

CALIX, INC
Form 10-Q
July 31, 2014
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 28, 2014

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	<input type="checkbox"/>	Accelerated Filer	<input checked="" type="checkbox"/>
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Non-accelerated filer	<input type="checkbox"/>	(Do not check if a smaller reporting Company)	Smaller Reporting Company	<input type="checkbox"/>
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Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes: ☐ No: ☒

As of July 21, 2014, there were 50,914,092 shares of the Registrant's common stock, par value \$0.025 outstanding.

Table of Contents

Calix, Inc.

Form 10-Q

TABLE OF CONTENTS

<u>PART I. FINANCIAL INFORMATION</u>	<u>3</u>
<u>Item 1. Financial Statements (Unaudited)</u>	<u>3</u>
<u>Condensed Consolidated Balance Sheets</u>	<u>3</u>
<u>Condensed Consolidated Statements of Comprehensive Loss</u>	<u>4</u>
<u>Condensed Consolidated Statements of Cash Flows</u>	<u>5</u>
<u>Notes to Condensed Consolidated Financial Statements</u>	<u>6</u>
<u>Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>16</u>
<u>Overview</u>	<u>17</u>
<u>Critical Accounting Policies and Estimates</u>	<u>17</u>
<u>Results of Operations</u>	<u>18</u>
<u>Liquidity and Capital Resources</u>	<u>20</u>
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	<u>22</u>
<u>Item 4. Controls and Procedures</u>	<u>22</u>
<u>PART II. OTHER INFORMATION</u>	<u>24</u>
<u>Item 1. Legal Proceedings</u>	<u>24</u>
<u>Item 1A. Risk Factors</u>	<u>24</u>
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>36</u>
<u>Item 3. Defaults Upon Senior Securities</u>	<u>36</u>
<u>Item 4. Mine Safety Disclosures</u>	<u>37</u>
<u>Item 5. Other Information</u>	<u>37</u>
<u>Item 6. Exhibits</u>	<u>38</u>
<u>SIGNATURES</u>	<u>39</u>

Table of Contents

PART I. FINANCIAL INFORMATION

ITEM 1. Financial Statements (Unaudited)

CALIX, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except share and per share data)

	June 28, 2014 (Unaudited)	December 31, 2013 (See Note 1)
ASSETS		
Current assets:		
Cash and cash equivalents	\$32,543	\$82,747
Marketable securities	46,439	—
Restricted cash	295	295
Accounts receivable, net	47,330	43,520
Inventory	45,888	51,071
Deferred cost of revenue	15,957	21,076
Prepaid expenses and other current assets	5,038	5,757
Total current assets	193,490	204,466
Property and equipment, net	17,289	17,473
Goodwill	116,175	116,175
Intangible assets, net	34,460	43,740
Other assets	1,503	1,745
Total assets	\$362,917	\$383,599
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$12,850	\$23,163
Accrued liabilities	34,689	32,075
Deferred revenue	26,346	34,862
Total current liabilities	73,885	90,100
Long-term portion of deferred revenue	18,640	18,431
Other long-term liabilities	958	1,145
Total liabilities	93,483	109,676
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 June 28, 2014 and December 31, 2013	—	—
Common stock, \$0.025 par value; 100,000,000 shares authorized; 50,910,446 shares and 50,224,952 shares issued and outstanding as of June 28, 2014 and December 31, 2013, respectively	1,273	1,256
Additional paid-in capital	791,756	782,253
Accumulated other comprehensive income	159	190
Accumulated deficit	(523,754)	(509,776)
Total stockholders' equity	269,434	273,923
Total liabilities and stockholders' equity	\$362,917	\$383,599

See accompanying notes to condensed consolidated financial statements.

Table of Contents

CALIX, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(In thousands, except per share data)

(Unaudited)

