

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

**FORM 10-Q**

(Mark One)

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

**For the quarterly period ended September 30, 2017**

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: 1-36254**

**Avid Technology, Inc.**

(Exact Name of Registrant as Specified in Its Charter)

**Delaware**

(State or Other Jurisdiction of  
Incorporation or Organization)

**04-2977748**

(I.R.S. Employer  
Identification No.)

**75 Network Drive**

**Burlington, Massachusetts 01803**

(Address of Principal Executive Offices, Including Zip Code)

**(978) 640-6789**

(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 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, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer ☐

Non-accelerated Filer ☐

(Do not check if smaller reporting company)

Accelerated Filer ☒

Smaller Reporting Company ☐

Emerging growth company ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

The number of shares outstanding of the registrant's Common Stock, par value \$0.01, as of November 6, 2017 was 41,186,120.

AVID TECHNOLOGY, INC.  
FORM 10-Q  
FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2017

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## CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q (“Form 10-Q”) includes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. For this purpose, any statements contained in this Form 10-Q that relate to future results or events are forward-looking statements. Forward-looking statements may be identified by use of forward-looking words, such as “anticipate,” “believe,” “confidence,” “could,” “estimate,” “expect,” “feel,” “intend,” “may,” “plan,” “should,” “seek,” “will” and “would,” or similar expressions.

Forward-looking statements may involve subjects relating to, among others, the following:

- our ability to successfully implement our Avid Everywhere strategic plan and other strategic initiatives, including our cost saving strategies;
- the anticipated trends and developments in our markets and the success of our products in these markets;
- our ability to develop, market and sell new products and services;
- our business strategies and market positioning;
- our ability to achieve our goal of expanding our market positions;
- anticipated trends relating to our sales, financial condition or results of operations, including our shift to a recurring revenue model and complex enterprise sales with elongated sales cycles;
- the expected timing of recognition of revenue backlog as revenue, and the timing of recognition of revenues from subscription offerings;
- our ability to successfully consummate acquisitions, or investment transactions and successfully integrate acquired businesses, including Orad Hi-Tech Ltd (“Orad”), into our operations;
- our anticipated benefits and synergies from, and the anticipated financial impact of, any acquired business (including Orad);
- the anticipated performance of our products;
- changes in inventory levels;
- plans regarding repatriation of foreign earnings;
- the outcome, impact, costs and expenses of any litigation or government inquiries to which we are or become subject;
- the effect of the continuing worldwide macroeconomic uncertainty on our business and results of operations, including Brexit;
- our ability to accelerate growth of our Cloud-enabled Avid Everywhere platform;
- our compliance with covenants contained in the agreements governing our indebtedness;
- our ability to service our debt and meet the obligations thereunder, including our ability to satisfy our conversion and repurchase obligations under our convertible notes due 2020;
- the effects of seasonality on our revenues and results of operations;
- fluctuations in foreign exchange and interest rates;
- our ability to effectively mitigate and remediate the material weakness in our internal control over financial reporting, and the expected timing thereof;
- the risk of restatement of our financial statements;
- estimated asset and liability values and amortization of our intangible assets;
- our capital resources and the adequacy thereof; and
- worldwide political uncertainty, in particular the risk that the United States may withdraw from or materially modify NAFTA or other international trade agreements.

Actual results and events in future periods may differ materially from those expressed or implied by forward-looking statements in this Form 10-Q. There are a number of factors that could cause actual events or results to differ materially from those indicated or implied by forward-looking statements, many of which are beyond our control, including the risk factors discussed herein and in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2016, in Part II and in other documents we file from time to time with the U.S. Securities and Exchange Commission (“SEC”). In

addition, the forward-looking statements contained in this Form 10-Q represent our estimates only as of the date of this filing and should not be relied upon as representing our estimates as of any subsequent date. While we may elect to update these forward-looking statements in the future, we specifically disclaim any obligation to do so, whether to reflect actual results, changes in assumptions, changes in other factors affecting such forward-looking statements or otherwise.

We own or have rights to trademarks and service marks that we use in connection with the operation of our business. Avid is a trademark of Avid Technology, Inc. Other trademarks, logos, and slogans registered or used by us and our subsidiaries in the United States and other countries include, but are not limited to, the following: Avid Everywhere, Avid NEXIS, AirSpeed, EUCON, iNEWS, Interplay, MediaCentral, Mbox, Media Composer, NewsCutter, Nitris, Pro Tools, Sibelius and Symphony. Other trademarks appearing in this Form 10-Q are the property of their respective owners.

# PART I - FINANCIAL INFORMATION

## ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

### AVID TECHNOLOGY, INC. CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (in thousands except per share data, unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
<b>Net revenues:</b>				
Products	\$ 54,319	\$ 63,740	\$ 152,980	\$ 223,841
Services	50,946	55,279	158,765	172,794
Total net revenues	105,265	119,019	311,745	396,635
<b>Cost of revenues:</b>				
Products	29,485	26,793	80,478	82,405
Services	13,472	14,885	41,747	45,126
Amortization of intangible assets	1,950	1,950	5,850	5,850
Total cost of revenues	44,907	43,628	128,075	133,381
<b>Gross profit</b>	<b>60,358</b>	<b>75,391</b>	<b>183,670</b>	<b>263,254</b>
<b>Operating expenses:</b>				
Research and development	16,025	19,953	51,904	62,791
Marketing and selling	25,652	27,231	80,481	89,027
General and administrative	15,193	13,822	43,268	48,359
Amortization of intangible assets	362	567	1,088	2,135
Restructuring (recoveries) costs, net	(582)	5,314	6,464	7,878
Total operating expenses	56,650	66,887	183,205	210,190
<b>Operating income</b>	<b>3,708</b>	<b>8,504</b>	<b>465</b>	<b>53,064</b>
Interest and other expense, net	(4,701)	(4,707)	(13,465)	(14,049)
<b>(Loss) income before income taxes</b>	<b>(993)</b>	<b>3,797</b>	<b>(13,000)</b>	<b>39,015</b>
Benefit from income taxes	(1,065)	(5,321)	(326)	(3,983)
<b>Net income (loss)</b>	<b>\$ 72</b>	<b>\$ 9,118</b>	<b>\$ (12,674)</b>	<b>\$ 42,998</b>
Net income (loss) per common share – basic	\$0.00	\$0.23	\$(0.31)	\$1.08
Net income (loss) per common share – diluted	\$0.00	\$0.23	\$(0.31)	\$1.08
Weighted-average common shares outstanding – basic	41,133	40,194	40,954	39,814
Weighted-average common shares outstanding – diluted	41,355	40,476	40,954	39,950

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

**AVID TECHNOLOGY, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**  
(in thousands, unaudited)

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2017</b>	<b>2016</b>	<b>2017</b>	<b>2016</b>
<b>Net income (loss)</b>	\$ 72	\$ 9,118	\$ (12,674)	\$ 42,998
<b>Other comprehensive income (loss):</b>				
Foreign currency translation adjustments	2,014	155	6,803	2,613
<b>Comprehensive income (loss)</b>	<u>\$ 2,086</u>	<u>\$ 9,273</u>	<u>\$ (5,871)</u>	<u>\$ 45,611</u>

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

**AVID TECHNOLOGY, INC.**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
(in thousands, unaudited)

	September 30, 2017	December 31, 2016
<b><u>ASSETS</u></b>		
<b>Current assets:</b>		
Cash and cash equivalents	\$ 44,094	\$ 44,948
Accounts receivable, net of allowances of \$10,494 and \$8,618 at September 30, 2017 and December 31, 2016, respectively	40,864	43,520
Inventories	41,160	50,701
Prepaid expenses	8,537	6,031
Other current assets	9,925	5,805
<b>Total current assets</b>	144,580	151,005
Property and equipment, net	23,273	30,146
Intangible assets, net	15,995	22,932
Goodwill	32,643	32,643
Long-term deferred tax assets, net	1,355	1,245
Other long-term assets	7,404	11,610
<b>Total assets</b>	<u>\$ 225,250</u>	<u>\$ 249,581</u>
<b><u>LIABILITIES AND STOCKHOLDERS' DEFICIT</u></b>		
<b>Current liabilities:</b>		
Accounts payable	\$ 28,620	\$ 26,435
Accrued compensation and benefits	32,734	25,387
Accrued expenses and other current liabilities	32,848	34,088
Income taxes payable	806	1,012
Short-term debt	5,072	5,000
Deferred revenues	122,475	146,014
<b>Total current liabilities</b>	222,555	237,936
Long-term debt	191,300	188,795
Long-term deferred tax liabilities, net	—	913
Long-term deferred revenues	72,091	79,670
Other long-term liabilities	9,726	12,178
<b>Total liabilities</b>	<u>495,672</u>	<u>519,492</u>
<b>Commitments and contingencies (Note 7)</b>		
<b>Stockholders' deficit:</b>		
Common stock	423	423
Additional paid-in capital	1,038,308	1,043,063
Accumulated deficit	(1,283,822)	(1,271,148)
Treasury stock at cost	(22,238)	(32,353)
Accumulated other comprehensive loss	(3,093)	(9,896)
<b>Total stockholders' deficit</b>	<u>(270,422)</u>	<u>(269,911)</u>
<b>Total liabilities and stockholders' deficit</b>	<u>\$ 225,250</u>	<u>\$ 249,581</u>

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

**AVID TECHNOLOGY, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(in thousands, unaudited)

	<b>Nine Months Ended September 30,</b>	
	<b>2017</b>	<b>2016</b>
<b>Cash flows from operating activities:</b>		
Net (loss) income	\$ (12,674)	\$ 42,998
Adjustments to reconcile net (loss) income to net cash provided by (used in) operating activities:		
Depreciation and amortization	16,932	19,169
(Recovery) provision for doubtful accounts	(158)	890
Stock-based compensation expense	5,874	6,116
Non-cash provision for restructuring	3,191	1,137
Non-cash interest expense	7,255	7,935
Unrealized foreign currency transaction losses	6,885	2,021
Benefit from deferred taxes	(925)	(5,187)
Changes in operating assets and liabilities:		
Accounts receivable	2,877	17,057
Inventories	9,542	(7,561)
Prepaid expenses and other assets	(3,958)	(1,493)
Accounts payable	2,065	(19,627)
Accrued expenses, compensation and benefits and other liabilities	543	(4,384)
Income taxes payable	(161)	347
Deferred revenues	(31,185)	(108,343)
<b>Net cash provided by (used in) operating activities</b>	<b>6,103</b>	<b>(48,925)</b>
<b>Cash flows from investing activities:</b>		
Purchases of property and equipment	(6,125)	(9,681)
Increase in other long-term assets	(24)	(17)
Decrease (increase) in restricted cash	1,790	(4,544)
<b>Net cash used in investing activities</b>	<b>(4,359)</b>	<b>(14,242)</b>
<b>Cash flows from financing activities:</b>		
Proceeds from long-term debt	912	100,000
Repayment of debt	(3,750)	(2,500)
Proceeds from the issuance of common stock under employee stock plans	219	5,914
Common stock repurchases for tax withholdings for net settlement of equity awards	(732)	(803)
Proceeds from revolving credit facilities	—	25,000
Payments on revolving credit facilities	—	(30,000)
Payments for credit facility issuance costs	—	(5,020)
<b>Net cash (used in) provided by financing activities</b>	<b>(3,351)</b>	<b>92,591</b>
Effect of exchange rate changes on cash and cash equivalents	753	391
Net (decrease) increase in cash and cash equivalents	(854)	29,815
Cash and cash equivalents at beginning of period	44,948	17,902
Cash and cash equivalents at end of period	<u>\$ 44,094</u>	<u>\$ 47,717</u>
<b>Supplemental information:</b>		
Cash paid for income taxes, net of refunds	\$ 463	\$ 1,678
Cash paid for interest	7,406	5,767

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



**AVID TECHNOLOGY, INC.**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**1. FINANCIAL INFORMATION**

The accompanying condensed consolidated financial statements include the accounts of Avid Technology, Inc. and its wholly owned subsidiaries (collectively, “Avid” or the “Company”). These financial statements are unaudited. However, in the opinion of management, the condensed consolidated financial statements reflect all normal and recurring adjustments necessary for their fair statement. Interim results are not necessarily indicative of results expected for any other interim period or a full year. The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions for Form 10-Q and, therefore, do not include all information and footnotes necessary for a complete presentation of operations, comprehensive income (loss), financial position and cash flows of the Company in conformity with accounting principles generally accepted in the United States of America (“U.S. GAAP”). The accompanying condensed consolidated balance sheet as of December 31, 2016 was derived from the Company’s audited consolidated financial statements and does not include all disclosures required by U.S. GAAP for annual financial statements. The Company filed audited consolidated financial statements as of and for the year ended December 31, 2016 in its Annual Report on Form 10-K for the year ended December 31, 2016, which included information and footnotes necessary for such presentation. The financial statements contained in this Form 10-Q should be read in conjunction with the audited consolidated financial statements in the Company’s Annual Report on Form 10-K for the year ended December 31, 2016.

The Company’s preparation of condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the dates of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the reported periods. Actual results could differ from the Company’s estimates.

The Company has generally funded operations in recent years through the use of existing cash balances, supplemented from time to time with the proceeds of long-term debt and borrowings under its credit facilities. The Company’s principal sources of liquidity include cash and cash equivalents totaling \$44.1 million as of September 30, 2017.

In February 2016, the Company committed to a cost efficiency program that encompassed a series of measures intended to allow the Company to more efficiently operate in a leaner, more directed cost structure. These measures included reductions in the Company’s workforce, consolidation of facilities, transfers of certain business processes to lower cost regions and reductions in other third-party service costs. The cost efficiency program was substantially complete as of June 30, 2017.

