

NEOPHOTONICS CORP  
Form 10-Q/A  
April 09, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q/A

(Amendment No. 2)

(Mark One)

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

For the quarterly period ended March 31, 2013

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: 001-35061

NeoPhotonics Corporation

(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of

94-3253730  
(I.R.S. Employer

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incorporation or organization) Identification No.)

2911 Zanker Road

San Jose, California 95134

(Address of principal executive offices, zip code)

(408) 232-9200

(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 ("Exchange Act") 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 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 ☐

Accelerated filer ☒

Non-accelerated filer ☐ (Do not check if a smaller reporting company) Smaller reporting company ☐

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

As of April 30, 2013, there were 30,611,417 shares of the registrant's Common Stock outstanding.

## Explanatory Note

NeoPhotonics Corporation (the “Company”), is filing this Amendment No. 2 to its Quarterly Report on Form 10-Q (“Amendment No. 2”) to restate and amend the Company’s previously issued and unaudited interim financial statements and related financial information as of March 31, 2013 and for the three months ended March 31, 2013, which was originally filed with the Securities and Exchange Commission (the “SEC”) on May 15, 2013 and subsequently amended in Amendment No. 1 (“Amendment No. 1”) filed with the SEC on August 8, 2013. Amendment No. 1 was filed to adjust the Company’s consolidated statement of cash flows for the three months ended March 31, 2013 for amounts related to purchases of property and equipment that were overstated.

As disclosed in the Company’s Current Report on Form 8-K filed with the SEC on November 14, 2013, the Company determined that its unaudited condensed consolidated financial statements for the three months ended March 31, 2013 contained an error related to its accounting for a real estate registration tax which was incorrectly reflected as a component of the property, plant and equipment acquired as part of the purchase of NeoPhotonics Semiconductor (formerly the Optical Component Unit of LAPIS Semiconductor (“OCI”). In addition, the Company has made other corrections related to the purchase of NeoPhotonics Semiconductor, classification of certain amounts and other corrections, all of which were discovered during the close of its September 30, 2013 accounting records. For further information regarding the restatement, see Note 2 of the Notes to the Condensed Consolidated Financial Statements.

Because of the corrections described above, management re-evaluated the Company’s control environment and concluded that additional material weaknesses existed at March 31, 2013 as more fully described in Item 4 “Controls and Procedures” in this Amendment No. 2.

Consistent with the information described above, the Company has revised the following items in this Amendment No. 2:

### Part I

Item 1- Condensed Consolidated Financial Statements

Item 2 – Management’s Discussion and Analysis of Financial Condition and Results of Operations

Item 4 – Controls and Procedures

### Part II

Item 1A- Risk Factors

Additionally, in this Amendment No. 2, the Company is including currently dated certifications from the Company’s Principal Executive Officer and Principal Financial Officer as required by Section 302 of the Sarbanes-Oxley Act of 2002 in Exhibits 31.1 and 31.2 and a currently dated certification from the Company’s Principal Executive Officer and Principal Financial Officer as required by Section 906 of the Sarbanes-Oxley Act of 2002 in Exhibit 32.1.

Except to the extent described above and set forth herein, the items and other disclosures in the Form 10-Q initially filed on May 15, 2013 (the “initial Form 10-Q”) as previously amended by Amendment No. 1 are unchanged and this Amendment No. 2 does not reflect any events that have occurred after the initial Form 10-Q was filed. Accordingly, this Amendment No. 2 should be read in conjunction with the Company’s initial Form 10-Q (as amended by Amendment No. 1) and the Company’s subsequent filings with the United States Securities and Exchange Commission.

In light of the restatement, readers should not rely on the Company's previously filed financial statements as of and for the three month period ended March 31, 2013.

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NEOPHOTONICS CORPORATION

For the Quarter Ended March 31, 2013

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## PART I. FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
NEOPHOTONICS CORPORATION

## CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

	As of March 31, 2013 Restated and Revised, see Notes 2 and 7	December 31, 2012 Revised, see Note 2
(In thousands, except share and per share data)		
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$51,404	\$ 36,940
Short-term investments	48,356	64,301
Restricted cash	2,108	2,626
Accounts receivable, net of allowance for doubtful accounts	63,267	70,354
Inventories	61,859	43,793
Prepaid expenses and other current assets	10,480	7,630
Total current assets	237,474	225,644
Long-term investments	331	188
Property, plant and equipment, net	70,001	54,440
Other intangible assets, net	18,766	14,213
Other long-term assets	1,361	1,147
Total assets	\$327,933	\$ 295,632
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$40,817	\$ 36,308
Notes payable	10,431	12,003
Current portion of long-term debt	8,960	5,000
Accrued and other current liabilities	24,874	19,959
Total current liabilities	85,082	73,270
Long-term debt, net of current portion	42,170	17,167
Deferred income tax liabilities	655	653
Other noncurrent liabilities	8,147	1,862
Total liabilities	136,054	92,952

Commitments and contingencies (Note 10)

Stockholders' equity:

Preferred stock, \$0.0025 par value

At March 31, 2013 and December 31, 2012: 10,000,000 shares authorized, no shares issued or outstanding;

— —

Common stock, \$0.0025 par value

At March 31, 2013: 100,000,000 shares authorized, 30,604,293 shares issued and outstanding;

At December 31, 2012: 100,000,000 shares authorized, 30,546,155 shares issued and outstanding

76 76

Additional paid-in capital

440,144 438,858

Accumulated other comprehensive income

11,982 11,829

Accumulated deficit

(260,323) (248,083 )

Total stockholders' equity

191,879 202,680

Total liabilities and stockholders' equity

\$327,933 \$ 295,632

See accompanying Notes to Condensed Consolidated Financial Statements.

## NEOPHOTONICS CORPORATION

## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	Three Months Ended March 31, 2013 Restated and Revised, see Note 2		2012
(In thousands, except share and per share data)			
Revenue	\$56,063		\$54,223
Cost of goods sold	44,306		42,817
Gross profit	11,757		11,406
Operating expenses:			
Research and development	9,707		10,538
Sales and marketing	3,586		3,023
General and administrative	5,059		6,601
Acquisition-related transaction costs	4,510		394
Amortization of purchased intangible assets	321		354
Restructuring charges	325		130
Adjustment to fair value of contingent consideration	—		1,907
Total operating expenses	23,508		22,947
Loss from operations	(11,751	)	(11,541
Interest income	131		132
Interest expense	(163	)	(154
Other expense, net	(274	)	(275
Total interest and other expense, net	(306	)	(297
Loss before income taxes	(12,057	)	(11,838
Income tax (expense) benefit	(183	)	60
Loss from continuing operations	(12,240	)	(11,778
Income from discontinued operations, net of tax (including gain on disposal of \$636, net of tax, for the three months ended March 31, 2012)	—		170
Net loss	\$(12,240	)	\$(11,608
Basic and diluted net income (loss) per share:			
Continuing operations	\$(0.40	)	\$(0.47
Discontinued operations	\$—		\$0.01
Net loss	\$(0.40	)	\$(0.46
Weighted average shares used to compute basic and diluted net income (loss) per share:	30,574,032		24,870,684

See accompanying Notes to Condensed Consolidated Financial Statements.





NEOPHOTONICS CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(Unaudited)

	Three months ended March 31, 2013 Restated and Revised, see Note 2      2012	
(In thousands)		
Net loss	\$(12,240)	\$(11,608)
Foreign currency translation adjustments	172	125
Unrealized gain (loss) on investments, net of tax of \$0	(19 )	296
Comprehensive loss	\$(12,087)	\$(11,187)

See accompanying Notes to Condensed Consolidated Financial Statements.

