

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549**

FORM 10-Q

(Mark One)

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

For the quarterly period ended July 31, 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: 001-37570

Pure Storage, Inc.

(Exact Name of Registrant as Specified in its Charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

27-1069557

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

**650 Castro Street, Suite 400
Mountain View, California
94041**

(Address of principal executive offices, including zip code)
(Zip Code)

(800) 379-7873

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

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

Large accelerated filer	<input checked="" type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/> (Do not check if a small reporting company)	Smaller reporting company	<input type="checkbox"/>
		Emerging growth company	<input type="checkbox"/>

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

As of August 25, 2017 the registrant had 97,037,611 shares of its Class A common stock outstanding and 114,445,493 shares of its Class B common stock outstanding.

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NOTE ABOUT FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act), about us and our industry that involve substantial risks and uncertainties. All statements other than statements of historical facts contained in this report, including statements regarding our future results of operations and financial condition, business strategy and plans and objectives of management for future operations, are forward-looking statements. In some cases, forward-looking statements may be identified by words such as “anticipate,” “believe,” “continue,” “could,” “design,” “estimate,” “expect,” “intend,” “may,” “plan,” “potentially,” “predict,” “project,” “should,” “will” or the negative of these terms or other similar expressions.

Forward-looking statements contained in this Quarterly Report on Form 10-Q include, but are not limited to, statements regarding our ability to sustain or manage our expansion and growth, our expectations that average sales prices may decrease over time, our plans to expand and continue to invest internationally, our plans to expand the research and development organization as well as the sales and marketing function and channel programs, our expectations regarding fluctuations in our revenue and operating results, our expectations that we may continue to experience losses despite significant revenue growth, our ability to successfully attract, motivate, and retain qualified personnel and maintain our culture, our expectations regarding our technological leadership and market opportunity, our ability to realize benefits from our investments, our ability to innovate and introduce new or enhanced products, our expectations regarding product acceptance and our technologies, products and solutions, our competitive position and the effects of competition and industry dynamics, including those of retrofitted or new products from incumbent vendors, hyperconverged products, defined as server compute and storage combined within a single chassis, or public cloud, our expectations concerning relationships with third parties, including partners and customers, the adequacy of our intellectual property rights, and expectations concerning pending legal proceedings and related costs.

We have based these forward-looking statements largely on our current expectations and projections about future events and financial trends that we believe may affect our financial condition, results of operations, business strategy, and financial needs. These forward-looking statements are subject to a number of known and unknown risks, uncertainties and assumptions, including risks described in the section titled “Risk Factors.” These risks are not exhaustive. Other sections of this report include additional factors that could harm our business and financial performance. Moreover, we operate in a very competitive and rapidly changing environment. New risk factors emerge from time to time, and it is not possible for our management to predict all risk factors nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ from those contained in, or implied by, any forward-looking statements.

Investors should not rely upon forward-looking statements as predictions of future events. We cannot assure investors that the events and circumstances reflected in the forward-looking statements will be achieved or occur. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. Except as required by law, we undertake no obligation to update publicly any forward-looking statements for any reason after the date of this report or to conform these statements to actual results or to changes in our expectations. Investors should read this Quarterly Report on Form 10-Q and the documents that we reference in this Quarterly Report on Form 10-Q and have filed as exhibits to this report with the understanding that our actual future results, levels of activity, performance and achievements may be materially different from what we expect. We qualify all of our forward-looking statements by these cautionary statements.

PART I—FINANCIAL INFORMATION

Item 1. Financial Statements.

PURE STORAGE, INC.
Condensed Consolidated Balance Sheets
(in thousands, except per share data, unaudited)

	As of January 31, 2017	As of July 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 183,675	\$ 171,894
Marketable securities	362,986	351,123
Accounts receivable, net of allowance of \$2,000 and \$2,020 as of January 31, 2017 and July 31, 2017	168,978	168,404
Inventory	23,498	33,660
Deferred commissions, current	15,787	19,700
Prepaid expenses and other current assets	25,157	24,494
Total current assets	780,081	769,275
Property and equipment, net	81,695	81,850
Intangible assets, net	6,560	5,808
Deferred income taxes, non-current	844	877
Other assets, non-current	30,565	32,322
Total assets	\$ 899,745	\$ 890,132
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 52,719	\$ 52,092
Accrued compensation and benefits	39,252	42,537
Accrued expenses and other liabilities	21,697	18,309
Deferred revenue, current	158,095	169,638
Liability related to early exercised stock options	1,362	816
Total current liabilities	273,125	283,392
Deferred revenue, non-current	145,031	157,961
Other liabilities, non-current	3,159	3,373
Total liabilities	421,315	444,726
Commitments and contingencies (Note 5)		
Stockholders' equity:		
Preferred stock, par value of \$0.0001 per share— 20,000 shares authorized as of January 31, 2017 and July 31, 2017; no shares issued and outstanding as of January 31, 2017 and July 31, 2017	—	—
Class A and Class B common stock, par value of \$0.0001 per share— 2,250,000 (Class A 2,000,000, Class B 250,000) shares authorized as of January 31, 2017 and July 31, 2017; 204,364 (Class A 87,027, Class B 117,337) and 210,975 (Class A 96,478, Class B 114,497) shares issued and outstanding as of January 31, 2017 and July 31, 2017	20	20
Additional paid-in capital	1,281,452	1,372,221
Accumulated other comprehensive loss	(562)	(280)
Accumulated deficit	(802,480)	(926,555)
Total stockholders' equity	478,430	445,406
Total liabilities and stockholders' equity	\$ 899,745	\$ 890,132

See the accompanying notes to condensed consolidated financial statements.

PURE STORAGE, INC.
Condensed Consolidated Statements of Operations
(in thousands, except per share data, unaudited)

	Three Months Ended July 31,		Six Months Ended July 31,	
	2016	2017	2016	2017
Revenue:				
Product	\$ 130,920	\$ 175,013	\$ 242,658	\$ 313,438
Support	32,294	49,448	60,503	93,654
Total revenue	163,214	224,461	303,161	407,092
Cost of revenue:				
Product	42,847	57,252	76,893	103,897
Support	14,000	19,199	26,934	36,102
Total cost of revenue	56,847	76,451	103,827	139,999
Gross profit	106,367	148,010	199,334	267,093
Operating expenses:				
Research and development	58,635	69,361	111,573	134,789
Sales and marketing	87,583	120,633	170,681	217,597
General and administrative	19,630	22,162	41,211	42,258
Total operating expenses	165,848	212,156	323,465	394,644
Loss from operations	(59,481)	(64,146)	(124,131)	(127,551)
Other income, net	37	3,266	1,319	5,261
Loss before provision for income taxes	(59,444)	(60,880)	(122,812)	(122,290)
Provision for income taxes	106	821	526	1,785
Net loss	\$ (59,550)	\$ (61,701)	\$ (123,338)	\$ (124,075)
Net loss per share attributable to common stockholders, basic and diluted	\$ (0.31)	\$ (0.29)	\$ (0.65)	\$ (0.60)
Weighted-average shares used in computing net loss per share attributable to common stockholders, basic and diluted	192,730	209,193	191,026	207,515

See the accompanying notes to condensed consolidated financial statements.

PURE STORAGE, INC.
Condensed Consolidated Statements of Comprehensive Loss
(in thousands, unaudited)

	<u>Three Months Ended July 31,</u>		<u>Six Months Ended July 31,</u>	
	<u>2016</u>	<u>2017</u>	<u>2016</u>	<u>2017</u>
Net loss	\$ (59,550)	\$ (61,701)	\$ (123,338)	\$ (124,075)
Other comprehensive income:				
Change in unrealized net gain on available-for-sale securities	45	165	852	282
Comprehensive loss	<u>\$ (59,505)</u>	<u>\$ (61,536)</u>	<u>\$ (122,486)</u>	<u>\$ (123,793)</u>

See the accompanying notes to condensed consolidated financial statements.

PURE STORAGE, INC.
Condensed Consolidated Statements of Cash Flows
(in thousands, unaudited)

	Six Months Ended July 31,	
	2016	2017
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	\$ (123,338)	\$ (124,075)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	22,336	30,000
Stock-based compensation expense	50,894	69,057
Other	494	797
Changes in operating assets and liabilities:		
Accounts receivable, net	6,589	25
Inventory	(2,392)	(10,487)
Deferred commissions	1,887	(4,607)
Prepaid expenses and other current assets	(809)	(186)
Accounts payable	(10,007)	201
Accrued compensation and other liabilities	8,687	310
Deferred revenue	41,102	24,473
Net cash used in operating activities	(4,557)	(14,492)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of property and equipment	(46,118)	(30,100)
Purchase of intangible assets	(1,000)	—
Purchases of marketable securities	(427,968)	(95,358)
Sales of marketable securities	59,071	33,529
Maturities of marketable securities	5,800	73,681
Net increase in restricted cash	(5,600)	—
Net cash used in investing activities	(415,815)	(18,248)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net proceeds from exercise of stock options	6,369	6,793
Proceeds from issuance of common stock under employee stock purchase plan	15,079	14,166
Net cash provided by financing activities	21,448	20,959
Net decrease in cash and cash equivalents	(398,924)	(11,781)
Cash and cash equivalents, beginning of period	604,742	183,675
Cash and cash equivalents, end of period	\$ 205,818	\$ 171,894
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash paid for income taxes	\$ 1,827	\$ 1,661
SUPPLEMENTAL DISCLOSURES OF NON-CASH INVESTING AND FINANCING INFORMATION		
Property and equipment purchased but not yet paid	\$ 7,691	\$ 6,578
Vesting of early exercised stock options	\$ 486	\$ 546

See the accompanying notes to condensed consolidated financial statements.

PURE STORAGE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

Note 1. Business Overview

Organization and Description of Business

Pure Storage, Inc. (the Company, we, us, or other similar pronouns) was originally incorporated in the state of Delaware in October 2009 under the name OS76, Inc. In January 2010, we changed our name to Pure Storage, Inc. We are building a data platform that transforms business through a dramatic increase in performance and reduction in complexity and costs. We are headquartered in Mountain View, California and have wholly owned subsidiaries throughout the world.

Note 2. Basis of Presentation and Summary of Significant Accounting Policies

Principles of Consolidation

The condensed consolidated financial statements include the accounts of the company and our wholly owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

Unaudited Interim Consolidated Financial Information

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States (U.S. GAAP) and applicable rules and regulations of the Securities and Exchange Commission (the SEC) regarding interim financial reporting. Certain information and note disclosures normally included in the financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to such rules and regulations. Therefore, these condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in our Annual Report on Form 10-K for the year ended January 31, 2017 .

In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all normal recurring adjustments necessary to present fairly the financial position, results of operations, comprehensive loss and cash flows for the interim periods, but are not necessarily indicative of the results of operations to be anticipated for the full fiscal year 2018 or any future period.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported and disclosed in the financial statements and accompanying notes. Actual results could differ from these estimates. Such estimates include, but are not limited to, the determination of best estimate of selling price included in multiple-element revenue arrangements, sales commissions, useful lives of intangible assets and property and equipment, fair values of stock-based awards, provision for income taxes, including related reserves, and contingent liabilities, among others. Management bases its estimates on historical experience and on various other assumptions which management believes to be reasonable, the results of which form the basis for making judgments about the carrying values of assets and liabilities.

Restricted Cash

Restricted cash is comprised of cash collateral for a vendor credit card program and letters of credit related to our facility leases. As of both January 31, 2017 and July 31, 2017 , we had restricted cash of \$12.7 million , which was included in other assets, non-current, in the condensed consolidated balance sheets.

Marketable Securities

We classify our marketable securities as available-for-sale at the time of purchase and reevaluate such classification at each balance sheet date. We may sell these securities at any time for use in current operations even if they have not yet reached maturity. As a result, we classify our securities, including those with maturities beyond twelve months, as current assets in the accompanying condensed consolidated balance sheets. We carry these securities at fair value and record unrealized gains and losses, in other comprehensive income (loss), which is reflected as a component of stockholders' equity. We evaluate our securities to assess whether those with unrealized loss positions are other than temporarily impaired. We consider impairments to be other than temporary if they are related

PURE STORAGE, INC.**Notes to Condensed Consolidated Financial Statements (Unaudited)**

to deterioration in credit risk or if it is likely we will sell the securities before the recovery of their cost basis. Realized gains and losses from the sale of marketable securities and declines in value deemed to be other than temporary are determined on the specific identification method. To date, there have been no declines in value deemed to be other than temporary in any of our securities. Realized gains and losses are reported in other income, net, in the condensed consolidated statements of operations.

Deferred Commissions

Deferred commissions consist of direct and incremental costs paid to our sales force related to customer contracts. The deferred commission amounts are recoverable through the revenue streams that will be recognized under the related customer contracts. Direct sales commissions are deferred when earned and amortized over the same period that revenue is recognized from the related customer contract. Amortization of deferred commissions is included in sales and marketing expense in the condensed consolidated statements of operations.

As of January 31, 2017 and July 31, 2017, we recorded deferred commissions, current, of \$15.8 million and \$19.7 million, and deferred commissions, non-current, of \$14.9 million and \$15.6 million, in other assets, non-current, in the condensed consolidated balance sheets. We recognized sales commission expenses of \$19.6 million and \$25.5 million during the three months ended July 31, 2016 and 2017, and \$37.2 million and \$46.0 million during the six months July 31, 2016 and 2017, respectively.

Recent Accounting Pronouncements Not Yet Adopted

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers* (ASU 2014-09), requiring an entity to recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. ASU 2014-09 will supersede nearly all existing revenue recognition guidance under U.S. GAAP when it becomes effective. In August 2015, the FASB issued ASU No. 2015-14, *Revenue from Contracts with Customers*, deferring the effective date for ASU 2014-09 by one year. The new standard will be effective for us beginning on February 1, 2018 which is the mandatory adoption date and we do not plan to early adopt. This standard may be adopted using either the full or modified retrospective methods. We currently anticipate adopting the standard retrospectively to all prior periods presented. We are evaluating the impact of the new standard on our accounting policies, processes, and system requirements, and have assigned internal and external resources to assist in our evaluation and system implementation. We have made and will continue to make investments in systems to enable timely and accurate reporting under the new standard. We are also evaluating the potential impact that the implementation of this standard will have on our consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)* (ASU 2016-02). ASU 2016-02 requires lessees to recognize all leases with terms in excess of one year on their balance sheet as a right-of-use asset and a lease liability at the commencement date. The new standard also simplifies the accounting for sale and leaseback transactions. The amendments in this update will be effective for us beginning on February 1, 2019 and must be adopted using a modified retrospective method for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. Early adoption is permitted. We are currently evaluating adoption methods and the impact of this standard on our consolidated financial statements.

In June 2016, the FASB issued ASU No. 2016-13, *Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments* (ASU 2016-13). ASU 2016-13 amends guidance on reporting credit losses for assets held at amortized cost basis and available-for-sale debt securities to require that credit losses on available-for-sale debt securities be presented as an allowance rather than as a write-down. The measurement of credit losses for newly recognized financial assets and subsequent changes in the allowance for credit losses are recorded in the statements of operations. The amendments in this update will be effective for us beginning on February 1, 2020 with early adoption permitted on or after February 1, 2019. We are currently evaluating the impact of this standard on our consolidated financial statements.

In November 2016, the FASB issued ASU No. 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash* (ASU 2016-18), which requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore,

PURE STORAGE, INC.**Notes to Condensed Consolidated Financial Statements (Unaudited)**

amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. ASU 2016-18 will be effective for us beginning on February 1, 2018 and will be applied on a retrospective basis. Early adoption is permitted. We do not expect the adoption of this standard to have any material impact on our consolidated financial statements.

In May 2017, the FASB issued ASU No 2017-09, *Compensation—Stock Compensation (Topic 718) — Scope of Modification Accounting*, to clarify when to account for a change to the terms or conditions of a share-based payment award as a modification. Under the new standard, modification is required only if the fair value, the vesting conditions, or the classification of an award as equity or liability changes as a result of the change in terms or conditions. ASU 2017-09 will be effective for us beginning February 1, 2018 and will be applied prospectively. Early adoption is permitted. We are currently evaluating the impact of this standard on our consolidated financial statements.

Note 3. Financial Instruments***Fair Value Measurements***

We measure our cash equivalents, marketable securities and restricted cash at fair value on a recurring basis. We define fair value as the exchange price that would be received from sale of an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. We measure our financial assets and liabilities at fair value at each reporting period using a fair value hierarchy which requires us to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. A financial instrument's classification within the fair value hierarchy is based upon the lowest level of input that is significant to the fair value measurement. Three levels of inputs may be used to measure fair value:

- *Level I* —Observable inputs are unadjusted quoted prices in active markets for identical assets or liabilities;
- *Level II* —Observable inputs are quoted prices for similar assets and liabilities in active markets or inputs other than quoted prices that are observable for the assets or liabilities, either directly or indirectly through market corroboration, for substantially the full term of the financial instruments; and
- *Level III* —Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. These inputs are based on our own assumptions used to measure assets and liabilities at fair value and require significant management judgment or estimation.

