A10 Networks, Inc.
Form 10-Q
August 05, 2016

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

Form 10-Q

(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 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	20-1446869
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
3 West Plumeria Drive San Jose, California	95134
(Address of Principal Executive Offices)	(Zip Code)

(408) 325-8668
(Registrant’s Telephone Number, Including Area Code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x 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 x No ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ¨	Accelerated filer x
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

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

As of July 29, 2016 the number of outstanding shares of the registrant's common stock, par value $0.00001 per share, was 65,772,934.

A10 Networks, Inc.
Quarterly Report on Form 10-Q
For the Three and Six Months Ended June 30, 2016

TABLE OF CONTENTS

	Page
PART I. FINANCIAL INFORMATION	2
Item 1. Condensed Consolidated Financial Statements (unaudited):	2
Condensed Consolidated Balance Sheets as of June 30, 2016 and December 31, 2015	2
Condensed Consolidated Statements of Operations for the Three and Six Months Ended June 30, 2016 and 2015	3
Condensed Consolidated Statements of Comprehensive Loss for the Three and Six Months Ended June 30, 2016 and 2015	
Condensed Consolidated Statements of Cash Flows for the Six Months Ended June 30, 2016 and 2015	5
Notes to Condensed Consolidated Financial Statements	6
Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations	22
Item 3. Quantitative and Qualitative Disclosures About Market Risk	34
Item 4. Controls and Procedures	35
PART II. OTHER INFORMATION	36
Item 1. Legal Proceedings	36
Item 1A. Risk Factors	36
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds	60
Item 3. Defaults Upon Senior Securities	60
Item 4. Mine Safety Disclosures	60
Item 5. Other Information	60
Item 6. Exhibits	60
Signatures	61
Exhibit Index	62

PART I. FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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

	June 30, 2016	December 31, 2015
ASSETS		
Current Assets:		
Cash and cash equivalents	$28,632	$ 98,117
Marketable securities	85,069	—
Accounts receivable, net of allowances of $4,614 and $4,067 as of June 30, 2016 and December 31, 2015	39,348	57,778
Inventory	14,333	18,291
Prepaid expenses and other current assets	5,427	5,064
Total current assets	172,809	179,250
Property and equipment, net	8,917	8,903
Goodwill and Intangible Assets	7,086	867
Other non-current assets	3,681	3,531
Total Assets	$192,493	$ 192,551
LIABILITIES AND STOCKHOLDERS’ EQUITY		
Current Liabilities:		
Accounts payable	$7,782	$ 10,508
Accrued liabilities	28,830	27,757
Deferred revenue, current	51,384	49,572
Total current liabilities	87,996	87,837
Deferred revenue, non-current	24,379	23,232
Other non-current liabilities	1,162	1,414
Total Liabilities	113,537	112,483
Commitments and contingencies (Note 5)		
Stockholders' Equity:		
Common stock, par value $0.00001 — 500,000 shares authorized as of June 30, 2016 and December 31, 2015; 65,585 and 64,172 shares issued and outstanding as of June 30, 2016 and December 31, 2015	1	1
Additional paid-in capital	315,156	301,886
Accumulated other comprehensive income	88	—
Accumulated deficit	(236,289)	(221,819)
Total Stockholders' Equity	78,956	80,068
Total Liabilities And Stockholders' Equity	$192,493	$ 192,551

See accompanying notes to the condensed consolidated financial statements.