## NEOPHOTONICS CORPORATION

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Three Months Ended March 31, 2013 Restated and Revised, see Note 2		2012
(In thousands)			
Cash flows from operating activities			
Net loss	\$(12,240)		\$(11,608)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:			
Depreciation and amortization	4,152		5,353
Asset impairment charges	34		14
Stock-based compensation expense	1,202		1,144
Deferred taxes	—		387
Loss on disposal of property and equipment	111		18
Gain on sale of discontinued operations	—		(750 )
Allowance for doubtful accounts	22		8
Write-down of inventories	30		721
Change in assets and liabilities, net of effects of acquisitions:			
Accounts receivable	7,155		9,155
Inventories	(4,682 )		(4,680 )
Prepaid expenses and other assets	(977 )		(1,800 )
Accounts payable	2,126		584
Acquisition-related transaction costs	3,948		—
Accrued and other liabilities	280		(184 )
Net cash provided by (used in) operating activities	1,161		(1,638 )
Cash flows from investing activities			
Purchase of property, plant and equipment	(5,134 )		(2,019 )
Purchase of marketable securities	(29,030)		(12,964)
Proceeds from sale of marketable securities	23,747		5,139
Proceeds from maturity of securities	20,900		15,100
Decrease in restricted cash	524		68
Acquisition of OCU, net of notes payable	(14,087)		—
Proceeds received on sale of discontinued operations, net of tax	—		1,825
Net cash provided by (used in) investing activities	(3,080 )		7,149
Cash flows from financing activities			
Proceeds from exercise of stock options	79		64
Proceeds from bank loans	26,443		—
Repayment of bank loans	(8,610 )		(1,250 )
Proceeds from issuance of notes payable	4,881		7,738
Repayment of notes payable	(6,482 )		(7,867 )

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Net cash provided by (used in) financing activities	16,311	(1,315 )
Effect of exchange rates on cash and cash equivalents	72	209
Net increase in cash and cash equivalents	14,464	4,405
Cash and cash equivalents at the beginning of the period	36,940	32,485
Cash and cash equivalents at the end of the period	\$51,404	\$36,890
Supplemental disclosure of noncash investing and financing activities:		
Issuance of notes to the seller of acquired business	\$11,130	\$—

See accompanying Notes to Condensed Consolidated Financial Statements.

NeoPhotonics Corporation

Notes to Condensed Consolidated Financial Statements

(Unaudited)

Note 1. Basis of presentation

The unaudited condensed consolidated financial statements of NeoPhotonics Corporation (“NeoPhotonics” or the “Company”) as of March 31, 2013 and December 31, 2012 and for the three months ended March 31, 2013 and 2012, have been prepared in accordance with the instructions on Form 10-Q pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”). In accordance with those rules and regulations, the Company has omitted certain information and notes normally provided in the Company’s annual consolidated financial statements. In the opinion of management, the condensed consolidated financial statements contain all adjustments, consisting only of normal recurring items, except as otherwise noted, necessary for the fair presentation of the Company’s financial position and results of operations for the interim periods. The year-end condensed balance sheet data was derived from audited financial statements, but does not include all disclosures required by U.S. generally accepted accounting principles (“U.S. GAAP”). These condensed consolidated financial statements should be read in conjunction with the Consolidated Financial Statements and Notes thereto included in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2012. The results of operations for the three months ended March 31, 2013 are not necessarily indicative of the results expected for the entire fiscal year. For purposes of these Notes to Condensed Consolidated Financial Statements, amounts have been restated and revised to give effect to the matters described in Note 2.

Consolidation

The condensed consolidated financial statements are prepared in accordance with U.S. GAAP and include the consolidated accounts of the Company and its majority owned subsidiaries. Intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in accordance with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported revenue and expenses during the reporting period. Significant estimates made by management include: the fair values of identifiable assets acquired and liabilities assumed in business combinations; the useful lives of property, plant and equipment and intangible assets as well as future cash flows to be generated by those assets; allowances for doubtful accounts; valuation allowances for deferred tax assets; write off of excess and obsolete inventories and the valuations of stock-based compensation, among others. Actual results could differ from these estimates.

Business Combinations—Acquisition Accounting

Under the acquisition method of accounting, the Company allocates the purchase price of acquired companies to the tangible and identifiable intangible assets acquired and liabilities assumed based on their estimated fair values. The Company records the excess of purchase price over the aggregate fair values of the tangible and identifiable intangible assets as goodwill. The Company determines the fair values of assets acquired and liabilities assumed. To establish fair value, the Company measures the price that would be received to sell an asset or paid to transfer a liability in an ordinary transaction between market participants. The measurement assumes the highest and best use of the asset by

the market participants that would maximize the value of the asset or the group of assets within which the asset would be used at the measurement date, even if the intended use of the asset is different.

The Company estimates the economic lives of certain acquired assets and these lives are used to calculate depreciation and amortization expenses. The Company estimates the future cash flows to be derived from such assets, and these estimates are used to determine the fair value of the assets. If any of these estimates change, depreciation or amortization expenses could be changed and/or the value of our intangible assets could be impaired.

Acquisition related costs, including real estate transaction taxes, finder's fees, advisory, legal, accounting, valuation and other professional or consulting fees are accounted for as expenses in the periods in which the costs are incurred or the services are received.

## Note 2. Restatement and Revision of unaudited condensed consolidated financial statements

The Company has restated and revised its March 31, 2013 unaudited condensed consolidated financial statements as described below.

The effects of the restatement and revisions on the condensed consolidated balance sheet as of March 31, 2013 are summarized in the following table:

March 31, 2013 (In thousands, except per share data)					
	Previously Reported	Corrections	Penalty Payment Derivative	Revision for Measurement Period Adjustments	Restated and Revised
<b>ASSETS</b>					
Current assets:					
Cash and cash equivalents	\$51,404	\$ —	\$ —	\$ —	\$51,404
Short-term investments	48,356	—	—	—	48,356
Restricted cash	2,108	—	—	—	2,108
Accounts receivable, net of allowance for doubtful accounts	63,267	—	—	—	63,267
Inventories	68,818	(212 )	—	(6,747 )	61,859
Prepaid expenses and other current assets	8,053	74	—	2,353	10,480
Total current assets	242,006	(138 )	—	(4,394 )	237,474
Long-term investments	331	—	—	—	331
Property, plant and equipment, net	65,079	2,156	—	2,766	70,001
Goodwill	2,188	(2,188 )	—	—	—
Other intangible assets, net	17,176	(72 )	—	1,662	18,766
Other long-term assets	4,206	(2,064 )	—	(781 )	1,361
Total assets	\$330,986	\$ (2,306 )	\$ —	\$ (747 )	\$327,933
<b>LIABILITIES, REDEEMABLE COMMON STOCK AND STOCKHOLDERS' EQUITY</b>					
Current liabilities:					
Accounts payable	\$40,963	\$ (146 )	\$ —	\$ —	\$40,817
Notes payable	10,431	—	—	—	10,431
Current portion of long-term debt	10,710	(1,750 )	—	—	8,960
Accrued and other current liabilities	23,520	1,225	—	129	24,874
Total current liabilities	85,624	(671 )	—	129	85,082
Long-term debt, net of current portion	40,420	1,750	—	—	42,170
Deferred income tax liabilities	655	—	—	—	655
Other noncurrent liabilities	10,506	(2,400 )	138	(97 )	8,147
Total liabilities	137,205	(1,321 )	138	32	136,054
Redeemable common stock	5,000	—	(5,000 )	—	—
Stockholders' equity:					
Preferred stock, \$0.0025 par value					
Common stock, \$0.0025 par value	76	—	—	—	76
Additional paid-in capital	435,282	—	4,862	—	440,144
Accumulated other comprehensive income	11,970	12	—	—	11,982
Accumulated deficit	(258,547)	(997 )	—	(779 )	(260,323)

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Total stockholders' equity	188,781	(985 )	4,862	(779 )	191,879
Total liabilities, redeemable common stock and stockholders' equity	\$330,986	\$ (2,306 )	\$ —	\$ (747 )	\$327,933

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The effects of the restatement and revision on the condensed consolidated statement of operations for the three months ended March 31, 2013 are summarized in the following table:

Three Months Ended March 31, 2013 (In thousands, except share and per share information)				
	Previously Reported	Corrections	Revision for Measurement Period Adjustments	Restated and Revised
Revenue	\$56,063	\$ —	\$—	\$56,063
Cost of goods sold	44,333	(27 )	—	44,306
Gross profit	11,730	27	—	11,757
Operating expenses:				
Research and development	9,707	—	—	9,707
Sales and marketing	3,586	—	—	3,586
General and administrative	8,545	1,024	—	9,569
Amortization of purchased intangible assets	321	—	—	321
Restructuring charges	325	—	—	325
Total operating expenses	22,484	1,024	—	23,508
Loss from operations	(10,754 )	(997 )	—	(11,751 )
Interest income	131	—	—	131
Interest expense	(163 )	—	—	(163 )
Other expense, net	(274 )	—	—	(274 )
Total interest and other expense, net	(306 )	—	—	(306 )
Loss before income taxes	(11,060 )	(997 )	—	(12,057 )
Income tax (expense) benefit	596	—	(779 )	(183 )
Net loss	\$(10,464 )	\$ (997 )	\$ (779 )	\$(12,240 )
Basic and diluted net loss per share:				
Net loss	\$(0.34 )			\$(0.40 )
Weighted average shares used to compute basic and diluted net loss per share	30,574,032			30,574,032