We classify our cash equivalents, marketable securities and restricted cash within Level 1 or Level 2 because they are valued using either quoted market prices or inputs other than quoted prices which are directly or indirectly observable in the market, including readily-available pricing sources for the identical underlying security which may not be actively traded. Our fixed income available-for-sale securities consist of high quality, investment grade securities from diverse issuers. The valuation techniques used to measure the fair value of our marketable securities were derived from non-binding market consensus prices that are corroborated by observable market data or quoted market prices for similar instruments.

Cash Equivalents, Marketable Securities and Restricted Cash

The following tables summarize our cash equivalents, marketable securities and restricted cash by significant investment categories as of January 31, 2017 and July 31, 2017 (in thousands):

PURE STORAGE, INC.
Notes to Condensed Consolidated Financial Statements (Unaudited)

As of January 31, 2017							
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Cash Equivalents	Marketable Securities	Restricted Cash
Level 1							
Money market accounts	\$ —	\$ —	\$ —	\$ 12,734	\$ —	\$ —	\$ 12,734
Level 2							
U.S. government treasury notes	148,298	22	(289)	148,031	13,226	134,805	—
U.S. government agencies	40,398	2	(159)	40,241	—	40,241	—
Corporate debt securities	185,701	242	(379)	185,564	—	185,564	—
Foreign government bonds	2,377	2	(3)	2,376	—	2,376	—
Total	\$ 376,774	\$ 268	\$ (830)	\$ 388,946	\$ 13,226	\$ 362,986	\$ 12,734

As of July 31, 2017							
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Cash Equivalents	Marketable Securities	Restricted Cash
Level 1							
Money market accounts	\$ —	\$ —	\$ —	\$ 12,734	\$ —	\$ —	\$ 12,734
Level 2							
U.S. government treasury notes	140,495	15	(317)	140,193	18,390	121,803	—
U.S. government agencies	44,861	3	(139)	44,725	—	44,725	—
Corporate debt securities	182,057	365	(205)	182,217	—	182,217	—
Foreign government bonds	2,380	—	(2)	2,378	—	2,378	—
Total	\$ 369,793	\$ 383	\$ (663)	\$ 382,247	\$ 18,390	\$ 351,123	\$ 12,734

The amortized cost and estimated fair value of our marketable securities are shown below by contractual maturity (in thousands):

	As of July 31, 2017	
	Amortized Cost	Fair Value
Due within one year	\$ 150,456	\$ 150,372
Due in one to five years	200,946	200,751
Total	\$ 351,402	\$ 351,123

PURE STORAGE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

Based on our evaluation of available evidence, we concluded that the gross unrealized losses on our marketable securities as of July 31, 2017 were temporary in nature. The following table presents gross unrealized losses and fair values for those investments that were in a continuous unrealized loss as of July 31, 2017, aggregated by investment category (in thousands).

	Less than 12 months		Greater than 12 months		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
U.S. government treasury notes	\$ 121,518	\$ (299)	\$ 1,986	\$ (18)	\$ 123,504	\$ (317)
U.S. government agencies	35,916	(112)	4,471	(27)	40,387	(139)
Corporate debt securities	62,323	(192)	4,271	(13)	66,594	(205)
Foreign government bonds	878	(2)	—	—	878	(2)
Total	\$ 220,635	\$ (605)	\$ 10,728	\$ (58)	\$ 231,363	\$ (663)

Gross realized gains or losses on sale of marketable securities for the three and six months ended July 31, 2016 were \$104,000 and \$110,000; and were not significant for three and six months ended July 31, 2017.

Note 4. Balance Sheet Components

Inventory

Inventory consists of the following (in thousands):

	As of January 31, 2017	As of July 31, 2017
Raw materials	\$ 3,003	\$ 2,966
Finished goods	20,495	30,694
Inventory	\$ 23,498	\$ 33,660

Property and Equipment, Net

Property and equipment, net, consists of the following (in thousands):

	As of January 31, 2017	As of July 31, 2017
Test equipment	\$ 105,955	\$ 125,348
Computer equipment and software	54,521	60,838
Furniture and fixtures	4,494	5,045
Leasehold improvements	10,332	13,092
Total property and equipment	175,302	204,323
Less: accumulated depreciation and amortization	(93,607)	(122,473)
Property and equipment, net	\$ 81,695	\$ 81,850

Depreciation and amortization expense was \$11.6 million and \$14.8 million for the three months ended July 31, 2016 and 2017, and \$21.7 million and \$29.2 million for the six months ended July 31, 2016 and 2017, respectively.

Intangible Assets, Net

Intangible assets, net, consist of the following (in thousands):

PURE STORAGE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

	As of January 31, 2017	As of July 31, 2017
Technology patents	\$ 10,125	\$ 10,125
Accumulated amortization	(3,565)	(4,317)
Intangible assets, net	<u>\$ 6,560</u>	<u>\$ 5,808</u>

Intangible assets amortization expense was \$342,000 and \$376,000 for the three months ended July 31, 2016 and 2017, and \$668,000 and \$752,000 for the six months ended July 31, 2016 and 2017. The weighted-average remaining useful life of technology patents is 3.9 years. Due to the defensive nature of these patents, the amortization is included in general and administrative expenses in the condensed consolidated statements of operations.

As of July 31, 2017, expected amortization expense for intangible assets for each of the next five years is as follows (in thousands):

Years Ending January 31,	Estimated Future Amortization Expense
Remainder of 2018	\$ 752
2019	1,504
2020	1,504
2021	1,504
2022	544
Total	<u>\$ 5,808</u>

Accrued Expenses and Other Liabilities

Accrued expenses and other liabilities consist of the following (in thousands):

	As of January 31, 2017	As of July 31, 2017
Sales and use tax payable	\$ 540	\$ 298
Accrued professional fees	1,765	1,325
Accrued marketing	6,718	6,164
Accrued travel and entertainment expenses	2,235	4,014
Income tax payable	1,135	1,317
Other accrued liabilities	9,304	5,191
Total accrued expenses and other liabilities	<u>\$ 21,697</u>	<u>\$ 18,309</u>

Note 5. Commitments and Contingencies

Operating Leases

During the six months ended July 31, 2017, we extended the lease term of an existing office facility with total additional lease obligations of approximately \$2.0 million with the lease expiring through March 2019.

Letters of Credit

As of January 31, 2017 and July 31, 2017, we had outstanding letters of credit in the aggregate amount of \$7.7 million, in connection with our facility leases. The letters of credit are collateralized by restricted cash in the same amount and mature at various dates through June 2024.

PURE STORAGE, INC.**Notes to Condensed Consolidated Financial Statements (Unaudited)****Legal Matters**

On September 1, 2016, a purported securities class action entitled *Ramsay v. Pure Storage, Inc., et al.* was filed in the Superior Court of the State of California (San Mateo County) against us and certain of our officers, directors, investors and underwriters for our initial public offering (IPO), asserting claims under sections 11, 12 and 15 of the Securities Act on behalf of a purported class consisting of purchasers of our common stock pursuant or traceable to our initial public offering, and seeking unspecified compensatory damages and other relief. Substantially identical lawsuits were subsequently filed in the same court, bringing the same claims against the same defendants, captioned *Peter Galanis v. Pure Storage, Inc., et al.* (filed September 14, 2016), *Curtis Wilson v. Pure Storage, Inc., et al.* (filed September 15, 2016), *Loren Moe v. Pure Storage, Inc., et al.* (filed September 23, 2016), and *Mason Delahooke and Mahsa Shirazikia v. Pure Storage, Inc., et al.* (filed October 5, 2016). On October 27, 2016, the aforementioned actions were consolidated under the caption *In re Pure Storage, Inc. Shareholder Litigation*. On December 13, 2016, the plaintiffs filed a consolidated complaint. On January 26, 2017, the defendants filed a demurrer (motion to dismiss) to the consolidated complaint on the grounds that the plaintiffs failed to state a claim under the Securities Act. On April 4, 2017, the court sustained the demurrer as to all claims with leave to amend. On May 15, 2017, the plaintiffs filed an amended complaint, again asserting claims under sections 11, 12 and 15 of the Securities Act against us and certain of our officers, directors and underwriters for our IPO. On May 26, 2017 the defendants filed a demurrer (motion to dismiss) to the amended complaint on the grounds that the plaintiffs failed to state a claim under the Securities Act. The Court heard arguments on the second demurrer on July 18, 2017 and on August 31, 2017 the Court sustained defendant's demurrer again as to all claims with leave to amend. We believe there is no merit to the allegations and intend to defend ourselves vigorously.

From time to time, we have become involved in claims and other legal matters arising in the normal course of business. We investigate these claims as they arise. Although claims are inherently unpredictable, we currently are not aware of any matters that may have a material adverse effect on our business, financial position, results of operations or cash flows. Accordingly, we have not recorded any loss contingency on our consolidated balance sheet as of July 31, 2017.

Indemnification

Our arrangements generally include certain provisions for indemnifying customers against liabilities if our products or services infringe a third party's intellectual property rights. Other guarantees or indemnification arrangements include guarantees of product and service performance and standby letters of credit for lease facilities. It is not possible to determine the maximum potential amount under these indemnification obligations due to the limited history of prior indemnification claims and the unique facts and circumstances involved in each particular agreement. To date, we have not incurred any material costs as a result of such obligations and have not accrued any liabilities related to such obligations in the consolidated financial statements. In addition, we indemnify our officers, directors and certain key employees while they are serving in good faith in their respective capacities. To date, there have been no claims under any indemnification provisions.

Note 6. Stockholders' Equity**Preferred Stock**

We have 20,000,000 authorized shares of undesignated preferred stock, the rights, preferences and privileges of which may be designated from time to time by our board of directors. As of July 31, 2017, there were no shares of preferred stock issued or outstanding.

Class A and Class B Common Stock

We have two classes of authorized common stock, Class A common stock and Class B common stock. As of July 31, 2017, we had 2,000,000,000 shares of Class A common stock authorized with a par value of \$0.0001 per share and 250,000,000 shares of Class B common stock authorized with a par value of \$0.0001 per share. As of July 31, 2017, 96,478,332 shares of Class A common stock were issued and outstanding and 114,497,355 shares of Class B common stock were issued and outstanding.

Note 7. Equity Incentive Plans**Equity Incentive Plans**

We maintain two equity incentive plans: the 2009 Equity Incentive Plan (our 2009 Plan) and the 2015 Equity Incentive Plan (our 2015 Plan). In August 2015, our board of directors adopted, and in September 2015 our stockholders approved, the 2015 Plan, which became effective in connection with our IPO and serves as the successor to our 2009 Plan. Our 2015 Plan provides for grants of incentive stock options, non-statutory stock options, stock appreciation rights, restricted stock awards, restricted stock unit awards, performance stock awards, performance cash awards, and other forms of stock awards to our employees, directors and consultants. We ceased grants of new awards under our 2009 Plan after the effective date of our 2015 Plan, and no new grants will be made from our 2009 Plan. Outstanding awards granted under our 2009 Plan will remain subject to the terms of our 2009 Plan and applicable award agreements, until such outstanding awards that are stock options are exercised, terminated or expired by their terms.

We initially reserved 27,000,000 shares of our Class A common stock for issuance under our 2015 Plan. The number of shares reserved for issuance under our 2015 Plan increases automatically on the first day of February of each year through 2025, in an amount equal to 5% of the total number of shares of our capital stock outstanding as of the immediately preceding January 31.

The exercise price of stock options will generally not be less than 100% of the fair market value of our common stock on the date of grant, as determined by our board of directors. Our equity awards generally vest over a two to four year period and expire no later than ten years from the date of grant.

2015 Employee Stock Purchase Plan

In August 2015, our board of directors adopted and our stockholders approved, the 2015 Employee Stock Purchase Plan (2015 ESPP), which became effective in connection with our IPO. A total of 3,500,000 shares of Class A common stock was initially reserved for issuance under the 2015 ESPP. The number of shares reserved for issuance under our 2015 ESPP increases automatically on the first day of February of each year through 2025, in an amount equal to the lesser of (i) 1% of the total number of shares of our capital stock outstanding as of the immediately preceding January 31, and (ii) 3,500,000 shares of Class A common stock.

The 2015 ESPP allows eligible employees to purchase shares of our Class A common stock at a discount through payroll deductions (or other payroll contributions) of up to 30% of their eligible compensation, subject to a cap of 3,000 shares on any purchase date or \$25,000 in any calendar year (as determined under applicable tax rules). The 2015 ESPP provides for 24 month offering periods beginning March 16th and September 16th of each year, and each offering period consists of four six -month purchase periods, subject to a reset provision. If the closing stock price on the offering date of a new offering falls below the closing stock price on the offering date of an ongoing offering, the ongoing offering would terminate immediately following the purchase of ESPP shares on the purchase date immediately preceding the new offering and participants in the terminated ongoing offering would automatically be enrolled in the new offering (ESPP reset). On each purchase date, eligible employees will purchase our Class A common stock at a price per share equal to 85% of the lesser of the fair market value of our Class A common stock (1) on the first trading day of the applicable offering period or (2) the purchase date. Our closing stock price on the new offering date of March 16, 2017 was lower than the closing stock prices for both the offerings that started on March 16, 2016 and September 16, 2016, which triggered an ESPP reset for those offerings. The ESPP reset resulted in a modification charge of approximately \$9.0 million , which is being recognized over the new 24 -month offering period ending on March 15, 2019. In addition, the original remaining unamortized stock-based compensation expense for each of the offerings is being recognized over the same 24 -month offering period ending on March 15, 2019.

We recognized stock-based compensation related to our 2015 ESPP of \$4.3 million and \$3.8 million during the three months ended July 31, 2016 and 2017 and \$8.6 million and \$7.9 million during the six months ended July 31, 2016 and 2017 . As of July 31, 2017 , there was \$24.1 million of unrecognized stock-based compensation expense related to our 2015 ESPP which is expected to be recognized over a weighted-average period of approximately 1.6 years .

PURE STORAGE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

Stock Options

A summary of stock option activity under our equity incentive plans and related information is as follows:

	Options Outstanding			
	Number of Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Life (In Years)	Aggregate Intrinsic Value (in thousands)
Balance as of January 31, 2017	56,840,189	\$ 7.15	7.0	\$ 315,502
Options granted	—	—		
Options exercised	(2,769,381)	2.53		
Options forfeited/cancelled	(1,266,826)	14.04		
Balance as of July 31, 2017	52,803,982	\$ 7.23	6.5	\$ 315,252
Vested and exercisable as of July 31, 2017	31,539,259	\$ 4.67	5.8	\$ 248,932

The aggregate intrinsic value of options vested and exercisable as of July 31, 2017 is calculated based on the difference between the exercise price and the closing price of \$12.07 of our Class A common stock on July 31, 2017.

As of July 31, 2017, total unrecognized employee compensation cost related to outstanding options was \$98.4 million, which is expected to be recognized over a weighted-average period of approximately 2.5 years.

Restricted Stock Units

A summary of the restricted stock unit activity under our 2015 Plan and related information is as follows:

	Number of Restricted Stock Units Outstanding	Weighted-Average Grant Date Fair Value	Aggregate Intrinsic Value (in thousands)
Unvested Balance as of January 31, 2017	8,783,024	\$ 13.06	\$ 99,863
Granted	9,807,355	10.59	—
Vested	(2,221,800)	12.46	—
Forfeited	(908,755)	11.50	—
Unvested Balance as of July 31, 2017	15,459,824	\$ 11.67	\$ 186,600

As of July 31, 2017, total unrecognized employee compensation cost related to unvested restricted stock units was \$161.5 million, which is expected to be recognized over a weighted-average period of approximately 2.6 years.

During the six months ended July 31, 2017, we granted 750,000 performance stock units (net of 77,000 canceled units during the three months ended July 31, 2017) with both performance and service vesting conditions payable in common shares from 0% to 150% of the target number granted, contingent upon the degree to which the performance condition is met. Management determined it is probable that the performance condition will be satisfied and accordingly, we began recognizing stock-based compensation expense during the three months ended April 30, 2017. Stock-based compensation expense for these units was \$1.2 million and \$1.6 million for the three and six months ended July 31, 2017 recognized on an accelerated attribution method.