In connection with the cost efficiency program, on February 26, 2016, the Company entered into a Financing Agreement (the “Financing Agreement”) with the lenders party thereto (the “Lenders”). Pursuant to the Financing Agreement, the Company entered into a term loan in the original aggregate principal amount of \$100.0 million. The Financing Agreement also originally provided the Company with the ability to draw up to a maximum of \$5.0 million in revolving credit. All outstanding loans under the Financing Agreement will become due and payable in February 2021, or in May 2020 if the \$125.0 million in outstanding principal of 2.00% convertible senior notes due June 15, 2020 (the “Notes”) has not been repaid or refinanced by such time.

The Financing Agreement contains customary representations and warranties, covenants, mandatory prepayments, and events of default under which the Company’s payment obligations may be accelerated. On March 14, 2017 (the “Amendment No. 1 Effective Date”), the Company entered into an amendment (the “First Amendment”) to the Financing Agreement. The First Amendment modified the covenant requiring the Company to maintain a Leverage Ratio (defined to mean the ratio of (a) total funded indebtedness to (b) consolidated EBITDA) such that following the Amendment No. 1 Effective Date, the Company is required to maintain a Leverage Ratio of no greater than 3.50:1.00 for the four quarters ended March 31, 2017, 4.20:1.00 for the four quarters ended June 30, 2017, 4.75:1.00 for the four quarters ended September 30, 2017, 4.80:1.00 for the four quarters ending December 31, 2017, 4.40:1.00 for each of the four quarters ending March 31, 2018 through March 31, 2019, respectively, and thereafter declining over time from 3.50:1.00 to 2.50:1.00. Following the Amendment No. 1 Effective Date, interest accrues on outstanding borrowings under the credit facility and the term loan (each as defined in the Financing Agreement) at a rate of either the LIBOR Rate (as defined in

the Financing Agreement) plus 7.25% or a Reference Rate (as defined in the Financing Agreement) plus 6.25%, at the option of the Company. As of September 30, 2017, the Company was in compliance with the Financing Agreement covenants.

On November 9, 2017 (the “Amendment No. 2 Effective Date”), the Company entered into an amendment (the “Second Amendment”) to the Financing Agreement. The Second Amendment extended an additional \$15.0 million term loan to the Company, thereby increasing the aggregate principal amount of the term loan to \$115.0 million. The Second Amendment also increased the amount of available revolving credit by \$5.0 million to an aggregate amount of \$10.0 million. The additional \$15.0 million term loan must be repaid in quarterly principal payments of \$187,500 commencing in March 2018. The Second Amendment also granted the Company the ability to use up to \$15.0 million to purchase Notes and modified the definition of consolidated EBITDA used in the Leverage Ratio calculation to adjust for expected changes in deferred revenue due to the adoption of Accounting Standards Codification (“ASC”) Topic 606, the new revenue recognition guidance.

The Company’s ability to satisfy the Leverage Ratio covenant in the future is dependent on its ability to maintain bookings and billings at or above levels experienced over the last 12 months. In recent quarters, the Company has experienced volatility in bookings and billings resulting from, among other things, (i) its transition towards subscription and recurring revenue streams and the resulting decline in traditional upfront product sales, (ii) volatility in currency rates and in particular the U.S. dollar against the Euro, (iii) significant changes and trends in the media industry and the impact they have had on the Company’s customers and (iv) the impact of new and anticipated product launches and features. In addition to the impact of new bookings and billings, U.S. GAAP revenues recognized as the result of the existence of Implied Maintenance Release PCS (as defined below) will be significantly lower in the remainder of 2017, as compared to 2016 periods, which will have an adverse impact on the Company’s Leverage Ratio.

In the event bookings and billings in future quarters are lower than the Company currently anticipates, the Company may be forced to take remedial actions which could include, among other things (and where allowed by the Lenders), (i) further cost reductions, (ii) seeking replacement financing, (iii) raising funds through the issuance of additional equity or debt securities or the incurrence of additional borrowings, or (iv) disposing of certain assets or businesses. Such remedial actions, which may not be available on favorable terms or at all, could have a material adverse impact on the Company’s business. If the Company is not in compliance with the Leverage Ratio and is unable to obtain an amendment or waiver, such noncompliance may result in an event of default under the Financing Agreement, which could permit acceleration of the outstanding indebtedness under the Financing Agreement and require the Company to repay such indebtedness before the scheduled due date. If an event of default were to occur, the Company might not have sufficient funds available to make the payments required. If the Company is unable to repay amounts owed, the lenders may be entitled to foreclose on and sell substantially all of the Company’s assets, which secure its borrowings under the Financing Agreement.

On January 26, 2017, the Company entered into an exclusive distributor agreement (the “Distributor Agreement”) with Beijing Jetsen Technology Co., Ltd. (“Jetsen”), pursuant to which Jetsen became the exclusive distributor for Avid products and services in the greater China region. The Distributor Agreement has a five-year term, and Jetsen is required to make at least \$75.8 million of aggregate purchases under the agreement over the first three years. At the same time, the Company also entered into a securities purchase agreement (the “Securities Purchase Agreement”), with Jetsen, pursuant to which it agreed to sell to Jetsen shares of Avid common stock. In June 2017, Avid and Jetsen amended the Securities Purchase Agreement. Under the amended terms, Jetsen will invest \$18.2 million in Avid, in return for a minority stake in the Company of between 4.5% and 8.9% of Avid outstanding common stock on a fully diluted basis. The closing of the investment is subject to closing conditions, including China regulatory approvals. In the event regulatory approval is not obtained in the fourth quarter of 2017, either party may elect to terminate the Securities Purchase Agreement for any reason. The exact number of shares to be issued and sold at closing will be determined by reference to the trading price of Avid common stock before closing.

The Company's cash requirements vary depending on factors such as the growth of its business, changes in working capital, and capital expenditures. Management expects to operate the business and execute its strategic initiatives principally with funds generated from operations, remaining net proceeds from the term loan borrowings under the Financing Agreement and draw up to a maximum of \$10.0 million under the Financing Agreement's revolving credit facility. Management anticipates that the Company will have sufficient internal and external sources of liquidity to fund operations and anticipated working capital and other expected cash needs for at least the next 12 months, as well as for the foreseeable future.

### ***Subsequent Events***

The Company evaluated subsequent events through the date of issuance of these financial statements and, except for the subsequent events disclosed above and in Note 7 and Note 10, no subsequent events required recognition or disclosure in these financial statements.

### ***Significant Accounting Policies - Revenue Recognition***

#### **General**

The Company commences revenue recognition when persuasive evidence of an arrangement exists, delivery has occurred, the sales price is fixed or determinable and collection is reasonably assured. Generally, the products the Company sells do not require significant production, modification or customization. Installation of the Company's products is generally routine, consists of implementation and configuration and does not have to be performed by the Company.

At the time of a sales transaction, the Company makes an assessment of the collectability of the amount due from the customer. Revenues are recognized only if it is reasonably assured that collection will occur. When making this assessment, the Company considers customer credit-worthiness and historical payment experience. If it is determined from the outset of the arrangement that collection is not reasonably assured, revenues are recognized on a cash basis, provided that all other revenue recognition criteria are satisfied. At the outset of the arrangement, the Company also assesses whether the fee associated with the order is fixed or determinable and free of contingencies or significant uncertainties. When assessing whether the fee is fixed or determinable, the Company considers the payment terms of the transaction, the Company's collection experience in similar transactions and the Company's involvement, if any, in third-party financing transactions, among other factors. If the fee is not fixed or determinable, revenues are recognized only as payments become due from the customer, provided that all other revenue recognition criteria are met. If a significant portion of the fee is due after the Company's normal payment terms, the Company evaluates whether the Company has sufficient history of successfully collecting past transactions with similar terms without offering concessions. If that collection history is sufficient, revenue recognition commences, upon delivery of the products, assuming all other revenue recognition criteria are satisfied. If the Company was to make different judgments or assumptions about any of these matters, it could cause a material increase or decrease in the amount of revenues reported in a particular period.

The Company often receives multiple purchase orders or contracts from a single customer or a group of related customers that are evaluated to determine if they are, in effect, part of a single arrangement. In situations when the Company has concluded that two or more orders with the same customer are so closely related that they are, in effect, parts of a single arrangement, the Company accounts for those orders as a single arrangement for revenue recognition purposes. In other circumstances, when the Company has concluded that two or more orders with the same customer are independent buying decisions, such as an earlier purchase of a product and a subsequent purchase of a software upgrade or maintenance contract, the Company accounts for those orders as separate arrangements for revenue recognition purposes.

For many of its products, the Company has had an ongoing practice of making available, at no charge to customers, minor feature and compatibility enhancements as well as bug fixes on a when-and-if-available basis (collectively "Software Updates"), for a period of time after initial sales to end users. The implicit obligation to make such Software Updates available to customers over a period of time represents implied post-contract customer support, which is deemed to be a deliverable in each arrangement and is accounted for as a separate element ("Implied Maintenance Release PCS").

Over the last two years, in connection with a strategic initiative to increase support and other recurring revenue streams, the Company has taken a number of steps to eliminate the longstanding practice of providing Implied Maintenance Release

PCS for many of its products, including Media Composer, Pro Tools and Sibelius product lines. In the third quarter and fourth quarter of 2015, respectively, the Company concluded that Implied Maintenance Release PCS for its Media Composer and Sibelius product lines had ceased. In the first quarter of 2016, in connection with the release of Cloud Collaboration in Pro Tools version 12.5, which was an undelivered feature that had prevented the Company from recognizing any revenue related to new Pro Tools 12 software sales as it represented a specified upgrade right for which vendor specific objective evidence (“VSOE”) of fair value was not available, the Company concluded that Implied Maintenance Release PCS for Pro Tools 12 product lines had also ended. As a result of the conclusion that Implied Maintenance Release PCS on Pro Tools 12 has ended, revenue and net income in the first quarter of 2016 increased approximately \$11.1 million, reflecting the recognition of orders received after the launch of Pro Tools 12 that would have qualified for earlier recognition using the residual method of accounting. In addition, the elimination of Implied Maintenance Release PCS also resulted in the accelerated recognition of maintenance and product revenues that were previously being recognized on a ratable basis over a much longer expected period of Implied Maintenance Release PCS rather than the contractual maintenance period. The reduction in the estimated amortization period of transactions being recognized on a ratable basis resulted in an additional \$12.0 million and \$33.7 million of revenue during the three and nine months ended September 30, 2016, respectively.

The Company enters into certain contractual arrangements that have multiple elements, one or more of which may be delivered subsequent to the delivery of other elements. These multiple-deliverable arrangements may include products, support, training, professional services and Implied Maintenance Release PCS. For these multiple-element arrangements, the Company allocates revenue to each deliverable of the arrangement based on the relative selling prices of the deliverables. In such circumstances, the Company first determines the selling price of each deliverable based on (i) VSOE of fair value if that exists, (ii) third-party evidence of selling price (“TPE”), when VSOE does not exist, or (iii) best estimate of the selling price (“BESP”), when neither VSOE nor TPE exists. Revenue is then allocated to the non-software deliverables as a group and to the software deliverables as a group using the relative selling prices of each of the deliverables in the arrangement based on the selling price hierarchy. The Company’s process for determining BESP for deliverables for which VSOE or TPE does not exist involves significant management judgment. In determining BESP, the Company considers a number of data points, including:

- the pricing established by management when setting prices for deliverables that are intended to be sold on a standalone basis;
- contractually stated prices for deliverables that are intended to be sold on a standalone basis;
- the pricing of standalone sales that may not qualify as VSOE of fair value due to limited volumes or variation in prices; and
- other pricing factors, such as the geographical region in which the products are sold and expected discounts based on the customer size and type.

In determining a BESP for Implied Maintenance Release PCS, which the Company does not sell separately, the Company considers (i) the service period for the Implied Maintenance Release PCS, (ii) the differential in value of the Implied Maintenance Release PCS deliverable compared to a full support contract, (iii) the likely list price that would have resulted from the Company’s established pricing practices had the deliverable been offered separately and (iv) the prices a customer would likely be willing to pay.

The Company estimates the service period of Implied Maintenance Release PCS based on the length of time the product version purchased by the customer is planned to be supported with Software Updates. If facts and circumstances indicate that the original service period of Implied Maintenance Release PCS for a product has changed significantly after original revenue recognition has commenced, the Company will modify the remaining estimated service period accordingly and recognize the then-remaining deferred revenue balance over the revised service period.

The Company has established VSOE of fair value for some of the Company’s professional services, training and support offerings. The Company’s policy for establishing VSOE of fair value consists of evaluating standalone sales to determine if a substantial portion of the transactions fall within a reasonable range. If a sufficient volume of standalone sales exist and the standalone pricing for a substantial portion of the transactions falls within a reasonable range, management concludes that VSOE of fair value exists.

In accordance with Accounting Standards Update (“ASU”) No. 2009-14, the Company excludes from the scope of software revenue recognition requirements the Company’s sales of tangible products that contain both software and non-software components that function together to deliver the essential functionality of the tangible products. The Company adopted ASU No. 2009-13 and ASU No. 2009-14 prospectively on January 1, 2011 for new and materially modified arrangements originating after December 31, 2010.

Prior to the Company’s adoption of ASU No. 2009-14, the Company primarily recognized revenues using the revenue recognition criteria of Accounting Standards Codification (“ASC”) Subtopic 985-605, Software-Revenue Recognition. As a result of the Company’s adoption of ASU No. 2009-14 on January 1, 2011, a majority of the Company’s products are now considered non-software elements under U.S. GAAP, which excludes them from the scope of ASC Subtopic 985-605 and includes them within the scope of ASC Topic 605, Revenue Recognition. Because the Company had not been able to establish VSOE of fair value for Implied Maintenance Release PCS, as described further below, substantially all revenue arrangements prior to January 1, 2011 were recognized on a ratable basis over the service period of Implied Maintenance Release PCS. Subsequent to January 1, 2011 and the adoption of ASU No. 2009-14, the Company determines a relative selling price for all elements of the arrangement through the use of BESP, as VSOE and TPE are typically not available, resulting in revenue recognition upon delivery of arrangement consideration attributable to product revenue, provided all other criteria for revenue recognition are met, and revenue recognition of Implied Maintenance Release PCS and other service and support elements over time as services are rendered.