The effects of the restatement and revision on the condensed consolidated statement of comprehensive loss for the three months ended March 31, 2013 are summarized in the following table:

Three Months Ended March 31, 2013 (In thousands)				
	Previously Reported	Corrections	Revision for Measurement Period Adjustments	Restated and Revised
Net loss	\$(10,464)	\$ (997 )	\$ (779 )	\$(12,240)
Foreign currency translation adjustments	160	12	—	172
Unrealized loss on investments, net of tax of \$0	(19 )	—	—	(19 )
Comprehensive loss	\$(10,323)	\$ (985 )	\$ (779 )	\$(12,087)



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The effects of the restatement and revision on the condensed consolidated statement of cash flows for the three months ended March 31, 2013 are summarized in the following table:

	Three Months Ended March 31, 2013 (In thousands)			Revision for Measurement Period Adjustment	Restated and Revised
	Previously Reported <sup>1</sup>	Corrections			
Cash flows from operating activities					
Net loss	\$(10,464)	\$ (997 )	\$ (779)		\$(12,240)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:					
Depreciation and amortization	4,590	(438 )	—		4,152
Asset impairment charges	34	—	—		34
Stock-based compensation expense	1,202	—	—		1,202
Deferred taxes	(781 )	—	781		—
Amortization of premiums and discounts on investments	—	—	—		—
Loss on disposal of property and equipment	111	—	—		111
Gain on sale of discontinued operations	—	—	—		—
Allowance for doubtful accounts	22	—	—		22
Write-down of inventories	30	—	—		30
Others	—	—	—		—
Change in assets and liabilities, net of effects of acquisitions:					
Accounts receivable	7,155	—	—		7,155
Inventories	(4,682 )	—	—		(4,682 )
Prepaid expenses and other assets	(1,256 )	281	(2 )		(977 )
Accounts payable	4,014	(1,888 )	—		2,126
Acquisition-related transaction costs	3,190	758	—		3,948
Accrued and other liabilities	(1,462 )	1,742	—		280
Net cash provided by (used in) operating activities	1,703	(542 )	—		1,161
Cash flows from investing activities					
Purchase of property, plant and equipment	(5,134 )	—	—		(5,134 )
Purchase of marketable securities	(29,030)	—	—		(29,030)
Proceeds from sale of marketable securities	23,747	—	—		23,747
Proceeds from maturity of securities	20,900	—	—		20,900
Decrease in restricted cash	524	—	—		524
Acquisition of OCU, net of notes payable	(14,629)	542	—		(14,087)
Net cash provided by (used in) investing activities	(3,622 )	542	—		(3,080 )
Cash flows from financing activities					
Proceeds from exercise of stock options	79	—	—		79
Proceeds from bank loans	40,000	(13,557 )	—		26,443
Repayment of bank loans	(22,167)	13,557	—		(8,610 )
Proceeds from issuance of notes payable	4,881	—	—		4,881
Repayment of notes payable	(6,482 )	—	—		(6,482 )
Net cash provided by (used in) financing activities	16,311	—	—		16,311
Effect of exchange rates on cash and cash equivalents	72	—	—		72
Net increase in cash and cash equivalents	14,464	—	—		14,464
Cash and cash equivalents at the beginning of the period	36,940	—	—		36,940

Cash and cash equivalents at the end of the period	\$51,404	\$ —	\$ —	\$51,404
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<sup>1</sup>The Company's condensed consolidated statement of cash flows for the three months ended March 31, 2013 was previously restated for amounts related to purchases of property and equipment that were inadvertently overstated resulting in the overstatement of cash used in investing activities by \$1.1 million and the overstatement of net cash provided by operating activities by the same amount.

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## Corrections

Subsequent to the filing of its Quarterly Report on Form 10-Q/A (Amendment 1) for the period ended March 31, 2013, the Company determined that its condensed consolidated financial statements as of March 31, 2013 and for the three months then ended contained errors requiring restatement. As further described below, the restatement reflects corrections related to the purchase of NeoPhotonics Semiconductor (formerly the Optical Component Unit of LAPIS Semiconductor), classification of certain amounts and other corrections. The corrections include consideration of the related income tax effect.

### Purchase Accounting Corrections

The Company has concluded that a real estate registration tax in the amount of \$0.5 million was incorrectly allocated to acquired property, plant and equipment acquired as part of the purchase of NeoPhotonics Semiconductor and should have been expensed. Additionally, the Company identified (i) real estate acquisition tax in the amount of \$0.8 million that should have been accrued as an acquisition cost in the three months ended March 31, 2013, (ii) a correction to the estimated fair value of property and equipment that increased property and equipment and reduced goodwill by \$2.2 million, (iii) unrecorded liabilities related to purchases of property and equipment of \$0.3 million, (iv) unrecorded warranty obligations of \$0.1 million and (v) certain inventory adjustments in the amount of \$0.2 million.

### Classification Corrections

The Company has concluded that it incorrectly separately classified a long-term asset related to the pension obligation assumed in the purchase of NeoPhotonics Semiconductor in the amount of \$2.1 million that instead should have been netted against the long-term pension liability at March 31, 2013. Additionally, the Company (i) overstated the current portion of long-term debt by \$1.8 million at March 31, 2013, (ii) misclassified certain costs totaling \$0.1 million between cost of goods sold and operating expenses in the three months ended March 31, 2013 and (iii) misclassified \$1.7 million between the change in accounts payable and the change in accrued and other liabilities within operating activities and overstated both proceeds from and repayment of bank loans by \$13.6 million within financing activities in its condensed consolidated statement of cash flows for the three months ended March 31, 2013.

### Other Corrections

The Company has concluded that it had incorrectly recorded amounts related to an asset retirement obligation and amounts related to certain purchased software maintenance contracts, which resulted in an overstatement of other long-term liabilities of \$0.3 million and an overstatement of property, plant and equipment of \$0.2 million. The Company also overstated an amount payable to a vendor resulting in an overstatement of previously reported cost of goods sold of \$0.1 million for the three months ended March 31, 2013.

### Penalty Payment Derivative

As further described in Note 11, the Company may be required to pay a \$5.0 million penalty if it does not achieve certain performance obligations agreed to in connection with the sale of its common stock in a private placement transaction on April 27, 2012. The penalty payment was originally classified outside of equity as redeemable common stock at December 31, 2012 and March 31, 2013 since, while the Company intends to meet its performance obligations, it determined the ability to satisfy some of the obligations may be outside of the Company's control. The Company has since determined that the \$5.0 million penalty payment is an embedded derivative instrument, with the underlying being the performance or nonperformance of meeting its performance obligations by the deadline, and has thus classified \$4.9 million of the \$5.0 million to additional paid-in capital and the remaining \$0.1 million, representing the estimated fair value of the penalty payment derivative, to other noncurrent liabilities at March 31, 2013 and December 31, 2012. The effect on the Company's balance sheet at December 31, 2012 for this matter was as

follows:

(in thousands)	December 31, 2012	
	Previously Reported	As Revised
Other noncurrent liabilities	\$1,724	\$1,862
Redeemable common stock	5,000	—
Additional paid-in capital	433,996	438,858

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## Revision for Purchase Price Allocation Measurement Period Adjustments

With the reissuance of these condensed consolidated financial statements, the Company has revised its March 31, 2013 condensed consolidated balance sheet from amounts previously reported to reflect measurement period adjustments in the estimated fair value of inventory, property and equipment and other tangible and intangible assets acquired in the purchase of NeoPhotonics Semiconductor. The changes in estimated fair value resulted from additional information obtained subsequent to the Company's initial acquisition accounting. The Company also recorded a valuation allowance against the NeoPhotonics Semiconductor deferred tax assets as a measurement period adjustment due to additional information received subsequent to the Company's initial acquisition accounting.

## Notes to Condensed Consolidated Financial Statements

In addition to the above adjustments, there were computational errors in deriving certain footnote amounts included within the Company's previous Amendment No. 1 to its Quarterly Report on Form 10-Q/A. Those amounts have been corrected herein.

