred to as “botnets.” TPS is augmented by the A10 Threat Intelligence Service which can block known bad connections (i.e., IP addresses) from entering protected networks. This service is based on software we license from ThreatSTOP, Inc.
- 5) *SSL Insight*. Thunder SSLi eliminates the inherent blind spot created by SSL encryption, offloading CPU-intensive SSL decryption functions that enable security devices to inspect and remove malware within encrypted traffic. Thunder SSLi decrypts SSL-encrypted traffic and forwards it to a third-party security device, such as a firewall, for deep packet inspection (“DPI”). Once the traffic has been analyzed and scrubbed, Thunder SSLi re-encrypts the traffic and forwards it to its intended destination.
- 6) *Convergent Firewall*. Thunder CFW consolidates multiple critical security capabilities in one package by consolidating multiple security and networking functions in a single appliance. CFW helps significantly lower capital and operating expenses for our customers. Its performance and scale, all within a small form factor, delivers superior value to customers. It streamlines customer operations with a cloud-ready programmable platform. CFW includes:
  - A high-performance Secure Web Gateway with integrated explicit proxy, URL filtering and SSL visibility. It enables security policy enforcement for outbound HTTP/HTTPS client traffic.
  - A high-performance data center firewall with integrated network denial-of-service protection and server load balancing. It provides a Layer 4 stateful firewall and Layer 7 application-level gateway functionality for protecting data center applications from emerging network and DDoS threats.
  - A high-performance Gi/SGi firewall with integrated network DDoS and CGNAT. The Gi/SGi firewall protects the mobile operator infrastructures from Internet-based DDoS and other security threats.
  - A high-performance IPsec site-to-site VPN that helps businesses secure application traffic between sites and global enterprises to use public networks for securely transporting application traffic.

### ***Product Form Factors***

*Thunder Series*. ADC, CGN, TPS, SSLi, and CFW products are available on our Thunder Series family of physical appliances. The Thunder Series products support throughput ranges from 2 Gbps to 300 Gbps. The appliance family provides a variety of other security and performance options.

*vThunder* virtual appliances operate on all major hypervisor platforms, including VMware, Microsoft Hyper-V and Linux KVM. vThunder is available from cloud providers like Amazon Web Services (“AWS”), Microsoft Azure, and service providers offering our Pay-as-you-Go licensing model.

*Thunder for Bare Metal* appliances run on a variety of Intel x86-based servers, enabling a software version in which the customer chooses the dedicated hardware platform. We offer Thunder ADC and CGN for bare metal.

*Lightning* is our cloud-native SaaS platform designed to boost the delivery and security of applications and microservices across public, private and hybrid clouds. A10 Lightning’s multi-cloud management capabilities allow flexible application deployment across multiple clouds with the ability to maintain and manage diverse workloads. A10 Lightning ADS will run natively on public cloud environments, such as Amazon Web Services, Microsoft Azure and Google Cloud Platforms.

*AX Series*: Our ADC and CGN solutions are available on select older models from our AX Series line.

## ***Centralized Management***

Our aGalaxy multi-device network management solution enables a network administrator to manage multiple A10 Thunder devices for both base configurations or advanced ADC or TPS configurations. While full control of our appliances can be achieved effectively out of the box, the benefit of central and automated management increases as more appliances are added. The user interface provides a quick, at-a-glance view of status using a standard web browser. aGalaxy is designed to provide lower operational costs, as staff are freed from repetitive tasks, while also increasing precision and accuracy with centralized and automated tasks, reducing the potential for human error. aGalaxy is available as a hardware appliance or a software-only virtual machine.

## **Our Underlying Technology**

Since our inception, we have been known for providing a portfolio geared for high performance at scale. The value and significance of our high-performance offerings reside in our portfolio's underlying operating system. With the exception of Lightning ADS, our products are built on our Advanced Core Operating System ("ACOS") platform and leverage its performance optimization and security features.

Our ACOS platform is optimized for modern 64-bit central processing units ("CPUs"), which increasingly have multiple parallel processing cores that operate within a single CPU for higher efficiency and performance scalability. In order to maximize the capabilities of these increasingly dense multi-core CPUs, ACOS implements a proprietary shared memory architecture that provides all cores with simultaneous access to common memory. This shared memory architecture enables our products to utilize these multi-core CPUs efficiently and scale performance with increasing CPU cores. As a result, we believe ACOS enables us to provide our customers with products that can deliver superior price performance benefits over products that lack these capabilities.

ACOS' high-performance design enables our products to address a wide range of performance-driven networking challenges. The flexible software design of ACOS allows us to apply our portfolio to a variety of markets for a variety of needs. For example, ACOS' design is a technological backbone for defending against the rising volume of large-scale, sophisticated Distributed Denial of Service ("DDoS") attacks. In 2016, we delivered the industry's most powerful DDoS protection appliance, which provides 300 Gbps throughput. Some notable details about ACOS include:

***High Performance and Intelligent Network I/O Processing.*** In order to maximize the efficiency of high density, multi-core processors, we have developed a high performance intelligent network I/O technology that can balance application traffic flows equitably across processor cores. Our Flexible Traffic Accelerator logic can be implemented either as software running within a standard x86 processor or a Field Programmable Gate Array ("FPGA") semiconductor. Our Flexible Traffic Accelerator also performs certain hardware-based security checks for each packet and can discard suspicious traffic before it can impact system performance.

***Scalable and Efficient Memory Usage.*** To improve the performance of our multi-core processor architecture, we have developed a shared memory technology to allow all processors to share common memory and the state of the system simultaneously. As a result, we avoid the overhead associated with Inter-Processor Communication architectures deployed in first-generation approaches. We optimize memory to be visible to all cores simultaneously, while minimizing communication overhead and contention among processors for allocated memory space. All processors share a common memory pool, allowing us to dynamically allocate memory space based on application processing requirements without constraints. Because configurations, policies and network databases are efficiently stored within a shared memory architecture, we can achieve greater performance and scalability from memory and processor resources.

***Optimized Application Networking and Security.*** Once data is processed and placed into a shared memory, then a processor can begin to apply ACOS common services and function-specific logic. To ensure that every processor is utilized to perform every function and thereby achieve greater system utilization, we designed ACOS to use all processor cores symmetrically for all functions and services. The ACOS common services perform a set of key operational functions, including configuration management, network I/O, aFlex scripting, Virtual Chassis System, or aVCS, aXAPI for management integration, Application Delivery Partitions, or ADP, virtualization to enable multi-tenancy, and common resource management such as buffer, system memory, timer management and other internal system management tasks. ACOS features a modular software design, which improves reliability by ensuring that modifications made to one module will not have unwanted side effects on other system functions.

***Other noteworthy ACOS Technologies.*** ACOS incorporates a number of other technologies to provide a rich environment for developing Layer 4-7 application networking solutions, including:

***aFlex Scripting.*** aFlex scripting technology is based on industry-standard tool command language and enables customers to write custom scripts to augment the application processing.

***ADP.*** ADP enables multi-tenancy in the ACOS common services so that multiple departments of an organization or multiple customers can share a physical/virtual appliance.

***aVCS.*** aVCS enables multiple physical/virtual appliances to be managed as a single chassis.



**aXAPI.** aXAPI is an industry standard representational state transfer (“RESTful”) program interface to enable management integration for automated management.

## **Support & Services**

One of our founding principles is to provide top-notch customer support. Our global support team is part of our engineering organization and is trained across all products and solutions. Our support team takes complete ownership of customer issues from the beginning to the end to achieve rapid response and resolution. We believe that our ability to provide consistent, high-quality customer service and technical support is a key factor in attracting and retaining customers of all sizes. Accordingly, we offer a broad range of support services that include installation, phone support, repair and replacement, software updates, online tools, consulting and training services.

All customers receive standard warranty support for 90 days with purchase of A10 products. Greater than 95 percent of our customers purchase one of our maintenance offerings, which entitles them to the support provided by our global support team. We offer four maintenance options - Basic, Basic Plus, Gold and Platinum support programs (Platinum available in select countries). Maintenance contracts may be purchased with products in 12 month increments up to five years. The average maintenance contract term is approximately 18 months. We invoice our channel partners or customers directly for maintenance contracts at the time of hardware purchase. All of our maintenance contracts are non-cancellable and are generally renewed through the same channel as originally purchased. Software updates are provided to all customers with a current maintenance contract on a when-and-if-available basis. We maintain technical support centers in the United States, Japan, China, India and the Netherlands.

In October 2016, we officially launched an enhanced support offering for Thunder TPS. The enhanced Thunder TPS support offering now includes access to the A10 DDoS Security Incident Response Team (“DSIRT”). Augmenting the standard support, the offering includes access to a dedicated team of DDoS mitigation experts specializing in DDoS prevention, offering immediate assistance for mitigating attacks, and a subscription to the A10 Threat Intelligence Service, leveraging collective intelligence to block known threats.

We have a professional services team that provides a full range of fee-based consulting services, including pre-sale network assessment, comprehensive network analysis and capacity planning, post-sale migration and implementation services, on-site installation and ongoing support.

## **Customers**

Our customers operate in a variety of industries, including telecommunications, technology, industrial, government, retail, financial, gaming, and education. Since our inception, our customer base has grown rapidly. As of December 31, 2016, we had sold our products to more than 5,400 customers across 82 countries. Our customers include the top four United States wireless carriers, seven of the top 10 United States cable providers, and the top three service providers in Japan, in addition to other global enterprises, Web giants and governmental organizations. Our business is geographically diversified with 52% of our total revenue from the United States, 23% from Japan and 25% from other geographic regions for the year ended December 31, 2016. During the years ended December 31, 2016, 2015 and 2014, purchases from our ten largest end-customers accounted for approximately 35%, 33% and 37% of our total revenue, respectively.

In 2016 and 2014, one distribution channel partner accounted for 14% and 13% of our total revenue, respectively. In 2015, no customer accounted for more than 10% of our total revenue.

## **Competition**

As cloud and security trends continue to gain prominence, the business and changes in application delivery needs, cyber security threats, and the technology landscape result in evolving customer requirements to address application performance and security. These trends and the novel solutions we provide to address these demands have expanded our addressable market into DDoS protection, CGN and multiple areas of network security, where we compete with a number of companies not included among traditional ADC vendors. The agility and flexibility of the ACOS platform enables us to rapidly innovate and deploy solutions into adjacent markets to ADC. We have also enhanced our portfolio of offerings with the availability of Lightning, our cloud-native SaaS offering, and now offer a comprehensive set of hardware, software and cloud offerings to better serve our customers.

To explore our competitive landscape in more detail, it is important to understand that the ADC, CGN, and networking security markets are characterized by a set of identifiable participants. We do not consider any of these markets to include a single dominant company, nor do we consider the markets to be fragmented. Our strategy is to compete across our entire portfolio and provide a multi-dimensional value proposition to our customers. We believe that our main competitors fall into the following categories:

- Companies that sell products in the traditional ADC market which includes companies that are established in this market, such as F5 Networks, Inc. (“F5 Networks”) and Citrix Systems, Inc. (“Citrix Systems”).

- Companies that sell open source, software-only, cloud-based ADC services, which include many startups. These companies include Avi Networks Inc. (“Avi Networks”), NGINX Inc. (“NGiNX”), and HAProxy Technologies, Inc. (“HAProxy”).
- Companies that sell CGN products, which were originally designed for other networking purposes, such as edge routers and security appliances from vendors like Alcatel-Lucent USA Inc. (“Alcatel-Lucent”), Cisco Systems, Inc. (“Cisco Systems”) and Juniper Networks, Inc. (“Juniper Networks”).
- Companies that sell traditional DDoS protection products, such as Arbor Networks, Inc., a subsidiary of NetScout Systems, (“Arbor Networks”) and Radware, Ltd. (“Radware”).
- Companies that sell SSL decryption and inspection products, such as Symantec Corporation (through its acquisition of Blue Coat Systems Inc. in 2016) and F5 Networks.
- Companies that sell certain network security products, including Secure Web Gateways, SSL Insight/SSL Intercept, data center firewalls and Gi/SGi firewalls.

Going forward, we believe that key competitive factors in our markets include:

- Ability to innovate and respond to customer needs rapidly
- Ability to address on-premise and cloud application environments in a secure, centrally managed manner
- Ability to accommodate any IT delivery model or combination of models, regardless of form factor
- Breadth and depth of product features and functionality
- Level of customer satisfaction
- Price, performance, and efficiency
- Ability for products to scale with high-speed network traffic
- Flexible and agile design of products
- Ability to detect and mitigate large-scale cyber security threats
- Brand awareness and reputation
- Strength of sales and marketing
- Ability to attract and retain talented employees

## **Sales and Marketing**

### ***Sales***

Our high-touch salesforce engages customers directly and through distribution channels. We believe that a high-touch, customer-focused selling process is important before, during and after the sale of our products to maximize our customers’ and our own success. Depending on size, geography, and complexity, some customer sales are originated and completed by our OEM and distribution channel partners with little or no direct engagement with our sales personnel. We fulfill nearly all orders globally through our distribution channel partners, which include distributors, value added resellers and system integrators.

Revenue fulfilled through our distribution channel partners accounted for 85%, 81% and 85% of our total revenue for the years ended December 31, 2016, 2015 and 2014, respectively. We also work closely with OEM partners. We believe that our high-touch sales organization is unique given our deep focus on technology competence and partnership with our end-customers’ network engineers and architects. We believe this sales approach allows us to leverage the benefits of the channel, such as expanding our market coverage, as well as maintain face-to-face relationships with our end-customers.

Our sales team is comprised of inside sales and field sales personnel who are organized by geography and maintain sales presence in 30 countries, including in the following countries and regions: United States, Western Europe, the Middle East, Japan, China, Taiwan, South Korea, Southeast Asia and Latin America. Our sales organization also includes sales engineers with deep technical domain expertise who are responsible for pre-sales technical support, solutions engineering for our end-customers, proof of concept work and technical training for our distribution channel partners. Our sales team is also comprised of a channel sales organization that is expanding

our market reach through partners. We expect to continue to grow our sales headcount, including in geographies where we currently do not have a sales presence.

## **Marketing**

Our strategy is focused on continuously modernizing our marketing practices to successfully increase awareness of our brand, drive greater demand for our products and services, and enable sales to win as that demand broadens. Our marketing efforts focus on positioning us as the only vendor who can centrally manage secure application services across traditional data center and cloud-based application environments. Our demand generation campaigns utilize the entire marketing mix on a global scale. In addition to our organic marketing efforts, we create additional awareness and demand via joint marketing campaigns with channel partners and strategic alliance partners worldwide. We are also actively engaged in driving global thought leadership via market research, industry analyst engagement, financial analyst engagement, media outreach, blogs, social media, events and speakerships, and other marcom strategies. Everything we do is based on the fundamental principles of integrated marketing: creating longitudinal campaign-based programs that combine the power of brand awareness, demand generation, and sales enablement into one well-oiled global machine.

## **Manufacturing**

We outsource the manufacturing of our hardware products to original design manufacturers. This approach allows us to benefit from the scale and experience of our manufacturing partners to reduce our costs, overhead and inventory while allowing us to adjust more quickly to changing customer demand. Our manufacturers are Lanner Electronics Inc. (“Lanner”) and AEWIN Technologies Co., Ltd. (“AEWIN”). These companies manufacture and assemble our hardware products using design specifications, quality assurance programs and standards that we establish. Our manufacturers procure components and assemble our products based on our demand forecasts and purchase orders. These forecasts represent our estimates of future demand for our products based upon historical trends and analysis from our sales and product management functions as adjusted for overall market conditions. The component parts incorporated into our products are sourced either by our manufacturing partners or directly by us.

We have agreements with both Lanner and AEWIN pursuant to which they manufacture, assemble, and test our products. The Lanner agreement has an initial one-year term, and the AEWIN agreement has an initial term of six years. Each agreement automatically renews for successive one-year terms unless either party gives notice that they do not want to renew. We do not have any long-term manufacturing contracts that guarantee us any fixed capacity or pricing. We perform quality assurance and testing at our San Jose, Taiwan and Japan distribution centers, as well as at our manufacturers’ locations. We warehouse and deliver our products out of our San Jose warehouse for the Americas. We also outsource warehousing and delivery to a third-party logistics provider in some regions.

## **Research and Development**

Our research and development effort is focused on developing new products and enhancing our existing products. Our engineering team works closely with customers and technology partners to identify future needs. A majority of our research and development team is focused on software development, with substantial experience in networking, network management, application delivery, performance optimization, security, software quality engineering and automation.

We believe that innovation and timely development of new features and products is essential to meeting the needs of our end-customer and improving our competitive position. We supplement our own research and development effort with open source technologies and technologies that we license from third parties. We test our products thoroughly to certify and ensure interoperability with third-party hardware and software products.

Our engineering teams are located mainly in our headquarters in San Jose, California, Beijing, China, Bangalore, India and Taipei, Taiwan. For the years ended December 31, 2016, 2015 and 2014, our research and development expenses were \$60.7 million, \$54.8 million and \$49.9 million, representing 26%, 28% and 28% of our total revenue, respectively.

## **Backlog**

As of December 31, 2016 and 2015, we had product backlog of approximately \$19.5 million and \$10.5 million. Backlog represents orders confirmed with a purchase order for products to be shipped generally within 90 days to customers with approved credit status. Orders are subject to cancellation, rescheduling by customers and product specification changes by customers. Although we believe that the backlog orders are firm, purchase orders may be canceled by the customer prior to shipment without significant penalty. For this reason, we believe that our product backlog at any given date is not a reliable indicator of future revenues.

For the years ended December 31, 2016, 2015 and 2014, our total revenue was \$230.0 million, \$199.0 million and \$179.5 million, respectively, representing growth of 28% from 2014 to 2016. Our total revenue grew 11% in 2015 as compared to 2014 and grew 16% in 2016 as compared to 2015. For the years ended December 31, 2016, 2015 and 2014, our gross margin was 76.1%, 75.5% and 76.1%,

respectively. We had net losses of \$20.9 million, \$40.0 million and \$34.7 million for the years ended December 31, 2016, 2015 and 2014, respectively.

## **Intellectual Property**

We rely on a combination of patent, copyright, trademark and trade secret laws, and restrictions on disclosure to protect our intellectual property rights. As of December 31, 2016, we had 81 United States (“U.S.”) patents issued and 67 U.S. patent applications pending, and 40 overseas patents issued and 44 overseas patent applications pending. Our issued U.S. patents, excluding 22 patents that we acquired, expire between 2026 and 2036. Our future success depends in part on our ability to protect our proprietary rights to the technologies used in our principal products. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy aspects of our products or to obtain and use trade secrets or other information that we regard as proprietary. In addition, the laws of some foreign countries do not protect our proprietary rights as fully as do the laws of the United States. Any issued patent may not preserve our proprietary position, and competitors or others may develop technologies similar to or superior to our technology. Our failure to enforce and protect our intellectual property rights could harm our business, operating results and financial condition.

We license software from third parties for development of or integration into our products, including proprietary and open source software. We pursue registration of our trademarks and domain names in the United States and other jurisdictions. See Part-I, *Item 1A. Risk Factors* included in this Annual Report on Form 10-K for additional information regarding the risks associated with protecting our intellectual property.

## **Employees**

As of December 31, 2016, we had 837 full-time employees, including 410 engaged in research and development and customer support, 348 in sales and marketing and 79 in general and administrative and other activities. None of our employees is represented by a labor union or is a party to any collective bargaining arrangement in connection with his or her employment with us. We have never experienced any work stoppages, and we consider our relations with our employees to be good.

## **Appcito Acquisition**

On June 23, 2016, we entered into an asset purchase agreement with Appcito, a privately held company engaged in providing a unified set of services for applications deployed on cloud infrastructure with facilities located in Santa Clara, California and Bangalore, India. Under the terms of the purchase agreement, we acquired substantially all of the assets of Appcito. This acquisition enhances our position as a comprehensive secure application services leader, and it represents a strategic step in our vision to help our customers become more secure and agile as they bridge traditional data center and cloud application environments. This acquisition has led to the launch of the cloud-native Lightning ADS. We expect to introduce additional options spanning public and private clouds.

## **Corporate Information**

A10 Networks, Inc. was incorporated in the State of California in 2004 and subsequently reincorporated in the State of Delaware in March 2014. Our website is located at [www.A10networks.com](http://www.A10networks.com), and our investor relations website is located at <http://investors.A10networks.com>. The following filings are available through our investor relations website after we file them with the SEC: Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, as well as any amendments to such reports and all other filings pursuant to Section 13(a) or 15(d) of the Securities Act. These filings are also available for download free of charge on our investor relations website. Additionally, copies of materials filed by us with the SEC may be accessed at the SEC’s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549 or at [www.sec.gov](http://www.sec.gov). For information about the SEC’s Public Reference Room, contact 1-800-SEC-0330.

We announce material information to the public about A10, our products and services and other matters through a variety of means, including our website ([www.A10networks.com](http://www.A10networks.com)), the investor relations section of our website ([www.investors.A10networks.com](http://investors.A10networks.com)), press releases, filings with the Securities and Exchange Commission, public conference calls, and social media, including our corporate Twitter account (@A10Networks) and our corporate Facebook page (<https://www.facebook.com/a10networks>). The contents of our website and social media contents are not intended to be incorporated by reference into this Annual Report on Form 10-K or in any other report or document we file with the Securities and Exchange Commission, or SEC, and any references to our websites are intended to be inactive textual references only. We encourage investors and others to review the information we make public in these locations, as such information could be deemed to be material information. Please note that this list may be updated from time to time.



## ITEM 1A. RISK FACTORS

*Investing in our common stock involves a high degree of risk. You should carefully consider the risks and uncertainties described below, together with all of the other information contained in this report, and in our other public filings. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties that we are unaware of, or that we currently believe are not material, may also become important factors that affect us. If any of the following risks occur, our business, financial condition, operating results, and prospects could be materially harmed. In that event, the trading price of our common stock could decline, perhaps significantly.*

***If we do not successfully anticipate market needs and opportunities or if the market does not continue to adopt our application networking products, our business, financial condition and results of operations could be significantly harmed.***

The application networking market is rapidly evolving and difficult to predict. Technologies, customer requirements, security threats and industry standards are constantly changing. As a result, we must anticipate future market needs and opportunities and then develop new products or enhancements to our current products that are designed to address those needs and opportunities, and we may not be successful in doing so.

Even if we are able to anticipate, develop and commercially introduce new products and enhancements that address the market's needs and opportunities, there can be no assurance that new products or enhancements will achieve widespread market acceptance. For example, organizations that use other conventional or first-generation application networking products for their needs may believe that these products are sufficient. In addition, as we launch new product offerings, organizations may not believe that such new product offerings offer any additional benefits as compared to the existing application networking products that they currently use. Accordingly, organizations may continue allocating their IT budgets for existing application networking products and may not adopt our products, regardless of whether our products can offer superior performance or security.

If we fail to anticipate market needs and opportunities or if the market does not continue to adopt our application networking products, then market acceptance and sales of our current and future application networking products could be substantially decreased or delayed, we could lose customers, and our revenue may not grow or may decline. Any of such events would significantly harm our business, financial condition and results of operations.

***Our success depends on our timely development of new products and features to address rapid technological changes and evolving customer requirements. If we are unable to timely develop and successfully introduce new products and features that adequately address these changes and requirements, our business and operating results could be adversely affected.***

Changes in application software technologies, data center and communications hardware, networking software and operating systems, and industry standards, as well as our end-customers' continuing business growth, result in evolving application networking needs and requirements. Our continued success depends on our ability to identify, develop and introduce in a timely and successful manner new products and new features for our existing products that meet these needs and requirements.

Our future plans include significant investments in research and development and related product opportunities. Developing our products and related enhancements is time-consuming and expensive. We have made significant investments in our research and development team in order to address these product development needs. Our investments in research and development may not result in significant design and performance improvements or marketable products or features, or may result in products that are more expensive than anticipated. We may take longer to generate revenue, or generate less revenue, than we anticipate from our new products and product enhancements. We believe that we must continue to dedicate a significant amount of resources to our research and development efforts to maintain our competitive position.

If we are unable to develop new products and features to address technological changes and new customer requirements in the application networking market or if our investments in research and development do not yield the expected benefits in a timely manner, our business and operating results could be adversely affected.

***We have experienced net losses in recent periods, anticipate increasing our operating expenses in the future and may not achieve or maintain profitability in the future. If we cannot achieve or maintain profitability, our financial performance will be harmed and our business may suffer.***

We experienced net losses for the years ended December 31, 2016, 2015 and 2014. Although we experienced revenue growth over these same periods and had achieved profitability in prior year periods, we may not be able to sustain or increase our revenue growth or achieve profitability in the future or on a consistent basis. During 2016, 2015 and 2014, we have invested in our sales, marketing and research and development teams in order to develop, market and sell our products. We expect to continue to invest significantly in these areas in the future. As a result of these increased expenditures, we will have to generate and sustain increased revenue, manage our cost structure and avoid significant liabilities to achieve future profitability.

Revenue growth may slow or decline, and we may incur significant losses in the future for a number of possible reasons, including our inability to develop products that achieve market acceptance, general economic conditions, increasing competition, decreased growth in the markets in which we operate, or our failure for any reason to capitalize on growth opportunities. Additionally, we may encounter unforeseen operating expenses, difficulties, complications, delays and other unknown factors that may result in losses in future periods. If these losses exceed our expectations or our revenue growth expectations are not met in future periods, our financial performance will be harmed and our stock price could be volatile or decline.

***Our operating results have varied and are likely to continue to vary significantly from period to period and may be unpredictable, which could cause the trading price of our common stock to decline.***

Our operating results, in particular, revenue, margins and operating expenses, have fluctuated in the past, and we expect this will continue, which makes it difficult for us to predict our future operating results. The timing and size of sales of our products are highly variable and difficult to predict and can result in significant fluctuations in our revenue from period to period. This is particularly true of sales to our largest end-customers, such as service providers, Web giants and governmental organizations, who typically make large and concentrated purchases and for whom close or sales cycles can be long, as a result of their complex networks and data centers, as well as requests that may be made for customized features. Our quarterly results may vary significantly based on when these large end-customers place orders with us and the content of their orders.

Our operating results may also fluctuate due to a number of other factors, many of which are outside of our control and may be difficult to predict. In addition to other risks listed in this “Risk Factors” section, factors that may affect our operating results include:

- fluctuations in and timing of purchases from, or loss of, large customers;
- the budgeting cycles and purchasing practices of end-customers;
- our ability to attract and retain new end-customers;
- changes in demand for our products and services, including seasonal variations in customer spending patterns or cyclical fluctuations in our markets;
- our reliance on shipments at the end of our quarters;
- variations in product mix or geographic locations of our sales, which can affect the revenue we realize for those sales;
- the timing and success of new product and service introductions by us or our competitors;
- our ability to increase the size of our distribution channel and to maintain relationships with important distribution channel partners;
- our ability to improve our overall sales productivity, and successfully execute our marketing strategies;
- the effect of currency exchange rates on our revenue and expenses;
- the cost and potential outcomes of existing and future litigation;
- the effect of discounts negotiated by our largest end-customers for sales or pricing pressure from our competitors;
- changes in the growth rate of the application networking market or changes in market needs;
- inventory write downs, which may be necessary for our older products when our new products are launched and adopted by our end-customers; and
- our third-party manufacturers’ and component suppliers’ capacity to meet our product demand forecasts on a timely basis, or at all.

Any one of the factors above or the cumulative effect of some of these factors may result in significant fluctuations in our financial and other operating results. This variability and unpredictability could result in our failure to meet our or our investors’ or securities analysts’ revenue, margin or other operating results expectations for a particular period, resulting in a decline in the trading price of our common stock.

***Reliance on shipments at the end of the quarter could cause our revenue for the applicable period to fall below expected levels.***

As a result of end-customer buying patterns and the efforts of our sales force and distribution channel partners to meet or exceed their sales objectives, we have historically received a substantial portion of purchase orders and generated a substantial portion of revenue during the last few weeks of each quarter. We can recognize such revenue in the quarter received, however,

only if all of the requirements of revenue recognition, especially shipment, are met by the end of the quarter. In addition, any significant interruption in our information technology systems, which manage critical functions such as order processing, revenue recognition, financial forecasts, inventory and supply chain management, could result in delayed order fulfillment and thus decreased revenue for that quarter. If expected revenue at the end of any quarter is delayed for any reason, including the failure of anticipated purchase orders to materialize (including delays by our customers or potential customers in consummating such purchase orders), our third-party manufacturers' inability to manufacture and ship products prior to quarter-end to fulfill purchase orders received near the end of the quarter, our failure to manage inventory to meet demand, our inability to release new products on schedule, any failure of our systems related to order review and processing, or any delays in shipments or achieving specified acceptance criteria, our revenue for that quarter could fall below our, or our investors' or securities analysts' expectations, resulting in a decline in the trading price of our common stock. We have experienced such delays in revenue in the past, including the quarter ended September 30, 2016.

***We face intense competition in our market, especially from larger, well-established companies, and we may lack sufficient financial or other resources to maintain or improve our competitive position.***

The application networking market is intensely competitive, and we expect competition to increase in the future. To the extent that we sell our solutions in adjacent markets, we expect to face intense competition in those markets as well. We believe that our main competitors fall into the following categories:

- Companies that sell products in the traditional ADC market which includes companies that are established in this market, such as F5 Networks and Citrix Systems
- Companies that sell open source, software-only, cloud-based ADC services, which include many startups. These companies include Avi Networks, NGiNX, and HAProxy
- Companies that sell CGN products, which were originally designed for other networking purposes, such as edge routers and security appliances from vendors like Alcatel-Lucent, Cisco Systems, and Juniper Networks
- Companies that sell traditional DDoS protection products, such as Arbor Networks and Radware
- Companies that sell SSL decryption and inspection products, such as Symantec Corporation (through its acquisition of Blue Coat Systems Inc. in 2016) and F5 Networks and
- Companies that sell certain network security products, including Secure Web Gateways, SSL Insight/SSL Intercept, data center firewalls and Gi/SGi firewalls.

Many of our competitors are substantially larger and have greater financial, technical, research and development, sales and marketing, manufacturing, distribution and other resources and greater name recognition. In addition, some of our larger competitors have broader products offerings and could leverage their customer relationships based on their other products. Potential customers who have purchased products from our competitors in the past may also prefer to continue to purchase from these competitors rather than change to a new supplier regardless of the performance, price or features of the respective products. We could also face competition from new market entrants, which may include our current technology partners. As we continue to expand globally, we may also see new competitors in different geographic regions. Such current and potential competitors may also establish cooperative relationships among themselves or with third parties that may further enhance their resources.

