

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

Form 10-Q

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

For the quarterly period ended March 26, 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: 001-33486

Infinera Corporation

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

77-0560433

(IRS Employer
Identification No.)

**140 Caspian Court
Sunnyvale, CA 94089**

(Address of principal executive offices, including zip code)

(408) 572-5200

(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 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 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

Non-accelerated filer

Smaller reporting company

(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

As of April 27, 2016, 141,465,906 shares of the registrant's Common Stock, \$0.001 par value, were issued and outstanding.

[Table of Contents](#)

INFINERA CORPORATION
QUARTERLY REPORT ON FORM 10-Q
FOR THE FISCAL QUARTER ENDED MARCH 26, 2016
INDEX

	<u>Page</u>
<u>PART I. FINANCIAL INFORMATION</u>	
Item 1.	Condensed Consolidated Financial Statements (Unaudited) 3
	Condensed Consolidated Balance Sheets – As of March 26, 2016 and December 26, 2015 3
	Condensed Consolidated Statements of Operations – Three months ended March 26, 2016 and March 28, 2015 4
	Condensed Consolidated Statements of Comprehensive Income – Three months ended March 26, 2016 and March 28, 2015 5
	Condensed Consolidated Statements of Cash Flows – Three months ended March 26, 2016 and March 28, 2015 6
	Notes to Condensed Consolidated Financial Statements 7
Item 2.	Management’s Discussion and Analysis of Financial Condition and Results of Operations 25
Item 3.	Quantitative and Qualitative Disclosures about Market Risk 32
Item 4.	Controls and Procedures 32
<u>PART II. OTHER INFORMATION</u>	
Item 1.	Legal Proceedings 33
Item 1A.	Risk Factors 34
Item 6.	Exhibits 51
	Signature Page 52

PART I. FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

INFINERA CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except par values)
(Unaudited)

	March 26, 2016	December 26, 2015
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 179,974	\$ 149,101
Short-term investments	95,116	125,561
Accounts receivable, net of allowance for doubtful accounts of \$630 in 2016 and \$630 in 2015	184,309	186,243
Inventory	189,744	174,699
Prepaid expenses and other current assets	29,689	29,511
Total current assets	678,832	665,115
Property, plant and equipment, net	115,372	110,861
Intangible assets	151,311	156,319
Goodwill	193,498	191,560
Long-term investments	80,488	76,507
Cost-method investment	14,500	14,500
Long-term restricted cash	5,331	5,310
Other non-current assets	4,032	4,009
Total assets	\$ 1,243,364	\$ 1,224,181
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 83,035	\$ 92,554
Accrued expenses	33,319	33,736
Accrued compensation and related benefits	34,572	49,887
Accrued warranty	17,663	17,889
Deferred revenue	48,285	42,977
Total current liabilities	216,874	237,043
Long-term debt, net	125,796	123,327
Accrued warranty, non-current	22,336	20,955
Deferred revenue, non-current	18,391	13,881
Deferred tax liability	35,436	35,731
Other long-term liabilities	18,528	16,183
Commitments and contingencies (Note 16)		
Stockholders' equity:		
Preferred stock, \$0.001 par value		
Authorized shares – 25,000 and no shares issued and outstanding	—	—
Common stock, \$0.001 par value		
Authorized shares – 500,000 as of March 26, 2016 and December 26, 2015		
Issued and outstanding shares – 141,425 as of March 26, 2016 and 140,197 as of December 26, 2015	141	140
Additional paid-in capital	1,313,783	1,300,301
Accumulated other comprehensive income	4,774	1,123
Accumulated deficit	(527,398)	(539,413)
Total Infinera Corporation stockholders' equity	791,300	762,151
Noncontrolling interest	14,703	14,910
Total stockholders' equity	806,003	777,061
Total liabilities and stockholders' equity	\$ 1,243,364	\$ 1,224,181

The accompanying notes are an integral part of these condensed consolidated financial statements.

INFINERA CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)
(Unaudited)

	Three Months Ended	
	March 26, 2016	March 28, 2015
Revenue:		
Product	\$ 216,082	\$ 160,843
Services	28,736	26,019
Total revenue	244,818	186,862
Cost of revenue:		
Cost of product	118,062	89,506
Cost of services	10,418	9,244
Total cost of revenue	128,480	98,750
Gross profit	116,338	88,112
Operating expenses:		
Research and development	54,145	39,257
Sales and marketing	30,009	21,042
General and administrative	17,313	12,656
Total operating expenses	101,467	72,955
Income from operations	14,871	15,157
Other income (expense), net:		
Interest income	522	414
Interest expense	(3,155)	(2,890)
Other gain (loss), net	(214)	301
Total other income (expense), net	(2,847)	(2,175)
Income before income taxes	12,024	12,982
Provision for income taxes	216	616
Net income	11,808	12,366
Less: Loss attributable to noncontrolling interest	(207)	—
Net income attributable to Infinera Corporation	\$ 12,015	\$ 12,366
Net income per common share attributable to Infinera Corporation:		
Basic	\$ 0.09	\$ 0.10
Diluted	\$ 0.08	\$ 0.09
Weighted average shares used in computing net income per common share:		
Basic	140,805	127,840
Diluted	146,880	137,304

The accompanying notes are an integral part of these condensed consolidated financial statements.

INFINERA CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(In thousands)
(Unaudited)

	Three Months Ended	
	March 26, 2016	March 28, 2015
Net income	\$ 11,808	\$ 12,366
Other comprehensive income:		
Unrealized gain on available-for-sale investments	383	267
Foreign currency translation adjustment	3,268	(159)
Net change in accumulated other comprehensive income	3,651	108
Less: Comprehensive loss attributable to noncontrolling interest	(207)	—
Comprehensive income attributable to Infinera Corporation	\$ 15,252	\$ 12,474

The accompanying notes are an integral part of these condensed consolidated financial statements.

INFINERA CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Three Months Ended	
	March 26, 2016	March 28, 2015
Cash Flows from Operating Activities:		
Net income	\$ 11,808	\$ 12,366
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	14,666	6,586
Amortization of debt discount and issuance costs	2,469	2,234
Amortization of premium on investments	481	954
Stock-based compensation expense	7,987	7,208
Other gain	—	(19)
Changes in assets and liabilities:		
Accounts receivable	2,165	23,391
Inventory	(16,155)	(12,103)
Prepaid expenses and other assets	(274)	1,141
Accounts payable	(9,041)	(10,317)
Accrued liabilities and other expenses	(15,036)	(12,895)
Deferred revenue	9,776	2,797
Accrued warranty	1,133	(1,501)
Net cash provided by operating activities	9,979	19,842
Cash Flows from Investing Activities:		
Purchase of available-for-sale investments	(37,393)	(80,022)
Proceeds from sales of available-for-sale investments	—	2,001
Proceeds from maturities of investments	63,759	91,280
Purchase of property and equipment	(10,844)	(7,367)
Change in restricted cash	(30)	352
Net cash provided by investing activities	15,492	6,244
Cash Flows from Financing Activities:		
Proceeds from issuance of common stock	7,787	10,131
Minimum tax withholding paid on behalf of employees for net share settlement	(2,444)	(3,950)
Net cash provided by financing activities	5,343	6,181
Effect of exchange rate changes on cash	59	(139)
Net change in cash and cash equivalents	30,873	32,128
Cash and cash equivalents at beginning of period	149,101	86,495
Cash and cash equivalents at end of period	\$ 179,974	\$ 118,623
Supplemental disclosures of cash flow information:		
Cash paid for income taxes, net of refunds	\$ 1,554	\$ 897
Cash paid for interest	\$ 37	\$ —
Supplemental schedule of non-cash investing activities:		
Transfer of inventory to fixed assets	\$ 1,409	\$ 1,403

The accompanying notes are an integral part of these condensed consolidated financial statements.

INFINERA CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. Basis of Presentation and Significant Accounting Policies

Basis of Presentation

Infinera Corporation (the "Company") prepared its interim condensed consolidated financial statements that accompany these notes in conformity with U.S. generally accepted accounting principles ("U.S. GAAP") and pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (the "SEC"), consistent in all material respects with those applied in the Company's Annual Report on Form 10-K for the fiscal year ended December 26, 2015.

The Company has made certain estimates, assumptions and judgments that can affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the condensed consolidated financial statements, as well as the reported amounts of revenue and expenses during the periods presented. Significant estimates, assumptions and judgments made by management include revenue recognition, stock-based compensation, inventory valuation, accrued warranty, business combinations, fair value measurement of investments and accounting for income taxes. Other estimates, assumptions and judgments made by management include allowances for sales returns, allowances for doubtful accounts, useful life of intangible assets, property, plant and equipment, and fair value measurement of the liability component of the Company's \$150.0 million of 1.75% convertible senior notes due June 1, 2018 (the "Notes"). Management believes that the estimates and judgments upon which they rely are reasonable based upon information available to them at the time that these estimates and judgments are made. To the extent there are material differences between these estimates and actual results, the Company's condensed consolidated financial statements will be affected.

The interim financial information is unaudited, but reflects all adjustments that are, in management's opinion, necessary to provide a fair presentation of results for the interim periods presented. All adjustments are of a normal recurring nature. The condensed consolidated financial statements include the accounts of the Company and its wholly-owned and majority-owned subsidiaries. All intercompany balances and transactions have been eliminated.

The Company reclassified certain amounts reported in previous periods to conform to the current presentation. This interim information should be read in conjunction with the consolidated financial statements in the Company's Annual Report on Form 10-K for the fiscal year ended December 26, 2015.

To date, a few of the Company's customers have accounted for a significant portion of its revenue. For the three months ended March 26, 2016, three customers individually accounted for 17%, 16% and 14% of the Company's total revenue, respectively, and for the corresponding period in 2015, two customers individually accounted for 18% and 16% of the Company's total revenue.

There have been no material changes in the Company's significant accounting policies for the three months ended March 26, 2016 as compared to those disclosed in the Company's Annual Report on Form 10-K for the fiscal year ended December 26, 2015.

2. Recent Accounting Pronouncements

In May 2016, the Financial Accounting Standards Board (the "FASB") issued Accounting Standards Update 2016-11, "Revenue Recognition (Topic 605) and Derivatives and Hedging (Topic 815): Rescission of SEC Guidance Because of Accounting Standards Updates 2014-09 and 2014-16 Pursuant to Staff Announcements at the March 3, 2016 EITF Meeting (SEC Update)" ("ASU 2016-11"), which rescinds various standards codified as part of Topic 605, Revenue Recognition in relation to the future adoption of Topic 606. These rescissions include changes to topics pertaining to revenue and expense recognition for freight Services in process, accounting for shipping and handling fees and costs and accounting for consideration given by a vendor to a customer. This guidance is effective for the Company in its first quarter of fiscal 2018 and early adoption is permitted. The Company is currently evaluating the method and impact the adoption of ASU 2016-11 will have on its consolidated financial statements.

In April 2016, the FASB issued Accounting Standards Update 2016-10, "Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing" ("ASU 2016-10"), to address the potential diversity in practice at initial application and cost; and the complexity of applying Topic 606, both at transition and on an ongoing basis related to identification of performance obligations and licensing arrangements.

The new accounting guidance is effective for the Company in its first quarter of fiscal 2018 and early adoption permitted. The Company is currently evaluating the impact of adoption of this update on its consolidated financial statements.

In March 2016, the FASB issued Accounting Standards Update 2016-09, "Improvements to Employee Share-Based Payment Accounting" ("ASU 2016-09"), which includes provisions intended to simplify various aspects related to how share-based payments are accounted for and presented in the financial statements, including the income tax effects of share-based payments and accounting for forfeitures. This guidance is effective for the Company in its first quarter of fiscal 2017 and early adoption is permitted. The Company is currently evaluating the method and impact the adoption of ASU 2016-09 will have on its consolidated financial statements.

In March 2016, the FASB issued Accounting Standards Update 2016-06, "Derivatives and Hedging (Topic 815): Contingent Put and Call Options in Debt Instruments (a consensus of the Emerging Issues Task Force)" ("ASU 2016-06"), which applies to all entities that are issuers of or investors in debt instruments (or hybrid financial instruments that are determined to have a debt host) with embedded call (put) options, and requires that embedded derivatives be separated from the host contract and accounted for separately as derivatives if certain criteria are met. One criterion is that the economic characteristics and risks of the embedded derivatives are not clearly and closely related to the economic characteristics and risks of the host contract. This guidance is effective for the Company in its first quarter of fiscal 2017 and early adoption is permitted. The Company is currently evaluating the method and impact the adoption of ASU 2016-06 will have on its consolidated financial statements.

In February 2016, the FASB issued Accounting Standards Update 2016-02, "Leases (Topic 842)" ("ASU 2016-02"), which amends the existing accounting standards for leases. The new standard requires lessees to record a right-of-use asset and a corresponding lease liability on the balance sheet (with the exception of short-term leases). For lessees, leases will continue to be classified as either operating or financing in the income statement. This guidance is effective for the Company in its first quarter of fiscal 2019 and early adoption is permitted. ASU 2016-02 is required to be applied with a modified retrospective approach and requires application of the new standard at the beginning of the earliest comparative period presented. The Company is currently evaluating the method and impact the adoption of ASU 2016-02 will have on its consolidated financial statements.

In September 2015, the FASB issued Accounting Standards Update 2015-16, "Business Combinations and Simplifying the Accounting for Measurement-Period Adjustments" ("ASU 2015-16"), which eliminates the requirement for an acquirer in a business combination to account for measurement-period adjustments retrospectively. Instead, an acquirer will recognize a measurement-period adjustment during the period in which it determines the amount of the adjustment. The guidance is effective for the Company in its first quarter of fiscal 2016. The Company's adoption of ASU 2015-16 had no impact on the Company's financial position, results of operations or cash flow.

In July 2015, the FASB issued Accounting Standards Update 2015-11, "Simplifying the Measurement of Inventory" ("ASU 2015-11"), to simplify the guidance on the subsequent measurement of inventory, excluding inventory measured using last-in, first-out or the retail inventory method. Under ASU 2015-11, inventory should be at the lower of cost and net realizable value. The new accounting guidance is effective for the Company in its first quarter of fiscal 2017 with early adoption permitted. The Company is currently evaluating the impact of the pending adoption of ASU 2015-11 on its consolidated financial statements.

In April 2015, the FASB issued Accounting Standards Update 2015-03, "Simplifying the Presentation of Debt Issuance Costs" ("ASU 2015-03"), which changes the presentation of debt issuance costs in financial statements. ASU 2015-03 requires an entity to present such costs in the balance sheet as a direct deduction from the related debt liability rather than as an asset. Amortization of the costs will continue to be reported as interest expense. The Company has adopted ASU 2015-03 during the first quarter of 2016. The December 26, 2015 balance sheet was retrospectively adjusted to reclassify \$2.1 million from other non-current assets to a reduction of the Notes payable liability.

In May 2014, the FASB issued Accounting Standards Update 2014-09, "Revenue from Contracts from Customers" ("ASU 2014-09"). ASU 2014-09 provides a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. ASU 2014-09 will require 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. This update creates a five-step model that requires entities to exercise judgment when considering the terms of the contract(s), which include (i) identifying the contract(s) with the customer; (ii) identifying the separate performance obligations in the contract; (iii) determining the

transaction price; (iv) allocating the transaction price to the separate performance obligations; and (v) recognizing revenue when each performance obligation is satisfied. In July 2015, the FASB deferred the effective date for annual reporting periods beginning after December 15, 2017 (including interim reporting periods within those periods). Early adoption is permitted to the original effective date of December 15, 2016 (including interim reporting periods within those periods). ASU 2014-09 will be effective for the Company's first quarter of 2018. The Company has the option to apply the provisions of ASU 2014-09 either retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of applying this standard recognized at the date of initial application. The Company is currently evaluating the method and impact the adoption of ASU 2014-09 will have on its consolidated financial statements.

3. Fair Value Measurements

Pursuant to the accounting guidance for fair value measurements and its subsequent updates, fair value is defined as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities required or permitted to be recorded at fair value, the Company considers the principal or most advantageous market in which it would transact and it considers assumptions that market participants would use when pricing the asset or liability.

Valuation techniques used by the Company are based upon observable and unobservable inputs. Observable or market inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's assumptions about market participant assumptions based on the best information available. Observable inputs are the preferred source of values. These two types of inputs create the following fair value hierarchy:

- Level 1 – Quoted prices in active markets for identical assets or liabilities.
- Level 2 – Quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 – Prices or valuations that require management inputs that are both significant to the fair value measurement and unobservable.

The Company measures its cash equivalents, foreign currency exchange forward contracts and marketable debt securities at fair value and classifies its investments in accordance with the fair value hierarchy. The Company's money market funds and U.S. treasuries are classified within Level 1 of the fair value hierarchy and are valued based on quoted prices in active markets for identical securities.