### Note 3. Significant accounting policies

Except as described in Note 2, there have been no changes in the Company's significant accounting policies for the three months ended March 31, 2013, as compared to the significant accounting policies described in its Annual Report on Form 10-K for the fiscal year ended December 31, 2012.

### Recent accounting pronouncements

In February 2013, the Financial Accounting Standard Board ("FASB") issued amendments to the FASB Accounting Standard Codification to improve the reporting of reclassifications out of accumulated other comprehensive income. The amendments require new disclosures for items reclassified out of accumulated other comprehensive income ("AOCI"), including (1) changes in AOCI balances by component and (2) significant items reclassified out of AOCI. The guidance does not amend any existing requirements for reporting net income or OCI in the financial statements. As this guidance only requires expanded disclosures, the adoption of this guidance did not have a material effect on the Company's consolidated financial statements.

In March 2013, the FASB issued amendments to the FASB Accounting Standard Codification, which indicates that the entire amount of a cumulative translation adjustment related to an entity's investment in a foreign entity should be released when there has been a (i) sale of a subsidiary or group of net assets within a foreign entity and the sale represents the substantially complete liquidation of the investment in the foreign entity, (ii) loss of a controlling financial interest in an investment in a foreign entity, or (iii) step acquisition for a foreign entity. The amendments are effective prospectively for fiscal years beginning after December 15, 2013. Early adoption is permitted. The adoption of this guidance is not expected to have a material impact to the Company's consolidated financial statements.

### Note 4. Discontinued operations

In the fourth quarter of 2011, the Company initiated a plan to sell a component of its business, Broadband, a subsidiary in China. The Company decided to sell Broadband because the nature of its operations was different than the core technology and strategy of the Company. On January 11, 2012, the Company entered into a purchase agreement with Guangdong Rainbow Electronic Ltd. (Rainbow) to dispose of its 100% equity interest in Broadband for a total cash consideration of RMB 13.0 million (\$2.1 million). The transaction closed on March 13, 2012. The

Company recognized a gain of \$0.6 million on the sale of Broadband, representing the difference between the consideration received and the net assets transferred to Rainbow, net of tax. The gain was included in income from discontinued operations, net of tax in the statement of operations for the three months ended March 31, 2012.

The results of operations associated with Broadband are presented as discontinued operations in the Company's consolidated statements of operations for the three months ended March 31, 2013 and 2012. Revenue and the components of net income related to the discontinued operations for all periods were as follows (in thousands):

	Three months ended March 31,	
	2013	2012
Revenue	\$ —	\$ 590
Income from discontinued operations before income taxes	—	284
Provision for income taxes	—	(114 )
Net income from discontinued operations	\$ —	\$ 170
Basic and diluted net income per share on discontinued operations	\$ —	\$ 0.01



## Note 5. Cash equivalents and investments and fair value disclosures

## Cash and cash equivalents

The following table summarizes the Company's unrealized gains and losses related to the cash equivalents and investments in marketable securities designated as available-for-sale (in thousands):

	As of March 31, 2013				As of December 31, 2012			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Cash and cash equivalents								
Money market funds	\$11	\$ —	\$ —	\$11	\$11	\$ —	\$ —	\$11
Short-term investments								
Money market funds	4,858	—	—	4,858	7,259	—	—	7,259
Corporate bonds	27,411	49	(6 )	27,454	23,151	43	(1 )	23,193
U.S. federal agencies	14,138	5	—	14,143	27,241	10	—	27,251
Foreign bonds and notes	—	—	—	—	4,682	14	—	4,696
Municipal obligations	1,901	—	—	1,901	1,902	—	—	1,902
Total investments in short-term investments	48,308	54	(6 )	48,356	64,235	67	(1 )	64,301
Total investments	\$48,319	\$ 54	\$ (6 )	\$48,367	\$64,246	\$ 67	\$ (1 )	\$64,312

As of March 31, 2013 and December 31, 2012, maturities of short-term investments are as follows (in thousands):

	March 31, 2013	December 31, 2012
Less than 1 year	\$ 39,647	\$ 51,861
Due in 1 to 2 years	4,811	10,550
Due in 2 to 5 years	2,008	—
Due after 5 years	1,901	1,901
Total	\$ 48,367	\$ 64,312

The Company may sell its security investments in the future to fund future operation needs. As a result, the Company recorded all its marketable securities in short-term investment as of March 31, 2013 and December 31, 2012, regardless of the contractual maturity date of the securities.

Realized gains and losses on the sale of marketable securities during the three months ended March 31, 2013 and 2012 were immaterial. The Company did not recognize any impairment losses on its marketable securities during the three months ended March 31, 2013 and 2012. As of March 31, 2013, the Company did not have any investments in marketable securities that were in an unrealized loss position for a period in excess of 12 months.

## Fair value disclosures

The following table sets forth the fair value of the Company's financial assets as of the dates presented (in thousands):

	As of March 31, 2013				As of December 31, 2012			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Money market funds	\$4,869	\$—	\$ —	\$4,869	\$7,270	\$—	\$ —	\$7,270
Marketable securities								
Corporate bonds	—	27,454	—	27,454	—	23,193	—	23,193
U.S. federal agencies	—	14,143	—	14,143	—	27,251	—	27,251
Foreign bonds and notes	—	—	—	—	—	4,696	—	4,696
Municipal obligations	—	1,901	—	1,901	—	1,902	—	1,902
	\$4,869	\$43,498	\$ —	\$48,367	\$7,270	\$57,042	\$ —	\$64,312

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Additionally, the Company's cash and cash equivalents at March 31, 2013 and December 31, 2012 included time deposits of \$11.9 million and \$14.7 million, respectively, for which the fair value approximates the carrying amount using inputs classified as level 2 in the fair value hierarchy.

The following table sets forth the fair value of the Company's financial liabilities as of the dates presented (in thousands):

	As of March 31, 2013				As of December 31, 2012			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Contingent consideration (Note 10)	\$—	\$ —	\$ 959	\$959	\$—	\$ —	\$ 959	\$959
Penalty payment derivative (Note 11)	\$—	\$ —	\$ 138	\$138	\$—	\$ —	\$ 138	\$138

Note 6. Net income (loss) per share attributable to NeoPhotonics Corporation common stockholders

The following table sets forth the computation of the basic and diluted net loss per share for the periods indicated (in thousands, except share and per share amounts):

	Three months ended March 31, 2013		2012	
<b>Numerator:</b>				
Loss from continuing operations	\$(12,240	)	\$(11,778	)
Income from discontinued operations, net of tax	—		170	
Net loss	\$(12,240	)	\$(11,608	)
<b>Denominator:</b>				
Weighted average shares used to compute basic and diluted net income (loss) per share	30,574,032		24,870,684	
<b>Basic and diluted net income (loss) per share:</b>				
Continuing operations	\$(0.40	)	\$(0.47	)
Discontinued operations	\$—		\$0.01	
Net loss	\$(0.40	)	\$(0.46	)

Shares of common stock subject to repurchase resulting from the early exercise of employee stock options are not considered participating securities and are therefore excluded from the basic weighted average common shares outstanding.

The following potentially dilutive securities were excluded from the computation of diluted net loss per share attributable to NeoPhotonics Corporation common stockholders, as their effect would have been antidilutive:

	March 31, 2013	2012
Employee stock options	2,758,964	2,613,907

Restricted stock units	848,867	662,944
Employee stock purchase plan	483,969	552,069
Common stock warrants	4,482	4,482
	4,096,282	3,833,402

## Note 7. Business Combination

### Optical Components Business Unit (OCU)

On March 29, 2013 (the “closing date”) the Company acquired certain assets and assumed certain liabilities related to the Optical Components Business Unit (the “OCU”) of Lapis Semiconductor Co., Ltd., a wholly owned subsidiary of Rohm Co., Ltd (“Lapis”) of Japan with the intention of operating the OCU as an ongoing business. The business is now known as NeoPhotonics Semiconductor.

The OCU is a leader in high speed semiconductor and high speed laser and photodetector devices for communications networks. The Company believes the acquisition will expand the Company’s solutions for high speed telecom and datacom applications and strengthen the Company’s customer base in Japan.

