

CALIX, INC
Form 10-Q
November 02, 2016
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 24, 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: 001-34674

Calix, Inc.
(Exact Name of Registrant as Specified in Its Charter)

Delaware 68-0438710
(State or Other Jurisdiction of (I.R.S. Employer
Incorporation or Organization) Identification No.)
1035 N. McDowell Blvd., Petaluma, CA 94954
(Address of Principal Executive Offices) (Zip Code)
(707) 766-3000
(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) the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes: No:

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

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 definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer Accelerated Filer

Non-accelerated filer (Do not check if a smaller reporting Company) Smaller Reporting Company

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

As of October 24, 2016, there were 48,789,247 shares of the Registrant's common stock, par value \$0.025 outstanding.

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PART I. FINANCIAL INFORMATION

ITEM 1. Financial Statements

CALIX, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except par value and share data)

	September 24, 2016 (Unaudited)	December 31, 2015 (See Note 1)
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 31,764	\$ 23,626
Marketable securities	29,554	49,964
Accounts receivable, net	57,256	47,155
Inventory	40,190	47,667
Deferred cost of revenue	14,718	4,918
Prepaid expenses and other current assets	15,700	9,470
Total current assets	189,182	182,800
Property and equipment, net	16,017	17,149
Goodwill	116,175	116,175
Intangible assets, net	1,627	6,618
Other assets	937	1,144
Total assets	\$ 323,938	\$ 323,886
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 19,340	\$ 19,603
Accrued liabilities	49,019	35,512
Deferred revenue	16,226	12,124
Total current liabilities	84,585	67,239
Long-term portion of deferred revenue	19,850	19,569
Other long-term liabilities	979	1,293
Total liabilities	105,414	88,101
Commitments and contingencies (See Note 7)		
Stockholders' equity:		
Preferred stock, \$0.025 par value; 5,000,000 shares authorized; no shares issued and outstanding as of September 24, 2016 and December 31, 2015	—	—
Common stock, \$0.025 par value; 100,000,000 shares authorized; 54,118,410 shares issued and 48,788,593 shares outstanding as of September 24, 2016, and 53,049,781 shares issued and 49,509,251 shares outstanding as of December 31, 2015	1,353	1,326
Additional paid-in capital	830,225	818,754
Accumulated other comprehensive loss	(226) (195)
Accumulated deficit	(572,842) (556,923)
Treasury stock, 5,329,817 shares and 3,540,530 shares as of September 24, 2016 and December 31, 2015, respectively	(39,986) (27,177)
Total stockholders' equity	218,524	235,785
Total liabilities and stockholders' equity	\$ 323,938	\$ 323,886

See accompanying notes to condensed consolidated financial statements.

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CALIX, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(In thousands, except per share data)

(Unaudited)

	Three Months Ended		Nine Months Ended	
	September 30,	September 26,	September 30,	September 26,
	2016	2015	2016	2015
Revenue	\$121,187	\$ 112,297	\$326,987	\$ 302,464
Cost of revenue:				
Products and services ⁽¹⁾	66,830	57,096	174,665	152,308
Amortization of intangible assets	813	2,088	3,290	6,264
Total cost of revenue	67,643	59,184	177,955	158,572
Gross profit	53,544	53,113	149,032	143,892
Operating expenses:				
Research and development ⁽¹⁾	28,119	22,120	75,925	66,885
Sales and marketing ⁽¹⁾	20,575	18,424	58,850	57,398
General and administrative ⁽¹⁾	8,615	9,140	32,940	28,728
Amortization of intangible assets	—	2,552	1,701	7,656
Litigation settlement gain	(4,500)	—	(4,500)	—
Total operating expenses	52,809	52,236	164,916	160,667
Income (loss) from operations	735	877	(15,884)	(16,775)
Interest and other income (expense), net:				
Interest income	184	297	611	1,014
Interest expense	(155)	(263)	(489)	(921)
Other income (expense), net	81	196	297	273
Income (loss) before provision for income taxes	845	1,107	(15,465)	(16,409)
Provision for income taxes	209	185	454	378
Net income (loss)	\$636	\$ 922	\$(15,919)	\$(16,787)
Net income (loss) per common share:				
Basic	\$0.01	\$ 0.02	\$(0.33)	\$(0.32)
Diluted	\$0.01	\$ 0.02	\$(0.33)	\$(0.32)
Weighted-average number of shares used to compute net income (loss) per common share:				
Basic	48,773	51,756	48,578	51,814
Diluted	49,309	52,016	48,578	51,814
Net income (loss)	\$636	\$ 922	\$(15,919)	\$(16,787)
Other comprehensive income (loss), net of tax:				
Unrealized gains (losses) on available-for-sale marketable securities, net	(9)	30	97	66
Foreign currency translation adjustments, net	(87)	(196)	(128)	(177)
Total other comprehensive income (loss), net of tax	(96)	(166)	(31)	(111)
Comprehensive income (loss)	\$540	\$ 756	\$(15,950)	\$(16,898)

