AVID TECHNOLOGY, INC.
Form 10-Q
November 09, 2016

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2016

OR

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

For the transition period from __________ to __________

Commission File Number: 1-36254

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

Delaware	04-2977748
(State or Other Jurisdiction of Incorporation or Organization)	(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 x   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 x   No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer ¨	Accelerated Filer x
Non-accelerated Filer ¨ (Do not check if smaller reporting company)	Smaller Reporting Company ¨

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

The number of shares outstanding of the registrant's Common Stock, par value $0.01, as of November 4, 2016 was 40,625,177.

AVID TECHNOLOGY, INC.
FORM 10-Q
FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2016

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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,” “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;
- our ability to develop, market and sell new products and services;
- 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;
- our ability to achieve our goal of expanding our market positions;
- the anticipated performance of our products;
- our business strategies and market positioning;
- our ability to successfully consummate acquisitions, or investment transactions and successfully integrate acquired businesses including the acquisition of 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 trends and developments in our markets and the success of our products in these markets;
- our ability to effectively mitigate and remediate the material weaknesses in our internal control over financial reporting, and the expected timing thereof;
- our capital resources and the adequacy thereof;
- 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 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 operation, including Brexit;
- the expected timing of recognition of revenue backlog as revenue, and the timing of recognition of revenues from subscription offerings;
- estimated asset and liability values and amortization of our intangible assets;
- our compliance with covenants contained in the agreements governing our indebtedness;
- changes in inventory levels;
- seasonal factors;
- plans regarding repatriation of foreign earnings;
- fluctuations in foreign exchange and interest rates; and
- the risk of restatement of our financial statements.

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, 2015, in Part II, Item 1A of our quarterly reports for the quarters ended March 31, 2016 and June 30, 2016 and in other documents we filed 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 at some point 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, except as required by law.

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 Motion Graphics, AirSpeed, EUCON, iNEWS, Interplay, ISIS, Avid MediaCentral Platform, 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		Nine Months Ended	
	September 30,		September 30,	
	2016	2015	2016	2015
Net revenues:				
Products	$63,740	$88,945	$223,841	$245,124
Services	55,279	48,491	172,794	121,665
Total net revenues	119,019	137,436	396,635	366,789
Cost of revenues:				
Products	26,793	32,256	82,405	92,416
Services	14,885	15,416	45,126	46,054
Amortization of intangible assets	1,950	1,950	5,850	2,113
Total cost of revenues	43,628	49,622	133,381	140,583
Gross profit	75,391	87,814	263,254	226,206
Operating expenses:				
Research and development	19,953	25,225	62,791	71,708
Marketing and selling	27,231	31,564	89,027	92,420
General and administrative	13,822	15,834	48,359	52,646
Amortization of intangible assets	567	786	2,135	1,568
Restructuring costs, net	5,314	—	7,878	539
Total operating expenses	66,887	73,409	210,190	218,881
Operating income	8,504	14,405	53,064	7,325
Interest expense	(4,702)	(2,469)	(13,702)	(3,722)
Other expense, net	(5)	(50)	(347)	(959)
Income before income taxes	3,797	11,886	39,015	2,644
(Benefit from) provision for income taxes	(5,321)	768	(3,983)	(4,221)
Net income	$9,118	$11,118	$42,998	$6,865
Net income per common share – basic and diluted	$0.23	$0.28	$1.08	$0.17
Weighted-average common shares outstanding – basic	40,194	39,231	39,814	39,417
Weighted-average common shares outstanding – diluted	40,476	39,750	39,950	40,727

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

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Net income	$9,118	$11,118	$42,998	$6,865
Other comprehensive income:				
Foreign currency translation adjustments	155	(1,735)	2,613	(5,403)
Comprehensive income	$9,273	$9,383	$45,611	$1,462