Total consideration for the OCU was approximately \$24.3 million, including cash of \$14.1 million paid upon closing and notes payable of \$11.1 million, partially offset by a net receivable from Lapis of \$1.0 million related to a working capital adjustment and certain other payments between the Company and Lapis. The cash of \$14.1 million includes \$2.0 million that was withheld and placed into escrow to cover certain indemnity obligations from the closing date through March 29, 2014. The notes payable of \$11.1 million are to be paid in three equal installments on the first, second and third anniversaries of the closing date. Each year an additional amount calculated as 1.5% per year of the unpaid balance of the notes becomes due. Lapis retains a lien on the land and building sold until the third payment is paid. The purchase price consideration and payment of notes payable are denominated in Japanese Yen.

In connection with the acquisition, the Company incurred approximately \$4.5 million in acquisition-related transaction costs related to investment banking, legal, accounting and other professional services and fees and transfer and acquisition taxes related to real property acquired. The acquisition costs were expensed as incurred and were included in operating expenses in the Company's condensed consolidated statement of operations in the first quarter of 2013.

The OCU's results of operations between the closing date of March 29, 2013 and the Company's quarter end date of March 31, 2013 were immaterial.

#### Assets Acquired and Liabilities Assumed

The Company accounted for its acquisition of the OCU assets and assumed liabilities as a business combination. The OCU's tangible and identifiable intangible assets acquired and liabilities assumed were recorded based upon their estimated fair values as of the closing date of the acquisition. After consideration of the purchase accounting corrections (see Note 2) the estimated fair values of the identifiable assets acquired and liabilities assumed approximated the purchase price; therefore, no goodwill was recorded. A preliminary assessment of the fair value of assets acquired and liabilities assumed ("initial preliminary fair value assessment") was made as of March 29, 2013.

During the quarter ended September 30, 2013 the Company updated its initial preliminary fair value assessment and has reflected the resulting measurement period adjustments as Revisions in the accompanying March 31, 2013 condensed consolidated balance sheet. These adjustments were based on additional information received subsequent to the Company's initial assessment that had a significant impact on a number of assumptions, including those related to inventory obsolescence, gross margin and working capital. The adjustments include a decrease in the fair value of inventory of \$6.7 million and increases in the fair value of property, plant and equipment of \$2.8 million and customer relationships of \$1.7 million.

The following table summarizes the acquisition accounting and the tangible and intangible assets acquired (in thousands):

Total purchase consideration:	
Cash paid upon closing	\$ 14,087
Net receivable from Lapis	(959 )
Notes payable	11,130
	\$24,258

Liabilities assumed:	
Pension and retirement obligations	\$6,471
Other compensation-related liabilities	1,083

Other current liabilities	1,265
	\$8,819
Fair value of assets acquired:	
Inventory	\$13,309
Other current assets	35
Land, property, plant and equipment <sup>(1)</sup>	14,433
Intangible assets acquired:	
Developed technology	2,120
Customer relationships	3,180
	\$33,077

<sup>(1)</sup>Includes land of \$3.5 million, buildings of \$3.9 million and machinery, equipment, furniture and fixtures of \$7.0 million.

The approach for measuring the fair value of the assets acquired and liabilities assumed is described below:

#### Net Tangible Assets

The OCU's tangible assets acquired and liabilities assumed as of March 29, 2013 were recorded at estimated fair value with the exception of the pension and retirement obligations. The Company estimated fair value by adjusting the OCU's historical value of property, plant and equipment to an estimate of depreciated replacement cost, adjusted for economic obsolescence. The Company depreciates property, plant and equipment over estimated lives of 2 to 10 years, and records the expense to cost of goods sold and operating expense. The fair value of inventory acquired was determined using a net realizable value approach based upon the expected sales value of the inventory, less any costs to complete and selling costs along with a reasonable profit margin based on historical and expected results. The fair value of accrued liabilities approximated the amounts due under the arrangements with employees and vendors due to short maturity. Pensions and retirement obligations are recorded to the extent the projected benefit obligation exceeded the fair value of the plan assets estimated as of March 29, 2013. The projected benefit obligation is measured at the actuarial present value of all benefits attributed by the plan's benefit formula to employee service rendered before March 29, 2013.

#### Intangible Assets

Developed technology represents products that have reached technological feasibility. The OCU's current product offerings include high speed semiconductor and high speed laser and photodetector devices for communication networks. The fair value of developed technology intangibles acquired was determined by using a royalty-avoidance method. The share of future revenue relating to current technology was forecasted, using an estimate for obsolescence such that the share declines over time. A royalty rate of two percent was used to calculate royalty savings on that revenue that are avoided since the Company owns the technology and does not need to license it from other parties. The after-tax royalty savings was then discounted to present value using the Company's discount rate. The Company amortizes the developed technology intangible assets over estimated lives of 4 to 5 years, and amortization expense is recorded to cost of goods sold.

The customer relationships asset represents the value of the ability to sell existing, in-process, and future versions of the technology to the OCU existing customer base. The Company utilized the excess earnings method, estimating future cash flows that will result from existing customers given assumed retention rates, and then discounting those flows to their present value using the Company's discount rate. The Company amortizes the customer relationships intangible asset over an average estimated life of 6 years, and amortization expense is recorded to operating expenses.

The weighted average amortization period for the total amount of intangible assets acquired is 5.4 years.

#### Pro Forma Financial Information

The unaudited financial information in the table below summarizes the combined results of operations of the Company with the results of OCU prior to the acquisition, on a pro forma basis, as though the companies had been combined as of the beginning of the period presented. The pro forma financial information for the quarter ended March 31, 2013 includes elimination of \$4.5 million of transaction costs and \$1.9 million of revenue and \$1.8 million of costs related to sales from OCU to the Company. The pro forma financial information for the quarter ended March 31, 2012 includes elimination of \$0.4 million of revenue and \$0.3 million of costs related to sales from OCU to the Company and a \$2.5 million increase in cost of goods sold due to a change in the value of inventory as a result of acquisition accounting. The pro forma financial information is presented for informational purposes only and is not indicative of the results of operations that would have been achieved had the acquisition taken place at the beginning of the period presented, nor does it intend to be a projection of future results.

	For the three months ended March 31,	
	2013	2012
Revenue	\$68,754	\$67,537
Net loss	\$(5,277 )	\$(12,038)
Basic and diluted net loss per share	\$(0.17 )	\$(0.48 )



## Note 8. Balance sheet components

## Accounts receivable, net

Accounts receivable, net consists of the following (in thousands):

	March 31, 2013	December 31, 2012
Accounts receivable	\$ 58,878	\$ 66,338
Trade notes receivable	5,375	4,979
Allowance for doubtful accounts	(986 )	(963 )
	\$ 63,267	\$ 70,354

## Inventories

Inventories consist of the following (in thousands):

	March 31, 2013	December 31, 2012
Raw materials	\$ 26,332	\$ 20,520
Work in process	20,560	8,603
Finished goods (1)	14,967	14,670
	\$ 61,859	\$ 43,793

(1) Finished goods inventory at offsite managed inventory locations was \$4.8 million and \$4.5 million as of March 31, 2013 and December 31, 2012, respectively.

## Purchased intangible assets

Purchased intangible assets consist of the following (in thousands):

	March 31, 2013			December 31, 2012		
	Gross Assets	Accumulated Amortization	Net Assets	Gross Assets	Accumulated Amortization	Net Assets
Technology and patents	\$34,295	\$ (23,405 )	\$ 10,890	\$32,176	\$ (22,869 )	\$ 9,307
Customer relationships	15,128	(8,392 )	6,736	11,898	(8,148 )	3,750
Leasehold interest	1,358	(234 )	1,124	1,355	(241 )	1,114
Noncompete agreements	950	(934 )	16	950	(908 )	42
	\$51,731	\$ (32,965 )	\$ 18,766	\$46,379	\$ (32,166 )	\$ 14,213

Amortization expense relating to technology and patents and the leasehold interest intangible assets is included within cost of goods sold, and customer relationships and the noncompete agreements within operating expenses. The following table presents details of the amortization expense of the Company's purchased intangible assets as reported in the condensed consolidated statements of operations (in thousands):

	Three months ended	
	March 31,	
	2013	2012
Cost of goods sold	\$ 428	\$ 598
Operating expenses	321	354
Total	\$ 749	\$ 952

The estimated future amortization expense of purchased intangible assets as of March 31, 2013, is as follows (in thousands):

2013 (remaining 9 months)	\$3,617
2014	4,505
2015	4,490
2016	3,743
2017	814
Thereafter	1,597
	\$18,766

Accrued and other current liabilities

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

	March 31, 2013	December 31, 2012
Employee-related	\$ 9,731	\$ 12,293
Other	15,143	7,666
	\$ 24,874	\$ 19,959

Warranty Accrual

The Company provides warranties to cover defects in workmanship, materials and manufacturing for a period of one to two years to meet the stated functionality as agreed to in each sales arrangement. Products are tested against specified functionality requirements prior to delivery, but the Company nevertheless from time to time experiences claims under its warranty guarantees. The Company accrues for estimated warranty costs under those guarantees based upon historical experience, and for specific items, at the time their existence is known and the amounts are determinable.