	Three Months Ended		Six Months Ended	
	June 28, 2014	June 29, 2013	June 28, 2014	June 29, 2013
Revenue	\$98,005	\$94,439	\$183,825	\$184,987
Cost of revenue:				
Products and services ⁽¹⁾	51,575	49,846	98,381	97,191
Amortization of intangible assets	2,088	2,088	4,176	4,176
Total cost of revenue	53,663	51,934	102,557	101,367
Gross profit	44,342	42,505	81,268	83,620
Operating expenses:				
Research and development ⁽¹⁾	19,544	20,035	39,174	40,206
Sales and marketing ⁽¹⁾	18,455	17,079	35,845	32,880
General and administrative ⁽¹⁾	7,681	7,684	14,932	15,815
Amortization of intangible assets	2,552	2,552	5,104	5,104
Total operating expenses	48,232	47,350	95,055	94,005
Loss from operations	(3,890)	(4,845)	(13,787)	(10,385)
Interest and other income (expense), net:				
Interest income	30	1	34	2
Interest expense	(58)	(42)	(115)	(70)
Other income (expense), net	70	(43)	103	(322)
Loss before provision for income taxes	(3,848)	(4,929)	(13,765)	(10,775)
Provision for income taxes	103	224	213	581
Net loss	\$(3,951)	\$(5,153)	\$(13,978)	\$(11,356)
Net loss per common share:				
Basic and diluted	\$(0.08)	\$(0.10)	\$(0.28)	\$(0.23)
Weighted-average number of shares used to compute net loss per common share:				
Basic and diluted	50,573	49,153	50,425	49,034
Other comprehensive (loss) income, net of tax:				
Unrealized gains (losses) on available-for-sale marketable securities adjustment, net	(25)	—	(25)	—
Foreign currency translation adjustment, net	(17)	30	(6)	12
Total other comprehensive (loss) income	(42)	30	(31)	12
Comprehensive loss	\$(3,993)	\$(5,123)	\$(14,009)	\$(11,344)

⁽¹⁾ Includes stock-based compensation as follows:

Cost of revenue	\$354	\$377	\$708	\$728
Research and development	1,306	1,300	2,486	2,486
Sales and marketing	1,462	1,464	2,830	2,743
General and administrative	1,282	2,134	2,282	4,037
	\$4,404	\$5,275	\$8,306	\$9,994

See accompanying notes to condensed consolidated financial statements.

Table of Contents

CALIX, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Six Months Ended	
	June 28, 2014	June 29, 2013
Operating activities:		
Net loss	\$(13,978)	\$(11,356)
Adjustments to reconcile net loss to net cash (used in) provided by operating activities:		
Depreciation and amortization	4,522	5,363
Loss on retirement of property and equipment	—	560
Amortization of intangible assets	9,280	9,280
Amortization of premiums related to available-for-sale securities	108	—
Stock-based compensation	8,306	9,994
Changes in operating assets and liabilities:		
Accounts receivable, net	(3,809)	(3,207)
Inventory	5,183	5,880
Deferred cost of revenue	5,119	(7,991)
Prepaid expenses and other assets	960	(2,009)
Accounts payable	(10,313)	(90)
Accrued liabilities	2,601	464
Deferred revenue	(8,307)	16,001
Other long-term liabilities	(188)	311
Net cash (used in) provided by operating activities	(516)	23,200
Investing activities:		
Purchase of marketable securities	(46,572)	—
Purchase of property and equipment	(4,328)	(3,265)
Net cash used in investing activities	(50,900)	(3,265)
Financing activities:		
Proceeds from exercise of stock options	139	288
Proceeds from employee stock purchase plan	2,453	2,464
Taxes paid for awards vested under equity incentive plans	(1,377)	(312)
Net cash (used in) provided by financing activities	1,215	2,440
Effect of exchange rate changes on cash and cash equivalents	(3)	9
Net (decrease) increase in cash and cash equivalents	(50,204)	22,384
Cash and cash equivalents at beginning of period	82,747	46,995
Cash and cash equivalents at end of period	\$32,543	\$69,379
Non-cash investing activities:		
Property and equipment acquired using credits from Ericsson Inc.	\$—	\$125

See accompanying notes to condensed consolidated financial statements.

Table of Contents

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 provider in North America 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, which the Company refers to as the Unified Access portfolio, that 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, 2013 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 for the year ended December 31, 2013, included in the Company's Form 10-K.

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 six months ended June 28, 2014 than in the six months ended June 29, 2013, and the same number of days in the three months ended June 28, 2014 as in the three months ended June 29, 2013. 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, 2013. Our significant accounting policies did not change during the six months ended June 28, 2014.

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ("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. The standard will be effective for the Company in the first quarter of fiscal 2017. Early adoption is not permitted. The Company is currently assessing the potential impact on its financial statements from adopting this new guidance.

In July 2013, the FASB issued Accounting Standards Update No. 2013-11, Income Taxes (Topic 740): Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists (a consensus of the FASB Emerging Issues Task Force) ("ASU 2013-11"), which provides explicit guidance on the financial statement presentation of an unrecognized tax benefit when a net operating loss carryforward or a tax credit carryforward exists. Under the new standard update, the Company's unrecognized tax benefit should be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward or a tax credit carryforward. The amendments should be applied prospectively to all unrecognized tax benefits that exist at the effective date. The accounting standard update became effective for the Company in the first quarter of 2014. As the Company's disclosures

Table of Contents

already conform to the required presentation, adoption of this standard did not impact the financial position or results of operations of the Company.