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, 2016	December 31, 2015
ASSETS		
Current assets:		
Cash and cash equivalents	$ 47,717	$ 17,902
Accounts receivable, net of allowances of $8,491 and $9,226 at September 30, 2016 and December 31, 2015, respectively	40,850	58,807
Inventories	55,634	48,073
Prepaid expenses	6,901	6,548
Other current assets	7,104	6,119
Total current assets	158,206	137,449
Property and equipment, net	32,969	35,481
Intangible assets, net	25,245	33,219
Goodwill	32,643	32,643
Long-term deferred tax assets, net	2,028	2,011
Other long-term assets	11,827	7,123
Total assets	$ 262,918	$ 247,926
LIABILITIES AND STOCKHOLDERS’ DEFICIT		
Current liabilities:		
Accounts payable	$ 25,852	$ 45,511
Accrued compensation and benefits	27,439	28,124
Accrued expenses and other current liabilities	33,434	35,354
Income taxes payable	658	1,023
Short-term debt	5,000	5,000
Deferred revenues	157,468	189,887
Total current liabilities	249,851	304,899
Long-term debt	188,301	95,950
Long-term deferred tax liabilities, net	1,367	3,443
Long-term deferred revenues	82,540	158,495
Other long-term liabilities	13,592	14,711
Total liabilities	535,651	577,498
Contingencies (Note 8)		
Stockholders’ deficit:		
Common stock	423	423
Additional paid-in capital	1,043,563	1,055,838
Accumulated deficit	(1,276,369)	(1,319,318)
Treasury stock at cost	(34,784)	(58,336)
Accumulated other comprehensive loss	(5,566)	(8,179)
Total stockholders’ deficit	(272,733)	(329,572)
Total liabilities and stockholders’ deficit	$ 262,918	$ 247,926

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

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

	Nine Months Ended September 30,	
	2016	2015
Cash flows from operating activities:		
Net income	$42,998	$6,865
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	19,169	13,936
Provision (recovery) for doubtful accounts	890	(175)
Stock-based compensation expense	6,116	7,731
Non-cash provision for restructuring	1,137	—
Non-cash interest expense	7,935	1,544
Unrealized foreign currency transaction losses (gains)	2,021	(5,098)
Benefit for deferred taxes	(5,187)	(6,504)
Changes in operating assets and liabilities, net of effects from acquisitions:		
Accounts receivable	17,057	6,844
Inventories	(7,561)	4,028
Prepaid expenses and other current assets	(1,493)	1,772
Accounts payable	(19,627)	4,932
Accrued expenses, compensation and benefits and other liabilities	(4,384)	(17,764)
Income taxes payable	347	1,268
Deferred revenues	(108,343)	(55,466)
Net cash used in operating activities	(48,925)	(36,087)
Cash flows from investing activities:		
Purchases of property and equipment	(9,681)	(11,110)
Payments for business and technology acquisitions, net of cash acquired	—	(65,967)
Increase in other long-term assets	(17)	(575)
Increase in restricted cash	(4,544)	(1,047)
Net cash used in investing activities	(14,242)	(78,699)
Cash flows from financing activities:		
Proceeds from long-term debt	100,000	120,401
Repayment of debt	(2,500)	—
Payments for repurchase of common stock	—	(7,999)
Cash paid for capped call transaction	—	(10,125)
Proceeds from the issuance of common stock under employee stock plans	5,914	3,113
Common stock repurchases for tax withholdings for net settlement of equity awards	(803)	(1,442)
Proceeds from revolving credit facilities	25,000	49,500
Payments on revolving credit facilities	(30,000)	(39,500)
Payments for credit facility issuance costs	(5,020)	(1,193)
Net cash provided by financing activities	92,591	112,755
Effect of exchange rate changes on cash and cash equivalents	391	(1,045)
Net increase (decrease) in cash and cash equivalents	29,815	(3,076)
Cash and cash equivalents at beginning of period	17,902	25,056
Cash and cash equivalents at end of period	$47,717	$21,980
Supplemental information:		
Cash paid for income taxes, net of refunds	$1,678	$1,538

Cash paid for interest	5,767	1,492

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

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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 (loss) income, 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, 2015 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, 2015 in its Annual Report on Form 10-K for the year ended December 31, 2015, which included all 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, 2015.

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 $47.7 million as of September 30, 2016.

In February 2016, the Company committed to a cost efficiency program that encompasses a series of measures intended to allow the Company to more efficiently operate in a leaner, and more directed cost structure. These measures include reductions in the Company's workforce, facilities consolidation, transferring certain business processes to lower cost regions and reducing other third-party service costs. In connection with this cost efficiency program, the Company has incurred $14.5 million of the total expected incremental cash expenditures, approximately $25 million, relating to termination benefits, facility costs, employee overlap expenses and related actions. The Company anticipates that the cost efficiency program will be substantially complete by the end of the second quarter of 2017 and, when fully implemented, will result in annualized costs savings of approximately $76 million.