The table below summarizes the movement in the warranty accrual (in thousands):

	Three months ended March 31,	
	2013	2012
Beginning balance	\$ 1,072	\$ 1,443
Warranty accruals	26	19
Settlements and adjustments	86	(247 )
Ending balance	\$ 1,184	\$ 1,215

Restructuring charges

During the three months ended March 31, 2013, the Company exited and closed one facility at its headquarters location to align its facilities usage with its current size. As a result, the Company recorded a restructuring charge related to the facility impairment of approximately \$0.3 million. As of March 31, 2013, the remaining balance of this restructuring obligation was \$0.3 million, which the Company expects to pay through 2015.

Other noncurrent liabilities

Other noncurrent liabilities consist of the following (in thousands):

	March 31, 2013	December 31, 2012
Employee-related	\$6,712	\$ 188
Penalty payment derivative (Note 11)	138	138
Other	1,297	1,536
	\$8,147	\$ 1,862

## Note 9. Debt

The Company records debt at its carrying amount. The Company uses a market approach to determine fair value, which results in a Level 2 fair value measurement. The following table provides the components of debt, obligations, weighted average interest rate and additional fair value information relating to the Company's outstanding debt instruments (in thousands, except percentages):

	March 31, 2013		Weighted Average Interest Rate		December 31, 2012		Weighted Average Interest Rate
	Carrying Amount	Fair Value			Carrying Amount	Fair Value	
Notes payable	\$10,431	\$10,431			\$12,003	\$12,003	
Notes payable related to OCU acquisition	3,710	3,710	1.50	%	-	-	
Short-term debt	5,250	5,250	5.00	%	5,000	4,892	2.20 %
Total short-term debt	\$8,960	\$8,960			\$5,000	\$4,892	
Long-term notes payable related to OCU acquisition	7,420	7,420	1.50	%	-	-	
Long-term debt	34,750	34,750	4.91	%	17,167	16,336	2.20 %
Total long-term debt	\$42,170	\$42,170			\$17,167	\$16,336	
Notes payable							

The Company frequently directs its banking partners to issue notes payable to its suppliers in China in exchange for accounts payable. These banks issue notes to vendors and issue payment to the vendors upon redemption. The Company owes the payable balance to the issuing bank. These notes are unsecured, noninterest bearing and are due approximately six months after issuance. As a condition of the notes payable lending arrangements, the Company is required to keep a compensating balance at the issuing banks that is a percentage of the total notes payable balance until the notes payable are paid by its subsidiaries in China. These balances are classified as restricted cash on the Company's condensed consolidated balance sheets. As of March 31, 2013, restricted cash totaled \$2.1 million.

## Notes payable for OCU acquisition

In connection with the acquisition of OCU on March 29, 2013, the Company is obligated to pay \$11.1 million in three equal installments on the first, second and third anniversaries of the closing date for the purchase of the real estate used by the OCU. The payment is denominated in Japanese Yen. The amount presented in the table is the short-term portion of \$3.7 million and the long-term portion of \$7.4 million. The obligation bears interest at 1.5% per year and the real property is security for the loan.

## Long-term debt

The Company has lending arrangements with several financial institutions, including a loan and security agreement with Comerica Bank in the U.S., which has been amended several times. As of December 31, 2012, the Company's loan and security agreement in the U.S. included the following components:

- As of December 31, 2012, \$8.0 million was outstanding under the revolving line of credit agreement and \$0.0 million was available for borrowing. Borrowings under this facility bear interest at a rate of LIBOR plus 2%.

- As of December 31, 2012, no amounts were outstanding under the equipment advance line advance and all \$7.0 million was available for borrowing. Borrowings under this facility would bear interest at a rate of LIBOR plus 2%.
- As of December 31, 2012, \$14.2 million was outstanding under the acquisition advance and \$5.8 million was available for borrowing. The advances bear interest at a rate of LIBOR plus 2%.

On March 21, 2013, the Company amended and restated in its entirety the Loan and Security Agreement with the same bank and added East-West Bank as a lender. The components of the available credit facilities as of March 31, 2013 are as follows:

- As of March 31, 2013, \$12.0 million was outstanding under the revolving line of credit agreement and \$8.0 million was available for borrowing. Amounts are due on or before March 2016 and borrowings under this revolving line of credit include an interest rate option of a base rate as defined in the agreement plus 1.5% or LIBOR plus 2.5%.
- As of March 31, 2013, \$28.0 million was outstanding under the term loan of the credit facility and interest is payable quarterly in arrears; the principal is paid in equal quarterly installments over the term of the loan ending in June 2017. Borrowings under the term loan include an interest rate option of a base rate as defined in the agreement plus 1.75% or LIBOR plus 2.75%.

The Company's U.S. loan and security agreement requires it to maintain specified financial covenants, including a liquidity ratio, restricts its ability to incur additional debt or to engage in specified transactions and is secured by substantially all of its U.S. assets, other than intellectual property assets. As of March 31, 2013 and December 31, 2012, the Company was in compliance with the covenants contained in this agreement.

In connection with the original loan and security agreement in 2007, the Company issued a warrant to Comerica Bank to purchase 4,482 shares of common stock at an exercise price of \$29.00 per share. As of March 31, 2013, the warrant had not been exercised.

#### Note 10. Commitments and contingencies

##### Leases

The Company leases various facilities under noncancelable operating leases. As of March 31, 2013, the future minimum commitments under all operating leases are as follows (in thousands):

2013 (remaining 9 months)	\$1,593
2014	1,385
2015	1,188
2016	666
2017	500
Thereafter	968
	\$6,300

Rent expense under the Company's operating leases was \$0.6 million and \$0.5 million for the three months ended March 31, 2013 and 2012, respectively.

##### Litigation

From time to time, the Company is subject to various claims and legal proceedings, either asserted or unasserted, that arise in the ordinary course of business. The Company accrues for legal contingencies if the Company can estimate the potential liability and if the Company believes it is more likely than not that the case will be ruled against it. If a legal claim for which the Company did not accrue is resolved against it, the Company would record the expense in the

period in which the ruling was made. The Company does not believe that the ultimate amount of liability, if any, for any pending claims of any type (alone or combined) will materially affect the Company's financial position, results of operations or cash flows. The ultimate outcome of any litigation is uncertain, however, and unfavorable outcomes could have a material negative impact on the Company's financial condition and operating results. Regardless of outcome, litigation can have an adverse impact on the Company because of defense costs, negative publicity, diversion of management resources and other factors.



On January 5, 2010, Finisar Corporation, or Finisar, filed a complaint in the U.S. District Court for the Northern District of California against Source Photonics, Inc., MRV Communications, Inc., Oplink Communications, Inc. and the Company, or collectively, the co-defendants. In the complaint, Finisar alleged infringement of certain of its U.S. patents arising from the codefendants' respective manufacture, importation, use, sale of or offer to sell certain optical transceiver products. Finisar sought to recover unspecified damages, up to treble the amount of actual damages, together with attorneys' fees, interest and costs. Finisar alleged that at least some of the patents asserted are a part of certain digital diagnostic standards for optoelectronics transceivers, and, therefore, are being utilized in such digital diagnostic standards. On March 23, 2010, the Company filed an answer to the complaint and counterclaims, asserting two claims of patent infringement and additional claims asserting that Finisar has violated state and federal competition laws and violated its obligations to license on reasonable and non-discriminatory terms. On May 5, 2010, the court dismissed without prejudice all co-defendants (including the Company) except Source Photonics, Inc., on grounds that such claims should have been asserted in four separate lawsuits, one against each defendant. This dismissal without prejudice does not prevent Finisar from bringing a new similar lawsuit against the Company. The Company and Finisar had agreed to suspend their respective claims for a 90 day period and not to refile the originally asserted claims against each other until one or more specified events occur resulting in the partial or complete resolution of the litigation between Source Photonics and Finisar. On September 10, 2010, Source Photonics and Finisar settled their lawsuit, commencing the suspension period, which ended in December 2010. On January 18, 2011, the Company and Finisar again agreed to suspend their respective claims and not to refile the originally asserted claims against each other until at least 90 days after one or more specified events occur resulting in the partial or complete resolution of litigation involving the same Finisar patents between Oplink Communications, Inc. and Finisar. This tolling period expired on April 30, 2012. On May 3, 2012 the Company and Finisar agreed to further toll their respective claims until the refiling of certain of the previously asserted claims from this dispute. As a result, Finisar is permitted to bring a new lawsuit against the Company if it chooses to do so, and the Company may bring new claims against Finisar upon seven days written notice prior to filing such claims. The Company is currently unable to predict the outcome of this dispute and therefore cannot determine the likelihood of loss nor estimate a range of possible loss.