#### Revenue Recognition of Non-Software Deliverables

Revenue from products that are considered non-software deliverables is recognized upon delivery of the product to the customer. Products are considered delivered to the customer once they have been shipped and title and risk of loss has been transferred. For most of the Company’s product sales, these criteria are met at the time the product is shipped. Revenue from support that is considered a non-software deliverable is initially deferred and is recognized ratably over the contractual period of the arrangement, which is generally 12 months. Professional services and training services are typically sold to customers on a time and materials basis. Revenue from professional services and training services that are considered non-software deliverables is recognized for these deliverables as services are provided to the customer. Revenue for Implied Maintenance Release PCS that is considered a non-software deliverable is recognized ratably over the service period of Implied Maintenance Release PCS, which ranges from one to eight years.

#### Revenue Recognition of Software Deliverables

The Company recognizes the following types of elements sold using software revenue recognition guidance: (i) software products and software upgrades, when the software sold in a customer arrangement is more than incidental to the arrangement as a whole and the product does not contain hardware that functions with the software to provide essential functionality, (ii) initial support contracts where the underlying product being supported is considered to be a software deliverable, (iii) support contract renewals and (iv) professional services and training that relate to deliverables considered to be software deliverables. Because the Company does not have VSOE of the fair value of its software products, the Company is permitted to account for its typical customer arrangements that include multiple elements using the residual method. Under the residual method, the VSOE of fair value of the undelivered elements (which could include support, professional services or training, or any combination thereof) is deferred and the remaining portion of the total arrangement fee is recognized as revenue for the delivered elements. If evidence of the VSOE of fair value of one or more undelivered elements does not exist, revenues are deferred and recognized when delivery of those elements occurs or when VSOE of fair value can be established. VSOE of fair value is typically based on the price charged when the element is sold separately to customers. The Company is unable to use the residual method to recognize revenues for some arrangements that include products that are software deliverables under U.S. GAAP since VSOE of fair value does not exist for Implied Maintenance Release PCS elements, which are included in some of the Company’s arrangements.

For software products that include Implied Maintenance Release PCS, an element for which VSOE of fair value does not exist, revenue for the entire arrangement fee, which could include combinations of product, professional services, training and support, is recognized ratably as a group over the longest service period of any deliverable in the arrangement, with recognition commencing on the date delivery has occurred for all deliverables in the arrangement (or begins to occur in the case of professional services, training and support). Standalone sales of support contracts are recognized ratably over the service period of the product being supported.

From time to time, the Company offers certain customers free upgrades or specified future products or enhancements. When a software deliverable arrangement contains an Implied Maintenance Release PCS deliverable, revenue recognition of the entire arrangement will only commence when any free upgrades or specified future products or enhancements have been delivered, assuming all other products in the arrangement have been delivered and all services, if any, have commenced.

### ***Recently Adopted Accounting Pronouncement***

In January 2017, the FASB issued Accounting Standards Update (ASU) No. 2017-04, *Simplifying the Test for Goodwill Impairment*. The guidance simplifies the accounting for goodwill impairment by removing Step 2 of the goodwill impairment test, which requires a hypothetical purchase price allocation. Goodwill impairment will now be the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. The revised guidance will be applied prospectively, and is effective for calendar year-end SEC filers in 2020. Early adoption is permitted for annual and interim goodwill impairment testing dates after January 1, 2017. The Company adopted the revised guidance during the first quarter of 2017. The adoption of ASU 2017-04 had no immediate impact on the Company's condensed consolidated financial statements upon adoption, however, it could impact the calculation of goodwill impairments in future periods.

### ***Recent Accounting Pronouncements to be Adopted***

In May, 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*. ASU No. 2014-09 is the final updated standard on revenue recognition. The standard supersedes the most current revenue recognition guidance, including industry-specific guidance. The new revenue recognition guidance becomes effective for the Company on January 1, 2018, and early adoption as of January 1, 2017 is permitted.

Subsequently, the FASB has issued the following standards related to ASU No. 2014-09: ASU No. 2016-08, *Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations*; ASU No. 2016-10, *Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing*; and ASU No. 2016-12, *Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients*. The Company must adopt ASU No. 2016-08, ASU No. 2016-10 and ASU No. 2016-12 with ASU No. 2014-09 (collectively, the "new revenue standards").

Entities have the option of using either a full retrospective or a modified approach to adopt the new revenue standards. The Company expects to elect the modified transition method and, while the Company is still in the process of evaluating the impact of this new accounting standard, it expects the impact will be significant. The adoption will result in a significant cumulative reduction in deferred revenue as of January 1, 2018 because the Company will no longer require VSOE of fair value to recognize software deliverables with Implied Maintenance Release PCS upon delivery. Upon adoption of ASC 606, the Company expects to recognize a greater proportion of revenue upon delivery of its products, whereas some of the Company's current product sales are initially recorded in deferred revenue and recognized over a long period of time (as described in detail in the "Significant Accounting Policies - Revenue Recognition" section above). Accordingly, the Company's operating results may become more volatile as a result of the adoption.

On February 25, 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*. The guidance requires an entity to recognize virtually all of their leases on the balance sheet, by recording a right-of-use asset and lease liability. The new guidance becomes effective for the Company on January 1, 2019, and early adoption is permitted upon issuance. The Company is evaluating the potential impact of adopting this standard on its financial statements, as well as the timing of its adoption of the standard.

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flow (Topic 230)*. The guidance reduces diversity in how certain cash receipts and cash payments are presented and classified in the Statements of Cash Flows. Certain of ASU No. 2016-15 requirements are as follows: (i) cash payments for debt prepayment or debt extinguishment costs should be classified as cash outflows for financing activities, (ii) contingent consideration payments made soon after a business combination should be classified as cash outflows for investing activities and cash payment made thereafter should be classified as cash outflows for financing up to the amount of the contingent consideration liability recognized at the

acquisition date with any excess classified as operating activities, (iii) cash proceeds from the settlement of insurance claims should be classified on the basis of the nature of the loss, (iv) cash proceeds from the settlement of Corporate-Owned Life Insurance (“COLI”) Policies should be classified as cash inflows from investing activities and cash payments for premiums on COLI policies may be classified as cash outflows for investing activities, operating activities, or a combination of investing and operating activities and (v) cash paid to a tax authority by an employer when withholding shares from an employee's award for tax-withholding purposes should be classified as cash outflows for financing activities. The new guidance becomes effective for the Company on January 1, 2018, and early adoption is permitted upon issuance. The Company is currently evaluating the potential impact of adopting this standard on its financial statements, as well as the timing of its adoption of the standard.

In October 2016, the FASB issued ASU No. 2016-16, *Income Taxes (Topic 740)*. The guidance requires companies to recognize the income tax effects of intercompany sales and transfers of assets, other than inventory, in the income statement as income tax expense (or benefit) in the period in which the transfer occurs. The new guidance becomes effective for the Company on January 1, 2018, and early adoption is permitted upon issuance. The Company is currently evaluating the impact of the adoption of ASU No. 2016-16 on its financial statements, as well as timing of its adoption of the standard.

In November 2016, the FASB issued ASU No. 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash*. The guidance requires companies to show the changes in the total of cash, cash equivalents, restricted cash and restricted cash equivalents in the statement of cash flows. As a result, companies will no longer present transfers between cash and cash equivalents and restricted cash and restricted cash equivalents in the statement of cash flows. When cash, cash equivalents, restricted cash and restricted cash equivalents are presented in more than one line item on the balance sheet, a reconciliation of the totals in the statement of cash flows to the related captions in the balance sheet is required. The new guidance becomes effective for the Company on January 1, 2018, and early adoption is permitted upon issuance. The Company is currently evaluating the potential impact of adopting this standard on its financial statements, as well as the timing of its adoption of the standard.

## 2. NET INCOME PER SHARE

Net income per common share is presented for both basic income per share (“Basic EPS”) and diluted income per share (“Diluted EPS”). Basic EPS is based on the weighted-average number of common shares outstanding during the period. Diluted EPS is based on the weighted-average number of common shares and common share equivalents outstanding during the period.

The potential common shares that were considered anti-dilutive securities were excluded from the diluted earnings per share calculations for the relevant periods either because the sum of the exercise price per share and the unrecognized compensation cost per share was greater than the average market price of the Company’s common stock for the relevant period, or because they were considered contingently issuable. The contingently issuable potential common shares result from certain stock options and restricted stock units granted to the Company’s employees that vest based on performance conditions, market conditions, or a combination of performance and market conditions.

The following table sets forth (in thousands) potential common shares that were considered anti-dilutive securities at September 30, 2017 and for the nine months ended September 30, 2016.

	September 30, 2017	September 30, 2016
Options	2,334	3,939
Non-vested restricted stock units	3,289	687
Anti-dilutive potential common shares	5,623	4,626

On June 15, 2015, the Company issued \$125.0 million aggregate principal amount of its 2.00% Convertible Senior Notes due 2020 (the “Notes”). The Notes are convertible into cash, shares of the Company’s common stock or a combination of cash and shares of common stock, at the Company’s election, based on an initial conversion rate, subject to adjustment. In connection with the offering of the Notes, the Company entered into a capped call transaction with a third party. The Company uses the treasury stock method in computing the dilutive impact of the Notes. The Notes are convertible into

shares of the Company's common stock but the Company's stock price was less than the conversion price as of September 30, 2017, and, therefore, the Notes are excluded from Diluted EPS. The Capped Call is not reflected in diluted net income per share as it will always be anti-dilutive.

### 3. FAIR VALUE MEASUREMENTS

#### *Assets Measured at Fair Value on a Recurring Basis*

The Company measures deferred compensation investments on a recurring basis. As of September 30, 2017 and December 31, 2016, the Company's deferred compensation investments were classified as either Level 1 or Level 2 in the fair value hierarchy. Assets valued using quoted market prices in active markets and classified as Level 1 are money market and mutual funds. Assets valued based on other observable inputs and classified as Level 2 are insurance contracts.

The following tables summarize the Company's deferred compensation investments measured at fair value on a recurring basis (in thousands):

		Fair Value Measurements at Reporting Date Using		
	September 30, 2017	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial assets:				
Deferred compensation assets	\$ 1.838	\$ 460	\$ 1,378	\$ —

		Fair Value Measurements at Reporting Date Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	December 31, 2016			
Financial assets:				
Deferred compensation assets	\$ 2,035	\$ 493	\$ 1,542	\$ —

#### *Financial Instruments Not Recorded at Fair Value*

The carrying amounts of the Company's other financial assets and liabilities including cash, accounts receivable, accounts payable and accrued liabilities approximate their respective fair values because of the relatively short period of time between their origination and their expected realization or settlement. As of September 30, 2017, the net carrying amount of the Notes was \$106.1 million, and the fair value of the Notes was approximately \$95.1 million based on open market trading activity, which constitutes a Level 1 input in the fair value hierarchy.

### 4. INVENTORIES

Inventories consisted of the following (in thousands):

	September 30, 2017	December 31, 2016
Raw materials	\$ 11,518	\$ 10,481
Work in process	300	291
Finished goods	29,342	39,929
Total	<u>\$ 41,160</u>	<u>\$ 50,701</u>



As of September 30, 2017 and December 31, 2016, finished goods inventory included \$9.5 million and \$8.6 million, respectively, associated with products shipped to customers and deferred labor costs for arrangements where revenue recognition had not yet commenced.

## 5. INTANGIBLE ASSETS AND GOODWILL

Amortizing identifiable intangible assets related to the Company's acquisitions or capitalized costs of internally developed or externally purchased software that form the basis for the Company's products consisted of the following (in thousands):

	September 30, 2017			December 31, 2016		
	Gross	Accumulated Amortization	Net	Gross	Accumulated Amortization	Net
Completed technologies and patents	\$ 58,562	\$ (45,074)	\$ 13,488	\$ 57,994	\$ (38,657)	\$ 19,337
Customer relationships	54,906	(52,399)	2,507	54,597	(51,002)	3,595
Trade names	1,346	(1,346)	—	1,346	(1,346)	—
Capitalized software costs	4,911	(4,911)	—	4,911	(4,911)	—
Total	\$ 119,725	\$ (103,730)	\$ 15,995	\$ 118,848	\$ (95,916)	\$ 22,932

Amortization expense related to all intangible assets in the aggregate was \$2.3 million and \$2.5 million, respectively, for the three months ended September 30, 2017 and 2016, and \$6.9 million and \$8.0 million, respectively, for the nine months ended September 30, 2017 and 2016. The Company expects amortization of acquired intangible assets to be \$2.3 million for the remainder of 2017, \$9.3 million in 2018 and \$4.4 million in 2019.

The acquisition of Orad in 2015 resulted in goodwill of \$32.6 million as of September 30, 2017 and December 31, 2016.

## 6. OTHER LONG-TERM LIABILITIES

Other long-term liabilities consisted of the following (in thousands):

	September 30, 2017	December 31, 2016
Deferred rent	\$ 3,292	\$ 5,458
Accrued restructuring	843	1,256
Deferred compensation	5,591	5,464
Total	\$ 9,726	\$ 12,178

## 7. COMMITMENTS AND CONTINGENCIES

### Commitments

The Company entered into a long-term agreement to purchase a variety of information technology solutions from a third party in the second quarter of 2017, which included an unconditional commitment to purchase a minimum of \$12.8 million of products and services over the initial three-year term of the agreement.

The Company has letters of credit that are used as security deposits in connection with the Company's leased Burlington, Massachusetts office space. In the event of default on the underlying leases, the landlords would, at September 30, 2017, be eligible to draw against the letters of credit to a maximum of \$1.3 million in the aggregate. The letters of credit are subject to aggregate reductions provided the Company is not in default under the underlying leases and meets certain financial performance conditions. In no case will the letters of credit amounts be reduced to below \$1.2 million in the aggregate throughout the lease periods, all of which extend to May 2020.