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Revenue:				
Products	$38,797	$33,331	$75,171	$63,847
Services	18,333	14,205	35,763	27,706
Total revenue	57,130	47,536	110,934	91,553
Cost of revenue:				
Products	9,804	7,909	18,502	14,972
Services	4,405	3,692	8,934	7,415
Total cost of revenue	14,209	11,601	27,436	22,387
Gross profit	42,921	35,935	83,498	69,166
Operating expenses:				
Sales and marketing	26,773	24,962	53,541	49,484
Research and development	14,486	13,671	29,263	27,980
General and administrative	7,230	5,703	13,891	13,230
Litigation and settlement expense	202	1,025	1,993	1,470
Total operating expenses	48,691	45,361	98,688	92,164
Loss from operations	(5,770)	(9,426)	(15,190)	(22,998)
Other income (expense), net:				
Interest expense	(126)	(104)	(252)	(231)
Interest income and other income (expense), net	1,020	(216)	1,235	(189)
Total other income (expense), net	894	(320)	983	(420)
Loss before provision for income taxes	(4,876)	(9,746)	(14,207)	(23,418)
Provision for income taxes	59	231	263	293
Net loss	$(4,935)	$(9,977)	$(14,470)	$(23,711)
Net loss per share:				
Basic and diluted	$(0.08)	$(0.16)	$(0.22)	$(0.38)
Weighted-average shares used in computing net loss per share:				
Basic and diluted	64,861	61,945	64,584	61,690

See accompanying notes to the condensed consolidated financial statements.

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Net loss	$(4,935)	$(9,977)	$(14,470)	$(23,711)
Other comprehensive income, net of tax:				
Unrealized gain on marketable securities	32	—	88	—
Comprehensive loss	$(4,903)	$(9,977)	$(14,382)	$(23,711)

See accompanying notes to the condensed consolidated financial statements.

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

	Six Months Ended June 30,	
	2016	2015
Cash flows from operating activities:		
Net loss	$(14,470)	$(23,711)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	3,717	4,673
Stock-based compensation	8,481	8,638
Other non-cash items	1,051	273
Changes in operating assets and liabilities:		
Accounts receivable, net	17,535	7,723
Inventory	2,846	1,861
Prepaid expenses and other assets	(479)	44
Accounts payable	(2,668)	(3,048)
Accrued liabilities	348	(1,619)
Deferred revenue	2,960	8,559
Other	(65)	84
Net cash provided by operating activities	19,256	3,477
Cash flows from investing activities:		
Purchases of marketable securities	(92,682)	—
Proceeds from sales and maturities of marketable securities	7,609	—
Payment for acquisition	(4,380)	—
Purchases of property and equipment	(2,588)	(1,811)
Net cash used in investing activities	(92,041)	(1,811)
Cash flows from financing activities:		
Proceeds from issuance of common stock under employee equity incentive plans, net of repurchases	3,350	2,626
Other	(50)	—
Net cash provided by financing activities	3,300	2,626
Net increase (decrease) in cash and cash equivalents	(69,485)	4,292
Cash and cash equivalents—beginning of period	98,117	91,905
Cash and cash equivalents—end of period	$28,632	$96,197
Supplemental Disclosure of Non-Cash Investing and Financing Activities:		
Common stock issued under asset purchase agreement	$1,313	$—
Inventory transfers to property and equipment	$1,112	$1,187
Purchases of property and equipment included in accounts payable and accrued liabilities	$428	$486

See accompanying notes to the condensed consolidated financial statements.

A10 Networks, Inc.

Notes to Condensed Consolidated Financial Statements
(unaudited)

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 enterprises, service providers, Web giants and government organizations to accelerate, secure and optimize the performance of their data center applications and secure their users, applications and infrastructure from internet, web and network threats at scale. We offer four software based advanced application networking and network security solutions to address end-customer needs, including Application Delivery Controllers ("ADC") to optimize web and back-office application performance, Carrier Grade Network Address Translation ("CGN") to provide network address, protocol translation services for service provider networks, Threat Protection System ("TPS") for network-wide multi-vector DDoS security protection and Convergent Firewall ("CFW") for protecting data centers and mobile infrastructure, improving web security, and encrypting site-to-site communications. Our solutions are cloud-ready and available, in a variety of form factors such as optimized hardware appliances, in the cloud as software, and as virtual appliances.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of A10 Networks, Inc., and our wholly owned subsidiaries. All inter-company balances and transactions have been eliminated in consolidation.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”) and following the requirements of the Securities and Exchange Commission (“SEC”) for interim reporting. As permitted under those rules, certain notes or other financial information that are normally required by U.S. GAAP can be condensed or omitted. These financial statements have been prepared on the same basis as our annual financial statements and, in the opinion of management, reflect all adjustments, consisting only of normal recurring adjustments that are necessary for a fair presentation of our financial information. The results of operations for the three and six months ended June 30, 2016 are not necessarily indicative of the results to be expected for the year ending December 31, 2016 or for any other interim period or for any other future year. The balance sheet as of December 31, 2015 has been derived from audited financial statements at that date but does not include all of the information required by U.S. GAAP for complete financial statements.