PURE STORAGE, INC.
Notes to Condensed Consolidated Financial Statements (Unaudited)
Stock-Based Compensation Expense

The following table summarizes the components of stock-based compensation expense recognized in the condensed consolidated statements of operations (in thousands):

	Three Months Ended July 31,		Six Months Ended July 31,	
	2016	2017	2016	2017
Cost of revenue—product	\$ 181	\$ 358	\$ 287	\$ 755
Cost of revenue—support	1,712	2,245	2,804	4,019
Research and development	13,976	17,971	25,634	33,559
Sales and marketing	8,732	11,439	16,251	22,065
General and administrative	3,295	4,825	5,918	8,659
Total stock-based compensation expense	\$ 27,896	\$ 36,838	\$ 50,894	\$ 69,057

The tax benefit related to stock-based compensation expense for all periods presented was not material.

Note 8. Net Loss per Share Attributable to Common Stockholders

Basic and diluted net loss per share attributable to common stockholders is presented in conformity with the two-class method required for participating securities.

Basic net loss per share attributable to common stockholders is computed by dividing the net loss by the weighted-average number of shares of common stock outstanding during the period, less shares subject to repurchase. Diluted net loss per share attributable to common stockholders is computed by giving effect to all potentially dilutive common stock equivalents outstanding for the period. For purposes of this calculation, stock options, unvested restricted stock awards, repurchasable shares from early exercised stock options, and shares subject to ESPP withholding are considered to be common stock equivalents but have been excluded from the calculation of diluted net loss per share attributable to common stockholders as their effect is anti-dilutive.

The rights, including the liquidation and dividend rights, of the holders of our Class A and Class B common stock are identical, except with respect to voting. As the liquidation and dividend rights are identical, the undistributed earnings are allocated on a proportionate basis and the resulting net loss per share attributed to common stockholders will, therefore, be the same for both Class A and Class B common stock on an individual or combined basis. We did not present dilutive net loss per share on an if-converted basis because the impact was not dilutive.

The following table sets forth the computation of basic and diluted net loss per share attributable to common stockholders (in thousands, except per share data):

	Three Months Ended July 31,		Six Months Ended July 31,	
	2016	2017	2016	2017
Net loss	\$ (59,550)	\$ (61,701)	\$ (123,338)	\$ (124,075)
Weighted-average shares used in computing net loss per share attributable to common stockholders, basic and diluted	192,730	209,193	191,026	207,515
Net loss per share attributable to common stockholders, basic and diluted	\$ (0.31)	\$ (0.29)	\$ (0.65)	\$ (0.60)

PURE STORAGE, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

The following weighted-average outstanding shares of common stock equivalents were excluded from the computation of diluted net loss per share attributable to common stockholders for the periods presented because including them would have been anti-dilutive (in thousands):

	Three Months Ended July 31,		Six Months Ended July 31,	
	2016	2017	2016	2017
Stock options to purchase common stock	65,567	53,878	66,974	54,864
Restricted stock units	4,682	15,710	3,046	13,759
Early exercised stock options	2,446	279	2,555	333
Employee stock purchase plan	953	898	953	898
Total	73,648	70,765	73,528	69,854

Note 9. Income Taxes

Our provision for income taxes was primarily due to taxes on international operations and state income taxes. The difference between the provision for income taxes that would be derived by applying the statutory rate to our loss before income taxes and the provision for income taxes recorded was primarily attributable to changes in our valuation allowance, non-deductible stock-based compensation expense and the tax rate differential between the U.S. and foreign countries.

As of July 31, 2017, there were no material changes to either the nature or the amounts of the uncertain tax positions previously determined for the year ended January 31, 2017.

Note 10. Segment Information

Our chief operating decision maker is a group which is comprised of our Chief Executive Officer, our Chief Financial Officer, and our President. This group reviews financial information presented on a consolidated basis for purposes of allocating resources and evaluating financial performance. We have one business activity and there are no segment managers who are held accountable for operations or operating results. Accordingly, we have a single reportable segment.

The following table sets forth revenue by geographic area based on the billing address of our customers (in thousands):

	Three Months Ended July 31,		Six Months Ended July 31,	
	2016	2017	2016	2017
United States	\$ 122,103	\$ 165,466	\$ 233,330	\$ 311,960
Rest of the world	41,111	58,995	69,831	95,132
Total revenue	\$ 163,214	\$ 224,461	\$ 303,161	\$ 407,092

Long-lived assets by geographic area are summarized as follows (in thousands):

	As of January 31, 2017	As of July 31, 2017
United States	\$ 78,692	\$ 78,207
Rest of the world	3,003	3,643
Total long-lived assets	\$ 81,695	\$ 81,850

Note 11. Subsequent Events

PURE STORAGE, INC.**Notes to Condensed Consolidated Financial Statements (Unaudited)**

In August 2017, we entered into a seven -year term operating lease for approximately 45,831 square feet of office space in Mountain View, California with total rent obligation of \$31.6 million . In connection with the lease, we have issued a letter of credit of \$2.6 million .

On August 22, 2017, Scott Dietzen resigned from his position as chief executive officer and was appointed as the chairman of our board of directors. On August 22, 2017, our board of directors appointed Charles H. Giancarlo, as the new chief executive officer and a member on our board of directors, effective immediately.

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

The following discussion and analysis of our financial condition, results of operations and cash flows should be read in conjunction with the (1) unaudited condensed consolidated financial statements and the related notes thereto included elsewhere in this Quarterly Report on Form 10-Q, and (2) the audited consolidated financial statements and notes thereto and management's discussion and analysis of financial condition and results of operations included in our Annual Report on Form 10-K for the year ended January 31, 2017. This Quarterly Report on Form 10-Q contains "forward-looking statements" within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act. These statements are often identified by the use of words such as "may," "will," "expect," "believe," "anticipate," "intend," "could," "estimate," or "continue," and similar expressions or variations. Such forward-looking statements are subject to risks, uncertainties and other factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified herein, and those discussed in the section titled "Risk Factors", set forth in Part II, Item 1A of this Form 10-Q and in our other SEC filings. We disclaim any obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements. Our fiscal year end is January 31.

Overview

We are building the data platform for the cloud era. As the demand for data and the need for real-time analytics increase, we are focused on delivering software-defined all-flash solutions that are uniquely fast and cloud-capable for customers, enabling customers to put data to work for their businesses. Our innovative data platform replaces storage systems designed for mechanical disk with all-flash systems optimized end-to-end for solid-state memory. At the same time, our innovative business model replaces the traditional forklift upgrade cycle with an *Evergreen Storage* model of hardware and software innovation, support and maintenance.

We were incorporated in 2009 with a vision to define the next generation of enterprise storage by pioneering the all-flash array category and innovating a customer-centric business model. We deliver our platform as our flash-optimized software and modular and scalable all-flash hardware in our *FlashArray* and *FlashBlade* products, inclusive of our *Purity Operating Environment (Purity OE)* software, our *Pure1* cloud-based software, and *FlashStack* , our joint converged infrastructure solution with Cisco. This entire platform is powered by innovative software which can be managed from anywhere and supported by our *Evergreen Storage* business model.

Since launching in May 2012, our customer base has grown to over 3,700 customers, including over 25% of the Fortune 500. Our customers include large and mid-size organizations across a diverse set of industry verticals, including cloud-based software and service providers, consumer web, education, energy, financial services, governments, healthcare, manufacturing, media, retail, automobile, and telecommunications. We define a customer as an end user that purchases our products and services either from one of our channel partners or from us directly. No customer represented over 10% of revenue for the three and six months ended July 31, 2016 and 2017 .

We have grown rapidly in recent periods, with revenue for the three months ended July 31, 2016 and 2017 of \$ 163.2 million and \$224.5 million , representing year-over-year growth of 38% . For the six months ended July 31, 2016 and 2017 , our revenue was \$303.2 million and \$407.1 million , representing year-over-year revenue growth rate of 34% . We expect that our revenue growth rate may continue to decline as our business scales, even if our revenue continues to grow in absolute terms. We have continued to make significant expenditures and investments, including in personnel-related costs, sales and marketing, infrastructure and operations, and have incurred net losses in each period since our inception, including net losses of \$59.6 million and \$61.7 million for the three months ended July 31, 2016 and 2017 , and \$123.3 million and \$124.1 million for the six months ended July 31, 2016 and 2017 .

Since our founding, we have invested heavily in growing our business. Our headcount increased from over 1,700 employees as of January 31, 2017, and to over 1,900 employees as of July 31, 2017 . We intend to continue to invest in our research and development organization to extend our technology leadership, enhance the functionality of our existing products and introduce new products. By investing in research and development, we believe we will be well positioned to continue our rapid growth and take advantage of our large market opportunity.

We also intend to continue to invest and expand our sales and marketing functions and channel programs, including expanding our global network of channel partners and carrying out associated marketing activities in key geographies. By investing in sales and technical training, demand generation and partner programs, we believe we can enable many of our partners to independently identify, qualify, sell and upgrade customers, with limited involvement from us.

In addition, we intend to expand and continue to invest in our international operations, which we believe will be an important factor in our continued growth. However, our international operations are relatively new and we have limited experience operating in foreign jurisdictions. Our revenue generated from customers outside of the United States was 23% of our total revenue for both the year ended January 31, 2017 and the six months ended July 31, 2017 .

As a result of our strategy to increase our investments in research and development, sales, marketing, support and international expansion, we expect to continue to incur operating losses and negative cash flows from operations in the near future and may require additional capital resources to execute strategic initiatives to grow our business.

Recent Development

On August 22, 2017, Scott Dietzen resigned from his position as chief executive officer and was appointed as the chairman of our board of directors. On August 22, 2017, our board of directors appointed Charles H. Giancarlo, as the new chief executive officer and a member on our board of directors, effective immediately.

In April 2017, we launched *FlashArray//X* , our first all-NVMe, enterprise-class all-flash array, on directed basis. *FlashArray//X* is targeted to be generally available in the second half of the fiscal year ending on January 31, 2018.

Our Business Model

We sell our data platform predominantly through a high touch, channel-fulfilled model. Our sales force works collaboratively with our channel partners and is responsible for large account penetration, global account coordination, and overall market development. Our channel partners help market and sell our products, typically with assistance from our sales force. This joint sales approach provides us with the benefit of direct relationships with substantially all of our customers and expands our reach through the relationships of our channel partners.

Our channel partners typically place orders with us upon receiving an order from a customer and do not stock inventory. Our sales organization is supported by systems engineers with deep technical expertise and responsibility for pre-sales technical support and engineering for our customers. We support our channel partners through product education and sales and support training. We intend to continue to invest in the channel to add more partners and to expand our reach to customers through our channel partners' relationships. No channel partner represented over 10% of revenue for the six months ended July 31, 2016 . One channel partner represented over 10% of revenue for the six months ended July 31, 2017 .

Our business model enables customers to broadly adopt flash for a wide variety of workloads in their data center, with some of our most innovative customers adopting all-flash data centers. We do not charge separately for software, meaning that when a customer buys a *FlashArray* or *FlashBlade* , all software functionality is included in the base purchase price, and the customer is entitled to updates and new features as long as the customer maintains an active maintenance and support agreement. Product revenue is recognized at the time title and risk of loss have transferred. Support revenue is recognized ratably over the term of the related maintenance and support agreement, generally ranging from 1 to 6 years. By keeping our business model simple and efficient, we allow customers to buy more products and expand their footprint more easily while allowing us to reduce our sales and marketing costs.

To deliver on the next level of operational simplicity and support excellence, we designed *Pure1* , our integrated cloud-based management and support. *Pure1* enables our customers, support staff and partners to collaborate to achieve the best customer experience and is included with an active maintenance and support agreement. In addition,

our *Evergreen Storage* program provides our customers who continually maintain active and eligible maintenance and support for three years with an included controller refresh with each additional three year maintenance and support renewal. In this way, our customers improve and extend the service life of their arrays, we reduce our cost of support by keeping the array modern and we encourage capacity expansion. In accordance with multiple-element arrangement accounting guidance, we recognize the allocated revenue of the controllers and expense the related cost in the period in which we ship these controllers.

The combination of our high-performance, all-flash products, our exceptional support and our innovative business model has had a substantial impact on customer success and loyalty and are strong drivers of both initial purchase and additional purchases of our products. Of all the customers that have been with us for at least 12 months as of July 31, 2017, our top 25 customers on average spent approximately \$12 on new product purchases for every \$1 of initial product purchase, in the first 18 months following their initial purchase.

Trends in Our Business and Industry

Demand for Data in the Cloud Era

In today's digital economy, we believe that data is key. Data is the strategic core that enables competitiveness and differentiation for businesses in the cloud era -- collecting vast amounts of data, analyzing it rapidly, discovering new insights, and ultimately delivering new innovations and experiences otherwise impossible without data. We continue to make significant investments in our business to develop and deliver a data platform to support today and tomorrow's volume and velocity of data and to ensure the performance required for new data-driven applications, while substantially reducing costs and complexity for our customers. Our ability to deliver new and enhanced products will be a key factor in capturing mindshare with our target customers to become their data platform of choice.

Adoption of All-Flash Storage Systems

Organizations are increasingly replacing traditional disk-based systems with all-flash storage systems, due to their higher performance, reliability and efficiency. Flash is expected to penetrate the data center at a rapid rate, and our success depends on the adoption of all-flash storage systems. To the extent more organizations recognize the benefits of all-flash storage and the adoption of all-flash storage increases, our target customer base will expand, and demand for all-flash storage will rise.

Adding New Customers and Expanding Sales to Our Existing Customer Base

We believe that all-flash storage market is still in the early stages of adoption. In order to capture long-term strategic opportunities, we intend to continue to target new customers, including large enterprises, service providers and government organizations, by continuing to invest in our field sales force and extending our relationships with key channel partners. We also expect that a substantial portion of our future sales will continue to be sales to existing customers, including expansion of existing arrays.

Seasonality in our Business Operations

Consistent with the seasonality of enterprise IT as a whole, we generally experience the lowest demand for our products and services in the first quarter of our fiscal year and the greatest demand for our products and services in the last quarter of our fiscal year. Furthermore, we typically focus investments into our sales organization, along with significant product launches, in the first half of our fiscal year. As a result, we expect that our business and results of operations will fluctuate from quarter to quarter, reflecting seasonally softer revenue and operating margin in the first half of our fiscal year, followed by a stronger second half, the relative impact of which will grow as we operate at a larger scale.

Components of Results of Operations

Revenue

We derive revenue from the sale of our storage products and support services. Provided that all other revenue recognition criteria have been met, we typically recognize product revenue upon shipment, as title and risk of loss are transferred to our channel partners at that time. Products are typically shipped directly by us to customers, and our

channel partners do not stock our inventory. We expect our product revenue may vary from period to period based on, among other things, the timing and size of orders and delivery of products and the impact of significant transactions.

We provide our support services pursuant to maintenance and support agreements, which involve customer support, hardware maintenance and software upgrades for a period of generally 1 to 6 years. We recognize revenue from maintenance and support agreements ratably over the contractual service period. We expect our support revenue to increase as we add new customers and our existing customers renew maintenance and support agreements.

Cost of Revenue

Cost of product revenue primarily consists of costs paid to our third-party contract manufacturers, which includes the costs of our components, and personnel costs associated with our manufacturing operations. Personnel costs consist of salaries, bonuses and stock-based compensation expense. Our cost of product revenue also includes freight, allocated overhead costs and inventory write-offs. Allocated overhead costs consist of certain employee benefits and facilities related costs. We expect our cost of product revenue to increase in absolute dollars, as our product revenue increases.

Cost of support revenue includes personnel costs associated with our customer support organization and allocated overhead costs. Cost of support revenue also includes parts replacement costs. We expect our cost of support revenue to increase in absolute dollars, as our support revenue increases.

Operating Expenses

Our operating expenses consist of research and development, sales and marketing, and general and administrative expenses. Salaries and personnel-related costs, including stock-based compensation expense, are the most significant component of each category of operating expenses. Operating expenses also include allocated overhead costs for certain employee benefits and facilities related costs.

Research and Development . Research and development expense consists primarily of employee compensation and related expenses, prototype expenses, depreciation associated with assets acquired for research and development, third-party engineering and contractor support costs, as well as allocated overhead. We expect our research and development expense to increase in absolute dollars and to decrease as a percentage of revenue, as we continue to invest in new and existing products and build upon our technology leadership.

Sales and Marketing . Sales and marketing expense consists primarily of employee compensation and related expenses, sales commissions, marketing programs, travel and entertainment expenses, as well as allocated overhead. Marketing programs consist of advertising, events, corporate communications and brand-building activities. We expect our sales and marketing expense to increase in absolute dollars and to decrease as a percentage of revenue, as we expand our sales force and increase our marketing resources, expand into new markets and further develop our channel program.

General and Administrative . General and administrative expense consists primarily of compensation and related expenses for administrative functions including finance, legal, human resources and fees for third-party professional services, as well as allocated overhead. We expect our general and administrative expense to increase in absolute dollars and to decrease as a percentage of revenue, as we continue to invest in the growth of our business.