The Company classifies its certificates of deposit, commercial paper, U.S. agency notes, corporate bonds and foreign currency exchange forward contracts within Level 2 of the fair value hierarchy as follows:

Certificates of Deposit

The Company reviews market pricing and other observable market inputs for the same or similar securities obtained from a number of industry standard data providers. In the event that a transaction is observed for the same or similar security in the marketplace, the price on that transaction reflects the market price and fair value on that day. In the absence of any observable market transactions for a particular security, the fair market value at period end would be equal to the par value. These inputs represent quoted prices for similar assets or these inputs have been derived from observable market data.

Commercial Paper

The Company reviews market pricing and other observable market inputs for the same or similar securities obtained from a number of industry standard data providers. In the event that a transaction is observed for the same or similar security in the marketplace, the price on that transaction reflects the market price and fair value on that day and then follows a revised accretion schedule to determine the fair market value at period end. In the absence of any observable market transactions for a particular security, the fair market value at period end is derived by accreting from the last observable market price. These inputs represent quoted prices for similar assets or these inputs have been derived from observable market data accreted mathematically to par.

U.S. Agency Notes

The Company reviews trading activity and pricing for its U.S. agency notes as of the measurement date. When sufficient quoted pricing for identical securities is not available, the Company uses market pricing and other observable market inputs for similar securities obtained from a number of industry standard data providers. These inputs represent quoted prices for similar assets in active markets or these inputs have been derived from observable market data.

Corporate Bonds

The Company reviews trading activity and pricing for each of the corporate bond securities in its portfolio as of the measurement date and determines if pricing data of sufficient frequency and volume in an active market exists in order to support Level 1 classification of these securities. If sufficient quoted pricing for identical securities is not available, the Company obtains market pricing and other observable market inputs for similar securities from a number of industry standard data providers. In instances where multiple prices exist for similar securities, these prices are used as inputs into a distribution-curve to determine the fair market value at period end.

Foreign Currency Exchange Forward Contracts

As discussed in Note 5, "Derivative Instruments" to the Notes to Condensed Consolidated Financial Statements, the Company mainly holds non-speculative foreign exchange forward contracts to hedge certain foreign currency exchange exposures. The Company estimates the fair values of derivatives based on quoted market prices or pricing models using current market rates. Where applicable, these models project future cash flows and discount the future amounts to a present value using market-based observable inputs including interest rate curves, credit risk, foreign

exchange rates, and forward and spot prices for currencies.

Table of Contents

The following tables represent the Company's fair value hierarchy for its assets and liabilities measured at fair value on a recurring basis (in thousands):

	As of March 26, 2016				As of December 26, 2015			
	Fair Value Measured Using				Fair Value Measured Using			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Assets								
Money market funds	\$ 61,077	\$ —	\$ —	\$ 61,077	\$ 37,829	\$ —	\$ —	\$ 37,829
Certificates of deposit	—	3,565	—	3,565	—	5,001	—	5,001
Commercial paper	—	8,980	—	8,980	—	10,997	—	10,997
Corporate bonds	—	120,002	—	120,002	—	163,400	—	163,400
U.S. agency notes	—	10,761	—	10,761	—	10,717	—	10,717
U.S. treasuries	39,289	—	—	39,289	24,851	—	—	24,851
Foreign currency exchange forward contracts	—	325	—	325	—	490	—	490
Total assets	\$ 100,366	\$ 143,633	\$ —	\$ 243,999	\$ 62,680	\$ 190,605	\$ —	\$ 253,285
Liabilities								
Foreign currency exchange forward contracts	\$ —	\$ (16)	\$ —	\$ (16)	\$ —	\$ (44)	\$ —	\$ (44)

During the three months ended March 26, 2016, there were no transfers of assets or liabilities between Level 1 and Level 2 of the fair value hierarchy.

Investments at fair value were as follows (in thousands):

	March 26, 2016			
	Adjusted Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Money market funds	\$ 61,077	\$ —	\$ —	\$ 61,077
Certificates of deposit	3,560	5	—	3,565
Commercial paper	8,985	—	(5)	8,980
Corporate bonds	120,097	23	(118)	120,002
U.S. agency notes	10,786	—	(25)	10,761
U.S. treasuries	39,293	12	(16)	39,289
Total available-for-sale investments	\$ 243,798	\$ 40	\$ (164)	\$ 243,674

	December 26, 2015			
	Adjusted Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Money market funds	\$ 37,829	\$ —	\$ —	\$ 37,829
Certificates of deposit	5,000	1	—	5,001
Commercial paper	10,997	—	—	10,997
Corporate bonds	163,797	—	(397)	163,400
U.S. agency notes	10,786	—	(69)	10,717
U.S. treasuries	24,894	—	(43)	24,851
Total available-for-sale investments	\$ 253,303	\$ 1	\$ (509)	\$ 252,795

As of March 26, 2016, the Company's available-for-sale investments in certificates of deposit, commercial paper, U.S. agency notes and corporate bonds have a contractual maturity term of up to 22 months. Gross realized gains and losses on short-term and long-term investments for the three months ended March 26, 2016 and March 28, 2015 were insignificant in both periods. The specific identification method is used to account for gains and losses on available-for-sale investments.

[Table of Contents](#)

As of March 26, 2016 and December 26, 2015, the Company held \$111.9 million and \$98.4 million of cash in banks, respectively, excluding restricted cash.

4. Cost-method Investment

As of March 26, 2016, the Company had an investment of \$14.5 million in a privately-held company. This investment is accounted for as a cost-method investment as the Company owns less than 20% of the voting securities and does not have the ability to exercise significant influence over operating and financial policies of the entity. This investment is carried at historical cost in the Company's condensed consolidated financial statements. The Company regularly evaluates the carrying value of this cost-method investment for impairment. If the Company believes that the carrying value of the cost basis investment is in excess of estimated fair value, the Company's policy is to record an impairment charge in other income (expense), net, in the accompanying condensed consolidated statements of operations to adjust the carrying value to estimated fair value, when the impairment is deemed other-than-temporary. As of March 26, 2016, no event had occurred that would adversely affect the carrying value of this investment and thus no impairment charges have been recorded for this cost-method investment.

5. Derivative Instruments

Foreign Currency Exchange Forward Contracts

The Company enters into foreign currency exchange forward contracts to manage its exposure to fluctuations in foreign exchange rates that arise primarily from its euro and British pound denominated receivables and euro denominated restricted cash balance amounts that are pledged as collateral for certain stand-by and commercial letters of credit. Gains and losses on these contracts are intended to offset the impact of foreign exchange rate fluctuations on the underlying foreign currency denominated accounts receivables and restricted cash, and therefore, do not subject the Company to material balance sheet risk. These forward contracts entered into during the three months ended March 26, 2016 were denominated in euros and British pounds, and had maturities of no more than 1 year. The contracts are settled for U.S. dollars and Swedish kronor at maturity and at rates agreed to at inception of the contracts.

For the three months ended March 26, 2016 and March 28, 2015, the before-tax effect of the foreign currency exchange forward contracts related to the euro and British pound denominated receivables were a loss of \$0.9 million and a gain of \$3.3 million, respectively. In each of these periods, the impact of the gross gains and losses were offset by foreign exchange rate fluctuations on the underlying foreign currency denominated amounts. As of March 26, 2016, the Company did not designate foreign currency exchange forward contracts as hedges for accounting purposes and accordingly, changes in the fair value are recorded in other gain (loss), net, in the accompanying condensed consolidated statements of operations. These contracts were with two high-quality institutions and the Company consistently monitors the creditworthiness of the counterparties.

The fair value of derivative instruments in the Company's condensed consolidated balance sheets was as follows (in thousands):

	As of March 26, 2016			As of December 26, 2015		
	Gross Notional ⁽¹⁾	Prepaid Expense and Other Assets	Other Accrued Liabilities	Gross Notional ⁽¹⁾	Prepaid Expense and Other Assets	Other Accrued Liabilities
Foreign currency exchange forward contracts						
Related to euro denominated receivables	\$ 26,277	\$ 34	\$ (16)	\$ 46,753	\$ 319	\$ (44)
Related to British pound denominated receivables	\$ 6,818	291	—	\$ 6,686	171	—
Related to restricted cash	\$ 256	—	—	\$ 252	—	—
		<u>\$ 325</u>	<u>\$ (16)</u>		<u>\$ 490</u>	<u>\$ (44)</u>

⁽¹⁾ Represents the face amounts of forward contracts that were outstanding as of the period noted.

6. Business Combination

On August 20, 2015 (the "Acquisition Date"), the Company completed its public offer to the shareholders of Transmode, acquiring 95.8% of the outstanding common shares and voting interest in Transmode. Transmode is a metro packet-optical networking company based in Stockholm, Sweden. The combination of the two companies brings together a complementary set of customers, products, and technologies into one company. With the acquisition of Transmode, Infinera now offers an end-to-end product portfolio of packet-optical solutions for metro, data center interconnect, long-haul and subsea networks.

Shortly after the Acquisition Date, the Company initiated compulsory acquisition proceedings in accordance with Swedish law (the "Squeeze-out Proceedings") in order to acquire the remaining 4.2% or 1.2 million Transmode shares not tendered through the end of the offer period. As of the Acquisition Date, the fair value of the noncontrolling interest was approximately \$15.4 million, which was based on the implied enterprise value of Transmode at the Acquisition Date. The Squeeze-out Proceedings are expected to be completed during 2016.

The Company has accounted for this transaction as a business combination in exchange for total consideration of approximately \$350.6 million, which consisted of the following (in thousands, except shares):

Cash	\$	181,133
Common stock (7,873,055 shares)		169,507
Total	\$	350,640

The fair value of the 7.9 million shares of common stock issued was determined based on the closing market price of the Company's common stock on the Acquisition Date.

The Company allocated the fair value of the purchase price of the acquisition to the tangible and intangible assets acquired as well as liabilities assumed, based on their estimated fair values. The excess of the purchase price over the fair values of these identifiable assets and liabilities was recorded as goodwill.

The Company prepared an initial determination of the fair value of assets acquired and liabilities assumed as of the acquisition date using preliminary information. In accordance with Accounting Standard Codification 805, "Business Combinations," during the measurement period an acquirer shall retrospectively adjust the provisional amounts recognized at the acquisition date to reflect information obtained about facts and circumstances that existed as of the Acquisition Date that, if known, would have affected the measurement of the amounts recognized as of the Acquisition Date. Accordingly, the Company has recognized measurement period adjustments made during the first quarter of 2016 to the fair value of certain assets acquired and liabilities assumed as a result of additional information obtained. These adjustments were retrospectively applied to the Acquisition Date balance sheet. None of the adjustments had an impact on the Company's previously reported results of operations.

The following table summarizes the Company's preliminary allocation of the purchase consideration based on the fair value of assets acquired and liabilities assumed as of the Acquisition Date (in thousands):

	Amounts Recognized as of Acquisition Date	Measurement Period Adjustments	Total
Cash	\$ 36,688	\$ —	\$ 36,688
Accounts receivable	16,183	—	16,183
Inventory	19,886	—	19,886
Other assets	8,320	—	8,320
Intangible assets, net	161,845	—	161,845
Goodwill	187,220	669	187,889
Current liabilities	(24,320)	(800)	(25,120)
Deferred tax liabilities	(39,221)	131	(39,090)
Long-term liabilities	(589)	—	(589)
Noncontrolling interest	(15,372)	—	(15,372)
Total net assets	\$ 350,640	\$ —	\$ 350,640

The Company expects to finalize the allocation of the purchase consideration as soon as practicable, pending finalization of income taxes and any other adjustments related to acquired assets or liabilities, but no later than 12 months from the Acquisition Date.

The following table presents details of the identified intangible assets acquired at the Acquisition Date (in thousands):

	Fair Value	Estimated Useful Life (Years)
Trade name	\$ 234	0.5
Customer relationships	49,033	8
Developed technology	92,450	5
In-process technology	20,128	N/A
Total	\$ 161,845	

Goodwill generated from this business combination is primarily attributable to the synergies from combining the operations of Transmode with that of the Company, which resulted in expanded selling opportunities of both metro and long-haul solutions. The goodwill recognized is not tax deductible for Swedish income tax purposes.

Noncontrolling interest were as follows (in thousands):

	Three Months Ended	
	March 26, 2016	December 26, 2015
Beginning noncontrolling interest	\$ 14,910	\$ —
Noncontrolling interest investment	—	15,373
Loss attributable to noncontrolling interest	(207)	(463)
Ending noncontrolling interest	\$ 14,703	\$ 14,910

7. Goodwill and Intangible Assets

Goodwill

Goodwill is recorded when the purchase price of an acquisition exceeds the fair value of the net tangible and identified intangible assets acquired.

The following table presents details of the Company's goodwill during the three months ended March 26, 2016 (in thousands):

Balance as of December 26, 2015	\$ 191,560
Foreign currency translation adjustments	1,938
Accumulated impairment loss	—
Balance as of March 26, 2016	\$ 193,498

The gross carrying amount of goodwill may change due to the effects of foreign currency fluctuations as a result of acquiring an international business. Additional information existing as of the Acquisition Date but unknown to the Company may become known during the remainder of the measurement period, not to exceed 12 months from the Acquisition Date, which may result in changes to the amounts and allocations recorded.

Intangible Assets

The following tables present details of the Company's intangible assets as of March 26, 2016 and December 26, 2015 (in thousands):

	March 26, 2016			
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Weighted Average Remaining Useful Life (In Years)
Intangible assets with finite lives:				
Trade names	\$ 241	\$ (241)	\$ —	—
Customer relationships	50,497	(3,798)	46,699	7.4
Developed technology	99,066	(11,620)	87,446	4.5
Other intangible assets	819	(526)	293	5.4
Total intangible assets with finite lives	\$ 150,623	\$ (16,185)	\$ 134,438	5.5
In-process technology	16,873	—	16,873	
Total intangible assets	\$ 167,496	\$ (16,185)	\$ 151,311	

	December 26, 2015			
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Weighted Average Remaining Useful Life (In Years)
Intangible assets with finite lives:				
Trade names	\$ 239	\$ (168)	\$ 71	0.2
Customer relationships	49,991	(2,197)	47,794	7.7
Developed technology	94,256	(6,629)	87,627	4.6
Other intangible assets	819	(513)	306	5.6
Total intangible assets with finite lives	\$ 145,305	\$ (9,507)	\$ 135,798	5.7
In-process technology	20,521	—	20,521	
Total intangible assets	\$ 165,826	\$ (9,507)	\$ 156,319	

The gross carrying amount of intangible assets and the related amortization expense of intangible assets may change due to the effects of foreign currency fluctuations as a result of acquiring an international business. Amortization expense was \$6.5 million for the three months ended March 26, 2016 and was not significant for the three months ended March 28, 2015.

Intangible assets are carried at cost less accumulated amortization. Amortization expenses are recorded to the appropriate cost and expense categories. During the three months ended March 26, 2016, the Company transferred \$3.9 million of its in-process technology, acquired from Transmode during the third quarter of 2015, to developed technology, which is being amortized over a maximum useful life of 10 years. In-process technology of \$16.9 million has not reached technological feasibility as of March 26, 2016 and is not subject to amortization. As such, the Company excluded it in the future amortization expense table below.

The following table summarizes the Company's estimated future amortization expense of intangible assets with finite lives as of March 26, 2016 (in thousands):

	Fiscal Years						
	Total	Remainder of 2016	2017	2018	2019	2020	2021 and Thereafter
Total future amortization expense	\$ 134,438	\$ 19,547	\$ 26,064	\$ 26,064	\$ 25,999	\$ 19,303	\$ 17,461

[Table of Contents](#)

8. Balance Sheet Details

The following table provides details of selected balance sheet items (in thousands):

	March 26, 2016	December 26, 2015
Inventory:		
Raw materials	\$ 33,085	\$ 27,879
Work in process	59,394	52,599
Finished goods	97,265	94,221
Total inventory	<u>\$ 189,744</u>	<u>\$ 174,699</u>
Property, plant and equipment, net:		
Computer hardware	\$ 12,062	\$ 11,097
Computer software ⁽¹⁾	22,676	22,548
Laboratory and manufacturing equipment	197,561	189,168
Furniture and fixtures	2,018	1,897
Leasehold improvements	41,545	38,946
Construction in progress	30,426	31,060
Subtotal	<u>\$ 306,288</u>	<u>\$ 294,716</u>
Less accumulated depreciation and amortization	(190,916)	(183,855)
Total property, plant and equipment, net	<u>\$ 115,372</u>	<u>\$ 110,861</u>
Accrued expenses:		
Loss contingency related to non-cancelable purchase commitments	\$ 6,160	\$ 6,821
Professional and other consulting fees	5,168	5,363
Taxes payable	2,560	3,295
Royalties	4,449	4,290
Other accrued expenses	14,982	13,967
Total accrued expenses	<u>\$ 33,319</u>	<u>\$ 33,736</u>

⁽¹⁾ Included in computer software at March 26, 2016 and December 26, 2015 were \$7.9 million and \$7.9 million, respectively, related to an enterprise resource planning ("ERP") system that the Company implemented during 2012. The unamortized ERP costs at March 26, 2016 and December 26, 2015 were \$3.7 million and \$4.0 million, respectively.