The Company also has letters of credit in connection with security deposits for other facility leases totaling \$1.1 million in the aggregate, as well as letters of credit totaling \$1.2 million that otherwise support its ongoing operations. These letters

of credit have various terms and expire during 2017 and beyond, while some of the letters of credit may automatically renew based on the terms of the underlying agreements.

### **Contingencies**

The Company's industry is characterized by the existence of a large number of patents and frequent claims and litigation regarding patent and other intellectual property rights. In addition to the legal proceedings described below, the Company is involved in legal proceedings from time to time arising from the normal course of business activities, including claims of alleged infringement of intellectual property rights and contractual, commercial, employee relations, product or service performance, or other matters. The Company does not believe these matters will have a material adverse effect on the Company's financial position or results of operations. However, the outcome of legal proceedings and claims brought against the Company is subject to significant uncertainty. Therefore, the Company's financial position or results of operations may be negatively affected by the unfavorable resolution of one or more of these proceedings for the period in which a matter is resolved. The Company's results could be materially adversely affected if the Company is accused of, or found to be, infringing third parties' intellectual property rights.

On October 30, 2017 the Company entered into settlement and patent cross-licensing agreements with Harmonic Inc. ("Harmonic"), ending its patent infringement litigation against Harmonic which commenced in 2011. Under the terms of the agreements, Harmonic will pay the Company \$6.0 million. The first payment of \$2.5 million was made on October 24, 2017; the remaining \$3.5 million will be paid in two installments of \$1.5 million and \$2.0 million in 2019 and 2020, respectively. The Company will record a gain associated with the settlement of past patent infringements in the fourth quarter of 2017.

In November 2016, a purported securities class action lawsuit was filed in the U.S. District Court for the District of Massachusetts (Mohanty v. Avid Technology, Inc. et al., No. 16-cv-12336) against the Company and certain of its executive officers seeking unspecified damages and other relief on behalf of a purported class of purchasers of the Company's common stock between August 4, 2016 and November 9, 2016, inclusive. The complaint purported to state a claim for violation of federal securities laws as a result of alleged violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 ("the Exchange Act") and Rule 10b-5 promulgated thereunder. The complaint's allegations relate generally to the Company's disclosure surrounding the level of implementation of the Company's Avid NEXIS solution product offerings. On February 7, 2017, the Court appointed a lead plaintiff and counsel in the matter. On June 14, 2017, the Company moved to dismiss the action. On July 31, 2017, the lead plaintiff filed an opposition to the Company's motion to dismiss, and on August 21, 2017, the Company filed its reply brief. On October 13, 2017, after a mediation, the parties reached an agreement in principle to settle this litigation. The Company expects the majority of the settlement to be funded by its insurers. Finalization of the settlement is subject to a number of conditions, including execution of definitive documentation and approval by the court.

The Company considers all claims on a quarterly basis and based on known facts assesses whether potential losses are considered reasonably possible, probable and estimable. Based upon this assessment, the Company then evaluates disclosure requirements and whether to accrue for such claims in its consolidated financial statements. The Company records a provision for a liability when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. These provisions are reviewed at least quarterly and adjusted to reflect the impacts of negotiations, settlements, rulings, advice of legal counsel and other information and events pertaining to a particular case.

At September 30, 2017 and as of the date of filing of these consolidated financial statements, the Company believes that, other than as set forth in this note, no provision for liability nor disclosure is required related to any claims because: (a) there is no reasonable possibility that a loss exceeding amounts already recognized (if any) may be incurred with respect to such claim, (b) a reasonably possible loss or range of loss cannot be estimated; or (c) such estimate is immaterial.

Additionally, the Company provides indemnification to certain customers for losses incurred in connection with intellectual property infringement claims brought by third parties with respect to the Company's products. These indemnification provisions generally offer perpetual coverage for infringement claims based upon the products covered by the agreement and the maximum potential amount of future payments the Company could be required to make under these indemnification provisions is theoretically unlimited. To date, the Company has not incurred material costs related to these indemnification provisions; accordingly, the Company believes the estimated fair value of these indemnification provisions

is immaterial. Further, certain of the Company's arrangements with customers include clauses whereby the Company may be subject to penalties for failure to meet certain performance obligations; however, the Company has not recorded any related material penalties to date.

The Company provides warranties on externally sourced and internally developed hardware. For internally developed hardware, and in cases where the warranty granted to customers for externally sourced hardware is greater than that provided by the manufacturer, the Company records an accrual for the related liability based on historical trends and actual material and labor costs. The following table sets forth the activity in the product warranty accrual account for the nine months ended September 30, 2017 and 2016 (in thousands):

	Nine Months Ended September 30,	
	2017	2016
Accrual balance at beginning of year	\$ 2,518	\$ 2,234
Accruals for product warranties	1,872	1,992
Costs of warranty claims	(1,897)	(1,872)
Accrual balance at end of period	<u>\$ 2,493</u>	<u>\$ 2,354</u>

The warranty accrual is included in the caption "accrued expenses and other current liabilities" in the Company's condensed consolidated balance sheet.

## 8. RESTRUCTURING COSTS AND ACCRUALS

In February 2016, the Company committed to a restructuring plan that encompassed a series of measures intended to allow the Company to more efficiently operate in a leaner, more directed cost structure. These included reductions in the Company's workforce, consolidation of facilities, transfers of certain business processes to lower cost regions, and reductions in other third-party services costs. The cost efficiency program was substantially complete as of June 30, 2017.

During the three and nine months ended September 30, 2017, the Company recorded recoveries of \$0.6 million and restructuring charges of \$6.5 million, respectively. The restructuring charges for the nine months ended September 30, 2017 included \$1.0 million for the severance costs and estimate adjustments related to approximately 64 terminated employees and \$5.4 million for the closure of certain excess facility space, including \$3.2 million of leasehold improvement write-offs and \$0.8 million adjustments related to sublease assumptions associated with prior abandoned facilities.

During the three and nine months ended September 30, 2016, the Company recorded restructuring charges of \$5.3 million and restructuring charges of \$7.9 million, respectively. During the nine months ended September 30, 2016, the Company recorded restructuring charges of \$5.0 million for the severance costs and estimate adjustments related to approximately 123 terminated employees and \$2.9 million for the closure of certain excess facility space, including \$1.1 million of leasehold improvement write-offs, and \$0.8 million adjustments related to sublease assumptions associated with prior abandoned facilities.

## Restructuring Summary

The following table sets forth the activity in the restructuring accruals for the nine months ended September 30, 2017 (in thousands):

	Employee-Related	Facilities/Other-Related	Total
Accrual balance as of December 31, 2016	\$ 7,018	\$ 3,093	\$ 10,111
New restructuring charges – operating expenses	1,930	1,485	3,415
Revisions of estimated liabilities	(902)	760	(142)
Non-cash write-offs	—	3,191	3,191
Accretion	—	278	278
Cash payments	(5,479)	(2,970)	(8,449)
Foreign exchange impact on ending balance	(46)	15	(31)
Accrual balance as of September 30, 2017	<u>\$ 2,521</u>	<u>\$ 5,852</u>	<u>\$ 8,373</u>

The employee-related accruals at September 30, 2017 represent severance costs to former employees that will be paid out within 12 months, and are, therefore, included in the caption “accrued expenses and other current liabilities” in the Company’s consolidated balance sheets.

The facilities/other-related accruals at September 30, 2017 represent contractual lease payments, net of estimated sublease income, on space vacated as part of the Company’s restructuring actions. The leases, and payments against the amounts accrued, extend through December 2021 unless the Company is able to negotiate earlier terminations. Of the total facilities/other-related balance, \$1.9 million is included in the caption “accrued expenses and other current liabilities”, \$0.8 million is included in the caption “other long-term liabilities”, and \$3.2 million of fixed asset write-off is reflected in the caption “property and equipment, net” in the Company’s condensed consolidated balance sheet as of September 30, 2017.

## 9. PRODUCT AND GEOGRAPHIC INFORMATION

The Company, through the evaluation of the discrete financial information that is regularly reviewed by the chief operating decision makers (the Company’s chief executive officer and chief financial officer), has determined that the Company has one reportable segment. The following table is a summary of the Company’s revenues by type for the three and nine months ended September 30, 2017 and 2016 (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Video products and solutions net revenues	\$ 27,058	\$ 39,182	\$ 82,585	\$ 118,252
Audio products and solutions net revenues	27,261	24,558	70,395	105,589
Products and solutions net revenues	54,319	63,740	152,980	223,841
Services net revenues	50,946	55,279	158,765	172,794
Total net revenues	<u>\$ 105,265</u>	<u>\$ 119,019</u>	<u>\$ 311,745</u>	<u>\$ 396,635</u>

The following table sets forth the Company's revenues by geographic region for the three and nine months ended September 30, 2017 and 2016 (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
<b>Revenues:</b>				
United States	\$ 38,624	\$ 45,982	\$ 121,309	\$ 145,384
Other Americas	7,377	9,702	20,581	30,674
Europe, Middle East and Africa	41,526	44,524	121,647	159,243
Asia-Pacific	17,738	18,811	48,208	61,334
Total net revenues	<u>\$ 105,265</u>	<u>\$ 119,019</u>	<u>\$ 311,745</u>	<u>\$ 396,635</u>

## 10. LONG-TERM DEBT AND CREDIT AGREEMENT

Long-term debt consisted of the following (in thousands):

	September 30, 2017	December 31, 2016
Term Loan, net of unamortized debt issuance costs of \$3,144 at September 30, 2017 and \$4,042 at December 31, 2016	\$ 89,356	\$ 92,208
Notes, net of unamortized original issue discount and debt issuance costs of \$18,896 at September 30, 2017 and \$23,413 at December 31, 2016, respectively	106,104	101,587
Other long-term debt	912	—
Total debt	196,372	193,795
Less: current portion	5,072	5,000
Total long-term debt	<u>\$ 191,300</u>	<u>\$ 188,795</u>

### 2.00% Convertible Senior Notes due 2020

On June 15, 2015, the Company issued \$125.0 million aggregate principal amount of its Notes in an offering conducted in accordance with Rule 144A under the Securities Act of 1933. The Notes pay interest semi-annually on June 15 and December 15 of each year at an annual rate of 2.00% and mature on June 15, 2020, unless earlier converted or repurchased in accordance with their terms prior to such date. Total interest expense for the nine months ended September 30, 2017 and 2016 was \$6.4 million and \$6.1 million, respectively, reflecting the coupon and accretion of the discount.

### Credit Facility

On February 26, 2016, the Company entered into the Financing Agreement with the Lenders. Pursuant to the Financing Agreement, the Lenders originally agreed to provide the Company with (a) a term loan in the aggregate principal amount of \$100.0 million (the "Term Loan") and (b) a revolving credit facility (the "Credit Facility") of up to a maximum of \$5.0 million in borrowings outstanding at any time. All outstanding loans under the Financing Agreement will become due and payable on the earlier of February 26, 2021 and the date that is 30 days prior to June 15, 2020 if the \$125.0 million in outstanding principal of the Notes has not been repaid or refinanced by such time. The Company granted a security interest on substantially all of its assets to secure the obligations under the Credit Facility and the Term Loan. The Company borrowed the full amount of the Term Loan, or \$100.0 million, as of the closing date of the Financing Agreement, and there were no amounts outstanding under the Credit Facility as of September 30, 2017.

The Company may prepay all or any portion of the Term Loan prior to its stated maturity, subject to the payment of certain fees based on the amount repaid. The Term Loan requires quarterly principal payments of \$1.25 million, which commenced in June 2016. The Term Loan also requires the Company to use 50% of excess cash flow, as defined in the Financing Agreement, to repay outstanding principal of the loans under the Financing Agreement.

The Financing Agreement contains customary representations and warranties, covenants, mandatory prepayments, and events of default under which the Company's payment obligations may be accelerated. On March 14, 2017 (the "Amendment No. 1 Effective Date"), the Company entered into an amendment (the "First Amendment") to the Financing Agreement. The First Amendment modified the covenant requiring the Company to maintain a Leverage Ratio (defined to mean the ratio of (a) total funded indebtedness to (b) consolidated EBITDA) such that following the Amendment No. 1 Effective Date, the Company is required to maintain a Leverage Ratio of no greater than 3.50:1.00 for the four quarters ended March 31, 2017, 4.20:1.00 for the four quarters ended June 30, 2017, 4.75:1.00 for the four quarters ended September 30, 2017, 4.80:1.00 for the four quarters ending December 31, 2017, 4.40:1.00 for each of the four quarters ending March 31, 2018 through March 31, 2019, respectively, and thereafter declining over time from 3.50:1.00 to 2.50:1.00. Following the Amendment No. 1 Effective Date, interest accrues on outstanding borrowings under the credit facility and the term loan (each as defined in the Financing Agreement) at a rate of either the LIBOR Rate (as defined in the Financing Agreement) plus 7.25% or a Reference Rate (as defined in the Financing Agreement) plus 6.25%, at the option of the Company. The Company recorded \$5.9 million and \$4.6 million of interest expense on the Term Loan for the nine months ended September 30, 2017 and 2016, respectively. As of September 30, 2017, the Company was in compliance with the Financing Agreement covenants.

On November 9, 2017 (the "Amendment No. 2 Effective Date"), the Company entered into an amendment (the "Second Amendment") to the Financing Agreement. The Second Amendment extended an additional \$15.0 million term loan to the Company, thereby increasing the aggregate principal amount of the term loan to \$115.0 million. The Second Amendment also increased the amount of available revolving credit by \$5.0 million to an aggregate amount of \$10.0 million. The additional \$15.0 million term loan must be repaid in quarterly principal payments of \$187,500 commencing in March 2018. The Second Amendment also granted the Company the ability to use up to \$15.0 million to purchase Notes and modified the definition of consolidated EBITDA used in the Leverage Ratio calculation to adjust for expected changes in deferred revenue due to the adoption of ASC 606.

