EXTREME NETWORKS INC
Form 10-Q
January 31, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

Form 10-Q

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

For the quarterly period ended December 31, 2012

OR

o 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 000-25711

EXTREME NETWORKS, INC.
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| DELAWARE<br>[State or other jurisdiction<br>of incorporation or organization] | 77-0430270<br>[I.R.S Employer<br>Identification No.] |
| 3585 Monroe Street,<br>Santa Clara, California<br>[Address of principal executive office] | 95051<br><br>[Zip Code] |

Registrant's telephone number, including area code: (408) 579-2800

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

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 (§ 229.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

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 | o | Accelerated filer | x |
| Non-accelerated filer | o (Do not check if a smaller reporting company) | Smaller reporting company | o |

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

The number of shares of the Registrant's Common Stock, $.001 par value, outstanding at January 25, 2013 was 93,730,671.

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EXTREME NETWORKS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share and per share amounts)
(Unaudited)

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| | December 31, 2012 | June 30, 2012 |
|---|---|---|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | $ 89,766 | $ 54,596 |
| Short-term investments | 35,204 | 23,358 |
| Accounts receivable, net of allowances of $1,689 at December 31, 2012 and $1,646 at June 30, 2012 | 42,583 | 41,166 |
| Inventories | 17,866 | 26,609 |
| Deferred income taxes | 281 | 644 |
| Prepaid expenses and other current assets | 5,407 | 5,655 |
| Assets held for sale | — | 17,081 |
| Total current assets | 191,107 | 169,109 |
| Property and equipment, net | 9,510 | 25,180 |
| Marketable securities | 71,208 | 75,561 |
| Intangible assets, net | 4,639 | 5,106 |
| Other assets | 8,939 | 9,634 |
| Total assets | $ 285,403 | $ 284,590 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | $ 11,341 | $ 19,437 |
| Accrued compensation and benefits | 11,168 | 13,409 |
| Restructuring liabilities | 5,032 | 463 |
| Accrued warranty | 2,971 | 2,871 |
| Deferred revenue, net | 29,441 | 31,769 |
| Deferred distributors revenue, net of cost of sales to distributors | 15,404 | 15,319 |
| Other accrued liabilities | 12,768 | 13,480 |
| Total current liabilities | 88,125 | 96,748 |
| Deferred revenue, less current portion | 8,133 | 7,559 |
| Other long-term liabilities | 837 | 643 |
| Commitments and contingencies (Note 7) | | |
| Stockholders' equity: | | |
| Convertible preferred stock, $.001 par value, issuable in series, 2,000,000 shares authorized; none issued | — | — |
| Common stock, $.001 par value, 750,000,000 shares authorized; 93,684,318 shares issued and outstanding at December 31, 2012 and 133,965,455 and 94,333,619 shares issued and outstanding, respectively, at June 30, 2012 | 94 | 134 |
| Treasury stock, zero and 39,631,836 shares at December 31, 2012 and June 30, 2012, respectively | — | (149,666) |
| Additional paid-in-capital | 820,023 | 970,609 |
| Accumulated other comprehensive income | 58 | (861) |
| Accumulated deficit | (631,867) | (640,576) |
| Total stockholders' equity | 188,308 | 179,640 |
| Total liabilities and stockholders' equity | $ 285,403 | $ 284,590 |

See accompanying notes to condensed consolidated financial statements.

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EXTREME NETWORKS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME (LOSS)
(In thousands, except per share amounts)
(Unaudited)