9. Accumulated Other Comprehensive Income

Accumulated other comprehensive income includes certain changes in equity that are excluded from net income. The following table sets forth the changes in accumulated other comprehensive income by component for the three months ended March 26, 2016 (in thousands):

	Unrealized Gain (Loss) on Other Available-for-Sale Securities	Foreign Currency Translation	Accumulated Tax Effect	Total
Balance at December 26, 2015	\$ (506)	\$ 2,389	\$ (760)	\$ 1,123
Net current-period other comprehensive income	383	3,268	—	3,651
Balance at March 26, 2016	<u>\$ (123)</u>	<u>\$ 5,657</u>	<u>\$ (760)</u>	<u>\$ 4,774</u>

10. Basic and Diluted Net Income Per Common Share

Basic net income per common share is computed by dividing net income attributable to Infinera Corporation by the weighted average number of common shares outstanding during the period. Diluted net income attributable to Infinera Corporation per common share is computed using net income attributable to Infinera Corporation and the weighted average number of common shares outstanding plus potentially dilutive common shares outstanding during the period. Potentially dilutive common shares include the assumed exercise of outstanding stock options, assumed release of outstanding restricted stock units ("RSUs") and performance stock units ("PSUs"), and assumed issuance of common stock under the Company's 2007 Employee Stock Purchase Plan ("ESPP") using the treasury stock method. Potentially dilutive common shares also include the assumed conversion of convertible senior notes from the conversion spread (as discussed in Note 11, "Convertible Senior Notes"). The Company includes the common shares underlying PSUs in the calculation of diluted net income per share only when they become contingently issuable. In net loss periods, these potentially diluted common shares have been excluded from the diluted net loss calculation.

The following table sets forth the computation of net income per common share – basic and diluted (in thousands, except per share amounts):

	Three Months Ended	
	March 26, 2016	March 28, 2015
Numerator:		
Net income attributable to Infinera Corporation	\$ 12,015	\$ 12,366
Denominator:		
Basic weighted average common shares outstanding	140,805	127,840
Effect of dilutive securities:		
Employee equity plans	3,822	6,569
Assumed conversion of convertible senior notes from conversion spread	2,253	2,895
Diluted weighted average common shares outstanding	<u>146,880</u>	<u>137,304</u>
Net income per common share attributable to Infinera Corporation		
Basic	<u>\$ 0.09</u>	<u>\$ 0.10</u>
Diluted	<u>\$ 0.08</u>	<u>\$ 0.09</u>

During the three months ended March 26, 2016 and March 28, 2015, the Company included the dilutive effects of the Notes in the calculation of diluted net income per common share as the average market price was above the conversion price of the Notes. The dilutive impact of the Notes was based on the difference between the Company's average stock price during the period and the conversion price of the Notes. Upon conversion of the Notes, it is the Company's intention to pay cash equal to the lesser of the aggregate principal amount or the conversion value of the Notes being converted, therefore, only the conversion spread relating to the Notes would be included in the Company's diluted earnings per share calculation unless their effect is anti-dilutive.

The effects of certain potentially outstanding shares were not included in the calculation of diluted net income per share for the three months ended March 26, 2016 and March 28, 2015 because their effect were anti-dilutive under the treasury stock method or the performance condition of the award had not been met.

The following sets forth the potentially dilutive shares excluded from the computation of the diluted net income per share because their effect was anti-dilutive (in thousands):

	Three Months Ended	
	March 26, 2016	March 28, 2015
Stock options	9	10
RSUs	779	1,505
PSUs	302	292
ESPP shares	581	415
Total	1,671	2,222

In the three months ended March 26, 2016 and March 28, 2015, the Company included the dilutive effects of the Notes in the calculation of diluted net income per common share as the applicable average market price for certain periods were above the conversion price of the Notes.

11. Convertible Senior Notes

In May 2013, the Company issued the Notes, which will mature on June 1, 2018, unless earlier purchased by the Company or converted. Interest is payable semi-annually in arrears on June 1 and December 1 of each year, commencing December 1, 2013. The net proceeds to the Company were approximately \$144.5 million.

The Notes are governed by an indenture dated as of May 30, 2013 (the "Indenture"), between the Company, as issuer, and U.S. Bank National Association, as trustee. The Notes are unsecured and do not contain any financial covenants or any restrictions on the payment of dividends, the incurrence of senior debt or other indebtedness, or the issuance or repurchase of securities by the Company.

Upon conversion, it is the Company's intention to pay cash equal to the lesser of the aggregate principal amount or the conversion value of the Notes as cash, shares of common stock or a combination of cash and shares of common stock, at the Company's election, for any remaining conversion obligation. The initial conversion rate is 79.4834 shares of common stock per \$1,000 principal amount of Notes, subject to anti-dilution adjustments. The initial conversion price is approximately \$12.58 per share of common stock.

Throughout the term of the Notes, the conversion rate may be adjusted upon the occurrence of certain events, including for any cash dividends. Holders of the Notes will not receive any cash payment representing accrued and unpaid interest upon conversion of a Note. Accrued but unpaid interest will be deemed to be paid in full upon conversion rather than canceled, extinguished or forfeited. Holders may convert their Notes under the following circumstances:

- during any fiscal quarter commencing after the fiscal quarter ended on March 28, 2013 (and only during such fiscal quarter) if the last reported sale price of the common stock for at least 20 trading days (whether or not consecutive) during a period of 30 consecutive trading days ending on the last trading day of the immediately preceding fiscal quarter is greater than or equal to 130% of the conversion price on each applicable trading day;
- during the five business day period after any five consecutive trading day period (the "measurement period") in which the trading price per \$1,000 principal amount of Notes for each trading day of the measurement period was less than 98% of the product of the last reported sale price of the Company's common stock and the conversion rate on each such trading day;
- upon the occurrence of specified corporate events described under the Indenture, such as a consolidation, merger or binding share exchange; or
- at any time on or after December 1, 2017 until the close of business on the second scheduled trading day immediately preceding the maturity date, holders may convert their Notes at any time, regardless of the foregoing circumstances.

If the Company undergoes a fundamental change as defined in the Indenture governing the Notes, holders may require the Company to repurchase for cash all or any portion of their Notes at a repurchase price equal to 100% of the principal amount of the Notes to be repurchased, plus accrued and unpaid interest to, but excluding,

[Table of Contents](#)

the fundamental change repurchase date. In addition, upon the occurrence of a “make-whole fundamental change” (as defined in the Indenture), the Company may, in certain circumstances, increase the conversion rate by a number of additional shares for a holder that elects to convert its Notes in connection with such make-whole fundamental change.

The net carrying amounts of the debt obligation were as follows (in thousands):

	March 26, 2016	December 26, 2015
Principal	\$ 150,000	\$ 150,000
Unamortized discount ⁽¹⁾	(22,287)	(24,560)
Unamortized issuance cost ⁽¹⁾	(1,918)	(2,113)
Net carrying amount	<u>\$ 125,795</u>	<u>\$ 123,327</u>

⁽¹⁾ Unamortized debt conversion discount and issuance costs will be amortized over the remaining life of the Notes, which is approximately two years.

As of March 26, 2016 and December 26, 2015, the carrying amount of the equity components of the Notes was as follows (in thousands):

Debt discount related to value of conversion option	\$ 45,000
Debt issuance cost	(1,659)
Total	<u>\$ 43,341</u>

In accounting for the issuance of the Notes, the Company separated the Notes into liability and equity components. The carrying amount of the liability component was calculated by measuring the fair value of a similar debt instrument that does not have an associated convertible feature. The carrying amount of the equity component representing the conversion option was determined by deducting the fair value of the liability component from the par value of the Notes. The equity component is not remeasured as long as it continues to meet the conditions for equity classification. The excess of the principal amount of the liability component over its carrying amount (“debt discount”) is amortized to interest expense over the term of the Notes.

In accounting for the issuance costs of \$5.5 million related to the Notes, the Company allocated the total amount incurred to the liability and equity components of the Notes based on their relative values. Issuance costs attributable to the liability component were initially recorded as other non-current assets and will be amortized to interest expense over the term of the Notes. ASU 2015-03 requires an entity to present such costs in the balance sheet as a direct deduction from the related debt liability rather than as an asset. The Company has adopted ASU 2015-03 during the first quarter of 2016. The December 26, 2015 balance sheet was retrospectively adjusted to reclassify \$2.1 million from other non-current assets to a reduction of the Notes payable liability.

The issuance costs attributable to the equity component were netted with the equity component in stockholders’ equity. Additionally, the Company initially recorded a deferred tax liability of \$17.0 million in connection with the issuance of the Notes, and a corresponding reduction in valuation allowance. The impact of both was recorded to stockholders’ equity.

The Company determined that the embedded conversion option in the Notes does not require separate accounting treatment as a derivative instrument because it is both indexed to the Company’s own stock and would be classified in stockholder’s equity if freestanding.

The following table sets forth total interest expense recognized related to the Notes (in thousands):

	Three Months Ended	
	March 26, 2016	March 28, 2015
Contractual interest expense	\$ 656	\$ 656
Amortization of debt issuance costs	196	177
Amortization of debt discount	2,274	2,057
Total interest expense	<u>\$ 3,126</u>	<u>\$ 2,890</u>

[Table of Contents](#)

The coupon rate is 1.75% . For the three months ended March 26, 2016 and March 28, 2015 , the debt discount and debt issuance costs are amortized, using an annual effective interest rate of 10.23% , to interest expense over the term of the Notes.

As of March 26, 2016 , the fair value of the Notes was \$204.9 million . The fair value was determined based on the quoted bid price of the Notes in an over-the-counter market on March 25, 2016. The Notes are classified as Level 2 of the fair value hierarchy.

During the three months ended March 26, 2016 , the closing price of the Company's common stock did not meet the conversion criteria; therefore, holders of the Notes may not convert their notes during the second quarter of 2016. Should the closing price conditions be met during the 30 consecutive trading days prior to the end of the second quarter of 2016 or a future quarter, the Notes will be convertible at their holders' option during the immediately following quarter. Based on the closing price of the Company's common stock of \$15.30 on March 25, 2016, the if-converted value of the Notes exceeded their principal amount by approximately \$32.4 million .

12. Stockholders' Equity

Stock-based Compensation Plans

The Company has stock-based compensation plans pursuant to which the Company has granted stock options, RSUs and PSUs. The Company also has an ESPP for all eligible employees. As of March 26, 2016 , there were a total of 14.6 million shares of common stock available for grant under the Company's 2007 Equity Incentive Plan ("2007 Plan"). The following tables summarize the Company's equity award activity and related information (in thousands, except per share data):

	Number of Stock Options	Weighted-Average Exercise Price Per Share	Aggregate Intrinsic Value
Outstanding at December 26, 2015	2,511	\$ 7.26	\$ 28,288
Stock options granted	—	\$ —	
Stock options exercised	(57)	\$ 5.14	\$ 600
Stock options canceled	—	\$ —	
Outstanding at March 26, 2016	2,454	\$ 7.31	\$ 19,672
Vested and expected to vest as of March 26, 2016	2,454		\$ 19,670
Exercisable at March 26, 2016	2,443	\$ 7.30	\$ 19,600

	Number of Restricted Stock Units	Weighted- Average Grant Date Fair Value Per Share	Aggregate Intrinsic Value
Outstanding at December 26, 2015	4,932	\$ 12.76	\$ 91,285
RSUs granted	604	\$ 15.43	
RSUs released	(279)	\$ 9.75	\$ 4,022
RSUs canceled	(142)	\$ 12.98	
Outstanding at March 26, 2016	5,115	\$ 13.23	\$ 78,263
Expected to vest at March 26, 2016	4,855		\$ 74,278

[Table of Contents](#)

	Number of Performance Stock Units	Weighted-Average Grant Date Fair Value Per Share	Aggregate Intrinsic Value
Outstanding at December 26, 2015	731	\$ 12.35	\$ 13,540
PSUs granted	424	\$ 15.29	
PSUs performance earned ⁽¹⁾	154	\$ 9.43	
PSUs released	(462)	\$ 9.43	\$ 6,650
PSUs canceled	(71)	\$ 15.65	
Outstanding at March 26, 2016	776	\$ 14.51	\$ 11,865
Expected to vest at March 26, 2016	744		\$ 11,384

⁽¹⁾ Represents the additional PSUs awarded resulting from the achievement of performance goals above the performance targets established at grant since the original grants were at 100% of target amounts.

The aggregate intrinsic value of unexercised stock options is calculated as the difference between the closing price of the Company's common stock of \$15.30 at March 24, 2016 (the last trading day of the fiscal quarter) and the exercise prices of the underlying stock options. The aggregate intrinsic value of the stock options that have been exercised is calculated as the difference between the fair market value of the common stock at the date of exercise and the exercise price of the underlying stock options.

The aggregate intrinsic value of unreleased RSUs and unreleased PSUs is calculated using the closing price of the Company's common stock of \$15.30 at March 24, 2016 (the last trading day of the fiscal quarter). The aggregate intrinsic value of RSUs and PSUs released is calculated using the fair market value of the common stock at the date of release.

The following table presents total stock-based compensation cost for instruments granted but not yet amortized, net of estimated forfeitures, of the Company's equity compensation plans as of March 26, 2016. These costs are expected to be amortized on a straight-line basis over the following weighted-average periods (in thousands, except for weighted-average period):

	Unrecognized Compensation Expense, Net	Weighted-Average Period (in years)
Stock options	\$ 40	1.8
RSUs	\$ 42,653	2.4
PSUs	\$ 7,962	1.8

Employee Stock Options

The Company did not grant any stock options during the three months ended March 26, 2016. Amortization of stock-based compensation related to stock options in the three months ended March 26, 2016 and March 28, 2015 was insignificant in both periods.

Employee Stock Purchase Plan

The fair value of the ESPP shares was estimated at the date of grant using the following assumptions (expense amounts in thousands):

Employee Stock Purchase Plan	Three Months Ended	
	March 26, 2016	March 28, 2015
Volatility	56%	53%
Risk-free interest rate	0.52%	0.13%
Expected life	0.5 years	0.5 years
Estimated fair value	\$4.53	\$5.15
Total stock-based compensation expense	\$1,242	\$1,051

Restricted Stock Units

During the three months ended March 26, 2016, the Company granted RSUs to employees and members of the Company's board of directors to receive an aggregate of 0.6 million shares of the Company's common stock, respectively. All RSUs awarded are subject to each individual's continued service to the Company through each applicable vesting date. The Company accounted for the fair value of the RSUs using the closing market price of the Company's common stock on the date of grant. Amortization of stock-based compensation related to RSUs in the three months ended March 26, 2016 and March 28, 2015 was approximately \$6.1 million and \$5.2 million, respectively.

Performance Stock Units

Pursuant to the 2007 Plan, the Company has granted PSUs to certain of the Company's executive officers, senior management and employees. All PSUs awarded are subject to each individual's continued service to the Company through each applicable vesting date and if the performance metrics are not met within the time limits specified in the award agreements, the PSUs will be canceled.

A number of PSUs granted to the Company's executive officers and senior management are based on the total shareholder return of the Company's common stock price as compared to the total shareholder return of a designated index over the span of one year, two years and three years. The number of shares to be issued upon vesting of these PSUs range from 0 to 2.0 times the target number of PSUs granted depending on the Company's performance against the index.

The ranges of estimated values of the PSUs granted that are compared to an index, as well as the assumptions used in calculating these values were based on estimates as follows:

	2016	2015	2014	2013
Index	SPGIIPTR	SPGIIPTR	SPGIIPTR	NASDAQ Telecom Composite
Index volatility	18%	18% - 19%	25%	23%
Infinera volatility	55%	48%	49% - 50%	55%
Risk-free interest rate	0.95%	0.97% - 1.10%	0.66% - 0.71%	0.42%
Correlation with index	0.58	0.52	0.60	0.56
Estimated fair value	\$12.10 - \$16.62	\$18.08 - \$19.29	\$6.59 - \$7.60	\$6.27 - \$7.06

In addition, certain other PSUs granted to the Company's executive officers, senior management and certain employees will only vest upon the achievement of specific financial or operational performance criteria.

The following table summarizes by grant year, the Company's PSU activity for the three months ended March 26, 2016 (in thousands):

	Total Number of Performance Stock Units	2013	2014	2015	2016
Outstanding at December 26, 2015	731	147	260	324	—
PSUs granted	424	—	—	—	424
PSUs performance earned ⁽¹⁾	154	70	53	31	—
PSUs released	(462)	(211)	(158)	(93)	—
PSUs canceled	(71)	(6)	(8)	(57)	—
Outstanding at March 26, 2016	776	—	147	205	424

⁽¹⁾ Represents the additional PSUs awarded resulting from the achievement of performance goals above the performance targets established at grant since the original grants were at 100% of target amounts.

Amortization of stock-based compensation related to PSUs in the three months ended March 26, 2016 and March 28, 2015 was approximately \$0.8 million and \$0.9 million, respectively.