## 11. STOCKHOLDERS' EQUITY

### *Stock-Based Compensation*

Information with respect to option shares granted under all the Company's stock incentive plans for the nine months ended September 30, 2017 was as follows:

	Time-Based Shares	Performance-Based Shares	Total Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (years)	Aggregate Intrinsic Value (in thousands)
Options outstanding at January 1, 2017	2,847,502	—	2,847,502	\$10.43		
Granted	—	—	—	\$—		
Exercised	—	—	—	\$—		
Forfeited or canceled	(513,285)	—	(513,285)	\$13.49		
Options outstanding at September 30, 2017	2,334,217	—	2,334,217	\$9.75	2.51	\$—
Options vested at September 30, 2017 or expected to vest			2,334,217	\$9.75	2.51	\$—
Options exercisable at September 30, 2017			2,315,467	\$9.77	2.51	\$—

Information with respect to the Company's non-vested restricted stock units for the nine months ended September 30, 2017 was as follows:

	Non-Vested Restricted Stock Units					
	Time-Based Shares	Performance-Based Shares	Total Shares	Weighted-Average Grant-Date Fair Value	Weighted-Average Remaining Contractual Term (years)	Aggregate Intrinsic Value (in thousands)
Non-vested at January 1, 2017	1,513,098	642,683	2,155,781	\$6.85		
Granted	1,130,596	639,703	1,770,299	\$4.61		
Vested	(538,384)	—	(538,384)	\$7.84		
Forfeited	(70,142)	(28,276)	(98,418)	\$6.17		
Non-vested at September 30, 2017	2,035,168	1,254,110	3,289,278	\$5.16	0.86	\$14,900
Expected to vest			2,674,871	\$5.08	0.86	\$12,117

Stock-based compensation was included in the following captions in the Company's condensed consolidated statements of operations for the three and nine months ended September 30, 2017 and 2016 (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Cost of products revenues	\$ 14	\$ 12	\$ 39	\$ 43
Cost of services revenues	49	145	508	445
Research and development expenses	222	73	474	222
Marketing and selling expenses	582	547	1,375	1,508
General and administrative expenses	1,614	951	3,478	3,898
	<u>\$ 2,481</u>	<u>\$ 1,728</u>	<u>\$ 5,874</u>	<u>\$ 6,116</u>

## ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

### EXECUTIVE OVERVIEW

#### *Business Overview*

We develop, market, sell, and support software and hardware for digital media content production, management and distribution. We do this by providing an open and efficient platform for digital media, along with a comprehensive set of tools and workflow solutions, that enable the creation, distribution and optimization of audio and video content. Digital media are video, audio or graphic elements in which the image, sound or picture is recorded and stored as digital values, as opposed to analog or tape-based signals. Our products are used in production and post-production facilities; film studios; network, affiliate, independent and cable television stations; recording studios; live-sound performance venues; advertising agencies; government and educational institutions; corporate communications departments; and by independent video and audio creative professionals, as well as aspiring professionals. Projects produced using our products include feature films, television programming, live events, news broadcasts, sports productions, commercials, music, video and other digital media content.

Our mission is to create the most powerful and collaborative media network that enables the creation, distribution and monetization of the most inspiring content in the world. Guided by our Avid Everywhere strategic vision, we strive to deliver the industry’s most open, tightly integrated and efficient platform for media, connecting content creation with collaboration, asset protection, distribution and consumption of media in the world - from the most prestigious and award-winning feature films, music recordings, and television shows, to live concerts, sporting events and news broadcasts. We have been honored over time for our technological innovation with 15 Emmy Awards, one Grammy Award, two Oscars and the first ever America Cinema Editors Technical Excellence Award. Our solutions were used in all 2017 Oscar nominated films for Best Picture, Best Film Editing and Best Original Song. Every 2017 Grammy nominee for Record of the Year and Album of The Year relied on our music creation solutions powered by our MediaCentral Platform.

#### *Operations Overview*

Our strategy is built on three pillars, Avid Everywhere, The Avid Advantage and the Avid Customer Association, (“ACA”). Avid Everywhere is our strategic vision for connecting creative professionals and media organizations with their audiences in a more powerful, efficient, collaborative, and profitable way. Central to the Avid Everywhere vision is the Avid MediaCentral Platform, an open, extensible, and customizable foundation that streamlines and simplifies workflows by integrating all Avid or third party products and services that run on top of it. The platform provides secure and protected access, which enables the creation and delivery of content faster and easier through a set of modular application suites and new public and private marketplaces, that together, represent an open, integrated and flexible production and distribution environment for the media industry. The Avid Advantage complements Avid Everywhere by offering a new standard in service, support and education to enable our customers to derive more efficiency from their Avid investment. Finally, the ACA is an association of dedicated media community visionaries, thought leaders and users designed to provide essential strategic leadership to the media industry, facilitate collaboration between Avid and key industry leaders and visionaries, and strengthen relationships between our customers and us. This preeminent client and user community helps shape our collective future.

Another key element of our strategy is our transition to a subscription or recurring revenue based model. We started offering cloud-based subscription licensing options for some of our products and solutions in 2014, and had more than 84,000 paying cloud-enabled subscribers in the third quarter of 2017, a 69% increase from the third quarter of 2016. These licensing options offer choice in pricing and deployment to suit our customers’ needs and are expected to increase recurring revenue on a longer term basis. However, during our transition to a recurring revenue model, we expect that our revenue, deferred revenue, and cash flow from operations will be adversely affected as an increasing portion of our total revenue is recognized ratably rather than up front, and as new product offerings are sold at a wider variety of price points.

In April 2017, we entered into a strategic alliance agreement with Microsoft Corporation to develop and market cloud-based solutions and cloud services aimed at the media and entertainment industry. As part of the agreement, we have chosen Microsoft Azure as our preferred cloud hosting platform, and will develop and launch a range of Software-as-a-Service (“SaaS”) and Platform-as-a-Service (PaaS) offerings powered by the Avid MediaCentral Platform.

As a complement to our core strategy, we continue to review and implement programs throughout the Company to reduce costs, increase operational efficiencies, align talent and enhance our business, including the cost efficiency program announced in



February 2016. The cost efficiency program encompassed a series of measures intended to allow us to more efficiently operate in a leaner, more directed cost structure. These measures included reductions in our workforce, consolidation of facilities, transfers of certain business processes to lower cost regions and reductions in other third-party services costs. The cost efficiency program was substantially complete as of June 30, 2017.

## **CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

Our condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosures of contingent assets and liabilities as of the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. We base our estimates and judgments on historical experience and various other factors we believe to be reasonable under the circumstances, the results of which form the basis for judgments about the carrying values of assets and liabilities and the amounts of revenues and expenses. Actual results may differ from these estimates.

We believe that our critical accounting policies and estimates are those related to revenue recognition and allowances for sales returns and exchanges; stock-based compensation; income tax assets and liabilities; and restructuring charges and accruals. We believe these policies and estimates are critical because they most significantly affect the portrayal of our financial condition and results of operations and involve our most complex and subjective estimates and judgments. A discussion of our critical accounting policies and estimates may be found in our Annual Report on Form 10-K for the year ended December 31, 2016 in Item 7, “Management's Discussion and Analysis of Financial Condition and Results of Operations,” under the heading “Critical Accounting Policies and Estimates” and below. There have been no significant changes to the identification of the accounting policies and estimates that are deemed critical, nor have there been any significant changes to the policies applied or methodologies used by management to measure the critical accounting estimates.

### ***Revenue Recognition***

#### **General**

We commence revenue recognition when persuasive evidence of an arrangement exists, delivery has occurred, the sales price is fixed or determinable and collection is reasonably assured. Generally, the products we sell do not require significant production, modification or customization. Installation of our products is generally routine, consists of implementation and configuration and does not have to be performed by us.

At the time of a sales transaction, we make an assessment of the collectability of the amount due from the customer. Revenues are recognized only if it is reasonably assured that collection will occur. When making this assessment, we consider customer credit-worthiness and historical payment experience. If it is determined from the outset of the arrangement that collection is not reasonably assured, revenues are recognized on a cash basis, provided that all other revenue recognition criteria are satisfied. At the outset of the arrangement, we also assess whether the fee associated with the order is fixed or determinable and free of contingencies or significant uncertainties. When assessing whether the fee is fixed or determinable, we consider the payment terms of the transaction, our collection experience in similar transactions without making concessions and our involvement, if any, in third-party financing transactions, among other factors. If the fee is not fixed or determinable, revenues are recognized only as payments become due from the customer, provided that all other revenue recognition criteria are met. If a significant portion of the fee is due after our normal payment terms, we evaluate whether we have sufficient history of successfully collecting past transactions with similar terms without offering concessions. If that collection history is sufficient, revenue recognition commences, upon delivery of the products, assuming all other revenue recognition criteria are satisfied. If we were to make different judgments or assumptions about any of these matters, it could cause a material increase or decrease in the amount of revenues reported in a particular period.

We often receive multiple purchase orders or contracts from a single customer or a group of related customers that are evaluated to determine if they are, in effect, part of a single arrangement. In situations when we have concluded that two or more orders with the same customer are so closely related that they are, in effect, parts of a single arrangement, we account for those orders as a single arrangement for revenue recognition purposes. In other circumstances, when we have concluded that two or more orders with the same customer are independent buying decisions, such as an earlier purchase of a product and a subsequent purchase of a software upgrade or maintenance contract, we account for those orders as separate arrangements for revenue recognition purposes.

For many of our products, we have had an ongoing practice of making available, at no charge to customers, minor feature and compatibility enhancements as well as bug fixes on a when-and-if-available basis (collectively the “Software Updates”) for a period of time after initial sales to end users. The implicit obligation to make such Software Updates available to customers over a period of time represents implied post-contract customer support, which is deemed to be a deliverable in each arrangement and is accounted for as a separate element, or Implied Maintenance Release PCS.

Over the last two years, in connection with a strategic initiative to increase support and other recurring revenue streams, we have taken a number of steps to eliminate the longstanding practice of providing Implied Maintenance Release PCS for many of our products, including our Media Composer, Pro Tools and Sibelius product lines. In the third quarter and fourth quarter of 2015, respectively, we concluded that Implied Maintenance Release PCS for our Media Composer and Sibelius product lines had ceased. In the first quarter of 2016, in connection with the release of Cloud Collaboration in Pro Tools version 12.5, which was an undelivered feature that had prevented us from recognizing any revenue related to new Pro Tools 12 software sales as it represented a specified upgrade right for which vendor specific objective evidence or (“VSOE”) of fair value was not available, we concluded that Implied Maintenance Release PCS for our Pro Tools 12 product lines had also ended. As a result of the conclusion that Implied Maintenance Release PCS on Pro Tools 12 has ended, revenue and net income in the first quarter of 2016 increased approximately \$11.1 million, reflecting the recognition of orders received after the launch of Pro Tools 12 that would have qualified for earlier recognition using the residual method of accounting. In addition, the elimination of Implied Maintenance Release PCS also resulted in the accelerated recognition of maintenance and product revenues that were previously being recognized on a ratable basis over a much longer expected period of Implied Maintenance Release PCS rather than the contractual maintenance period. The reduction in the estimated amortization period of transactions being recognized on a ratable basis resulted in an additional \$12.0 million and \$33.7 million of revenue during the three and nine months ended September 30, 2016, respectively.

Management will continue to evaluate the judgment of whether Implied Maintenance Release PCS exists on each product line and version. Since the remaining products that contain Implied Maintenance Release PCS largely consist of products that fall under the non-software revenue recognition guidance, where management defers a small portion of revenue based on the best estimated selling price of Implied Maintenance Release PCS rather than the entire order value as required for transactions that fall under software revenue recognition guidance, any further determinations that Implied Maintenance Release PCS no longer exists for other product lines will be unlikely to result in a significant impact to the financial statements in any future periods.

As a result of the conclusion that Implied Maintenance Release PCS no longer exists for Pro Tools 12, prospective revenue recognition on new product orders will be recognized upfront, assuming all other revenue recognition criteria are met and VSOE of fair value exists for all undelivered elements. The cessation of Implied Maintenance Release PCS for Pro Tools and other products subject to software revenue recognition guidance, in addition to the initial impact of immediately recognizing revenue related to orders that would have qualified for earlier recognition using the residual method of accounting, resulted in increased revenue throughout 2016 as the elimination of Implied Maintenance Release PCS also results in the accelerated recognition of preexisting maintenance and product revenues that still do not qualify for the residual method of accounting but are now being recognized on an accelerated basis over a shorter remaining contractual maintenance period as compared to (i) the previous model of being recognized over a longer expected period of Implied Maintenance Release PCS and (ii) the prospective model of recognizing revenue ratably over a longer original contractual maintenance support period. As a result of the compressed recognition period for these prior transactions and longer recognition of the respective renewals, we expect significant decreases in revenues related to impacted product lines in 2017 as recognition from old contracts is completed and new contracts are recognized over a traditional maintenance period.

We enter into certain contractual arrangements that have multiple elements, one or more of which may be delivered subsequent to the delivery of other elements. These multiple-deliverable arrangements may include products, support, training, professional services and Implied Maintenance Release PCS. For these multiple-element arrangements, we allocate revenue to each deliverable of the arrangement based on the relative selling prices of the deliverables. In such circumstances, we first determine the selling price of each deliverable based on (i) VSOE of fair value if that exists, (ii) third-party evidence of selling price, or TPE, when VSOE does not exist; or (iii) best estimate of the selling price or (“BESP”) when neither VSOE nor TPE exists. Revenue is then allocated to the non-software deliverables as a group and to the software deliverables as a group using the relative selling prices of each of the deliverables in the arrangement based on the selling price hierarchy. Our process for determining BESP for deliverables for which VSOE or TPE does not exist involves significant management judgment. In determining BESP, we consider a number of data points, including:

- the pricing established by management when setting prices for deliverables that are intended to be sold on a standalone basis;

- contractually stated prices for deliverables that are intended to be sold on a standalone basis;
- the pricing of standalone sales that may not qualify as VSOE of fair value due to limited volumes or variation in prices; and
- other pricing factors, such as the geographical region in which the products are sold and expected discounts based on the customer size and type.