#### Indemnifications

In the normal course of business, the Company enters into agreements that contain a variety of representations and warranties and provide for general indemnification. The Company's exposure under these agreements is unknown because it involves claims that may be made against the Company in the future, but have not yet been made. To date, the Company has not paid any claims or been required to defend any action related to its indemnification obligations. However, the Company may record charges in the future as a result of these indemnification obligations. As of March 31, 2013, the Company does not have any material indemnification claims that were probable or reasonably possible.

#### Purchase obligations

The Company has purchase obligations with certain suppliers for the purchase of goods and services entered in the ordinary course of business. As of March 31, 2013, total outstanding purchase obligations were \$26.2 million, primarily due within the next 12 months.

#### Other contingencies

In connection with the Company's acquisition of Santur that the Company completed in October 2011, the Company may be required to pay up to an additional \$7.5 million in cash as further consideration for the business acquisition, contingent upon Santur's gross profit performance during 2012. The fair value of the contingent consideration is re-measured each reporting period and any changes in the fair value of the contingent consideration are recognized as a gain or loss in the consolidated statements of operations. As of March 31, 2013 and December 31, 2012, the Company estimated the fair value of the contingent consideration was \$1.0 million and \$1.0 million, respectively, and has included this liability within accrued and other current liabilities in its condensed consolidated balance sheets.

The Company classifies this liability within level 3 as it is valued using significant unobservable inputs. To estimate the fair value, the Company used Santur's gross profit as defined in the acquisition agreement and an estimated discount rate. Although the Company believes the fair value of the contingent consideration is in accordance with the terms of the Santur acquisition agreements, the selling parties dispute the final amount to be paid. Any adjustment to the fair value of the contingent consideration may impact the results of operations in the period the adjustment is made.

## Note 11. Stockholders' equity

## Common Stock

As of March 31, 2013, the Company had reserved the following shares of authorized but unissued common stock:

	Common Stock
Stock option plans	5,088,612
Stock purchase plan	257,734
Warrants	4,482
	5,350,828

## Private Sale of Common Stock

On April 27, 2012, the Company issued and sold approximately 4.97 million shares of its common stock in a private placement transaction at a price of \$8.00 per share for a gross amount of approximately \$39.8 million.

The shares of common stock are restricted from transfer pursuant to a lockup agreement for up to two years, at the end of which the Company is obligated to file one or more registration statements covering the potential resale of the shares of common stock.

In connection with this private placement transaction, the Company agreed to certain performance obligations including establishing a wholly-owned subsidiary in the Russian Federation and making a \$30.0 million investment commitment (the 'Investment Obligation') towards the Company's Russian operations. The Investment Obligation can be partially satisfied by investment outside of the Russian Federation and/or by way of non-cash asset transfers, including but not limited to capital equipment, small tools, intellectual property, and other intangibles. A minimum of \$15.0 million of the Investment Obligation is required to be satisfied by making capital expenditures and the remaining \$15.0 million can be satisfied through general working capital and research and development expenditures. All of the amount for general working capital can be spent either inside or outside of Russia. However, at least 80% of the amount expended for research and development expenditure must be spent inside Russia. General working capital can include acquisition of other businesses or portions thereof to be owned by the Russian subsidiary.

The purchaser of the common stock has non-transferable veto rights over the Company's Russian subsidiary's annual budget during the investment period and must approve non-cash asset transfers to be made in satisfaction of the Investment Obligation. Spending and/or commitments to spend for general working capital and research and development do not require approval by the purchaser. There are no legal restrictions on the specific usage of the \$39.8 million received in the private placement transaction or on withdrawal from the Company's bank accounts for use in general corporate purposes.

The Company is required to satisfy the Investment Obligation by July 31, 2014 or, in the event the Company has not recorded aggregate revenue from sales of its products in the Russian Federation of at least \$26.8 million during the period beginning July 1, 2012 and ending June 30, 2014, then will be automatically extended from July 31, 2014 to March 31, 2015. The Company expects the date for achievement of the Investment Obligation will be extended to March 31, 2015. Therefore, the Company intends to meet its Investment Obligation by March 31, 2015. If the Company fails to meet the Investment Obligation by the deadline, including failure to meet the Investment Obligation because the purchaser of the common stock does not approve the transfer of non-cash assets, the Company will be required to pay a \$5.0 million penalty (the 'Penalty Payment') as the sole and exclusive remedy for damages and monetary relief available to the purchaser for failure to meet the Investment Obligation.

The Company has accounted for the \$5.0 million Penalty Payment as an embedded derivative instrument, with the underlying being the performance or nonperformance of meeting the Investment Obligation by the extended deadline of March 31, 2015 and has classified \$4.9 million of the \$5.0 million as additional paid-in capital and the remaining \$0.1 million, representing the estimated fair value of the Penalty Payment derivative, as other noncurrent liabilities.

The fair value of the Penalty Payment derivative has been estimated at the date of the original common stock sale (April 27, 2012) and at each subsequent balance sheet date using a probability-weighted discounted future cash flow approach using unobservable inputs, which are classified as Level 3 within the fair value hierarchy. The primary inputs for this approach include the probability of achieving the Investment Obligation and a discount rate that approximates the Company's incremental borrowing rate. After the initial measurement, changes in the fair value of this derivative were recorded in other income (expense). The change in fair value of the Penalty Payment derivative from April 27, 2012 to December 31, 2012 and to March 31, 2013 was not significant.

## Accumulated Deficit

Approximately \$6.3 million of the Company's accumulated deficit at December 31, 2012 was subject to restriction due to the fact that the Company's subsidiaries in China are required to set aside at least 10% of their respective accumulated profits each year to fund statutory common reserves as well as allocate a discretionary portion of their after-tax profits to their staff welfare and bonus fund.

## Equity Incentive Programs

The Company grants stock options, restricted stock units, stock appreciation units and stock purchase rights pursuant to stockholder and board approved equity incentive plans. These equity incentive plans are described in further detail in Note 12 of the Notes to Consolidated Financial Statements in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2012.

## Stock options and restricted stock units

The following table summarizes the Company's stock option activity during the three months ended March 31, 2013:

	Stock Options			Restricted Stock Units	
	Shares available for grant	Number of shares	Weighted average exercise price	Number of units	Weighted average grant date fair value
Balance at December 31, 2012	382,668	2,773,887	\$ 5.87	924,823	\$ 5.84
Authorized for issuance	1,069,115	-	0.00	-	0.00
Granted	(30,000 )	17,800	5.60	12,200	5.74
Exercised/Converted	-	(18,251 )	4.32	(51,634 )	6.12
Forfeited	58,998	(14,472 )	8.43	(36,522 )	5.84
Balance at March 31, 2013	1,480,781	2,758,964	\$ 5.86	848,867	\$ 5.82

The following table summarizes information about stock options outstanding as of March 31, 2013:

	Options Outstanding			
	Number of shares	Weighted average exercise price	Weighted average remaining contractual term (years)	Aggregate intrinsic value (in thousands)
Vested and expected to vest	2,700,303	\$ 5.87	6.39	\$ 1,228
Exercisable	1,902,220	\$ 5.67	5.50	\$ 1,143

The intrinsic value of options vested and expected to vest and exercisable as of March 31, 2013 is calculated based on the difference between the exercise price and the fair value of the Company's common stock as of March 31, 2013. The intrinsic value of options exercised during the three months ended March 31, 2013 and 2012 was \$16,000 and

\$14,000, respectively.