[Table of Contents](#)

Stock-Based Compensation

The following tables summarize the effects of stock-based compensation on the Company's condensed consolidated balance sheets and statements of operations for the periods presented (in thousands):

	March 26, 2016	December 26, 2015
Stock-based compensation effects in inventory	\$ 3,282	\$ 3,129
Stock-based compensation effects in deferred inventory cost	\$ 13	\$ 13
Stock-based compensation effects in fixed assets	\$ 87	\$ 93

	Three Months Ended	
	March 26, 2016	March 28, 2015
Stock-based compensation effects included in net income before income taxes		
Cost of revenue	\$ 673	\$ 482
Research and development	2,321	2,578
Sales and marketing	2,235	1,721
General and administration	1,899	1,666
	\$ 7,128	\$ 6,447
Cost of revenue – amortization from balance sheet ⁽¹⁾	859	761
Total stock-based compensation expense	\$ 7,987	\$ 7,208

(1) Stock-based compensation expense deferred to inventory and deferred inventory costs in prior periods and recognized in the current period.

13. Income Taxes

Provision for income taxes during the three months ended March 26, 2016 was \$0.2 million on pre-tax income of \$12.0 million. This compares to a tax provision of \$0.6 million on a pre-tax income of \$13.0 million during the three months ended March 28, 2015. The results for the three months ended March 26, 2016 reflect approximately \$7.0 million of purchase accounting amortization and other charges related to the acquisition of Transmode, with a corresponding tax benefit of approximately \$1.5 million. Exclusive of this tax benefit, provision for income taxes otherwise increased by approximately \$1.1 million in the three months ended March 26, 2016 compared to March 28, 2015, which relates to a higher effective tax rate applied to a higher pre-tax income. The increase in effective tax rate is attributed to higher state income taxes provided in those states where loss carryforwards are now exhausted as well as higher foreign income taxes related to the Transmode operations and increased spending in certain of the Company's cost-plus foreign subsidiaries.

In all periods, the tax expense projected in the Company's effective tax rate assumptions primarily represents foreign taxes of the Company's overseas subsidiaries compensated on a cost-plus basis, as well as the operating results of Transmode, inclusive of purchase accounting charges and amortization for the three months ended March 26, 2016. Due to the Company's significant U.S. loss carryforward position and corresponding full valuation allowance, the Company has not been subject to federal or state tax on its U.S. income because of the availability of loss carryforwards, with the exception of some state taxes for which the losses are limited. The release of transfer pricing reserves in the future will have a beneficial impact to tax expense, but the timing of the impact depends on factors such as expiration of the statute of limitations or settlements with tax authorities. No significant releases are expected in the near future based on information available at this time.

The Company must assess the likelihood that some portion or all of its deferred tax assets will be recovered from future taxable income within the respective jurisdictions. In the past, the Company established a valuation allowance against its deferred tax assets as it determined that its ability to recover the value of these assets did not meet the "more-likely-than-not" standard. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management judgment is required on an on-going basis to determine whether it needs to maintain the valuation allowance recorded against its net deferred tax assets. At March 26, 2016, the Company has been profitable for eight consecutive quarters beginning with the second quarter of 2014. Despite this trend, the

Company must consider other positive and negative evidence, including its forecasts of taxable income over the applicable carryforward periods, its current financial performance, its market environment, and other factors in evaluating the need for a valuation allowance against its net U.S. deferred tax assets. At March 26, 2016, the Company believes that it is more likely than not, that it would not be able to utilize its deferred tax assets in the foreseeable future. Accordingly, the domestic net deferred tax assets continued to be fully reserved with a valuation allowance. To the extent that the Company determines that deferred tax assets are realizable on a more-likely-than-not basis, and adjustment is needed, that adjustment will be recorded in the period that the determination is made and would generally decrease the valuation allowance and record a corresponding benefit to earnings.

14. Segment Information

Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker, or decision making group, in deciding how to allocate resources and in assessing performance. The Company's chief operating decision maker is the Company's Chief Executive Officer ("CEO"). The Company's CEO reviews financial information presented on a consolidated basis, accompanied by information about revenue by geographic region for purposes of allocating resources and evaluating financial performance. The Company has one business activity. Accordingly, the Company is considered to be in a single reporting segment and operating unit structure.

Revenue by geographic region is based on the shipping address of the customer. The following tables set forth revenue and long-lived assets by geographic region (in thousands):

Revenue

	Three Months Ended	
	March 26, 2016	March 28, 2015
Americas:		
United States	\$ 174,515	\$ 127,003
Other Americas	3,259	7,086
	177,774	134,089
Europe, Middle East and Africa	59,876	45,879
Asia Pacific and Japan	7,168	6,894
Total revenue	\$ 244,818	\$ 186,862

Property, plant and equipment, net

	March 26, 2016	December 26, 2015
United States	\$ 106,833	\$ 102,702
Other Americas	301	173
	107,134	102,875
Europe, Middle East and Africa	5,618	5,417
Asia Pacific and Japan	2,620	2,569
Total property, plant and equipment, net	\$ 115,372	\$ 110,861

15. Guarantees

Product Warranties

The Company warrants that its products will operate substantially in conformity with product specifications. Hardware warranties provide the purchaser with protection in the event that the product does not perform to product specifications. During the warranty period, the purchaser's sole and exclusive remedy in the event of such defect or failure to perform is limited to the correction of the defect or failure by repair, refurbishment or replacement, at the Company's sole option and expense. The Company's hardware warranty periods generally range from one to five years from date of acceptance for hardware and the Company's software warranty is 90 days. Upon delivery of the Company's products, the Company provides for the estimated cost to repair or replace products that may be returned under warranty. The hardware warranty accrual is based on actual historical returns and cost of repair experience and the application of those historical rates to the Company's in-warranty installed base. The provision

for warranty claims fluctuates depending upon the installed base of products and the failure rates and costs of repair associated with these products under warranty. Furthermore, the Company's costs of repair vary based on repair volume and its ability to repair, rather than replace, defective units. In the event that actual product failure rates and costs to repair differ from the Company's estimates, revisions to the warranty provision are required. In addition, from time to time, specific hardware warranty accruals may be made if unforeseen technical problems arise with specific products. The Company regularly assesses the adequacy of its recorded warranty liabilities and adjusts the amounts as necessary.

Activity related to product warranty was as follows (in thousands):

	Three Months Ended	
	March 26, 2016	March 28, 2015
Beginning balance	\$ 38,844	\$ 27,040
Charges to operations	6,754	5,348
Utilization	(4,987)	(1,818)
Change in estimate ⁽¹⁾	(612)	(5,031)
Balance at the end of the period	<u>\$ 39,999</u>	<u>\$ 25,539</u>

⁽¹⁾ The Company records hardware warranty liabilities based on the latest quality and cost information available as of that date. The changes in estimate shown here are due to changes in overall actual failure rates, the mix of new versus used units related to replacement of failed units, and changes in the estimated cost of repair. As the Company's products mature over time, failure rates and repair costs generally decline leading to favorable changes in warranty reserves.

Letters of Credit and Bank Guarantees

The Company had \$5.2 million of standby letters of credit and bank guarantees outstanding as of March 26, 2016 and December 26, 2015. These consisted of \$3.1 million related to customer performance guarantees, \$1.2 million related to a value added tax and customs' licenses, and \$0.9 million related to property leases.

The Company had a line of credit for approximately \$1.5 million to support the issuance of letters of credit, of which \$0.3 million had been issued and outstanding as of March 26, 2016 and December 26, 2015. The Company has pledged approximately \$4.8 million of assets of a subsidiary to secure this line of credit and other obligations.

16. Litigation and Contingencies

From time to time, the Company is subject to various legal proceedings, claims and litigation arising in the ordinary course of business. While the outcome of these matters is currently not determinable, the Company does not expect that the ultimate costs to resolve these matters will have a material effect on its consolidated financial position, results of operations or cash flows.

The Company is subject to the possibility of various losses arising in the ordinary course of business. These may relate to disputes, litigation and other legal actions. In the preparation of its quarterly and annual financial statements, the Company considers the likelihood of loss or the incurrence of a liability, including whether it is probable, reasonably possible or remote that a liability has been incurred, as well as the Company's ability to reasonably estimate the amount of loss, in determining loss contingencies. In accordance with U.S. GAAP, an estimated loss contingency is accrued when it is probable that a liability has been incurred and the amount of loss can be reasonably estimated. The Company regularly evaluates current information to determine whether any accruals should be adjusted and whether new accruals are required. As of March 26, 2016, the Company has accrued the estimated liabilities associated with the Company's potential loss contingencies.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

This Quarterly Report on Form 10-Q contains "forward-looking statements" that involve risks and uncertainties, as well as assumptions that, if they never materialize or prove incorrect, could cause our results to differ materially from those expressed or implied by such forward-looking statements. Such forward-looking statements include our expectations regarding revenue, gross margin, operating expenses, cash flows and other financial items; any statements of the plans, strategies and objectives of management for future operations and personnel; factors that may affect our operating results; anticipated customer needs and activity; statements concerning new or existing products or services; statements related to our integration efforts in connection with our acquisition of Transmode and the squeeze-out proceedings; statements related to capital expenditures; statements related to future economic conditions, performance, market growth or our sales cycle; statements related to our convertible senior notes; statements related to the effects of litigation on our financial position, results of operations or cash flows; statements related to the timing and impact of transfer pricing reserves; statements related to deferred tax assets; statements as to industry trends and other matters that do not relate strictly to historical facts or statements of assumptions underlying any of the foregoing. These statements are often identified by the use of words such as "anticipate," "believe," "continue," "could," "estimate," "expect," "intend," "may," or "will," and similar expressions or variations. These statements are based on the beliefs and assumptions of our management based on information currently available to management. Such forward-looking statements are subject to risks, uncertainties and other factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified below, and those discussed in the section titled "Risk Factors" included elsewhere in this Form 10-Q and in our other SEC filings, including our Annual Report on Form 10-K for the fiscal year ended December 26, 2015 filed on February 23, 2016. Such forward-looking statements speak only as of the date of this report. We disclaim any obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements. The following discussion and analysis should be read in conjunction with our condensed consolidated financial statements and notes thereto included elsewhere in this Quarterly Report on Form 10-Q.

Overview

We provide optical transport networking equipment, software and services to telecommunications service providers, Internet content providers ("ICPs"), cable providers, wholesale and enterprise carriers, research and education institutions, and government entities (collectively, "Service Providers") across the globe. Optical transport networks are deployed by Service Providers facing significant demands for optical bandwidth prompted by increased use of high-speed Internet access, mobile broadband, high-definition video streaming services, business Ethernet services and cloud-based services.

We manufacture large-scale Indium Phosphide PICs, which are used as a key differentiating component inside most of our Intelligent Transport Network platforms. We believe that our vertical integration of PICs, DSPs and software, incorporated in the Infinera Intelligent Transport Network architecture, gives us a structural technology advantage, enabling Service Providers to scale network bandwidth, accelerate service innovation, simplify optical network operations, take advantage of power savings that reduce cost of ownership, and ultimately, create rich end-user experiences for their customers. Building on our leadership in long-haul and sub-sea networks, our Cloud Xpress platform targets the data center interconnect ("DCI") market, which we believe is a rapidly growing market as cloud infrastructures continue to evolve to address the massive ongoing demand of server-to-server traffic.

On August 20, 2015, we successfully completed our public offer to the shareholders of Transmode AB ("Transmode"), acquiring 95.8% of the outstanding common shares and voting interest in Transmode, a metro packet-optical networking company based in Stockholm, Sweden. The combination of the two companies brings together a complementary set of customers, products and technologies into one company. With the acquisition of Transmode and the introduction of the Infinera DTN-X XTC-2/2E during 2015, we now provide an end-to-end portfolio of packet-optical solutions for metro, DCI, long-haul and subsea networks. With the TM-Series products from Transmode and our product portfolio, we believe we are well positioned to address the evolving requirements of our growing customer base.

Across the broader market, we believe we have a good opportunity to increase revenue in 2016 through the inclusion of a full year of Transmode revenues, including potential cross-sell synergies gained through selling the metro portfolio into the Infinera customer base, along with capacity additions to previously deployed 100G long-haul footprint, increased market adoption of Cloud Xpress, and initial sales from the new products announced late last year. Our focus on revenue growth will be complemented with continued efforts to drive cost improvements across

[Table of Contents](#)

our product portfolio. With respect to operating expenses, we will need to increase our investment levels in the short-term to more closely align with our growing market opportunities across long-haul, metro and DCI. We have not scaled our operating expenses at the same rate as our revenue growth over the past few years as our revenue growth has exceeded our expectations. Over a longer period of time, we believe that with sustained revenue growth, we can further leverage our vertically-integrated manufacturing model, which combined with our expanding portfolio of purpose built products, continued capacity sales into deployed networks and expense management, can result in improved profitability and cash flow.

Our goal is to be the preeminent provider of optical transport networking systems to Service Providers around the world. Our revenue growth will depend on the continued acceptance of our products, growth of communications traffic and the proliferation of next-generation bandwidth-intensive services, which are expected to drive the need for increased levels of bandwidth.

Our near-term quarter-over-quarter revenue may likely be volatile and may be impacted by several factors including general economic and market conditions, time-to-market development and market acceptance of new products, acquisitions of new customers and the timing of large product deployments.

We maintain a diverse customer base across customer verticals and geographies, with several customers capable of spending significantly in a given quarter. For the three months ended March 26, 2016, three customers individually accounted for 17%, 16% and 14%, of our total revenue, respectively, and for the corresponding period in 2015, two customers individually accounted for 18% and 16% of our total revenue, respectively.

We are headquartered in Sunnyvale, California, with employees located throughout the Americas, Europe and the Asia Pacific region. We expect to continue to add personnel in the United States and internationally to develop our products and provide additional sales, marketing and technical support coverage. We primarily sell our products through our direct sales force but also sell indirectly through resellers. We derived 96% and 95% of our revenue from direct sales to customers during the three months ended March 26, 2016 and March 28, 2015, respectively. We are working to expand our indirect sales programs in the future to allow us to address a broader pool of customers with more channel friendly products such as the Cloud Xpress platform and TM-Series products. We expect to continue generating a substantial majority of our revenue from direct sales in the near future.

Critical Accounting Policies and Estimates

Management's Discussion and Analysis of Financial Condition and Results of Operations is based upon our condensed consolidated financial statements, which we have prepared in accordance with the U.S. generally accepted accounting principles ("U.S. GAAP"). The preparation of these financial statements requires management to make estimates, assumptions and judgments that can affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. Management bases its estimates on historical experience and on various other assumptions that it believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

An accounting policy is deemed to be critical if it requires a significant accounting estimate to be made based on assumptions about matters that are highly uncertain at the time the estimate is made, if different estimates reasonably could have been used, or if changes in the estimate that are reasonably likely to occur could materially impact the financial statements. Management believes that there have been no significant changes during the three months ended March 26, 2016 to the items that we disclosed as our critical accounting policies and estimates in Management's Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the fiscal year ended December 26, 2015.

Results of Operations

The results of operations for the three months ended March 26, 2016 reflects the inclusion of the Transmode business, which was acquired on August 20, 2015. The following sets forth, for the periods presented, certain unaudited condensed consolidated statements of operations information (in thousands, except percentages):

	Three Months Ended					
	March 26, 2016		March 28, 2015		Change	% Change
	Amount	% of total revenue	Amount	% of total revenue		
Revenue:						
Product	\$ 216,082	88%	\$ 160,843	86%	\$ 55,239	34%
Services	28,736	12%	26,019	14%	2,717	10%
Total revenue	\$ 244,818	100%	\$ 186,862	100%	\$ 57,956	31%
Cost of revenue:						
Product	\$ 118,062	48%	\$ 89,506	48%	\$ 28,556	32%
Services	10,418	4%	9,244	5%	1,174	13%
Total cost of revenue	\$ 128,480	52%	\$ 98,750	53%	\$ 29,730	30%
Gross profit	\$ 116,338	47.5%	\$ 88,112	47.2%	\$ 28,226	32%

Revenue

Product revenue increased by \$55.2 million , or 34% , during the three months ended March 26, 2016 compared to the corresponding period in 2015. The increase was driven by the inclusion of revenue from Transmode metro products as well as continued growth associated with the Infinera DTN-X platform largely through capacity additions to existing networks. We also experienced strong growth in revenue associated with our Cloud Xpress platform.

Services revenue increased by \$2.7 million , or 10% , during the three months ended March 26, 2016 compared to the corresponding period in 2015, primarily due to the higher on-going support services as we have significantly grown our installed base over the last year. Our services revenue also benefited from the inclusion of Transmode's services revenue since the acquisition.

We currently expect that total revenue in the second quarter of 2016 will be moderately higher as compared to the prior quarter.

The following table summarizes our revenue by geography and sales channel for the periods presented (in thousands, except percentages):

	Three Months Ended					
	March 26, 2016		March 28, 2015		Change	% Change
	Amount	% of total revenue	Amount	% of total revenue		
Total revenue by geography:						
Domestic	\$ 174,515	71%	\$ 127,003	68%	\$ 47,512	37%
International	70,303	29%	59,859	32%	10,444	17%
	\$ 244,818	100%	\$ 186,862	100%	\$ 57,956	31%
Total revenue by sales channel:						
Direct	\$ 234,951	96%	\$ 177,993	95%	\$ 56,958	32%
Indirect	9,867	4%	8,869	5%	998	11%
	\$ 244,818	100%	\$ 186,862	100%	\$ 57,956	31%

Domestic revenue increased by \$47.5 million , or 37% , during the three months ended March 26, 2016 compared to the corresponding period in 2015, primarily driven by customers in our cable and wholesale and

[Table of Contents](#)

enterprise carrier verticals, and to a lesser extent, our ICP vertical. Many of our largest customers are based in this region, including each of our greater than 10% of revenue customers for the three months ended March 26, 2016.