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | December 31, 2012 | January 1, 2012 | December 31, 2012 | January 1, 2012 |
| Net revenues: | | | | |
| Product | $60,259 | $68,094 | $121,378 | $131,307 |
| Service | 15,292 | 14,718 | 30,300 | 30,399 |
| Total net revenues | 75,551 | 82,812 | 151,678 | 161,706 |
| Cost of revenues: | | | | |
| Product | 29,377 | 30,821 | 59,853 | 60,299 |
| Service | 5,435 | 5,723 | 11,111 | 11,603 |
| Total cost of revenues | 34,812 | 36,544 | 70,964 | 71,902 |
| Gross profit: | | | | |
| Product | 30,882 | 37,273 | 61,525 | 71,008 |
| Service | 9,857 | 8,995 | 19,189 | 18,796 |
| Total gross profit | 40,739 | 46,268 | 80,714 | 89,804 |
| Operating expenses: | | | | |
| Research and development | 11,007 | 11,082 | 21,573 | 23,490 |
| Sales and marketing | 22,093 | 22,734 | 44,120 | 44,855 |
| General and administrative | 6,644 | 7,954 | 12,003 | 14,224 |
| Restructuring charge, net of reversals | 5,176 | 437 | 5,167 | 1,392 |
| Litigation settlement | (421) | — | (421) | — |
| Gain on sale of facilities | — | — | (11,539) | — |
| Total operating expenses | 44,499 | 42,207 | 70,903 | 83,961 |
| Operating (loss) income | (3,760) | 4,061 | 9,811 | 5,843 |
| Interest income | 261 | 342 | 531 | 635 |
| Interest expense | (1) | (38) | (1) | (75) |
| Other income (expense), net | (300) | (39) | (649) | 17 |
| (Loss) income before income taxes | (3,800) | 4,326 | 9,692 | 6,420 |
| Provision for income taxes | 406 | 219 | 983 | 731 |
| Net (loss) income | $(4,206) | $4,107 | $8,709 | $5,689 |
| Basic and diluted net income per share: | | | | |
| Net (loss) income per share – basic | $(0.04) | $0.04 | $0.09 | $0.06 |
| Net (loss) income per share – diluted | $(0.04) | $0.04 | $0.09 | $0.06 |
| Shares used in per share calculation – basic | 94,501 | 93,247 | 94,619 | 92,978 |
| Shares used in per share calculation – diluted | 94,501 | 94,118 | 95,514 | 94,056 |

See accompanying notes to condensed consolidated financial statements.

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EXTREME NETWORKS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(In thousands, except per share amounts)
(Unaudited)

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | December 31, 2012 | January 1, 2012 | December 31, 2012 | January 1, 2012 |
| Net (loss) income: | $(4,206) | $4,107 | $8,709 | $5,689 |
| Other comprehensive income (loss), net of tax: | | | | |
| Change in unrealized (loss) gain on investment | (164) | 63 | 138 | (380) |
| Change in net foreign currency translation adjustment | (61) | (828) | 780 | (1,689) |
| Other comprehensive (loss) income | (225) | (765) | 918 | (2,069) |
| Total comprehensive (loss) income | $(4,431) | $3,342 | $9,627 | $3,620 |

See accompanying notes to condensed consolidated financial statements.

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EXTREME NETWORKS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

| | Six Months Ended | |
|---|---|---|
| | December 31, 2012 | January 1, 2012 |
| Cash flows from operating activities: | | |
| Net income | $8,709 | $5,689 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Decrease in accrued investment income | 763 | 1,539 |
| Depreciation and amortization | 2,292 | 2,602 |
| Amortization of intangible assets | 801 | 1,030 |
| Provision for doubtful accounts | 49 | (72) |
| Deferred income taxes | 73 | (30) |
| Stock-based compensation | 3,784 | 3,176 |
| Gain on disposition of long lived assets, net | (11,451) | — |
| Unrealized gain on foreign exchange transactions | (74) | (649) |
| Changes in operating assets and liabilities, net | | |
| Accounts receivable | (1,466) | (5,263) |
| Inventories | 8,743 | 192 |
| Prepaid expenses and other assets | 1,255 | 6,172 |
| Accounts payable | (8,096) | 828 |
| Accrued compensation and benefits | (2,241) | (701) |
| Restructuring liabilities | 4,569 | (2,449) |
| Other current and long term liabilities | 367 | (8,110) |
| Net cash provided by operating activities | 8,077 | 3,954 |
| Cash flows from investing activities: | | |
| Capital expenditures | (3,026) | (2,011) |
| Purchases of investments | (25,886) | (34,015) |
| Proceeds from maturities of investments and marketable securities | 9,322 | 13,889 |
| Proceeds from sales of investments and marketable securities | 8,447 | 18,192 |
| Purchases of intangible assets | (335) | — |
| Proceeds from sales of facilities | 42,659 | — |
| Net cash provided by (used in) investing activities | 31,181 | (3,945) |
| Cash flows from financing activities: | | |
| Proceeds from issuance of common stock | 1,614 | 698 |
| Repurchases of common stock | (6,171) | — |
| Net cash (used in) provided by financing activities | (4,557) | 698 |
| Foreign currency effect on cash | 469 | (1,260) |
| Net increase (decrease) in cash and cash equivalents | 35,170 | (553) |
| Cash and cash equivalents at beginning of period | 54,596 | 49,972 |
| Cash and cash equivalents at end of period | $89,766 | $49,419 |