The accompanying unaudited condensed consolidated financial statements should be read in conjunction with our audited consolidated financial statements for the year ended December 31, 2015, which are included in the Annual Report on Form 10-K for the year ended December 31, 2015 filed with the SEC on March 1, 2016.

Use of Estimates

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

Summary of Significant Accounting Policies

Marketable securities

We classify our investments in debt and equity securities as available-for-sale and record these investments at fair value. Investments with an original maturity of three months or less at the date of purchase are considered cash equivalents, while all other investments are classified as current assets based on their availability for use in current operations. Unrealized gains or losses are reported in accumulated other comprehensive income, net of taxes, in stockholders' equity. Realized gains and losses are determined based on the specific identification method, and are reflected in our Condensed Consolidated Statements of Operations. Realized gains or losses and charges for other-than-temporary declines in value, if any, on marketable securities are reported in interest income 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.

Goodwill

Goodwill is measured as the excess of consideration transferred and the net of the acquisition date fair value of assets acquired and liabilities assumed in a business acquisition. Goodwill is not amortized for accounting purposes. We review goodwill for possible impairment annually in the fourth quarter or whenever events or changes in circumstances indicate its carrying amount may not be recoverable. For annual goodwill impairment test in all periods to date, we operate under one reporting unit 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. Otherwise, no further testing 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 comparison of the fair value of a reporting unit with our carrying amount, including goodwill. If the fair value of the reporting unit is less than our 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, patent and acquired customer relationships resulting from acquisitions. Intangible assets are recorded at fair value and are amortized on a straight-line basis over their estimated useful lives, which range from five to ten years.

Impairment of Long-Lived Assets

We periodically evaluate whether changes have occurred that would render our long-lived assets not recoverable. If such circumstances arise, we use an estimate of the undiscounted value of expected future operating cash flows to determine whether the long-lived assets are impaired. If the aggregate undiscounted cash flows are less than the carrying amount of the assets, the resulting impairment charge to be recorded is calculated based on the excess of the carrying amount of the assets over the fair value of such assets, with the fair value generally determined based on an estimate of discounted future cash flows.

There have been no other changes to the significant accounting policies described in the Annual Report on Form 10-K for the year ended December 31, 2015, filed with the SEC on March 1, 2016, that have had a material impact on our condensed consolidated financial statements and related notes.

Concentration of Credit Risk and Significant Customers

Financial instruments that potentially subject us to concentrations of credit risk consist of cash, cash equivalents, marketable securities and accounts receivable. Our cash, cash equivalents and marketable securities are invested in high-credit quality financial instruments maintained with banks and financial institutions. Management believes that the financial institutions that hold our cash, cash equivalents and marketable securities are financially sound and, accordingly, are subject to minimal credit risk. In some instances, deposits held with banks and financial institutions may be in excess of insured limits provided on such deposits.

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 of our customers to assess the probability of accounts receivable collection based on a number of factors, including past transaction experience with the customer, evaluation of their credit history, limiting the credit extended 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 for the three and six months ended June 30, 2016 and 2015 are as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
Customers	2016	2015	2016	2015
Customer A (a distribution channel partner)	11%	*	11%	*
Customer B (a direct customer)	10%	14%	*	