International revenue increased by \$10.4 million, or 17%, during the three months ended March 26, 2016 compared to the corresponding period in 2015. The increase in absolute dollars was primarily led by the Europe, Middle East and Africa ("EMEA") region due to the inclusion of revenue from Transmode, which generates most of its revenue from within the EMEA region and our success in adding capacity to certain pan-European customer long-haul networks.

Cost of Revenue and Gross Margin

Gross margin was 47.5% during the three months ended March 26, 2016, up slightly from 47.2% in the corresponding period in 2015. The increase is attributable to a variety of factors including benefits from our vertical integration and capacity additions to existing long-haul networks. Our vertically integrated operating model enables us to spread our primarily fixed manufacturing costs over a broader base of units as volumes continue to grow, leading to lower costs of each unit produced. Capacity additions to existing customer networks both in the form of line card additions and additional licenses under the Infinera Instant Bandwidth program will drive gross margin levels upward since these capacity additions carry a higher gross margin profile than the footprint builds of new networks. These benefits were partially offset by \$5.1 million of purchase accounting costs, primarily related to amortization of intangibles associated with the Transmode acquisition.

We currently expect that gross margin in the second quarter of 2016 will be relatively lower as compared to the prior quarter as we expect new deployments across our product portfolio, which we believe are important to our long-term success, to slightly offset the continued underlying strength of customers adding capacity to their long-haul networks and cost benefits from our vertically integrated model.

Operating Expenses

The following tables summarize our operating expenses for the periods presented (in thousands, except percentages):

	Three Months Ended				Change	% Change
	March 26, 2016		March 28, 2015			
	Amount	% of total revenue	Amount	% of total revenue		
Operating expenses:						
Research and development	\$ 54,145	22%	\$ 39,257	21%	\$ 14,888	38%
Sales and marketing	30,009	12%	21,042	11%	8,967	43%
General and administrative	17,313	7%	12,656	7%	4,657	37%
Total operating expenses	<u>\$ 101,467</u>	<u>41%</u>	<u>\$ 72,955</u>	<u>39%</u>	<u>\$ 28,512</u>	<u>39%</u>

Research and Development Expenses

Research and development expenses increased by \$14.9 million, or 38%, during the three months ended March 26, 2016 compared to the corresponding period in 2015. The increase was primarily due to increased personnel costs of \$9.4 million as a result of incremental headcount to support our expanding product roadmap. In addition, we increased spending on prototype and other engineering materials of \$2.4 million, outside professional services costs of \$1.7 million and discretionary spending of \$1.4 million to support our growing business.

[Table of Contents](#)

Sales and Marketing Expenses

Sales and marketing expenses increased by \$9.0 million , or 43% , during the three months ended March 26, 2016 compared to the corresponding period in 2015. The increase was primarily driven by higher personnel costs of \$5.7 million due to incremental headcount to support the continued expansion of our business into new markets and customer verticals. In addition, the increase also included amortization of intangible assets of \$1.6 million and higher discretionary spending of \$2.4 million to support our expanding business. The increases during the three month period were offset by lower prototype and lab trial spending of \$0.7 million due to timing of certain projects.

General and Administrative Expenses

General and administrative expenses increased by \$4.7 million , or 37% , during the three months ended March 26, 2016 compared to the corresponding period in 2015. The increase was primarily due to higher personnel-related costs of \$2.4 million, driven by incremental headcount to allow our infrastructure to scale to support our expanding business. We also incurred increased outside professional services costs of \$1.0 million and higher discretionary spending of \$1.3 million.

Other Income (Expense), Net

	Three Months Ended			
	March 26, 2016	March 28, 2015	Change	% Change
	(In thousands)			
Interest income	\$ 522	\$ 414	\$ 108	26 %
Interest expense	(3,155)	(2,890)	(265)	9 %
Other gain (loss), net	(214)	301	(515)	(171)%
Total other income (expense), net	<u>\$ (2,847)</u>	<u>\$ (2,175)</u>	<u>\$ (672)</u>	<u>31 %</u>

Interest income increased by \$0.1 million for the three months ended March 26, 2016 compared to the corresponding period in 2015 due to higher yield, partially offset by lower cash and investment balances. Interest expense for the three months ended March 26, 2016 increased by \$0.3 million due to an increase of amortization of discount and issuance costs related to the \$150.0 million of 1.75% convertible senior notes due June 1, 2018 (the "Notes"). The \$0.5 million increase in other gain (loss), net, during the three months ended March 26, 2016 compared to the corresponding period in 2015 was primarily due to losses from foreign exchange related transactions.

Income Tax Provision

Provision for income taxes during the three months ended March 26, 2016 was \$0.2 million on pre-tax income of \$12.0 million . This compares to a tax provision of \$0.6 million on a pre-tax income of \$13.0 million during the three months ended March 28, 2015. The results for the three months ended March 26, 2016 reflect approximately \$7.0 million of purchase accounting amortization and other charges related to the acquisition of Transmode, with a corresponding tax benefit of approximately \$1.5 million. Exclusive of this tax benefit, provision for income taxes otherwise increased by approximately \$1.1 million during the three months ended March 26, 2016 compared to March 28, 2015, which relates to a higher effective tax rate applied to a higher pre-tax income. The increase in effective tax rate is attributed to higher state income taxes provided in those states where loss carryforwards are now exhausted as well as higher foreign income taxes related to the Transmode operations and increased spending in certain of our cost-plus foreign subsidiaries.

We must assess the likelihood that some portion or all of our deferred tax assets will be recovered from future taxable income within the respective jurisdictions. In the past, we established a valuation allowance against our deferred tax assets as we determined that our ability to recover the value of these assets did not meet the "more-likely-than-not" standard. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management judgment is required on an on-going basis to determine whether we need to maintain the valuation allowance recorded against our net deferred tax assets. At March 26, 2016, we have been profitable for eight consecutive quarters beginning with the second quarter of 2014. Despite this trend, we must consider other positive and negative evidence, including our forecasts of taxable income over the applicable carryforward periods, our current financial performance, our market environment, and other factors in evaluating the need for a valuation allowance against our net U.S. deferred tax assets. At March 26, 2016, we believe that it is more-likely-than-not, that we would not be able to utilize our deferred tax assets in the foreseeable future. Accordingly, the domestic net deferred tax

[Table of Contents](#)

assets continued to be fully reserved with a valuation allowance. To the extent that we determine that deferred tax assets are realizable on a more likely than not basis, and adjustment is needed, that adjustment will be recorded in the period that the determination is made and would generally decrease the valuation allowance and record a corresponding benefit to earnings.

Liquidity and Capital Resources

	Three Months Ended	
	March 26, 2016	March 28, 2015
	(In thousands)	
Net cash flow provided by:		
Operating activities	\$ 9,979	\$ 19,842
Investing activities	\$ 15,492	\$ 6,244
Financing activities	\$ 5,343	\$ 6,181

	March 26, 2016	December 26, 2015
	(In thousands)	
Cash and cash equivalents	\$ 179,974	\$ 149,101
Short and long-term investments	175,604	202,068
Long-term restricted cash	5,331	5,310
	<u>\$ 360,909</u>	<u>\$ 356,479</u>

Cash, cash equivalents and short-term investments consist of highly-liquid investments in certificates of deposits, commercial paper, money market funds, corporate bonds and U.S. treasuries. Long-term investments primarily consist of corporate bonds. The restricted cash balance amounts are primarily pledged as collateral for certain stand-by and commercial letters of credit related to customer proposal guarantees, value added tax licenses and property leases.

Operating Activities

Net cash provided by operating activities during the three months ended March 26, 2016 was \$10.0 million as compared to net cash provided by operating activities of \$19.8 million for the corresponding period in 2015.

Net income adjusted for non-cash items was \$37.4 million during the three months ended March 26, 2016 compared to net income adjusted for non-cash items of \$29.3 million for the corresponding period in 2015. The increase in the current year was primarily attributable to purchase accounting related amortization of intangibles associated with the Transmode acquisition.

Net cash used to fund working capital was \$27.4 million during the three months ended March 26, 2016. Inventory increased by \$16.2 million as a result of stocking more components due to longer lead times with suppliers and building up PIC die bank inventory to meet future demand. Accounts payable decreased by \$9.0 million primarily reflecting timing of purchases and payments during the period. Accrued liabilities and other expenses decreased \$15.0 million primarily due to the corporate bonus payout during the quarter. Deferred revenue increased \$9.8 million due to higher on-going support services as we continue to grow our installed base.

Net cash used to fund working capital was \$9.5 million during the three months ended March 28, 2015. Accounts receivables decreased by \$23.4 million primarily reflecting linearity of invoicing and collections activities in the period. Inventory increased by \$12.1 million in order to support higher seasonal demand in the second quarter. Accounts payable decreased by \$10.3 million primarily reflecting timing of inventory purchases and payments during the period. Accrued liabilities decreased \$12.9 million primarily due to the corporate bonus payout during the quarter.

[Table of Contents](#)

Investing Activities

Net cash provided by investing activities during the three months ended March 26, 2016 was \$15.5 million compared to \$6.2 million for the corresponding period in 2015. Investing activities during the three months ended March 26, 2016 included net proceeds of \$26.4 million associated with purchases, maturities and sales of investments, offset by capital expenditures of \$10.8 million. Investing activities during the three months ended March 28, 2015 included net proceeds of \$13.3 million associated with purchases, maturities and sales of investments, offset by capital expenditures of \$7.4 million.

Financing Activities

Net cash provided by financing activities during the three months ended March 26, 2016 was \$5.3 million compared to \$6.2 million in the corresponding period of 2015. Financing activities during both periods included net proceeds from the exercise of stock options and issuance of shares under our 2007 Employee Stock Purchase Plan ("ESPP"). These proceeds were offset by the minimum tax withholdings paid on behalf of employees for net share settlements of restricted stock units.

Liquidity

We believe that our current cash, cash equivalents and investments, together with cash generated from operations, exercise of employee stock options and purchases under our ESPP will be sufficient to meet our anticipated cash needs for working capital and capital expenditures for at least the next 12 months, including any cash we will be required to disburse as part of the Transmode related squeeze-out proceedings. For more information regarding the squeeze-out proceedings, see Note 6, "Business Combination" to the Notes to Condensed Consolidated Financial Statements. If these sources of cash are insufficient to satisfy our liquidity requirements beyond 12 months, we may require additional capital from equity or debt financings to fund our operations, to respond to competitive pressures or strategic opportunities, or otherwise. We may not be able to secure timely additional financing on favorable terms, or at all. The terms of any additional financings may place limits on our financial and operating flexibility. If we raise additional funds through further issuances of equity, convertible debt securities or other securities convertible into equity, our existing stockholders could suffer dilution in their percentage ownership of us, and any new securities we issue could have rights, preferences and privileges senior to those of holders of our common stock.

In May 2013, we issued the Notes, which will mature on June 1, 2018, unless earlier purchased by us or converted. Interest is payable semi-annually in arrears on June 1 and December 1 of each year, commencing December 1, 2013. The net proceeds from the Notes issuance were approximately \$144.5 million and were intended to be used for working capital and other general corporate purposes.

During the three months ended March 26, 2016, the closing price of our common stock did not meet the conversion criteria; therefore, holders of the Notes may not convert their notes during the second quarter of 2016. Any conversion of the Notes prior to their maturity or acceleration of the repayment of the Notes could have a material adverse effect on our cash flows, business, results of operations and financial condition, if we choose to settle the amounts in cash. Should the closing price conditions be met during the 30 consecutive trading days prior to the end of the second quarter of 2016 or a future quarter, the Notes will be convertible at their holders' option during the immediately following quarter. Under current market conditions, we do not expect the Notes will be converted in the short-term, even if the conversion criteria is met.

Upon conversion, it is our intention to pay cash equal to the lesser of the aggregate principal amount or the conversion value of the Notes. For any remaining conversion obligation, we intend to pay cash, shares of common stock or a combination of cash and shares of common stock, at our election. As of March 26, 2016, long-term debt, net, was \$125.8 million, which represents the liability component of the \$150.0 million principal balance, net of \$24.2 million of unamortized debt discount and debt issuance costs. The debt discount and debt issuance costs are currently being amortized over the remaining term until maturity of the Notes on June 1, 2018. To the extent that the holders of the Notes request conversion during an early conversion window, we may require funds for repayment of such Notes prior to their maturity date.

As of March 26, 2016, contractual obligations related to the Notes are payments of \$2.6 million due in the remainder of 2016, \$2.6 million due in 2017 and \$151.3 million due in 2018. These amounts represent principal and interest cash payments over the term of the Notes. Any future redemption or conversion of the Notes could impact the amount or timing of our cash payments. For more information regarding the Notes, see Note 11, "Convertible Senior Notes" to the Notes to Consolidated Financial Statements.

[Table of Contents](#)

As of March 26, 2016, we had \$275.1 million of cash, cash equivalents, and short-term investments, including \$54.8 million of cash and cash equivalents held by our foreign subsidiaries. Our cash in foreign locations is used primarily for operational activities in those locations, and we do not currently have the need or the intent to repatriate those funds to the United States. Our policy with respect to undistributed foreign subsidiaries' earnings is to consider those earnings to be indefinitely reinvested. If we were to repatriate these funds, we would be required to accrue and pay U.S. taxes on such amounts, however, due to our significant net operating loss carryforward position for both federal and state tax purposes, as well as the full valuation allowance provided against our U.S. and state net deferred tax assets, we would currently be able to offset any such tax obligations in their entirety. However, foreign withholding taxes may be applicable.

Off-Balance Sheet Arrangements

As of March 26, 2016, we did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

For a discussion of our exposure to market risk, see "Quantitative and Qualitative Disclosures About Market Risk" in Part II, Item 7A of our Annual Report on Form 10-K for the fiscal year ended December 26, 2015. There have been no material changes to our market risk during the three months ended March 26, 2016.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

An evaluation was performed by management, with the participation of our chief executive officer ("CEO") and our chief financial officer ("CFO"), of the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")). Disclosure controls and procedures are designed to ensure that information required to be disclosed in our reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Based on this evaluation, our CEO and CFO have concluded that, as of the end of the fiscal period covered by this quarterly report on Form 10-Q, our disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified by the SEC's rules and forms and that such information is accumulated and communicated to management, including the CEO and CFO, as appropriate, to allow timely decisions regarding required disclosures.

Changes in Internal Control over Financial Reporting

There were no changes to our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. *Legal Proceedings*

From time to time, we are subject to various legal proceedings, claims and litigation arising in the ordinary course of business. While the outcome of these matters is currently not determinable, we do not expect that the ultimate costs to resolve these matters will have a material effect on our consolidated financial position, results of operations or cash flows.

Item 1A. Risk Factors

A description of the risks and uncertainties associated with our business is set forth below. This description includes any material changes to and supersedes the description of the risks and uncertainties associated with our business previously disclosed in Part I, Item 1A of our Annual Report on Form 10-K for the fiscal year ended December 26, 2015. You should carefully consider such risks and uncertainties, together with the other information contained in this report, our Annual Report on Form 10-K for the fiscal year ended December 26, 2015 and in our other public filings. If any of such risks and uncertainties actually occurs, our business, financial condition or operating results could differ materially from the plans, projections and other forward-looking statements included in the section titled "Management's Discussion and Analysis of Financial Condition and Results of Operations" and elsewhere in this report and in our other public filings. In addition, if any of the following risks and uncertainties, or if any other risks and uncertainties, actually occurs, our business, financial condition or operating results could be harmed substantially, which could cause the market price of our stock to decline, perhaps significantly.

Our quarterly results may vary significantly from period to period, which could make our future results difficult to predict and could cause our operating results to fall below investor or analyst expectations.

Our quarterly results, in particular, our revenue, gross margins, operating expenses, operating margins and net income, have historically varied from period to period and may continue to do so in the future. In fiscal years prior to the fiscal year ended December 27, 2014, we had significant operating losses and there is no guarantee that we will be able to sustain profitability in the future. As of March 26, 2016, our accumulated deficit was \$527.4 million. As a result, comparing our operating results on a period-to-period basis may not be meaningful. Our budgeted expense levels are based, in large part, on our expectations of future revenue and the development efforts associated with that future revenue. Given the relatively fixed nature of our operating costs including those relating to our personnel and facilities, particularly for our engineering personnel, any substantial adjustment to our expenses to account for lower levels of revenue will be difficult to execute and may take significant time. Consequently, if our revenue does not meet projected levels in the short-term, our inventory levels and operating expenses would be high relative to revenue, resulting in potential operating losses. In addition, given the increase in the size of our business as a result of the acquisition of Transmode, our historical results may not be indicative of our combined operations going forward.