In determining a BESP for Implied Maintenance Release PCS, which we do not sell separately, we consider (i) the service period for the Implied Maintenance Release PCS, (ii) the differential in value of the Implied Maintenance Release PCS deliverable compared to a full support contract, (iii) the likely list price that would have resulted from our established pricing practices had the deliverable been offered separately and (iv) the prices a customer would likely be willing to pay.

We estimate the service period of Implied Maintenance Release PCS based on the length of time the product version purchased by the customer is planned to be supported with Software Updates. If facts and circumstances indicate that the original service period of Implied Maintenance Release PCS for a product has changed significantly after original revenue recognition has commenced, we will modify the remaining estimated service period accordingly and recognize the then-remaining deferred revenue balance over the revised service period.

We have established VSOE of fair value for all professional services and training and for some of our support offerings. Our policy for establishing VSOE of fair value consists of evaluating standalone sales to determine if a substantial portion of the transactions fall within a reasonable range. If a sufficient volume of standalone sales exist and the standalone pricing for a substantial portion of the transactions falls within a reasonable range, management concludes that VSOE of fair value exists.

In accordance with Accounting Standards Update, or ASU, No. 2009-14, we exclude from the scope of software revenue recognition requirements our sales of tangible products that contain both software and non-software components that function together to deliver the essential functionality of the tangible products. We adopted ASU No. 2009-13 and ASU No. 2009-14 prospectively on January 1, 2011 for new and materially modified arrangements originating after December 31, 2010.

Prior to our adoption of ASU No. 2009-14, we primarily recognized revenues using the revenue recognition criteria of Accounting Standards Codification, or ASC, Subtopic 985-605, *Software-Revenue Recognition*. As a result of our adoption of ASU No. 2009-14 on January 1, 2011, a majority of our products are now considered non-software elements under U.S. GAAP, which excludes them from the scope of ASC Subtopic 985-605 and includes them within the scope of ASC Topic 605, *Revenue Recognition*. Because we had not been able to establish VSOE of fair value for Implied Maintenance Release PCS, as described further below, substantially all revenue arrangements prior to January 1, 2011 were recognized on a ratable basis over the service period of Implied Maintenance Release PCS. Subsequent to January 1, 2011 and the adoption of ASU No. 2009-14, we determine a relative selling price for all elements of the arrangement through the use of BESP, as VSOE and TPE are typically not available, resulting in revenue recognition upon delivery of arrangement consideration attributable to product revenue, provided all other criteria for revenue recognition are met, and revenue recognition of Implied Maintenance Release PCS and other service and support elements over time as services are rendered.

The timing of revenue recognition of customer arrangements follows a number of different accounting models determined by the characteristics of the arrangement, and that timing can vary significantly from the timing of related cash payments due from customers. One significant factor affecting the timing of revenue recognition is the determination of whether each deliverable in the arrangement is considered to be a software deliverable or a non-software deliverable. For transactions occurring after January 1, 2011, our revenue recognition policies have generally resulted in the recognition of approximately 70% of billings as revenue in the year of billing, and prior to January 1, 2011, the previously applied revenue recognition policies resulted in the recognition of approximately 30% of billings as revenue in the year of billing. We expect this trend to continue in future periods.

#### Revenue Recognition of Non-Software Deliverables

Revenue from products that are considered non-software deliverables is recognized upon delivery of the product to the customer. Products are considered delivered to the customer once they have been shipped and title and risk of loss has been transferred. For most of our product sales, these criteria are met at the time the product is shipped. Revenue from support that is considered a non-software deliverable is initially deferred and is recognized ratably over the contractual period of the arrangement, which is generally 12 months. Professional services and training services are typically sold to customers on a time and materials basis. Revenue from professional services and training services that are considered non-software deliverables is recognized for these deliverables as services are provided to the customer. Revenue for Implied Maintenance Release PCS that is considered a non-

software deliverable is recognized ratably over the service period of Implied Maintenance Release PCS, which ranges from one to eight years.

#### Revenue Recognition of Software Deliverables

We recognize the following types of elements sold using software revenue recognition guidance: (i) software products and software upgrades, when the software sold in a customer arrangement is more than incidental to the arrangement as a whole and the product does not contain hardware that functions with the software to provide essential functionality, (ii) initial support contracts where the underlying product being supported is considered to be a software deliverable, (iii) support contract renewals and (iv) professional services and training that relate to deliverables considered to be software deliverables. Because we do not have VSOE of the fair value of our software products, we are permitted to account for our typical customer arrangements that include multiple elements using the residual method. Under the residual method, the VSOE of fair value of the undelivered elements (which could include support, professional services or training, or any combination thereof) is deferred and the remaining portion of the total arrangement fee is recognized as revenue for the delivered elements. If evidence of the VSOE of fair value of one or more undelivered elements does not exist, revenues are deferred and recognized when delivery of those elements occurs or when VSOE of fair value can be established. VSOE of fair value is typically based on the price charged when the element is sold separately to customers. We are unable to use the residual method to recognize revenues for some arrangements that include products that are software deliverables under U.S. GAAP since VSOE of fair value does not exist for Implied Maintenance Release PCS elements, which are included in some of our arrangements.

For software products that include Implied Maintenance Release PCS, an element for which VSOE of fair value does not exist, revenue for the entire arrangement fee, which could include combinations of product, professional services, training and support, is recognized ratably as a group over the longest service period of any deliverable in the arrangement, with recognition commencing on the date delivery has occurred for all deliverables in the arrangement (or begins to occur in the case of professional services, training and support). Standalone sales of support contracts are recognized ratably over the service period of the product being supported.

From time to time, we offer certain customers free upgrades or specified future products or enhancements. When a software deliverable arrangement contains an Implied Maintenance Release PCS deliverable, revenue recognition of the entire arrangement will only commence when any free upgrades or specified future products or enhancements have been delivered, assuming all other products in the arrangement have been delivered and all services, if any, have commenced.

## RESULTS OF OPERATIONS

The following table sets forth certain items from our consolidated statements of operations as a percentage of net revenues for the three and nine months ended September 30, 2017 and 2016:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Net revenues:				
Product	51.6 %	53.6 %	49.1 %	56.4 %
Services	48.4 %	46.4 %	50.9 %	43.6 %
Total net revenues	100.0 %	100.0 %	100.0 %	100.0 %
Cost of revenues	42.7 %	36.7 %	41.1 %	33.6 %
Gross margin	57.3 %	63.3 %	58.9 %	66.4 %
Operating expenses:				
Research and development	15.2 %	16.8 %	16.6 %	15.8 %
Marketing and selling	24.4 %	22.9 %	25.8 %	22.4 %
General and administrative	14.4 %	11.6 %	13.9 %	12.2 %
Amortization of intangible assets	0.3 %	0.5 %	0.4 %	0.5 %
Restructuring costs, net	(0.6)%	4.5 %	2.1 %	2.0 %
Total operating expenses	53.7 %	56.3 %	58.8 %	52.9 %
Operating income	3.6 %	7.0 %	0.1 %	13.5 %
Interest and other expense, net	(4.5)%	(4.0)%	(4.3)%	(3.5)%
(Loss) income before income taxes	(0.9)%	3.0 %	(4.2)%	10.0 %
Benefit from income taxes	(1.0)%	(4.5)%	(0.1)%	(1.0)%
Net income (loss)	0.1 %	7.5 %	(4.1)%	11.0 %

### Net Revenues

Our net revenues are derived mainly from sales of video and audio hardware and software products and solutions for digital media content production, management and distribution, and related professional services and maintenance contracts. We commonly sell large, complex solutions to our customers that, due to their strategic nature, have long lead times where the timing of order execution and fulfillment can be difficult to predict. In addition, the rapid evolution of the media industry is changing our customers' needs, businesses and revenue models, which is influencing their short-term and long-term purchasing decisions. As a result of these factors, the timing and amount of product revenue recognized each quarter related to these large orders, as well as the services associated with them, can fluctuate from quarter to quarter and cause significant volatility in our quarterly operating results. For a discussion of these factors, see the risk factors discussed in Part I - Item 1A under the heading "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2016.

### Net Revenues for the Three Months Ended September 30, 2017 and 2016

	(dollars in thousands)			
	2017 Net Revenues	Change		2016 Net Revenues
		\$	%	
Video products and solutions	\$ 27,058	\$ (12,124)	(30.9)%	\$ 39,182
Audio products and solutions	27,261	2,703	11.0%	24,558
Products and solutions	54,319	(9,421)	(14.8)%	63,740
Services	50,946	(4,333)	(7.8)%	55,279
Total net revenues	\$ 105,265	\$ (13,754)	(11.6)%	\$ 119,019

**Net Revenues for the Nine Months Ended September 30, 2017 and 2016**

(dollars in thousands)				
	2017	Change		2016
	Net Revenues	\$	%	Net Revenues
Video products and solutions	\$ 82,585	\$ (35,667)	(30.2)%	\$ 118,252
Audio products and solutions	70,395	(35,194)	(33.3)%	105,589
Products and solutions	152,980	(70,861)	(31.7)%	223,841
Services	158,765	(14,029)	(8.1)%	172,794
Total net revenues	\$ 311,745	\$ (84,890)	(21.4)%	\$ 396,635

The following table sets forth the percentage of our net revenues attributable to geographic regions for the three and nine months ended September 30, 2017 and 2016:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
United States	37%	39%	39%	37%
Other Americas	7%	8%	7%	8%
Europe, Middle East and Africa	39%	37%	39%	40%
Asia-Pacific	17%	16%	15%	15%

**Video Products and Solutions Revenues**

Video products and solutions revenues are derived primarily from sales of our storage and workflow solutions, our media management solutions and our video creative tools. Video products and solutions revenues decreased \$12.1 million, or 30.9%, for the three months ended September 30, 2017, and decreased \$35.7 million, or 30.2%, for the nine months ended September 30, 2017 compared to the same periods in 2016. The decrease in video revenues was primarily due to lower amortization of deferred revenues attributable to transactions executed on or before December 31, 2010. As a result of our adoption of ASU No. 2009-13 and ASU No. 2009-14 on January 1, 2011, many of our product orders now qualify for upfront revenue recognition; however, prior to adoption of this accounting guidance, the same orders required ratable recognition over periods of up to eight years. Deferred revenue associated with transactions executed prior to the adoption of ASU No. 2009-13 and ASU No. 2009-14 was largely amortized in 2016.

**Audio Products and Solutions Revenues**

Audio products and solutions revenues are derived primarily from sales of our digital audio software and workstation solutions and our control surfaces, consoles and live-sound systems. Audio products and solutions revenues increased \$2.7 million, or 11.0%, for the three months ended September 30, 2017, and decreased \$35.2 million, or 33.3%, for the nine months ended September 30, 2017, compared to the same periods in 2016. The increase for the three months ended September 30, 2017 was primarily due to strengthened sales of our Pro Tools and control surface products. The decrease in audio revenues for the nine months ended September 30, 2017 was primarily due to the accelerated revenue recognition of Pro Tools 12 during the nine months ended September 30, 2016 as a result of the cessation of Implied Maintenance Release PCS for Pro Tools. The decrease during the period was also due to the previously discussed lower amortization of deferred revenues attributable to transactions executed on or before December 31, 2010.

**Services Revenues**

Services revenues are derived primarily from maintenance contracts, as well as professional services and training. Services revenues decreased \$4.3 million, or 7.8%, for the three months ended September 30, 2017, and decreased \$14.0 million, or 8.1%, for the nine months ended September 30, 2017, compared to the same periods in 2016. The decrease was primarily due to the accelerated revenue recognition of maintenance contracts and increasing conversion rates of new maintenance contracts into revenue during the three and nine months ended September 30, 2016 as the result of the determination that Implied Maintenance Release PCS on Pro Tools 12 no longer existed during the three months ended March 31, 2016. The previously discussed lower

amortization of deferred revenues attributable to transactions executed on or before December 31, 2010 also contributed to the decreases.

### ***Cost of Revenues, Gross Profit and Gross Margin Percentage***

Cost of revenues consists primarily of costs associated with:

- procurement of components and finished goods;
- assembly, testing and distribution of finished products;
- warehousing;
- customer support related to maintenance;
- royalties for third-party software and hardware included in our products;
- amortization of technology; and
- providing professional services and training.

Amortization of technology represents the amortization of developed technology assets acquired as part of acquisitions.

#### **Costs of Revenues and Gross Profit for the Three Months Ended September 30, 2017 and 2016**

(dollars in thousands)				
	2017	Change		2016
	Costs	\$	%	Costs
Products	\$ 29,485	\$ 2,692	10.0%	\$ 26,793
Services	13,472	(1,413)	(9.5)%	14,885
Amortization of intangible assets	1,950	—	—%	1,950
Total cost of revenues	<u>\$ 44,907</u>	<u>\$ 1,279</u>	2.9%	<u>\$ 43,628</u>
Gross profit	\$ 60,358	\$ (15,033)	(19.9)%	\$ 75,391

#### **Costs of Revenues and Gross Profit for the Nine Months Ended September 30, 2017 and 2016**

(dollars in thousands)				
	2017	Change		2016
	Costs	\$	%	Costs
Products	\$ 80,478	\$ (1,927)	(2.3)%	\$ 82,405
Services	41,747	(3,379)	(7.5)%	45,126
Amortization of intangible assets	5,850	—	—%	5,850
Total cost of revenues	<u>\$ 128,075</u>	<u>\$ (5,306)</u>	(4.0)%	<u>\$ 133,381</u>
Gross profit	\$ 183,670	\$ (79,584)	(30.2)%	\$ 263,254

### Gross Margin Percentage

Gross margin percentage, which is net revenues less costs of revenues divided by net revenues, fluctuates based on factors such as the mix of products sold, the cost and proportion of third-party hardware and software included in the systems sold, the offering of product upgrades, price discounts and other sales-promotion programs, the distribution channels through which products are sold, the timing of new product introductions, sales of aftermarket hardware products such as disk drives and currency exchange-rate fluctuations. For a discussion of these factors, see the risk factors discussed in Part I - Item 1A under the heading "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2016. Our total gross margin percentage for the three months ended September 30, 2017 decreased to 57.3% from 63.3% for the same period in 2016, and for the nine months ended September 30, 2017 decreased to 58.9% from 66.4% for the same period in 2016. The decreases were primarily due to the decreased revenue from our products and services as discussed above, partially offset by cost savings resulting from our programs to reduce costs and increase operational efficiencies.