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 aggregate principal amount of $100 million. The Financing Agreement also provides the Company with the ability to draw up to a maximum of $5 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 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. Proceeds from the Financing Agreement have been used to replace an existing $35 million revolving credit facility, finance the Company's efficiency program and other initiatives, and provide operating flexibility throughout the remainder of the transformation in this period of heightened market volatility.

After paying for both debt issuance costs and the cost efficiency program, the new financing provided approximately $70 million of available liquidity, about half of which replaced the prior revolving credit facility with the remainder providing incremental liquidity to fund operations. The Financing Agreement requires the Company to comply with a financial statement covenant that stipulates a maximum leverage ratio (defined to mean the ratio of (a) consolidated total funded indebtedness to (b) consolidated EBITDA) of no greater than 4.35:1.00 for the four quarters ending June 30, 2016; 5.40:1.00 for the four quarters ending September 30, 2016; 4.20:1.00 for the four quarters ending December 31, 2016 and thereafter declining over time from 3.50:1.00 to 2.50:1.00. The Financing Agreement also restricts the Company from making capital expenditures in excess of $20 million in any fiscal year. As of September 30, 2016 the Company was in compliance with these covenants.

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The Company’s ability to satisfy the leverage ratio covenant in the future is heavily dependent on its ability to increase bookings and billings 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 strengthening of the US dollar against the Euro, (iii) dramatic changes in the media industry and the impact it has 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, GAAP revenues recognized as the result of the existence of Implied Maintenance Release PCS (as defined below) in prior periods will decline significantly for the remainder of 2016 and in 2017, 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, it 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 additional equity 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.

The Company’s cash requirements vary depending on factors such as the growth of the business, changes in working capital, capital expenditures, and obligations under the cost efficiency program. 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 $5.0 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 twelve 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 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 without making concessions, 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 the Company's products, there has been an ongoing practice of Avid 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 course of 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. The determination that Pro Tools 12 Implied Maintenance Release PCS had ended was based on management (i) clearly communicating a policy of no longer providing any Software Updates or other support to customers that are not covered under a paid support plan and (ii) implementing robust digital rights management tools to enforce the policy. With the new policy and technology for Pro Tools 12 in place, combined with management's intent to continue to adhere to the policy, management concluded in the first quarter of 2016 that Implied Maintenance Release PCS for Pro Tools 12 transactions no longer exists. 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;

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- 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 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, or 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 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 many arrangements that include products that are software deliverables under GAAP since VSOE of fair value does not exist for Implied Maintenance Release PCS elements, which are included in many 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.

Recent Accounting Pronouncements to be Adopted

In May, 2014, the FASB issued a 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. Entities have the option of using either a full retrospective or a modified approach to adopt the guidance in the ASU. The Company has not yet selected a transition method and is evaluating the effect that the updated standard will have on its consolidated financial statements and related disclosures.

In August 2014, the FASB issued ASU 2014-15, Presentation of Financial Statements - Going Concern. ASU 2014-15 provides guidance around management’s responsibility to evaluate whether there is substantial doubt about an entity’s ability to continue as a going concern and to provide related footnote disclosures. For each reporting period, management will be required to evaluate whether there are conditions or events that raise substantial doubt about a company’s ability to continue as a going concern within one year from the date the financial statements are issued. The new standard is effective for the Company beginning January 1, 2017. Early adoption is permitted. The Company is evaluating the potential impact of adopting this standard on its financial statements, as well as timing of its adoption of the standard.

On February 25, 2016, the FASB issued new accounting guidance on leases. Lessees will need 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.

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 for the nine months ended September 30, 2016 and 2015.

	September 30, 2016	September 30, 2015
Options	3,939	1,023
Non-vested restricted stock units	687	231
Anti-dilutive potential common shares	4,626	1,254

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 (see Note 11). In connection with the offering of the Notes, the Company entered into a capped call transaction with a third party (the "Capped Call") (see Note 11, Long-Term Debt and Credit Agreement). 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, 2016, 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. ACQUISITION

On June 23, 2015, the Company completed the acquisition of Orad Hi-Tech Systems Ltd. ("Orad"). Orad provides 3D real-time graphics, video servers and related asset management solutions. The acquisition adds applications to Avid's Studio Suite which the Company intends to connect to the Avid MediaCentral Platform.