Other Income (Expense), Net

Other income (expense), net consists primarily of interest income earned on cash, cash equivalents and marketable securities and gains and losses from foreign currency transactions.

Provision for Income Taxes

Provision for income taxes consists primarily of income taxes in certain foreign jurisdictions in which we conduct business and state income taxes in the United States. We have recorded no U.S. federal income tax and provided a full valuation allowance for U.S. deferred tax assets, which includes net operating loss, carryforwards and tax credits related primarily to research and development. We expect to maintain this full valuation allowance for the foreseeable future as it is more likely than not that the assets will not be realized based on our history of losses.

Results of Operations

The following tables set forth our results of operations for the periods presented in dollars and as a percentage of total revenue (in thousands):

	Three Months Ended July 31,		Six Months Ended July 31,	
	2016	2017	2016	2017
(unaudited)				
Consolidated Statements of Operations Data:				
Revenue:				
Product	\$ 130,920	\$ 175,013	\$ 242,658	\$ 313,438
Support	32,294	49,448	60,503	93,654
Total revenue	163,214	224,461	303,161	407,092
Cost of revenue:				
Product ⁽¹⁾	42,847	57,252	76,893	103,897
Support ⁽¹⁾	14,000	19,199	26,934	36,102
Total cost of revenue	56,847	76,451	103,827	139,999
Gross profit	106,367	148,010	199,334	267,093
Operating expenses:				
Research and development ⁽¹⁾	58,635	69,361	111,573	134,789
Sales and marketing ⁽¹⁾	87,583	120,633	170,681	217,597
General and administrative ⁽¹⁾	19,630	22,162	41,211	42,258
Total operating expenses	165,848	212,156	323,465	394,644
Loss from operations	(59,481)	(64,146)	(124,131)	(127,551)
Other income, net	37	3,266	1,319	5,261
Loss before provision for income taxes	(59,444)	(60,880)	(122,812)	(122,290)
Provision for income taxes	106	821	526	1,785
Net loss	\$ (59,550)	\$ (61,701)	\$ (123,338)	\$ (124,075)

(1) Includes stock-based compensation expense as follows:

	Three Months Ended July 31,		Six Months Ended July 31,	
	2016	2017	2016	2017
(unaudited)				
Cost of revenue—product	\$ 181	\$ 358	\$ 287	\$ 755
Cost of revenue—support	1,712	2,245	2,804	4,019
Research and development	13,976	17,971	25,634	33,559
Sales and marketing	8,732	11,439	16,251	22,065
General and administrative	3,295	4,825	5,918	8,659
Total stock-based compensation expense	\$ 27,896	\$ 36,838	\$ 50,894	\$ 69,057

	Three Months Ended July 31,		Six Months Ended July 31,	
	2016	2017	2016	2017
(unaudited)				
Condensed Consolidated Statements of Operations				
Data:				
Revenue:				
Product	80 %	78 %	80 %	77 %
Support	20	22	20	23
Total revenue	100	100	100	100
Cost of revenue:				
Product	26	25	25	25
Support	9	9	9	9
Total cost of revenue	35	34	34	34
Gross profit	65	66	66	66
Operating expenses:				
Research and development	36	31	37	33
Sales and marketing	54	54	56	54
General and administrative	12	10	14	10
Total operating expenses	102	95	107	97
Loss from operations	(37)	(29)	(41)	(31)
Other income (expense), net	—	2	—	1
Loss before provision for income taxes	(37)	(27)	(41)	(30)
Provision for income taxes	—	—	—	—
Net loss	(37)%	(27)%	(41)%	(30)%

Revenue

	Three Months Ended July 31,		Change		Six Months Ended July 31,		Change	
	2016	2017	\$	%	2016	2017	\$	%
(dollars in thousands, unaudited)								
Product revenue	\$ 130,920	\$ 175,013	\$ 44,093	34%	\$ 242,658	\$ 313,438	\$ 70,780	29%
Support revenue	32,294	49,448	17,154	53%	60,503	93,654	33,151	55%
Total revenue	\$ 163,214	\$ 224,461	\$ 61,247	38%	\$ 303,161	\$ 407,092	\$ 103,931	34%

Total revenue increased by \$61.2 million , or 38% , during the three months ended July 31, 2017 compared to the three months ended July 31, 2016 and increased by \$103.9 million , or 34% , during the six months ended July 31, 2017 compared to the six months ended July 31, 2016 . The increase in product revenue was primarily driven by repeat purchases from existing customers and a growing number of new customers. The number of customers grew from over 2,300 as of July 31, 2016 to over 3,700 as of July 31, 2017 . The increase in support revenue was driven primarily by an increase in maintenance and support agreements sold with increased product sales, as well as increased recognition of deferred support revenue.

Cost of Revenue and Gross Margin

	Three Months Ended July 31,		Change		Six Months Ended July 31,		Change	
	2016	2017	\$	%	2016	2017	\$	%
(dollars in thousands, unaudited)								
Product cost of revenue	\$ 42,847	\$ 57,252	\$ 14,405	34%	\$ 76,893	\$ 103,897	\$ 27,004	35%
Support cost of revenue	14,000	19,199	5,199	37%	26,934	36,102	9,168	34%
Total cost of revenue	\$ 56,847	\$ 76,451	\$ 19,604	34%	\$ 103,827	\$ 139,999	\$ 36,172	35%
Product gross margin	67%	67%			68%	67%		
Support gross margin	57%	61%			55%	61%		
Total gross margin	65%	66%			66%	66%		

Cost of revenue increased by \$19.6 million , or 34% , during the three months ended July 31, 2017 compared to the three months ended July 31, 2016 and increased by \$36.2 million , or 35% , during the six months ended July 31, 2017 compared to the six months ended July 31, 2016 . The increase in product cost of revenue was primarily driven by increased product sales and, to a lesser extent, by the increased costs in our manufacturing operations, including increased personnel costs associated with increased headcount. The increase in support cost of revenue was primarily attributable to costs in our customer support organization as we continue to expand. These costs are primarily driven by increased personnel costs associated with increased headcount and an increase in parts replacement associated with a higher number of maintenance and support agreements. Total headcount in these functions increased 50% from July 31, 2016 to July 31, 2017 .

Total gross margin increased from 65% during the three months ended July 31, 2016 to 66% during the three months ended July 31, 2017 , and remained constant at 66% during the six months ended July 31, 2016 and 2017 . Product gross margin decreased 1 point from the six months ended July 31, 2016 to the six months ended July 31, 2017 , primarily driven by both pricing and product mix dynamics including the introduction of our *FlashBlade* products. Support gross margin increase d 4 and 6 points from the three and six months ended July 31, 2016 to the three and six months ended July 31, 2017 , primarily attributed to increased recognition of deferred support revenue resulting from the increase in our customer base, as well as operational efficiencies in our support organization.

Operating Expenses

Research and Development

	Three Months Ended July 31,		Change		Six Months Ended July 31,		Change	
	2016	2017	\$	%	2016	2017	\$	%
(dollars in thousands, unaudited)								
Research and development	\$ 58,635	\$ 69,361	\$ 10,726	18%	\$ 111,573	\$ 134,789	\$ 23,216	21%

Research and development expense increased by \$10.7 million , or 18% , during the three months ended July 31, 2017 compared to the three months ended July 31, 2016 , as we continued to develop new and enhanced product offerings including our *FlashBlade* and *FlashArray//X* products. The increase was primarily driven by an increase of \$8.3 million in salary and related costs, including an increase of \$4.0 million in stock-based compensation expense, as headcount increased by 7% from July 31, 2016 to July 31, 2017 . The remainder of the increase was primarily attributable to \$1.7 million in depreciation expense on our test equipment.

Research and development expense increased by \$23.2 million , or 21% , during the six months ended July 31, 2017 compared to the six months ended July 31, 2016 , as we continued to develop new and enhanced product offerings including our *FlashBlade* and *FlashArray//X* products. The increase was primarily driven by an increase of \$19.2 million in salary and related costs, including an increase of \$7.9 million in stock-based compensation expense, as headcount increased by 7% from July 31, 2016 to July 31, 2017 . The remainder of the increase was primarily attributable to \$4.2 million in depreciation expense on our test equipment.

Sales and Marketing

	Three Months Ended July 31,		Change		Six Months Ended July 31,		Change	
	2016	2017	\$	%	2016	2017	\$	%
(dollars in thousands, unaudited)								
Sales and marketing	\$ 87,583	\$ 120,633	\$ 33,050	38%	\$ 170,681	\$ 217,597	\$ 46,916	27%

Sales and marketing expense increased by \$33.1 million , or 38% , during the three months ended July 31, 2017 compared to the three months ended July 31, 2016 , as we grew our sales force and expanded our geographic footprint. The increase was primarily driven by an increase of \$19.2 million in salary and related costs, including an increase of \$5.9 million in sales commission expense and an increase of \$2.7 million in stock-based compensation expense, as headcount increased by 20% from July 31, 2016 to July 31, 2017 . The remainder of the increase was primarily attributable to \$8.1 million in sales conferences, marketing and brand awareness program costs, including expenses related to our annual Pure //Accelerate conference in June 2017, \$2.0 million in allocated overhead costs, \$1.8 million in travel and related costs and \$1.4 million in outside services costs.

Sales and marketing expense increased by \$46.9 million , or 27% , during the six months ended July 31, 2017 compared to the six months ended July 31, 2016 , as we grew our sales force and expanded our geographic footprint. The increase was primarily driven by an increase of \$33.3 million in salary and related costs, including an increase of \$8.7 million in sales commission expense and an increase of \$5.8 million in stock-based compensation expense, as headcount increased by 20% from July 31, 2016 to July 31, 2017 . The remainder of the increase was primarily attributable to \$4.5 million in sales conference, marketing and brand awareness program costs, including expenses related to our annual Pure //Accelerate conference in June 2017, \$3.6 million in allocated overhead costs, \$3.0 million in outside services costs, and \$1.8 million in travel and related costs.

General and Administrative

	Three Months Ended July 31,		Change		Six Months Ended July 31,		Change	
	2016	2017	\$	%	2016	2017	\$	%
(dollars in thousands, unaudited)								
General and administrative	\$ 19,630	\$ 22,162	\$ 2,532	13%	\$ 41,211	\$ 42,258	\$ 1,047	3%

General and administrative expense increased by \$2.5 million , or 13% , during the three months ended July 31, 2017 compared to the three months ended July 31, 2016 . The increase was primarily due to a \$3.4 million increase in salary and related costs, including an increase of \$1.5 million in stock-based compensation expense, as we increased our general and administrative headcount by 30% from July 31, 2016 to July 31, 2017 , which was partially offset by a \$1.1 million decrease in legal and other fees.

General and administrative expense increased by \$1.0 million , or 3% , during the six months ended July 31, 2017 compared to the six months ended July 31, 2016 . The increase was primarily due to a \$6.5 million increase in salary and related costs, including an increase of \$2.7 million in stock-based compensation expense as we increased our general and administrative headcount by 30% from July 31, 2016 to July 31, 2017 , a \$2.6 million increase in consulting, accounting and audit fees, and a \$1.0 million increase in office and related costs, partially offset by a \$8.4 million decrease in legal and other fees.

Other Income, Net

	Three Months Ended July 31,		Change	Six Months Ended July 31,		Change
	2016	2017		2016	2017	
(dollars in thousands, unaudited)						
Other income, net	\$ 37	\$ 3,266	\$ 3,229	\$ 1,319	\$ 5,261	\$ 3,942

The increases in other income, net during the three and six months ended July 31, 2017 compared to the three and six months ended July 31, 2016 were driven by increases in net gains from foreign currency transactions and increases in interest income earned on our cash, cash equivalents and marketable securities.

Provision for Income Taxes

	Three Months Ended July 31,		Change	Six Months Ended July 31,		Change
	2016	2017		2016	2017	
(dollars in thousands, unaudited)						
Provision for income taxes	\$ 106	\$ 821	\$ 715	\$ 526	\$ 1,785	\$ 1,259

The increase in provision for income taxes during the six months ended July 31, 2017 compared to the six months ended July 31, 2016 was driven by less excess tax benefit related to our employee stock-based activities.

Liquidity and Capital Resources

As of July 31, 2017, we had cash, cash equivalents and marketable securities of \$523.0 million. Our cash and cash equivalents primarily consist of bank deposits and money market accounts. Our marketable securities consist of highly rated debt instruments of the U.S. government and its agencies, debt instruments of highly rated corporations and debt instruments issued by foreign governments. We have generated significant operating losses and negative cash flows from operations as reflected in our accumulated deficit of \$926.6 million. We expect to continue to incur operating losses and negative cash flows from operations in the near future and require additional capital resources to execute strategic initiatives to grow our business.

We believe our existing cash, cash equivalents and marketable securities will be sufficient to fund our operating and capital needs for at least the next 12 months. Our future capital requirements will depend on many factors including our growth rate, the timing and extent of spending to support development efforts, the expansion of sales and marketing and international operation activities, the timing of new product introductions, and the continuing market acceptance of our products and services. We may in the future enter into arrangements to acquire or invest in complementary businesses, services and technologies, including intellectual property rights. We may be required to seek additional equity or debt financing. In the event that additional financing is required from outside sources, we may not be able to raise it on terms acceptable to us or at all. If we are unable to raise additional capital when desired, our business, operating results and financial condition would be adversely affected.

As of January 31, 2017 and July 31, 2017, we had letters of credit in the aggregate amount of \$7.7 million, in connection with our facility leases. The letters of credit are collateralized by restricted cash in the same amount and mature at various dates through June 2024.

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

	Six Months Ended July 31,	
	2016	2017
Net cash used in operating activities	\$ (4,557)	\$ (14,492)
Net cash used in investing activities	\$ (415,815)	\$ (18,248)
Net cash provided by financing activities	\$ 21,448	\$ 20,959

Operating Activities

Net cash used in operating activities during the six months ended July 31, 2017 was \$14.5 million , which resulted primarily from a net loss of \$124.1 million , partially offset by non-cash charges for stock-based compensation expense of \$69.1 million , depreciation and amortization of \$30.0 million , and net cash inflows of \$9.7 million from changes in operating assets and liabilities. The net cash inflows from changes in operating assets and liabilities were primarily the result of a \$24.5 million increase in deferred revenue, partially offset by a \$10.5 million increase in inventory and a \$4.6 million increase in deferred commission. The increase s in deferred revenue and deferred commission were primarily due to new sales order growth during the six months ended July 31, 2017 . The increase in inventory was primarily as a result of increased purchases to manage component costs and availability to meet higher demand for our products.

Net cash provided by operating activities during the six months ended July 31, 2016 was \$4.6 million, which resulted from a net loss of \$123.3 million, partially offset by non-cash charges for stock-based compensation expense of \$50.9 million, \$22.3 million for depreciation and amortization and net cash inflows of \$45.1 million from changes in operating assets and liabilities. The net cash inflows from changes in operating assets and liabilities were primarily the result of a \$41.1 million increase in deferred revenue, a \$8.7 million increase in accrued compensation and other liabilities, a \$6.6 million decrease in accounts receivable and a decrease in deferred commissions of \$1.9 million, partially offset by a \$10.0 million decrease in accounts payable and a \$2.4 million increase in inventory. The increase in deferred revenue was primarily due to new sales order growth during the six months ended July 31, 2016. The decreases in accounts receivable and accounts payable and the increase in accrued compensation and other liabilities were primarily attributable to the timing of collections and payments.

Investing Activities

Net cash used in investing activities during the six months ended July 31, 2017 of \$18.2 million resulted from capital expenditures of \$30.1 million , partially offset by net sales and maturities of marketable securities of \$11.9 million .

Net cash used in investing activities during the six months ended July 31, 2016 of \$415.8 million resulted from net purchases of marketable securities of \$363.1 million, capital expenditures of \$46.1 million, an increase in restricted cash of \$5.6 million related to a vendor credit card program and security deposit for office space, as well as the purchase of a portfolio of technology patents for \$1.0 million.

Financing Activities

Net cash provided by financing activities during the six months ended July 31, 2017 of \$21.0 million was primarily attributed to \$14.2 million in proceeds from issuance of common stock under employee stock purchase plan (ESPP) and \$6.8 million in proceeds from the exercise of stock options.

Net cash provided by financing activities during the six months ended July 31, 2016 of \$21.4 million during the six months ended July 31, 2016 was primarily due to \$15.1 million in proceeds from issuance of common stock under ESPP and \$6.4 million in proceeds from the exercise of stock options.

Contractual Obligations and Commitments

During the six months ended July 31, 2017 , we extended the lease term of an existing office facility with total additional lease obligations of approximately \$2.0 million with the lease expiring through March 2019.