See accompanying notes to the condensed consolidated financial statements.

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EXTREME NETWORKS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

## 1. Basis of Presentation

The unaudited condensed consolidated financial statements of Extreme Networks, Inc. (referred to as the "Company" or "Extreme Networks") included herein have been prepared under the rules and regulations of the Securities and Exchange Commission ("SEC"). Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted under such rules and regulations. The condensed consolidated balance sheet at December 31, 2012 was derived from audited financial statements as of that date but does not include all disclosures required by generally accepted accounting principles for complete financial statements. These interim financial statements and notes should be read in conjunction with the Company's audited consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2012.

The unaudited condensed consolidated financial statements reflect all adjustments, consisting only of normal recurring adjustments that, in the opinion of management, are necessary for a fair presentation of the results of operations and cash flows for the interim periods presented and the financial condition of Extreme Networks at December 31, 2012. The results of operations for the three and six months ended December 31, 2012 are not necessarily indicative of the results that may be expected for fiscal 2013 or any future periods.

## 2. Summary of Significant Accounting Policies

### Revenue Recognition

The Company's revenue is primarily derived from sales of networking products, which are tangible products containing software and non-software components that function together to deliver the tangible product's essential functionality. In addition to tangible products, the Company's sales arrangements may include other deliverables such as standalone software licenses, or service offerings. For multiple deliverable arrangements, the Company recognizes revenue in accordance with the accounting standard for multiple deliverable revenue arrangements, which provides guidance on whether multiple deliverables exist, how deliverables in an arrangement should be separated, and how consideration should be allocated. Software revenue recognition guidance is applied to the sales of the Company's standalone software products, including software upgrades and software that is not essential to the functionality of the hardware with which it is sold.

Pursuant to the guidance of the accounting standard for multiple deliverable revenue arrangements, when the Company's sales arrangements contain multiple elements, such as products, software licenses, maintenance agreements, or professional services, the Company determines the standalone selling price for each element based on a selling price hierarchy. The application of the multiple deliverable revenue accounting standard does not change the units of accounting for the Company's multiple element arrangements. Under the selling price hierarchy, the selling price for each deliverable is based on the Company's vendor-specific objective evidence ("VSOE"), which is determined by a substantial majority of the Company's historical standalone sales transactions for a product or service falling within a narrow range. If VSOE is not available due to a lack of standalone sales transactions or lack of pricing within a narrow range, then third party evidence ("TPE"), as determined by the standalone pricing of competitive vendor products in similar markets, is used, if available. TPE typically is difficult to establish due to the proprietary differences of competitive products and difficulty in obtaining reliable competitive standalone pricing information. When neither VSOE nor TPE is available, the Company determines its best estimate of standalone selling price ("ESP") for a product or service and does so by considering several factors including, but not limited to, the 12-month historical median sales price, sales channel, geography, gross margin objective, competitive product pricing, and product life cycle. In consideration of all relevant pricing factors, the Company applies management judgment to determine the Company's best estimate of selling price through consultation with and formal approval by the Company's management for all products and services for which neither VSOE nor TPE is available. Generally the standalone selling price of services is determined using VSOE and the standalone selling price of other deliverables is determined by using ESP. The Company regularly reviews VSOE, TPE and ESP for all of its products and services and maintains internal controls over the establishment and updates of these estimates.