Many of our existing and potential competitors enjoy substantial competitive advantages, such as:

- longer operating histories;
- the capacity to leverage their sales efforts and marketing expenditures across a broader portfolio of products and services at a greater range of prices;
- the ability to incorporate functionality into existing products to gain business in a manner that discourages users from purchasing our products, including through selling at zero or negative margins, product bundling or closed technology platforms;
- broader distribution and established relationships with distribution channel partners in a greater number of worldwide locations;
- access to larger end-customer bases;
- the ability to use their greater financial resources to attract our research and development engineers as well as other employees of ours;
- larger intellectual property portfolios; and
- the ability to bundle competitive offerings with other products and services.

Our ability to compete will depend upon our ability to provide a better solution than our competitors at a competitive price. We may be required to make substantial additional investments in research and development, marketing and sales in order to respond to competition, and there is no assurance that these investments will achieve any returns for us or that we will be able to compete successfully in the future. We also expect increased competition if our market continues to expand. Moreover, conditions in our market could change rapidly and significantly as a result of technological advancements or other factors.

In addition, current or potential competitors may be acquired by third parties that have greater resources available. As a result of these acquisitions, our current or potential competitors might take advantage of the greater resources of the larger organization to compete more vigorously or broadly with us. In addition, continued industry consolidation might adversely impact end-customers' perceptions of the viability of smaller and even medium-sized networking companies and, consequently, end-customers' willingness to purchase from companies like us.

As a result, increased competition could lead to fewer end-customer orders, price reductions, reduced margins and loss of market share.

***If we are unable to attract new end-customers, sell additional products to our existing end-customers or achieve the anticipated benefits from our investment in additional sales personnel and resources, our revenue may decline, and our gross margin will be adversely affected.***

To maintain and increase our revenue, we must continually add new end-customers and sell additional products to existing end-customers. The rate at which new and existing end-customers purchase solutions depends on a number of factors, including some outside of our control, such as general economic conditions. If our efforts to sell our solutions to new end-customers and additional solutions to our existing end-customers are not successful, our business and operating results will suffer.

In recent periods, we have been adding personnel and other resources to our sales and marketing functions, as we focus on growing our business, entering new markets and increasing our market share. We expect to incur significant additional expenses by hiring additional sales personnel and expanding our international operations in order to seek revenue growth. The return on these and future investments may be lower, or may be realized more slowly, than we expect, if realized at all. If we do not achieve the benefits anticipated from these investments, or if the achievement of these benefits is delayed, our growth rates will decline, and our gross margin would likely be adversely affected.

***If we are not able to maintain and enhance our brand and reputation, our business and operating results may be harmed in tangible or intangible ways.***

We believe that maintaining and enhancing our brand and reputation are critical to our relationships with, and our ability to attract, new end-customers, technology partners and employees. The successful promotion of our brand will depend largely upon our ability to continue to develop, offer and maintain high-quality products and services, our marketing and public relations efforts, and our ability to differentiate our products and services successfully from those of our competitors. Our brand promotion activities may not be successful and may not yield increased revenue. In addition, extension of our brand to products and uses different from our traditional products and services may dilute our brand, particularly if we fail to maintain the quality of products and services in these new areas. We have in the past, and may in the future, become involved in litigation that could negatively affect our brand. If we do not successfully maintain and enhance our brand and reputation, our growth rate may decline, we may have reduced pricing power relative to competitors with stronger brands or reputations, and we could lose end-customers or technology partners, all of which would harm our business, operating results and financial condition.

***A limited number of our end-customers, including service providers, make large and concentrated purchases that comprise a significant portion of our revenue. Any loss or delay of expected purchases by our largest end-customers could adversely affect our operating results.***

As a result of the nature of our target market and the current stage of our development, a substantial portion of our revenue in any period comes from a limited number of large end-customers, including service providers. During the years ended December 31, 2016, 2015 and 2014, purchases from our ten largest end-customers accounted for approximately 35%, 33% and 37% of our total revenue. The composition of the group of these ten largest end-customers changes from period to period, but often includes service providers, who accounted for approximately 41%, 45%, and 46% of our total revenue during the years ended December 31, 2016, 2015 and 2014.

Sales to these large end-customers have typically been characterized by large but irregular purchases with long initial sales cycles. After initial deployment, subsequent purchases of our products typically have a more compressed sales cycle. The timing of these purchases and of the requested delivery of the purchased product is difficult to predict. As a consequence, any acceleration or delay in anticipated product purchases by or requested deliveries to our largest end-customers could materially affect our revenue and operating results in any quarter and cause our quarterly revenue and operating results to fluctuate from quarter to quarter.



We cannot provide any assurance that we will be able to sustain or increase our revenue from our largest end-customers nor that we will be able to offset any absence of significant purchases by our largest end-customers in any particular period with purchases by new or existing end-customers in that or a subsequent period. We expect that sales of our products to a limited number of end-customers will continue to contribute materially to our revenue for the foreseeable future. The loss of, or a significant delay or reduction in purchases by, a small number of end-customers could have a material adverse effect on our consolidated financial position, results of operations or cash flows.

***Some of our large end-customers demand favorable terms and conditions from their vendors and may request price or other concessions from us. As we seek to sell more products to these end-customers, we may agree to terms and conditions that may have an adverse effect on our business.***

Some of our large end-customers have significant purchasing power and, accordingly, may request from us and received more favorable terms and conditions, including lower prices than we typically provide. As we seek to sell products to this class of end-customer, we may agree to these terms and conditions, which may include terms that reduce our gross margin and have an adverse effect on our business.

***Our gross margin may fluctuate from period to period based on the mix of products sold, the geographic location of our customers, price discounts offered, required inventory write downs and current exchange rate fluctuations.***

Our gross margin may fluctuate from period to period in response to a number of factors, such as the mix of our products sold and the geographic locations of our sales. Our products tend to have varying gross margins in different geographic regions. We also may offer pricing discounts from time to time as part of a targeted sales campaign or as a result of pricing pressure from our competitors. In addition, our larger end-customers may negotiate pricing discounts in connection with large orders they place with us. The sale of our products at discounted prices could have a negative impact on our gross margin. We also must manage our inventory of existing products when we introduce new products.

If we are unable to sell the remaining inventory of our older products prior to or following the launch of such new product offerings, we may be forced to write down inventory for such older products, which could also negatively affect our gross margin. Our gross margin may also vary based on international currency exchange rates. In general, our sales are denominated in U.S. dollars; however, in Japan they are denominated in Japanese yen. Changes in the exchange rate between the U.S. dollar and the Japanese yen may therefore affect our actual revenue and gross margin.

***We have been, may presently be, or in the future may be, a party to litigation and claims regarding intellectual property rights, resolution of which has been and may in the future be time-consuming, expensive and adverse to us, as well as require a significant amount of resources to prosecute, defend, or make our products non-infringing.***

Our industry is characterized by the existence of a large number of patents and by increasingly frequent claims and related litigation based on allegations of infringement or other violations of patent and other intellectual property rights. In the ordinary course of our business, we have been and may presently be in disputes and licensing discussions with others regarding their patents and other claimed intellectual property and proprietary rights. Intellectual property infringement and misappropriation lawsuits and other claims are subject to inherent uncertainties due to the complexity of the technical and legal issues involved, and we cannot be certain that we will be successful in defending ourselves against such claims or in concluding licenses on reasonable terms or at all.

We may have fewer issued patents than some of our major competitors, and therefore may not be able to utilize our patent portfolio effectively to assert defenses or counterclaims in response to patent infringement claims or litigation brought against us by third parties. Further, litigation may involve patent holding companies or other adverse patent owners that have no relevant products revenue and against which our potential patents may provide little or no deterrence. In addition, many potential litigants have the capability to dedicate substantially greater resources than we can to enforce their intellectual property rights and to defend claims that may be brought against them. We expect that infringement claims may increase as the number of product types and the number of competitors in our market increases. Also, to the extent we gain greater visibility, market exposure and competitive success, we face a higher risk of being the subject of intellectual property infringement claims.

If we are found in the future to infringe the proprietary rights of others, or if we otherwise settle such claims, we could be compelled to pay damages or royalties and either obtain a license to those intellectual property rights or alter our products such that they no longer infringe. Any license could be very expensive to obtain or may not be available at all. Similarly, changing our products or processes to avoid infringing the rights of others may be costly, time-consuming or impractical. Alternatively, we could also become subject to an injunction or other court order that could prevent us from offering our products. Any of these claims, regardless of their merit, may be time-consuming, result in costly litigation and diversion of technical and management personnel, or require us to cease using infringing technology, develop non-infringing technology or enter into royalty or licensing agreements.

Many of our commercial agreements require us to indemnify our end-customers, distributors and resellers for certain third-party intellectual property infringement actions related to our technology, which may require us to defend or otherwise become involved in such infringement claims, and we could incur liabilities in excess of the amounts we have received for the relevant products and/or services from our end-customers, distributors or resellers. These types of claims could harm our relationships with our end-customers, distributors and resellers, may deter future end-customers from purchasing our products or could expose us to litigation for these claims. Even if we are not a party to any litigation between an end-customer, distributor or reseller, on the one hand, and a third party, on the other hand, an adverse outcome in any such litigation could make it more difficult for us to defend our intellectual property rights in any subsequent litigation in which we are a named party.

***We may not be able to adequately protect our intellectual property, and if we are unable to do so, our competitive position could be harmed, or we could be required to incur significant expenses to enforce our rights.***

We rely on a combination of patent, copyright, trademark and trade secret laws, and contractual restrictions on disclosure of confidential and proprietary information, to protect our intellectual property. Despite the efforts we take to protect our intellectual property and other proprietary rights, these efforts may not be sufficient or effective at preventing their unauthorized use. In addition, effective trademark, patent, copyright and trade secret protection may not be available or cost-effective in every country in which we have rights. There may be instances where we are not able to protect intellectual property or other proprietary rights in a manner that maximizes competitive advantage. If we are unable to protect our intellectual property and other proprietary rights from unauthorized use, the value of those assets may be reduced, which could negatively impact our business.

We also rely in part on confidentiality and/or assignment agreements with our technology partners, employees, consultants, advisors and others. These protections and agreements may not effectively prevent disclosure of our confidential information and may not provide an adequate remedy in the event of unauthorized disclosure. In addition, others may independently discover our trade secrets and intellectual property information we thought to be proprietary, and in these cases we would not be able to assert any trade secret rights against those parties. Despite our efforts to protect our intellectual property, unauthorized parties may attempt to copy or otherwise obtain and use our intellectual property or technology. Monitoring unauthorized use of our intellectual property is difficult and expensive. We have not made such monitoring a priority to date and will not likely make this a priority in the future. We cannot be certain that the steps we have taken or will take will prevent misappropriation of our technology, particularly in foreign countries where the laws may not protect our proprietary rights as fully as in the United States.

If we fail to protect our intellectual property adequately, our competitors might gain access to our technology, and our business might be harmed. In addition, even if we protect our intellectual property, we may need to license it to competitors, which could also be harmful. For example, we have already licensed all of our issued patents, pending applications, and future patents and patent applications that we may acquire, obtain, apply for or have a right to license to Brocade until May 2025, for the life of each such patent. In addition, we might incur significant expenses in defending our intellectual property rights. Any of our patents, copyrights, trademarks or other intellectual property rights could be challenged by others or invalidated through administrative process or litigation.

We may in the future initiate claims or litigation against third parties for infringement of our proprietary rights or to establish the validity of our proprietary rights. Any litigation, whether or not resolved in our favor, could result in significant expense to us and divert the efforts of our management and technical personnel, as well as cause other claims to be made against us, which might adversely affect our business, operating results and financial condition.

***We generate a significant amount of revenue from sales to distributors, resellers, and end-customers outside of the United States, and we are therefore subject to a number of risks that could adversely affect these international sources of our revenue.***

A significant portion of our revenue is generated in international markets, including Japan, Western Europe, China, Taiwan and South Korea. During the years ended December 31, 2016, 2015 and 2014, approximately 48%, 46% and 52% of our total revenue was generated from customers located outside of the United States. If we are unable to maintain or continue to grow our revenue in these markets, our financial results may suffer.

As a result, we must hire and train experienced personnel to staff and manage our foreign operations. To the extent that we experience difficulties in recruiting, training, managing and retaining an international staff, and specifically sales management and sales personnel, we may experience difficulties in sales productivity in foreign markets. We also seek to enter into distributor and reseller relationships with companies in certain international markets where we do not have a local presence. If we are not able to maintain successful distributor relationships internationally or recruit additional companies to enter into distributor relationships, our future success in these international markets could be limited. Business practices in the international markets that we serve may differ from those in the United States and may require us in the future to include terms in customer contracts other than our standard terms. To the extent that we may enter into customer contracts in the future that include non-standard terms, our operating results may be adversely impacted.

***We have a significant presence in international markets and plan to continue to expand our international operations, which exposes us to a number of risks that could affect our future growth.***

Our sales team is comprised of field sales and inside sales personnel who are organized by geography and maintain sales presence in 30 countries, including in the following countries and regions: United States, Western Europe, the Middle East, Japan, China, Taiwan, South Korea, Southeast Asia and Latin America. We expect to continue to increase our sales headcount in all markets, particularly in markets where we currently do not have a sales presence. As we continue to expand our international sales and operations, we are subject to a number of risks, including the following:

- greater difficulty in enforcing contracts and accounts receivable collection and longer collection periods;
- increased expenses incurred in establishing and maintaining office space and equipment for our international operations;
- greater difficulty in recruiting local experienced personnel, and the costs and expenses associated with such activities;
- general economic and political conditions in these foreign markets;
- economic uncertainty around the world, including continued economic uncertainty as a result of sovereign debt issues in Europe and the United Kingdom's decision to exit the European Union (commonly referred to as "Brexit");
- management communication and integration problems resulting from cultural and geographic dispersion;
- risks associated with trade restrictions and foreign legal requirements, including the importation, certification, and localization of our products required in foreign countries;
- greater risk of unexpected changes in regulatory practices, tariffs, and tax laws and treaties;
- the uncertainty of protection for intellectual property rights in some countries;
- greater risk of a failure of foreign employees to comply with both U.S. and foreign laws, including antitrust regulations, the U.S. Foreign Corrupt Practices Act ("FCPA"), and any trade regulations ensuring fair trade practices; and
- heightened risk of unfair or corrupt business practices in certain geographies and of improper or fraudulent sales arrangements that may impact financial results and result in restatements of, or irregularities in, financial statements.

Because of our worldwide operations, we are also subject to risks associated with compliance with applicable anticorruption laws. One such applicable anticorruption law is the FCPA, which generally prohibits U.S. companies and their employees and intermediaries from making payments to foreign officials for the purpose of obtaining or keeping business, securing an advantage, or directing business to another, and requires public companies to maintain accurate books and records and a system of internal accounting controls. Under the FCPA, U.S. companies may be held liable for actions taken by directors, officers, employees, agents, or other strategic or local partners or representatives. As such, if we or our intermediaries, such as channel partners and distributors, fail to comply with the requirements of the FCPA or similar legislation, governmental authorities in the United States and elsewhere could seek to impose civil and/or criminal fines and penalties which could have a material adverse effect on our business, operating results and financial condition.

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

Our consolidated results of operations, financial position and cash flows are subject to fluctuations due to changes in foreign currency exchange rates. Historically, the majority of our revenue contracts are denominated in U.S. dollars, with the most significant exception being Japan, where we invoice primarily in the Japanese yen. Our expenses are generally denominated in the currencies in which our operations are located, which is primarily in North America and Japan. Revenue resulting from selling in local currencies and costs incurred in local currencies are exposed to foreign currency exchange rate fluctuations that can affect our operating income. The unfavorable currency exchange impact of the foreign exchange rates on our net loss was \$2.4 million and \$1.6 million for the three and twelve months ended December 31, 2016, respectively. As exchange rates vary, our operating income may differ from expectations. To the extent our foreign currency exposures become more material, we may elect to deploy normal and customary hedging practices designed to more proactively mitigate such exposure. The use of such hedging activities may not offset any, or more than a portion, of the adverse financial effects of unfavorable movements in currency exchange rates over the limited time the hedges are in place and would not protect us from long term shifts in currency exchange rates.

***Our success depends on our key personnel and our ability to hire, retain and motivate qualified product development, sales, marketing and finance personnel.***

Our success depends to a significant degree upon the continued contributions of our key management, product development, sales, marketing and finance personnel, many of whom may be difficult to replace. The complexity of our products, their integration into existing networks and ongoing support of our products requires us to retain highly trained professional services, customer support and sales personnel with specific expertise related to our business. Competition for qualified professional services, customer support, engineering and sales personnel in our industry is intense, because of the limited number of people available with the necessary technical skills and understanding of our products. Our ability to recruit and hire these personnel is harmed by tightening labor markets, particularly in the engineering field, in several of our key geographic hiring areas. We may not be successful in attracting, integrating, or retaining qualified personnel to fulfill our current or future needs, nor may we be successful in keeping the qualified personnel we currently have. Our ability to hire and retain these personnel may be adversely affected by volatility or reductions in the price of our common stock, since these employees are generally granted equity-based awards.

Our future performance also depends on the continued services and continuing contributions of our senior management to execute on our business plan and to identify and pursue new opportunities and product innovations. In particular, Lee Chen, our founder and Chief Executive Officer, and Rajkumar Jalan, our Chief Technology Officer, are critical to the development of our technology and the future vision and strategic direction of our company. The loss of services of senior management could significantly delay or prevent the achievement of our development and strategic objectives, which could adversely affect our business, financial condition, and operating results.

***Adverse general economic conditions or reduced information technology spending may adversely impact our business.***

A substantial portion of our business depends on the demand for information technology by large enterprises and service providers, the overall economic health of our current and prospective end-customers and the continued growth and evolution of the Internet. The timing of the purchase of our products is often discretionary and may involve a significant commitment of capital and other resources. Volatility in the global economic market or other effects of global or regional economic weakness, including limited availability of credit, a reduction in business confidence and activity, deficit-driven austerity measures that continue to affect governments and educational institutions, and other difficulties may affect one or more of the industries to which we sell our products and services. If economic conditions in the United States, Europe and other key markets for our products continue to be volatile or do not improve or those markets experience another downturn, many end-customers may delay or reduce their IT spending. This could result in reductions in sales of our products and services, longer sales cycles, slower adoption of new technologies and increased price competition. Any of these events would likely harm our business, operating results and financial condition. In addition, there can be no assurance that IT spending levels will increase following any recovery.

***Exposure to UK political developments, including the outcome of the UK referendum on membership in the European Union, could have a material adverse effect on us.***

On June 23, 2016, a referendum was held on the United Kingdom's membership in the European Union, the outcome of which was a vote in favor of leaving the European Union (commonly referred to as "Brexit"). The Brexit vote creates an uncertain political and economic environment in the United Kingdom and potentially across other European Union member states, which may last for a number of months or years.

The result of the Brexit vote means that the nature of the United Kingdom's long-term relationship with the European Union is unclear and that there is considerable uncertainty as to when any such relationship will be agreed and implemented. In the interim, there is a risk of economic instability for both the United Kingdom and the European Union, which could adversely affect our results, financial condition and prospects.

The political and economic uncertainty created by the Brexit vote has caused and may continue to cause significant volatility in global financial markets and in the value of the Pound Sterling currency or other currencies, including the Euro. Depending on the terms reached regarding any exit from the European Union, it is possible that there may be adverse practical and/or operational implications on our business.

Consequently, no assurance can be given as to the overall impact of the Brexit and, in particular, no assurance can be given that our operating results, financial condition and prospects would not be adversely impacted by the result.

***We are dependent on third-party manufacturers, and changes to those relationships, expected or unexpected, may result in delays or disruptions that could harm our business.***

We outsource the manufacturing of our hardware components to third-party original design manufacturers who assemble these hardware components to our specifications. Our primary manufacturers are Lanner and AEWIN, each of which is located in Taiwan. Our



reliance on these third-party manufacturers reduces our control over the manufacturing process and exposes us to risks, including reduced control over quality assurance, product costs, and product supply and timing. Any manufacturing disruption at these manufacturers could severely impair our ability to fulfill orders. Our reliance on outsourced manufacturers also may create the potential for infringement or misappropriation of our intellectual property rights or confidential information. If we are unable to manage our relationships with these manufacturers effectively, or if these manufacturers suffer delays or disruptions for any reason, experience increased manufacturing lead-times, experience capacity constraints or quality control problems in their manufacturing operations, or fail to meet our future requirements for timely delivery, our ability to ship products to our end-customers would be severely impaired, and our business and operating results would be seriously harmed.

These manufacturers typically fulfill our supply requirements on the basis of individual orders. We do not have long-term contracts with our manufacturers that guarantee capacity, the continuation of particular pricing terms, or the extension of credit limits. Accordingly, they are not obligated to continue to fulfill our supply requirements, which could result in supply shortages, and the prices we are charged for manufacturing services could be increased on short notice. In addition, our orders may represent a relatively small percentage of the overall orders received by our manufacturers from their customers. As a result, fulfilling our orders may not be considered a priority by one or more of our manufacturers in the event the manufacturer is constrained in its ability to fulfill all of its customer obligations in a timely manner.

Although the services required to manufacture our hardware components may be readily available from a number of established manufacturers, it is time-consuming and costly to qualify and implement such relationships. If we are required to change manufacturers, whether due to an interruption in one of our manufacturers' businesses, quality control problems or otherwise, or if we are required to engage additional manufacturers, our ability to meet our scheduled product deliveries to our customers could be adversely affected, which could cause the loss of sales to existing or potential customers, delayed revenue or an increase in our costs that could adversely affect our gross margin.

***Because some of the key components in our products come from limited sources of supply, we are susceptible to supply shortages or supply changes, which could disrupt or delay our scheduled product deliveries to our end-customers and may result in the loss of sales and end-customers.***

Our products incorporate key components, including certain integrated circuits that we and our third-party manufacturers purchase on our behalf from a limited number of suppliers, including some sole-source providers. In addition, the lead times associated with these and other components of our products can be lengthy and preclude rapid changes in quantities and delivery schedules. Moreover, long-term supply and maintenance obligations to our end-customers increase the duration for which specific components are required, which may further increase the risk we may incur component shortages or the cost of carrying inventory. If we are unable to obtain a sufficient quantity of these components in a timely manner for any reason, sales and/or shipments of our products could be delayed or halted, which would seriously affect present and future sales and cause damage to end-customer relationships, which would, in turn, adversely affect our business, financial condition and results of operations.

In addition, our component suppliers change their selling prices frequently in response to market trends, including industry-wide increases in demand, and because we do not necessarily have contracts with these suppliers, we are susceptible to price fluctuations related to raw materials and components. If we are unable to pass component price increases along to our end-customers or maintain stable pricing, our gross margin and operating results could be negatively impacted. Furthermore, poor quality in sole-sourced components or certain other components in our products could also result in lost sales or lost sales opportunities. If the quality of such components does not meet our standards or our end-customers' requirements, if we are unable to obtain components from our existing suppliers on commercially reasonable terms, or if any of our sole source providers cease to continue to manufacture such components or to remain in business, we could be forced to redesign our products and qualify new components from alternate suppliers. The development of alternate sources for those components can be time-consuming, difficult and costly, and we may not be able to develop alternate or second sources in a timely manner. Even if we are able to locate alternate sources of supply, we could be forced to pay for expedited shipments of such components or our products at dramatically increased costs.

***Real or perceived defects, errors, or vulnerabilities in our products or services or the failure of our products or services to block a threat or prevent a security breach could harm our reputation and adversely impact our results of operations.***

Because our products and services are complex, they have contained and may contain design or manufacturing defects or errors that are not detected until after their commercial release and deployment by our end-customers. Even if we discover those weaknesses, we may not be able to correct them promptly, if at all. Defects may cause our products to be vulnerable to security attacks, cause them to fail to help secure networks, or temporarily interrupt end-customers' networking traffic. Furthermore, our products may fail to detect or prevent malware, viruses, worms or similar threats for any number of reasons, including our failure to enhance and expand our platform to reflect industry trends, new technologies and new operating environments, the complexity of the environment of our end-customers and the sophistication of malware, viruses and other threats. Data thieves and hackers are increasingly sophisticated, often affiliated with organized crime and may operate large-scale and complex automated attacks. The techniques used to obtain unauthorized access or to

sabotage networks change frequently and may not be recognized until launched against a target. Additionally, as a well-known provider of enterprise security solutions, our networks, products, and services could be targeted by attacks specifically designed to disrupt our business and harm our reputation. As our products are adopted by an increasing number of enterprises and governments, it is possible that the individuals and organizations behind advanced attacks will focus on finding ways to defeat our products. In addition, defects or errors in our updates to our products could result in a failure of our services to effectively update end-customers' products and thereby leave our end-customers vulnerable to attacks. Our data centers and networks may experience technical failures and downtime, may fail to distribute appropriate updates, or may fail to meet the increased requirements of a growing installed end-customer base, any of which could temporarily or permanently expose our end-customers' networks, leaving their networks unprotected against security threats. Our end-customers may also misuse our products, which may result in loss or a breach of business data. For all of these reasons, we may be unable to anticipate all data security threats or provide a solution in time to protect our end-customers' networks. If we fail to identify and respond to new and increasingly complex methods of attack and to update our products to detect or prevent such threats in time to protect our end-customers' critical business data, our business, operating results and reputation could suffer.

If any companies or governments that are publicly known to use our platform are the subject of an advanced cyberattack that becomes publicized, our other current or potential channel partners or end-customers may look to our competitors for alternatives to our products. Real or perceived security breaches of our end-customers' networks could cause disruption or damage to their networks or other negative consequences and could result in negative publicity to us, damage to our reputation, declining sales, increased expenses and end-customer relations issues. To the extent potential end-customers or industry analysts believe that the occurrence of any actual or perceived failure of our products to detect or prevent malware, viruses, worms or similar threats is a flaw or indicates that our products do not provide significant value, our reputation and business could be harmed.

Any real or perceived defects, errors, or vulnerabilities in our products, or any failure of our products to detect a threat, could result in:

- a loss of existing or potential end-customers or channel partners;
- delayed or lost revenue;
- a delay in attaining, or the failure to attain, market acceptance;
- the expenditure of significant financial and product development resources in efforts to analyze, correct, eliminate, or work around errors or defects, to address and eliminate vulnerabilities, or to identify and ramp up production with third-party providers;
- an increase in warranty claims, or an increase in the cost of servicing warranty claims, either of which would adversely affect our gross margins;
- harm to our reputation or brand; and
- litigation, regulatory inquiries, or investigations that may be costly and further harm our reputation.

***Our business is subject to the risks of warranty claims, product returns, product liability, and product defects.***

Real or perceived errors, failures or bugs in our products could result in claims by end-customers for losses that they sustain. If end-customers make these types of claims, we may be required, or may choose, for customer relations or other reasons, to expend additional resources in order to help correct the problem. Historically, the amount of warranty claims has not been significant, but there are no assurances that the amount of such claims will not be material in the future. Liability provisions in our standard terms and conditions of sale, and those of our resellers and distributors, may not be enforceable under some circumstances or may not fully or effectively protect us from customer claims and related liabilities and costs, including indemnification obligations under our agreements with resellers, distributors or end-customers. The sale and support of our products also entail the risk of product liability claims. We maintain insurance to protect against certain types of claims associated with the use of our products, but our insurance coverage may not adequately cover any such claims. In addition, even claims that ultimately are unsuccessful could result in expenditures of funds in connection with litigation and divert management's time and other resources.

***Failure to protect and ensure the confidentiality and security of data could lead to legal liability, adversely affect our reputation and have a material adverse effect on our operating results, business and reputation.***

We may collect, store and use certain confidential information in the course of providing our services, and we have invested in preserving the security of this data. We may also outsource operations to third-party service providers to whom we transmit certain confidential data. There are no assurances that any security measures we have in place, or any additional security measures that our subcontractors may have in place, will be sufficient to protect this confidential information from unauthorized security breaches.

We cannot assure you that, despite the implementation of these security measures, we will not be subject to a security incident or other data breach or that this data will not be compromised. We may be required to expend significant capital and other resources to protect against security breaches or to alleviate problems caused by security breaches, or to pay penalties as a result of such breaches. Despite our implementation of security measures, techniques used to obtain unauthorized access or to sabotage systems change frequently and may not be recognized until launched against a target. As a result, we may be unable to anticipate these techniques or implement adequate preventative measures to protect this data. In addition, security breaches can also occur as a result of non-technical issues, including intentional or inadvertent breaches by our employees or service providers or by other persons or entities with whom we have commercial relationships. Any compromise or perceived compromise of our security could damage our reputation with our end-customers, and could subject us to significant liability, as well as regulatory action, including financial penalties, which would materially adversely affect our brand, results of operations, financial condition, business and prospects.

***We have incurred, and expect to continue to incur, significant costs to protect against security breaches. We may incur significant additional costs in the future to address problems caused by any actual or perceived security breaches.***

Breaches of our security measures or those of our third-party service providers, or other security incidents, could result in: unauthorized access to our sites, networks and systems; unauthorized access to, misuse or misappropriation of information, including personally identifiable information, or other confidential or proprietary information of ourselves or third parties; viruses, worms, spyware or other malware being served from our sites, networks or systems; deletion or modification of content or the display of unauthorized content on our sites; interruption, disruption or malfunction of operations; costs relating to notification of individuals, or other forms of breach remediation; deployment of additional personnel and protection technologies; response to governmental investigations and media inquiries and coverage; engagement of third-party experts and consultants; litigation, regulatory investigations, prosecutions, and other actions; and other potential liabilities. If any of these events occurs, or is believed to occur, our reputation and brand could be damaged, our business may suffer, we could be required to expend significant capital and other resources to alleviate problems caused by such actual or perceived breaches, we could be exposed to a risk of loss, litigation or regulatory action and possible liability, and our ability to operate our business, including our ability to provide maintenance and support services to our channel partners and end-customers, may be impaired. If current or prospective channel partners and end-customers believe that our systems and solutions do not provide adequate security for their businesses' needs, our business and our financial results could be harmed. Additionally, actual, potential or anticipated attacks may cause us to incur increasing costs, including costs to deploy additional personnel and protection technologies, train employees and engage third-party experts and consultants.