In August 2017, we entered into a seven-year term operating lease for approximately 45,831 square feet of office space in Mountain View, California with a total base rent obligation of \$31.6 million. In connection with the lease, we have issued a letter of credit of \$2.6 million.

Critical Accounting Policies and Estimates

Our financial statements are prepared in accordance with U.S. generally accepted accounting principles (GAAP). The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, expenses, and related disclosures. We evaluate our estimates and assumptions on an ongoing basis. Our estimates are based on historical experience and various other assumptions that we believe to be reasonable under the circumstances. Our actual results could differ from these estimates.

Please see Note 2 of Part I, Item 1 of this Quarterly Report on Form 10-Q for the summary of significant accounting policies. In addition, please see “Critical Accounting Policies and Estimates” in our latest 10-K. There have been no material changes to our critical accounting policies and estimates since our 10-K filed on March 29, 2017.

Available Information

Our website is located at www.purestorage.com, and our investor relations website is located at <http://investor.purestorage.com>. The following filings will be available through our investor relations website after we file them with the SEC: Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, and our Proxy Statements for our annual meetings of stockholders, and are also available for download free of charge. We will also provide a link to the section of the SEC's website at www.sec.gov that has all of our public filings, including Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, all amendments to those reports, our Proxy Statements, and other ownership related filings. Further, a copy of this Quarterly Report on Form 10-Q is located at the SEC's Public Reference Room at 100 F Street, NE, Room 1580, Washington, D.C. 20549. Information on the operation of the Public Reference Room can be obtained by calling the SEC at 1-800-SEC-0330.

We webcast our earnings calls and certain events we participate in or host with members of the investment community on our investor relations website. Additionally, we provide notifications of news or announcements regarding our financial performance, including SEC filings, investor events, press and earnings releases, social media accounts (Twitter, Facebook and LinkedIn), and blogs as part of our investor relations website. Investors and others can receive notifications of new information posted on our investor relations website in real time by signing up for email alerts and RSS feeds. Further corporate governance information, including our certificate of incorporation, bylaws, governance guidelines, board committee charters, and code of conduct, is also available on our investor relations website under the heading “Corporate Governance.” The content of our websites are not incorporated by reference into this Quarterly Report on Form 10-Q or in any other report or document we file with the SEC, and any references to our websites are intended to be inactive textual references only.

Item 3. Quantitative and Qualitative Disclosures about Market Risk.

We have operations both within the United States and internationally, and we are exposed to market risk in the ordinary course of our business.

Interest Rate Risk

Our cash, cash equivalents and marketable securities primarily consist of bank deposits and money market accounts, U.S. government notes and U.S. agency notes, and highly rated corporate debt. As of July 31, 2017, we had cash, cash equivalents and marketable securities of \$523.0 million. The carrying amount of our cash equivalents reasonably approximates fair value, due to the short maturities of these instruments. The primary objectives of our investment activities are the preservation of capital, the fulfillment of liquidity needs and the fiduciary control of cash and investments. We do not enter into investments for trading or speculative purposes. Our investments are exposed to market risk due to a fluctuation in interest rates, which may affect our interest income and the fair value of our investments.

We considered the historical volatility of short-term interest rates and determined that it was reasonably possible that an adverse change of 100 basis points could be experienced in the near term. A hypothetical 1.00% (100 basis

points) increase in interest rates would have resulted in a decrease in the fair value of our marketable securities of approximately \$3.6 million as of July 31, 2017 .

Foreign Currency Exchange Risk

Our sales contracts are primarily denominated in U.S. dollars with a small number of contracts denominated in foreign currencies. A portion of our operating expenses are incurred outside the United States and denominated in foreign currencies and are subject to fluctuations due to changes in foreign currency exchange rates, particularly changes in the British pound and Euro. Additionally, fluctuations in foreign currency exchange rates may cause us to recognize transaction gains and losses in our statement of operations. Given the impact of foreign currency exchange rates has not been material to our historical operating results, we have not entered into any derivative or hedging transactions, but we may do so in the future if our exposure to foreign currency exchange should become more significant.

We considered the historical trends in currency exchange rates and determined that it was reasonably possible that adverse changes in exchange rates of 10% for all currencies could be experienced in the near term. These reasonably possible adverse changes in exchange rates of 10% were applied to total monetary assets and liabilities denominated in currencies other than U.S. dollar at July 31, 2017 to compute the adverse impact these changes would have had on our loss before income taxes in the near term. These changes would have resulted in an adverse impact on loss before income taxes of approximately \$6.7 million as of July 31, 2017 .

Item 4. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer (CEO) and Chief Financial Officer (CFO), evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act), as of the end of the period covered by this report. Based on such evaluation, our CEO and CFO concluded that, as of July 31, 2017 , our disclosure controls and procedures were designed at a reasonable assurance level and were effective to provide reasonable assurance that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our CEO and CFO, as appropriate, to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting identified in connection with the evaluation required by Rules 13a-15(d) or 15d-15(d) of the Exchange Act that occurred during the quarter ended July 31, 2017 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Limitations on Effectiveness of Controls

In designing and evaluating the disclosure controls and procedures and internal control over financial reporting, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures and internal control over financial reporting must reflect the fact that there are resource constraints and that management is required to apply judgment in evaluating the benefits of possible controls and procedures relative to their costs.

PART II—OTHER INFORMATION

Item 1. Legal Proceedings.

The information set forth under the "Legal Matters" subheading in Note 5. Commitments and Contingencies of Notes to Condensed Consolidated Financial Statements in Part I, Item 1 of this Quarterly Report on Form 10-Q is incorporated herein by reference.

In addition, we may from time to time, be involved in various legal proceedings arising from the normal course of business, and an unfavorable resolution of any of these matters could materially affect our future results of operations, cash flows or financial position.

Item 1A. Risk Factors.

Investing in our Class A common stock involves a high degree of risk. Investors should carefully consider the risks and uncertainties described below, together with all of the other information contained in this report, including our consolidated financial statements and the related notes appearing in this quarterly report, before deciding to invest in our Class A common stock. If any of the following risks actually occur, it could harm our business, prospects, operating results and financial condition. In such event, the trading price of our Class A common stock could decline and investors might lose all or part of their investment.

Risks Related to Our Business and Industry

We have experienced rapid growth in recent periods, and we may not be able to sustain or manage future growth effectively.

We have significantly expanded our overall business, customer base, headcount, channel partner relationships and operations in recent periods, and we anticipate that we will continue to expand and may experience significant growth in future periods. For example, from January 31, 2016 to January 31, 2017, our headcount increased from over 1,300 to over 1,700 employees, and to over 1,900 employees as of July 31, 2017. Our future operating results will depend to a large extent on our ability to successfully sustain our growth and manage our anticipated expansion. To sustain and manage our growth successfully, we believe that we must, among other things, effectively:

- maintain and extend our product leadership;
- recruit, hire, train and manage additional personnel;
- maintain and further develop our channel partner relationships;
- enhance and expand our distribution and supply chain infrastructure;
- expand our support capabilities;
- forecast and control expenses;
- enhance and expand our international operations; and
- implement, improve and maintain our internal systems, procedures and controls.

We expect that our future growth will continue to place a significant strain on our managerial, administrative, operational, financial and other resources. We will incur costs associated with this future growth prior to realizing the anticipated benefits, and the return on these investments may be lower, may develop more slowly than we expect or may never materialize. If we are unable to sustain or manage our growth effectively, we may not be able to take advantage of market opportunities or develop new products or enhancements to existing products in a timely manner, and we may fail to satisfy customers' expectations, maintain product quality, execute on our business plan or adequately respond to competitive pressures, each of which could adversely impact our growth and affect our business and operating results.

We intend to continue focusing on revenue growth and increasing our market penetration and international presence by investing heavily in our business and this may put pressure on near-term profitability.

Our strategy is to continue with our investments in marketing, sales, support and research and development. We believe our decision to continue investing heavily in our business will be critical to our future success and to meet our growth objectives. We anticipate that our operating costs and expenses will continue to increase in absolute terms.

In addition, we expect to continue incurring significant legal, accounting and other expenses in order to operate effectively as a public company at our scale. Even if we achieve or maintain significant revenue growth, we expect to continue to experience losses, forgoing near-term profitability.

We have not achieved profitability for any year since our inception. We incurred a net loss of \$245.1 million for the year ended January 31, 2017 and \$124.1 million for the six months ended July 31, 2017, and we had an accumulated deficit of \$802.5 million as of January 31, 2017 and \$926.6 million as of July 31, 2017. Our operating expenses largely are based on anticipated revenue, and a high percentage of our expenses are, and will continue to be, fixed in the short term. If we fail to adequately increase revenue and manage costs, we may not achieve or maintain profitability in the future. As a result, our business could be harmed and our operating results could suffer.

We have a limited operating history, which makes our future operating results difficult to predict.

We were founded in October 2009, but have generated substantially all of our revenue in our last three fiscal years. We have a limited operating history in an industry characterized by rapid technological change, changing customer needs, evolving industry standards and frequent introductions of new products and services. Our limited operating history makes it difficult to evaluate our current business and our future prospects, including our ability to plan for and model future growth. All of these factors make our future operating results difficult to predict, which may impair our ability to manage our business and reduce investors' ability to assess our prospects.

Investors should not consider our revenue growth in prior quarterly or annual periods as indicative of our future performance. In future periods, we do not expect to achieve similar percentage revenue growth rates as we have achieved in some past periods. If we are unable to maintain adequate revenue or revenue growth, our stock price could be volatile, and it may be difficult to achieve and maintain profitability.

The market for all-flash storage products is rapidly evolving, which makes it difficult to forecast customer adoption rates and demand for our products.

The market for all-flash storage products is rapidly evolving. As a result, our future financial performance will depend on the continued growth of this market and on our ability to adapt to competitive dynamics and emerging customer demands and trends. Sales of our products have largely focused on use cases that require performance storage products such as virtualization and transaction processing. Some potential customers have not purchased all-flash storage products and may not have the desire or available budget to invest in a new technology such as ours. Incumbent vendors are actively promoting storage products retrofitted with flash, which may reduce the perceived value of purpose-built, all-flash products like ours. It is difficult to predict with any precision customer adoption rates of flash, customer demand for our products or the future growth rate and size of our market. Our products may never reach mass adoption, and changes or advances in alternative technologies or adoption of cloud storage offerings not utilizing our storage platform could adversely affect the demand for our products. For instance, offerings from large-scale cloud providers are expanding quickly and may serve as alternatives to our products for a variety of customer workloads. Since these providers are known for developing storage systems internally, this trend could reduce the demand for storage systems developed by original equipment manufacturers, such as us. Further, although flash storage has a number of advantages as compared to other data storage alternatives, such as hard disk drives, flash storage has certain limitations as well, including, in some use cases, a higher price per gigabyte of raw storage, more limited methods for data recovery and reduced performance gains for certain uses, such as sequential input/output, or I/O, transactions. A slowing in or reduced demand for all-flash storage products caused by lack of customer acceptance, technological challenges, alternative technologies and products or otherwise would result in a lower revenue growth rate or decreased revenue, either of which would negatively impact our business and operating results.

We face intense competition from a number of established companies and new entrants.

We face intense competition from a number of established companies that sell competitive storage products. These competitors include Dell EMC, HP Enterprise, Hitachi Data Systems, IBM, Lenovo and NetApp. These competitors, as well as other potential competitors, may have:

- greater name recognition and longer operating histories;
- larger sales and marketing and customer support budgets and resources;
- broader distribution and established relationships with distribution partners and customers;
- the ability to bundle storage products with other products and services to address customers' requirements;

- greater resources to make acquisitions;
- larger and more mature product and intellectual property portfolios; and
- substantially greater financial, technical and other resources.

We also face competition from a number of other companies, one or more of which may become significant competitors in the future. For example, we compete against certain cloud providers and vendors that offer products that combine compute, networking and storage, or hyperconverged products. Some cloud providers are expanding quickly, and their offerings could, if we are unable to effectively sell to these providers, displace demand for our products. Vendors offering hyperconverged products are attempting to displace dedicated storage products like ours. New competitors could emerge and acquire significant market share. The acquisitions of EMC by Dell, Nimble Storage by HP Enterprise and SolidFire by NetApp have introduced new competitive dynamics. All of our competitors may utilize a broad range of competitive strategies. For example, some of our competitors have offered bundled products and services in order to reduce the initial cost of their storage products. Our competitors may also choose to adopt more aggressive pricing policies than we choose to adopt. Some of our competitors have offered their products either at significant discounts or even for free in competing against us and in response to our efforts to market the overall benefits and technological merits of our products.

Many competitors have developed competing all-flash or hybrid storage technologies. For example, several of our competitors have introduced all-flash storage products with performance-focused designs and/or with data reduction technologies that directly compete with our products, or have introduced business programs that attempt to compete with, or mitigate against, the value of our innovative programs, such as our *Evergreen Storage* model of hardware and software upgrades and maintenance. We expect our competitors to continue to improve the performance of their products, reduce their prices and introduce new features, services and technologies that may, or that they may claim to, offer greater performance and improved total cost of ownership as compared to our products. In addition, our competitors may develop enhancements to, or future generations of, competitive products that may render our products or technologies obsolete or less competitive. These and other competitive pressures may prevent us from competing successfully against current or future competitors.

Our business may be harmed by trends in the overall external storage market.

Despite ongoing data growth, the external storage market in which we compete has not experienced overall growth in the past few years due to a combination of technology transitions, increased storage efficiency, and changing economic and business environments. Customers are rethinking how they consume IT, increasing spending toward public cloud, software as a service, hyperconverged and converged infrastructure and software-defined storage. The future impact of these industry, technological or market changes on both short-term and long-term growth trends is uncertain. If the overall storage market declines, or if the growth rates of the specific markets in which we compete decline, and/or if the consumption model of storage changes and our new and existing products do not receive customer acceptance, our business and operating results could be harmed.

Many of our established competitors have long-standing relationships with key decision makers at many of our current and prospective customers, which may inhibit our ability to compete effectively and maintain or increase our market share.

Many of our competitors benefit from established brand awareness and long-standing relationships with key decision makers at many of our current and prospective customers. Our competitors often leverage these existing relationships to discourage customers from evaluating or purchasing our products. In particular, when competing against us, our competitors promote the adequacy of their all-flash or hybrid storage products and emphasize the perceived risks of relying on products from a company that has a shorter operating history. Sales and marketing tactics by established competitors may include incomplete or misleading statements about their products, or about us and our products that could harm or impede our business. Additionally, most of our prospective customers have existing storage systems manufactured by our competitors. This gives an incumbent competitor an advantage in retaining the customer because the incumbent competitor already understands the customer's IT infrastructure, user demands and needs. In the event that we are unable to successfully sell our products to new customers or persuade our customers to continue purchasing our products, we will not be able to maintain or increase our market share and revenue, which could adversely affect our business and operating results.

Our ability to increase our revenue will substantially depend on our ability to attract, motivate and retain sales, engineering and other key personnel, including our management team, and any failure to attract, motivate and retain these employees could harm our business, operating results and financial condition.

Our ability to increase our revenue will substantially depend on our ability to attract and retain qualified sales, engineering and other key employees, including our management. These positions may require candidates with specific backgrounds in software and the storage industry, and competition for employees with such expertise is intense. Our ability to attract, motivate or retain employees may be reduced, as the value of our stock fluctuates and as our employees have the opportunity to sell their equity awards. We may not be successful in attracting, motivating and retaining qualified personnel. We have from time to time experienced, and we expect to continue to experience, difficulty in hiring and retaining highly skilled employees with appropriate qualifications. To the extent that we are successful in hiring to fill these positions, we need a significant amount of time to train the new employees before they can become effective and efficient in performing their jobs. From time to time, there may be changes in our management team resulting from the hiring or departure of those individuals. Members of our management team, including our executive officers, are generally employed on an at-will basis, which means that they could terminate their employment with us at any time. If we are unable to attract, motivate and retain qualified sales, engineering and other key employees, including our management, our business and operating results could suffer.

If we fail to adequately expand and optimize our sales force, our growth will be impeded.

We will need to continue to expand and optimize our sales infrastructure in order to grow our customer base and our business. We plan to continue to expand and train our sales force, both domestically and internationally. Identifying, recruiting and training qualified sales personnel require significant time, expense and attention. We must design and implement effective sales incentive programs, and it can take time before our sales representatives are fully trained and productive. Our business may be adversely affected if our efforts to expand and train our sales force do not generate a corresponding increase in revenue. In particular, if we are unable to hire, develop and retain qualified sales personnel or if new sales personnel are unable to achieve desired productivity levels in a reasonable period of time, we may not be able to realize the expected benefits of this investment or increase our revenue.

If we fail to develop and introduce new or enhanced products on a timely basis, our ability to attract and retain customers could be impaired and our competitive position could be harmed.