The following table summarizes information about restricted stock units outstanding as of March 31, 2013:

Restricted Stock Units Outstanding				
	Number	Weighted	Weighted	Aggregate
	of	average	average	intrinsic value
	shares	grant date	remaining	
		fair value	contractual	(in thousands)
			term	
			(years)	
Vested and expected to vest	782,071	\$ 5.82	1.15	\$ 3,996

The intrinsic value of restricted stock units vested and expected to vest as of March 31, 2013 is calculated based on the fair value of the Company's common stock as of March 31, 2013. The intrinsic value of restricted stock units converted during the three months ended March 31, 2013 and 2012 was \$301,000 and \$0, respectively.

## Stock appreciation units

The following table summarizes the Company's stock appreciation unit activity during the three months ended March 31, 2013:

	Stock Appreciation Units	Weighted average exercise price
Stock appreciation units outstanding as of December 31, 2012	212,534	\$ 7.07
Stock appreciation units cancelled	(4,423 )	8.93
Stock appreciation units exercised	(316 )	4.25
Stock appreciation units outstanding as of March 31, 2013	207,795	\$ 7.04

The following table summarizes information about stock appreciation units outstanding as of March 31, 2013:

Stock Appreciation Units Outstanding				
	Number of units	Weighted average exercise price	Weighted average remaining contractual term (years)	Aggregate intrinsic value (in thousands)
Vested and expected to vest	207,396	\$ 7.03	5.86	\$ 101
Exercisable	181,913	\$ 6.71	5.69	\$ 98

The intrinsic value of stock appreciation units vested and expected to vest and exercisable as of March 31, 2013 is calculated based on the difference between the exercise price and the fair value of the Company's common stock as of March 31, 2013. The intrinsic value of stock appreciation units exercised during the three months ended March 31, 2013 and 2012 was \$0 and \$6,000, respectively.

## Note 12. Stock-based compensation

## Stock-based compensation expense

The Company's stock-based compensation expense was recorded as follows (in thousands):

	Three months ended March 31,	
(in thousands)	2013	2012
Cost of goods sold	\$ 243	\$ 188

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Research and development	418	469
Sales and marketing	238	209
General and administrative	303	278
	\$ 1,202	\$ 1,144

Stock options

The following tables summarize the components of stock-based compensation expense for stock options for the three months ended March 31, 2013 and 2012, respectively (in thousands):

	Three months ended March 31,	
	2013	2012
Cost of goods sold	\$ 79	\$ 61
Research and development	174	209
Sales and marketing	78	94
General and administrative	173	174
	\$ 504	\$ 538

The weighted-average fair value of options granted was \$3.80 and \$4.33 per share for the three months ended March 31, 2013 and 2012, respectively. At March 31, 2013, there was \$3.1 million of unrecognized stock-based compensation expense that will be recognized over the remaining weighted-average period of 2.41 years.



The Company estimated the fair value of all employee stock options using a Black-Scholes valuation model with the following assumptions:

Stock Options	Three months ended March 31,			
	2013		2012	
Weighted-average expected term (years)	6.55		6.71	
Weighted-average volatility	76	%	71	%
Risk-free interest rate	1.08	%	1.81	%
Expected dividends	0	%	0	%

Expected term. The expected term was estimated using the Company's historical and expected future exercise behavior.

Volatility. Due to the limited history of the trading of the Company's common stock since the initial public offering in February 2011, the expected volatility used by the Company is based on the actual volatility of similar entities. In evaluating similarity, factors such as industry, stage of life cycle, size, and financial leverage are taken into consideration. The term over which volatility was measured was commensurate with the expected term.

Risk-free interest rate. The risk-free rate that the Company uses in the Black-Scholes option valuation model is based on U.S. Treasury zero-coupon issues with remaining terms similar to the expected term.

Expected dividends. The Company has never declared or paid any cash dividends and does not plan to pay cash dividends in the foreseeable future, and, therefore, used an expected dividend yield of zero in the valuation model.

The Company is required to estimate forfeitures at the time of grant and revise those estimates in subsequent periods if actual forfeitures differ from those estimates. The Company uses historical data to estimate pre-vesting option forfeitures and record stock-based compensation expense only for those awards that are expected to vest. All stock-based payment awards are amortized on a straight-line basis over the requisite service periods of the awards, which are generally the vesting periods.

#### Stock appreciation units

Stock appreciation units are remeasured each period at fair value. The following table summarizes the expense (credit) recognized for stock appreciation units for the three months ended March 31, 2013 (in thousands):

	Three months ended March 31,	
	2013	2012
Cost of goods sold	\$ (24 )	\$ (5 )
Research and development	(32 )	(9 )
Sales and marketing	(13 )	(4 )
General and administrative	(9 )	(3 )
	\$ (78 )	\$ (21 )

As of March 31, 2013 and December 31, 2012, the liabilities for the settlement of the stock appreciation units were \$0.3 million and \$0.4 million, respectively and were included in accrued and other current liabilities on the condensed

consolidated balance sheet.

Based on the fair value of the stock appreciation units as of March 31, 2013, the Company had \$0.05 million of unrecognized stock-based compensation expense that would be recognized over the remaining weighted-average period of 1.10 years. The Company estimated the fair value of all employee stock appreciation units using a Black-Scholes valuation model with the following assumptions:

	Three months ended	
	March 31,	
	2013	2012
Stock appreciation units		
Weighted-average expected term (years)	2.61	3.39
Weighted-average volatility	63%	69%
Risk-free interest rate	0.20 - 0.46%	0.42 - 1.04%
Expected dividends	0%	0%

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**Expected term.** Vested stock appreciation units first become exercisable upon the expiration of the lock-up period associated with the initial public offering. Therefore, the Company estimated the term of the award based on an average of the weighted-average exercise period and the remaining contractual term.

**Volatility.** Due to the limited history of the trading of the Company's common stock since the initial public offering in February 2011, the expected volatility used by the Company is based on the actual volatility of similar entities. In evaluating similarity, factors such as industry, stage of life cycle, size, and financial leverage are taken into consideration. The term over which volatility was measured was commensurate with the expected term.

**Risk-free interest rate.** The risk-free rate that the Company uses in the Black-Scholes option valuation model is based on U.S. Treasury zero-coupon issues with remaining terms similar to the expected term.

**Expected dividends.** The Company has never declared or paid any cash dividends and does not plan to pay cash dividends in the foreseeable future, and, therefore, used an expected dividend yield of zero in the valuation model.

### Employee stock purchase plan ("ESPP")

The following tables summarize the components of ESPP expense for the three months ended March 31, 2013 and 2012, respectively (in thousands):

	Three months ended March 31,	
	2013	2012
Cost of goods sold	\$ 80	\$ 67
Research and development	120	176
Sales and marketing	38	40
General and administrative	40	37
	\$ 278	\$ 320

As of March 31, 2013 there was \$0.4 million of unrecognized stock-based compensation expense for stock purchase rights that will be recognized over the remaining offering period, through November 2013.

The value of the stock purchase right consists of: (1) the 15% discount on the purchase of the stock, (2) 85% of the call option and (3) 15% of the put option. The call option and put option were valued using the Black-Scholes option pricing model with the following assumptions:

	Three months ended March 31,	
	2013	2012
Stock purchase rights		
Weighted-average expected term (years)	0.74	0.72
Weighted-average volatility	48%	71%
Risk-free interest rate	0.13 - 0.16%	0.04 - 0.11%
Expected dividends	0%	0%

**Expected term.** The expected term represents the period of time from the beginning of the offering period to the purchase date.

Volatility. Due to the limited history of the trading of the Company's common stock since the initial public offering in February 2011, the expected volatility used by the Company is based on the actual volatility of similar entities. In evaluating similarity, factors such as industry, stage of life cycle, size, and financial leverage are taken into consideration. The term over which volatility was measured was commensurate with the expected term.

Risk-free interest rate. The risk-free rate that the Company uses in the Black-Scholes option valuation model is based on U.S. Treasury zero-coupon issues with remaining terms similar to the expected term.

Expected dividends. The Company has never declared or paid any cash dividends and does not plan to pay cash dividends in the foreseeable future, and, therefore, used an expected dividend yield of zero in the valuation model.

Restricted stock units

The following table summarizes the stock-based compensation expense recognized for restricted stock units for the three months ended March 31, 2013 (in thousands):

	Three months ended	
	March 31,	
	2013	2012
Cost of goods sold	\$ 108	