Although we maintain privacy, data breach and network security liability insurance, we cannot be certain that our coverage will be adequate for liabilities actually incurred or that insurance will continue to be available to us on economically reasonable terms, or at all. Any actual or perceived compromise or breach of our security measures, or those of our third-party service providers, or any unauthorized access to, misuse or misappropriation of personally identifiable information, channel partners' or end-customers information, or other information, could violate applicable laws and regulations, contractual obligations or other legal obligations and cause significant legal and financial exposure, adverse publicity and a loss of confidence in our security measures, any of which could have a material adverse effect on our business, financial condition and operating results.

***Our failure to adequately protect personal data could have a material adverse effect on our business.***

A wide variety of provincial, state, national, foreign, and international laws and regulations apply to the collection, use, retention, protection, disclosure, transfer, and other processing of personal data. These data protection and privacy-related laws and regulations are evolving and being tested in courts and may result in ever-increasing regulatory and public scrutiny and escalating levels of enforcement and sanctions. Our failure to comply with applicable laws and regulations, or to protect such data, could result in enforcement action against us, including fines, imprisonment of company officials and public censure, claims for damages by end-customers and other affected persons and entities, damage to our reputation and loss of goodwill (both in relation to existing and prospective channel partners and end-customers), and other forms of injunctive or operations-limiting relief, any of which could have a material adverse effect on our operations, financial performance, and business. Evolving and changing definitions of personal data and personal information, within the European Union, the United States, and elsewhere, especially relating to classification of Internet Protocol (IP) addresses, machine identification, location data, and other information, may limit or inhibit our ability to operate or expand our business, including limiting strategic partnerships that may involve the sharing of data. We may be required to expend significant resources to modify our solutions and otherwise adapt to these changes, which we may be unable to do on commercially reasonable terms or at all, and our ability to develop new solutions and features could be limited. These developments could harm our business, financial condition and results of operations. Even if not subject to legal challenge, the perception of privacy concerns, whether or not valid, may harm our reputation and inhibit adoption of our products by current and prospective end-customers.

***If the general level of advanced cyberattacks declines, or is perceived by our current or potential customers to have declined, our business could be harmed.***

Our security business may be dependent on enterprises and governments recognizing that advanced cyberattacks are pervasive and are not effectively prevented by legacy security solutions. High visibility attacks on prominent companies and governments have increased market awareness of advanced cyberattacks and help to provide an impetus for enterprises and governments to devote resources to protecting against advanced cyberattacks, which may include testing, purchasing, and deploying our products. If advanced cyberattacks were to decline, or enterprises or governments perceived a decline in the general level of advanced cyberattacks, our ability to attract new channel partners and end-customers and expand our offerings within existing channel partners and end-customers could be materially and adversely affected. An actual or perceived reduction in the threat landscape could increase our sales cycles and harm our business, results of operations and financial condition.

***Undetected software or hardware errors may harm our business and results of operations.***

Our products may contain undetected errors or defects when first introduced or as new versions are released. We have experienced these errors or defects in the past in connection with new products and product upgrades. We expect that these errors or defects will be found from time to time in new or enhanced products after commencement of commercial distribution. These problems have in the past and may in the future cause us to incur significant warranty and repair costs, divert the attention of our engineering personnel from our product development efforts and cause significant customer relations problems. We may also be subject to liability claims for damages related to product errors or defects. While we carry insurance policies covering this type of liability, these policies may not provide sufficient protection should a claim be asserted. A material product liability claim may harm our business and results of operations.

Any errors, defects or vulnerabilities in our products could result in:

- expenditures of significant financial and product development resources in efforts to analyze, correct, eliminate or work around errors and defects or to address and eliminate vulnerabilities;
- loss of existing or potential end-customers or distribution channel partners;
- delayed or lost revenue;
- delay or failure to attain market acceptance;
- indemnification obligations under our agreements with resellers, distributors and/or end-customers;
- an increase in warranty claims compared with our historical experience or an increased cost of servicing warranty claims, either of which would adversely affect our gross margin; and
- litigation, regulatory inquiries, or investigations that may be costly and harm our reputation.

***Our use of open source software in our products could negatively affect our ability to sell our products and subject us to possible litigation.***

We incorporate open source software such as the Linux operating system kernel into our products. We have implemented a formal open source use policy, including written guidelines for use of open source software and business processes for approval of that use. We have developed and implemented our open source policies according to industry practice; however, best practices in this area are subject to change, because there is little reported case law on the interpretation of material terms of many open source licenses. We are in the process of reviewing our open source use and our compliance with open source licenses and implementing remediation and changes necessary to comply with the open source licenses related thereto. We cannot guarantee that our use of open source software has been, and will be, managed effectively for our intended business purposes and/or compliant with applicable open source licenses. We may face legal action by third parties seeking to enforce their intellectual property rights related to our use of such open source software. Failure to adequately manage open source license compliance and our use of open source software may result in unanticipated obligations regarding our products and services, such as a requirement that we license proprietary portions of our products or services on unfavorable terms, that we make available source code for modifications or derivative works we created based upon, incorporating or using open source software, that we license such modifications or derivative works under the terms of the particular open source license and/or that we redesign the affected products or services, which could result, for example, in a loss of intellectual property rights, or delay in providing our products and services. From time to time, there have been claims against companies that distribute or use third-party open source software in their products and services, asserting that the open source software or its combination with the products or services infringes third parties' patents or copyrights, or that the companies' distribution or use of the open source software does not comply with the terms of the applicable open source licenses. Use of certain open source software can lead to greater risks than use of warranted third-party commercial software, as open source licensors generally do not provide warranties or controls on the origin of such open source software. From time to time, there have been claims against companies that use open source software in their products,



challenging the ownership of rights in such open source software. As a result, we could also be subject to suits by parties claiming ownership of rights in what we believe to be open source software and so challenging our right to use such software in our products. If any such claims were asserted against us, we could be required to incur significant legal expenses defending against such a claim. Further, if our defenses to such a claim were not successful, we could be, for example, subject to significant damages, be required to seek licenses from third parties in order to continue offering our products and services without infringing such third party's intellectual property rights, be required to re-engineer such products and services, or be required to discontinue making available such products and services if re-engineering cannot be accomplished on a timely or successful basis. The need to engage in these or other remedies could increase our costs or otherwise adversely affect our business, operating results and financial condition.

***Our products must interoperate with operating systems, software applications and hardware that are developed by others and if we are unable to devote the necessary resources to ensure that our products interoperate with such software and hardware, we may fail to increase, or we may lose market share and we may experience a weakening demand for our products.***

Our products must interoperate with our end-customers' existing infrastructure, specifically their networks, servers, software and operating systems, which may be manufactured by a wide variety of vendors and original equipment manufacturers. As a result, when problems occur in a network, it may be difficult to identify the source of the problem. The occurrence of software or hardware problems, whether caused by our products or another vendor's products, may result in the delay or loss of market acceptance of our products. In addition, when new or updated versions of our end-customers' software operating systems or applications are introduced, we must sometimes develop updated versions of our software so that our products will interoperate properly. We may not accomplish these development efforts quickly, cost-effectively or at all. These development efforts require capital investment and the devotion of engineering resources. If we fail to maintain compatibility with these applications, our end-customers may not be able to adequately utilize our products, and we may, among other consequences, fail to increase, or we may lose market share and experience a weakening in demand for our products, which would adversely affect our business, operating results and financial condition.

***We license technology from third parties, and our inability to maintain those licenses could harm our business.***

Many of our products include proprietary technologies licensed from third parties. In the future, it may be necessary to renew licenses for third party technology or obtain new licenses for other technology. These third-party licenses may not be available to us on acceptable terms, if at all. As a result, we could also face delays or be unable to make changes to our products until equivalent technology can be identified, licensed or developed and integrated with our products. Such delays or an inability to make changes to our products, if it were to occur, could adversely affect our business, operating results and financial condition. The inability to obtain certain licenses to third-party technology, or litigation regarding the interpretation or enforcement of license agreements and related intellectual property issues, could have a material adverse effect on our business, operating results and financial condition.

***Failure to prevent excess inventories or inventory shortages could result in decreased revenue and gross margin and harm our business.***

We purchase products from our manufacturers outside of, and in advance of, reseller or end-customer orders, which we hold in inventory and sell. We place orders with our manufacturers based on our forecasts of our end-customers' requirements and forecasts provided by our distribution channel partners. These forecasts are based on multiple assumptions, each of which might cause our estimates to be inaccurate, affecting our ability to provide products to our customers. There is a risk we may be unable to sell excess products ordered from our manufacturers. Inventory levels in excess of customer demand may result in obsolete inventory and inventory write-downs. The sale of excess inventory at discounted prices could impair our brand image and have an adverse effect on our financial condition and results of operations. Conversely, if we underestimate demand for our products or if our manufacturers fail to supply products we require at the time we need them, we may experience inventory shortages. Inventory shortages might delay shipments to resellers, distributors and customers and cause us to lose sales. These shortages may diminish the loyalty of our distribution channel partners or customers.

The difficulty in forecasting demand also makes it difficult to estimate our future financial condition and results of operations from period to period. A failure to accurately predict the level of demand for our products could adversely affect our total revenue and net income, and we are unlikely to forecast such effects with any certainty in advance. For example, we failed to predict the slowdown in the United States sales during the three months ended September 30, 2014 which resulted in lower revenue, gross margin and net income than expected.

***Our sales cycles can be long and unpredictable, primarily due to the complexity of our end-customers' networks and data centers and the length of their budget cycles. As a result, our sales and revenue are difficult to predict and may vary substantially from period to period, which may cause our operating results to fluctuate significantly.***

The timing of our sales is difficult to predict because of the length and unpredictability of our products' sales cycles. A sales cycle is the period between initial contact with a prospective end-customer and any sale of our products. Our sales cycle, in particular to our large end-customers, may be lengthy due to the complexity of their networks and data centers. Because of this complexity, prospective end-customers generally consider a number of factors over an extended period of time before committing to purchase our products. End-customers often view the purchase of our products as a significant and strategic decision that can have important implications on their

existing networks and data centers and, as a result, require considerable time to evaluate, test and qualify our products prior to making a purchase decision and placing an order to ensure that our products will successfully interoperate with our end-customers' complex network and data centers. Additionally, the budgetary decisions at these entities can be lengthy and require multiple organization reviews. The length of time that end-customers devote to their evaluation of our products and decision making process varies significantly. The length of our products' sales cycles typically ranges from three to 12 months but can be longer for our large end-customers. In addition, the length of our close or sales cycle can be affected by the extent to which customized features are requested, in particular in our large deals.

For all of these reasons, it is difficult to predict whether a sale will be completed or the particular fiscal period in which a sale will be completed, both of which contribute to the uncertainty of our future operating results. If our close or sales cycles lengthen, our revenue could be lower than expected, which would have an adverse impact on our operating results and could cause our stock price to decline.

***Our ability to sell our products is highly dependent on the quality of our support and services offerings, and our failure to offer high-quality support could have a material adverse effect on our business, revenue and results of operations.***

We believe that our ability to provide consistent, high quality customer service and technical support is a key factor in attracting and retaining end-customers of all sizes and is critical to the deployment of our products. When support is purchased our end-customers depend on our support organization to provide a broad range of support services, including on-site technical support, 24-hour support and shipment of replacement parts on an expedited basis. If our support organization or our distribution channel partners do not assist our end-customers in deploying our products effectively, succeed in helping our end-customers resolve post-deployment issues quickly, or provide ongoing support, it could adversely affect our ability to sell our products to existing end-customers and could harm our reputation with potential end-customers. We currently have technical support centers in the United States, Japan, China, India and the Netherlands. As we continue to expand our operations internationally, our support organization will face additional challenges, including those associated with delivering support, training and documentation in languages other than English.

We typically sell our products with maintenance and support as part of the initial purchase, and a substantial portion of our support revenue comes from renewals of maintenance and support contracts. Our end-customers have no obligation to renew their maintenance and support contracts after the expiration of the initial period. If we are unable to provide high quality support, our end-customers may elect not to renew their maintenance and support contracts or to reduce the product quantity under their maintenance and support contracts, thereby reducing our future revenue from maintenance and support contracts.

Our failure or the failure of our distribution channel partners to maintain high-quality support and services could have a material and adverse effect on our business, revenue and operating results.

***We depend on growth in markets relating to network security, management and analysis, and lack of growth or contraction in one or more of these markets could have a material adverse effect on our results of operations and financial condition.***

Demand for our products is linked to, among other things, growth in the size and complexity of network infrastructures and the demand for networking technologies addressing the security, management and analysis of such infrastructures. These markets are dynamic and evolving. Our future financial performance will depend in large part on continued growth in the number of organizations investing in their network infrastructure and the amount they commit to such investments. If this demand declines, our results of operations and financial condition would be materially and adversely affected. Segments of the network infrastructure industry have in the past experienced significant economic downturns. Furthermore, the market for network infrastructure may not continue to grow at historic rates, or at all. The occurrence of any of these factors in the markets relating to network security, management and analysis could materially and adversely affect our results of operations and financial condition.

***Our revenue growth rate in recent periods may not be indicative of our future performance.***

You should not consider our revenue growth rate in recent periods as indicative of our future performance. We have recently experienced revenue growth rates of 16%, 11% and 27% in 2016, 2015 and 2014 as compared to the same prior periods. We may not achieve similar revenue growth rates 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. 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.

***Our business and operations have experienced rapid growth in certain prior periods and may experience rapid growth at certain times in the future, and if we do not effectively manage any future growth or are unable to improve our controls, systems and processes, our operating results will be adversely affected.***

In certain recent periods, we have significantly increased the number of our employees and independent contractors. As we hire new employees and independent contractors and expand into new locations outside the United States, we are required to comply with varying local laws for each of these new locations. We anticipate that further expansion of our infrastructure and headcount will be required. Our growth has placed, and will continue to place, a significant strain on our administrative and operational infrastructure and financial resources. Our ability to manage our operations and growth across multiple countries will require us to continue to refine our operational, financial and management controls, human resource policies, and reporting systems and processes.

We need to continue to improve our internal systems, processes, and controls to effectively manage our operations and growth. We may not be able to successfully implement improvements to these systems, processes and controls in an efficient or timely manner. In addition, our systems and processes may not prevent or detect all errors, omissions, or fraud. We may experience difficulties in managing improvements to our systems, processes, and controls or in connection with third-party software, which could impair our ability to provide products or services to our customers in a timely manner, causing us to lose customers, limit us to smaller deployments of our products, increase our technical support costs, or damage our reputation and brand. Our failure to improve our systems and processes, or their failure to operate in the intended manner, may result in our inability to manage the growth of our business and to accurately forecast our revenue, expenses, and earnings, or to prevent certain losses, any of which may harm our business and results of operations.

***We may not be able to sustain or develop new distributor and reseller relationships, and a reduction or delay in sales to significant distribution channel partners could hurt our business.***

We sell our products and services through multiple distribution channels in the United States and internationally. We may not be able to increase our number of distributor or reseller relationships or maintain our existing relationships. Recruiting and retaining qualified distribution channel partners and training them on our technologies requires significant time and resources. These distribution channel partners may also market, sell and support products and services that are competitive with ours and may devote more resources to the marketing, sales and support of such competitive products. Our sales channel structure could subject us to lawsuits, potential liability and reputational harm if, for example, any of our distribution channel partners misrepresent the functionality of our products or services to end-customers or violate laws or our corporate policies. If we are unable to establish or maintain our sales channels or if our distribution channel partners are unable to adapt to our future sales focus and needs, our business and results of operations will be harmed.

***The terms of the 2016 Credit Facility could restrict our operations, particularly our ability to respond to changes in our business or to take specified actions.***

In November 2016, we entered into a loan and security agreement (the “2016 Credit Facility”) with Silicon Valley Bank (“SVB”), as lender. The 2016 Credit Facility contains a number of restrictive covenants that impose operating and financial restrictions on us, including restrictions on our ability to take actions that may be in our best interests. The 2016 Credit Facility requires us to satisfy a specified financial covenant. Our ability to meet the financial covenant can be affected by events beyond our control, and we may not be able to continue to meet the covenant. Upon the occurrence of an event of default, SVB could elect to declare all amounts outstanding under the 2016 Credit Facility to be immediately due and payable and terminate all commitments to extend further credit. If SVB accelerates the repayment, if any, we may not have sufficient funds to repay our existing debt. If we were unable to repay those amounts, SVB could proceed against the collateral granted to it to secure such indebtedness. We have pledged substantially all of our assets, excluding our intellectual property, as collateral under the 2016 Credit Facility. Through the date of this filing, we had no outstanding balance under the 2016 Credit Facility and were in compliance with all facility covenants.

***Our sales to governmental organizations are subject to a number of challenges and risks.***

We sell to governmental organization end-customers. Sales to governmental organizations are subject to a number of challenges and risks. Selling to governmental organizations 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. We have not yet received security clearance from the United States government, which prevents us from being able to sell directly for certain governmental uses. There can be no assurance that such clearance will be obtained, and failure to do so may adversely affect our operating results. Governmental organization demand and payment for our products may be impacted by public sector budgetary cycles and funding authorizations, with funding reductions or delays adversely affecting public sector demand for our products. Governmental organizations may have statutory, contractual or other legal rights to terminate contracts with our distributors and resellers for convenience or due to a default, and any such termination may adversely impact our future operating results.

***Failure to comply with governmental laws and regulations could harm our business.***

Our business is subject to regulation by various federal, state, local and foreign governmental entities, including agencies responsible for monitoring and enforcing employment and labor laws, workplace safety, product safety, environmental laws, consumer protection laws, anti-bribery laws, import/export controls, federal securities laws, and tax laws and regulations. In certain jurisdictions, these regulatory requirements may be more stringent than those in the United States. Noncompliance with applicable regulations or requirements could subject us to investigations, sanctions, mandatory product recalls, enforcement actions, disgorgement of profits, fines, damages, civil and criminal penalties, or injunctions. If any governmental sanctions are imposed, or if we do not prevail in any possible civil or criminal litigation, our business, operating results, and financial condition could be materially adversely affected. In addition, responding to any action will likely result in a significant diversion of management’s attention and resources and an increase in professional fees. Enforcement actions and sanctions could harm our business, operating results and financial condition.

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

Our products are subject to U.S. export controls and may be exported outside the United States only with the required level of export license or through an export license exception because we incorporate encryption technology into our products. In addition, various countries regulate the import of certain encryption technology and have enacted laws that could limit our ability to distribute our products or our end-customers' ability to implement our products in those countries. Changes in our products or changes in export and import regulations may create delays in the introduction of our products in international markets, prevent our end-customers with international operations from deploying our products throughout their global systems or, in some cases, prevent the export or import of our products to certain countries altogether. Any change in export or import regulations or related legislation, shift in approach to the enforcement or scope of existing regulations or change in the countries, persons or technologies targeted by such regulations, could result in decreased use of our products by, or in our decreased ability to export or sell our products to, existing or potential end-customers with international operations. Any decreased use of our products or limitation on our ability to export or sell our products would likely adversely affect our business, operating results and financial condition.

We discovered that trial software was inadvertently available for download by any international user and, on limited occasions, was downloaded by individuals located in a U.S. sanctioned country. We implemented corrective actions and filed a Voluntary Self Disclosure in February 2017 with the U.S. Department of Commerce and U.S. Department of Treasury regarding these technical violations. We do not believe the potential imposition of any fines by the U.S. government would be material to us.

***We are subject to various environmental laws and regulations that could impose substantial costs upon us.***

Our company must comply with local, state, federal, and international environmental laws and regulations in the countries in which we do business. We are also subject to laws, which restrict certain hazardous substances, including lead, used in the construction of our products, such as the European Union Restriction on the Use of Hazardous Substances in electrical and electronic equipment directive. We are also subject to the European Union Directive, known as the Waste Electrical and Electronic Equipment Directive ("WEEE Directive"), which requires producers of certain electrical and electronic equipment to properly label products, register as a WEEE producer, and provide for the collection, disposal, and recycling of waste electronic products. Failure to comply with these environmental directives and other environmental laws could result in the imposition of fines and penalties, inability to sell covered products in certain countries, the loss of revenue, or subject us to third-party property damage or personal injury claims, or require us to incur investigation, remediation or engineering costs. Our operations and products will be affected by future environmental laws and regulations, but we cannot predict the ultimate impact of any such future laws and regulations at this time.

***Our products must conform to industry standards in order to be accepted by end-customers in our markets.***

Generally, our products comprise only a part of a data center. The servers, network, software and other components and systems of a data center must comply with established industry standards in order to interoperate and function efficiently together. We depend on companies that provide other components of the servers and systems in a data center to support prevailing industry standards. Often, these companies are significantly larger and more influential in driving industry standards than we are. Some industry standards may not be widely adopted or implemented uniformly, and competing standards may emerge that may be preferred by our end-customers. If larger companies do not support the same industry standards that we do, or if competing standards emerge, market acceptance of our products could be adversely affected and we may need to incur substantial costs to conform our products to such standards, which could harm our business, operating results and financial condition.

***Our business could be adversely impacted by changes demanded by our customers in the deployment and payment models for our products.***

Our customers have traditionally demanded products deployed in physical, appliance-based on-premise data centers that are paid in full at the time of purchase and include perpetual licenses for our software products. While these products remain central to our business, new deployment and payment models are emerging in our industry that may provide some of our customers with additional technical, business agility and flexibility options. These new models include cloud-based applications provided as SaaS and software subscription licenses where license and service fees are ratable and correlate to the type of service used, the quantity of services consumed or the length of time of the subscription. These models have accounting treatments that may require us to recognize revenue ratably over an extended period of time. If a substantial portion of our customers transition from on-premise-based products to such cloud-based, consumption and subscription-based models, this could adversely affect our operating results and could make it more difficult to compare our operating results during such transition period with our historical operating results.



***We are dependent on various information technology systems, and failures of or interruptions to those systems could harm our business.***

Many of our business processes depend upon our information technology systems, the systems and processes of third parties, and on interfaces with the systems of third parties. If those systems fail or are interrupted, or if our ability to connect to or interact with one or more networks is interrupted, our processes may function at a diminished level or not at all. This could harm our ability to ship or support our products, and our financial results may be harmed.

In addition, reconfiguring or upgrading our information technology systems or other business processes in response to changing business needs may be time-consuming and costly and is subject to risks of delay or failed deployment. To the extent this impacts our ability to react timely to specific market or business opportunities, our financial results may be harmed.

***Future acquisitions we may undertake may not result in the financial and strategic goals that are contemplated at the time of the transaction.***

We completed the acquisition of substantially all of the assets of Appcito in June 2016 and may make future acquisitions of complementary companies, products or technologies. With respect to the Appcito acquisition or any other future acquisitions we may undertake, we may find that the acquired businesses, products or technologies do not further our business strategy as expected, that we paid more than what the assets are later worth or that economic conditions change, all of which may generate future impairment charges. The Appcito acquisition or any future acquisitions may be viewed negatively by customers, financial markets or investors. There may be difficulty integrating the operations and personnel of an acquired business, and we may have difficulty retaining the key personnel of an acquired business. We may have difficulty in integrating acquired technologies or products with our existing product lines. Any integration process may require significant time and resources, and we may not be able to manage the process successfully. Our ongoing business and management's attention may be disrupted or diverted by transition or integration issues and the complexity of managing geographically and culturally diverse locations. We may have difficulty maintaining uniform standards, controls, procedures and policies across locations. We may experience significant problems or liabilities associated with product quality, technology and other matters.

Our inability to successfully operate and integrate future acquisitions appropriately, effectively and in a timely manner, or to retain key personnel of any acquired business, could have a material adverse effect on our revenue, gross margin and expenses.

***Our ability to use our net operating loss carryforwards may be subject to limitation and may result in increased future tax liability to us.***

Generally, a change of more than 50% in the ownership of a corporation's stock, by value, over a three-year period constitutes an ownership change for U.S. federal income tax purposes. An ownership change may limit a company's ability to use its net operating loss carryforwards attributable to the period prior to such change. In the event we have undergone an ownership change under Section 382 of the Internal Revenue Code, if we earn net taxable income, our ability to use our pre-change net operating loss carryforwards to offset U.S. federal taxable income may become subject to limitations, which could potentially result in increased future tax liability to us.

***Unanticipated changes in effective tax rates or adverse outcomes resulting from examination of our income or other tax returns could adversely affect our operating results and financial condition.***

We are subject to income taxes in the United States and various foreign jurisdictions, and our domestic and international tax liabilities will be subject to the allocation of expenses in differing jurisdictions. Our future effective tax rates could be subject to volatility or adversely affected by a number of factors, including:

- changes in the valuation of our deferred tax assets and liabilities;
- expected timing and amount of the release of tax valuation allowances;
- expiration of, or detrimental changes in, research and development tax credit laws;
- tax effects of stock-based compensation;
- costs related to intercompany restructurings;
- changes in tax laws, regulations, accounting principles or interpretations thereof;
- future earnings being lower than anticipated in countries where we have lower statutory tax rates and higher than anticipated earnings in countries where we have higher statutory tax rates; or
- examinations by US federal, state or foreign jurisdictions that disagree with interpretations of tax rules and regulations in regards to positions taken on tax filings.

***Changes in our effective tax rate could adversely affect our results of operations.***

As our business grows, we are required to comply with increasingly complex taxation rules and practices. We are subject to tax in multiple U.S. tax jurisdictions and in foreign tax jurisdictions as we expand internationally. The development of our tax strategies requires additional expertise and may impact how we conduct our business. Our future effective tax rates could be unfavorably affected by changes in, or interpretations of, tax rules and regulations in the jurisdictions in which we do business or changes in the valuation of our deferred tax assets and liabilities. Furthermore, we provide for certain tax liabilities that involve significant judgment. We are subject to the examination of our tax returns by federal, state and foreign tax authorities, which could focus on our intercompany transfer pricing methodology as well as other matters. If our tax strategies are ineffective or we are not in compliance with domestic and international tax laws, our financial position, operating results and cash flows could be adversely affected.

***We are exposed to the credit risk of our distribution channel partners and end-customers, which could result in material losses and negatively impact our operating results.***

Most of our sales are on an open credit basis, with typical payment terms ranging from 30 to 90 days depending on local customs or conditions that exist in the sale location. If any of the distribution channel partners or end-customers responsible for a significant portion of our revenue becomes insolvent or suffers a deterioration in its financial or business condition and is unable to pay for our products, our results of operations could be harmed.

***Concentration of ownership among our existing executive officers, a small number of stockholders, directors and their affiliates may prevent new investors from influencing significant corporate decisions.***

Our executive officers and directors, together with affiliated entities, own 30.8% of our outstanding common stock as of December 31, 2016. Accordingly, these stockholders, acting together, have significant influence over the election of our directors, over whether matters requiring stockholder approval are approved or disapproved and over our affairs in general. The interests of these stockholders could conflict with your interests. These stockholders may also have an interest in pursuing acquisitions, divestitures, financings or other transactions that, in their judgment, could enhance their investments, even though such transactions might involve risks to you. In addition, this concentration of ownership could have the effect of delaying or preventing a liquidity event such as a merger or liquidation of our company.

***We may need to raise additional funds in future private or public offerings, and such funds may not be available on acceptable terms, if at all. If we do raise additional funds, existing stockholders will suffer dilution.***

We may need to raise additional funds in private or public offerings, and these funds may not be available to us when we need them or on acceptable terms, if at all. If we raise additional funds through further issuances of equity or convertible debt securities, you could suffer significant dilution, and any new equity securities we issue could have rights, preferences and privileges superior to those of our then-existing capital stock. Any debt financing secured by us in the future could involve restrictive covenants relating to our capital raising activities and other financial and operational matters, which may make it more difficult for us to obtain additional capital and to pursue business opportunities. If we cannot raise additional funds when we need them, our business and prospects could fail or be materially and adversely affected.

***The price of our common stock has been and may continue to be volatile, and the value of your investment could decline.***

Technology stocks have historically experienced high levels of volatility. The trading price of our common stock has been and is likely to continue to be volatile and subject to fluctuations in response to many factors, some of which are beyond our control and may not be related to our operating performance. These fluctuations could cause you to lose all or part of your investment in our common stock. Factors that could cause fluctuations in the trading price of our common stock include the following:

- announcements of new products, services or technologies, commercial relationships, acquisitions or other events by us or our competitors;
- price and volume fluctuations in the overall stock market from time to time;
- significant volatility in the market price and trading volume of technology companies in general and of companies in our industry;
- fluctuations in the trading volume of our shares or the size of our public float;
- actual or anticipated changes or fluctuations in our results of operations;
- whether our results of operations meet the expectations of securities analysts or investors;
- actual or anticipated changes in the expectations of investors or securities analysts;

- litigation or investigations involving us, our industry, or both;
- regulatory developments in the United States, foreign countries or both;
- general economic conditions and trends;
- major catastrophic events;
- sales of large blocks of our common stock; or
- departures of key personnel.

In addition, if the market for technology stocks or the stock market in general experiences a loss of investor confidence, the trading price of our common stock could decline for reasons unrelated to our business, results of operations or financial condition. The trading price of our common stock might also decline in reaction to events that affect other companies in our industry even if these events do not directly affect us. In the past, following periods of volatility in the market price of a company's securities, securities class action litigation has often been brought against that company. The price of our common stock has been highly volatile since our initial public offering ("IPO") in March 2014. In January 2015, several substantially identical lawsuits alleging violations of securities laws were filed against us, our directors and certain of our executive officers (which actions were consolidated on May 29, 2015) and in June 2015, the related Derivative Action (as defined below) was filed. These and any future securities litigation, including any related to shareholder derivative litigation, could result in substantial costs and divert our management's attention and resources from our business. This could have a material adverse effect on our business, results of operations and financial condition.

***Sales of substantial amounts of our common stock in the public markets, or the perception that such sales might occur, could reduce the price that our common stock might otherwise attain and may dilute your voting power and your ownership interest in us.***

Sales of a substantial number of shares of our common stock in the public market, or the perception that such sales could occur, could adversely affect the market price of our common stock and may make it more difficult for you to sell your common stock at a time and price that you deem appropriate. As of December 31, 2016, there were approximately 5.7 million vested and exercisable options to purchase our common stock, in addition to the 67.9 million common shares outstanding as of such date. All outstanding shares and all shares issuable upon exercise of outstanding and vested options are freely tradable, subject in some cases to volume and other restrictions of Rules 144 and 701 under the Securities Act, as well as our insider trading policy. In addition, holders of certain shares of our outstanding common stock, including an aggregate of 9.5 million shares held by funds affiliated with Summit Partners, L.P. as of December 31, 2016 are entitled to rights with respect to registration of these shares under the Securities Act pursuant to an investors' rights agreement.