We operate in a dynamic environment characterized by rapidly changing technologies and industry standards and technological obsolescence. To compete successfully, we must design, develop, market and sell new or enhanced products that provide increasingly higher levels of performance, capacity and reliability and that meet the cost expectations of our customers, which is a complex and uncertain process. The introduction of new products by our competitors, the market acceptance of products based on new or alternative technologies or the emergence of new industry standards could render our existing or future products obsolete or less competitive. As we introduce new or enhanced products, we must successfully manage product launches and transitions to the next generations of our products. For example, we started initial shipments of our new *FlashBlade* products for direct availability in July 2016 and for general availability in January 2017 and started initial shipments of new *FlashArray//X* products for direct availability in April 2017. If we are not able to successfully manage the development and release of new or enhanced products, our business, operating results and financial condition could be harmed. Similarly, if we fail to introduce new or enhanced products, such as new or improved software features, that meet the needs of our customers in a timely or cost-effective fashion, we may lose market share and our operating results could be adversely affected.

Our research and development efforts may not produce successful products that result in significant revenue in the near future, if at all.

Developing new products and related enhancements, including new or improved features, is expensive and time intensive. Our investments in research and development may result in products that may not achieve market adoption, are more expensive to develop than anticipated, may take longer to generate revenue or may generate less revenue than we anticipate. Our future plans include significant investments in research and development for new products and related opportunities. We believe that we must continue to dedicate significant resources to our research and development efforts to maintain or expand our competitive position. However, these efforts may not result in significant revenue in the near future, if at all, which could adversely affect our business and operating results.

If we fail to successfully maintain or grow our relationships with channel partners, our business, operating results and financial condition could be harmed.

Our future success is highly dependent upon our ability to establish and maintain successful relationships with a variety of channel partners. In addition to selling our products, our partners may offer installation, post-sale service and support on our behalf in their local markets. In markets where we rely on partners more heavily, we have less contact with our customers and less control over the sales process and the quality and responsiveness of our partners. As a result, it may be more difficult for us to ensure the proper delivery and installation of our products or the quality or responsiveness of the support and services being offered. Any failure on our part to effectively identify, train and manage our channel partners and to monitor their sales activity, as well as the customer support and services being provided to our customers in their local markets, could harm our business, operating results and financial condition.

Our channel partners may choose to discontinue offering our products and services or may not devote sufficient attention and resources toward selling our products and services. We typically enter into non-exclusive, written agreements with our channel partners. These agreements generally have a one-year, self-renewing term, have no minimum sales commitment and do not prohibit our channel partners from offering products and services that compete with ours. Accordingly, our channel partners may choose to discontinue offering our products and services or may not devote sufficient attention and resources toward selling our products and services. Additionally, our competitors provide incentives to our existing and potential channel partners to use, purchase or offer their products and services or to prevent or reduce sales of our products and services. The occurrence of any of these events could harm our business, operating results and financial condition.

Our gross margins are impacted by a variety of factors, are subject to variation from period to period and are difficult to predict.

Our gross margins fluctuate from period to period due primarily to product costs, customer mix and product mix. Over the last six quarters, our quarterly gross margins ranged from 65% to 66%. Our gross margins may fluctuate and may be affected by a variety of factors, including:

- demand for our products;
- sales and marketing initiatives, discount levels, rebates and competitive pricing;
- changes in customer, geographic or product mix, including mix of product configurations;
- the cost of freight and components, including NAND and DRAM flash;
- new product introductions and enhancements, potentially with initial sales at relatively small volumes and higher product costs;
- the timing and amount of revenue recognized and deferred;
- excess inventory levels or purchase commitments as a result of changes in demand forecasts or product transitions;
- an increase in product returns, order rescheduling and cancellations;
- the timing of technical support service contracts and contract renewals;
- inventory stocking requirements to mitigate supply constraints, accommodate unforeseen demand or support new product introductions; and
- product quality and serviceability issues.

Due to such factors, gross margins are subject to variation from period to period and are difficult to predict. If we are unable to manage these factors effectively, our gross margins may decline, and fluctuations in gross margins may make it difficult to manage our business and achieve or maintain profitability, which could materially harm our business, operating results and financial condition.

Our operating results may fluctuate significantly, which could make our future results difficult to predict and could cause our operating results to fall below expectations.

Our operating results may fluctuate due to a variety of factors, many of which are outside of our control. As a result, comparing our results on a period-to-period basis may not be meaningful. Investors should not rely on our past

results as an indication of our future performance. If our revenue or operating results fall below the expectations of investors or any securities analysts that follow our company, the price of our Class A common stock would likely decline.

Factors that are difficult to predict and that could cause our operating results to fluctuate include:

- the timing and magnitude of orders, shipments and acceptance of our products in any quarter, including product returns, order rescheduling and cancellations by our customers;
- fluctuations in demand and prices for our products;
- potential seasonality in the markets we serve;
- our ability to control the costs of the components we use in our hardware products;
- our ability to timely adopt subsequent generations of components into our hardware products;
- disruption in our supply chains, component availability and related procurement costs;
- reductions in customers' budgets for IT purchases;
- changes in industry standards in the data storage industry;
- our ability to develop, introduce and ship in a timely manner new products and product enhancements that meet customer requirements;
- our ability to effectively manage product transitions as we introduce new products;
- any change in the competitive dynamics of our markets, including new entrants or discounting of product prices;
- our ability to control costs, including our operating expenses; and
- future accounting pronouncements and changes in accounting policies.

The occurrence of any one of these risks could negatively affect our operating results in any particular quarter, which could cause the price of our Class A common stock to decline.

Our sales cycles can be long and unpredictable, particularly with respect to large orders, and our sales efforts require considerable time and expense. As a result, it can be difficult for us to predict when, if ever, a particular customer will choose to purchase our products, which may cause our operating results to fluctuate.

Our sales efforts involve educating our customers about the use and benefits of our products, including their technical capabilities and cost saving potential. Larger customers often undertake an evaluation and testing process that can result in a lengthy sales cycle. We spend substantial time and resources on our sales efforts without any assurance that our efforts will produce any sales. In addition, product purchases are frequently subject to budget constraints, multiple approvals and unplanned administrative, processing and other delays. A substantial portion of our quarterly sales typically occurs during the last several weeks of the quarter, which we believe largely reflects customer buying patterns of products similar to ours and other products in the technology industry generally. Since we do not recognize revenue from a sale until title is transferred for the product, if we have a substantial portion of our sales at the end of a quarter, we may be unable to transfer title and recognize the associated revenue in that quarter. Furthermore, our products come with a 30-day money back guarantee, allowing a customer to return a product within 30 days of receipt if the customer is not satisfied with its purchase for any reason. In addition, a portion of our sales in any quarter is generated by sales activity initiated during the quarter. These factors, among others, make it difficult for us to predict when customers may purchase our products. We may expend significant resources on an opportunity without ever achieving a sale, which may adversely affect our operating results and cause our operating results to fluctuate. In addition, if sales expected from a specific customer for a particular quarter are not realized in that quarter or at all, our operating results may suffer.

Our company culture has contributed to our success, and if we cannot maintain this culture as we grow, we could lose the innovation, creativity and teamwork fostered by our culture, and our business may be harmed.

We believe that a critical contributor to our success has been our company culture, which we believe fosters innovation, creativity, teamwork, passion for customers and focus on execution, as well as facilitating critical knowledge transfer and knowledge sharing. In particular, we believe that the difference between our sales, support and engineering cultures, relative to those of incumbent vendors, is a key competitive advantage and differentiator for our customers.

As we grow and change, we may find it difficult to maintain these important aspects of our company culture, which could limit our ability to innovate and operate effectively. Any failure to preserve our culture could also negatively affect our ability to retain and recruit personnel, continue to perform at current levels or execute on our business strategy.

Because our long-term success depends, in part, on our ability to expand the sales of our products to customers located outside of the United States, our business is susceptible to risks associated with international operations.

We maintain operations outside of the United States. We have been expanding and intend to continue to expand these operations in the future. We have limited experience operating in foreign jurisdictions. Our inexperience in operating our business outside of the United States increases the risk that our international expansion efforts may not be successful. In addition, conducting and expanding international operations subjects us to new risks that we have not generally faced in the United States. These include:

- exposure to foreign currency exchange rate risk;
- difficulties in collecting payments internationally, and managing and staffing international operations;
- establishing relationships with channel partners in international locations;
- the increased travel, infrastructure and legal compliance costs associated with international locations;
- the burdens of complying with a wide variety of laws associated with international operations, including taxes and customs;
- significant fines, penalties and collateral consequences if we fail to comply with anti-bribery laws;
- heightened risk of improper, unfair or corrupt business practices in certain geographies;
- potentially adverse tax consequences, including repatriation of earnings;
- increased financial accounting and reporting burdens and complexities;
- political, social and economic instability abroad, terrorist attacks and security concerns in general; and
- reduced or varied protection for intellectual property rights in some countries.

The occurrence of any one of these risks could negatively affect our international operations and, consequently, our business, operating results and financial condition generally.

The sales prices of our products and services may decrease, which may reduce our gross profits and adversely impact our financial results.

The sales prices for our products and services may decline for a variety of reasons, including competitive pricing pressures, discounts, a change in our mix of products and services, and the introduction of competing products or services or promotional programs. Competition continues to increase in the markets in which we participate, and we expect competition to further increase in the future, thereby leading to increased pricing pressures. Larger competitors with more diverse product and service offerings may reduce the price of products or services that compete with ours or may bundle them with other products and services. Additionally, although we price our products and services predominantly in U.S. dollars, currency fluctuations in certain countries and regions may negatively impact actual prices that partners and customers are willing to pay in those countries and regions. Furthermore, we anticipate that the sales prices for our products will decrease over product life cycles. We cannot assure investors that we will be successful in developing and introducing new offerings with enhanced functionality on a timely basis, or that our new product and services offerings, if introduced, will enable us to maintain or improve our gross margins and achieve profitability.

We derive substantially all of our revenue from a single family of products, and a decline in demand for these products would cause our revenue to grow more slowly or to decline.

Our *FlashArray* family of products has historically accounted for substantially all of our revenue and will continue to comprise a significant portion of our revenue for the foreseeable future. As a result, our revenue could be reduced by:

- the failure of our current products to achieve broad market acceptance;

- any decline or fluctuation in demand for our products, whether as a result of product obsolescence, technological change, customer budgetary constraints or other factors;
- the introduction of competing products and technologies that replace or substitute, or represent an improvement over, our products; and
- our inability to release enhanced versions of our products, including any related software, on a timely basis.

If the market for all-flash storage products grows more slowly than anticipated or if demand for our products declines, we may not be able to increase our revenue or achieve and maintain profitability.

Our products are highly technical and may contain undetected defects, which could cause data unavailability, loss or corruption that might, in turn, result in liability to our customers and harm to our reputation and business.

Our products are highly technical and complex and are often used to store information critical to our customers' business operations. Our products may contain undetected errors, defects or security vulnerabilities that could result in data unavailability, loss, corruption or other harm to our customers. Some errors in our products may only be discovered after they have been installed and used by customers. Any errors, defects or security vulnerabilities discovered in our products after commercial release could result in a loss of revenue or delay in revenue recognition, injury to our reputation, a loss of customers or increased service and warranty costs, any of which could adversely affect our business and operating results. In addition, errors or failures in the products of third-party technology vendors may be attributed to us and may harm our reputation.

We could face claims for product liability, tort or breach of warranty. Many of our contracts with customers contain provisions relating to warranty disclaimers and liability limitations, which may be difficult to enforce. Defending a lawsuit, regardless of its merit, would be costly and might divert management's attention and adversely affect the market's perception of us and our products. Our business liability insurance coverage could prove inadequate with respect to a claim and future coverage may be unavailable on acceptable terms or at all. These product-related issues could result in claims against us, and our business, operating results and financial condition could be harmed.

Our brand name and our business may be harmed by the marketing strategies of our competitors.

Because of the early stage of our business, we believe that building and maintaining brand recognition and customer goodwill is critical to our success. Our efforts in this area have, on occasion, been hampered by the marketing efforts of our competitors, which have included statements about us and our products. If we are unable to effectively respond to the marketing efforts of our competitors and protect our brand and customer goodwill now or in the future, our business will be adversely affected.

Our products must interoperate with third party operating systems, software applications and hardware, and if we are unable to devote the necessary resources to ensure that our products interoperate with such software and hardware, we may lose or fail to increase our market share and may experience reduced demand for our products.

Our products must interoperate with our customers' existing infrastructure, specifically their networks, servers, software and operating systems, which may be manufactured by a wide variety of vendors. When new or updated versions of these software operating systems or applications are introduced, we must sometimes develop updated versions of our software so that our products will interoperate properly. For example, our *Pure1* cloud-based management and support includes connectors to virtualization platforms, allowing our customers to manage our products within native management tools, such as VMware and OpenStack. We may not deliver or maintain interoperability quickly, cost-effectively or at all. These efforts require capital investment and engineering resources. If we fail to maintain compatibility of our products with these infrastructure components, our customers may not be able to fully utilize our products, and we may, among other consequences, lose or fail to increase our market share and experience reduced demand for our products, which may harm our business, operating results and financial condition.

Our products must conform to industry standards in order to be accepted by customers in our markets.

Generally, our products comprise only a part of a data center. The servers, network, software and other components and systems of a data center must comply with established industry standards in order to interoperate

and function efficiently together. We depend on companies that provide other systems in a data center to conform to prevailing industry standards. Often, these companies are significantly larger and more influential in driving industry standards than we are. Some industry standards may not be widely adopted or implemented uniformly, and competing standards may emerge that may be preferred by our customers. If larger companies do not conform to the same industry standards that we do, or if competing standards emerge, market acceptance of our products could be adversely affected, which may harm our business.

Our ability to successfully market and sell our products is dependent in part on ease of use and the quality of our support offerings, and any failure to offer high-quality installation and technical support could harm our business.

Once our products are deployed within our customers' data centers, customers depend on our support organization to resolve technical issues relating to our products. Our ability to provide effective support is largely dependent on our ability to attract, train and retain qualified personnel, as well as to engage with qualified support partners that provide a similar level of customer support. In addition, our sales process is highly dependent on our product and business reputation and on recommendations from our existing customers. Although our products are designed to be interoperable with existing servers and systems, we may need to provide customized installation and configuration support to our customers before our products become fully operational in their environments. Any failure to maintain, or a market perception that we do not maintain, high-quality installation and technical support could harm our reputation, our ability to sell our products to existing and prospective customers and our business.

We rely on contract manufacturers to manufacture our products, and if we fail to manage our relationship with our contract manufacturers successfully, our business could be negatively impacted.

We rely on a limited number of contract manufacturers to manufacture our products. Our reliance on contract manufacturers reduces our control over the assembly process, and exposes us to risks, such as reduced control over quality assurance, costs and product supply. If we fail to manage our relationships with these contract manufacturers effectively, or if these contract manufacturers experience delays, disruptions, capacity constraints or quality control problems, our ability to timely ship products to our customers could be impaired and our competitive position and reputation could be harmed. If we are required to change contract manufacturers or assume internal manufacturing operations, we may lose revenue, incur increased costs and damage our customer relationships. Qualifying a new contract manufacturer and commencing production is expensive and time-consuming. We may need to increase our component purchases, contract manufacturing capacity and internal test and quality functions if we experience increased demand. The inability of our contract manufacturers to provide us with adequate supplies of high-quality products could cause a delay in our order fulfillment, and our business, operating results and financial condition may be harmed.

We rely on a limited number of suppliers, and in some cases single-source suppliers, and any disruption or termination of these supply arrangements could delay shipments of our products and could harm our relationships with current and prospective customers.

We rely on a limited number of suppliers, and in some cases, on single-source suppliers, for several key components of our products, and we have not generally entered into agreements for the long-term purchase of these components. For example, the CPUs utilized in our products are supplied by Intel Corporation (Intel), and neither we nor our contract manufacturers have an agreement with Intel for the procurement of these CPUs. Instead, we purchase the CPUs either directly from Intel or through a reseller on a purchase order basis. Intel or its resellers could stop selling to us at any time or could raise their prices without notice.

This reliance on a limited number of suppliers and the lack of any guaranteed sources of supply exposes us to several risks, including:

- the inability to obtain an adequate supply of key components, including solid-state drives;
- price volatility for the components of our products;
- failure of a supplier to meet our quality or production requirements;
- failure of a supplier of key components to remain in business or adjust to market conditions; and
- consolidation among suppliers, resulting in some suppliers exiting the industry or discontinuing the manufacture of components.