#### **Gross Margin % for the Three Months Ended September 30, 2017 and 2016**

	<b>2017 Gross Margin %</b>	<b>Change</b>	<b>2016 Gross Margin %</b>
Products	45.7%	(12.3)%	58.0%
Services	73.6%	0.5%	73.1%
Total	57.3%	(6.0)%	63.3%

#### **Gross Margin % for the Nine Months Ended September 30, 2017 and 2016**

	<b>2017 Gross Margin %</b>	<b>Change</b>	<b>2016 Gross Margin %</b>
Products	47.4%	(15.8)%	63.2%
Services	73.7%	(0.2)%	73.9%
Total	58.9%	(7.5)%	66.4%

### ***Operating Expenses and Operating Income***

#### **Operating Expenses and Operating Income for the Three Months Ended September 30, 2017 and 2016**

<b>(dollars in thousands)</b>				
	<b>2017</b>	<b>Change</b>		<b>2016</b>
	<b>Expenses</b>	<b>\$</b>	<b>%</b>	<b>Expenses</b>
Research and development	\$ 16,025	\$ (3,928)	(19.7)%	\$ 19,953
Marketing and selling	25,652	(1,579)	(5.8)%	27,231
General and administrative	15,193	1,371	9.9%	13,822
Amortization of intangible assets	362	(205)	(36.2)%	567
Restructuring costs, net	(582)	(5,896)	(111.0)%	5,314
Total operating expenses	<u>\$ 56,650</u>	<u>\$ (10,237)</u>	<u>(15.3)%</u>	<u>\$ 66,887</u>
Operating income	\$ 3,708	\$ (4,796)	(56.4)%	\$ 8,504



**Operating Expenses and Operating Income for the Nine Months Ended September 30, 2017 and 2016**

(dollars in thousands)				
	2017 Expenses	Change		2016 Expenses
		\$	%	
Research and development	\$ 51,904	\$ (10,887)	(17.3)%	\$ 62,791
Marketing and selling	80,481	(8,546)	(9.6)%	89,027
General and administrative	43,268	(5,091)	(10.5)%	48,359
Amortization of intangible assets	1,088	(1,047)	(49.0)%	2,135
Restructuring costs, net	6,464	(1,414)	(17.9)%	7,878
Total operating expenses	\$ 183,205	\$ (26,985)	(12.8)%	\$ 210,190
Operating income	\$ 465	\$ (52,599)	(99.1)%	\$ 53,064

**Research and Development Expenses**

Research and development (“R&D”) expenses include costs associated with the development of new products and the enhancement of existing products, and consist primarily of employee compensation and benefits; facilities costs; depreciation; costs for consulting and temporary employees; and prototype and other development expenses. R&D expenses decreased \$3.9 million, or 19.7%, for the three months ended September 30, 2017, and decreased \$10.9 million, or 17.3%, for the nine months ended September 30, 2017, compared to the same periods in 2016. The table below provides further details regarding the changes in components of R&D expenses.

**Change in R&D Expenses for the Three Months Ended September 30, 2017 and 2016**

(dollars in thousands)		
	2017 Decrease From 2016	
	\$	%
Personnel-related	\$ (2,371)	(21.1)%
Facilities and information technology	(799)	(19.3)%
Consulting and outside services	(588)	(16.6)%
Other	(170)	(16.5)%
Total research and development expenses decrease	\$ (3,928)	(19.7)%

**Change in R&D Expenses for the Nine Months Ended September 30, 2017 and 2016**

(dollars in thousands)		
	2017 Decrease From 2016	
	\$	%
Personnel-related	\$ (6,701)	(18.8)%
Consulting and outside services	(1,715)	(15.3)%
Facilities and information technology	(1,634)	(13.3)%
Computer hardware and supplies	(422)	(31.1)%
Other	(415)	(17.3)%
Total research and development expenses decrease	\$ (10,887)	(17.3)%

The decreases in all R&D expense categories for the three and nine months ended September 30, 2017, compared to the same periods in 2016, were primarily the result of our cost efficiency program.

### Marketing and Selling Expenses

Marketing and selling expenses consist primarily of employee compensation and benefits for selling, marketing and pre-sales customer support personnel; commissions; travel expenses; advertising and promotional expenses; web design costs and facilities costs. Marketing and selling expenses decreased \$1.6 million, or 5.8%, for the three months ended September 30, 2017, and decreased \$8.5 million, or 9.6%, for the nine months ended September 30, 2017, compared to the same periods in 2016. The table below provides further details regarding the changes in components of marketing and selling expenses.

Change in Marketing and Selling Expenses for the Three Months Ended September 30, 2017 and 2016		
(dollars in thousands)		
	2017 (Decrease) Increase From 2016	
	\$	%
Foreign exchange losses	\$ 1,076	194.9 %
Personnel-related	(997)	(5.8)%
Advertising and promotion	(539)	(28.0)%
Bad debt	(467)	(89.2)%
Facilities and information technology	(416)	(8.6)%
Consulting and outside services	(406)	(28.1)%
Other	170	20.9 %
Total marketing and selling expenses decrease	<u>\$ (1,579)</u>	<u>(5.8)%</u>

Change in Marketing and Selling Expenses for the Nine Months Ended September 30, 2017 and 2016		
(dollars in thousands)		
	2017 (Decrease) Increase From 2016	
	\$	%
Personnel-related	\$ (6,648)	(11.9)%
Foreign exchange losses	2,990	164.6 %
Consulting and outside services	(2,406)	(39.7)%
Advertising and promotion	(1,566)	(19.7)%
Bad debt	(1,048)	(117.8)%
Other	132	0.8 %
Total marketing and selling expenses decrease	<u>\$ (8,546)</u>	<u>(9.6)%</u>

The decreases in personnel-related, consulting and outside services, and advertising and promotion expenses for the three and nine months ended September 30, 2017, compared to the same periods in 2016, were primarily the result of our cost efficiency program. The decreases in bad debt expense for the three and nine months ended September 30, 2017, compared to the same periods in 2016, were due to high bad debt reserve set up during 2016 and no additional reserve required in 2017. During the three and nine months ended September 30, 2017, net foreign exchange losses (specifically, resulting from foreign currency denominated transactions and the revaluation of foreign currency denominated assets and liabilities), which are included in marketing and selling expenses, were \$1.6 million and \$4.8 million, respectively, compared to loss of \$0.6 million and \$1.8 million, respectively, during the three and nine months ended September 30, 2016.

### General and Administrative Expenses

General and administrative (“G&A”) expenses consist primarily of employee compensation and benefits for administrative, executive, finance and legal personnel; audit, legal and strategic consulting fees; and insurance, information systems and

facilities costs. Information systems and facilities costs reported within general and administrative expenses are net of allocations to other expenses categories. G&A expenses increased \$1.4 million, or 9.9%, for the three months ended September 30, 2017, and decreased \$5.1 million, or 10.5%, for the nine months ended September 30, 2017, compared to the same periods in 2016. The table below provides further details regarding the changes in components of G&A expenses.

**Change in G&A Expenses for the Three Months Ended September 30, 2017 and 2016**

(dollars in thousands)		
	2017 Increase (Decrease) From 2016	
	\$	%
Consulting and outside services	\$ 1,551	44.2 %
Other	(180)	(1.8)%
Total general and administrative expenses decrease	<u>\$ 1,371</u>	<u>9.9 %</u>

**Change in G&A Expenses for the Nine Months Ended September 30, 2017 and 2016**

(dollars in thousands)		
	2017 Decrease From 2016	
	\$	%
Personnel-related	\$ (3,893)	(17.0)%
Facilities and information technology	(611)	(8.2)%
Consulting and outside services	(327)	(2.3)%
Other	(260)	(6.9)%
Total general and administrative expenses decrease	<u>\$ (5,091)</u>	<u>(10.5)%</u>

The decreases in all G&A expense categories for the nine months ended September 30, 2017, compared to the same period in 2016, were primarily the result of our cost efficiency program. The increase in consulting and outside services for the three months ended September 30, 2017, compared to the same period in 2016, was primarily due to increased legal professional fees related to class actions and settlements.

***Benefit from Income Taxes***

**Benefit from Income Taxes for the Three Months Ended September 30, 2017 and 2016**

(dollars in thousands)				
	2017	Change		2016
		\$	%	
Benefit from income taxes	\$ (1,065)	\$ 4,256	(80.0)%	\$ (5,321)

**Benefit from Income Taxes for the Nine Months Ended September 30, 2017 and 2016**

(dollars in thousands)				
	2017	Change		2016
		\$	%	
Benefit from income taxes	\$ (326)	\$ 3,657	(91.8)%	\$ (3,983)

We had a tax benefit of 2.5% and (10.2)%, respectively, as a percentage of loss or income before tax for the nine months ended September 30, 2017 and 2016. The \$3.7 million increase in the tax provision for the nine month period ended September 30, 2017 is primarily related to the 2016 benefit for an uncertain tax position related to the foreign implications arising from changes in revenue recognition, which was not present in the 2017 period. This benefit was \$5.2 million and \$3.2 million in the three and

nine month periods of 2016, respectively. Changes in the jurisdictional mix of earnings partially offset the increase in the three-month period and slightly augmented the increase in the nine-month period, respectively. No benefit was provided for the tax loss generated in the United States due to a full valuation on the deferred tax asset. In addition, the estimated annual effective tax rate excluded the United States because the earnings could not be reliably estimated due to anticipated marginal profitability.

## LIQUIDITY AND CAPITAL RESOURCES

### *Liquidity and Sources of Cash*

We have generally funded operations in recent years through the use of existing cash balances, supplemented from time to time with the proceeds of long-term debt and borrowings under our credit facilities. Our principal sources of liquidity include cash and cash equivalents totaling \$44.1 million as of September 30, 2017.

In February 2016, we committed to a cost efficiency program that encompassed a series of measures intended to allow us to more efficiently operate in a leaner, more directed cost structure. These measures included reductions in our workforce, consolidation of facilities, transfers of certain business processes to lower cost regions and reductions in other third-party services costs. The cost efficiency program was substantially complete as of June 30, 2017.

In connection with the cost efficiency program, on February 26, 2016, we entered into the Financing Agreement with the Lenders. Pursuant to the Financing Agreement, we entered into a term loan in the original aggregate principal amount of \$100.0 million. The Financing Agreement also originally provided us with the ability to draw up to a maximum of \$5.0 million in revolving credit. All outstanding loans under the Financing Agreement will become due and payable in February 2021, or in May 2020 if the \$125.0 million in outstanding principal of the Notes has not been repaid or refinanced by such time.

The Financing Agreement contains customary representations and warranties, covenants, mandatory prepayments, and events of default under which our payment obligations may be accelerated. On March 14, 2017, we entered into the First Amendment to our Financing Agreement. The First Amendment modifies the covenant requiring us to maintain a Leverage Ratio (defined to mean the ratio of (a) total funded indebtedness to (b) consolidated EBITDA) such that following the Amendment No. 1 Effective Date, we are required to keep a Leverage Ratio of no greater than 3.50:1.00 for the four quarters ended March 31, 2017, 4.20:1.00 for the four quarters ended June 30, 2017, 4.75:1.00 for the four quarters ended September 30, 2017, 4.80:1.00 for the four quarters ending December 31, 2017, 4.40:1.00 for each of the four quarters ending March 31, 2018 through March 31, 2019, respectively, and thereafter declining over time from 3.50:1.00 to 2.50:1.00. Following the Amendment No. 1 Effective Date, interest accrues on outstanding borrowings under the credit facility and the term loan (each as defined in the Financing Agreement) at a rate of either the LIBOR Rate (as defined in the Financing Agreement) plus 7.25% or a Reference Rate (as defined in the Financing Agreement) plus 6.25%, at the option of Avid. As of September 30, 2017, we were in compliance with the Financing Agreement covenants.

On November 9, 2017 (the "Amendment No. 2 Effective Date"), we entered into the Second Amendment to the Financing Agreement. The Second Amendment extended an additional \$15.0 million term loan to the Company, thereby increasing the aggregate principal amount of the term loan to \$115.0 million. The Second Amendment also increased the amount of available revolving credit by \$5.0 million to an aggregate amount of \$10.0 million. The additional \$15.0 million term loan must be repaid in quarterly principal payments of \$187,500 commencing in March 2018. The Second Amendment also granted us the ability to use up to \$15.0 million to purchase Notes and modified the definition of consolidated EBITDA used in the Leverage Ratio calculation to adjust for expected changes in deferred revenue due to the adoption of ASC 606.

Our ability to satisfy the Leverage Ratio covenant in the future is dependent on our ability to maintain bookings and billings at or above levels experienced over the last 12 months. In recent quarters, we have experienced volatility in bookings and billings resulting from, among other things, (i) our transition towards subscription and recurring revenue streams and the resulting decline in traditional upfront product sales, (ii) volatility in currency rates and in particular the U.S. dollar against the Euro, (iii) significant changes and trends in the media industry and the impact they have had on our customers and (iv) the impact of new and anticipated product launches and features. In addition to the impact of new bookings and billings, U.S. GAAP revenues recognized as the result of the existence of Implied Maintenance Release PCS will be significantly lower in the remainder of 2017, as compared to 2016 periods, which will have an adverse impact on our Leverage Ratio.