If these holders of our common stock, by exercising their registration rights, sell a large number of shares, they could adversely affect the market price for our common stock. If we file a registration statement for the purposes of selling additional shares to raise capital and are required to include shares held by these holders pursuant to the exercise of their registration rights, our ability to raise capital may be impaired. Sales of substantial amounts of our common stock in the public market, or the perception that these sales could occur, could cause the market price of our common stock to decline.

***We are an emerging growth company, and any decision on our part to comply only with certain reduced disclosure requirements applicable to emerging growth companies could make our common stock less attractive to investors.***

We are an emerging growth company, and, for as long as we continue to be an emerging growth company, we may choose to take advantage of exemptions from various reporting requirements applicable to other public companies but not to "emerging growth companies," including, but not limited to, not being required to have our independent registered public accounting firm audit our internal control over financial reporting under Section 404 of the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements, and exemptions from the requirements of holding a nonbinding advisory vote on executive compensation and stockholder approval of any golden parachute payments not previously approved. We could be an emerging growth company for up to five years following the completion of our initial public offering. We will remain an emerging growth company until the earliest of: (a) the last day of the year (i) following the fifth anniversary of the completion of the initial public offering, (ii) in which we have total annual gross revenue of at least \$1.0 billion, or (iii) in which we qualify as a large accelerated filer, which means the market value of our common stock that is held by non-affiliates exceeds \$700 million as of the prior June 30, or (b) the date on which we have issued more than \$1.0 billion in non-convertible debt securities during the prior three-year period. We cannot predict if investors will find our common stock less attractive if we choose to rely on these exemptions. If some investors find our common stock less attractive as a result of any choices to reduce future disclosure, there may be a less active trading market for our common stock and the price of our common stock may be more volatile.

Under the JOBS Act, emerging growth companies can also delay adopting new or revised accounting standards until such time as those standards apply to private companies. We have irrevocably elected not to avail ourselves of this accommodation allowing for delayed adoption of new or revised accounting standards, and, therefore, we will be subject to the same new or revised accounting standards as other public companies that are not emerging growth companies.

***We are obligated to implement and maintain effective internal control over financial reporting. We may not complete our analysis of our internal control over financial reporting in a timely manner, or our internal control over financial reporting may not be determined to be effective, or we may discover significant deficiencies or material weakness in our internal control over financial reporting in the future, all of which may adversely affect investor confidence in our company and, as a result, the value of our common stock.***

We are required, pursuant to the Exchange Act, to furnish a report by management on, among other things, the effectiveness of our internal control over financial reporting for each fiscal year. This assessment will need to include disclosure of any material weaknesses identified by our management in our internal control over financial reporting.

We have, in the past, experienced issues with our internal control over financial reporting, such as the material weakness discovered in connection with our review of internal control over financial reporting as of December 31, 2014, related to an incorrect methodology used to compute share-based compensation associated with our 2014 Purchase Plan for the fourth quarter of 2014, and which resulted in a material adjustment to decrease share-based compensation in our fourth quarter ended December 31, 2014. While we believe that this material weakness was remediated during the year ended December 31, 2015, it is possible that we may discover significant deficiencies or material weaknesses in our internal control over financial reporting in the future. If we are unable to conclude that our internal control over financial reporting is effective, or if we are required to restate our financial statements as a result of ineffective internal control over financial reporting, we could lose investor confidence in the accuracy and completeness of our financial reports, which would cause the price of our common stock to decline.

We are required to disclose material changes made in our internal control and procedures on a quarterly basis. However, our independent registered public accounting firm will not be required to formally attest to the effectiveness of our internal control over financial reporting pursuant to Section 404 of the Sarbanes-Oxley Act until the year following the date we are no longer an emerging growth company as defined in the JOBS Act, if we take advantage of the exemptions contained in the JOBS Act. To comply with these requirements, we may need to undertake various actions, such as implementing new internal controls and procedures and hiring accounting or internal audit staff.

***If securities or industry analysts do not publish research or reports about our business, or publish inaccurate or unfavorable research reports about our business, our share price and trading volume could decline.***

The market for our common stock, to some extent, depends on the research and reports that securities or industry analysts publish about us or our business. We do not have any control over these analysts. If one or more of the analysts who cover us should downgrade our shares or change their opinion of our shares, our share price would likely decline. If one or more of these analysts should cease coverage of our company or fail to regularly publish reports on us, we could lose visibility in the financial markets, which would cause our share price or trading volume to decline.

***Our charter documents and Delaware law could discourage takeover attempts and lead to management entrenchment.***

Our restated certificate of incorporation and bylaws contain provisions that could delay or prevent a change in control of our company. These provisions could also make it difficult for stockholders to elect directors that are not nominated by the current members of our board of directors or take other corporate actions, including effecting changes in our management. These provisions include:

- a classified board of directors with three-year staggered terms, which could delay the ability of stockholders to change the membership of a majority of our board of directors;
- the ability of our board of directors to issue shares of preferred stock and to determine the price and other terms of those shares, including preference and voting rights, without stockholder approval, which could be used to significantly dilute the ownership of a hostile acquirer;
- the exclusive right of our board of directors to elect a director to fill a vacancy created by the expansion of our board of directors or the resignation, death or removal of a director, which prevents stockholders from being able to fill vacancies on our board of directors;
- a prohibition on stockholder action by written consent, which forces stockholder action to be taken at an annual or special meeting of our stockholders;

- the requirement that a special meeting of stockholders may be called only by the chairman of our board of directors, our Chief Executive Officer, our secretary, or a majority vote of our board of directors, which could delay the ability of our stockholders to force consideration of a proposal or to take action, including the removal of directors;
- the requirement for the affirmative vote of holders of at least 66-2/3% of the voting power of all of the then-outstanding shares of the voting stock, voting together as a single class, to amend the provisions of our restated certificate of incorporation relating to the issuance of preferred stock and management of our business or our bylaws, which may inhibit the ability of an acquirer to effect such amendments to facilitate an unsolicited takeover attempt;
- the ability of our board of directors, by majority vote, to amend the bylaws, which may allow our board of directors to take additional actions to prevent an unsolicited takeover and inhibit the ability of an acquirer to amend the bylaws to facilitate an unsolicited takeover attempt; and
- advance notice procedures with which stockholders must comply to nominate candidates to our board of directors or not to propose matters to be acted upon at a stockholders' meeting, which may discourage or deter a potential acquirer from conducting a solicitation of proxies to elect the acquiror's own slate of directors or otherwise attempting to obtain control of us.

In addition, as a Delaware corporation, we are subject to Section 203 of the Delaware General Corporation Law. These provisions may prohibit large stockholders, in particular those owning 15% or more of our outstanding voting stock, from merging or combining with us for a certain period of time.

***Our business is subject to the risks of earthquakes, fire, power outages, floods, and other catastrophic events, and to interruption by man-made problems such as acts of war and terrorism.***

A significant natural disaster, such as an earthquake, fire, a flood, or significant power outage could have a material adverse impact on our business, operating results, and financial condition. Our corporate headquarters are located in the San Francisco Bay Area, a region known for seismic activity. In addition, our two primary manufacturers are located in Taiwan, which is near major earthquake fault lines and subject to typhoons during certain times of the year. In the event of a major earthquake or typhoon, or other natural or man-made disaster, our manufacturers in Taiwan may face business interruptions, which may impact quality assurance, product costs, and product supply and timing. In the event our or our service providers' information technology systems or manufacturing or logistics abilities are hindered by any of the events discussed above, shipments could be delayed, resulting in missed financial targets, such as revenue and shipment targets, and our operations could be disrupted, for the affected quarter or quarters. In addition, cyber security attacks, acts of war or terrorism, or other geo-political unrest could cause disruptions in our business or the business of our supply chain, manufacturers, logistics providers, partners, or end-customers or the economy as a whole. Any disruption in the business of our supply chain, manufacturers, logistics providers, partners or end-customers that impacts sales at the end of a quarter could have a significant adverse impact on our quarterly results. All of the aforementioned risks may be further increased if the disaster recovery plans for us and our suppliers prove to be inadequate. To the extent that any of the above should result in delays or cancellations of customer orders, or the delay in the manufacture, deployment or shipment of our products, our business, financial condition and operating results would be adversely affected.

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

We intend to retain any earnings to finance the operation and expansion of our business, and we do not anticipate paying any cash dividends in the future. In addition, the 2016 Credit Facility currently restricts our ability to pay cash dividends while this facility remains outstanding. As a result, you may only receive a return on your investment in our common stock if the value of our common stock increases.

## **ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

## **ITEM 2. PROPERTIES**

Our corporate headquarters is located in San Jose, California, where we currently lease 79,803 square feet of space under a lease agreement that expires in February 2022. We also lease space for offices internationally and for sales offices in locations throughout the United States and various international locations, including, among others, China, Japan, the United Kingdom, the Netherlands, Taiwan, Korea, Singapore and India. We believe that our current facilities are adequate to meet our current needs. We intend to expand our facilities or add new facilities as we add employees and enter new geographic markets. We believe that alternative or additional space suitable for our requirements will be available as needed to accommodate ongoing operations and any such growth. We do however expect to incur additional expenses in connection with any such new or expanded facilities.

We consider these current facilities suitable and adequate to meet our requirements.



### **ITEM 3. LEGAL PROCEEDINGS**

We have been and may currently be involved in various legal proceedings, the outcomes of which are not within our complete control or may not be known for prolonged periods of time. Management is required to assess the probability of loss and amount of such loss, if any, in preparing our consolidated financial statements. We evaluate the likelihood of a potential loss from legal proceedings to which we are a party. We record a liability for such claims when a loss is deemed probable and the amount can be reasonably estimated. Significant judgment may be required in the determination of both probability and whether an exposure is reasonably estimable. Our judgments are subjective based on the status of the legal proceedings, the merits of our defenses and consultation with in-house and outside legal counsel. As additional information becomes available, we reassess the potential liability related to pending claims and may revise our estimates. Due to the inherent uncertainties of the legal processes in the multiple jurisdictions in which we operate, our judgments may be materially different than the actual outcomes, which could have material adverse effects on our business, financial conditions and results of operations.

Additional information with respect to this Item may be found in Note 5. *Commitments and Contingencies*, in the Notes to Consolidated Financial Statements of this Annual Report on Form 10-K, which is incorporated by reference.

### **ITEM 4. MINE SAFETY DISCLOSURES**

None.

## PART II.

### ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

#### Market for Registrant's Common Equity

Our common stock has been quoted on the New York Stock Exchange ("NYSE") under the symbol "ATEN" since March 21, 2014. Prior to that time, there was no public market for our stock. The following table sets forth the high and low closing sales price per share of our common stock for the periods indicated.

	Fiscal Year 2016 Quarter Ended				Fiscal Year 2015 Quarter Ended			
	March 31, 2016	June 30, 2016	September 30, 2016	December 31, 2016	March 31, 2015	June 30, 2015	September 30, 2015	December 31, 2015
Low .....	\$ 4.92	\$ 5.74	\$ 6.52	\$ 7.44	\$ 3.96	\$ 4.18	\$ 4.98	\$ 5.68
High .....	\$ 6.61	\$ 6.92	\$ 10.69	\$ 10.77	\$ 5.58	\$ 7.38	\$ 7.40	\$ 8.30

There were approximately 165 stockholders of record on February 13, 2017. Because many shares of our common stock are held by brokers and other institutions on behalf of stockholders, we are unable to estimate the total number of stockholders represented by these holders of record.

#### Dividends

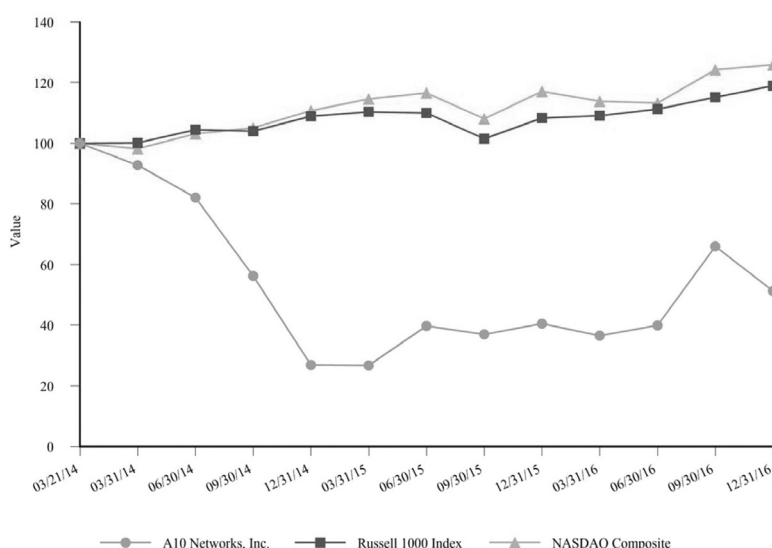
We have never declared or paid any cash dividends on our common stock. We currently intend to retain any future earnings and do not expect to pay any cash dividends on our common stock for the foreseeable future. Any determination to pay dividends in the future will be at the discretion of our board of directors and will be dependent on a number of factors, including our earnings, capital requirements and overall financial conditions. Currently, the agreement for our revolving credit facility contains restrictions on our ability to pay cash dividends.

#### Equity Compensation Plan Information

See Item 12. *Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters* for information regarding securities authorized for issuance.

## Comparison of Stockholder Return

The following graph compares the quarterly percentage change in the cumulative total return on our common stock, the NASDAQ Composite Index and the Russell 1000 Index. The graph assumes \$100 was invested on March 21, 2014 in our common stock and each index and all dividends were reinvested. The stock price performance on the following graph is not necessarily indicative of future stock price performance.



	3/21/14	3/31/14	6/30/14	9/30/14	12/31/14	3/31/15	6/30/15	9/30/15	12/31/15	3/31/16	6/30/16	9/30/16	12/31/16
A10 Networks, Inc.	100.00	92.78	82.05	56.20	26.90	26.71	39.73	36.95	40.47	36.52	39.91	65.95	51.27
NASDAQ Composite	100.00	98.18	103.07	105.06	110.74	114.59	116.6	108.03	117.08	113.86	113.23	124.20	125.86
Russell 1000	100.00	100.23	104.84	105.02	109.61	110.81	110.4	102.34	108.41	109.08	111.25	115.15	118.92

## Stock Repurchase Program

On October 27, 2016, our board of directors authorized a share repurchase program for up to \$20.0 million of our common stock over the next 12 months. Under the repurchase authorization, shares may be purchased from time to time, subject to general business and market conditions and other investment opportunities, through open market purchases, privately negotiated transactions or other means. The repurchase authorization may be commenced, suspended or discontinued at any time at our discretion.

Share repurchase activity during the three months ended December 31, 2016 was as follows:

Period	Total Number of Shares Repurchased	Average Price Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (in thousands)
Beginning repurchase authority				\$ 20,000
Shares repurchased:				
October 1, 2016 – October 31, 2016	—	—	—	\$ 20,000
November 1, 2016 – November 30, 2016	145,876	\$ 7.85	145,876	\$ 18,855
December 1, 2016 – December 31, 2016	80,800	\$ 8.04	80,800	\$ 18,205
Total	<u>226,676</u>		<u>226,676</u>	

## Unregistered Sales of Equity Securities

None.



## ITEM 6. SELECTED FINANCIAL DATA

The following tables set forth the selected consolidated financial data for each of the years in the five-year period ended December 31, 2016. These selected consolidated financial data should be read in conjunction with the consolidated financial statements and accompanying notes, Management's Discussion and Analysis of Financial Condition and Results of Operations and other financial information is included elsewhere in this Annual Report on Form 10-K. We have derived the consolidated statement of operations data for the years ended December 31, 2016, 2015 and 2014 and the consolidated balance sheet data as of December 31, 2016 and 2015 from the consolidated audited financial statements included in *Item 8. Financial Statements and Supplemental Data* in this Annual Report on Form 10-K. The consolidated statement of operations data for the years ended December 31, 2013 and 2012 and the consolidated balance sheet data as of December 31, 2014, 2013 and 2012 were derived from the consolidated audited financial statements that are not included in this Annual Report on Form 10-K.

	Year Ended December 31,				
	2016	2015	2014	2013	2012
	(in thousands)				
<b>Consolidated Statement of Operations Data:</b>					
Revenue	\$ 230,003	\$ 198,955	\$ 179,507	\$ 141,738	\$ 120,066
Cost of revenue	\$ 54,910	\$ 48,768	\$ 42,937	\$ 33,396	\$ 24,510
Gross profit	\$ 175,093	\$ 150,187	\$ 136,570	\$ 108,342	\$ 95,556
Loss from operations	\$ (19,119)	\$ (38,446)	\$ (30,271)	\$ (22,843)	\$ (87,020)
Net loss attributable to common stockholders	\$ (20,940)	\$ (40,034)	\$ (35,870)	\$ (29,078)	\$ (90,150)
<b>Consolidated Balance Sheet Data:</b>					
Cash, cash equivalents and marketable securities	\$ 114,347	\$ 98,117	\$ 91,905	\$ 20,793	\$ 23,867
Working capital (deficit)	\$ 98,599	\$ 91,413	\$ 100,656	\$ 15,122	\$ (61,460)
Total assets	\$ 221,338	\$ 192,551	\$ 186,980	\$ 93,794	\$ 76,794
Total debt	\$ —	\$ —	\$ —	\$ 20,000	\$ 5,631
Deferred revenue, net - current and non-current	\$ 92,908	\$ 72,804	\$ 57,220	\$ 41,232	\$ 27,707
Redeemable convertible preferred stock	\$ —	\$ —	\$ —	\$ 81,426	\$ —
Convertible preferred stock	\$ —	\$ —	\$ —	\$ 44,749	\$ 41,737
Total stockholders' equity (deficit)	\$ 86,066	\$ 80,068	\$ 96,565	\$(134,880)	\$(111,892)

## ITEM 7. 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 Item 6. "Selected Financial Data," our consolidated financial statements and related notes included elsewhere in this document. In addition to historical information, the discussion below contains certain forward-looking statements that involve risks and uncertainties. These forward-looking statements include, but are not limited to, those matters discussed under the heading "Forward-looking Statements." Our actual results could differ materially from those anticipated by these forward-looking statements due to various factors, including, but not limited to, those set forth under Item 1A. Risk Factors in this Annual Report on Form 10-K and elsewhere in this document.*

### Overview

We are a leading provider of software and hardware solutions designed to address our customers' needs for secure application services. Our solutions enable our customers to secure and optimize the performance of their data center and cloud applications and secure their users, applications and infrastructure from internet, web and network threats at scale. We deliver a broad portfolio of hardware, software, and cloud offerings to our customers. These solutions are designed to give customers the visibility, performance, and security their applications need across both on-premise and cloud environments to produce greater agility for their businesses. Our customers include cloud providers, web-scale companies, service providers, government organizations and enterprises.

Our product portfolio seeks to address many of the aforementioned challenges and solution requirements. The portfolio consists of six advanced application delivery and security products; ADC, Lightning ADS, CGN, TPS, SSLi and CFW. They are available in a variety of form factors, such as optimized hardware appliances, bare metal software, virtual appliances, and cloud-native software. These choices make our portfolio among the most comprehensive in the industry.

We derive revenue from sales of products and related support services. Products revenue is generated primarily by sales of hardware appliances with perpetual licenses to our embedded software solutions. We also derive revenue from licenses to, or subscription services for, software-only versions of our solutions. We generate services revenue primarily from sales of maintenance and support contracts. Our customers predominantly purchase maintenance and support in conjunction with purchases of our products. In addition, we also derive revenue from the sale of professional services.

We sell our products globally to service providers and enterprises that depend on data center applications and networks to generate revenue and manage operations efficiently. Our end-customers operate in a variety of industries, including telecommunications, technology, industrial, government, retail, financial, gaming, education and government. Since inception, our customer base has grown rapidly. As of December 31, 2016, we had sold products to more than approximately 5,400 customers across 82 countries.

We sell substantially all of our solutions through our high-touch sales organization as well as distribution channel partners, including distributors, value added resellers and system integrators, and fulfill nearly all orders globally through such partners. We believe this sales approach allows us to obtain the benefits of channel distribution, such as expanding our market coverage, while still maintaining face-to-face relationships with our end-customers. We outsource the manufacturing of our hardware products to original design manufacturers. We perform quality assurance and testing at our San Jose, Taiwan and Japan distribution centers, as well as at our manufacturers' locations.

During the year ended December 31, 2016, 52% of our total revenue was generated from the United States, 23% from Japan and 25% from other geographical regions. During the year ended December 31, 2015, 54% of our total revenue was generated from the United States, 18% from Japan and 28% from other geographical regions. During 2014, 48% of our total revenue was generated from the United States, 26% from Japan and 26% from other geographical regions.

As a result of the nature of our target market and the current stage of our development, a substantial portion of our revenue comes from a limited number of large customers, including service providers, in any period. During the years ended December 31, 2016, 2015 and 2014, purchases from our ten largest end-customers accounted for approximately 35%, 33% and 37% of our total revenue, respectively. Sales to these large end-customers have typically been characterized by large but irregular purchases with long sales cycles. The timing of these purchases and the delivery of the purchased products are difficult to predict. As a consequence, any acceleration or delay in anticipated product purchases, by or deliveries to, our largest customers could materially impact our revenue and operating results in any quarterly period. This may cause our quarterly revenue and operating results to fluctuate from quarter to quarter and make them difficult to predict.

We had \$29.0 million of cash and cash equivalents and \$85.4 million of marketable securities as of December 31, 2016. Cash generated by operating activities was \$18.8 million in 2016 as compared to \$3.4 million in 2015.

We intend to continue to invest for long-term growth. We have invested and expect to continue to invest in our product development efforts to deliver new products and additional features in our current products to address customer needs. In addition, we expect to continue to expand our global sales and marketing organizations, expand our distribution channel partner programs and increase awareness of our solutions on a global basis. Additionally, we will be investing in general and administrative resources to meet the requirements to operate as a public company. Our investments in growth in these areas may affect our short-term profitability.

## Results of Operations

A summary of our consolidated statements of operations for the years ended December 31, 2016, 2015 and 2014 is as follows (dollars in thousands):

	Years Ended December 31,				Change	
	2016		2015			
	Amount	Percentage of Total Revenue	Amount	Percentage of Total Revenue	Amount	Percent
Revenue:						
Products . . . . .	\$ 153,920	66.9%	\$ 138,301	69.5%	\$ 15,619	11.3%
Services . . . . .	76,083	33.1	60,654	30.5	15,429	25.4%
Total revenue . . . . .	<u>230,003</u>	<u>100.0</u>	<u>198,955</u>	<u>100.0</u>	<u>31,048</u>	<u>15.6%</u>
Cost of revenue:						
Products . . . . .	37,680	16.4	33,096	16.6	4,584	13.9%
Services . . . . .	17,230	7.5	15,672	7.9	1,558	9.9%
Total cost of revenue . . . . .	<u>54,910</u>	<u>23.9</u>	<u>48,768</u>	<u>24.5</u>	<u>6,142</u>	<u>12.6%</u>
Gross profit . . . . .	<u>175,093</u>	<u>76.1</u>	<u>150,187</u>	<u>75.5</u>	<u>24,906</u>	<u>16.6%</u>
Operating expenses:						
Sales and marketing . . . . .	104,360	45.3	104,531	52.5	(171)	(0.2)%
Research and development . . . . .	60,700	26.4	54,843	27.6	5,857	10.7%
General and administrative . . . . .	27,063	11.8	27,055	13.6	8	—%
Litigation expense (benefit) . . . . .	2,089	0.9	2,204	1.1	(115)	(5.2)%
Total operating expenses . . . . .	<u>194,212</u>	<u>84.4</u>	<u>188,633</u>	<u>94.8</u>	<u>5,579</u>	<u>3.0%</u>
Loss from operations . . . . .	<u>(19,119)</u>	<u>(8.3)</u>	<u>(38,446)</u>	<u>(19.3)</u>	<u>19,327</u>	<u>50.3%</u>
Other expense, net:						
Interest expense . . . . .	(424)	(0.2)	(509)	(0.2)	85	16.7%
Interest and other income (expense), net . . . . .	(640)	(0.3)	(332)	(0.2)	(308)	(92.8)%
Total other expense, net . . . . .	<u>(1,064)</u>	<u>(0.5)</u>	<u>(841)</u>	<u>(0.4)</u>	<u>(223)</u>	<u>(26.5)%</u>
Loss before income taxes . . . . .	<u>(20,183)</u>	<u>(8.8)</u>	<u>(39,287)</u>	<u>(19.7)</u>	<u>19,104</u>	<u>48.6%</u>
Provision for income taxes . . . . .	757	0.3	747	0.4	10	1.3%
Net loss . . . . .	<u>\$ (20,940)</u>	<u>(9.1)%</u>	<u>\$ (40,034)</u>	<u>(20.1)%</u>	<u>\$ 19,094</u>	<u>47.7%</u>

	Years Ended December 31,				Change	
	2015		2014			
	Amount	Percentage of Total Revenue	Amount	Percentage of Total Revenue	Amount	Percent
Revenue:						
Products . . . . .	\$ 138,301	69.5%	\$ 134,486	74.9%	\$ 3,815	2.8%
Services . . . . .	60,654	30.5	45,021	25.1	15,633	34.7%
Total revenue . . . . .	<u>198,955</u>	<u>100.0</u>	<u>179,507</u>	<u>100.0</u>	<u>19,448</u>	<u>10.8%</u>
Cost of revenue:						
Products . . . . .	33,096	16.6	31,084	17.3	2,012	6.5%
Services . . . . .	15,672	7.9	11,853	6.6	3,819	32.2%
Total cost of revenue . . . . .	<u>48,768</u>	<u>24.5</u>	<u>42,937</u>	<u>23.9</u>	<u>5,831</u>	<u>13.6%</u>
Gross profit . . . . .	<u>150,187</u>	<u>75.5</u>	<u>136,570</u>	<u>76.1</u>	<u>13,617</u>	<u>10.0%</u>
Operating expenses:						
Sales and marketing . . . . .	104,531	52.5	96,837	54.0	7,694	7.9%
Research and development . . . . .	54,843	27.6	49,903	27.8	4,940	9.9%
General and administrative . . . . .	27,055	13.6	22,938	12.8	4,117	17.9%
Litigation expense (benefit) . . . . .	2,204	1.1	(2,837)	(1.6)	5,041	(177.7)%
Total operating expenses . . . . .	<u>188,633</u>	<u>94.8</u>	<u>166,841</u>	<u>93.0</u>	<u>21,792</u>	<u>13.1%</u>
Loss from operations . . . . .	<u>(38,446)</u>	<u>(19.3)</u>	<u>(30,271)</u>	<u>(16.9)</u>	<u>(8,175)</u>	<u>(27.0)%</u>
Other expense, net:						
Interest expense . . . . .	(509)	(0.2)	(1,028)	(0.5)	519	50.5%
Interest and other income (expense), net . . . . .	(332)	(0.2)	(1,914)	(1.1)	1,582	82.7%
Total other expense, net . . . . .	<u>(841)</u>	<u>(0.4)</u>	<u>(2,942)</u>	<u>(1.6)</u>	<u>2,101</u>	<u>71.4%</u>
Loss before income taxes . . . . .	<u>(39,287)</u>	<u>(19.7)</u>	<u>(33,213)</u>	<u>(18.5)</u>	<u>(6,074)</u>	<u>(18.3)%</u>
Provision for income taxes . . . . .	747	0.4	1,507	0.8	(760)	(50.4)%
Net loss . . . . .	<u>\$ (40,034)</u>	<u>(20.1)%</u>	<u>\$ (34,720)</u>	<u>(19.3)%</u>	<u>\$ (5,314)</u>	<u>(15.3)%</u>

### Revenue

Our products revenue primarily consists of revenue from sales of our hardware appliances upon which our software is installed. Such software includes our ACOS software platform plus one of our ADC, CGN, TPS, SSLi or CFW solutions. Purchase of a hardware appliance includes a perpetual license to the included software. We recognize products revenue at the time of shipment, provided that all other revenue recognition criteria have been met. As a percentage of revenue, our products revenue may vary from quarter to quarter based on, among other things, the timing of orders and delivery of products, cyclicity and seasonality, changes in currency exchange rates and the impact of significant transactions with unique terms and conditions.

We generate services revenue from sales of post contract support (“PCS”), which is bundled with sales of products and professional services. We offer tiered PCS services under renewable, fee-based PCS contracts, primarily including technical support, hardware repair and replacement parts, and software upgrades on a when-and-if-released basis. We recognize services revenue ratably over the term of the PCS contract, which is typically one year, but can be up to five years.

A summary of our total revenue is as follows (dollars in thousands):

	Years Ended December 31,		Change	
	2016	2015	Amount	Percent
Revenue:				
Products . . . . .	\$ 153,920	\$ 138,301	\$ 15,619	11%
Services . . . . .	76,083	60,654	15,429	25%
Total revenue . . . . .	<u>\$ 230,003</u>	<u>\$ 198,955</u>	<u>\$ 31,048</u>	16%
Revenue by geographic location:				
United States . . . . .	\$ 118,750	\$ 106,842	\$ 11,908	11%
Japan . . . . .	52,951	35,636	17,315	49%
Asia Pacific, excluding Japan . . . . .	29,829	23,847	5,982	25%
EMEA . . . . .	23,093	27,193	(4,100)	(15)%
Other . . . . .	5,380	5,437	(57)	(1)%
Total revenue . . . . .	<u>\$ 230,003</u>	<u>\$ 198,955</u>	<u>\$ 31,048</u>	16%

	Years Ended December 31,		Net Change	
	2015	2014	Amount	Percent
Revenue:				
Products . . . . .	\$ 138,301	\$ 134,486	\$ 3,815	3%
Services . . . . .	60,654	45,021	15,633	35%
Total revenue . . . . .	<u>\$ 198,955</u>	<u>179,507</u>	<u>\$ 19,448</u>	11%
Revenue by geographic location:				
United States . . . . .	\$ 106,842	\$ 85,325	\$ 21,517	25%
Japan . . . . .	35,636	45,787	(10,151)	(22)%
Asia Pacific, excluding Japan . . . . .	23,847	20,434	3,413	17%
EMEA . . . . .	27,193	19,254	7,939	41%
Other . . . . .	5,437	8,707	(3,270)	(38)%
Total revenue . . . . .	<u>\$ 198,955</u>	<u>\$ 179,507</u>	<u>\$ 19,448</u>	11%

*2016 Revenue Compared to 2015 Revenue*

Total revenue increased \$31.0 million, or 16%, in 2016 as compared to 2015, which consisted of a \$15.6 million increase in products revenue and a \$15.4 million increase in services revenue. Revenue from enterprise and service provider customers increased 22% and 7%, respectively, in 2016 as compared to 2015.