In accordance with the software revenue recognition accounting standard, the Company continues to recognize revenue for software using the residual method for its sale of standalone software products, including optional software upgrades and other software that is not essential to the functionality of the hardware with which it is sold. After allocation of the relative selling price to each element of the arrangement, the Company recognizes revenue in accordance with the Company's policies for product, software, and service revenue recognition.

3. Balance Sheet Accounts

Cash, Cash Equivalents, Short-Term Investments and Marketable Securities

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EXTREME NETWORKS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Summary of Cash and Available-for-Sale Securities (in thousands)

| | December 31, 2012 | June 30, 2012 |
|---|---|---|
| Cash | $30,656 | $18,455 |
| | | |
| Cash equivalents | $59,110 | $36,141 |
| Short-term investments | 35,204 | 23,358 |
| Marketable securities | 71,208 | 75,561 |
| Total available-for-sale | $165,522 | $135,060 |
| | | |
| Total cash and available for sale securities | $196,178 | $153,515 |

Available-for-Sale Securities
The following is a summary of available-for-sale securities (in thousands):

| | Amortized Cost | Fair Value | Unrealized Holding Gains | Unrealized Holding Losses |
|---|---|---|---|---|
| December 31, 2012 | | | | |
| Money market funds | $59,110 | $59,110 | $— | $— |
| U.S. corporate debt securities | 98,706 | 98,899 | 268 | (75) |
| U.S. government agency securities | 7,508 | 7,513 | 5 | — |
| | $165,324 | $165,522 | $273 | $(75) |
| Classified as: | | | | |
| Cash equivalents | $59,110 | $59,110 | $— | $— |
| Short-term investments | 35,125 | 35,204 | 79 | — |
| Marketable securities | 71,089 | 71,208 | 194 | (75) |
| | $165,324 | $165,522 | $273 | $(75) |
| June 30, 2012 | | | | |
| Money market funds | $36,141 | $36,141 | $— | $— |
| U.S. corporate debt securities | 84,882 | 84,949 | 148 | (81) |
| U.S. government agency securities | 11,241 | 11,234 | 3 | (10) |
| U.S. municipal bonds | 2,738 | 2,736 | — | (2) |
| | $135,002 | $135,060 | $151 | $(93) |
| Classified as: | | | | |
| Cash equivalents | $36,141 | $36,141 | $— | $— |
| Short-term investments | 23,311 | 23,358 | 48 | (1) |
| Marketable securities | 75,550 | 75,561 | 103 | (92) |
| | $135,002 | $135,060 | $151 | $(93) |

The amortized cost and estimated fair value of available-for-sale investments in debt securities at December 31, 2012, by contractual maturity, were as follows (in thousands):

| | Amortized Cost | Fair Value |
|---|---|---|

| | | |
|---|---|---|
| Due in 1 year or less | $35,125 | $35,204 |
| Due in 1-2 years | 31,367 | 31,447 |
| Due in 2-5 years | 39,722 | 39,761 |
| Total investments in available for sale debt securities | $106,214 | $106,412 |

The Company considers highly liquid investments with maturities of three months or less at the date of purchase to be cash equivalents. Investments with maturities of greater than three months, but less than one year at the balance sheet date are classified as Short Term Investments. Investments with maturities of greater than one year at balance sheet date are classified as Marketable Securities. Except for direct obligations of the United States government, securities issued by agencies of the United States government, and money market funds, the Company diversifies its investments by limiting its holdings with any individual issuer.