Factors that may contribute to fluctuations in our quarterly results, many of which are outside our control and may be difficult to predict, include:

- fluctuations in demand, sales cycles and prices for products and services, including discounts given in response to competitive pricing pressures;
- changes in customers' budgets for optical transport network equipment purchases and changes in their purchasing cycles;
- fluctuations in our customer, product or geographic mix, including the impact of new customer deployments, which typically carry lower gross margins;
- the process of integrating the Transmode business with our business and the associated potential disruptions to our business;
- how quickly, or at all, the market adopts our solutions, including in new markets like metro and DCI;
- order cancellations or reductions or delays in delivery schedules by our customers;
- our ability to control costs, including our operating expenses and the costs of components we purchase for our products;
- our ability to maintain volumes and yields on products manufactured in our internal manufacturing facilities;
- the timing of product releases or upgrades by us;
- any significant changes in the competitive dynamics of our market, including any new entrants, or customer or competitor consolidation;
- readiness of customer sites for installation of our products;
- availability of third party suppliers to provide contract engineering and installation services for us;
- the timing of recognizing revenue in any given quarter, including the impact of revenue recognition standards and any future changes in U.S. GAAP or new interpretations of existing accounting rules;

[Table of Contents](#)

- the impact of a significant natural disaster, such as an earthquake, severe weather, or tsunami or other flooding, as well as interruptions or shortages in the supply of utilities such as water and electricity, in a key location such as our Northern California facilities, which is located near major earthquake fault lines and in a designated flood zone; and
- general economic conditions in domestic and international markets.

Many factors affecting our results of operations are beyond our control and make it difficult to predict our results for a particular quarter or to accurately predict future revenue beyond a one-quarter time horizon. If our revenue or operating results do not meet the expectations of investors or securities analysts or fall below any guidance we provide to the market, the price of our common stock may decline substantially.

Our business and operations have experienced rapid growth in recent periods, including growth related to the acquisition of Transmode, and if we do not effectively manage any future growth or are unable to improve our systems, processes and controls, our operating results may be adversely affected.

We have experienced rapid growth and increased demand for our products over the last few years. Our employee headcount and number of end-customers have increased significantly, and we expect to continue to grow over the next year. For example, from the end of fiscal 2013 to the end of fiscal 2015, our headcount increased from 1,318 to 2,056 employees. The growth and expansion of our business and product and service offerings places a continuous significant strain on our management, and operational and financial resources. To manage any future growth effectively, we must continue to improve and expand our information technology and financial infrastructure, our operating and administrative systems, and our ability to manage headcount and processes in an efficient manner.

We may not be able to successfully scale improvements to our enterprise resource planning system or implement or scale improvements to our other systems, processes and controls in an efficient or timely manner, or in a manner that does not negatively affect our operating results. In addition, our existing systems, processes and controls 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 disrupt existing customer relationships, cause us to lose customers, or increase our technical support costs. Our failure to improve our systems, processes and controls, 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. Failure to manage any future growth effectively could result in increased costs, negatively impact our customers' satisfaction with our products and services, and harm our operating results.

We may not be able to successfully integrate our business with the business of Transmode, and we may not be able to achieve the anticipated strategic benefits from our acquisition of Transmode.

The transaction to acquire Transmode was completed on August 20, 2015, and Transmode's business became a part of our business as of that date. The integration of our company with Transmode has been and will continue to be a complex, costly and time-consuming process. The integration process will require substantial management time and attention, which may divert attention and resources from other important areas, including our existing business. Additional unanticipated costs may be incurred in the course of integrating the respective businesses. In addition, we may not be able to fully realize the anticipated strategic benefits of the combination, which include the ability to achieve revenue synergies, increased negotiating leverage with third-party suppliers as a result of higher volumes, and, to a lesser extent, certain operating expense synergies expected from avoiding duplicative costs. The failure to successfully integrate the combined operations, including retention of key employees, could impact our ability to realize the full benefits of our acquisition of Transmode. If we are not able to achieve the anticipated strategic benefits of the combination, it could adversely affect our business, financial condition and results of operations, and could adversely affect the market price of our common stock if the integration or the anticipated financial and strategic benefits of the acquisition are not realized as rapidly as, or to the extent anticipated by investors and analysts. Failure to achieve these anticipated benefits could result in increased costs and decreases in future revenue and/or net income following the acquisition.

Our gross margin may fluctuate from quarter-to-quarter and may be adversely affected by a number of factors, some of which are beyond our control.

Our gross margin fluctuates from period-to-period and varies by customer and by product. Over the past eight fiscal quarters, our gross margin has ranged from 42.5% to 47.5%. Our gross margin is likely to continue to fluctuate and will be affected by a number of factors, including:

- the mix in any period of the types of customers purchasing our products as well as the product mix;
- significant new customer deployments, often with a higher portion of lower margin common equipment as we deploy network footprint;
- the volume of Infinera Instant Bandwidth licenses sold;
- price discounts negotiated by our customers;
- charges for excess or obsolete inventory;
- changes in the price or availability of components for our products;
- changes in our manufacturing costs, including fluctuations in yields and production volumes; and
- increased warranty or repair costs.

It is likely that the average unit prices of our products will decrease over time in response to competitive pricing pressures, increased negotiated sales discounts, new product introductions by us or our competitors or other factors. In addition, some of our customer contracts contain clauses that require us to annually decrease the sales price of our products to these customers. In response, we will need to reduce the cost of our products through manufacturing efficiencies, design improvements and cost reductions. If these efforts are not successful or if we are unable to reduce our costs by more than the reduction in the price of our products, our revenue and gross margin will decline, causing our operating results to decline. Fluctuations in gross margin may make it difficult to manage our business and achieve or maintain profitability.

Aggressive business tactics by our competitors may harm our business.

The markets in which we compete are extremely competitive and this often results in aggressive business tactics by our competitors, including:

- aggressively pricing their optical transport products and other portfolio products, including offering significant one-time discounts and guaranteed future price decreases;
- offering optical products at a substantial discount or free when bundled together with the customers' router or wireless equipment purchases;
- providing financing, marketing and advertising assistance to customers;
- influencing customer requirements to emphasize different product capabilities, which better suit their products;
- offering to repurchase our equipment from existing customers; and
- asserting intellectual property rights.

The level of competition and pricing pressure tend to increase when competing for larger high-profile opportunities or during periods of economic weakness when there are fewer network build-out projects. If we fail to compete successfully against our current and future competitors, or if our current or future competitors continue or expand aggressive business tactics, including those described above, demand for our products could decline, we could experience delays or cancellations of customer orders, and/or we could be required to reduce our prices to compete in the market.

Our ability to increase our revenue will depend upon continued growth of demand by consumers and businesses for additional network capacity and on the level and timing of capital spending by our customers.

Our future success depends on factors that increase the amount of data transmitted over communications networks and the growth of optical transport networks to meet the increased demand for optical capacity. These factors include the growth of mobile, video, and cloud-based services, increased broadband connectivity and the continuing adoption of high-capacity, revenue-generating services. If demand for such bandwidth does not continue, or slows down, the need for increased bandwidth across networks and the market for optical transport networking equipment may not continue to grow and our product sales would be negatively impacted.

In addition, demand for our products depends on the level and timing of capital spending in optical networks by Service Providers as they construct, expand and upgrade the capacity of their optical networks. Capital spending is cyclical in our industry and spending by customers can change on short notice. Any future decisions by our customers to reduce capital spending, whether caused by weakening economic conditions, changes in government regulations relating to telecommunications and data networks, or other reasons, could have a material adverse effect on our business, results of operations and financial condition.

If we lose key personnel or fail to attract and retain additional qualified personnel when needed, our business may be harmed.

Our success depends to a significant degree upon the continued contributions of our key management, engineering, sales and marketing, and finance personnel, many of whom would be difficult to replace. For example, senior members of our engineering team have unique technical experience that would be difficult to replace. We do not have long-term employment contracts or key person life insurance covering any of our key personnel. Because our products are complex, we must hire and retain a large number of highly trained customer service and support personnel to ensure that the deployment of our products does not result in network disruption for our customers. We believe our future success will depend in large part upon our ability to identify, attract and retain highly skilled managerial, engineering, sales, marketing, finance, and customer service and support personnel. Competition for these individuals is intense in our industry, especially in the San Francisco Bay Area where we are headquartered. We may not succeed in identifying, attracting and retaining appropriate personnel. The loss of the services of any of our key personnel, the inability to identify, attract or retain qualified personnel in the future or delays in hiring qualified personnel, particularly engineers and sales personnel, could make it difficult for us to manage our business and meet key objectives, such as timely product introductions.

Any delays in the development and introduction of our products or in releasing enhancements to our existing products may harm our business.

Because our products are based on complex technology, including, in some cases, the development of next-generation PICs and specialized ASICs, we may experience unanticipated delays in developing, improving, manufacturing or deploying these products. The development process for our PICs is lengthy, and any modifications to our PICs, including the development of our next-generation PICs, entail significant development cost and risks.

At any given time, various new product introductions and enhancements to our existing products, including future products based on our next-generation PICs, are in the development phase and are not yet ready for commercial manufacturing or deployment. We rely on third parties, some of which are relatively early stage companies, to develop and manufacture components for our next-generation products, which can require custom development. The maturing process from laboratory prototype to customer trials, and subsequently to general availability, involves a significant number of simultaneous development efforts. These efforts often must be completed in a timely manner so that they may be introduced into the product development cycle for our systems, and include:

- completion of product development, including the completion of any associated PIC development, such as our next-generation PICs, and the completion of associated module development, including modules developed by third parties;
- the qualification and multiple sourcing of critical components;
- validation of manufacturing methods and processes;
- extensive quality assurance and reliability testing and staffing of testing infrastructure;

[Table of Contents](#)

- validation of software; and
- establishment of systems integration and systems test validation requirements.

Each of these steps, in turn, presents risks of failure, rework or delay, any one of which could decrease the speed and scope of product introduction and marketplace acceptance of our products. New generations of our PICs, specialized ASICs and intensive software testing are important to the timely introduction of new products and enhancements to our existing products, and are subject to these development risks. In addition, unexpected intellectual property disputes, failure of critical design elements, and a host of other development execution risks may delay, or even prevent, the introduction of new products or enhancements to our existing products. If we do not develop and successfully introduce or enhance products in a timely manner, our competitive position will suffer. In addition, if we do not develop and successfully introduce or enhance products in sufficient time so as to satisfy our customer's expectations, we may lose future business from such customers and harm our reputation and our customer relationships, either of which would harm our business and operating results.

The markets in which we compete are highly competitive and we may not be able to compete effectively.

Competition in the optical transport networking equipment market is intense, and we expect such competition to increase. In the long-haul market, our main competitors include current WDM suppliers, such as Alcatel-Lucent (acquired by Nokia), Ciena Corporation, Coriant, Huawei and ZTE. In the metro market we face the same competitors as in long-haul, plus Cisco, Adva, Arista and Fujitsu. In addition, there are also several smaller, but established, companies that offer one or more products that compete directly or indirectly with our offerings. In the DCI market, we believe we are one of the few companies shipping purpose built small form factor devices. Several other competitors including many named above have announced competing solutions that we expect to be shipping in 2016.

Competition in the markets we serve is based on any one or a combination of the following factors:

- price and other commercial terms;
- functionality;
- form factor or density;
- power consumption;
- heat dissipation;
- customer qualification testing;
- existing business and customer relationships;
- the ability of products and services to meet customers' immediate and future network requirements;
- installation and operation simplicity;
- service and support;
- scalability and investment protection; and
- product lead times.

In addition to the current competitors, other companies have, or may in the future develop, products that are or could be competitive with our products. In particular, if a competitor develops a photonic integrated circuit or another solution with similar and/or better functionality than our PICs, our business could be harmed. We also expect to encounter further consolidation in the markets in which we compete. Consolidation among our competitors could lead to a changing competitive landscape, capabilities and market share, which could harm our results of operations.

Some of our competitors have substantially greater name recognition and technical, financial and marketing resources along with better established relationships with Service Providers and other potential customers than we have. Many of our competitors have more resources and more experience in developing or acquiring new products and technologies and in creating market awareness for those products and technologies. In addition, many of our competitors have the financial resources to offer competitive products at aggressive pricing levels that could prevent us from competing effectively. Further, many of our competitors have built long-standing relationships with some of our prospective customers and have the ability to provide financing to customers and could, therefore, have an inherent advantage in selling products to those customers.

We also compete with low-cost producers from China that can increase pricing pressure on us and a number of smaller companies that provide competition for a specific product, customer segment or geographic market. These competitors often base their products on the latest commercially available technologies. Due to the narrower focus of their efforts, these competitors may achieve commercial availability of their products more quickly than we can and may provide attractive alternatives to our customers.

Our large customers have substantial negotiating leverage, which may require that we agree to terms and conditions that result in decreased revenue due to lower average selling prices and potentially higher cost of sales leading to lower gross margin, all of which would harm our operating results.

Substantial changes in the optical transport networking industry have occurred over the last few years. Many potential customers have experienced static or declining revenue. Many of our customers have substantial debt burdens, many have experienced financial distress, and some have gone out of business, been acquired by other service providers, or announced their withdrawal from segments of the business. Consolidation in the markets in which we compete has resulted in changes in the structure of the communications networking industry, with greater concentration of purchasing power in a small number of large service providers, cable operators and ICPs. The increased concentration among our customer base may also lead to increased competition for new network deployments and increased negotiating power for our customers. This may require us to decrease our average selling prices, which would have an adverse impact on our operating results.

Further, many of our customers are large Service Providers that have substantial purchasing power and leverage in negotiating contractual arrangements with us. Our customers have and may continue to seek advantageous pricing, payment and other commercial terms. We have and may continue to be required to agree to unfavorable commercial terms with these customers, including reducing the average selling price of our products or agreeing to extended payment terms in response to these commercial requirements or competitive pricing pressures. To maintain acceptable operating results, we will need to comply with these commercial terms, develop and introduce new products and product enhancements on a timely basis and continue to reduce our costs.

We must respond to rapid technological change and comply with evolving industry standards and requirements for our products to be successful.

The optical transport networking equipment market is characterized by rapid technological change, changes in customer requirements and evolving industry standards. We continually invest in research and development to sustain or enhance our existing products, but the introduction of new communications technologies and the emergence of new industry standards or requirements could render our products obsolete. Further, in developing our products, we have made, and will continue to make, assumptions with respect to which standards or requirements will be adopted by our customers and competitors. If the standards or requirements adopted by our prospective customers are different from those on which we have focused our efforts, market acceptance of our products would be reduced or delayed and our business would be harmed.

We are continuing to invest a significant portion of our research and development efforts in the development of our next-generation products. We expect our competitors to continue to improve the performance of their existing products and to introduce new products and technologies and to influence customers' buying criteria so as to emphasize product capabilities that we do not, or may not, possess. To be competitive, we must properly anticipate future customer requirements and we must continue to invest significant resources in research and development, sales and marketing, and customer support. If we do not anticipate these future customer requirements and invest in the technologies necessary to enable us to have and to sell the appropriate solutions, it may limit our competitive position and future sales, which would have an adverse effect on our business and financial condition. We may not have sufficient resources to make these investments and we may not be able to make the technological advances necessary to be competitive.

The manufacturing process for our PICs is very complex and the partial or complete loss of our manufacturing facilities, or a reduction in yields or an inability to scale capacity to meet customer demands could harm our business.

The manufacturing process for our PICs and certain components of our products is very complex. In the event that any of the manufacturing facilities utilized to build these components were fully or partially destroyed, as a result of fire, water damage, or otherwise, it would limit our ability to produce our products. Because of the complex nature of our manufacturing facilities, such loss would take a considerable amount of time to repair or rebuild. The partial or complete loss of any of our manufacturing facilities, or an event causing the interruption in our

use of such facility for any extended period of time would cause our business, financial condition and operating results to be harmed.

Minor deviations in the PIC manufacturing process can cause substantial decreases in yields and, in some cases, cause production to be suspended. In the past, we have had significant variances in our PIC yields, including production interruptions and suspensions and may have continued yield variances, including additional interruptions or suspensions in the future. We expect our manufacturing yield for our next-generation PICs to be lower initially and increase as we achieve full production. Poor yields from our PIC manufacturing process or defects, integration issues or other performance problems in our products could limit our ability to satisfy customer demand requirements, and could damage customer relations and cause business reputation problems, harming our business and operating results.

Our inability to obtain sufficient manufacturing capacity to meet demand, either in our own facilities or through foundry or similar arrangements with third parties, could harm our relationships with our customers, our business and our operating results.

We are dependent on sole source and limited source suppliers for several key components, and if we fail to obtain these components on a timely basis, we will not meet our customers' product delivery requirements.