⁽¹⁾ Includes stock-based compensation as follows:

Cost of revenue	\$174	\$ 163	\$484	\$ 549
Research and development	1,573	964	3,719	3,659
Sales and marketing	1,661	688	3,323	3,769

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General and administrative	1,269	775	2,840	2,616
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See accompanying notes to condensed consolidated financial statements.

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CALIX, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Nine Months Ended	
	September 26, 2016	September 26, 2015
Operating activities:		
Net loss	\$(15,919)	\$(16,787)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	6,282	7,602
Loss on retirement of property and equipment	—	14
Amortization of intangible assets	4,991	13,920
Amortization of premiums related to available-for-sale securities	337	743
Stock-based compensation	10,366	10,593
Changes in operating assets and liabilities:		
Restricted cash	—	295
Accounts receivable, net	(10,104)	(17,443)
Inventory	7,477	2,983
Deferred cost of revenue	(9,800)	2,082
Prepaid expenses and other assets	(6,058)	4,181
Accounts payable	(356)	(6,841)
Accrued liabilities	13,974	(1,055)
Deferred revenue	4,383	(1,312)
Other long-term liabilities	(313)	(167)
Net cash provided by (used in) operating activities	5,260	(1,192)
Investing activities:		
Purchases of property and equipment	(5,364)	(5,943)
Purchases of marketable securities	—	(46,750)
Maturities of marketable securities	20,170	51,265
Net cash provided by (used in) investing activities	14,806	(1,428)
Financing activities:		
Proceeds from exercise of stock options	14	625
Proceeds from employee stock purchase plan	2,905	2,865
Payments for repurchases of common stock	(12,809)	(11,124)
Taxes paid for awards vested under equity incentive plans	(1,787)	(2,093)
Net cash used in financing activities	(11,677)	(9,727)
Effect of exchange rate changes on cash and cash equivalents	(251)	(288)
Net increase (decrease) in cash and cash equivalents	8,138	(12,635)
Cash and cash equivalents at beginning of period	23,626	48,829
Cash and cash equivalents at end of period	\$31,764	\$36,194

See accompanying notes to condensed consolidated financial statements.

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CALIX, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Company and Basis of Presentation

Company

Calix, Inc. (together with its subsidiaries, "Calix," the "Company," "our," "we," or "us") was incorporated in August 1999, and is a Delaware corporation. The Company is a leading global provider of broadband communications access systems and software for fiber- and copper-based network architectures that enable communications service providers ("CSPs") to transform their networks and connect to their residential and business subscribers. The Company enables CSPs to provide a wide range of revenue-generating services, from basic voice and data to advanced broadband services, over legacy and next-generation access networks. The Company focuses solely on CSP access networks, the portion of the network that governs available bandwidth and determines the range and quality of services that can be offered to subscribers. The Company develops and sells carrier-class hardware and software products, referred to as the Unified Access portfolio, which are designed to enhance and transform CSP access networks to meet the changing demands of subscribers rapidly and cost-effectively.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements, including the accounts of Calix, Inc. and its wholly-owned subsidiaries, have been prepared in accordance with the requirements of the U.S. Securities and Exchange Commission ("SEC") for interim reporting. As permitted under those rules, certain footnotes or other financial information that are normally required by U.S. generally accepted accounting principles ("GAAP") can be condensed or omitted. In the opinion of management, the financial statements include all normal and recurring adjustments that are considered necessary for the fair presentation of the Company's financial position and operating results. All significant intercompany balances and transactions have been eliminated in consolidation. The Condensed Consolidated Balance Sheet at December 31, 2015 has been derived from the audited financial statements at that date. The results of the Company's operations can vary during each quarter of the year. Therefore, the results and trends in these interim financial statements may not be the same as those for the full year or any future periods. The information included in this Quarterly Report on Form 10-Q should be read in conjunction with the audited financial statements included in the Company's Form 10-K for the year ended December 31, 2015.