Investments include available-for-sale investment-grade debt securities that the Company carries at fair value. The Company accumulates unrealized gains and losses on the Company's available-for-sale debt securities, net of tax, in accumulated other comprehensive income (loss) in the stockholders' equity section of its balance sheets. Such an unrealized gain or loss does not reduce net income for the applicable accounting period. If the fair value of an available-for-sale debt instrument is less than its amortized cost basis, an other-than-temporary impairment is triggered in circumstances where (1) the Company intends to sell the instrument, (2) it is more likely than not that the Company will be required to sell the instrument before recovery of its amortized cost basis, or (3) the Company does not expect to recover the entire amortized cost basis of the instrument (that is, a credit loss exists). If the Company intends to sell or it is more likely than not that the Company will be required to sell the available-for-sale debt instrument before recovery of its amortized cost basis, the Company recognizes an other-than-temporary impairment in earnings equal to the entire difference between the debt instruments' amortized cost basis and its fair value. For available-for-sale debt instruments that are considered other-than-temporarily impaired due to the existence of a credit loss, if the Company does not intend to sell and it is not more likely than not that the Company will be required to sell the instrument before recovery of its remaining amortized cost basis (amortized cost basis less any current-period credit loss), the Company separates the amount of the impairment into the amount that is credit related and the amount due to all other factors. The credit loss component is recognized in earnings and is the difference between the debt instrument's amortized cost basis and the present value of its expected future cash flows. The remaining difference between the debt instrument's fair value and the present value of future expected cash flows is due to factors that are not credit related and is recognized in other comprehensive income.

The following table presents the Company’s investments’ gross unrealized losses and fair values, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position.

| | Less than 12 months | | 12 months or more | | Total | |
|---|---|---|---|---|---|---|
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| December 31, 2012 | | | | | | |
| U.S. corporate debt securities | $26,202 | $(75) | $— | $— | $26,202 | $(75) |
| | $26,202 | $(75) | $— | $— | $26,202 | $(75) |

The Company determines the basis of the cost of a security sold or the amount reclassified out of accumulated other comprehensive income into earnings using the specific identification method. During the three and six months ended December 31, 2012, realized gains or losses recognized on the sale of investments were not significant. As of December 31, 2012, thirteen out of sixty-four investment securities had unrealized losses. The unrealized gains / (losses) on the Company’s investments were caused by interest rate fluctuations. Substantially all of the Company’s available-for-sale investments are investment grade government and corporate debt securities that have maturities of less than three years. The Company does not intend to sell the investments and it is not more likely than not that the Company will be required to sell the investments before recovery of its amortized costs.

Inventories

Inventory is stated at the lower of cost or market. Cost is computed using standard cost, which approximates actual cost, on a first-in, first-out basis. The Company reduces the carrying value of inventory to net realizable value based on excess and obsolete inventories which are primarily determined by age of inventory and future demand forecasts. At the point of the loss recognition, a new, lower-cost basis for that inventory is established, and subsequent changes in facts and circumstances do not result in the restoration or increase in that newly established cost basis. Any written down or obsolete inventory subsequently sold has not had a material impact on gross profit for any of the periods disclosed.

Long-Lived Assets

Long-lived assets include property and equipment, intangible assets, and service inventory. Property and equipment and intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets or asset groups may not be recoverable. If such facts and circumstances exist, the Company assesses the recoverability of these assets by comparing the projected undiscounted net cash flows associated with the related asset or group of assets over their remaining lives against their respective carrying amounts. Impairments, if any, are based on the excess of the carrying amount

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EXTREME NETWORKS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

over the fair value of those assets. The Company reduces the carrying value of service inventory to net realizable value based on excess and obsolete inventories which are primarily determined by age of inventory and future demand forecasts.

On September 11, 2012, the Company completed the sale of its corporate campus and accompanying 16 acres of land in Santa Clara, California for net cash proceeds of approximately $44.7 million and realized a gain of $11.5 million.