We currently purchase several key components for our products from single or limited sources. In particular, we rely on our own production of certain components of our products, such as PICs, and on third parties as sole source suppliers for certain of the components of our products, including ASICs, field-programmable gate arrays, processors, and other semiconductor and optical components. We have increased our reliance on third parties to develop and manufacture components for certain products, some of which require custom development. We purchase these components on a purchase order basis and have no long-term contracts with many of these sole source or limited source suppliers. If any of our sole source or limited source suppliers suffer from capacity constraints, lower than expected yields, deployment delays, work stoppages or any other reduction or disruption in output, they may be unable to meet our delivery schedule which could result in lost revenue, additional product costs and deployment delays that could harm our business and customer relationships. Further, our suppliers could enter into exclusive arrangements with our competitors, refuse to sell their products or components to us at commercially reasonable prices or at all, go out of business or discontinue their relationships with us. We may be unable to develop alternative sources for these components.

The loss of a source of supply, or lack of sufficient availability of key components, could require us to redesign products that use such components, which could result in lost revenue, additional product costs and deployment delays that could harm our business and customer relationships. In addition, if we do not receive critical components for our products in a timely manner, we will be unable to deliver those components to our contract manufacturer in a timely manner and would, therefore, be unable to meet our prospective customers' product delivery requirements. In the past, we have experienced delivery delays because of lack of availability of components or reliability issues with components that we were purchasing. In addition, some of our suppliers have gone out of business, merged with another supplier, or limited their supply of components to us, which may cause us to experience longer than normal lead times and supply delays. We may in the future experience a shortage of certain components as a result of our own manufacturing issues, manufacturing issues at our suppliers or contract manufacturers, capacity problems experienced by our suppliers or contract manufacturers, strong demand in the industry for such components, or other disruptions in our supply chain. In addition, global macroeconomic conditions are likely to continue to create pressure on us and our suppliers to accurately project overall component demand and manufacturing capacity. These supplier disruptions may continue to occur in the future, which could limit our ability to produce our products and cause us to fail to meet a customer's delivery requirements. Any failure to meet our customers' product delivery requirements could harm our reputation and our customer relationships, either of which would harm our business and operating results.

If we fail to accurately forecast demand for our products, we may have excess or insufficient inventory, which may increase our operating costs, decrease our revenue and harm our business.

We are required to generate forecasts of future demand for our products several months prior to the scheduled delivery to our prospective customers. This requires us to make significant investments before we know if corresponding revenue will be recognized. Lead times for materials and components, including ASICs, that we need to order for the manufacture of our products vary significantly and depend on factors such as the specific supplier, contract terms and demand for each component at a given time. In the past, we have experienced lengthening in lead times for certain components. If the lead times for components are lengthened, we may be required to purchase increased levels of such components to satisfy our delivery commitments to our customers.

If we overestimate market demand for our products and, as a result, increase our inventory in anticipation of customer orders that do not materialize, we will have excess inventory, which could result in increased risk of obsolescence and significant inventory write-downs. Furthermore, this will result in reduced production volumes and our fixed costs will be spread across fewer units, increasing our per unit costs. If we underestimate demand for our products, we will have inadequate inventory, which could slow down or interrupt the manufacturing of our products and result in delays in shipments and our ability to recognize revenue. In addition, we may be unable to meet our supply commitments to customers, which could result in a loss of certain customer opportunities or a breach of our customer agreements resulting in payment of damages.

We are dependent on a small number of key customers for a significant portion of our revenue and the loss of, or a significant reduction in, orders from one or more of our key customers would reduce our revenue and harm our operating results.

A relatively small number of customers account for a large percentage of our revenue. For example, for the three months ended March 26, 2016, three customers accounted for approximately 47% of our total revenue. As a result, our business will be harmed if any of our key customers do not generate as much revenue as we forecast, stop purchasing from us, or substantially reduce their orders to us. In addition, our business will be harmed if we fail to maintain our competitive advantage with our key customers. While we view our diverse customer base across multiple customer verticals as a strength and expect greater overall customer diversification as a result of our acquisition of Transmode, we expect a relatively small number of customers to continue to account for a large percentage of revenue from period to period.

Our ability to continue to generate revenue from our key customers will depend on our ability to maintain strong relationships with these customers and introduce new products that are desirable to these customers at competitive prices, and we may not be successful at doing so. In most cases, our sales are made to these customers pursuant to standard purchase agreements rather than long-term purchase commitments, and orders may be canceled or reduced readily. In the event of a cancellation or reduction of an order, we may not have enough time to reduce operating expenses to minimize the effect of the lost revenue on our business. Our operating results will continue to depend on our ability to sell our products to our key customers.

If our contract manufacturers do not perform as we expect, our business may be harmed.

We rely on third party contract manufacturers to perform a portion of the manufacturing of our products, and our future success will depend on our ability to have sufficient volumes of our products manufactured in a cost-effective and quality-controlled manner. We have engaged third parties to manufacture certain elements of our products at multiple contract manufacturing sites located around the world but do not have long-term agreements in place with some of our manufacturers and suppliers that will guarantee product availability, or the continuation of particular pricing or payment terms. There are a number of risks associated with our dependence on contract manufacturers, including:

- reduced control over delivery schedules, particularly for international contract manufacturing sites;
- reliance on the quality assurance procedures of third parties;
- potential uncertainty regarding manufacturing yields and costs;
- potential lack of adequate capacity during periods of high demand;
- potential uncertainty related to the use of international contract manufacturing sites;
- limited warranties on components;
- potential misappropriation of our intellectual property; and

- potential manufacturing disruptions (including disruptions caused by geopolitical events, military actions or natural disasters).

Any of these risks could impair our ability to fulfill orders. Our contract manufacturers may not be able to meet the delivery requirements of our customers, which could decrease customer satisfaction and harm our product sales. If our contract manufacturers are unable or unwilling to continue manufacturing our products or components of our products in required volumes or our relationship with any of our contract manufacturers is discontinued for any reason, we would be required to identify and qualify alternative manufacturers, which could cause us to be unable to meet our supply requirements to our customers and result in the breach of our customer agreements. Qualifying a new contract manufacturer and commencing volume production is expensive and time-consuming and if we are required to change or qualify a new contract manufacturer, we could lose revenue and damage our customer relationships.

If we fail to protect our intellectual property rights, our competitive position could be harmed or we could incur significant expense to enforce our rights.

We depend on our ability to protect our proprietary technology. We rely on a combination of methods to protect our intellectual property, including limiting access to certain information, and utilizing trade secret, patent, copyright and trademark laws and confidentiality agreements with employees and third parties, all of which offer only limited protection. The steps we have taken to protect our proprietary rights may be inadequate to preclude misappropriation or unauthorized disclosure of our proprietary information or infringement of our intellectual property rights, and our ability to police such misappropriation, unauthorized disclosure or infringement is uncertain, particularly in countries outside of the United States. This is likely to become an increasingly important issue as we expand our operations and product development into countries that provide a lower level of intellectual property protection. We do not know whether any of our pending patent applications will result in the issuance of patents or whether the examination process will require us to narrow our claims, and even if patents are issued, they may be contested, circumvented or invalidated. Moreover, the rights granted under any issued patents may not provide us with a competitive advantage, and, as with any technology, competitors may be able to develop similar or superior technologies to our own now or in the future.

Protecting against the unauthorized use of our products, trademarks and other proprietary rights is expensive, difficult, time consuming and, in some cases, impossible. Litigation may be necessary in the future to enforce or defend our intellectual property rights, to protect our trade secrets or to determine the validity or scope of the proprietary rights of others. Such litigation could result in substantial cost and diversion of management resources, either of which could harm our business, financial condition and operating results. Furthermore, many of our current and potential competitors have the ability to dedicate substantially greater resources to enforce their intellectual property rights than we do. Accordingly, despite our efforts, we may not be able to prevent third parties from infringing upon or misappropriating our intellectual property.

Claims by others that we infringe their intellectual property could harm our business.

Our industry is characterized by the existence of a large number of patents and frequent claims and related litigation regarding patent and other intellectual property rights. In particular, many leading companies in the optical transport networking industry, including our competitors, have extensive patent portfolios with respect to optical transport networking technology. We expect that infringement claims may increase as the number of products and competitors in our market increases and overlaps occur. From time to time, third parties may assert exclusive patent, copyright, trademark and other intellectual property rights to technologies and related standards that are important to our business or seek to invalidate the proprietary rights that we hold. Competitors or other third parties have, and may continue to assert claims or initiate litigation or other proceedings against us or our manufacturers, suppliers or customers alleging infringement of their proprietary rights, or seeking to invalidate our proprietary rights, with respect to our products and technology. In addition, we have had certain patent licenses with third parties that have not been renewed, and if we cannot successfully renew these licenses, we could face claims of infringement. In the event that we are unsuccessful in defending against any such claims, or any resulting lawsuit or proceedings, we could incur liability for damages and/or have valuable proprietary rights invalidated.

Any claim of infringement from a third party, even one without merit, could cause us to incur substantial costs defending against the claim, and could distract our management from running our business. Furthermore, a party making such a claim, if successful, could secure a judgment that requires us to pay substantial damages. A judgment could also include an injunction or other court order that could prevent us from offering our products. In addition, we might be required to seek a license for the use of such intellectual property, which may not be available

on commercially reasonable terms or at all. Alternatively, we may be required to develop non-infringing technology, which would require significant effort and expense and may ultimately not be successful. Any of these events could harm our business, financial condition and operating results. Competitors and other third parties have and may continue to assert infringement claims against our customers and sales partners. Any of these claims would require us to initiate or defend potentially protracted and costly litigation on their behalf, regardless of the merits of these claims, because we generally indemnify our customers and sales partners from claims of infringement of proprietary rights of third parties. If any of these claims succeed, we may be forced to pay damages on behalf of our customers or sales partners, which could have an adverse effect on our business, financial condition and operating results.

We incorporate open source software into our products. Although we monitor our use of open source software closely, the terms of many open source licenses have not been interpreted by U.S. courts, and there is a risk that such licenses could be construed in a manner that could impose unanticipated conditions or restrictions on our ability to commercialize our products. In such event, we could be required to seek licenses from third parties in order to continue offering our products, to re-engineer our products or to discontinue the sale of our products in the event re-engineering cannot be accomplished on a timely basis, any of which could adversely affect our business, operating results and financial condition.

The trading price of our common stock has been volatile and is likely to be volatile in the future.

The trading prices of our common stock and the securities of other technology companies have been and may continue to be highly volatile. Factors affecting the trading price of our common stock include:

- variations in our operating results;
- announcements of technological innovations, new services or service enhancements, strategic alliances or agreements by us or by our competitors;
- the gain or loss of customers;
- recruitment or departure of key personnel;
- changes in the estimates of our future operating results or external guidance on those results or changes in recommendations or business expectations by any securities analysts that elect to follow our common stock;
- our ability to integrate Transmode's business with our business efficiently;
- mergers and acquisitions by us or by our competitors;
- market conditions in our industry, the industries of our customers and the economy as a whole; and
- adoption or modification of regulations, policies, procedures or programs applicable to our business.

In addition, if the market for technology stocks or the stock market in general experiences loss of investor confidence, the trading price of our common stock could decline for reasons unrelated to our business, financial condition or operating results. 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. Each of these factors, among others, could harm the value of your investment in our common stock. Some companies that have had volatile market prices for their securities have had securities class action lawsuits filed against them. If a suit were filed against us, regardless of its merits or outcome, it could result in substantial costs and divert management's attention and resources.

Unfavorable macroeconomic and market conditions may adversely affect our industry, business and gross margin.

Our business depends on the overall demand for additional bandwidth capacity and on the economic health and willingness of our customers and potential customers to make capital commitments to purchase our products and services. As a result of macroeconomic or market uncertainty, we may face new risks that we have not yet identified. In addition, a number of the risks associated with our business, which are disclosed in these risk factors, may increase in likelihood, magnitude or duration.

In the past, unfavorable macroeconomic and market conditions have resulted in sustained periods of decreased demand for optical communications products. These conditions may also result in the tightening of credit markets, which may limit or delay our customers' ability to obtain necessary financing for their purchases of our

[Table of Contents](#)

products. A lack of liquidity in the capital markets or the continued uncertainty in the global economic environment may cause our customers to delay or cancel their purchases, increase the time they take to pay or default on their payment obligations, each of which would negatively affect our business and operating results. Continued weakness and uncertainty in the global economy could cause some of our customers to become illiquid, delay payments or adversely affect our collection of their accounts, which could result in a higher level of bad debt expense. In addition, currency fluctuations could negatively affect our international customers' ability or desire to purchase our products.

Challenging economic conditions have from time to time contributed to slowdowns in the telecommunications industry in which we operate. Such slowdowns may result in:

- reduced demand for our products as a result of constraints on capital spending by our customers;
- increased price competition for our products, not only from our competitors, but also as a result of our customer's or potential customer's utilization of inventoried or underutilized products, which could put additional downward pressure on our near term gross profits;
- risk of excess or obsolete inventories;
- excess manufacturing capacity and higher associated overhead costs as a percentage of revenue; and
- more limited ability to accurately forecast our business and future financial performance.

A lack of liquidity and economic uncertainty may adversely affect our suppliers or the terms on which we purchase products from these suppliers. It may also cause some of our suppliers to become illiquid. Any of these impacts could limit our ability to obtain components for our products from these suppliers and could adversely impact our supply chain or the delivery schedule to our customers. This also could require us to purchase more expensive components, or re-design our products, which could cause increases in the cost of our products and delays in the manufacturing and delivery of our products. Such events could harm our gross margin and harm our reputation and our customer relationships, either of which could harm our business and operating results.

Product performance problems, including undetected errors in our hardware or software, or deployment delays could harm our business and reputation.

The development and production of products with high technology content is complicated and often involves problems with software, components and manufacturing methods. Complex hardware and software systems, such as our products, can often contain undetected errors when first introduced or as new versions are released. In addition, errors associated with components we purchase from third parties, including customized components, may be difficult to resolve. We have experienced issues in the past in connection with our products, including failures due to the receipt of faulty components from our suppliers. We suspect that errors, including potentially serious errors, may be found from time to time in our products. Our products may suffer degradation of performance and reliability over time.

If reliability, quality or network monitoring problems develop, a number of negative effects on our business could result, including:

- delays in our ability to recognize revenue;
- costs associated with fixing software or hardware defects or replacing products;
- high service and warranty expenses;
- delays in shipments;
- high inventory excess and obsolescence expense;
- high levels of product returns;
- diversion of our engineering personnel from our product development efforts;
- delays in collecting accounts receivable;
- payment of liquidated damages, performance guarantees or similar penalties;
- reduced orders from existing customers; and
- declining interest from potential customers.

[Table of Contents](#)

Because we outsource the manufacturing of certain components of our products, we may also be subject to product performance problems as a result of the acts or omissions of third parties.

From time to time, we encounter interruptions or delays in the activation of our products at a customer's site. These interruptions or delays may result from product performance problems or from issues with installation and activation, some of which are outside our control. If we experience significant interruptions or delays that we cannot promptly resolve, the associated revenue for these installations may be delayed or confidence in our products could be undermined, which could cause us to lose customers and fail to add new customers.

Our debt obligations may adversely affect our ability to raise additional capital and will be a burden on our future cash flows and cash resources, particularly if these obligations are settled in cash upon maturity or sooner upon an event of default.

In May 2013, we issued the Notes. The degree to which we are leveraged could have important consequences, including, but not limited to, the following:

- our ability to obtain additional financing in the future for working capital, capital expenditures, acquisitions, litigation, general corporate or other purposes may be limited;
- a substantial portion of our future cash balance may be dedicated to the payment of the principal of our indebtedness as we have the intention to pay the principal amount of the Notes in cash upon conversion if specified conditions are met or when due, such that we would not have those funds available for use in our business; and
- if, upon any conversion of the Notes we are required to satisfy our conversion obligation with shares of our common stock or if a make-whole fundamental change occurs, our existing stockholders' interest in us would be diluted.

Our ability to meet our payment obligations under our debt instruments depends on our future cash flow performance. This, to some extent, is subject to general economic, financial, competitive, legislative and regulatory factors, as well as other factors that may be beyond our control. There can be no assurance that our business will generate positive cash flow from operations, or that additional capital will be available to us, in an amount sufficient to enable us to meet our debt payment obligations and to fund other liquidity needs. If we are unable to generate sufficient cash flow to service our debt obligations, we may need to refinance or restructure our debt, sell assets, reduce or delay capital investments, or seek to raise additional capital. If we were unable to implement one or more of these alternatives, we may be unable to meet our debt payment obligations. As a result, we may be more vulnerable to economic downturns, less able to withstand competitive pressures and less flexible in responding to changing business and economic conditions.

We may issue additional shares of our common stock in connection with the conversion of the Notes, and thereby dilute our existing stockholders and potentially adversely affect the market price of our common stock.

In the event that some or all of the Notes are converted into common stock, the ownership interests of existing stockholders will be diluted, and any sales in the public market of any shares of our common stock issuable upon such conversion of the Notes could adversely affect the prevailing market price of our common stock. In addition, the anticipated conversion of the Notes could depress the market price of our common stock.

The make-whole fundamental change provisions of the Notes may delay or prevent an otherwise beneficial takeover attempt of us.