In allocating the total purchase consideration of $73.4 million for Orad based on the fair value as of June 23, 2015, the Company recorded $32.6 million of goodwill, $37.2 million of identifiable intangibles assets, and $3.6 million to other net assets. Intangible assets acquired included core and completed technology, customer relationships and trade name.

4. 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, 2016 and December 31, 2015, 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, 2016	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	$ 2,035	$495	$ 1,540	$ —

		Fair Value Measurements at Reporting Date Using		
	December 31, 2015	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	$ 3,617	$572	$ 3,045	$ —

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, 2016, the net carrying amount of the Notes was $100.1 million, and the fair value of the Notes was approximately $104.7 million based on open market trading activity, which constitutes a Level 1 input in the fair value hierarchy.

5. INVENTORIES

Inventories consisted of the following (in thousands):

	September 30, 2016	December 31, 2015
Raw materials	$ 10,371	$ 9,594
Work in process	252	256
Finished goods	45,011	38,223
Total	$ 55,634	$ 48,073

As of September 30, 2016 and December 31, 2015, finished goods inventory included $7.8 million and $5.3 million, respectively, associated with products shipped to customers and deferred labor costs for arrangements where revenue recognition had not yet commenced.

6. 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, 2016			December 31, 2015		
	Gross	Accumulated Amortization	Net	Gross	Accumulated Amortization	Net
Completed technologies and patents	$58,257	$ (36,969)	$21,288	$58,032	$ (30,902)	$27,130
Customer relationships	54,753	(50,796)	3,957	54,656	(48,767)	5,889
Trade names	1,346	(1,346)	—	1,346	(1,146)	200
Capitalized software costs	4,911	(4,911)	—	4,911	(4,911)	—
Total	$119,267	$ (94,022)	$25,245	$118,945	$ (85,726)	$33,219

Amortization expense related to all intangible assets in the aggregate was $2.5 million and $2.7 million, respectively, for the three months ended September 30, 2016 and 2015 and $8.0 million and $3.7 million, respectively, for the nine months ended September 30, 2016 and 2015. The Company expects amortization of acquired intangible assets to be $2.3 million for the remainder of 2016, $9.3 million in 2017, $9.3 million in 2018, and $4.4 million in 2019.

Goodwill at September 30, 2016 and December 31, 2015 was $32.6 million, which resulted from the acquisition of Orad in 2015.

7. OTHER LONG-TERM LIABILITIES

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

	September 30, 2016	December 31, 2015
Deferred rent	$ 5,793	$ 6,755
Accrued restructuring	1,513	647
Deferred compensation	6,286	7,309
Total	$ 13,592	$ 14,711

8. 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. 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.

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.

As of September 30, 2016 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

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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 entered a License Agreement with Nexidia Inc., which grants Avid a limited, exclusive, and restricted to the Media Market, non-assignable worldwide, non-sublicensable, license to use media and entertainment technologies and solutions and associated language packs (the "Licensed Software"). In accordance with the terms of the License Agreement, the Company will pay Nexidia a non-refundable initial license fee of $2.0 million by no later than January 2, 2017. The initial license fee entitles Avid to sell such amounts and numbers of the Licensed Software based on a license fee per license software.

The Company has letters of credit that are used as security deposits in connection with the Company's Burlington, Massachusetts office space and other facilities. In the event of default on the underlying leases, the landlords would, as of September 30, 2016, be eligible to draw against the letters of credit to a maximum of $2.2 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. Also, the Company has letters of credit totaling $1.2 million that support its ongoing operations. These letters of credit have various terms and expiration dates during 2016 and beyond, and some of the letters of credit may automatically renew based on the terms of the underlying agreements.