Intangible Assets

The following tables summarize the components of gross and net intangible asset balances (in thousands):

| | Weighted Average Remaining Amortization Period | Gross Carrying Amount | Accumulated Amortization | Net Carrying Amount |
|---|---|---|---|---|
| December 31, 2012 | | | | |
| Patents | 7.2 years | $1,800 | $775 | $1,025 |
| License Agreements | 10 years | 10,158 | 6,845 | 3,313 |
| Other Intangibles | 2.7 years | 659 | 358 | 301 |
| | | $12,617 | $7,978 | $4,639 |

| | Weighted Average Remaining Amortization Period | Gross Carrying Amount | Accumulated Amortization | Net Carrying Amount |
|---|---|---|---|---|
| June 30, 2012 | | | | |
| Patents | 7.4 years | $1,800 | $669 | $1,131 |
| License Agreements | 9.3 years | 10,158 | 6,231 | 3,927 |
| Other Intangibles | 0.3 years | 324 | 276 | 48 |
| | | $12,282 | $7,176 | $5,106 |

Amortization expense was $0.4 million and $0.5 million for the three months ended December 31, 2012 and January 1, 2012, respectively. Amortization expense was $0.8 million and $1.0 million for the six months ended December 31, 2012 and January 1, 2012, respectively. Amortization expense expected to be recorded for each of the next five years is as follows (in thousands):

| | |
|---|---|
| For the fiscal year ending: | |
| Remaining for fiscal 2013 | $680 |
| 2014 | 916 |
| 2015 | 549 |
| 2016 | 375 |
| 2017 | 302 |
| Thereafter | 1,817 |
| Total | $4,639 |

Deferred Revenue, Net

Deferred revenue, net represents amounts for (i) deferred services revenue (support arrangements, professional services and training), and (ii) deferred product revenue net of the related cost of revenue when the revenue recognition criteria have not been met. The following table summarizes deferred revenue, net at December 31, 2012 and June 30, 2012, respectively (in thousands):

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| | December 31, 2012 | June 30, 2012 |
|---|---|---|
| Deferred services | $36,118 | $37,708 |
| Deferred product: | | |
| Deferred revenue | 2,231 | 2,236 |
| Deferred cost of sales | (775) | (616) |
| Deferred product revenue, net | 1,456 | 1,620 |
| Balance at end of period | 37,574 | 39,328 |
| Less: current portion | 29,441 | 31,769 |
| Non-current deferred revenue, net | $8,133 | $7,559 |

The Company offers for sale to its customers renewable support arrangements, including extended warranty contracts, that range from one to five years. Deferred support revenue is included within deferred revenue, net within the Services category above. The change in the Company's deferred support revenue balance in relation to these arrangements was as follows (in thousands):

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | December 31, 2012 | January 1, 2012 | December 31, 2012 | January 1, 2012 |
| Balance beginning of period | $35,661 | $35,730 | $37,461 | $35,802 |
| New support arrangements | 14,776 | 15,960 | 27,313 | 30,560 |
| Recognition of support revenue | (14,640) | (14,274) | (28,977) | (28,946) |
| Balance end of period | 35,797 | 37,416 | 35,797 | 37,416 |
| Less: current portion | 27,664 | 29,853 | 27,664 | 29,853 |
| Non-current deferred revenue | $8,133 | $7,563 | $8,133 | $7,563 |

Deferred Distributors Revenue, Net of Cost of Sales to Distributors

The Company records revenue from its distributors on a sell-through basis, recording deferred revenue and deferred cost of sales associated with all sales transactions to its distributors in "Deferred distributors revenue, net of cost of sales to distributors" in the liability section of its condensed consolidated balance sheet. When the Company ships products to its distributors, legal title to the products passes to its distributors, and a legally enforceable obligation is created for the distributors to pay on a current basis. Therefore, the Company records a trade receivable at the contractual discount to the list selling price and relieves inventory for the cost of goods shipped to the distributor. The amount shown as "Total deferred distributors revenue, net of cost of sales to distributors" represents the deferred gross margin on sales to distributors based on contractual pricing. Distributors purchase products from the Company at a contractual discount based on geographic region and resell the Company's products at a very broad range of individually negotiated price points depending on competitive factors and other market conditions. A portion of the deferred revenue balance represents an amount of the distributors' original purchase price that will be remitted back to the distributors after resale transactions are reported to the Company. Therefore, the amount of gross margin the Company will recognize in future periods from distributor sales will be less than the deferred amount recorded for the original sale to the distributor as a result of the price concessions negotiated at the time of sell-through. The wide range and variability of negotiated price credits granted to distributors do not allow the Company to accurately estimate the portion of the balance in the deferred revenue that will be credited to the distributors in the future. Therefore, the Company does not reduce deferred revenue by anticipated future price credits; instead, price credits are recorded against revenue and accounts receivable when incurred, which is generally at the time the distributor sells the product.