Products revenue increased \$15.6 million, or 11%, in 2016 as compared to 2015, which is primarily attributable to increases from Japan, Asia Pacific excluding Japan and the United States, partially offset by a decrease from EMEA. Products revenue from enterprise and service provider customers increased 22% and decreased 1%, respectively, in 2016 as compared to 2015. The number of our customers increased to approximately 5,400 in 2016 as compared to 4,700 in 2015.

Services revenue increased \$15.4 million, or 25%, in 2016 as compared to 2015, which is primarily attributable to the increase in PCS sales in connection with our increasing installed customer base as well as an increase in our professional services and subscription revenue. During 2016, services revenue recognized from our installed customer base with contracts existing at the beginning of the year grew by 28% as compared to the same measure in 2015. Services revenue from enterprise and service provider customers increased 23% and 29%, respectively, in 2016 as compared to 2015.

During 2016, \$118.8 million, or 52%, of total revenue was generated from the United States, which represents an 11% increase in revenue as compared to 2015. The increase was primarily due to higher products revenue as well as higher PCS sales in connection with our increased installed customer base.

During 2016, \$53.0 million, or 23%, of total revenue was generated from Japan, which represents a 49% increase in revenue as compared to 2015. The increase was primarily due to higher revenue from service provider customers and expansion to new customers in Japan. In addition, the favorable currency exchange impact of the Japanese yen on products revenue was \$4.5 million during 2016.



During 2016, \$29.8 million, or 13%, of total revenue was generated from the Asia Pacific regions excluding Japan, which represents a 25% increase in revenue as compared to 2015. The increase was primarily due to higher products revenue resulting from our continuous efforts in expanding our presence in these regions as well as higher PCS sales in connection with our increased installed customer base.

During 2016, \$23.1 million, or 10%, of total revenue was generated from EMEA, which represents a 15% decrease in revenue as compared to 2015. The decrease was primarily due to lower products revenue as a result of overall economic weakness and uncertainty in the EMEA markets as well as personnel turnover in our Middle East operations, partially offset by an increase in services revenue.

#### *2015 Revenue Compared to 2014 Revenue*

Total revenue increased \$19.4 million, or 11%, in 2015 as compared to 2014, which consisted of a \$3.8 million increase in products revenue and a \$15.6 million increase in services revenue.

Products revenue increased \$3.8 million, or 3%, in 2015 as compared to 2014, which is primarily attributable to increases from the United States, EMEA and Asia Pacific excluding Japan, partially offset by a decrease from Japan. In 2014, our products revenue from Japan was positively impacted by a higher backlog entering the year that resulted from strong demand for our products in Japan in the fourth quarter of 2013. In addition, Japan's revenue was more adversely impacted by the unfavorable currency exchange impact of the Japanese yen in 2015 as compared to 2014. Product revenue from enterprise customers and service provider customers increased 4% and 2%, respectively, in 2015 as compared to 2014.

Services revenue increased \$15.6 million, or 35%, in 2015 as compared to 2014, which is primarily attributable to the increase in PCS sales in connection with our increasing installed customer base as well as increases in our professional services revenue. During 2015, services revenue recognized from our installed customer base with contracts existing at the beginning of the year grew by 41% as compared to the same measure in 2014. Services revenue from enterprise and service provider customers increased 42% and 25%, respectively, in 2015 as compared to 2014.

During 2015, \$106.8 million, or 54% of total revenue was generated from the United States, which represents a 25% increase as compared to 2014. The increase was primarily attributable to higher products revenue from service provider customers as well as higher PCS sales in connection with our increased installed customer base.

During 2015, \$35.6 million, or 18%, of total revenue was generated from Japan, which represents a 22% decrease as compared to 2014. In 2014, our products revenue from Japan was positively impacted by a higher backlog entering the year that resulted from strong demand in the fourth quarter of 2013. The decrease in products revenue was partially offset by an increase in services revenue. In addition, Japan's revenue was adversely impacted by the unfavorable currency exchange impact of the Japanese yen in 2015 as compared to 2014.

During 2015, \$23.8 million, or 12%, of total revenue was generated from the Asia Pacific regions excluding Japan, which represents a 17% increase as compared to 2014. During 2015, \$27.2 million, or 14%, of total revenue was generated from EMEA, which represents a 41% increase as compared to 2014. These increases were primarily due to our efforts in expanding our presence in these regions.

#### ***Cost of Revenue, Gross Profit and Gross Margin***

##### *Cost of revenue*

Cost of products revenue is primarily comprised of cost of third-party manufacturing services and cost of component inventory for the hardware component of our products. Cost of products revenue also includes warehouse personnel costs, shipping costs, inventory write-downs, certain allocated facilities and information technology infrastructure costs, and expenses associated with logistics and quality control.

Cost of services revenue is primarily comprised of personnel costs for our technical support, training and professional service teams. Cost of services revenue also includes the costs of inventory used to provide hardware replacements to end- customers under PCS contracts and certain allocated facilities and information technology infrastructure costs.

A summary of our cost of revenue is as follows (dollars in thousands):

	Years Ended December 31,		Change	
	2016	2015	Amount	Percent
Cost of revenue:				
Products . . . . .	\$ 37,680	\$ 33,096	\$ 4,584	14%
Services . . . . .	17,230	15,672	1,558	10%
Total cost of revenue . . . . .	<u>\$ 54,910</u>	<u>\$ 48,768</u>	<u>\$ 6,142</u>	13%

	Years Ended December 31,		Change	
	2015	2014	Amount	Percent
Cost of revenue:				
Products . . . . .	\$ 33,096	\$ 31,084	\$ 2,012	6%
Services . . . . .	15,672	11,853	3,819	32%
Total cost of revenue . . . . .	<u>\$ 48,768</u>	<u>\$ 42,937</u>	<u>\$ 5,831</u>	14%

**Gross Margin**

Gross margin may vary and be unpredictable from period to period due to a variety of factors. These may include the mix of revenue from each of our regions, the mix of our products sold within a period, discounts provided to customers, inventory write-downs and foreign currency exchange rates.

Our sales are generally denominated in U.S. dollars, however, in Japan they are denominated in Japanese yen. Changes in the exchange rates between the U.S. dollar and Japanese yen will therefore affect our revenue and gross margin.

Any of the factors noted above can generate either a favorable or unfavorable impact on gross margin.

A summary of our gross profit and gross margin is as follows (dollars in thousands):

	Years Ended December 31,				Change	
	2016		2015		Amount	Gross Margin
	Amount	Gross Margin	Amount	Gross Margin		
Gross profit:						
Products . . . . .	\$ 116,240	75.5%	\$ 105,205	76.1%	\$ 11,035	(0.6)%
Services . . . . .	58,853	77.4%	44,982	74.2%	13,871	3.2%
Total gross profit . . . . .	<u>\$ 175,093</u>	76.1%	<u>\$ 150,187</u>	75.5%	<u>\$ 24,906</u>	0.6%

	Years Ended December 31,				Change	
	2015		2014		Amount	Gross Margin
	Amount	Gross Margin	Amount	Gross Margin		
Gross profit:						
Products . . . . .	\$ 105,205	76.1%	\$ 103,402	76.9%	\$ 1,803	(0.8)%
Services . . . . .	44,982	74.2%	33,168	73.7%	11,814	0.5%
Total gross profit . . . . .	<u>\$ 150,187</u>	75.5%	<u>\$ 136,570</u>	76.1%	<u>\$ 13,617</u>	(0.6)%

**2016 Gross Margin to 2015 Gross Margin**

Products gross margin decreased by 0.6% in 2016 as compared to 2015 primarily due to higher inventory reserve for excess and obsolete products, partially offset by improved geographic revenue mix. We had more sales from geographic regions and products with higher gross margins in 2016 as compared to 2015.

Services gross margin increased by 3.2% in 2016 as compared to 2015 primarily due to higher services revenue while the personnel costs related to support, professional services and maintenance remained relatively constant.

## 2015 Gross Margin to 2014 Gross Margin

Products gross margin decreased by 0.8% in 2015 as compared to 2014 primarily due to the unfavorable currency exchange impact of the Japanese Yen, partially offset by improved geographic sales mix. We had more sales from geographic regions and products with higher gross margins in 2015 as compared to 2014.

Services gross margin increased by 0.5% in 2015 as compared to 2014 primarily due to higher services revenue while the personnel costs related to support, professional services and maintenance increased only modestly.

### **Operating Expenses**

Our operating expenses consist of sales and marketing, research and development, general and administrative and litigation expenses. The largest component of our operating expenses is personnel costs which consist of wages, benefits, bonuses, and, with respect to sales and marketing expenses, sales commissions. Personnel costs also include stock-based compensation. We expect our personnel costs to increase as our business continues to grow and we hire new employees.

A summary of our operating expenses is as follows (dollars in thousands):

	Years Ended December 31,		Change	
	2016	2015	Amount	Percent
Operating expenses:				
Sales and marketing . . . . .	\$ 104,360	\$ 104,531	\$ (171)	—%
Research and development . . . . .	60,700	54,843	5,857	11%
General and administrative . . . . .	27,063	27,055	8	—%
Litigation expense . . . . .	2,089	2,204	(115)	(5)%
Total operating expenses . . . . .	<u>\$ 194,212</u>	<u>\$ 188,633</u>	<u>\$ 5,579</u>	3%

	Years Ended December 31,		Change	
	2015	2014	Amount	Percent
Operating expenses:				
Sales and marketing . . . . .	\$ 104,531	\$ 96,837	\$ 7,694	8%
Research and development . . . . .	54,843	49,903	4,940	10%
General and administrative . . . . .	27,055	22,938	4,117	18%
Litigation expense (benefit) . . . . .	2,204	(2,837)	5,041	178%
Total operating expenses . . . . .	<u>\$ 188,633</u>	<u>\$ 166,841</u>	<u>\$ 21,792</u>	13%

### **Sales and Marketing**

Sales and marketing expenses are our largest functional category of operating expenses and primarily consist of personnel costs. Sales and marketing expenses also include the cost of marketing programs, trade shows, consulting services, promotional materials, demonstration equipment, depreciation and certain allocated facilities and information technology infrastructure costs.

Sales and marketing expenses remained relatively unchanged in 2016 as compared to 2015 as a \$0.9 million decrease in depreciation expense, a \$0.8 million decrease in contractors and consultants fees and \$0.7 million decrease in recruiting fees were partially offset by a \$1.9 million increase in personnel costs due to higher headcount and commissions, and a \$0.3 million increase in rent for sales offices.

Sales and marketing expenses increased \$7.7 million, or 8%, in 2015 as compared to 2014 primarily attributable to an \$8.1 million increase in personnel costs and a \$0.7 million increase in company meeting expenses. The increase in personnel costs, which includes a \$4.5 million increase in sales commission and a \$1.9 million increase in stock-based compensation, was primarily attributable to higher headcount and higher bonus and sales commissions. The increase was partially offset by a \$1.1 million decrease in trade show and market development costs.

We expect our sales and marketing expenses to increase in the future as we expand our sales presence in existing countries and into new countries.

### **Research and Development**

Research and development efforts are focused on new product development and on developing additional functionality for our existing products. These expenses primarily consist of personnel costs, and, to a lesser extent, prototype materials, depreciation and certain allocated facilities and information technology infrastructure costs. We expense research and development costs as incurred.

Research and development expenses increased \$5.9 million, or 11%, in 2016 as compared to 2015. This increase was primarily due to a \$4.5 million increase in personnel costs due to higher headcount and impact from the acquisition of Appcito, a \$0.6 million increase in amortization expense mainly due to purchased intangibles from the acquisition of Appcito and a \$0.6 million increase in professional services.

Research and development expenses increased \$4.9 million, or 10%, in 2015 as compared to 2014 primarily attributable to a \$6.5 million increase in personnel costs, which includes a \$1.5 million increase in stock-based compensation. The increase in personnel costs was primarily attributable to higher salaries and benefits and to a lesser extent higher headcount in 2015 as compared to 2014. The increase was partially offset by a \$0.7 million decrease in professional services due to lower product certification related activities and a \$0.8 million decrease in depreciation expense.

We expect our research and development expenses to increase in the future as we continue to develop new products and enhance our existing products.

### ***General and Administrative***

General and administrative expenses primarily consist of personnel costs, professional services and office expenses. General and administrative personnel costs include executive, finance, human resources, information technology, facility and legal (excluding litigation) related expenses. Professional services primarily consist of fees for outside accounting, tax, legal, recruiting and other administrative services.

General and administrative expenses remained relatively unchanged in 2016 as compared to 2015 as a \$2.8 million increase in personnel costs was partially offset by a \$1.6 million decrease in contractors and consultants fees, a \$0.5 million decrease in professional services, a \$0.4 million decrease in bad debt expense and a \$0.2 million decrease in depreciation expense.

General and administrative expenses increased \$4.1 million, or 18% in 2015 as compared to 2014 primarily attributable to a \$3.1 million increase in personnel costs due to higher headcount and a \$1.5 million increase in bad debt expense. The increase was partially offset by a \$0.8 million decrease in sales and use tax expense due to adjustments related to reassessment of previously accrued sales and use tax liabilities.

We expect general and administrative expenses to increase in the future.

### ***Litigation Expense (Benefit)***

Litigation expense (benefit) is comprised of legal expenses incurred related to litigation and, if applicable, charges for litigation reserves. Litigation expenses consist of professional fees incurred in defending ourselves against litigation matters and are expensed as incurred when professional services are provided. The litigation reserve, if any, consists of accruals we make related to estimated losses in pending legal proceedings. Litigation reserves, if any, are adjusted as we change our estimates or make payments in damages or settlements.

Litigation expense decreased \$0.1 million in 2016 as compared to 2015 due to fewer litigation-related activities following the agreements to settle the Class Action and the Derivative Action lawsuits in 2016.

Litigation expense increased \$5.0 million from \$2.8 million litigation benefit in 2014 to \$2.2 million litigation expense in 2015. The litigation benefit of \$2.8 million in 2014 was due to a \$7.0 million reduction of previously accrued contractual liability following a settlement agreement with one of our legal services providers. Other litigation expense decreased by \$2.0 million in 2015 as compared to 2014 mainly due to a reduction in litigation related activities.

### ***Interest Expense***

Interest expense consists primarily of interest expense and amortization of debt issuance costs. At December 31, 2016 and 2015, we had no outstanding balances on our credit facility. We expect to continue to incur commitment fees associated with the undrawn balance of our credit facility. At such time we choose to draw down on the credit facility, we would reduce the commitment fees accrued and increase the interest on outstanding balances.

Interest expense remained relatively unchanged in 2016 as compared to 2015.

Interest expense decreased \$0.5 million in 2015 as compared to 2014, primarily due to lower borrowing related activities in 2015 as compared to 2014. During 2014, we recorded a \$0.3 million contingent payment due to a lender upon completion of our initial public offering and \$0.2 million of interest expense related to our revolving credit facility. We completed our initial public offering and repaid the outstanding balance under our revolving credit facility in March 2014.

### ***Interest and Other Income (Expense), Net***

Interest income consists primarily of interest income earned on our cash and cash equivalents and marketable securities. Other income (expense) consists primarily of foreign currency exchange gains and losses.

Interest and other income (expense), net, increased by \$0.3 million in 2016 as compared to 2015 primarily due to a \$1.0 million increase in foreign exchange losses, partially offset by a \$0.8 million increase in interest income attributable to increases in our investment in marketable securities.

Interest and other income (expense), net, decreased by \$1.6 million in 2015 as compared to 2014 primarily due to a \$1.4 million decrease in foreign exchange losses.

### ***Provision for Income Taxes***

We recorded income tax provision of \$0.8 million, \$0.7 million and \$1.5 million for the years ended December 31, 2016, 2015 and 2014, respectively. Our provision for income taxes consists primarily of income and withholding taxes in foreign jurisdictions in which we conduct business, state income taxes in the United States and the effect of unrecognized tax benefits. We estimate income taxes in each of the jurisdictions in which we operate. This process involves determining income tax expense together with calculating the deferred income tax expense related to temporary differences resulting from the differing treatment of items for tax and accounting purposes. We maintain a full valuation allowance against our U.S. deferred tax assets as management does not believe that it is more likely than not that the said deferred taxes will be realized. As a result, our provision for income taxes primarily relates only to foreign taxes at this time.

### **Liquidity and Capital Resources**

As of December 31, 2016, we had cash and cash equivalents of \$29.0 million, including approximately \$3.7 million held outside the United States in our foreign subsidiaries, and \$85.4 million of marketable securities. We currently do not have any plans to repatriate our earnings from our foreign operations. As of December 31, 2016, we had working capital of \$98.6 million, an accumulated deficit of \$242.8 million and total stockholders' equity of \$86.1 million.

We plan to continue to invest for long-term growth and anticipate our investment will continue to increase. We believe that our existing cash and cash equivalents, marketable securities and other available financial resources will be sufficient to meet our anticipated cash needs for at least the next 12 months. Our future capital requirements will depend on many factors, including our growth rate, the expansion of sales and marketing activities, the timing and extent of spending to support development efforts, the introduction of new and enhanced product and service offerings and the continuing market acceptance of our products. In the event that additional financing is required from outside sources, we may not be able to raise such financing on terms acceptable to us or at all. If we are unable to raise additional capital when desired, our business, operating results and financial condition could be adversely affected.

On October 27, 2016, we announced that our board of directors authorized a share repurchase program for up to \$20.0 million of our common stock over the next 12 months. Under the repurchase authorization, shares may be purchased from time to time, subject to general business and market conditions and other investment opportunities, through open market purchases, privately negotiated transactions or other means. The repurchase authorization may be commenced, suspended or discontinued at any time at our discretion. Since the authorization and through December 31, 2016, we repurchased 226,676 shares at a weighted average effective price of \$7.92 per share and used approximately \$1.8 million of cash.

In addition, as described in *Note 5. Commitments and Contingencies* to the consolidated financial statements, we are currently, or may be from time to time be, involved in ongoing litigation. Any adverse settlements or judgments in any litigation could have a material adverse impact on our results of operations, cash balances and cash flows in the period in which such events occur.

### ***Credit Facilities***

In September 2013, we entered into a credit agreement with Royal Bank of Canada, acting as administrative agent and lender, and JPMorgan Chase Bank, N.A. and Bank of America, N.A. as lenders (the "2013 Credit Facility"). The 2013 Credit Facility provided a three-year \$35.0 million revolving credit facility, which included a maximum \$10.0 million letter of credit facility. The 2013 Credit Facility expired on September 30, 2016.

In November 2016, we entered into the 2016 Credit Facility with SVB, as the lender. The 2016 Credit Facility provides a three-year, \$25.0 million revolving credit facility, which includes a maximum of \$25.0 million letter of credit subfacility. When our net cash equals or exceeds \$50.0 million, loans may be advanced under the 2016 Credit Facility up to the full \$25.0 million. When our net cash falls below \$50.0 million, loans may be advanced under the 2016 Credit Facility based on a borrowing base equal to a specified percentage of the value of the our eligible accounts receivable. The loans bear interest, at our option, at (i) the prime rate reported in The Wall Street Journal, minus 0.50% or (ii) a LIBOR rate determined in accordance with the 2016 Credit Facility, plus 2.50%.



Our obligations under the 2016 Credit Facility are secured by substantially all of our assets, excluding our intellectual property. The 2016 Credit Facility contains customary affirmative and negative covenants, in each case subject to customary exceptions, and customary events of default. In addition, the 2016 Credit Facility requires us to maintain compliance with an adjusted quick ratio of not less than 1.50:1.00, as determined in accordance with the 2016 Credit Facility. As of December 31, 2016, we had no outstanding balance under the 2016 Credit Facility and were in compliance with all facility covenants.

### ***Statements of Cash Flows***

The following table summarizes our cash flow related activities (in thousands):

	<b>Years Ended December 31,</b>		
	<b>2016</b>	<b>2015</b>	<b>2014</b>
Cash provided by (used in):			
Operating activities . . . . .	\$ 18,778	\$ 3,391	\$ (30,538)
Investing activities . . . . .	(96,355)	(3,477)	(6,100)
Financing activities . . . . .	8,435	6,298	107,750
Net increase (decrease) in cash and cash equivalents . . . . .	<u>\$ (69,142)</u>	<u>\$ 6,212</u>	<u>\$ 71,112</u>

### ***Cash Flows from Operating Activities***

Our cash provided by (used in) operating activities is driven primarily by sales of our products and management of working capital investments. Our primary uses of cash from operating activities have been for personnel-related expenditures, manufacturing costs, marketing and promotional expenses, costs related to our facilities and litigation expenses. Our cash flows from operating activities will continue to be affected principally by the extent to which we increase spending on our business, our working capital requirements, and litigation expenses.

During the year ended December 31, 2016, cash provided by operating activities was \$18.8 million, consisting of a net loss of \$20.9 million, cash increase resulting from the net change in operating assets and liabilities of \$11.9 million and non-cash charges of \$27.8 million. Our non-cash charges consisted primarily of stock-based compensation of \$16.9 million, depreciation and amortization of \$8.3 million and provision for doubtful accounts and sales returns allowance of \$1.7 million. The net change in our operating assets and liabilities primarily reflect an inflow from the changes in deferred revenue of \$20.1 million, accrued liabilities of \$3.1 million and inventory of \$0.9 million, and an outflow from the change in accounts receivable of \$11.3 million.

The increase in deferred revenue was primarily due to increased PCS sales in connection with higher installed customer base. The increase in accrued liabilities was primarily due to higher commissions accrual. The decrease in inventory was primarily due to improved management of inventory balances and increased inventory reserves. The increase in accounts receivable was primarily due to higher revenues.

During the year ended December 31, 2015, cash provided by operating activities was \$3.4 million, consisting of a net loss of \$40.0 million, cash increase resulting from the net change in operating assets and liabilities of \$15.4 million and non-cash charges of \$28.0 million. Our non-cash charges consisted primarily of stock-based compensation of \$16.9 million, depreciation and amortization of \$8.7 million and provision for doubtful accounts and sales returns allowance of \$2.5 million. Net change in our operating assets and liabilities primarily reflect an inflow from the changes in deferred revenue of \$15.6 million, accounts payable and accrued liabilities of \$6.5 million, and an outflow from the change in accounts receivable of \$6.0 million.

During the year ended December 31, 2014, cash used in operating activities was \$30.5 million, consisting of a net loss of \$34.7 million, cash decrease resulting from the net change in operating assets and liabilities of \$12.2 million and non-cash charges of \$16.4 million. Our non-cash charges consisted primarily of stock-based compensation of \$12.4 million and depreciation and amortization of \$10.1 million, partially offset by gain on the settlement of a contractual liability \$7.0 million which represents a reduction of a previously accrued contractual liability. The net change in our operating assets and liabilities primarily reflect an outflow from the changes in accounts receivable of \$17.3 million, inventory of \$8.9 million, accrued litigation of \$6.1 million and prepaid expense and other current assets of \$3.0 million, and an inflow from the changes in deferred revenue of \$16.0 million and accounts payable and accrued liabilities of \$7.6 million.

### ***Cash Flows from Investing Activities***

During the year ended December 31, 2016, cash used in investing activities was \$96.4 million, primarily consisting of \$85.6 million of net purchases of marketable securities, \$4.9 million for purchases of property and equipment, \$4.4 million for payment for the acquisition of Appcito and \$1.5 million for purchase of intangible assets.

During the years ended December 31, 2015 and 2014, cash used in investing activities was \$3.5 million and \$6.1 million, respectively, for purchases of property and equipment.

### ***Cash Flows from Financing Activities***

During the year ended December 31, 2016, cash provided by financing activities was \$8.4 million, primarily consisting of proceeds from common stock of issuances of \$10.3 million related to the exercise of stock options and our employee stock purchase plan, partially offset by the stock repurchase of \$1.8 million.

During the year ended December 31, 2015, cash provided by financing activities was \$6.3 million, primarily consisting of proceeds from common stock issuances under our equity incentive plans, net of repurchases of common stock.

During the year ended December 31, 2014, cash provided by financing activities was \$107.8 million, primarily consisting of net proceeds from the issuance of our common stock to outside investors in our IPO of \$121.0 million and proceeds from common stock issuance under our equity incentive plans of \$7.0 million, partially offset by the repayment of our revolving credit facility of \$20.0 million.

### ***Contractual Obligations***

Our contractual obligations consist of capital leases, operating leases, purchase commitments, and other contractual obligations.

The following table summarizes our contractual obligations as of December 31, 2016 (in thousands):

	<u>Total</u>	<u>Less Than 1 Year</u>	<u>1 to 3 Years</u>	<u>3 to 5 Years</u>	<u>More than 5 years</u>
Leases and Other Contractual Obligations . . . . .	\$ 7,647	\$ 2,811	\$ 4,385	\$ 444	\$ 7
Purchase Commitments . . . . .	14,900	14,900	—	—	—
	<u>\$ 22,547</u>	<u>\$ 17,711</u>	<u>\$ 4,385</u>	<u>\$ 444</u>	<u>\$ 7</u>

The contractual obligations table above excludes \$3.3 million of tax liabilities related to uncertain tax positions because we are unable to make a reasonably reliable estimate of the timing of settlement, if any, of these future payments.

### ***Off-Balance Sheet Arrangements***

As of December 31, 2016, we did not have any relationships with any unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities that would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

### ***Critical Accounting Policies and Estimates***

Our consolidated financial statements are prepared in accordance with generally accepted accounting principles in the United States. The preparation of these consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, expenses and related disclosures. We evaluate our estimates and assumptions on an ongoing basis. Our estimates are based on historical experience and various other assumptions that we believe to be reasonable under the circumstances. Our actual results could differ from these estimates.

We believe the following critical accounting policies require us to make significant judgments and estimates in the preparation of our consolidated financial statements.

#### ***Allowance for Doubtful Accounts***

We maintain an allowance for doubtful accounts for estimated losses in the collection of accounts receivable. We evaluate the collectability of our accounts receivable based on known collection risks and historical experience. In circumstances where we are aware of a specific customer's inability to meet its financial obligations to us (e.g., bankruptcy filings or substantial downgrading of credit ratings), we record a specific reserve for bad debts against amounts due to reduce the net recognized receivable to the amount we reasonably believe will be collected. For all other customers, we record reserves for bad debts based on the length of time the receivables are past due and our historical experience of collections and write-offs.

## ***Inventory***

Inventory consists primarily of finished goods and related component parts and is stated at the lower of standard cost (which approximates actual cost on a first-in, first-out basis) or market value (estimated net realizable value). We evaluate inventory for excess and obsolete products, based on management's assessment of future demand and market conditions. Inventory write-downs, once established, are not reversed as they establish a new cost basis for the inventory. Inventory write downs are included as a component of cost of products revenue in the accompanying consolidated statements of operations.

## ***Revenue Recognition***

We derive revenue from two sources: (i) products revenue, which includes hardware and perpetual software license revenue; and (ii) services revenue, which include post contract support ("PCS"), professional services, and training. A substantial portion of our revenue is from sales of our products and services through distribution channel partners, such as resellers and distributors. Revenue is recognized, net of applicable taxes, when all of the following criteria are met: persuasive evidence of an arrangement exists, delivery or performance has occurred, the sales price is fixed or determinable, and collection is reasonably assured.

We define each of the four criteria above as follows:

- ***Persuasive evidence of an arrangement exists.*** Evidence of an arrangement consists of a purchase order issued pursuant to the terms and conditions of a master sales agreement.
- ***Delivery or performance has occurred.*** We use shipping documents or written evidence of customer acceptance, when applicable, to verify delivery or performance. We recognize product revenue upon transfer of title and risk of loss, which primarily is upon shipment to customers. We do not have significant obligations for future performance, such as customer acceptance provisions, rights of return, or pricing credits, associated with our sales.
- ***The sales price is fixed or determinable.*** We assess whether the sales price is fixed or determinable based on payment terms and whether the sales price is subject to refund or adjustment. Standard payment terms to customers range from 30 to 90 days.
- ***Collection is reasonably assured.*** We assess probability of collection on a customer-by-customer basis. Our customers are subjected to a credit review process that evaluates their financial condition and ability to pay for products and services.

PCS revenue includes arrangements for software support and technical support for our products. PCS is offered under renewable, fee-based contracts, which include technical support, hardware repair and replacement parts, bug fixes, patches, and unspecified upgrades on a when-and-if available basis. Revenue for PCS services is recognized on a straight-line basis over the service contract term, which is typically one year, but can be up to five years. Unearned PCS revenue is included in deferred revenue.

Professional service revenue primarily consists of the fees we earn related to installation and consulting services. We recognize revenue from professional services upon delivery or completion of performance. Professional service arrangements are typically short term in nature and are largely completed within 30 to 90 days from the start of service.

## ***Multiple-Element Arrangements***

Our hardware with the embedded software solutions (which is a proprietary operating system that together with the hardware delivers the functionality desired by our customers), is considered a separate unit of accounting from PCS because it has value to the customer on a standalone basis and our sales arrangements do not include a right of return for delivered products. For multiple-element arrangements, we allocate revenue to each unit of accounting based on an estimated selling price at the inception of the arrangement. The total arrangement consideration is allocated to each separate unit of accounting using the relative selling price method. We limit the amount of revenue recognized for delivered elements to an amount that is not contingent upon future delivery of additional products or service.

When applying the relative selling price method, we determine the selling price for each element using (i) vendor-specific objective evidence, or VSOE, of selling price, if available; (ii) third-party evidence, or TPE, of selling price, if VSOE is not available; and (iii) best estimate of selling price, or BEBP, if neither VSOE nor TPE is available.

- ***VSOE.*** We determine VSOE based on our historical pricing and discounting practices for the specific products and services when sold separately. In determining VSOE, we require that a substantial majority of the stand-alone selling prices fall within a reasonably narrow pricing range.
- ***TPE.*** When VSOE cannot be established for deliverables in multiple-element arrangements, we apply judgment with respect to whether we can establish a selling price based on TPE. TPE is determined based on competitor prices for interchangeable products or services when sold separately to similarly situated customers. However, as our products contain a significant

element of proprietary technology and our solutions offer substantially different features and functionality, the comparable pricing of products with similar functionality typically cannot be obtained. Additionally, as we are unable to reliably determine what competitors products' selling prices are on a stand-alone basis, we are not typically able to determine TPE.

- **BESP.** When we are unable to establish selling price using VSOE or TPE, we use BESP in our allocation of arrangement consideration.