In the event bookings and billings in future quarters are lower than we currently anticipate, we may be forced to take remedial actions which could include, among other things (and where allowed by the Lenders), (i) further cost reductions, (ii) seeking replacement financing, (iii) raising funds through the issuance of additional equity or debt securities or the incurrence of additional borrowings, or (iv) disposing of certain assets or businesses. Such remedial actions, which may not be available on favorable terms or at all, could have a material adverse impact on our business. If we are not in compliance with the Leverage Ratio and are unable to obtain an amendment or waiver, such noncompliance may result in an event of default under the Financing Agreement, which could permit acceleration of the outstanding indebtedness under the Financing Agreement and require us to repay such indebtedness before the scheduled due date. If an event of default were to occur, we might not have sufficient funds available to make the payments required. If we are unable to repay amounts owed, the Lenders may be entitled to foreclose on and sell substantially all of our assets, which secure our borrowings under the Financing Agreement.

On January 26, 2017, we entered into an exclusive distributor agreement, or the Distributor Agreement, with Beijing Jetsen Technology Co., Ltd., or Jetsen, pursuant to which Jetsen became the exclusive distributor for Avid products and services in the greater China region. The Distributor Agreement has a five-year term, and Jetsen is required to make at least \$75.8 million of aggregate purchases under the agreement over the first three years. At the same time, we also entered into a securities purchase agreement, or the Securities Purchase Agreement, with Jetsen, pursuant to which we agreed to sell to Jetsen shares of Avid common stock. In June 2017, we and Jetsen amended the Securities Purchase Agreement. Under the amended terms, Jetsen will invest \$18.2 million in Avid, in return for a minority stake in Avid of between 4.5% and 8.9% of Avid outstanding common stock on a fully diluted basis. The closing of the investment is subject to closing conditions, including China regulatory approvals. In the event regulatory approval is not obtained in the fourth quarter of 2017, either party may elect to terminate the Securities Purchase Agreement for any reason. The exact number of shares to be issued and sold at closing will be determined by reference to the trading price of Avid common stock before closing.

Our cash requirements vary depending on factors such as the growth of our business, changes in working capital, and capital expenditures. We expect to operate the business and execute our strategic initiatives principally with funds generated from operations, remaining net proceeds from the term loan borrowings under the Financing Agreement, and draw up to a maximum of \$10.0 million under the Financing Agreement's revolving credit facility. We anticipate that we will have sufficient internal and external sources of liquidity to fund operations and anticipated working capital and other expected cash needs for at least the next 12 months as well as for the foreseeable future.

## Cash Flows

The following table summarizes our cash flows for the periods presented (in thousands):

	Nine Months Ended September 30,	
	2017	2016
Net cash provided by (used in) operating activities	\$ 6,103	\$ (48,925)
Net cash used in investing activities	(4,359)	(14,242)
Net cash (used in) provided by financing activities	(3,351)	92,591
Effect of foreign currency exchange rates on cash and cash equivalents	753	391
Net (decrease) increase in cash and cash equivalents	\$ (854)	\$ 29,815

### Cash Flows from Operating Activities

Cash provided by operating activities aggregated \$6.1 million for the nine months ended September 30, 2017. The significant improvement compared to the nine months ended September 30, 2016 was primarily attributable to (i) significantly lower operating expenses as the result of our cost efficiency program, (ii) significantly lower inventory purchases due to improved inventory management, (iii) severance and other restructuring related payments during the nine months ended September 30, 2016 that did not reoccur at the same levels in the 2017 period, and (iv) the timing of annual bonus payments, which were paid in the second quarter in 2016 and in the fourth quarter in 2017.

### Cash Flows from Investing Activities

For the nine months ended September 30, 2017, net cash flows used in investing activities reflected \$6.1 million used for the purchase of property and equipment, and \$1.8 million of cash released from the cash collateral for our letters of credit. Our

purchases of property and equipment largely consist of computer hardware and software to support R&D activities and information systems.

*Cash Flows from Financing Activities*

For the nine months ended September 30, 2017, net cash flows used in financing activities were primarily the principal payment of the Term Loan.

**RECENT ACCOUNTING PRONOUNCEMENTS**

***Recently Adopted Accounting Pronouncement and Recent Accounting Pronouncements To Be Adopted***

Our recently adopted and to be adopted accounting pronouncements are set forth under Part I, Item 1 of this Form 10-Q.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK**

#### ***Foreign Currency Exchange Risk***

We have significant international operations and derive more than half of our revenues from customers outside the United States. This business is, for the most part, transacted through international subsidiaries and generally in the currency of the end-user customers. Therefore, we are exposed to the changes in foreign currency exchange rates that could adversely affect our revenues, net income and cash flow.

During the nine months ended September 30, 2017 and 2016, we recorded net losses of \$4.8 million and \$1.8 million, respectively, that resulted from foreign currency denominated transactions and the revaluation of foreign currency denominated assets and liabilities.

A hypothetical change of 10% in appreciation or depreciation of foreign currency exchange rates from the quoted foreign currency exchange rates as of September 30, 2017, would not have a significant impact on our financial position, results of operations or cash flows.

#### ***Interest Rate Risk***

On February 26, 2016, we borrowed \$100.0 million under the Term Loan, and borrowed an additional \$15.0 million under the Term Loan on November 9, 2017. On March 14, 2017 (the "Amendment No. 1 Effective Date"), we entered into an amendment (the "First Amendment") to the Financing Agreement, with the lenders party thereto. Following the Amendment No.1 Effective Date, interest accrues on outstanding borrowings under the credit facility and the term loan (each as defined in the Financing Agreement) at a rate of either the LIBOR Rate (as defined in the Financing Agreement) plus 7.25% or a Reference Rate (as defined in the Financing Agreement) plus 6.25%, at our option. We also maintain a revolving Credit Facility that allows us to borrow up to \$10.0 million. A hypothetical 10% increase or decrease in interest rates paid on outstanding borrowings under the Financing Agreement would not have a material impact on our financial position, results of operations or cash flows.

On June 15, 2015, we issued \$125.0 million aggregate principal amount of our Notes pursuant to the terms of an indenture. The Notes pay interest semi-annually on June 15 and December 15 of each year, beginning on December 15, 2015, at an annual rate of 2.00% and mature on June 15, 2020 unless earlier converted or repurchased in accordance with their terms prior to such date. The fair value of the Notes is dependent on the price and volatility of our common stock as well as movements in interest rates. The fair value of our common stock and interest rate changes affect the fair value of the Notes, but do not impact our financial position, cash flows or results of operations due to the fixed nature of the debt obligations.

### **ITEM 4. CONTROLS AND PROCEDURES**

#### ***Evaluation of Disclosure Controls and Procedures***

Our management, with the participation and supervision of our Chief Executive Officer and Chief Financial Officer, is responsible for our disclosure controls and procedures pursuant to Rules 13a-15(e) and 15d-15(e) under the Exchange Act. Disclosure controls and procedures are controls and other procedures that 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 under SEC rules and forms. Disclosure controls and procedures include controls and procedures designed to ensure that information required to be disclosed in our reports filed under the Exchange Act is accumulated and communicated to our principal executive officer and our principal financial officer, as appropriate, to allow timely decisions regarding required disclosure.

Our management, including the Chief Executive Officer and the Chief Financial Officer, carried out an evaluation of the effectiveness of our disclosure controls and procedures as of September 30, 2017. Based on this evaluation, our management concluded that as of September 30, 2017 these disclosure controls and procedures were not effective at the reasonable assurance level as a result of the material weakness in our internal controls over financial reporting, due to the

ineffective controls over licensing and provisioning of software described in Item 9A of our Annual Report on Form 10-K for the year ended December 31, 2016. As discussed below, our internal control over financial reporting is an integral part of our disclosure controls and procedures.

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

Under applicable SEC rules (Exchange Act Rules 13a-15(c) and 15d-15(c)) management is required to evaluate any changes in internal control over financial reporting that occurred during each fiscal quarter that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting. As discussed in Item 9A of our Annual Report on Form 10-K for the year ended December 31, 2016, we have undertaken remedial actions to address the material weakness in our internal control over financial reporting over the licensing and provisioning of software by enhancing the design of our controls to now require our development team to formalize and sign-off testing procedures currently in place to ensure documentation is sufficient for compliance purposes. Our enhanced controls were operational for the three months ended September 30, 2017, however, the material weakness cannot be considered remediated until (i) the control has operated for a sufficient period of time and (ii) management has concluded, through testing, that the control is operating effectively. We expect that the material weakness will be remediated in the fourth quarter of 2017.

### ***Inherent Limitation on the Effectiveness of Internal Controls***

The effectiveness of any system of internal control over financial reporting is subject to inherent limitations, including the exercise of judgment in designing, implementing, operating, and evaluating the controls and procedures, and the inability to eliminate misconduct completely. Accordingly, any system of internal control over financial reporting can only provide reasonable, not absolute, assurances. In addition, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. We intend to continue to monitor and upgrade our internal controls as necessary or appropriate for our business, but cannot assure that such improvements will be sufficient to provide us with effective internal control over financial reporting.



## **PART II - OTHER INFORMATION**

### **ITEM 1. LEGAL PROCEEDINGS**

See Note 7 “Contingencies” of our Notes to Condensed Consolidated Financial Statements regarding our legal proceedings. Aside from the disclosure below, there have been no material developments from the disclosures contained in our Annual Report on Form 10-K for the fiscal year ended December 31, 2016.

In November 2016, a purported securities class action lawsuit was filed in the U.S. District Court for the District of Massachusetts (Mohanty v. Avid Technology, Inc. et al., No. 16-cv-12336) against us and certain executive officers seeking unspecified damages and other relief on behalf of a purported class of purchasers of our common stock between August 4, 2016 and November 9, 2016, inclusive. The complaint purported to state a claim for violation of federal securities laws as a result of alleged violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 (“the Exchange Act”) and Rule 10b-5 promulgated thereunder. The complaint’s allegations relate generally to our disclosure surrounding the level of implementation of our Avid NEXIS solution product offerings. On February 7, 2017, the Court appointed a lead plaintiff and counsel in the matter. On June 14, 2017, we moved to dismiss the action. On July 31, 2017, the lead plaintiff filed an opposition to our motion to dismiss, and on August 21, 2017, we filed its reply brief. On October 13, 2017, after a mediation, the parties reached an agreement in principle to settle this litigation. We expect the majority of the settlement to be funded by our insurers. Finalization of the settlement is subject to a number of conditions, including execution of definitive documentation and approval by the court.

### **ITEM 1A. RISK FACTORS**

Investing in our common stock involves a high degree of risk. You should carefully consider the risks and uncertainties described in Part I - Item 1A under the heading “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2016 in addition to the other information included in this Form 10-Q before making an investment decision regarding our common stock. If any of these risks actually occurs, our business, financial condition or operating results would likely suffer, possibly materially, the trading price of our common stock could decline, and you could lose part or all of your investment.

### **ITEM 6. EXHIBITS**

The list of exhibits, which are filed or furnished with this Form 10-Q or are incorporated herein by reference, is set forth in the Exhibit Index immediately preceding the exhibits and is incorporated herein by reference.

## EXHIBIT INDEX

Exhibit No.	Description	Filed with this Form 10-Q	Incorporated by Reference		
			Form or Schedule	SEC Filing Date	SEC File Number
31.1	<a href="#"><u>Certification of Principal Executive Officer pursuant to Rules 13a-14 and 15d-14 under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u></a>	X			
31.2	<a href="#"><u>Certification of Principal Financial Officer pursuant to Rules 13a-14 and 15d-14 under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u></a>	X			
32.1	<a href="#"><u>Certifications pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u></a>	X			
*101.INS	XBRL Instance Document	X			
*101.SCH	XBRL Taxonomy Extension Schema Document	X			
*101.CAL	XBRL Taxonomy Calculation Linkbase Document	X			
*101.DEF	XBRL Taxonomy Definition Linkbase Document	X			
*101.LAB	XBRL Taxonomy Label Linkbase Document	X			
*101.PRE	XBRL Taxonomy Presentation Linkbase Document	X			

\* Pursuant to Rule 406T of Regulation S-T, XBRL (Extensible Business Reporting Language) information is deemed not filed or a part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, is deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934 and otherwise is not subject to liability under these sections.

## SIGNATURE

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.

### **AVID TECHNOLOGY, INC.**

(Registrant)

Date: November 9, 2017

By: /s/ Brian E. Agle

Name: Brian E. Agle

Title: Senior Vice President and Chief Financial Officer

## CERTIFICATION

I, Louis Hernandez, Jr., certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Avid Technology, Inc.;
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.

Date: November 9, 2017

/s/ Louis Hernandez, Jr.

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Louis Hernandez, Jr.

Chairman and Chief Executive Officer  
(Principal Executive Officer)

## CERTIFICATION

I, Brian E. Agle, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Avid Technology, Inc.;
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.

Date: November 9, 2017

/s/ Brian E. Agle

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Brian E. Agle

Senior Vice President and Chief Financial Officer  
(Principal Financial Officer)

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

In connection with the Quarterly Report on Form 10-Q of Avid Technology, Inc. (the “Company”) for the quarter ended September 30, 2017 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), the undersigned, Louis Hernandez, Jr., Chairman and Chief Executive Officer of the Company, and Brian E. Agle, Senior Vice President and Chief Financial Officer of the Company, each hereby certifies, pursuant to 18 U.S.C. Section 1350, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 9, 2017

/s/ Louis Hernandez, Jr.

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Louis Hernandez, Jr.

Chairman and Chief Executive Officer  
(Principal Executive Officer)

Date: November 9, 2017

/s/ Brian E. Agle

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Brian E. Agle

Senior Vice President and Chief Financial Officer  
(Principal Financial Officer)

*A certification furnished pursuant to this item will not be deemed “filed” for purposes of Section 18 of the Exchange Act (15 U.S.C. 78r), or otherwise subject to the liability of that section. Such certification will not be deemed to be incorporated by reference into any filing under the Securities Act or the Exchange Act, except to the extent that the registrant specifically incorporates it by reference.*