The Company's fiscal year begins on January 1st and ends on December 31st. Quarterly periods are based on a 4-4-5 fiscal calendar with the first, second and third fiscal quarters ending on the 13th Saturday of each fiscal period. As a result, the Company had one fewer day in the nine months ended September 24, 2016 than in the nine months ended September 26, 2015. The preparation of financial statements in conformity with GAAP for interim financial reporting requires management to make estimates and assumptions that affect the amounts reported in the condensed consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

2. Significant Accounting Policies

The Company's significant accounting policies are disclosed in our Annual Report on Form 10-K for the year ended December 31, 2015. Our significant accounting policies did not change during the nine months ended September 24, 2016.

Concentration of Customer Risk

The Company had two customers that each accounted for more than 10% of its total revenue for the three and nine months ended September 24, 2016 and one of these customers accounted for more than 10% of the Company's total revenue for the three and nine months ended September 26, 2015. These two customers together represented 37% and 34% of the Company's total revenue for the three and nine months ended September 24, 2016, respectively, and 27% and 26% of the Company's total revenue for the three and nine months ended September 26, 2015, respectively. Each of these two customers represented more than 10% of the Company's accounts receivable as of September 24, 2016 and one of these customers represented more than 10% of the Company's accounts receivable as of December 31, 2015.

Recent Accounting Pronouncements

In March 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update No. 2016-09, Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting ("ASU 2016-09"), which simplifies several aspects of the accounting for employee share-based payment transactions for both public and nonpublic entities, including the accounting for income taxes, forfeitures, and statutory tax withholding requirements, as well as classification in the statement of cash flows. ASU 2016-09 will be effective for the Company beginning in the first quarter of fiscal 2017. Early application is permitted in any interim or annual period, with any adjustments reflected as of the beginning of the fiscal year of adoption. The Company is currently assessing the potential impact of adopting this new guidance on its consolidated financial statements.

In February 2016, the FASB issued Accounting Standards Update No. 2016-02, Leases (Topic 842) ("ASU 2016-02"), which requires recognition of an asset and liability for lease arrangements longer than twelve months. ASU 2016-02 will be effective for the Company beginning in the first quarter of fiscal 2019. Early application is permitted, and it is required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. The Company is currently assessing the potential impact of adopting this new guidance on its consolidated financial statements.

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In July 2015, the FASB issued Accounting Standards Update No. 2015-11, Inventory (Topic 330): Simplifying the Measurement of Inventory ("ASU 2015-11"), which requires measurement of inventory at lower of cost and net realizable value, versus lower of cost or market. Net realizable value is the estimated selling price in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. ASU 2015-11 will be effective for the Company beginning in the first quarter of fiscal 2017. Early application is permitted, and the guidance should be applied prospectively. The Company is currently assessing the potential impact of adopting this new guidance on its consolidated financial statements.

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (Topic 606) ("ASU 2014-09"), which provides guidance for revenue recognition. ASU 2014-09 supersedes the revenue recognition requirements in Topic 605, Revenue Recognition, and most industry-specific guidance. Additionally, it supersedes some cost guidance included in Subtopic 605-35, Revenue Recognition-Construction-Type and Production-Type Contracts, and creates new Subtopic 340-40, Other Assets and Deferred Costs-Contracts with Customers. The standard's core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. In doing so, companies will need to use more judgment and make more estimates than under the previous guidance. These may include identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. On August 12, 2015, the FASB issued Accounting Standards Update No. 2015-14, Revenue from Contracts with Customers (Topic 606), Deferral of the Effective Date ("ASU 2015-14") to defer the effective date of ASU 2014-09 by one year. As a result, the standard will be effective for the Company in the first quarter of fiscal 2018. ASU 2015-14 permits early adoption of the new revenue standard, but not before its original effective date. The Company is currently assessing the method of adoption and the potential impact of adopting this new guidance on its consolidated financial statements.

3. Cash, Cash Equivalents and Marketable Securities

The Company has invested its excess cash primarily in money market funds and highly liquid marketable securities such as corporate debt instruments, U.S. government agency securities and commercial paper. The Company considers all investments with maturities of three months or less when purchased to be cash equivalents. Marketable securities represent highly liquid corporate debt instruments, U.S. government agency securities and commercial paper with maturities greater than 90 days at date of purchase. Marketable securities with maturities greater than one year are classified as current because management considers all marketable securities to be available for current operations.