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, 2016 and 2015 (in thousands):

	Nine Months Ended September 30,	
	2016	2015
Accrual balance at beginning of year	$2,234	$2,792
Accruals for product warranties	1,992	2,429
Costs of warranty claims	(1,872)	(2,747)
Accrual balance at end of period	$2,354	$2,474

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

9. RESTRUCTURING COSTS AND ACCRUALS

2016 Restructuring Plan

In February 2016, the Company committed to a restructuring plan that encompasses a series of measures intended to allow the Company to more efficiently operate in a leaner, and more directed cost structure. These include reductions in the Company's workforce, facilities consolidation, transferring certain business processes to lower cost regions, and reducing other third-party services costs.

During the quarter ended December 31, 2015, the Company recorded restructuring costs of $5.8 million, which represented an initial elimination of 111 positions worldwide during January and February of 2016. During the quarter ended March 31, 2016, the Company recorded restructuring costs of $2.8 million, representing the elimination of an additional 63 positions worldwide. During the quarter ended June 30, 2016, the Company recorded additional restructuring costs of $0.4 million, and recoveries totaling $0.6 million as a result of severance pay estimate changes primarily for the eliminated positions in Europe. During the quarter ended September 30, 2016, the Company recorded restructuring charges of $2.4 million related to severance costs for an additional 60 positions eliminated and severance pay estimate adjustments, and $2.1 million for the partial closure of facilities in Burlington, Massachusetts, which included non-cash amounts of $1.1 million for fixed asset write-off.

Prior Years' Restructuring Plans

In September 2016, the Company recorded a revision of restructuring costs of $0.8 million resulting from an update to the sublease assumption related to the Company's Mountain View, California facility that was partially abandoned in 2012.

The accrual balance of $1.7 million as of September 30, 2016 was related to the closure of part of the Company's Mountain View, California, and Dublin, Ireland facilities under restructuring plans that were made in 2012 and 2008, respectively. No further actions are anticipated under those plans.

Restructuring Summary

The following table sets forth the activity in the restructuring accruals for the nine months ended September 30, 2016 (in thousands):

	Employee-Related	Facilities/Other-Related	Total
Accrual balance as of December 31, 2015	$ 5,509	$ 1,671	$7,180
New restructuring charges – operating expenses	5,536	943	6,479
Revisions of estimated liabilities	(501)	763	262
Non-cash write-offs	—	1,137	1,137
Accretion	—	211	211
Cash payments	(7,053)	(988)	(8,041)
Foreign exchange impact on ending balance	(72)	8	(64)
Accrual balance as of September 30, 2016	$ 3,419	$ 3,745	$7,164

The employee-related accruals as of September 30, 2016 represent severance costs to former employees that will be paid out within twelve 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 as of September 30, 2016 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, $1.1 million is included in the caption "accrued expenses and other current liabilities", $1.5 million is included in the caption "other long-term liabilities", and $1.1 million of fixed assets write-off relating to the partial closure of facilities in Burlington, Massachusetts is reflected in the caption "property and equipment, net" in the Company's condensed consolidated balance sheet as of September 30, 2016.

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10. 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, 2016 and 2015 (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Video products and solutions net revenues	$39,182	$62,851	$118,252	$152,798
Audio products and solutions net revenues	24,558	26,094	105,589	92,326
Products and solutions net revenues	63,740	88,945	223,841	245,124
Services net revenues	55,279	48,491	172,794	121,665
Total net revenues	$119,019	$137,436	$396,635	$366,789

The following table sets forth the Company's revenues by geographic region for the three and nine months ended September 30, 2016 and 2015 (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Revenues:				
United States	$45,982	$48,146	$145,384	$135,225
Other Americas	9,702	10,212	30,674	24,384
Europe, Middle East and Africa	44,524	55,061	159,243	151,314
Asia-Pacific	18,811	24,017	61,334	55,866
Total net revenues	$119,019	$137,436	$396,635	$366,789

11. LONG TERM DEBT AND CREDIT AGREEMENT

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

	September 30, 2016	December 31, 2015
Term Loan, net of unamortized debt issuance costs of $4,324 at September 30, 2016	$ 93,175	$ —
Notes, net of unamortized original issue discount and debt issuance costs of $24,874 at September 30, 2016 and $29,050 at December 31, 2015, respectively	100,126	95,950
Credit Agreement	—	5,000
Total debt	193,301	100,950
Less: current portion	5,000	5,000
Total long-term debt	$ 188,301	$ 95,950

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 net proceeds from the offering were $120.3 million after deducting the offering expenses.

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. Additional interest may be payable upon the occurrence