3. Cash, Cash Equivalents and Marketable Securities

The Company has invested its excess cash primarily in money market funds and highly liquid corporate debt instruments. The Company considers all investments with maturities of three months or less when purchased to be cash equivalents. Marketable securities represent highly liquid debt instruments 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.

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 in stockholders' equity until realized. Realized gains and losses on sales of marketable securities, if any, are reclassified from accumulated other comprehensive income 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 sell, 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 June 28, 2014 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):

	June 28, 2014	December 31, 2013
Cash and cash equivalents:		
Cash	\$17,377	\$62,905
Money market funds	15,166	19,842
Total cash and cash equivalents	32,543	82,747
Marketable securities:		
Corporate debt securities	41,048	—
Commercial paper	5,391	—
Total marketable securities	46,439	—
Total cash, cash equivalents and marketable securities	\$78,982	\$82,747

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

As of June 28, 2014, 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	\$41,073	\$1	\$(26)	\$41,048
Commercial paper	5,391	—	\$—	5,391
Total marketable securities	\$46,464	\$1	\$(26)	\$46,439

As of June 28, 2014, there are no available-for-sale securities that have been in a continuous unrealized loss position in excess of twelve months.

As of June 28, 2014, the amortized cost and fair value of marketable securities by contractual maturity were as follows (in thousands):

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	Amortized Cost	Fair Value
Due in 1 year or less	\$23,744	\$23,734
Due in 1-2 years	\$22,720	\$22,705
Total marketable securities	\$46,464	\$46,439

7

Table of Contents

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 June 28, 2014 and December 31, 2013, based on the three-tier fair value hierarchy (in thousands):

As of June 28, 2014	Level 1	Level 2	Total
Money market funds	\$15,166	\$—	\$15,166
Corporate debt securities	—	41,048	41,048
Commercial paper	—	5,391	5,391
Total	\$15,166	\$46,439	\$61,605

As of December 31, 2013	Level 1	Level 2	Total
Money market funds	\$19,842	\$—	\$19,842
Corporate debt securities	—	—	—
Commercial paper	—	—	—
Total	\$19,842	\$—	\$19,842

The fair values of money market funds classified as Level 1 were derived from quoted market prices as active markets for these instruments exist. The fair values of corporate debt securities and commercial paper classified as Level 2 were derived from quoted market prices for similar instruments indexed to prevailing market yield rates. The Company has no level 3 financial assets. The Company did not have any transfers between Level 1 and Level 2 of the fair value hierarchy during the six months ended June 28, 2014 and June 29, 2013.

5. Goodwill and Intangible Assets

Goodwill

Goodwill was recorded as a result of the Company's acquisitions of Occam Networks, Inc. ("Occam") in February 2011 and Optical Solutions, Inc. ("OSI") in February 2006. This goodwill is not deductible for tax purposes, and there have been no adjustments to goodwill since the acquisition dates.

Goodwill is not amortized but instead is subject to an annual impairment test or more frequently if events or changes in circumstances indicate that it may be impaired. We evaluate goodwill on an annual basis at the end of the second quarter of each year. Management has determined that we operate as a single reporting unit and, therefore, evaluates goodwill impairment at the enterprise level. Management assessed qualitative factors to determine whether it was more likely than not (that is, a likelihood of more than 50 percent) that the fair value of the Company was less than its carrying amount, including goodwill, as of June 28, 2014. In assessing the qualitative factors, management considered the impact of these key factors: macro-economic conditions, industry and market environment, overall financial performance of the Company, cash flow from operating activities, market capitalization and stock price. Management concluded that the fair value of the Company was more likely than not greater than its carrying amount as of June 28, 2014. As such, it was not necessary to perform the two-step goodwill impairment test at the time.

Based on the above assessment, the Company concluded that there was no impairment to the carrying value of the Company's goodwill as of June 28, 2014.

Table of Contents

Intangible Assets

Intangible assets are carried at cost, less accumulated amortization. The details of intangible assets as of June 28, 2014 and December 31, 2013 are disclosed in the following table (in thousands):

	June 28, 2014			December 31, 2013		
	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
Core developed technology	\$68,964	\$(51,515)	) \$17,449	\$68,964	\$(47,339)	) \$21,625
Customer relationships	54,740	(37,729)	) 17,011	54,740	(32,625)	) 22,115
Total intangible assets, excluding goodwill	\$123,704	\$(89,244)	) \$34,460	\$123,704	\$(79,964)	) \$43,740