Cash equivalents are stated at amounts that approximate fair value based on quoted market prices. Marketable securities are recorded at their fair values.

The Company's investments have been classified and accounted for as available-for-sale. Such investments are recorded at fair value and unrealized holding gains and losses are reported as a separate component of accumulated other comprehensive income (loss) in the stockholders' equity until realized. Realized gains and losses on sales of marketable securities, if any, are determined on the specific identification method and are reclassified from accumulated other comprehensive income (loss) to results of operations as other income (expense).

The Company, to date, has not determined that any of the unrealized losses on its investments are considered to be other-than-temporary. The Company reviews its investment portfolio to determine if any security is other-than-temporarily impaired, which would require the Company to record an impairment charge in the period any such determination is made. In making this judgment, the Company evaluates, among other things: the duration and extent to which the fair value of a security is less than its cost; the financial condition of the issuer and any changes thereto; and the Company's intent and ability to hold its investment for a period of time sufficient to allow for any anticipated recovery in market value, or whether the Company will more likely than not be required to sell the security before recovery of its amortized cost basis. The Company has evaluated its investments as of September 24, 2016 and has determined that no investments with unrealized losses are other-than-temporarily impaired. No investments have been in a continuous loss position greater than one year.

Cash, cash equivalents and marketable securities consisted of the following (in thousands):

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	September 24, 2016	December 31, 2015
Cash and cash equivalents:		
Cash	\$ 17,708	\$ 13,378
Money market funds	14,056	10,248
Total cash and cash equivalents	31,764	23,626
Marketable securities:		
Corporate debt securities	23,051	35,799
U.S. government agency securities	6,503	10,520
Commercial paper	—	3,645
Total marketable securities	29,554	49,964
Total cash, cash equivalents and marketable securities	\$ 61,318	\$ 73,590

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The carrying amounts of our money market funds approximate their fair values due to their nature, duration and short maturities.

As of September 24, 2016, the amortized cost and fair value of marketable securities were as follows (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Corporate debt securities	\$ 23,050	\$ 4	\$ (3)	\$23,051
U.S. government agency securities	6,501	2	—	6,503
Total marketable securities	\$ 29,551	\$ 6	\$ (3)	\$29,554

As of December 31, 2015, the amortized cost and fair value of marketable securities were as follows (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Corporate debt securities	\$ 35,869	\$ 2	\$ (72)	\$35,799
U.S. government agency securities	10,544	—	(24)	10,520
Commercial paper	3,645	—	—	3,645
Total marketable securities	\$ 50,058	\$ 2	\$ (96)	\$49,964

As of September 24, 2016, the amortized cost and fair value of marketable securities by contractual maturity were as follows (in thousands):

	Amortized Cost	Fair Value
Due in 1 year or less	\$ 29,551	\$29,554

4. Fair Value Measurements

In accordance with Accounting Standard Codification (“ASC”) Topic 820, Fair Value Measurements and Disclosures, (“ASC Topic 820”), the Company measures its cash equivalents and marketable securities at fair value on a recurring basis. ASC Topic 820 clarifies that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. As a basis for considering such assumptions, ASC Topic 820 establishes a three-tier value hierarchy, which prioritizes the inputs used in measuring fair value as follows:

Level 1 – Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 – Observable inputs other than quoted prices included in Level 1 for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-driven valuations in which all significant inputs and significant value drivers are observable in active markets.

Level 3 – Unobservable inputs to the valuation derived from fair valuation techniques in which one or more significant inputs or significant value drivers are unobservable.

The following table sets forth the Company's financial assets measured at fair value on a recurring basis as of September 24, 2016 and December 31, 2015, based on the three-tier fair value hierarchy (in thousands):

As of September 24, 2016	Level 1	Level 2	Total
Money market funds	\$14,056	\$—	\$14,056
Corporate debt securities	—	23,051	23,051
U.S. government agency securities	—	6,503	6,503
Total	\$14,056	\$29,554	\$43,610

As of December 31, 2015	Level 1	Level 2	Total
Money market funds	\$10,248	\$—	—\$10,248
Corporate debt securities	—	35,799	35,799

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U.S. government agency securities	—	10,520	10,520
Commercial paper	—	3,645	