If a make-whole fundamental change such as an acquisition of our company occurs prior to the maturity of the Notes, under certain circumstances, the conversion rate for the Notes will increase such that additional shares of our common stock will be issued upon conversion of the Notes in connection with such make-whole fundamental change. The increase in the conversion rate will be determined based on the date on which the make-whole fundamental change occurs or becomes effective and the price paid (or deemed paid) per share of our common stock in such transaction. This increase will be dilutive to our existing stockholders. Our obligation to increase the conversion rate upon the occurrence of a make-whole fundamental change may, in certain circumstances, delay or prevent a takeover of us that might otherwise be beneficial to our stockholders.

The acquisition of Transmode may not be accretive to our earnings and may cause dilution to our earnings per share, which may negatively affect the market price of our common stock.

We currently anticipate that the acquisition will be accretive to our earnings per share in the fiscal year 2016. This expectation is based on preliminary estimates that may materially change. We may encounter additional integration-related costs, fail to realize the benefits anticipated in the acquisition or be subject to other factors that adversely affect preliminary estimates. Any of these factors could delay or significantly reduce the expected accretive effect of the acquisition and contribute to a decrease in the price of our common stock.

If we need additional capital in the future, it may not be available to us on favorable terms, or at all.

Our business requires significant capital. We have historically relied on outside debt or equity financing as well as cash flow from operations to fund our operations, capital expenditures and expansion. We may require additional capital from equity or debt financings in the future to fund our operations or respond to competitive pressures or strategic opportunities. We have a history of significant operating losses, including a net loss of \$32.1 million for 2013. In the event that we require additional capital, we may not be able to secure timely additional financing on favorable terms, or at all. The terms of any additional financing may place limits on our financial and operating flexibility. If we raise additional funds through further issuances of equity, convertible debt securities or other securities convertible into equity, our existing stockholders could suffer dilution in their percentage ownership of our company, and any new securities we issue could have rights, preferences and privileges senior to those of holders of our common stock. If we are unable to obtain adequate financing or financing on terms satisfactory to us, if and when we require it, our ability to grow or support our business and to respond to business challenges could be limited and our business will be harmed.

Our sales cycle can be long and unpredictable, which could result in an unexpected revenue shortfall in any given quarter.

Our products can have a lengthy sales cycle, which can extend from six to twelve months and may take even longer for larger prospective customers. Our prospective customers conduct significant evaluation, testing, implementation and acceptance procedures before they purchase our products. We incur substantial sales and marketing expenses and expend significant management effort during this time, regardless of whether we make a sale.

Because the purchase of our equipment involves substantial cost, most of our customers wait to purchase our equipment until they are ready to deploy it in their network. As a result, it is difficult for us to accurately predict the timing of future purchases by our customers. In addition, product purchases are often subject to budget constraints, multiple approvals and unplanned administrative processing and other delays. If sales expected from customers for a particular quarter are not realized in that quarter or at all, our revenue will be negatively impacted.

Our international sales and operations subject us to additional risks that may harm our operating results, some of which may be enhanced following our acquisition of Transmode.

Sales of our products into international markets are an important part of our business and these international sales, particularly in the EMEA region, are expected to increase as a result of the Transmode acquisition. During the three months ended March 26, 2016 and March 28, 2015, we derived approximately 29% and 32%, respectively, of our revenue from customers outside of the United States. We expect that significant management attention and financial resources will be required for our international activities over the foreseeable future as we continue to expand our international presence, including as a result of our acquisition of Transmode. We have a limited history and experience selling our products into developing international markets, such as Asia Pacific, Middle East and Africa, and Latin America. Furthermore, in some countries, our success in selling our products and growing revenue will depend in part on our ability to form relationships with local partners. Our inability to identify appropriate partners or reach mutually satisfactory arrangements for international sales of our products could impact our ability to maintain or increase international market demand for our products. In addition, many of the companies we compete against internationally have greater name recognition and a more substantial sales and marketing presence.

We have sales and support personnel in numerous countries worldwide. In addition, we have established development centers in Canada, China, India and Sweden, and expect to continue to increase hiring of personnel for these facilities. There is no assurance that our reliance upon development resources in international locations will enable us to achieve meaningful cost reductions or greater resource efficiency.

[Table of Contents](#)

Our international operations are subject to inherent risks, and our future results could be adversely affected by a variety of factors, many of which are outside of our control, including:

- greater difficulty in collecting accounts receivable and longer collection periods;
- difficulties of managing and staffing international offices, and the increased travel, infrastructure and legal compliance costs associated with multiple international locations;
- political, social and economic instability, including wars, terrorism, political unrest, boycotts, curtailment of trade and other business restrictions;
- tariff and trade barriers and other regulatory requirements or contractual limitations on our ability to sell or develop our products in certain foreign markets;
- less effective protection of intellectual property than is afforded to us in the United States or other developed countries;
- local laws and practices that favor local companies, including business practices that we are prohibited from engaging in by the Foreign Corrupt Practices Act and other anti-corruption laws and regulations;
- potentially adverse tax consequences; and
- effects of changes in currency exchange rates, particularly relative increases in the exchange rate of the U.S. dollar versus other currencies that could negatively affect our financial results and cash flows.

International customers may also require that we comply with certain testing or customization of our products to conform to local standards. The product development costs to test or customize our products could be extensive and a material expense for us.

Our international operations are subject to increasingly complex foreign and U.S. laws and regulations, including but not limited to anti-corruption laws, such as the Foreign Corrupt Practices Act and the UK Bribery Act and equivalent laws in other jurisdictions, antitrust or competition laws, and data privacy laws, among others. Violations of these laws and regulations could result in fines and penalties, criminal sanctions against us, our officers, or our employees, prohibitions on the conduct of our business and on our ability to offer our products and services in one or more countries, and could also materially affect our reputation, our international expansion efforts, our ability to attract and retain employees, our business, and our operating results. Although we have implemented policies, procedures and training designed to ensure compliance with these laws and regulations, there can be no complete assurance that any individual employee, contractor or agent will not violate our policies. Additionally, the costs of complying with these laws (including the costs of investigations, auditing and monitoring) could also adversely affect our current or future business.

As we continue to expand our business globally, our success will depend, in large part, on our ability to anticipate and effectively manage these and other risks associated with our international operations. Our failure to manage any of these risks could harm our international operations and reduce our international sales.

We may be adversely affected by fluctuations in currency exchange rates.

A portion of our sales and expenses stem from countries outside of the United States, and are in currencies other than U.S. dollars, and therefore subject to foreign currency fluctuation. We expect the acquisition of Transmode to increase our sales and expenses that are denominated in currencies other than U.S. dollars. Accordingly, fluctuations in foreign currency rates could have a material impact on our financial results in future periods. We may enter into other financial contracts to reduce the impact of foreign currency fluctuations. We currently enter into foreign currency exchange forward contracts to reduce the impact of foreign currency fluctuations on accounts receivable. These forward contracts reduce the impact of currency exchange rate movements on certain transactions, but do not cover all foreign-denominated transactions and therefore do not entirely eliminate the impact of fluctuations in exchange rates that could negatively affect our results of operations and financial condition.

If we fail to maintain effective internal control over financial reporting in the future, the accuracy and timing of our financial reporting may be adversely affected.

We are required to comply with Section 404 of the Sarbanes-Oxley Act of 2002. The provisions of the act require, among other things, that we maintain effective internal control over financial reporting and disclosure controls and procedures. Preparing our financial statements involves a number of complex processes, many of which are done manually and are dependent upon individual data input or review. These processes include, but are not limited to, calculating revenue, deferred revenue and inventory costs. While we continue to automate our processes and enhance our review and put in place controls to reduce the likelihood for errors, we expect that for the foreseeable future, many of our processes will remain manually intensive and thus subject to human error.

Any acquisitions we make could disrupt our business and harm our financial condition and operations.

We have made strategic acquisitions of businesses, technologies and other assets in the past, such as the recently completed acquisition of Transmode. The expansion of our business through acquisitions allows us to complement our technological capabilities and address new markets. In the event of any future acquisitions, we may not ultimately strengthen our competitive position or achieve our goals, or they may be viewed negatively by customers, financial markets or investors and we could:

- issue stock that would dilute our current stockholders' percentage ownership;
- incur debt and assume other liabilities;
- use a substantial portion of our cash resources; or
- incur amortization expenses related to other intangible assets and/or incur large and immediate write-offs.

Acquisitions can result in adverse tax consequences, warranty or product liability exposure related to acquired assets, additional stock-based compensation expense, and write-up of acquired inventory to fair value. In addition, we may record goodwill and other purchased intangible assets in connection with an acquisition and incur impairment charges in the future. If our actual results, or the plans and estimates used in future impairment analyses, are less favorable than the original estimates used to assess the recoverability of these assets, we could incur additional impairment charges.

Acquisitions also involve numerous risks that could disrupt our ongoing business and distract our management team, including:

- problems integrating the acquired operations, technologies or products with our own;
- diversion of management's attention from our core business;
- adverse impact on overall company operating results;
- adverse effects on existing business relationships with suppliers and customers;
- risks associated with entering new markets; and
- loss of key employees.

Our failure to adequately manage the risks associated with an acquisition could have an adverse effect on our business, financial condition and operating results.

Unforeseen health, safety and environmental costs could harm our business.

Our manufacturing operations use substances that are regulated by various federal, state and international laws governing health, safety and the environment, including the Waste Electrical and Electronic Equipment Directive, Directive on the Restriction of the Use of Certain Hazardous Substances in Electrical and Electronic Equipment, and the Registration, Evaluation, Authorization, and Restriction of Chemicals regulations adopted by the European Union. If we experience a problem with complying with these regulations, it could cause an interruption or delay in our manufacturing operations or could cause us to incur liabilities for any costs related to health, safety or environmental remediation. We could also be subject to liability if we do not handle these substances in compliance with safety standards for storage and transportation and applicable laws. If we experience a problem or fail to comply with such safety standards, our business, financial condition and operating results may be harmed.

We are subject to governmental regulations that could adversely affect our business.

We are subject to export control laws that limit which products we sell and where and to whom we sell our products. These export control laws also limit our ability to conduct product development activities in certain countries. In addition, various countries regulate the import of certain technologies and have enacted laws that could limit our ability to distribute our products or could limit our customers' ability to implement our products in those countries. Changes in our products or changes in import and export regulations may create delays in the introduction of our products in international markets, prevent our customers with international operations from deploying our products throughout their global systems or, in some cases, prevent the import and export of our products to certain countries altogether. Any change in import and export 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 customers with international operations. Failure to comply with these and similar laws on a timely basis, or at all, decreased use of our products or any limitation on our ability to export or sell our products would adversely affect our business, financial condition and operating results.

Our product or manufacturing standards could also be impacted by new or revised environmental rules and regulations or other social initiatives. For instance, the SEC adopted new disclosure requirements in 2012 relating to the sourcing of certain minerals from the Democratic Republic of Congo and certain other adjoining countries. Those rules, which required reporting for the first time in calendar 2014, could adversely affect our costs, the availability of minerals used in our products and our relationships with customers and suppliers.

The Federal Communications Commission ("FCC") has jurisdiction over the entire U.S. communications industry and, as a result, our products and our U.S. customers are subject to FCC rules and regulations. Current and future FCC regulations, including regulations on net neutrality or generally affecting communications services, our products or our customers' businesses could negatively affect our business. In addition, international regulatory standards could impair our ability to develop products for international customers in the future. Moreover, many jurisdictions are evaluating or implementing regulations relating to cybersecurity, privacy and data protection, which can affect the market and requirements for networking and communications equipment. Delays caused by our compliance with regulatory requirements could result in postponements or cancellations of product orders. Further, we may not be successful in obtaining or maintaining any regulatory approvals that may, in the future, be required to operate our business. Any failure to obtain such approvals could harm our business and operating results.

Natural disasters, terrorist attacks or other catastrophic events could harm our operations.

Our headquarters and the majority of our infrastructure, including our PIC fabrication manufacturing facility, are located in Northern California, an area that is susceptible to earthquakes, floods and other natural disasters. Further, a terrorist attack aimed at Northern California or at the United States energy or telecommunications infrastructure could hinder or delay the development and sale of our products. In the event that an earthquake, terrorist attack or other man-made or natural catastrophe were to destroy any part of our facilities, or certain of our contract manufacturers' facilities, destroy or disrupt vital infrastructure systems or interrupt our operations for any extended period of time, our business, financial condition and operating results would be harmed.

Security incidents, such as data breaches and cyber-attacks, could compromise our intellectual property and proprietary or confidential information and cause significant damage to our business and reputation.

In the ordinary course of our business, we maintain sensitive data on our networks, including data related to our intellectual property and data related to our business, customers and business partners, which is considered proprietary or confidential information. We believe that companies in the technology industry have been increasingly subject to a wide variety of security incidents, cyber-attacks and other attempts to gain unauthorized access. While the secure maintenance of this information is critical to our business and reputation, our network and storage applications may be subject to unauthorized access by hackers or breached due to operator error, malfeasance or other system disruptions. It may be difficult to anticipate or immediately detect such security incidents or data breaches and the damage caused as a result. Accordingly, a data breach, cyber-attack, or unauthorized access or disclosure of our information, could compromise our intellectual property and reveal proprietary or confidential business information. In addition, these security incidents could also cause us to incur significant remediation costs and expenses, disrupt key business operations, subject us to liability and divert attention of management and key information technology resources, any of which could cause significant harm to our business and reputation.

Anti-takeover provisions in our charter documents and Delaware law could discourage, delay or prevent a change in control of our company and may affect the trading price of our common stock.

We are a Delaware corporation and the anti-takeover provisions of the Delaware General Corporation Law, which apply to us, may discourage, delay or prevent a change in control by prohibiting us from engaging in a business combination with an interested stockholder for a period of three years after the person becomes an interested stockholder, even if a change of control would be beneficial to our existing stockholders. In addition, our amended and restated certificate of incorporation and amended and restated bylaws may discourage, delay or prevent a change in our management or control over us that stockholders may consider favorable. Our amended and restated certificate of incorporation and amended and restated bylaws:

- authorize the issuance of “blank check” convertible preferred stock that could be issued by our board of directors to thwart a takeover attempt;
- establish a classified board of directors, as a result of which the successors to the directors whose terms have expired will be elected to serve from the time of election and qualification until the third annual meeting following their election;
- require that directors only be removed from office for cause and only upon a supermajority stockholder vote;
- provide that vacancies on the board of directors, including newly-created directorships, may be filled only by a majority vote of directors then in office rather than by stockholders;
- prevent stockholders from calling special meetings; and
- prohibit stockholder action by written consent, requiring all actions to be taken at a meeting of the stockholders.

[Table of Contents](#)

Item 6. Exhibits

<u>Exhibit No.</u>	<u>Description</u>
3.1	Amended and Restated Bylaws, incorporated herein by reference to Exhibit 3.1 of the Registrant's Current Report on Form 8-K (No. 001-33486), filed with the SEC on February 29, 2016.
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
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

The certification attached as Exhibit 32.1 that accompanies this Quarterly Report on Form 10-Q is not deemed filed with the SEC and is not to be incorporated by reference into any of our filings 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 Quarterly Report on Form 10-Q, irrespective of any general incorporation language contained in such filing.

SIGNATURES

Pursuant to the requirements 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.

Infinera Corporation

By: _____ /s/ BRAD FELLER

Brad Feller
Chief Financial Officer
(Duly Authorized Officer and Principal
Financial Officer)

Date: May 4, 2016

**CERTIFICATION PURSUANT TO RULE 13a-14(a) OR 15d-14(a) OF THE SECURITIES EXCHANGE ACT OF 1934,
AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Thomas J. Fallon, certify that:

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

Dated: May 4, 2016

By: _____ /s/ THOMAS J. FALLON
Thomas J. Fallon
Chief Executive Officer
(Principal Executive Officer)

**CERTIFICATION PURSUANT TO RULE 13a-14(a) OR 15d-14(a) OF THE SECURITIES EXCHANGE ACT OF 1934,
AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Brad Feller, certify that:

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

Dated: May 4, 2016

By: _____ /s/ BRAD FELLER
Brad Feller
Chief Financial Officer
(Principal Financial and Accounting Officer)

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

I, Thomas J. Fallon, certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report on Form 10-Q of Infinera Corporation for the quarterly period ended March 26, 2016 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and the information contained in such Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of Infinera Corporation.

Date: May 4, 2016

/s/ THOMAS J. FALLON

Thomas J. Fallon
Chief Executive Officer
(Principal Executive Officer)

I, Brad Feller, certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report on Form 10-Q of Infinera Corporation for the quarterly period ended March 26, 2016 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and the information contained in the Quarterly Report on Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of Infinera Corporation.

Date: May 4, 2016

/s/ BRAD FELLER

Brad Feller
Chief Financial Officer
(Principal Financial and Accounting Officer)

A signed original of this written statement required by Section 906 of the Sarbanes-Oxley Act of 2002 has been provided to Infinera Corporation and will be retained by Infinera Corporation and furnished to the U.S. Securities and Exchange Commission or its staff upon request.

This certification "accompanies" the Quarterly Report on Form 10-Q to which it relates, is not deemed filed with the U.S. Securities and Exchange Commission and is not to be incorporated by reference into any filing of Infinera Corporation 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 the Quarterly Report on Form 10-Q), irrespective of any general incorporation language contained in such filing.