The objective of BESP is to determine the price at which we would transact a sale if the product or service was sold regularly on a standalone basis. As we have not been able to establish VSOE or TPE for our products and some of our services, we determine BESP for the purposes of allocating the arrangement, primarily based on historical transaction pricing. Historical transactions are segregated based on our pricing model and go-to-market strategy, which include factors such as the geographies in which our products and services were sold (domestic or international), offering type (product series, and level of support for PCS) and type of sales channel. The determination of BESP is made through consultation with and approval by management.

We may occasionally accept returns to address customer satisfaction issues or solution-fit issues even though there is no contractual provision for such returns. We estimate returns for sales to customers based on historical returns rates applied against current-period gross revenues. Specific customer returns and allowances are considered within this estimate. Management also analyzes changes in customer demand and acceptance of products when evaluating the adequacy of returns and sales allowances.

### ***Stock-Based Compensation***

Stock-based compensation expense is measured on the grant date based on the fair value of the award, net of estimated forfeitures, and recognized on a straight-line basis over the requisite service period. The fair value of restricted stock units ("RSUs") is estimated using our stock price on the grant date. The fair value of options and employee stock purchase rights is estimated using the Black-Scholes model on the grant date. The Black-Scholes model determines the fair value of share-based payment awards based on assumptions including expected term, stock price volatility, and risk-free interest rate. The fair value of market-performance based restricted stock units ("MSUs") is valued using the Monte Carlo simulation model, which uses the stock price, expected volatility and risk-free interest rate to determine the fair value.

### ***Income Taxes***

We account for income taxes using the asset and liability method, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been recognized in our consolidated financial statements or in our tax returns. Estimates and judgments occur in the calculation of certain tax liabilities and in the determination of the recoverability of certain deferred income tax assets, which arise from temporary differences and carryforwards. Deferred income tax assets and liabilities are measured using the currently enacted tax rates that apply to taxable income in effect for the years in which those tax assets are expected to be realized or settled. We regularly assess the likelihood that our deferred tax assets will be recovered from future taxable income and, to the extent we believe, based upon the weight of available evidence, that it is more likely than not that all or a portion of deferred tax assets will not be realized, a valuation allowance is established through an adjustment to income tax expense.

The factors used to assess the likelihood of realization of our deferred tax assets include our forecast of future taxable income and available tax planning strategies that could be implemented to realize the net deferred tax assets. Assumptions represent our best estimates and involve inherent uncertainties and the application of our judgment.

We account for uncertainty in income taxes recognized in our consolidated financial statements by regularly reviewing our tax positions and benefits to be realized. We recognize tax liabilities based upon our estimate of whether, and the extent to which, additional taxes will be due when such estimates are more-likely-than-not to be sustained. An uncertain income tax position will not be recognized if it has less than a 50% likelihood of being sustained upon examination by taxing authorities. The provision for income taxes includes the effects of any resulting tax reserves, or unrecognized tax benefits, that are considered appropriate as well as the related net interest and penalties.

### **Recent Accounting Pronouncements**

Information with respect to recent accounting pronouncements may be found in Note 1. *Description of Business and Summary of Significant Accounting Policies* in the notes to the consolidated financial statements included in this Annual Report on Form 10-K, which section is incorporated herein by reference.

**Supplementary Financial Information**

*Selected Quarterly Financial Data (unaudited, in thousands)*

	For the Three Months Ended			
	March 31, 2016	June 30, 2016	September 30, 2016	December 31, 2016
Revenue:				
Products .....	\$ 36,374	\$ 38,797	\$ 35,275	\$ 43,474
Services .....	17,430	18,333	19,793	20,527
Total revenue .....	<u>53,804</u>	<u>57,130</u>	<u>55,068</u>	<u>64,001</u>
Cost of revenue:				
Products .....	8,698	9,804	8,795	10,383
Services .....	4,529	4,405	4,153	4,143
Total cost of revenue .....	<u>13,227</u>	<u>14,209</u>	<u>12,948</u>	<u>14,526</u>
Gross profit .....	<u>40,577</u>	<u>42,921</u>	<u>42,120</u>	<u>49,475</u>
Operating expenses:				
Sales and marketing .....	26,768	26,773	24,331	26,488
Research and development .....	14,777	14,486	15,968	15,469
General and administrative .....	6,661	7,230	6,305	6,867
Litigation expense .....	1,791	202	66	30
Total operating expenses .....	<u>49,997</u>	<u>48,691</u>	<u>46,670</u>	<u>48,854</u>
Income (loss) from operations .....	<u>(9,420)</u>	<u>(5,770)</u>	<u>(4,550)</u>	<u>621</u>
Other income (expense), net:				
Interest expense .....	(126)	(126)	(145)	(27)
Interest and other income (expense), net .....	215	1,020	309	(2,184)
Total other income (expense), net .....	<u>89</u>	<u>894</u>	<u>164</u>	<u>(2,211)</u>
Loss before provision for income taxes .....	<u>(9,331)</u>	<u>(4,876)</u>	<u>(4,386)</u>	<u>(1,590)</u>
Provision for income taxes .....	204	59	298	196
Net loss .....	<u>\$ (9,535)</u>	<u>\$ (4,935)</u>	<u>\$ (4,684)</u>	<u>\$ (1,786)</u>
Net loss per share - basic and diluted .....	<u>\$ (0.15)</u>	<u>\$ (0.08)</u>	<u>\$ (0.07)</u>	<u>\$ (0.03)</u>



	For the Three Months Ended			
	March 31, 2015	June 30, 2015	September 30, 2015	December 31, 2015
Revenue:				
Products .....	\$ 30,516	\$ 33,331	\$ 34,990	\$ 39,464
Services .....	13,501	14,205	15,788	17,160
Total revenue .....	<u>44,017</u>	<u>47,536</u>	<u>50,778</u>	<u>56,624</u>
Cost of revenue:				
Products .....	7,063	7,909	8,529	9,595
Services .....	3,723	3,692	4,186	4,071
Total cost of revenue .....	<u>10,786</u>	<u>11,601</u>	<u>12,715</u>	<u>13,666</u>
Gross profit .....	<u>33,231</u>	<u>35,935</u>	<u>38,063</u>	<u>42,958</u>
Operating expenses:				
Sales and marketing .....	24,522	24,962	25,774	29,273
Research and development .....	14,309	13,671	13,562	13,301
General and administrative .....	7,527	5,703	6,892	6,933
Litigation expense .....	445	1,025	469	265
Total operating expenses .....	<u>46,803</u>	<u>45,361</u>	<u>46,697</u>	<u>49,772</u>
Loss from operations .....	<u>(13,572)</u>	<u>(9,426)</u>	<u>(8,634)</u>	<u>(6,814)</u>
Other expense, net:				
Interest expense .....	(127)	(104)	(151)	(127)
Interest and other income (expense), net .....	27	(216)	22	(165)
Total other expense, net .....	<u>(100)</u>	<u>(320)</u>	<u>(129)</u>	<u>(292)</u>
Loss before provision for income taxes .....	<u>(13,672)</u>	<u>(9,746)</u>	<u>(8,763)</u>	<u>(7,106)</u>
Provision for income taxes .....	62	231	204	250
Net loss .....	<u>\$ (13,734)</u>	<u>\$ (9,977)</u>	<u>\$ (8,967)</u>	<u>\$ (7,356)</u>
Net loss per share - basic and diluted .....	<u>\$ (0.22)</u>	<u>\$ (0.16)</u>	<u>\$ (0.14)</u>	<u>\$ (0.12)</u>

## ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

### Foreign Currency Risk

Our consolidated results of operations, financial position and cash flows are subject to fluctuations due to changes in foreign currency exchange rates. Historically, the majority of our revenue contracts are denominated in U.S. dollars, with the most significant exception being Japan where we invoice primarily in the Japanese yen. Our costs and expenses are generally denominated in the currencies where our operations are located, which is primarily in North America, Japan and to a lesser extent EMEA and the Asia Pacific region. In 2016, we initiated a hedging program with respect to foreign currency risk. Revenue resulting from selling in local currencies and costs and expenses incurred in local currencies are exposed to foreign currency exchange rate fluctuations which can affect our revenue and operating income. As exchange rates vary, operating income may differ from expectations.

The functional currency of our foreign subsidiaries is the U.S. dollar. At the end of each reporting period, monetary assets and liabilities are remeasured to the functional currency using exchange rates in effect at the balance sheet date. Non-monetary assets and liabilities are remeasured at historical exchange rates. Gains and losses related to remeasurement are recorded in interest income and other income (expense), net in the consolidated statements of operations. A significant fluctuation in the exchange rates between our subsidiaries' local currencies, especially the Japanese yen, British Pounds and Euro, and the U.S. dollar could have an adverse impact on our consolidated financial position and results of operations.

We recorded \$1.6 million, \$0.5 million and \$2.0 million foreign exchange loss during the years ended December 31, 2016, 2015 and 2014, respectively. The effect of a hypothetical 10% change in our exchange rate would not have a significant impact on our consolidated results of operations.

### Interest Rate Risk

Our exposure to interest rates risk relates to our 2016 Credit Facility with variable interest rates, where an increase in interest rates may result in higher borrowing costs. Since we have no outstanding borrowings under our 2016 Credit Facility as of December 31, 2016, the effect of a hypothetical 10% change in interest rates would not have any impact on our interest expense.

Our exposure to market risk for changes in interest rates relates primarily to our marketable securities. Our marketable securities are comprised of certificates of deposit, corporate securities, U.S. Treasury and agency securities, commercial paper and asset-backed securities. At December 31, 2016, our investment portfolio included marketable securities with an aggregate fair market value of \$85.4 million and a cost basis of \$85.4 million.

The following table presents the hypothetical fair values of our marketable securities assuming immediate parallel shifts in the yield curve of 50 basis points ("BPS"), 100 BPS and 150 BPS as of December 31, 2016 (in thousands):

	<u>(150 BPS)</u>	<u>(100 BPS)</u>	<u>(50 BPS)</u>	<u>Fair Value as of 12/31/2016</u>	<u>50 BPS</u>	<u>100 BPS</u>	<u>150 BPS</u>
Marketable securities . . . . .	\$ 86,087	\$ 85,919	\$ 85,648	\$ 85,372	\$ 85,097	\$ 84,821	\$ 84,546

**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTAL DATA**

**INDEX TO CONSOLIDATED FINANCIAL STATEMENTS**

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## **Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Stockholders of A10 Networks, Inc.

San Jose, California

We have audited the accompanying Consolidated Balance Sheets of A10 Networks, Inc. and subsidiaries (the “Company”) as of December 31, 2016 and 2015, and the related Consolidated Statements of Operations, Comprehensive Loss, Stockholders’ Equity (Deficit), and Cash Flows for each of the three years in the period ended December 31, 2016. These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of A10 Networks, Inc. and subsidiaries as of December 31, 2016 and 2015, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2016, in conformity with accounting principles generally accepted in the United States of America.

/s/ Deloitte & Touche LLP

San Jose, California

February 23, 2017

**A10 NETWORKS, INC.**  
**CONSOLIDATED BALANCE SHEETS**  
(in thousands, except par value)

	<u>December 31, 2016</u>	<u>December 31, 2015</u>
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents .....	\$ 28,975	\$ 98,117
Marketable securities .....	85,372	—
Accounts receivable, net of allowances of \$3,619 and \$4,067 as of December 31, 2016 and December 31, 2015 .....	66,755	57,778
Inventory .....	15,070	18,291
Prepaid expenses and other current assets .....	5,137	5,064
Total current assets .....	<u>201,309</u>	<u>179,250</u>
Property and equipment, net .....	8,219	8,903
Goodwill and intangible assets .....	7,940	—
Other non-current assets .....	3,870	4,398
Total Assets .....	<u>\$ 221,338</u>	<u>\$ 192,551</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current Liabilities:		
Accounts payable .....	\$ 9,851	\$ 10,508
Accrued liabilities .....	31,525	27,757
Deferred revenue, current .....	61,334	49,572
Total current liabilities .....	<u>102,710</u>	<u>87,837</u>
Deferred revenue, non-current .....	31,574	23,232
Other non-current liabilities .....	988	1,414
Total Liabilities .....	<u>135,272</u>	<u>112,483</u>
Commitments and contingencies (Note 5) .....		
Stockholder's equity:		
Common stock, par value \$0.00001 – 500,000 shares authorized as of December 31, 2016 and 2015; 67,873 and 64,172 shares issued and outstanding as of December 31, 2016 and 2015 .....	1	1
Additional paid-in capital .....	328,869	301,886
Accumulated other comprehensive loss .....	(45)	—
Accumulated deficit .....	<u>(242,759)</u>	<u>(221,819)</u>
Total Stockholders' Equity .....	<u>86,066</u>	<u>80,068</u>
Total Liabilities and Stockholders' Equity .....	<u>\$ 221,338</u>	<u>\$ 192,551</u>

See accompanying notes to consolidated financial statements.



**A10 NETWORKS, INC.**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
(in thousands, except per share amounts)

	Years Ended December 31,		
	2016	2015	2014
Revenue:			
Products .....	\$ 153,920	138,301	\$ 134,486
Services .....	76,083	60,654	45,021
Total revenue .....	230,003	198,955	179,507
Cost of revenue:			
Products .....	37,680	33,096	31,084
Services .....	17,230	15,672	11,853
Total cost of revenue .....	54,910	48,768	42,937
Gross profit .....	175,093	150,187	136,570
Operating expenses:			
Sales and marketing .....	104,360	104,531	96,837
Research and development .....	60,700	54,843	49,903
General and administrative .....	27,063	27,055	22,938
Litigation expense (benefit) .....	2,089	2,204	(2,837)
Total operating expenses .....	194,212	188,633	166,841
Loss from operations .....	(19,119)	(38,446)	(30,271)
Other income (expense), net:			
Interest expense .....	(424)	(509)	(1,028)
Interest and other income (expense), net .....	(640)	(332)	(1,914)
Total other expense, net .....	(1,064)	(841)	(2,942)
Loss before income taxes .....	(20,183)	(39,287)	(33,213)
Provision for income taxes .....	757	747	1,507
Net loss .....	\$ (20,940)	\$ (40,034)	\$ (34,720)
Accretion of redeemable convertible preferred stock dividend .....	—	—	(1,150)
Net loss attributable to common stockholders .....	\$ (20,940)	\$ (40,034)	\$ (35,870)
Net loss per share attributable to common stockholders:			
Basic and diluted .....	\$ (0.32)	\$ (0.64)	\$ (0.74)
Weighted-average shares used in computing net loss per share attributable to common stockholders:			
Basic and diluted .....	65,701	62,428	48,682

See accompanying notes to consolidated financial statements.

**A10 NETWORKS, INC.**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS**  
(in thousands)

	Years Ended December 31,		
	2016	2015	2014
Net loss .....	\$ (20,940)	\$ (40,034)	\$ (34,720)
Other comprehensive loss, net of tax:			
Unrealized loss on marketable securities .....	(45)	—	—
Comprehensive loss .....	\$ (20,985)	\$ (40,034)	\$ (34,720)

See accompanying notes to consolidated financial statements.

**A10 NETWORKS, INC.**  
**CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (DEFICIT)**  
(in thousands)

	Redeemable Convertible Preferred Stock		Convertible Preferred Stock		Common Stock			Accumulated Deficit	Accumulated Other Comprehensive Loss	Total Stockholders' Equity (Deficit)
	Shares	Amount	Shares	Amount	Shares	Amount	Additional Paid-in Capital			
<b>Balance at December 31, 2013</b> . . .	80	\$ 81,426	30,569	\$ 44,749	10,032	\$ —	\$ 12,185	\$ (147,065)	\$ —	\$ (134,880)
Stock based compensation expense . . .	—	—	—	—	—	—	12,359	—	—	12,359
Accretion of Series D redeemable convertible preferred stock dividend . . . . .	—	1,150	—	—	—	—	(1,150)	—	—	(1,150)
Issuance of common stock in connection with initial public offering net of offering costs . . . . .	—	—	—	—	9,000	—	120,286	—	—	120,286
Conversion of preferred stock to common stock in connection with initial public offering . .	(80)	(82,576)	(30,569)	(44,749)	39,997	1	127,324	—	—	127,325
Common stock issued under employee equity incentive plans, net of unvested portion . . . . .	—	—	—	—	2,352	—	6,574	—	—	6,574
Vesting of early exercise stock options, net of repurchases . .	—	—	—	—	(4)	—	771	—	—	771
Net loss . . . . .	—	—	—	—	—	—	—	(34,720)	—	(34,720)
<b>Balance at December 31, 2014</b> . . .	—	—	—	—	61,377	1	278,349	(181,785)	—	96,565
Stock based compensation expense . . .	—	—	—	—	—	—	16,861	—	—	16,861
Common stock issued under employee equity incentive plans, net of unvested portion . . . . .	—	—	—	—	2,700	—	6,232	—	—	6,232
Vesting of early exercise stock options, net of repurchases . .	—	—	—	—	95	—	444	—	—	444
Net loss . . . . .	—	—	—	—	—	—	—	(40,034)	—	(40,034)
<b>Balance at December 31, 2015</b> . . .	—	—	—	—	64,172	1	301,886	(221,819)	—	80,068
Stock based compensation expense . . .	—	—	—	—	—	—	16,922	—	—	16,922
Common stock issued under employee equity incentive plans, net of unvested portion . . . . .	—	—	—	—	3,664	—	10,336	—	—	10,336
Common stock issued under asset purchase agreement . . . . .	—	—	—	—	227	—	1,313	—	—	1,313
Vesting of early exercise stock options, net of repurchases . .	—	—	—	—	37	—	211	—	—	211
Repurchase and retirement of common stock . . . . .	—	—	—	—	(227)	—	(1,799)	—	—	(1,799)
Unrealized loss on marketable securities, net of tax . . . . .	—	—	—	—	—	—	—	—	(45)	(45)
Net loss . . . . .	—	—	—	—	—	—	—	(20,940)	—	(20,940)
<b>Balance at December 31, 2016</b> . . .	—	\$ —	—	\$ —	67,873	\$ 1	\$ 328,869	\$ (242,759)	\$ (45)	\$ 86,066

See accompanying notes to consolidated financial statements.

**A10 NETWORKS, INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(in thousands)

	Years Ended December 31,		
	2016	2015	2014
Cash flows from operating activities:			
Net loss	\$ (20,940)	\$ (40,034)	\$ (34,720)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:			
Depreciation and amortization	8,267	8,716	10,121
Stock-based compensation	16,922	16,861	12,359
Gain on settlement of contractual liability	—	—	(6,993)
Provision for doubtful accounts and sales returns	1,731	2,531	935
Other non-cash items	875	(82)	32
Changes in operating assets and liabilities:			
Accounts receivable, net	(11,319)	(5,977)	(17,281)
Inventory	892	(430)	(8,914)
Prepaid expenses and other assets	(96)	(405)	(3,017)
Accounts payable	(334)	1,109	903
Accrued liabilities	3,140	5,345	6,724
Accrued litigation expenses	(151)	6	(6,066)
Deferred revenue	20,104	15,584	15,989
Other	(313)	167	(610)
Net cash provided by (used in) operating activities	<u>18,778</u>	<u>3,391</u>	<u>(30,538)</u>
Cash flows from investing activities:			
Proceeds from sales and maturities of marketable securities	40,628	—	—
Purchases of marketable securities	(126,231)	—	—
Purchases of property and equipment	(4,872)	(3,477)	(6,100)
Purchase of intangible asset	(1,500)	—	—
Payment for acquisition	(4,380)	—	—
Net cash used in investing activities	<u>(96,355)</u>	<u>(3,477)</u>	<u>(6,100)</u>
Cash flows from financing activities:			
Proceeds from issuance of common stock under employee equity incentive plans, net of repurchases	10,336	6,019	7,030
Repurchase and retirement of common stock	(1,799)	—	—
Proceeds from initial public offering, net of offering costs	—	—	121,017
Principal payments on revolving credit facility	—	—	(20,000)
Other	(102)	279	(297)
Net cash provided by financing activities	<u>8,435</u>	<u>6,298</u>	<u>107,750</u>
Net increase (decrease) in cash and cash equivalents	<u>(69,142)</u>	<u>6,212</u>	<u>71,112</u>
Cash and cash equivalents - beginning of period	98,117	91,905	20,793
Cash and cash equivalents - end of period	<u>\$ 28,975</u>	<u>\$ 98,117</u>	<u>\$ 91,905</u>
<b>Supplemental Disclosures:</b>			
Cash paid for income taxes, net of refunds	<u>\$ 581</u>	<u>\$ 980</u>	<u>\$ 1,108</u>
Cash paid for interest	<u>\$ 194</u>	<u>\$ 170</u>	<u>\$ 503</u>

See accompanying notes to consolidated financial statements.

**A10 NETWORKS, INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)**  
(in thousands)

	Years Ended December 31,		
	2016	2015	2014
<b>Non-Cash Investing and Financing Activities:</b>			
Inventory transfers to property and equipment . . . . .	\$ 2,360	\$ 2,840	\$ 5,379
Vesting of early exercised stock options . . . . .	\$ 211	\$ 444	\$ 771
Purchases of property and equipment included in accounts payable . . . . .	\$ 162	\$ 486	\$ 78
Conversion of preferred stock into common stock . . . . .	\$ —	\$ —	\$ 127,325
Accretion of Series D redeemable convertible preferred stock . . . . .	\$ —	\$ —	\$ 1,150
Costs related to the initial public offering included in accounts payable and accrued liabilities . . . . .	\$ —	\$ —	\$ 75
Common stock issued under asset purchase agreement . . . . .	\$ 1,313	\$ —	\$ —

See accompanying notes to consolidated financial statements.



## Notes to Consolidated Financial Statements

### 1. Description of Business and Summary of Significant Accounting Policies

#### *Description of Business*

A10 Networks, Inc. (together with our subsidiaries, the “Company”, “we”, “our” or “us”) was incorporated in California in 2004 and reincorporated in Delaware in March 2014. We are headquartered in San Jose, California and have wholly-owned subsidiaries throughout the world including Asia and Europe. Our solutions enable our customers to secure and optimize the performance of their data center and cloud applications and secure their users, applications and infrastructure from internet, web and network threats at scale. Our product portfolio consists of six advanced application delivery and security products; Application Delivery Controllers (“ADC”), Lightning Application Delivery Service (“Lightning ADS”), Carrier Grade Network Address Translation (“CGN”), Threat Protection System (“TPS”), SSL Insight (“SSLi”) and Convergent Firewall (“CFW”). They are available in a variety of form factors, such as optimized hardware appliances, bare metal software, virtual appliances, and cloud-native software. These choices make our portfolio among the most comprehensive in the industry.

#### *Basis of Presentation*

The accompanying consolidated financial statements include those of A10 Networks, Inc. and its subsidiaries, after elimination of all intercompany accounts and transactions. We have prepared the accompanying consolidated financial statements in accordance with generally accepted accounting principles in the United States of America (“U.S. GAAP”) and pursuant to the rules and regulations of the United States Securities and Exchange Commission (the “SEC”).

#### *Use of Estimates*

The preparation of the consolidated financial statements in conformity with U.S. GAAP requires us to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Those estimates and assumptions affect revenue recognition and deferred revenue, the allowance for doubtful accounts, the sales return reserve, the valuation of inventory, the fair value of marketable securities, contingencies and litigation, acquisition related purchase price allocations, accrued liabilities, and the determination of fair value of stock-based compensation. These estimates are based on information available as of the date of the consolidated financial statements; therefore, actual results could differ from management’s estimates.

### Significant Accounting Policies

#### *Cash and Cash Equivalents*

We consider all highly liquid investments with an original maturity of 90 days or less at the date of purchase to be cash equivalents.

#### *Marketable securities*

We classify our investments in debt and equity securities as available-for-sale and record these investments at fair value. These investments are classified as current assets and included in marketable securities on the consolidated balance sheets. Unrealized gains and losses are reported in accumulated other comprehensive income (loss), net of taxes, in stockholders’ equity. Realized gains and losses are determined based on the specific identification method and are reflected in our consolidated statements of operations. Realized gains and losses and other-than-temporary impairment charges, if any, on marketable securities are reported in interest and other income (expense), net as incurred.

We regularly review our investment portfolio to identify and evaluate investments that have indicators of possible impairment. Investments are considered impaired when a decline in fair value is judged to be other-than-temporary. If the cost of an individual investment exceeds its fair value, we evaluate, among other factors, general market conditions, the duration and extent to which the fair value is less than cost, and our intent and ability to hold the investment. Once a decline in fair value is determined to be other-than-temporary, we will record an impairment charge and establish a new cost basis in the investment.

#### *Fair Value Measurement*

Our financial instruments consist of cash, cash equivalents, marketable securities, accounts receivable and accounts payable. Accounts receivable and accounts payable are stated at their carrying value, which approximates fair value due to the short time to the expected receipt or payment. Our cash equivalents, which include money market funds, are measured and recorded at fair value on a

recurring basis. Marketable securities are comprised of certificates of deposit, corporate securities, U.S. Treasury and agency securities, commercial paper and asset-backed securities and are measured at fair value using the three-level valuation hierarchy as described below.

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

*Level 2*—Inputs are observable, quoted prices for identical assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the related assets or liabilities.

*Level 3*—Unobservable inputs that are significant to the measurement of the fair value of the assets or liabilities that are supported by little or no market data.

### ***Accounts Receivable and Allowance for Doubtful Accounts***

Accounts receivable are recorded at invoice amounts, net of allowances for doubtful accounts. We evaluate the collectability of our accounts receivable based on known collection risks and historical experience. In circumstances where we are aware of a specific customer's inability to meet its financial obligations to us (e.g., bankruptcy filings or substantial downgrading of credit ratings), we record a specific reserve for bad debts against amounts due to reduce the net recognized receivable to the amount we reasonably believe will be collected. For all other customers, we record reserves for bad debts based on the length of time the receivables are past due and our historical experience of collections and write-offs.

### ***Inventory***

Inventory consists primarily of finished goods and related component parts and is stated at the lower of standard cost (which approximates actual cost on a first-in, first-out basis) or market value (estimated net realizable value). We evaluate inventory for excess and obsolete products, based on management's assessment of future demand and market conditions. Inventory write-downs, once established, are not reversed as they establish a new cost basis for the inventory. Inventory write downs are included as a component of cost of products revenue in the accompanying consolidated statements of operations.

### ***Property and Equipment, Net***

Property and equipment, including leasehold improvements, are stated at cost, less accumulated depreciation and amortization. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets. Depreciation on property and equipment, excluding leasehold improvements, ranges from 1 to 3 years.

Leasehold improvements are amortized on a straight-line basis over the shorter of the estimated useful lives of the assets or the remaining lease term. Amortization on leasehold improvements ranges from 2 to 8 years.

### ***Goodwill***

Goodwill represents the excess of purchase consideration over the fair values of assets acquired and liabilities assumed in a business combination. Goodwill is not amortized but is reviewed for possible impairment annually in the fourth quarter or more frequently if impairment indicators arise. We have one reporting unit for goodwill impairment tests, and the fair value of our reporting unit has been determined by our enterprise value.

When assessing goodwill for impairment, we first perform a qualitative assessment to determine whether further impairment testing is necessary. If, as a result of its qualitative assessment, it is more-likely-than-not (i.e. greater than 50% chance) that the fair value of our reporting unit is less than its carrying amount, the quantitative impairment test will be required.

Examples of events and circumstances that might indicate that a reporting unit's fair value is less than the carrying amount include macro-economic conditions such as (i) a significant adverse change in customer demand or a severe deterioration in the entity's operating environment and market conditions; (ii) entity-specific events such as increasing costs, declining financial performance, or loss of key personnel; or (iii) other events such as an expectation that a reporting unit will be sold or there will be a sustained decrease in the stock price on either an absolute basis or relative to peers.

If it is determined, as a result of the qualitative assessment, that it is more-likely-than-not that the fair value of our reporting unit is less than its carrying amount, we perform a two-step impairment test on goodwill. The first step requires the identification of the reporting units and a comparison of the fair value of a reporting unit with its carrying amount, including goodwill. If the fair value of the reporting unit is less than its carrying value, an indication of goodwill impairment exists for the reporting unit, and the second step of the impairment test is performed to compute the amount of the impairment. Under the second step, an impairment loss is recognized for any excess of the carrying amount of the reporting unit's goodwill over the implied fair value of that goodwill.

### ***Intangible Assets***

Intangible assets consist primarily of developed technology, patents and acquired customer relationships resulting from acquisitions. Intangible assets are recorded at fair value and amortized on a straight-line basis over their estimated useful lives, which range from 5 to 10 years.

### ***Impairment of Long-Lived Assets***

We evaluate our property and equipment for impairment whenever events or changes in circumstances indicate that the carrying amount of our long-lived asset may not be recoverable. Recoverability of an asset group is measured by comparison of its carrying amount to the expected future undiscounted cash flows that the asset group is expected to generate. If it is determined that an asset group is not recoverable, an impairment loss is recorded in the amount by which the carrying amount of the asset group exceeds its fair value.

### ***Revenue Recognition***

We derive revenue from two sources: (i) products revenue, which includes hardware and perpetual software license revenue; and (ii) services revenue, which includes post contract support (“PCS”), subscription, professional services, and training. A substantial portion of our revenue is from sales of our products and services through distribution channel partners, such as resellers and distributors. Revenue is recognized, net of applicable taxes, when all of the following criteria are met: persuasive evidence of an arrangement exists, delivery or performance has occurred, the sales price is fixed or determinable, and collection is reasonably assured.

We define each of the four criteria above as follows:

- ***Persuasive evidence of an arrangement exists.*** Evidence of an arrangement consists of a purchase order issued pursuant to the terms and conditions of a master sales agreement.
- ***Delivery or performance has occurred.*** We use shipping documents or written evidence of customer acceptance, when applicable, to verify delivery or performance. We recognize product revenue upon transfer of title and risk of loss, which primarily is upon shipment to customers. We do not have significant obligations for future performance, such as customer rights of return or pricing credits associated with our sales.
- ***The sales price is fixed or determinable.*** We assess whether the sales price is fixed or determinable based on payment terms and whether the sales price is subject to refund or adjustment. Standard payment terms to customers range from 30 to 90 days.
- ***Collection is reasonably assured.*** We assess probability of collection on a customer-by-customer basis. Our customers are subjected to a credit review process that evaluates their financial condition and ability to pay for products and services.

PCS revenue includes arrangements for software support and technical support for our products. PCS is offered under renewable, fee-based contracts, which include technical support, hardware repair and replacement parts, bug fixes, patches, and unspecified upgrades on a when-and-if available basis. Revenue for PCS services is recognized on a straight-line basis over the service contract term, which is typically one year, but can be up to five years. Unearned PCS revenue is included in deferred revenue.