As a result of these risks, we cannot assure investors that we will be able to obtain enough of these key components in the future or that the cost of these components will not increase. If our supply of components is disrupted or delayed, or if we need to replace our existing suppliers, there can be no assurance that additional components will be available when required or that components will be available on terms that are favorable to us, which could extend our lead times, increase the costs of our components and harm our business, operating results and financial condition. Even if we are successful in growing our business, we may not be able to continue to procure components at reasonable prices, which may require us to enter into longer-term contracts with component suppliers to obtain these components at competitive prices. This could increase our costs and decrease our gross margins, harming our business, operating results and financial condition.

Managing the supply of our products and their components is complex. Insufficient supply and inventory may result in lost sales opportunities or delayed revenue, while excess inventory may harm our gross margins.

Our third-party contract manufacturers procure components and build our products based on our forecasts, and we generally do not hold inventory for a prolonged period of time. These forecasts are based on estimates of future demand for our products, which are in turn based on historical trends and analyses from our sales and marketing organizations, adjusted for overall market conditions. In order to reduce manufacturing lead times and plan for adequate component supply, from time to time we may issue forecasts for components and products that are non-cancelable and non-returnable. Our inventory management systems and related supply chain visibility tools may be inadequate to enable us to make accurate forecasts and effectively manage the supply of our products and components. We have, in the past, had to write off inventory in connection with transitions to new product models. If we ultimately determine that we have excess supply, we may have to reduce our prices and write down or write off excess or obsolete inventory, which in turn could result in lower gross margins. Alternatively, insufficient supply levels may lead to shortages that result in delayed revenue, reduced product margins or loss of sales opportunities altogether. If we are unable to effectively manage our supply and inventory, our results of operations could be adversely affected.

If we are unable to sell renewals of our maintenance and support services to our customers, our future revenue and operating results will be harmed.

Existing customers may not renew their maintenance and support agreements after the initial period, and given our limited operating history, we may not be able to accurately predict our renewal rates. Our customers' renewal rates may decline or fluctuate as a result of a number of factors, including their available budget and the level of their satisfaction with our storage platform, customer support and pricing as compared to that offered by our competitors. If our customers renew their contracts, they may renew on terms that are less economically beneficial to us. We cannot assure investors that our customers will renew their maintenance and support agreements, and if our customers do not renew their agreements or renew on less favorable terms, our revenue may grow more slowly than expected, if at all.

We expect that revenue from maintenance and support agreements will increase as a percentage of total revenue over time, and because we recognize this revenue over the term of the relevant contract period, downturns or upturns in sales are not immediately reflected in full in our results of operations.

We expect that revenue from maintenance and support agreements will increase as a percentage of total revenue over time. We recognize maintenance and support revenue ratably over the term of the relevant service period. As a result, much of the maintenance and support revenue we report each quarter is derived from maintenance and support agreements that we sold in prior quarters. Consequently, a decline in new or renewed maintenance and support agreements in any one quarter will not be fully reflected in revenue in that quarter but will negatively affect our revenue in future quarters. Accordingly, the effect of significant downturns in sales of maintenance and support is not reflected in full in our results of operations until future periods. Also, it is difficult for us to rapidly increase our maintenance and support revenue through additional sales in any period, as revenue from renewals must be recognized ratably over the applicable service period.

Adverse economic conditions or reduced data center spending may adversely impact our revenues and profitability.

Our operations and performance depend in part on worldwide economic conditions and the impact these conditions have on levels of spending on data center technology. Global economic uncertainty and political and fiscal challenges in the United States and abroad could adversely impact data center spending. Our business depends on the overall demand for data center infrastructure and on the economic health of our current and prospective customers.

Weak economic conditions, or a reduction in data center spending, would likely adversely impact our business, operating results and financial condition in a number of ways, including by reducing sales, lengthening sales cycles and lowering prices for our products and services.

Third-party claims that we are infringing the intellectual property rights of others, whether successful or not, could subject us to costly and time-consuming litigation or require us to obtain expensive licenses, and our business could be harmed.

There is a substantial amount of intellectual property litigation in the flash-based storage industry, and we may become party to, or threatened with, litigation or other adversarial proceedings regarding intellectual property rights with respect to our technology, including interference or derivation proceedings before the U.S. Patent and Trademark Office. Third parties may assert infringement claims against us based on existing or future intellectual property rights. The outcome of intellectual property litigation is subject to uncertainties that cannot be adequately quantified in advance. We have in the past received and may in the future receive inquiries from other intellectual property holders and may become subject to claims that we infringe their intellectual property rights, particularly as we expand our presence in the market and face increasing competition. For example, in 2013, EMC Corporation (EMC) brought lawsuits against us, alleging misappropriation of confidential information and trade secrets and patent infringement. In October 2016, we resolved pending disputes between EMC and us, resulting in the dismissal of the lawsuits.

Any intellectual property rights claim, such as the lawsuits brought by EMC, against us or our customers, suppliers, and channel partners, with or without merit, could be time-consuming and expensive to litigate or settle, could divert management's resources and attention from operating our business and could force us to acquire intellectual property rights and licenses, which may involve substantial royalty payments. Further, a party making such a claim, if successful, could secure a judgment that requires us to pay substantial damages, including treble damages and attorneys' fees if we are found to have willfully infringed a patent. An adverse determination also could invalidate our intellectual property rights and prevent us from manufacturing and offering our products to our customers and may require that we procure or develop substitute products that do not infringe, which could require significant effort and expense. We may not be able to re-engineer our products successfully to avoid infringement, and we may have to seek a license for the infringed technology, which may not be available on reasonable terms or at all, may significantly increase our operating expenses or may require us to restrict our business activities in one or more respects. Even if we were able to obtain a license, it could be non-exclusive, thereby giving our competitors access to the same technologies licensed to us. Claims that we have misappropriated the confidential information or trade secrets of third parties could have a similar negative impact on our business. Any of these events could harm our business and financial condition.

We currently have a number of agreements in effect pursuant to which we have agreed to defend, indemnify and hold harmless our customers, suppliers and channel partners from damages and costs which may arise from the infringement by our products of third-party patents, trademarks or other proprietary rights. The scope of these indemnity obligations varies, but may, in some instances, include indemnification for damages and expenses, including attorneys' fees. Our insurance may not cover intellectual property infringement claims. A claim that our products infringe a third party's intellectual property rights could harm our relationships with our customers, deter future customers from purchasing our products and expose us to costly litigation and settlement expenses. Even if we are not a party to any litigation between a customer and a third party relating to infringement by our products, an adverse outcome in any such litigation could make it more difficult for us to defend our products against intellectual property infringement claims in any subsequent litigation in which we are a named party. Any of these results could harm our brand and financial condition.

The success of our business depends in part on our ability to protect and enforce our intellectual property rights.

We rely on a combination of patent, copyright, service mark, trademark and trade secret laws, as well as confidentiality procedures and contractual restrictions, to establish and protect our proprietary rights, all of which provide only limited protection. We have over 700 issued patents and patent applications in the United States and foreign countries. We cannot assure investors that any patents will issue with respect to our currently pending patent applications in a manner that gives us the protection that we seek, if at all, or that any patents issued to us will not be challenged, invalidated, circumvented or held to be unenforceable in actions against alleged infringers. Our issued patents and any patents that may issue in the future with respect to pending or future patent applications may not provide sufficiently broad protection or they may not prove to be enforceable in actions against alleged infringers. Changes to the patent laws in the United States and other jurisdictions could also diminish the value of our patents and patent applications or narrow the scope of our patent protection. We cannot be certain that the steps we have

taken will prevent unauthorized use of our technology or the reverse engineering of our technology. Moreover, others may independently develop technologies that are competitive to ours or infringe our intellectual property. Furthermore, any of our trademarks may be challenged by others or invalidated through administrative process or litigation.

Protecting against the unauthorized use of our intellectual property, products and other proprietary rights is expensive and difficult. Litigation may be necessary in the future to enforce or defend our intellectual property rights or to determine the validity and scope of the proprietary rights of others. Any such litigation could result in substantial costs and diversion of management's resources and attention, either of which could harm our business, operating results and financial condition. Further, many of our current and potential competitors have the ability to dedicate substantially greater resources to defending intellectual property infringement claims and to enforcing their intellectual property rights than we have. Accordingly, we may not be able to prevent third parties from infringing upon or misappropriating our intellectual property. Effective patent, trademark, service mark, copyright and trade secret protection may not be available in every country in which our products are available. An inability to adequately protect and enforce our intellectual property and other proprietary rights could harm our business and financial condition.

If we are unable to protect the confidentiality of our trade secrets, the value of our technology could be materially adversely affected and our business could be harmed.

In addition to the protection afforded by patents, we rely on confidential proprietary information, including trade secrets and know-how to develop and maintain our competitive position. Any disclosure to or misappropriation by third parties of our confidential proprietary information could enable competitors to quickly duplicate or surpass our technological achievements, thus eroding our competitive position in our market. We seek to protect our confidential proprietary information, in part, by confidentiality agreements and invention assignment agreements with our employees, consultants, scientific advisors, contractors and collaborators. These agreements are designed to protect our proprietary information; however, we cannot be certain that such agreements have been entered into with all relevant parties, and we cannot be certain that our trade secrets and other confidential proprietary information will not be disclosed or that competitors will not otherwise gain access to our trade secrets or independently develop substantially equivalent information and techniques. For example, any of these parties may breach the agreements and disclose our proprietary information, including our trade secrets, and we may not be able to obtain adequate remedies for such breaches.

We also seek to preserve the integrity and confidentiality of our proprietary information by maintaining physical security of our premises and physical and electronic security of our IT systems, but it is possible that these security measures could be breached. If any of our confidential proprietary information were to be lawfully obtained or independently developed by a competitor, we may have no right to prevent such competitor from using that technology or information to compete with us, which could harm our competitive position. Further, the laws of some foreign countries do not protect proprietary rights to the same extent or in the same manner as the laws of the United States. As a result, we may encounter significant problems in protecting and defending our intellectual property both in the United States and abroad. If we are unable to prevent material disclosure of the intellectual property related to our technologies to third parties, we will not be able to establish or maintain a competitive advantage in our market, which could harm our business.

Our use of open source software could impose limitations on our ability to commercialize our products.

We use open source software in our products and expect to continue to use open source software in the future. Although we monitor our use of open source software, the terms of many open source licenses have not been interpreted by U.S. or foreign courts, and there is a risk that such licenses could be construed in a manner that imposes unanticipated conditions or restrictions on our ability to market our products. From time to time, we may face claims from third parties claiming ownership of, or demanding release of, the open source software or derivative works that we have developed using such software, which could include our proprietary source code, or otherwise seeking to enforce the terms of the applicable open source license. These claims could result in litigation and could require us to make our software source code freely available, seek licenses from third parties in order to continue offering our products for certain uses or cease offering the implicated solutions unless and until we can re-engineer them to avoid infringement. This re-engineering process could require significant additional research and development resources, and we may be required to discontinue providing some of our software in the event re-engineering cannot be accomplished on a timely basis, any of which could harm our business, operating results and financial condition.

System security risks, data protection breaches and cyber-attacks on our systems or products could compromise our proprietary information (or information of our customers), disrupt our internal operations and harm public perception of our products, which could cause our business and reputation to suffer, create additional liabilities and adversely affect our financial results and stock price.

In the ordinary course of business, we store sensitive data on our internal systems, networks and servers, which may include intellectual property, our proprietary business information and that of our customers, suppliers and business partners and sales data, which may include personally identifiable information. Additionally, we design and sell products that allow our customers to store our customers' data. The security of our own networks and the intrusion protection features of our product are both critical to our operations and business strategy.

We devote significant resources to network security, data encryption and other security measures to protect our systems and data, but these security measures cannot provide absolute security. For example, we use encryption and authentication technologies to secure the transmission and storage of data and prevent third party access to data or accounts, but these security measures are subject to third-party security breaches, employee error, malfeasance, faulty password management or other irregularities. Any destructive or intrusive breach of our internal systems could result in the information stored on our networks being accessed, publicly disclosed, lost or stolen. Additionally, an effective attack on our products could disrupt the proper functioning of our products, allow unauthorized access to sensitive, proprietary or confidential information of ours or our customers, disrupt or temporarily interrupt customers' operations or cause other destructive outcomes, including the theft of information sufficient to engage in fraudulent transactions. The risk that these types of events could seriously harm our business is likely to increase as we expand our network of channel partners, resellers and authorized service providers and operate in more countries. The economic costs to us to eliminate or alleviate cyber or other security problems, viruses, worms, malicious software systems and security vulnerabilities could be significant and may be difficult to anticipate or measure because the damage may differ based on the identity and motive of the programmer or hacker, which are often difficult to identify. If any of these types of security breaches, actual or perceived, were to occur and we were to be unable to protect sensitive data, our relationships with our business partners and customers could be materially damaged, our reputation and brand could be materially harmed, use of our products could decrease and we could be exposed to a risk of loss or litigation and possible liability.

We may further expand through acquisitions of, or investments in, other companies, each of which may divert our management's attention, resulting in additional dilution to our stockholders and consumption of resources that are necessary to sustain and grow our business.

Our business strategy may, from time to time, include acquiring complementary products, technologies or businesses. We also may enter into relationships with other businesses in order to expand our product offerings, which could involve preferred or exclusive licenses, additional channels of distribution or discount pricing or investments in other companies. Negotiating these transactions can be time-consuming, difficult and expensive, and our ability to close these transactions may be subject to third-party or government approvals, which are beyond our control. Consequently, we can make no assurance that these transactions, once undertaken and announced, will close.

These kinds of acquisitions or investments may result in unforeseen operating difficulties and expenditures. In particular, we may encounter difficulties assimilating or integrating the businesses, technologies, products, personnel or operations of the acquired companies, particularly if the key personnel of the acquired business choose not to work for us, and we may have difficulty retaining the customers of any acquired business. Acquisitions may also disrupt our ongoing business, divert our resources and require significant management attention that would otherwise be available for development of our business. Any acquisition or investment could expose us to unknown liabilities. Moreover, we cannot assure investors that the anticipated benefits of any acquisition or investment would be realized or that we would not be exposed to unknown liabilities. In connection with these types of transactions, we may issue additional equity securities that would dilute our stockholders, use cash that we may need in the future to operate our business, incur debt on terms unfavorable to us or that we are unable to repay, incur large charges or substantial liabilities, encounter difficulties integrating diverse business cultures and become subject to adverse tax consequences, substantial depreciation or deferred compensation charges. These challenges related to acquisitions or investments could harm our business and financial condition.

We may require additional capital to support business growth, and this capital might not be available on acceptable terms, or at all.

We intend to continue to make investments to support our business growth and may require additional funds to respond to business challenges, including the need to develop new products or enhance our existing products, enhance our operating infrastructure and acquire complementary businesses and technologies. Accordingly, we may need to engage in equity or debt financings to secure additional funds. If we raise additional funds through further issuances of equity or convertible debt securities, our stockholders could suffer significant dilution, and any new equity securities we issue could have rights, preferences and privileges superior to those of holders of our common stock. Any debt financing in the future could involve additional restrictive covenants relating to our capital raising activities and other financial and operational matters, which may make it more difficult for us to obtain additional capital and to pursue business opportunities, including potential acquisitions. We may not be able to obtain additional financing on terms favorable to us, if at all. If we are unable to obtain adequate financing or financing on terms satisfactory to us, when we require it, our ability to support our business growth and to respond to business challenges could be significantly limited and our prospects and financial condition could be harmed.

We are exposed to the credit risk of some of our customers, which could harm our business, operating results and financial condition.

Most of our sales are made on an open credit basis. As a general matter, we monitor individual customer payment capability when we grant open credit arrangements and may limit these open credit arrangements based on perceived creditworthiness. We also maintain allowances we believe are adequate to cover exposure for doubtful accounts. Although we have programs in place that are designed to monitor and mitigate these risks, we cannot assure investors these programs will be effective in managing our credit risks, especially as we expand our business internationally. If we are unable to adequately control these risks, our business, operating results and financial condition could be harmed.

Sales to U.S. federal, state and local governments are subject to a number of challenges and risks that may adversely impact our business.

Sales to U.S. federal, state and local governmental agencies may in the future account for a significant portion of our revenue. Sales to such government entities are subject to the following risks:

- selling to governmental agencies can be highly competitive, expensive and time consuming, often requiring significant upfront time and expense without any assurance that such efforts will generate a sale;
- government certification requirements applicable to our products may change and in doing so restrict our ability to sell into the U.S. federal government sector until we have attained the revised certification;
- government demand and payment for our products and services may be impacted by public sector budgetary cycles and funding authorizations, with funding reductions or delays adversely affecting public sector demand for our products and services;
- we sell our products to governmental agencies through our channel partners, and these agencies may have statutory, contractual or other legal rights to terminate contracts with our distributors and resellers for convenience or due to a default, and any such termination may adversely impact our future results of operations;
- governments routinely investigate and audit government contractors' administrative processes, and any unfavorable audit could result in the government refusing to continue buying our products, which would adversely impact our revenue and results of operations, or institute fines or civil or criminal liability if the audit uncovers improper or illegal activities; and
- governments may require certain products to be manufactured in the United States and other relatively high-cost manufacturing locations, and we may not manufacture all products in locations that meet these requirements, affecting our ability to sell these products to governmental agencies.