Professional service revenue primarily consists of the fees we earn related to installation and consulting services. We recognize revenue from professional services upon delivery or completion of performance. Professional service arrangements are typically short term in nature and are largely completed within 30 to 90 days from the start of service.

### ***Multiple-Element Arrangements***

Our hardware with the embedded software solutions (which is a proprietary operating system that together with the hardware delivers the functionality desired by our customers), is considered a separate unit of accounting from PCS because it has value to the customer on a standalone basis and our sales arrangements do not include a right of return for delivered products. For multiple-element arrangements, we allocate revenue to each unit of accounting based on an estimated selling price at the inception of the arrangement. The total arrangement consideration is allocated to each separate unit of accounting using the relative selling price method. We limit the amount of revenue recognized for delivered elements to an amount that is not contingent upon future delivery of additional products or service.

When applying the relative selling price method, we determine the selling price for each element using (i) vendor-specific objective evidence, or VSOE, of selling price, if available; (ii) third-party evidence, or TPE, of selling price, if VSOE is not available; and (iii) best estimate of selling price, or BEBP, if neither VSOE nor TPE is available.

- ***VSOE.*** We determine VSOE based on our historical pricing and discounting practices for the specific products and services when sold separately. In determining VSOE, we require that a substantial majority of the stand-alone selling prices fall within a reasonably narrow pricing range.

- **TPE.** When VSOE cannot be established for deliverables in multiple-element arrangements, we apply judgment with respect to whether we can establish a selling price based on TPE. TPE is determined based on competitor prices for interchangeable products or services when sold separately to similarly situated customers. However, as our products contain a significant element of proprietary technology and our solutions offer substantially different features and functionality, the comparable pricing of products with similar functionality typically cannot be obtained. Additionally, as we are unable to reliably determine what competitors products' selling prices are on a stand-alone basis, we are not typically able to determine TPE.
- **BESP.** When we are unable to establish selling price using VSOE or TPE, we use BESP in our allocation of arrangement consideration.

The objective of BESP is to determine the price at which we would transact a sale if the product or service was sold regularly on a standalone basis. As we have not been able to establish VSOE or TPE for our products and some of our services, we determine BESP for the purposes of allocating the arrangement, primarily based on historical transaction pricing. Historical transactions are segregated based on our pricing model and go-to-market strategy, which include factors such as the geographies in which our products and services were sold (domestic or international), offering type (product series, and level of support for PCS) and type of sales channel. The determination of BESP is made through consultation with and approval by management.

We may occasionally accept returns to address customer satisfaction issues or solution-fit issues even though there is no contractual provision for such returns. We estimate returns for sales to customers based on historical returns rates applied against current-period gross revenues. Specific customer returns and allowances are considered within this estimate. Management also analyzes changes in customer demand and acceptance of products when evaluating the adequacy of returns and sales allowances.

### ***Deferred Revenue***

Deferred product revenue relates to arrangements where not all revenue recognition criteria have been met. Deferred services revenue primarily represents PCS contracts billed in advance and revenue is recognized ratably over the service contract term, typically 1 to 5 years.

### ***Shipping and Handling***

Shipping and handling charges billed to customers are included in revenue in the period shipped and the related costs are included in cost of revenue.

### ***Research and Development Costs***

Research and development efforts are focused on new product development and on developing additional functionality for our existing products. These expenses consist of personnel costs, and to a lesser extent, prototype materials, depreciation and certain allocated facilities and information technology costs. We expense research and development costs as incurred.

### ***Stock-Based Compensation***

Stock-based compensation expense is measured on the grant date based on the fair value of the award, net of estimated forfeitures, and recognized on a straight-line basis over the requisite service period. The fair value of restricted stock units ("RSUs") is estimated using our stock price on the grant date. The fair value of options and employee stock purchase rights is estimated using the Black-Scholes model on the grant date. The Black-Scholes model determines the fair value of share-based payment awards based on assumptions including expected term, stock price volatility, and risk-free interest rate. The fair value of market-performance based restricted stock units ("MSUs") is valued using the Monte Carlo simulation model, which uses the stock price, expected volatility and risk-free interest rate to determine the fair value.

### ***Warranty Costs***

Our appliance hardware and software generally carry a warranty period of 90 days. Estimates of future warranty costs are based on historical returns and the application of the historical return rates to our in-warranty installed base. Warranty costs to repair or replace items sold to customers have been insignificant for the years ended December 31, 2016, 2015 and 2014.

### ***Foreign Currency***

The functional currency of our foreign subsidiaries is the U.S. dollar. Transactions denominated in non-functional currencies are remeasured to the functional currency at the average exchange rate for the period. Non-functional currency monetary assets and liabilities are remeasured to the functional currency using the exchange rate in effect at the balance sheet date, and non-monetary assets and liabilities are remeasured at historical exchange rates. Gains and losses related to remeasurement are recorded in interest and other income (expense), net in the consolidated statements of operations.

## ***Income Taxes***

We account for income taxes using the asset and liability method, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been recognized in our consolidated financial statements or in our tax returns. Estimates and judgments occur in the calculation of certain tax liabilities and in the determination of the recoverability of certain deferred income tax assets, which arise from temporary differences and carryforwards. Deferred income tax assets and liabilities are measured using the currently enacted tax rates that apply to taxable income in effect for the years in which those tax assets are expected to be realized or settled. We regularly assess the likelihood that our deferred tax assets will be recovered from future taxable income and, to the extent we believe, based upon the weight of available evidence, that it is more likely than not that all or a portion of deferred tax assets will not be realized, a valuation allowance is established through an adjustment to income tax expense.

The factors used to assess the likelihood of realization of our deferred tax assets include our forecast of future taxable income and available tax planning strategies that could be implemented to realize the net deferred tax assets. Assumptions represent our best estimates and involve inherent uncertainties and the application of our judgment.

We account for uncertainty in income taxes recognized in our consolidated financial statements by regularly reviewing our tax positions and benefits to be realized. We recognize tax liabilities based upon our estimate of whether, and the extent to which, additional taxes will be due when such estimates are more-likely-than-not to be sustained. An uncertain income tax position will not be recognized if it has less than a 50% likelihood of being sustained upon examination by taxing authorities. The provision for income taxes includes the effects of any resulting tax reserves, or unrecognized tax benefits, that are considered appropriate as well as the related net interest and penalties.

## ***Segment Information***

An operating segment is a component of an enterprise for which its discrete financial information is available and its operating results are regularly reviewed by chief operating decision maker for resource allocation decisions and performance assessment. Our chief operating decision maker is our Chief Executive Officer.

Our Chief Executive Officer reviews financial information presented on a consolidated basis for purposes of allocating resources and assessing performance of the Company. Accordingly, we have one reportable segment and one operating segment.

## ***Vendor Business Concentration***

We rely on third parties to manufacture our hardware appliances and we purchase raw materials from third-party vendors. We outsourced substantially all of our manufacturing services to two independent manufacturers. In addition, we purchase certain strategic component inventory which is consigned to our third-party manufacturers. Other hardware components included in our products are sourced from various suppliers by our manufacturers and are principally industry standard parts and components that are available from multiple vendors.

## ***Concentration of Credit Risk and Significant Customers***

Financial instruments that potentially subject us to concentrations of credit risk consist of cash, cash equivalents, short-term investments and accounts receivable. Our cash and investments are held and invested in high-credit quality financial instruments by recognized financial institutions and therefore subject to minimum credit risk.

Our accounts receivable are unsecured and represent amounts due to us based on contractual obligations of our customers. We mitigate credit risk in respect to accounts receivable by performing periodic credit evaluations based on a number of factors, including past transaction experience, evaluation of credit history and review of the invoicing terms of the contract. We generally do not require our customers to provide collateral to support accounts receivable.

Significant customers, including distribution channel partners and direct customers, are those which represent more than 10% of our total revenue for each period presented, or our gross accounts receivable balance as of each respective balance sheet date. Revenue from our significant customers as a percentage of our total revenue are as follows:

	Years Ended December 31,		
	2016	2015	2014
Customer A .....	14%	*	13%

\* represents less than 10% of total revenue

Three customers accounted for 15%, 13% and 11% of our total gross accounts receivable as of December 31, 2016. Two customers accounted for 27% and 11% of our gross accounts receivable as of December 31, 2015.



## Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standard Update (“ASU”) No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which will supersede most of the existing revenue recognition guidance under U.S. GAAP. This ASU requires an entity to recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services and requires the capitalization of incremental customer acquisition costs and amortization of these costs over the contract period or estimated customer life which will result in the recognition of a contract asset on our balance sheets. This standard is effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Early adoption of one year prior to the required effective date is permitted. However, we do not plan to early adopt. Accordingly, the updated standard is effective for us in the first quarter of 2018. The ASU allows for either full retrospective or modified retrospective adoption. We are still in the process of evaluating which transition method we plan to adopt with such decision depending on a number of factors, including system readiness and the magnitude of the potential impact on our financial statements. While we are continuing to assess all potential impacts of the new standard, we currently do not believe this standard will have a material impact on our consolidated financial statements and related disclosures.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*. This new accounting standard primarily requires lessees to recognize most leases on their balance sheets but record expenses on their income statements in a manner similar to current accounting. For lessors, the guidance modifies the classification criteria and the accounting for sales-type and direct financing leases. The guidance is effective for annual periods beginning after December 15, 2018 with early adoption permitted. We are currently evaluating the impact of this guidance on our financial statements.

In March 2016, the FASB issued ASU No. 2016-09, *Compensation—Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting*. The new guidance requires the recognition of the income tax effects of awards in the income statement when the awards vest or are settled, thus eliminating additional paid in capital pools. The guidance also allows for the employer to repurchase more of an employee’s shares for tax withholding purposes without triggering liability accounting. In addition, the guidance allows for a policy election to account for forfeitures as they occur rather than on an estimated basis. This guidance is effective for annual and interim reporting periods of public entities beginning after December 15, 2016 with early adoption permitted. We will be adopting this guidance in the first quarter of fiscal year 2017 and do not believe this standard will have a material impact on our consolidated financial statements.

## 2. Marketable Securities and Fair Value Measurements

As of December 31, 2016, the estimated fair value of our marketable securities, classified as available for sale, are as follows (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Certificates of deposit . . . . .	\$ 12,499	\$ 9	\$ —	\$ 12,508
Corporate securities . . . . .	42,765	9	(42)	42,732
U.S. Treasury and agency securities . . . . .	5,190	—	(14)	5,176
Commercial paper . . . . .	11,470	1	(2)	11,469
Asset-backed securities . . . . .	13,493	—	(6)	13,487
	<u>\$ 85,417</u>	<u>\$ 19</u>	<u>\$ (64)</u>	<u>\$ 85,372</u>

During the year ended December 31, 2016, we did not reclassify any amount to earnings from accumulated other comprehensive loss related to unrealized gains or losses. We did not have any marketable securities as of December 31, 2015.

The following table summarizes the cost and estimated fair value of marketable securities based on contractual maturities as of December 31, 2016 (in thousands):

	Amortized Cost	Fair Value
Less than 1 year . . . . .	\$ 53,500	\$ 53,503
Mature in 1 - 3 years . . . . .	31,917	31,869
	<u>\$ 85,417</u>	<u>\$ 85,372</u>

All available-for-sale securities have been classified as current assets, based on management’s ability to use the funds in current operations.

Marketable securities in an unrealized loss position as of December 31, 2016 consisted of the following (in thousands):

	Fair Value	Unrealized Losses
Corporate securities .....	\$ 28,537	\$ (42)
U.S. Treasury and agency securities .....	5,176	(14)
Commercial paper .....	8,974	(2)
Asset-backed securities .....	10,664	(6)
	<u>\$ 53,351</u>	<u>\$ (64)</u>

As of December 31, 2016, no marketable securities were in a continuous unrealized loss position for more than twelve months. Based on evaluation of securities that have been in a continuous loss position, we did not recognize any other-than-temporary impairment charges for the year ended December 31, 2016.

The following is a summary of our cash, cash equivalents and marketable securities measured at fair value on a recurring basis (in thousands):

	December 31, 2016				December 31, 2015			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Cash .....	\$ 18,672	\$ —	\$ —	\$ 18,672	\$ 27,036	\$ —	\$ —	\$ 27,036
Cash equivalents .....	10,303	—	—	10,303	71,081	—	—	71,081
Certificates of deposit .....	—	12,508	—	12,508	—	—	—	—
Corporate securities .....	—	42,732	—	42,732	—	—	—	—
U.S. Treasury and agency securities .....	—	5,176	—	5,176	—	—	—	—
Commercial paper .....	—	11,469	—	11,469	—	—	—	—
Asset-backed securities .....	—	13,487	—	13,487	—	—	—	—
	<u>\$ 28,975</u>	<u>\$ 85,372</u>	<u>\$ —</u>	<u>\$ 114,347</u>	<u>\$ 98,117</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 98,117</u>

### 3. Balance Sheets and Statement of Operations Components

#### *Allowance for Doubtful Accounts and Sales Return Reserve*

	December 31, 2016	December 31, 2015	December 31, 2014
		(in thousands)	
Allowance for doubtful accounts, beginning balance .....	\$ 2,887	\$ 1,904	\$ 1,836
Charged to expenses .....	1,166	1,590	76
Write-offs .....	(1,147)	(607)	(8)
Allowance for doubtful accounts, ending balance .....	<u>\$ 2,906</u>	<u>\$ 2,887</u>	<u>\$ 1,904</u>
		(in thousands)	
Sales return reserve, beginning balance .....	\$ 1,180	\$ 1,342	\$ 902
Charged to revenue .....	565	940	858
Utilization .....	(1,032)	(1,102)	(418)
Sales return reserve, ending balance .....	<u>\$ 713</u>	<u>\$ 1,180</u>	<u>\$ 1,342</u>

#### *Inventory*

	December 31, 2016	December 31, 2015
		(in thousands)
Raw materials .....	\$ 6,669	\$ 9,418
Finished goods .....	8,401	8,873
Total inventory .....	<u>\$ 15,070</u>	<u>\$ 18,291</u>

**Property and Equipment, Net**

	Useful Life (in years)	December 31, 2016	December 31, 2015
		(in thousands)	
Equipment	1-3	\$ 41,815	\$ 35,836
Software	1-3	3,801	3,548
Furniture and fixtures	1-3	865	864
Leasehold improvements	2-8	2,724	2,492
Construction in progress		258	83
Property and equipment, gross		49,463	42,823
Less: accumulated depreciation and amortization		(41,244)	(33,920)
Total property and equipment, net		<u>\$ 8,219</u>	<u>\$ 8,903</u>

Depreciation and amortization on our property and equipment for the years ended December 31, 2016, 2015 and 2014 was \$7.6 million, \$8.6 million and \$10.0 million, respectively.

**Goodwill and Intangible Assets**

Activity related to goodwill for the year ended December 31, 2016 is as follows (in thousands):

Balance as of December 31, 2015	\$ 72
Acquisitions	1,235
Balance as of December 31, 2016	<u>\$ 1,307</u>

Purchased intangible assets consisted of the following (in thousands):

	December 31, 2016			December 31, 2015		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Value	Gross Carrying Amount	Accumulated Amortization	Net Carrying Value
Developed technology	\$ 5,050	\$ (505)	\$ 4,545	\$ —	\$ —	\$ —
Patents	2,936	(848)	2,088	1,436	(641)	795
Total	<u>\$ 7,986</u>	<u>\$ (1,353)</u>	<u>\$ 6,633</u>	<u>\$ 3,182</u>	<u>\$ (2,387)</u>	<u>\$ 795</u>

Amortization expense related to purchased intangible assets for the years ended December 31, 2016, 2015 and 2014 was \$0.7 million, \$0.1 million and \$0.1 million, respectively. Purchased intangible assets are amortized over a remaining weighted average useful life of 4.6 years.

Future amortization expense for purchased intangible assets as of December 31, 2016 is as follows (in thousands):

Fiscal Years Ending December 31,	
2017	\$ 1,442
2018	1,442
2019	1,442
2020	1,442
2021	865
	<u>\$ 6,633</u>

**Accrued Liabilities**

	December 31, 2016	December 31, 2015
	(in thousands)	
Accrued compensation and benefits	\$ 22,326	\$ 18,134
Accrued tax liabilities	3,340	4,520
Other	5,859	5,103
Total accrued liabilities	<u>\$ 31,525</u>	<u>\$ 27,757</u>

## Deferred Revenue

	December 31, 2016	December 31, 2015
	(in thousands)	
Deferred revenue:		
Products .....	\$ 4,182	\$ 3,233
Services .....	88,726	69,571
Total deferred revenue .....	92,908	72,804
Less: current portion .....	(61,334)	(49,572)
Non-current portion .....	<u>\$ 31,574</u>	<u>\$ 23,232</u>

## Settlement of Contractual Liability

In May 2014, we reached a settlement agreement with one of our legal service providers which resulted in the reduction of a previously accrued contractual liability that totaled \$12.0 million. We made a payment of \$5.0 million in accordance with the terms of the settlement agreement in June 2014 and recorded a \$7.0 million benefit to litigation expense (benefit) at that time.

## 4. Credit Facility

In September 2013, we entered into a credit agreement (the “2013 Credit Facility”) with Royal Bank of Canada, JPMorgan Chase Bank, N.A. and Bank of America, N.A. as lenders. The 2013 Credit Facility provided a three-year \$35.0 million revolving credit facility, which included a maximum \$10.0 million letter of credit facility. We were required to pay quarterly facility fees of 0.45% per annum on the average daily unused portion of the revolving credit facility. We had no outstanding borrowings under this credit facility for any period prior to its expiration on September 30, 2016.

In November 2016, we entered into a loan and security agreement (the “2016 Credit Facility”) with Silicon Valley Bank (“SVB”), as the lender. The 2016 Credit Facility provides a three-year, \$25.0 million revolving credit subfacility, which includes a maximum of \$25.0 million letter of credit subfacility. When our net cash equals or exceeds \$50.0 million, loans may be advanced under the 2016 Credit Facility up to the full \$25.0 million. When our net cash falls below \$50.0 million, loans may be advanced under the 2016 Credit Facility based on a borrowing base equal to a specified percentage of the value of our eligible accounts receivable. The loans bear interest, at our option, at (i) the prime rate reported in The Wall Street Journal, minus 0.50% or (ii) a LIBOR rate determined in accordance with the 2016 Credit Facility, plus 2.50%. We are required to pay customary closing fees, commitment fees and letter of credit fees for a facility of this size and type.

Our obligations under the 2016 Credit Facility are secured by substantially all of our assets, excluding our intellectual property. The 2016 Credit Facility contains customary affirmative and negative covenants. In addition, the 2016 Credit Facility requires us to maintain compliance with an adjusted quick ratio of not less than 1:50:1.00, as determined in accordance with the 2016 Credit Facility. We had no outstanding balance under the 2016 Credit Facility and were in compliance with all facility covenants as of December 31, 2016.

## 5. Commitments and Contingencies

### Legal Proceedings

From time to time, we may be party or subject to various legal proceedings and claims, either asserted or unasserted, which arise in the ordinary course of business, including proceedings and claims that relate to intellectual property matters. Some of these proceedings involve claims that are subject to substantial uncertainties and unascertainable damages. Accordingly, except as disclosed, we have not established reserves or ranges of possible loss related to these proceedings, as at this time in the proceedings, if any, the matters do not relate to a probable loss and/or amounts cannot be reasonably estimated.

On January 29, 2015, the Company, the members of our Board of Directors, our Chief Financial Officer, and the underwriters of our March 21, 2014 IPO were named as defendants in a putative class action lawsuit alleging violations of the federal Securities Act of 1933 filed in the Superior Court of the State of California, County of Santa Clara, captioned *City of Warren Police and Fire Retirement System v. A10 Networks, Inc., et al.*, 1-15-CV-276207. Several substantially identical lawsuits were subsequently filed in the same court, bringing the same claims against the same defendants, captioned *Arkansas Teacher Retirement System v. A10 Networks, Inc., et al.*, 1-15-CV-278575 (filed March 25, 2015) and *Kaveny v. A10 Networks, Inc., et al.*, 1-15-CV-279006 (filed April 6, 2015). On May 29, 2015, the aforementioned putative class actions were consolidated under the caption *In re A10 Networks, Inc. Shareholder Litigation*, 1-15-CV-276207 (the “Class Action”). On July 31, 2015, the defendants filed demurrers to all claims, which were overruled in part on November 12, 2015.

On April 6, 2016, all parties entered into a memorandum of understanding reflecting an agreement in principle to settle all claims against all defendants asserted in the action and providing that we will make a payment of \$0.8 million, net of the expected proceeds of insurance policies. The parties subsequently executed a stipulation of settlement, dated June 30, 2016, and filed a motion with the Court seeking preliminary approval of the settlement, which was granted on September 15, 2016. The payment was made in October 2016. The final fairness hearing is scheduled to be held on February 24, 2017. The settlement releases all claims asserted against all defendants and includes the dismissal of all claims against all defendants without any liability or wrongdoing attributed to them. The settlement remains subject to final court approval and other customary conditions.

On June 24, 2015, our directors and certain of our officers were named as defendants in a putative derivative lawsuit filed in the Superior Court of the State of California, County of Santa Clara, captioned *Hornung v. Chen, et al.*, 1-15-CV-282286 (the “Derivative Action”). We were also named as a nominal defendant. The complaint seeks to allege breaches of fiduciary duties and other related claims, arising out of allegations that our officers and directors caused us to infringe patents and intellectual property, improperly approved the settlement of prior litigation, failed to adopt and implement effective internal controls, and caused us to issue false and misleading statements in connection with our IPO. Plaintiff seeks unspecified compensatory damages and other equitable relief. On January 29, 2016, the defendants filed demurrers and a motion to strike parts of the complaint as well as a motion to stay. On May 24, 2016, all parties entered into a memorandum of understanding reflecting an agreement in principle to settle all claims against all defendants asserted in the action, which provides that we implement certain corporate governance measures following final settlement approval. The parties subsequently executed a stipulation of settlement, dated August 26, 2016, and filed a motion with the Court seeking preliminary approval of the settlement. On November 22, 2016, the Court issued an order preliminarily approving the settlement. The final fairness hearing is scheduled to be held on February 24, 2017. The settlement releases all claims asserted against all defendants and includes the dismissal of all claims against all defendants without any liability or wrongdoing attributed to them. The settlement remains subject to final court approval and other customary conditions.

### ***Leases and Other Commitments***

We lease various operating spaces in the United States, Asia, and Europe under non-cancellable operating lease arrangements that expire on various dates through February 2022. These arrangements require us to pay certain operating expenses, such as taxes, repairs, and insurance and contain renewal and escalation clauses. We recognize rent expense under these arrangements on a straight-line basis over the term of the lease.

We have open purchase commitments with third-party contract manufacturers with facilities in Taiwan to supply nearly all of our finished goods inventories, spare parts, and accessories. These purchase orders are expected to be paid within one year of the issuance date.

The following table summarizes our non-cancellable operating leases and unconditional purchase obligations as of December 31, 2016 (in thousands):

<b>Years Ending December 31,</b>	<b>Leases and Other Contractual Obligations</b>	<b>Purchase Commitments</b>	<b>Total</b>
2017.....	\$ 2,811	\$ 14,900	\$ 17,711
2018.....	2,393	—	2,393
2019.....	1,992	—	1,992
2020.....	365	—	365
2021.....	79	—	79
Thereafter .....	7	—	7
	<u>\$ 7,647</u>	<u>\$ 14,900</u>	<u>\$ 22,547</u>

Rent expense was \$3.5 million, \$3.5 million and \$3.4 million for the years ended December 31, 2016, 2015 and 2014, respectively.

### ***Guarantees and Indemnifications***

In the normal course of business, we provide indemnifications to customers against claims of intellectual property infringement made by third parties arising from the use of our products. Other guarantees or indemnification arrangements include guarantees of product and service performance, and standby letters of credit for lease facilities and corporate credit cards. We have not recorded a liability related to these indemnification and guarantee provisions and our guarantees and indemnification arrangements have not had any significant impact on our consolidated financial statements to date.



## 6. Equity Award Plans

### *Equity Incentive Plans*

#### *2014 Equity Incentive Plan*

Our 2014 Equity Incentive Plan (the “2014 Plan”) was adopted by our board of directors and approved by our stockholders in March 2014. The 2014 Plan provides for the granting of stock options, restricted stock awards, restricted stock units, stock appreciation rights, performance units and performance shares to our employees, consultants and members of our board of directors. In June 2015, our board of directors adopted and our stockholders approved an amendment and restatement of our 2014 Plan, which increased the number of shares available for issuance under the 2014 Plan by the number of shares subject to awards granted under the 2008 Stock Plan (the “2008 Plan”) that were or may in the future be canceled or otherwise forfeited or repurchased by us after March 20, 2014. A maximum of 8,310,566 shares may become available from such awards granted under the 2008 Plan for issuance under the 2014 Plan.

As of December 31, 2015, we had 3,364,304 shares available for future grant. Annually, the shares authorized for the 2014 Plan will increase by the least of (i) 8,000,000 shares, (ii) 5% of the outstanding shares of common stock on the last day of our immediately preceding fiscal year, or (iii) such other amount as determined by our board of directors. On January 1, 2016, the number of shares in the 2014 Plan was increased by 3,211,211 shares, representing 5% of the prior year end’s common stock outstanding. In addition, 1,640,324 shares subject to awards granted under the 2008 Plan that had been canceled or otherwise forfeited or repurchased between March 21, 2014 and December 31, 2015 became available for issuance under the 2014 Plan.

As of December 31, 2016, we had 4,241,980 shares available for future grant. On January 1, 2017, the number of shares in the 2014 Plan was increased by 3,394,376 shares, representing 5% of the prior year end’s common stock outstanding. In addition 266,799 shares subject to awards granted under the 2008 Plan that had been canceled or otherwise forfeited or repurchased during the year ended December 31, 2016 became available for issuance under the 2014 Plan.

Vesting periods of awards granted under the 2014 Plan are determined by our board of directors or other committees responsible for administering the 2014 Plan (the “Plan Administrator”). The Plan Administrator determines the contractual terms of awards granted under the 2014 Plan, provided that incentive stock options and stock appreciation rights granted expire no more than ten years from the grant date. In the case of an incentive stock option granted to an employee, who at the time of grant, owns stock representing more than 10% of the total combined voting power of all classes of stock, the per share exercise price shall be no less than 110% of the fair value per share on the date of grant, and the incentive stock option shall expire no later than five years from the date of grant. For incentive stock options granted to any other employee, and nonstatutory stock options and stock appreciation rights granted to employees, consultants, or members of our board of directors, the per share exercise price shall be no less than 100% of the fair value per share on the date of grant.

#### *2014 Employee Stock Purchase Plan*

The 2014 Employee Stock Purchase Plan (the “2014 Purchase Plan”) was adopted by our board of directors and approved by our stockholders in March 2014.

The 2014 Purchase Plan consists of a twenty-four month offering period with four six-month purchase periods in each offering period. Employees purchase shares in each purchase period at 85% of the market value of our common stock at the beginning of the offering period or the end of the purchase period, whichever is lower. If the market value of our common stock at the end of the purchase period is less than the market value at the beginning of the offering period, participants will be withdrawn from the then current offering period following their purchase of shares, and automatically will be enrolled in the immediately following offering period. Participants may contribute up to 15% of their eligible compensation, subject to certain limits.

The 2014 Purchase Plan provided for an automatic share reserve increase on the first day of each fiscal year beginning 2015 by a number of shares equal to the least of (i) 3,500,000 shares, (ii) 1% of the outstanding common stock on the last day of the immediately preceding fiscal year, or (iii) such other amount as determined by our board of directors. On January 1, 2016, the number of shares in the 2014 Purchase Plan was increased by 642,242 shares, representing 1% of the prior year end’s common stock outstanding. In June 2016, our board of directors adopted, and our stockholders approved an amendment to our 2014 Purchase Plan which removed the automatic annual share increase and increased the number of shares available for issuance under the 2014 Purchase Plan by 4,000,000 shares. As of December 31, 2016, 4,104,060 shares were available for future issuance under the 2014 Purchase Plan.

Employees purchased 1,080,142 shares at an average price of \$3.93 and 1,105,015 shares at an average price of \$3.56 during the year ended December 31, 2016 and 2015, respectively. The intrinsic value of shares purchased during the year ended December 31, 2016 and 2015 was \$3.5 million and \$3.7 million, respectively. The intrinsic value is calculated as the difference between the market value on the date of purchase and the purchase price of the shares.

### Early Exercise of Stock Options

We have allowed certain employees and directors to exercise options granted prior to vesting. The unvested shares are subject to our repurchase right at the original purchase price. The proceeds from the early exercise of stock options initially are recorded in other non-current liabilities and reclassified to common stock as our repurchase right lapses. As of December 31, 2016 and 2015, 14,307 and 51,884 shares were subject to repurchase at an aggregate price of \$0.1 million and \$0.3 million, respectively.

### Option Exchange Program

On November 19, 2015, we commenced an option exchange which permitted certain employees and service providers to surrender certain outstanding stock options in exchange for replacement RSUs with a lesser number of shares, subject to a different vesting schedule. This option exchange was completed on December 17, 2015. A total of 344,248 options to purchase shares of common stock with a weighted-average exercise price of \$13.58 per share were canceled and replaced with 109,743 RSUs with per share market value of \$6.76, on December 17, 2015. The replacement RSUs started to vest on the one-year anniversary of the grant date. We accounted for this option exchange as a stock option modification in accordance with the provisions of ASC 718 *Share-Based Compensation*. We are recording the incremental expense of \$56,000 in addition to the remaining expense attributable to the exchanged stock options over the vesting period of the new awards.

### Stock-based Compensation

A summary of our stock-based compensation expense is as follows (in thousands):

	Years Ended December 31,		
	2016	2015	2014
Stock-based compensation by type of award:			
Stock options	\$ 4,153	\$ 5,565	\$ 5,852
Restricted stock units	12,567	8,871	3,217
Employee stock purchase rights	202	2,425	3,290
	<u>\$ 16,922</u>	<u>\$ 16,861</u>	<u>\$ 12,359</u>
Stock-based compensation by category of expense:			
Cost of revenue	\$ 1,105	\$ 1,533	\$ 1,063
Sales and marketing	7,006	7,735	5,829
Research and development	5,732	5,437	3,932
General and administrative	3,079	2,156	1,535
	<u>\$ 16,922</u>	<u>\$ 16,861</u>	<u>\$ 12,359</u>

As of December 31, 2016, we had \$32.0 million of unrecognized stock-based compensation expense, net of estimated forfeitures, related to unvested stock-based awards which will be recognized over a weighted-average period of 2.4 years.

The fair values of the options and employee stock purchase rights are estimated as of the grant date using the Black-Scholes option-pricing model with the following assumptions:

	Options			Employee Stock Purchase Rights		
	Years Ended December 31,			Years Ended December 31,		
	2016	2015	2014	2016	2015	2014
Expected term (in years)	4.9	4.8	4.8	1.3	1.3	1.3
Risk-free interest rate	1.4%	1.6%	1.8%	0.8%	0.5%	0.3%
Expected volatility	49%	50%	41%	42%	41%	27%
Dividend rate	—%	—%	—%	—%	—%	—%

- **Expected Term.** We estimate the expected life of options based on an analysis of our historical experience of employee exercise and post-vesting termination behavior considered in relation to the contractual life of the option. The expected term for the 2014 Purchase Plan is based on the term of the purchase period.
- **Risk-Free Interest Rate.** The risk-free interest rate is based on the U.S. Treasury yield curve in effect at the time of grant for zero coupon U.S. Treasury notes with maturities approximately equal to the expected terms of stock options and shares to be issued under the 2014 Purchase Plan.

- **Expected Volatility.** Due to the limited trading history of our own common stock, we determined the share price volatility factor based on a combination of the historical volatility of our own common stock and the historical volatility of our peer group.
- **Dividend Rate.** The expected dividend was assumed to be zero as we have never paid dividends and have no current plans to do so.

### Stock Options

The following table summarizes our stock option activities and related information:

	Number of Shares (thousands)	Weighted- Average Exercise Price	Weighted- Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value (thousands)
Outstanding as of December 31, 2015	9,291	\$ 4.78		
Granted	672	\$ 5.52		
Exercised	(1,444)	\$ 4.22		
Canceled (1)	(651)	\$ 6.23		
Outstanding as of December 31, 2016	<u>7,868</u>	\$ 4.82	6.2	\$ 28,931
Vested and expected to vest as of December 31, 2016	<u>7,758</u>	\$ 4.82	6.2	\$ 28,554
Vested and exercisable as of December 31, 2016	<u>5,688</u>	\$ 4.57	5.6	\$ 22,363

(1) Common shares subject to awards granted under the 2008 Plan and canceled after March 21, 2014 are reallocated to the 2014 Plan's share reserve and become available for issuance under the 2014 Plan. During the years ended 2016 and 2015, 266,799 shares and 1,640,324 shares of the canceled stock options, respectively, were reallocated and became available for issuance under the 2014 Plan.

As of December 31, 2016, the aggregate intrinsic value represents the excess of the closing price of our common stock of \$8.31 over the exercise price of the outstanding in-the-money options.

The following table provides information pertaining to our stock options (in thousands, except weighted-average fair values):

	Years Ended December 31,		
	2016	2015	2014
Fair value of options granted	\$ 1,603	\$ 869	\$ 11,683
Weighted-average fair value of options granted	\$ 2.38	\$ 2.13	\$ 2.79
Intrinsic value of options exercised	\$ 5,990	\$ 2,299	\$ 14,863

### Stock Awards

We have granted restricted stock unit awards ("RSUs") to our employees, consultants and members of our board of directors, and performance-based stock awards ("PSUs") and market performance-based stock restricted stock unit awards ("MSUs") to certain company executives.

In 2014 and 2015, we granted 540,000 MSUs and 40,000 MSUs, respectively, to certain executives. These MSUs will vest if the closing price of our common stock remains above certain predetermined target prices for 20 consecutive trading days within a 4-year period following the grant date, subject to continued service by the award holder. No MSUs were vested as of December 31, 2016.

In February 2016, we granted 547,000 PSUs with certain financial and operational targets. These PSUs are subject to service condition vesting requirements with 25% of the PSUs that become eligible to vest upon achievement of the performance targets scheduled to vest on each of the first, second, third and fourth year anniversary of the PSU grant date. None of these PSUs were vested as of December 31, 2016.

In October 2016, we granted 60,641 PSUs with certain financial and operational targets. These PSUs are subject to service condition vesting requirements with scheduled vesting dates March 2017 through June 2018 to the extent they become eligible to vest upon achievement of the performance targets. None of these PSUs were vested as of December 31, 2016.

The following table summarizes our stock award activities and related information:

	Number of Shares (thousands)	Weighted Average Grant Date Fair Value	Weighted- Average Remaining Vesting Term (Years)	Aggregate Intrinsic Value (thousands)
Outstanding as of December 31, 2015	3,452	\$ 5.88		
Granted	4,550	\$ 6.50		
Released	(1,139)	\$ 8.16		
Canceled	(904)	\$ 6.56		
Outstanding as of December 31, 2016	<u>5,959</u>	\$ 5.81	1.6	\$ 49,517

The aggregate intrinsic value of outstanding awards is calculated based on the closing price of our common stock of \$8.31 on December 31, 2016.

The aggregate fair value of stock awards released as of the respective vesting dates was approximately \$9.7 million and \$5.6 million for the years ended December 31, 2016 and 2015, respectively.

### ***Stock Repurchase Program***

On October 27, 2016, our board of directors authorized a share repurchase program for up to \$20.0 million of our common stock over the next 12 months. Under the repurchase authorization, shares may be purchased from time to time, subject to general business and market conditions and other investment opportunities, through open market purchases, privately negotiated transactions or other means. The repurchase authorization may be commenced, suspended or discontinued at any time at our discretion.

During 2016, we repurchased 226,676 shares at an average price of \$7.92 as a part of publicly announced program. The repurchased shares were retired upon delivery to us.

## **7. Net Loss Per Share**

Basic net loss per share is computed using the weighted average number of common shares outstanding for the period. Diluted net loss per share is computed using the weighted average number of common shares outstanding for the period plus potential dilutive common shares, including stock options, RSUs and employee stock purchase rights, unless the potential common shares are anti-dilutive. Since we had net losses in the years ended December 31, 2016, 2015 and 2014, none of the potential dilutive common shares were included in the computation of diluted shares for these periods, as inclusion of such shares would have been anti-dilutive.

The following table presents common shares related to potentially dilutive shares excluded from the calculation of diluted net loss per share as their effect would have been anti-dilutive (in thousands):

	Years Ended December 31,		
	2016	2015	2014
Stock options, RSUs and employee stock purchase rights	13,631	10,124	6,415
Common stock subject to repurchase	14	52	196
	<u>13,645</u>	<u>10,176</u>	<u>6,611</u>

## **8. Income Taxes**

The geographical breakdown of loss before provision for income taxes is as follows (in thousands):

	Years Ended December 31,		
	2016	2015	2014
Domestic loss	\$ (22,978)	\$ (41,677)	\$ (35,593)
Foreign income	2,795	2,390	2,380
Loss before provision for income taxes	<u>\$ (20,183)</u>	<u>\$ (39,287)</u>	<u>\$ (33,213)</u>

The provision for income taxes consists of the following (in thousands):

	Years Ended December 31,		
	2016	2015	2014
Current provision for income taxes:			
State	\$ 41	\$ 55	\$ 24
Foreign	1,009	675	1,054
Total current	1,050	730	1,078
Deferred tax expense (benefit):			
Federal	17	—	—
Foreign	(310)	17	429
Total deferred	(293)	17	429
Provision for income taxes	\$ 757	\$ 747	\$ 1,507

The reconciliation of the statutory federal income tax and our effective income tax is as follows (in thousands):

	Years Ended December 31,					
	2016		2015		2014	
	Amount	Percentage	Amount	Percentage	Amount	Percentage
Tax at statutory rate	\$ (6,862)	34.0%	\$ (13,358)	34.0%	\$ (11,292)	34.0%
State tax - net of federal benefits	27	(0.1)	36	(0.1)	16	(0.1)
Foreign rate differential	(666)	3.3	(422)	1.1	231	(0.7)
Changes in federal valuation allowance	7,141	(35.4)	11,926	(30.4)	10,547	(31.8)
Stock-based compensation	88	(0.4)	1,845	(4.7)	1,041	(3.1)
Other permanent items	583	(2.9)	415	(1.1)	513	(1.5)
Expenses for uncertain tax positions	358	(1.8)	227	(0.6)	330	(1.0)
Other	88	(0.4)	78	(0.1)	121	(0.4)
Provision for income taxes	\$ 757	(3.7)%	\$ 747	(1.9)%	\$ 1,507	(4.6)%

The tax effects of temporary differences that give rise to significant portions of deferred tax assets (liabilities) are as follows (in thousands):

	December 31, 2016	December 31, 2015
Deferred tax assets:		
Net operating loss carryforwards	\$ 47,197	\$ 46,317
Research and development credits, net of uncertain tax positions	12,953	9,517
Accruals, reserves, and other	21,288	17,904
Stock-based compensation	4,055	2,700
Depreciation and amortization	2,892	2,735
Gross deferred tax assets	88,385	79,173
Valuation allowance	(86,935)	(77,643)
Total deferred tax assets	1,450	1,530
Deferred tax liabilities:		
Other	(431)	(805)
Total deferred tax liabilities	(431)	(805)
Net deferred tax assets	\$ 1,019	\$ 725

Recognition of deferred tax assets is appropriate when realization of these assets is more likely than not. Based upon the weight of available evidence, which includes our historical operating performance and the recorded cumulative net losses in prior fiscal periods, we recorded a full valuation allowance of \$86.9 million and \$77.6 million against the net U.S. deferred tax assets as of December 31, 2016 and 2015, respectively. For the years ended December 31, 2016, 2015 and 2014, the valuation allowance increased by \$9.3 million, \$14.0 million and \$11.2 million, respectively.

As of December 31, 2016 and 2015, we had U.S. federal net operating loss carryforwards of \$139.0 million and \$130.6 million and state net operating loss carryforwards of \$68.6 million and \$68.4 million, respectively. We track the portion of our net operating loss attributable to stock option benefits in accordance with ASC 718 *Compensation-Share Compensation*, therefore, these amounts are no longer included in our gross or net deferred tax assets. The gross tax benefit of stock options totals \$10.8 million at December 31, 2016, and will only be recorded to additional paid in capital when these benefits reduce cash taxes payable. The federal net operating loss carryforwards will expire at various dates beginning in the year ending December 31, 2026, if not utilized. The state net operating losses expire in various years ending between 2017 and 2036, if not utilized.

Additionally, as of December 31, 2016 and 2015, we had U.S. federal research and development credit carryforwards of \$8.5 million and \$6.4 million and state research and development credit carryforwards of \$8.8 million and \$6.4 million. The federal credit carryforwards will begin to expire at various dates beginning in 2027 while the state credit carryforwards can be carried over indefinitely.

Utilization of the net operating losses and credit carryforwards may be subject to an annual limitation provided for in the Internal Revenue Code Section 382 and similar state codes. Any annual limitation could result in the expiration of net operating loss and credit carryforwards before utilization.

With respect to our undistributed foreign subsidiaries' earnings we consider those earnings to be indefinitely reinvested and, accordingly, no related provision for U.S. federal and state income taxes has been provided. Upon distribution of those earnings' in the form of dividends or otherwise, we may be subject to both U.S. income taxes subject to an adjustment for foreign tax credits and withholding taxes in the various countries. As of December 31, 2016 and 2015, the undistributed earnings approximated \$5.1 million and \$3.9 million, respectively. The determination of the future tax consequence of the remittance of these earnings is not practicable.

### ***Uncertain Tax Positions***

As of December 31, 2016 and 2015, we had gross unrecognized tax benefits of \$3.3 million and \$2.6 million. We have accrued net interest expense of \$9,000 (i.e., there was \$20,000 of gross accrued interest expense offset by \$11,000 of interest released due to a lapse of statute of limitations) related to unrecognized tax benefits reflected in the consolidated financial statements for the year ended December 31, 2016. Our policy for classifying interest and penalties associated with unrecognized income tax benefits is to include such items in income tax expense.

The activity related to the unrecognized tax benefits is as follows (in thousands):

	Years Ended December 31,		
	2016	2015	2014
Gross unrecognized tax benefits—beginning balance . . . . .	\$ 2,552	\$ 2,195	\$ 1,846
Increases (decrease) related to tax positions from prior years . . . . .	66	(4)	340
Increases related to tax positions taken during current year . . . . .	690	361	278
Decreases related to tax positions taken during the current year . . . . .	—	—	(269)
Gross unrecognized tax benefits—ending balance . . . . .	<u>\$ 3,308</u>	<u>\$ 2,552</u>	<u>\$ 2,195</u>

These amounts are related to certain deferred tax assets with a corresponding valuation allowance. As of December 31, 2016, the total amount of unrecognized tax benefits, if recognized, that would affect the effective tax rate is \$1.1 million. We believe that there will not be any significant changes in our unrecognized tax benefits in the next 12 months.

We are subject to taxation in the United States, various states, and several foreign jurisdictions. Because we have net operating loss and credit carryforwards, there are open statutes of limitations in which federal, state and foreign taxing authorities may examine our tax returns for all years from 2004 through the current period. During January 2017, the Internal Revenue Service (IRS) notified us that it intends to examine the 2014 and 2015 tax returns beginning in the first quarter of 2017.



## 9. Geographic Information

The following table is a summary of revenue by geographic regions based on ship to location (in thousands):

	Years Ended December 31,		
	2016	2015	2014
United States . . . . .	\$ 118,750	\$ 106,842	\$ 85,325
Japan . . . . .	52,951	35,636	45,787
Asia Pacific, excluding Japan . . . . .	29,829	23,847	20,434
EMEA . . . . .	23,093	27,193	19,254
Other . . . . .	5,380	5,437	8,707
Total revenue . . . . .	<u>\$ 230,003</u>	<u>\$ 198,955</u>	<u>\$ 179,507</u>

Our long-lived assets which include property and equipment, net and intangible assets, net is primarily located in the United States. No other geographic regions comprise 10% or more of long-lived assets as of December 31, 2016 and 2015.

## 10. Related-Party Transactions

An affiliate of one of our significant stockholders is also acting as a reseller of our products. On May 27, 2015, the significant stockholder reduced its ownership of our common stock, and ceased to be a related party. During the years ended December 31, 2015 and 2014, we recognized \$2.2 million and \$2.8 million, respectively, revenue from this reseller.

## 11. Employee Benefit Plan

We adopted a profit sharing plan qualified under Section 401(k) of the Internal Revenue Code which is offered to all of our United States employees. Participants in the plan may elect to contribute up to \$18,000 of their annual compensation to the plan for the 2016 calendar year. Individuals who are 50 or older may contribute an additional \$6,000 of their annual income. In 2016, we matched 50% of the first 6% of the employee's eligible compensation. We contributed \$0.9 million, \$0.8 million and zero during the years ended December 31, 2016, 2015 and 2014, respectively.

## 12. Appcito Acquisition

On June 23, 2016, we entered into an asset purchase agreement with Appcito, Inc. ("Appcito"), a privately held company engaged in providing a unified set of services for applications deployed on cloud infrastructure with facilities located in Santa Clara, California and Bangalore, India. Under the terms of the purchase agreement, we acquired substantially all of the assets of Appcito. This acquisition enhances our position as a comprehensive secure application services leader, and it represents a strategic step in our vision to help our customers become more secure and agile as they bridge traditional and cloud application environments.

The total purchase consideration was \$6.5 million. The fair value of the total purchase consideration was \$6.3 million, which consisted of \$5.0 million in cash consideration, less a holdback of \$0.7 million to cover any indemnification claims within twelve months of the acquisition date, and 227,404 unregistered shares of our common stock with an aggregated fair value of \$1.3 million. We allocated the total purchase consideration to the net assets acquired, including identifiable intangible assets, based on their respective fair values at the acquisition date.

The following table summarizes the allocation of the purchase price to the fair value of the assets acquired (in thousands):

Developed technology . . . . .	\$ 5,050
Goodwill . . . . .	1,235
Other tangible assets . . . . .	<u>58</u>
Total assets acquired . . . . .	<u>\$ 6,343</u>

Developed technology is amortized on a straight-line basis over the estimated useful life of five years. Goodwill of \$1.2 million was recognized as part of this acquisition is attributable primarily to the expected synergies and other benefits from this acquisition including adding to our existing momentum around providing secure application service solutions that meet several key demands like application analytics, visibility, and centralized control. This acquisition enhances our position as a comprehensive secure application services leader, and it represents a strategic step in our vision to help our customers become more secure and agile as they bridge traditional data center and cloud application environments. This acquisition has led to the launch of the cloud-native Lightning ADS. We expect to introduce additional options spanning public and private clouds.

We incurred approximately \$0.2 million in legal, accounting and other professional fees related to this acquisition, all of which were expensed during the year ended December 31, 2016.

We do not consider the acquisition of Appcito to be material to our results of operations or financial position, and therefore, we are not presenting pro-forma financial information of the combined operations.

This acquisition was taxable for income tax purposes, and the acquired assets have been recorded at fair value for both book and income tax purposes. Therefore, no deferred taxes have been recorded. The goodwill of \$1.2 million and the \$0.2 million of acquisition costs are capitalized and amortized over 15 years for income tax purposes.

## **ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None.

### **ITEM 9A. 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 required by Rule 13a-15(b) under the Securities Exchange Act of 1934 as of December 31, 2016. The term “disclosure controls and procedures,” as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, or the Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by the 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 SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company’s management, including our Chief Executive Officer and Chief Financial Officer, as the principal executive and financial officers, as appropriate to allow timely decisions regarding required disclosure.

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

Based upon our management’s evaluation of our disclosure controls and procedures as of December 31, 2016, our Chief Executive Officer and Chief Financial Officer concluded that, as of such date, our disclosure controls and procedures are designed at a reasonable assurance level and are effective to provide reasonable assurance that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

#### ***Management’s Report on Internal Control over Financial Reporting***

Our management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act). Our management conducted an assessment of the effectiveness of our internal control over financial reporting based on the criteria set forth in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework). Based on the assessment, our management has concluded that its internal control over financial reporting was effective as of December 31, 2016 to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with GAAP. Our independent registered public accounting firm, Deloitte & Touche, LLP, is not required to and has not issued a formal attestation report as of December 31, 2016 and will not be required to do so until the year following the date that we are no longer an emerging growth company as defined in the JOBS Act.

#### ***Changes in Internal Control over Financial Reporting***

There were no changes in our internal control over financial reporting during the quarter ended December 31, 2016 that have materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

### **ITEM 9B. OTHER INFORMATION**

None.

## **PART III.**

### **ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

The information required by this item will be included under the captions ““Executive Officers,” Executive Compensation,” “Election of Directors,” “Report of the Audit Committee” and “Section 16(a) Beneficial Ownership Reporting Compliance” for the 2017 Annual Meeting in our Proxy Statement with the SEC within 120 days of the year end December 31, 2016 (2017 Proxy Statement) and is incorporated herein by reference.

### **ITEM 11. EXECUTIVE COMPENSATION**

The information required by this item will be set forth in our 2017 Proxy Statement under the captions “Executive Compensation” and “Report of the Compensation Committee on Executive Compensation” and is incorporated herein by reference.

### **ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

Information related to the security ownership of certain beneficial owners and management will be set forth in our 2017 Proxy Statement under the caption “Security Ownership of Management and Principal Stockholders,” and is incorporated herein by reference.

### **ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE**

The information required by this item will be set forth in our 2017 Proxy Statement under the caption “Certain Relationships and Related Transactions, and Director Independence” and is incorporated herein by reference.

### **ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

The information required by this item will be set forth in our 2017 Proxy Statement under the captions “Audit and Related Fees” and “Policy on Audit Committee Pre-Approval of Audit and Permissible Non-Audit Services of Independent Auditors” and is incorporated herein by reference.

## PART IV.

### ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a) Financial Statements

1. Consolidated Financial Statements:

Our Consolidated Financial Statements are listed in the *Index to Consolidated Financial Statements* in Part II, Item 8 of this Annual Report on Form 10-K.

All other schedules have been omitted as they are not required, not applicable, or the required information is otherwise included.

2. Exhibits:

The documents listed in the Exhibit Index of this Annual Report on Form 10-K are incorporated by reference or are filed with this report, in each case as indicated therein (numbered in accordance with Item 601 of Regulation S-K).

## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

### A10 NETWORKS, INC.

Date: February 23, 2017

By: /s/ Lee Chen

**Lee Chen**

*Chief Executive Officer and President*

*(Principal Executive Officer)*

Pursuant to the requirements of the Securities Exchange Act of 1934, this annual report on Form 10-K has been signed below by the following persons on behalf of the Registrant and in the capacities and on the date indicated.

<u>Signature</u>	<u>Title</u>	<u>Date</u>
<u>/s/ Lee Chen</u> Lee Chen	Chief Executive Officer, President and Director (Principal Executive Officer)	February 23, 2017
<u>/s/ Greg Straughn</u> Greg Straughn	Chief Financial Officer (Principal Accounting and Financial Officer)	February 23, 2017
<u>/s/ Robert Cochran</u> Robert Cochran	Executive Vice President, Legal and Corporate Collaboration and Secretary and Director	February 23, 2017
<u>/s/ Peter Y. Chung</u> Peter Y. Chung	Director	February 23, 2017
<u>/s/ Alan S. Henricks</u> Alan S. Henricks	Director	February 23, 2017
<u>/s/ Phillip J. Salsbury</u> Phillip J. Salsbury	Director	February 23, 2017

## EXHIBIT INDEX

Exhibit Number	Description	Incorporated By Reference			
		Form	SEC File No.	Exhibit Number	Filing Date
3.1	Amended and Restated Certificate of Incorporation of the Registrant	S-1/A	333-194015	3.1	March 10, 2014
3.2	Amended and Restated Bylaws of the Registrant	S-1/A	333-194015	3.2	March 10, 2014
4.1	Form of common stock certificate of the Registrant.	S-1/A	333-194015	4.1	March 10, 2014
4.2	Amended and Restated Investors' Rights Agreement among the Registrant and certain holders of its capital stock, amended as of October 4, 2013.	S-1/A	333-194015	4.2	March 10, 2014
10.1*	Form of Indemnification Agreement between the Registrant and each of its directors and executive officers	S-1/A	333-194015	10.1	March 10, 2014
10.2*	2004 Stock Plan and forms of agreements thereunder	10-Q	001-36343	10.1	May 13, 2014
10.3*	2008 Stock Plan and forms of agreements thereunder	10-Q	001-36343	10.2	May 13, 2014
10.4*	Amended and Restated 2014 Equity Incentive Plan	10-Q	001-36343	10.1	August 6, 2015
10.5*	2014 Employee Stock Purchase Plan and forms of agreements thereunder	S-1/A	333-194015	10.5	March 10, 2014
10.6*	Form of Stock Option Agreement pursuant to the 2008 Stock Plan	10-Q	001-36343	10.2	August 4, 2014
10.7*	Form of Stock Option Agreement-Early Exercise pursuant to the 2008 Stock Plan	10-Q	001-36343	10.3	August 4, 2014
10.8*	Form of Stock Option Agreement pursuant to the Amended and Restated 2014 Equity Incentive Plan	10-Q	001-36343	10.4	August 4, 2014
10.9*	Form of Restricted Stock Unit Agreement pursuant to the Amended and Restated 2014 Equity Incentive Plan	10-Q	001-36343	10.5	August 4, 2014
10.10*	Offer Letter, dated July 30, 2004, by and between the Registrant and Lee Chen.	S-1/A	333-194015	10.6	March 10, 2014
10.11*	Offer Letter, dated November 3, 2008, by and between the Registrant and Rajkumar Jalan.	S-1/A	333-194015	10.7	March 10, 2014
10.12*	Offer Letter, dated May 31, 2011, by and between the Registrant and Greg Straughn.	S-1/A	333-194015	10.8	March 10, 2014
10.13*	Offer Letter, dated January 4, 2012, by and between the Registrant and Robert Cochran.	S-1/A	333-194015	10.9	March 10, 2014
10.14*	Offer Letter, dated July 18, 2013, by and between the Registrant and Ray Smets.	S-1/A	333-194015	10.10	March 10, 2014
10.15*	Offer Letter, dated March 15, 2015, by and between the Registrant and Sanjay Kapoor.	10-K	001-6343	10.15	March 1, 2016
10.16	Reseller Agreement, dated April 2, 2009, by and between the Registrant and NEC Corporation.	S-1/A	333-194015	10.12	February 18, 2014
10.17	First Amendment to Reseller Agreement, dated May 19, 2011, by and between the Registrant and NEC Corporation.	S-1/A	333-194015	10.13	February 18, 2014
10.18	Second Amendment to Reseller Agreement, dated April 1, 2011, by and between the Registrant and NEC Corporation.	S-1/A	333-194015	10.14	February 18, 2014



Exhibit Number	Description	Incorporated By Reference			
		Form	SEC File No.	Exhibit Number	Filing Date
10.19	Third Amendment to Reseller Agreement, dated April 1, 2011, by and between the Registrant and NEC Corporation.	S-1/A	333-194015	10.15	February 18, 2014
10.20	Fourth Amendment to Reseller Agreement, dated October 3, 2011, by and between the Registrant and NEC Corporation.	S-1/A	333-194015	10.16	February 18, 2014
10.21	Fifth Amendment to Reseller Agreement, dated April 2, 2012, by and between the Registrant and NEC Corporation.	S-1/A	333-194015	10.17	February 18, 2014
10.22	Sixth Amendment to Reseller Agreement, dated November 29, 2012, by and between the Registrant and NEC Corporation.	S-1/A	333-194015	10.18	February 18, 2014
10.23	Seventh Amendment to Reseller Agreement, dated April 9, 2013, by and between the Registrant and NEC Corporation.	S-1/A	333-194015	10.19	February 18, 2014
10.24	Eighth Amendment to Reseller Agreement, dated October 22, 2013, by and between the Registrant and NEC Corporation.	S-1/A	333-194015	10.20	February 18, 2014
10.25	Ninth Amendment to Reseller Agreement, executed on April 22, 2014, by and between the Registrant and NEC Corporation	10-Q	001-36343	10.1	August 4, 2014
10.26	Manufacturing Services Agreement, dated December 8, 2006, by and between the Registrant and Lanner Electronics (USA).	S-1/A	333-194015	10.21	February 18, 2014
10.27	Amendment No. 1 to Manufacturing Services Agreement, dated June 27, 2013, by and between the Registrant and Lanner Electronics (USA).	S-1/A	333-194015	10.22	February 18, 2014
10.28	Contract Manufacturer Agreement, dated July 1, 2008, by and between the Registrant and AEWIN Technologies, Inc.	S-1/A	333-194015	10.23	February 18, 2014
10.29	Amendment No. 1 to Contract Manufacturer Agreement, dated July 1, 2008, by and between the Registrant and AEWIN Technologies, Inc.	10-K	001-36343	10.31	March 11, 2015
10.30	Credit Agreement, dated as of September 30, 2013, among the Registrant, Royal Bank of Canada, as lender and administrative agent, and JPMorgan Chase Bank, N.A., and Bank of America, N.A., as lenders.	S-1/A	333-194015	10.24	March 10, 2014
10.31*	Form of Change in Control and Severance Agreement.	S-1/A	333-194015	10.25	March 10, 2014
10.32*	Executive Incentive Compensation Plan	10-K	001-6343	10.32	March 1, 2016
10.33*	Separation Agreement, dated March 31, 2016, by and between the Registrant and Sanjay Kapoor.	10-Q	001-36343	10.1	May 5, 2016
10.34*	Offer Letter, dated March 2, 2016, by and between the Registrant and Neil Wu Becker.	10-Q	001-36343	10.2	May 5, 2016
10.35	Loan and Security Agreement, dated as of November 1, 2016, between A10 Networks, Inc. and Silicon Valley Bank.	10-Q	001-36343	10.1	November 3, 2016
21.1	List of subsidiaries of the Registrant.				

Exhibit Number	Description	Incorporated By Reference		
		Form	SEC File No.	Exhibit Number
23.1	Consent of Deloitte & Touche LLP, independent registered public accounting firm.			
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act			
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act			
32.1 **	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act			
32.2 **	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act			
101.INS	XBRL Instance Document.			
101.SCH	XBRL Taxonomy Extension Schema Document.			
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.			
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.			
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.			
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.			

\* Indicates a management contract or compensatory plan.

\*\* The certifications attached as Exhibit 32.1 and 32.2 that accompany this Annual Report on Form 10-K are not deemed filed with the Securities and Exchange Commission and are not to be incorporated by reference into any filing of A10 Networks, Inc. under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, whether made before or after the date of this Annual Report on Form 10-K, irrespective of any general incorporation language contained in such filing.

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## BOARD OF DIRECTORS

### Peter Y. Chung

Managing Director and  
Chief Executive Officer, Summit Partners  
Chairman of Compensation Committee

### Phillip J. Salsbury

Lead Independent Director  
Chairman of Governance Committee

### Alan S. Henricks

Chairman of Audit Committee

### Robert Cochran

Executive Vice President of Legal and  
Corporate Collaboration, A10 Networks

### Lee Chen

Chief Executive Officer, A10 Networks

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## MANAGEMENT TEAM

### Lee Chen

Chief Executive Officer

### Shiva Natarajan

Interim Chief Financial Officer

### Robert Cochran

Executive Vice President of Legal and  
Corporate Collaboration

### Rajkumar Jalan

Chief Technology Officer

### Ray Smets

Executive Vice President of  
Worldwide Sales

### Neil Wu Becker

Vice President of Worldwide  
Marketing and Communications

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## ADDITIONAL CORPORATE INFORMATION

### General Legal Counsel

Wilson Sonsini Goodrich & Rosati, P.C.  
650 Page Mill Road  
Palo Alto, California 94304

### Investor Relations

3 W Plumeria Drive  
San Jose, California 95134  
Email: [investors@a10networks.com](mailto:investors@a10networks.com)  
<http://investors.a10networks.com>

### Independent Registered Public Accounting Firm

Deloitte & Touche LLP  
225 W Santa Clara Street  
Suite 600  
San Jose, California 95113

### Transfer Agent and Registrar

Computershare Trust Company, N.A.  
250 Royall Street  
Canton, Massachusetts 02021  
Phone: (800) 962-4284

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## CORPORATE HEADQUARTERS

3 W Plumeria Drive, San Jose, California 95134 | Phone: +1 (408) 325-8668 | Fax: +1 (408) 325-8666 | [www.a10networks.com](http://www.a10networks.com)