We need to maintain effective internal control over financial reporting in accordance with Section 404 of the Sarbanes-Oxley Act, and the failure to do so could have a material adverse effect on our business and stock price.

The Sarbanes-Oxley Act requires, among other things, that we maintain effective internal control over financial reporting and disclosure controls and procedures. We are required to perform system and process evaluation and testing of our internal control over financial reporting to allow management to report on the effectiveness of our internal control over financial reporting, as required by Section 404 of the Sarbanes-Oxley Act, or Section 404. Our independent registered public accounting firm also needs to attest to the effectiveness of our internal control over financial reporting. Over the last year, we have taken and continue to take additional steps to upgrade our finance and accounting function, including the hiring of additional finance and accounting personnel, and implement additional policies and procedures associated with the financial statement close process. Our compliance with Section 404 may require us to continue to incur substantial expense and expend significant management efforts. If we are unable to comply with the requirements of Section 404 in a timely manner, or if we or our independent registered public accounting firm notes or identifies deficiencies in our internal control over financial reporting that are deemed to be material weaknesses, the market price of our Class A common stock could decline and we could be subject to sanctions or investigations by the SEC, or other regulatory authorities, which would require additional financial and management resources.

Our international operations subject us to potentially adverse tax consequences.

We generally conduct our international operations through wholly-owned subsidiaries and report our taxable income in various jurisdictions worldwide based upon our business operations in those jurisdictions. In the future, we may decide to reorganize our corporate tax structure and intercompany relationships to more closely align our corporate organization with the expansion of our international business activities. Although we anticipate that such steps could achieve a reduction in our overall effective tax rate in the future as a result of implementing the new corporate structure, our restructuring efforts will require us to incur expenses in the near term for which we may not realize any benefits.

Our intercompany relationships are, and after the implementation of our new corporate tax structure will continue to be, subject to complex transfer pricing regulations administered by taxing authorities in various jurisdictions. The relevant taxing authorities may disagree with our determinations as to the income and expenses attributable to specific jurisdictions. If such a disagreement were to occur, and our position were not sustained, we could be required to pay additional taxes, interest and penalties, which could result in tax charges, higher effective tax rates, reduced cash flows and lower overall profitability of our operations. In addition, following the implementation of our new corporate tax structure, if the intended tax treatment of the structure is not accepted by the applicable taxing authorities, there are changes in tax law that negatively impact the structure or we do not operate our business consistent with the structure and applicable tax laws and regulations, we may fail to achieve any tax advantages as a result of the new corporate structure, and our future operating results and financial condition may be negatively impacted.

Current U.S. tax laws, including limitations on the ability of taxpayers to claim and utilize foreign tax credits and the deferral of certain tax deductions until earnings outside of the United States are repatriated to the United States, as well as changes to U.S. tax laws that may be enacted in the future, could impact the tax treatment of our foreign earnings. Due to expansion of our international business activities, any changes in the U.S. taxation of such activities may increase our worldwide effective tax rate and adversely affect our financial condition and operating results.

Failure to comply with governmental laws and regulations could harm our business.

Our business is subject to regulation by various federal, state, local and foreign governmental agencies, including agencies responsible for monitoring and enforcing employment and labor laws, workplace safety, product safety, environmental laws, consumer protection laws, anti-bribery laws, import/export controls, federal securities laws and tax laws and regulations. In certain jurisdictions, these regulatory requirements may be more stringent than in the United States. For example, the European Union has adopted certain directives to facilitate the recycling of electrical and electronic equipment sold in the European Union, including the Restriction on the Use of Certain Hazardous Substances in Electrical and Electronic Equipment directive and the Waste Electrical and Electronic Equipment directive. Changes in applicable laws, regulations and standards could harm our business, operating results and financial condition. For example, we have a presence in the European Union, including in United Kingdom, and our business could be impacted, to some extent, by the United Kingdom's exit from the European Union and related changes in law and regulation. Noncompliance with applicable regulations or requirements could subject us to investigations, sanctions, mandatory product recalls, enforcement actions, disgorgement of profits, fines, damages, civil and criminal penalties or injunctions. If any governmental sanctions are imposed, or if we do not prevail in any

possible civil or criminal litigation, our business, operating results and financial condition could be harmed. In addition, responding to any action will likely result in a significant diversion of management's attention and resources and an increase in professional fees. Enforcement actions and sanctions could harm our business, operating results and financial condition.

Governmental regulations affecting the import or export of products could negatively affect our revenue.

The U.S. and various foreign governments have imposed controls, export license requirements and restrictions on the import or export of some technologies, especially encryption technology. From time to time, governmental agencies have proposed additional regulation of encryption technology, such as requiring the escrow of imports or exports. If we fail to obtain required import or export approval for our products, our international and domestic sales could be harmed and our revenue may be adversely affected. In many cases, we rely on vendors and channel partners to handle logistics associated with the import and export of our products, so our visibility and control over these matters may be limited. In addition, failure to comply with such regulations could result in penalties, costs and restrictions on export privileges, which could harm our business, operating results and financial condition.

Our business is subject to the risks of earthquakes, floods and other natural catastrophic events, and to interruption by man-made factors such as computer viruses or terrorism.

We and our suppliers have operations in locations, including our headquarters in California, that are subject to earthquakes, floods and other natural catastrophic events, such as severe weather and geological events, which could disrupt our operations or the operations of our customers and suppliers. Our customers affected by a natural disaster could postpone or cancel orders of our products, which could negatively impact our business. Moreover, should any of our key suppliers fail to deliver components to us as a result of a natural disaster, we may be unable to purchase these components in necessary quantities or may be forced to purchase components in the open market at significantly higher costs. We may also be forced to purchase components in advance of our normal supply chain demand to avoid potential market shortages. We may not have adequate business interruption insurance to compensate us for losses due to a significant natural disaster or due to man-made factors. In addition, acts of terrorism or malicious computer viruses could cause disruptions in our or our customers' businesses or the economy as a whole. To the extent that these disruptions result in delays or cancellations of customer orders or the deployment of our products, our business, operating results and financial condition could be harmed.

Risks Related to Our Common Stock

The dual class structure of our common stock has the effect of concentrating voting control with those stockholders who hold our Class B common stock, including our executive officers, employees and directors and their affiliates, which limits investors' ability to influence the outcome of important transactions, including a change in control.

Our Class B common stock has ten votes per share, and our Class A common stock has one vote per share. Stockholders who hold shares of our Class B common stock, including our executive officers, employees and directors and their affiliates, collectively hold the vast majority of the voting power of our outstanding capital stock. Because of the ten-to-one voting ratio between our Class B common stock and Class A common stock, the holders of our Class B common stock will therefore be able to control all matters submitted to our stockholders for approval so long as the shares of our Class B common stock represent at least 10% of all outstanding shares of our Class A common stock and Class B common stock. These holders of our Class B common stock may also have interests that differ from investors and may vote in a way with which investors disagree and which may be adverse to investors' interests. This concentrated control may have the effect of delaying, preventing or deterring a change in control of our company, could deprive our stockholders of an opportunity to receive a premium for their capital stock as part of a sale of our company and might ultimately affect the market price of our Class A common stock.

Future transfers by holders of our Class B common stock will generally result in those shares converting into shares of our Class A common stock, subject to limited exceptions, such as certain transfers effected for estate planning purposes. The conversion of shares of our Class B common stock into shares of our Class A common stock will have the effect, over time, of increasing the relative voting power of those holders of Class B common stock who retain their shares in the long term. If, for example, Dr. Dietzen and Messrs. Colgrove and Hatfield retain a significant portion of their holdings of our Class B common stock for an extended period of time, they could control a significant portion of the voting power of our capital stock for the foreseeable future. As board members, Dr. Dietzen and Mr. Colgrove each owe a fiduciary duty to our stockholders and must act in good faith and in a manner they reasonably believe to be in the best interests of our stockholders. However, as stockholders, Dr. Dietzen and Messrs. Colgrove and Hatfield are entitled to vote their shares in their own interests, which may not always be in the interests of our stockholders generally.

Substantial sales of shares of our common stock in the future could cause the market price of our common stock to decline.

The price of our common stock could decline if there are substantial sales of our common stock, particularly sales by any of our large stockholders. For example, we have two large stockholders that each hold well over 10% of our outstanding common stock. While volume limitations under Rule 144 under the Securities Act could partially limit sales by directors, executive officers and other affiliates, the market price of the shares of our common stock could decline as a result of sales of a substantial number of our shares in the public market or the perception in the market that the holders of a large number of shares intend to sell their shares.

The trading price of our Class A common stock has been and may continue to be highly volatile, and an active, liquid, and orderly market for our Class A common stock may not be sustained.

The trading price of our Class A common stock has been, and will likely continue to be, highly volatile. Since shares of our Class A common stock were sold in our initial public offering in October 2015 at a price of \$17.00 per share, our closing stock price has ranged from \$9.40 to \$19.74, through August 25, 2017. Some of the factors, many of which are beyond our control, affecting our volatility may include:

- price and volume fluctuations in the overall stock market from time to time;
- significant volatility in the market price and trading volume of technology companies in general and of companies in our industry;
- actual or anticipated changes in our results of operations or fluctuations in our operating results;
- whether our operating results meet the expectations of securities analysts or investors;
- actual or anticipated changes in the expectations of investors or securities analysts;
- actual or anticipated developments in our competitors' businesses or the competitive landscape generally;
- litigation involving us, our industry or both;
- general economic conditions and trends;
- major catastrophic events;
- sales of large blocks of our stock; or
- departures of key personnel.

The stock markets in general, and market prices for the securities of technology-based companies like ours in particular, have from time to time experienced volatility that often has been unrelated to the operating performance of the underlying companies. A certain degree of stock price volatility can be attributed to being a newly public company. These broad market and industry fluctuations may adversely affect the market price of our Class A common stock, regardless of our operating performance. In several recent situations where the market price of a stock has been volatile, holders of that stock have instituted securities class action litigation against the company that issued the stock, such as the consolidated class action we currently are defending against. If any of our stockholders were to bring a lawsuit against us, the defense and disposition of the lawsuit could be costly and divert the time and attention of our management and harm our business, operating results and financial condition.

If securities analysts do not publish research or reports about our business, or if they downgrade our stock, the price of our stock could decline.

The trading market for our Class A common stock will likely be influenced by research and reports that securities or industry analysts publish about us or our business. In the event securities or industry analysts cover our company and one or more of these analysts downgrades our stock, lowers their price target, or publishes inaccurate or unfavorable research about our business, our stock price would likely decline. If one or more of these analysts ceases coverage of our company or fails to publish reports on us regularly, demand for our stock could decrease, which could cause our stock price and trading volume to decline.

We have never paid dividends on our common stock and we do not anticipate paying any cash dividends in the foreseeable future.

We have never declared or paid any dividends on our common stock. We intend to retain any earnings to finance the operation and expansion of our business, and we do not anticipate paying any cash dividends in the future. As a result, investors may only receive a return on their investment in our Class A common stock if the market price of our common stock increases.

We will continue to incur increased costs as a result of being a public company.

As a public company, we have incurred and expect to continue to incur significant legal, accounting and other expenses. In addition, new rules implemented by the SEC and New York Stock Exchange require changes in corporate governance practices of public companies. We expect these rules and regulations to continue to increase our legal and financial compliance costs and to make some activities more time-consuming and costly. We will continue to incur additional costs associated with our public company reporting requirements. We expect these rules and regulations to make it more difficult and more expensive for us to obtain director and officer liability insurance, and we may be required to accept reduced policy limits and coverage or incur substantially higher costs to obtain the same or similar coverage. As a result, it may be more difficult for us to attract and retain qualified people to serve on our board of directors or as executive officers.

Provisions in our amended and restated certificate of incorporation and amended and restated bylaws and under Delaware law might discourage, delay or prevent a change of control of our company or changes in our management and, therefore, depress the trading price of our Class A common stock.

Our amended and restated certificate of incorporation and amended and restated bylaws contain provisions that could depress the trading price of our Class A common stock by acting to discourage, delay or prevent a change of control of our company or changes in our management that the stockholders of our company may deem advantageous. These provisions:

- provide for a dual class common stock structure, so that certain stockholders will have significant influence over all matters requiring stockholder approval, including the election of directors and significant corporate transactions, such as a merger or other sale of our company or its assets and which could discourage others from initiating any potential merger, takeover or other change of control transaction that other stockholders may view as beneficial;
- establish a classified board of directors so that not all members of our board of directors are elected at one time;
- authorize the issuance of “blank check” preferred stock that our board of directors could issue to increase the number of outstanding shares to discourage a takeover attempt;
- prohibit stockholder action by written consent, which requires all stockholder actions to be taken at a meeting of our stockholders;
- prohibit stockholders from calling a special meeting of our stockholders;
- provide that the board of directors is expressly authorized to make, alter or repeal our bylaws; and
- establish advance notice requirements for nominations for elections to our board of directors or for proposing matters that can be acted upon by stockholders at stockholder meetings.

Additionally, we are subject to Section 203 of the Delaware General Corporation Law, which generally prohibits a Delaware corporation from engaging in any of a broad range of business combinations with any “interested”

stockholder for a period of three years following the date on which the stockholder became an “interested” stockholder and which may discourage, delay, or prevent a change of control of our company.

Any provision of our amended and restated certificate of incorporation, bylaws or Delaware law that has the effect of delaying or deterring a change in control could limit the opportunity for our stockholders to receive a premium for their shares of our common stock, and could also affect the price that some investors are willing to pay for our Class A common stock.

Our amended and restated certificate of incorporation provides that the Court of Chancery of the State of Delaware will be the exclusive forum for substantially all disputes between us and our stockholders, which could limit our stockholders’ ability to obtain a favorable judicial forum for disputes with us or our directors, officers or employees.

Our amended and restated certificate of incorporation provides that the Court of Chancery of the State of Delaware is the exclusive forum for any derivative action or proceeding brought on our behalf; any action asserting a breach of fiduciary duty; any action asserting a claim against us arising pursuant to the Delaware General Corporation Law, our amended and restated certificate of incorporation or our bylaws; or any action asserting a claim against us that is governed by the internal affairs doctrine. The choice of forum provision may limit a stockholder’s ability to bring a claim in a judicial forum that it finds favorable for disputes with us or our directors, officers or other employees, which may discourage such lawsuits against us and our directors, officers and other employees. If a court were to find the choice of forum provision contained in our amended and restated certificate of incorporation to be inapplicable or unenforceable in an action, we may incur additional costs associated with resolving such action in other jurisdictions, which could harm our business and financial condition.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

Unregistered Sales of Equity Securities

Not applicable.

Use of Proceeds from our Initial Public Offering of Class A Common Stock

Not applicable.

Item 3. Defaults upon Senior Securities.

Not applicable.

Item 4. Mine Safety Disclosures.

Not applicable.

Item 5. Other Information.

On June 20, 2017, we held our annual meeting of stockholders (the Annual Meeting). At the Annual Meeting, our stockholders voted on five proposals, as described in the definitive proxy statement filed with the U.S. Securities and Exchange Commission on May 8, 2017. As disclosed in a Form 8-K filed on June 23, 2017, our stockholders approved, on an advisory basis, the frequency of future stockholder advisory votes on our executive compensation of “One Year.” In August 2017, based on the voting results and in consideration of the appropriate voting frequency at this time, our board of directors resolved that the company will hold an advisory vote on the compensation of our named executive officers every year.

Item 6. Exhibits.

See the Exhibit Index following the signature page to this Quarterly Report on Form 10-Q for a list of exhibits filed or furnished with this report, which Exhibit Index is incorporated herein by reference.

Exhibit Index

Exhibit Number	Description	Incorporation By Reference			
		Form	SEC File No.	Exhibit	Filing Date
3.1	Amended and Restated Certificate of Incorporation.	10-Q	001-37570	3.1	12/11/2015
3.2	Bylaws.	S-1	333-206312	3.4	9/9/2015
4.1	Form of Class A Common Stock Certificate of the Company.	S-1	333-206312	4.1	9/9/2015
4.2	Reference is made to Exhibits 3.1 and 3.2.				
31.1*	Certification of Principal Executive Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.				
31.2*	Certification of Principal Financial Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.				
32.1**	Certification of Principal Executive Officer and Principal Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.				
101.INS	XBRL Instance Document				
101.SCH	XBRL Taxonomy Extension Schema Document				
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document				
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document				
101.LAB	XBRL Taxonomy Extension Label Linkbase Document				
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document				

* Filed herewith.

** Furnished herewith.