The following table summarizes deferred distributors revenue, net of cost of sales to distributors at December 31, 2012 and June 30, 2012, respectively (in thousands):

| | December 31, 2012 | June 30, 2012 |
|---|---|---|
| Deferred distributors revenue | $20,200 | $20,361 |
| Deferred cost of sales to distributors | (4,796) | (5,042) |
| Total deferred distributors revenue, net of cost of sales to distributors | $15,404 | $15,319 |

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EXTREME NETWORKS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Guarantees and Product Warranties
Upon issuance of a standard product warranty, the Company discloses and recognizes a liability for the obligation it assumes under the warranty. The following table summarizes the activity related to the Company's product warranty liability during the three and six months ended December 31, 2012 and January 1, 2012:

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | December 31, 2012 | January 1, 2012 | December 31, 2012 | January 1, 2012 |
| Balance beginning of period | $2,971 | $2,702 | $2,871 | $2,640 |
| New warranties issued | 1,942 | 1,589 | 3,504 | 3,237 |
| Warranty expenditures | (1,942) | (1,640) | (3,404) | (3,226) |
| Balance end of period | $2,971 | $2,651 | $2,971 | $2,651 |

The Company's standard hardware warranty period is typically 12 months from the date of shipment to end-users and 90 days for software. For certain access products, the Company offers a limited lifetime hardware warranty commencing on the date of shipment from the Company and ending five (5) years following the Company's announcement of the end of sale of such product. Upon shipment of products to its customers, the Company estimates expenses for the cost to repair or replace products that may be returned under warranty and accrue a liability in cost of product revenue for this amount. The determination of the Company's warranty requirements is based on actual historical experience with the product or product family, estimates of repair and replacement costs and any product warranty problems that are identified after shipment. The Company estimates and adjusts these accruals at each balance sheet date in accordance with changes in these factors.

In the normal course of business to facilitate sales of its products, the Company indemnifies its resellers and end-user customers with respect to certain matters. The Company has agreed to hold the customer harmless against losses arising from a breach of intellectual property infringement or other claims made against certain parties. These agreements may limit the time within which an indemnification claim can be made and the amount of the claim. It is not possible to estimate the maximum potential amount under these indemnification agreements due to the limited history of prior indemnification claims and the unique facts and circumstances involved in each particular agreement. Historically, payments made by the Company under these agreements have not had a material impact on its operating results or financial position.

Concentrations
The Company may be subject to concentration of credit risk as a result of certain financial instruments consisting principally of marketable investments and accounts receivable. The Company has placed its investments with high-credit quality issuers. The Company does not invest an amount exceeding 10% of its combined cash, cash equivalents, short-term investments and marketable securities in the securities of any one obligor or maker, except for obligations of the United States government, obligations of United States government agencies and money market accounts.

The Company performs ongoing credit evaluations of its customers and generally does not require collateral in exchange for credit.

The following table sets forth major customers accounting for 10% or more of our net revenue (amounts for the three and six months ended January 1, 2012 have been revised to correct previously disclosed amounts):

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | December 31, 2012 | January 1, 2012 | December 31, 2012 | January 1, 2012 |

| | | | | |
|---|---|---|---|---|
| Westcon Group Inc. | 14 % | 22 % | 15 % | 19 % |
| Scansource, Inc. | 12 % | * | 12 % | 13 % |
| Tech Data Corporation | 12 % | * | 11 % | * |
| Ericsson AB | 10 % | 12 % | 10 % | 11 % |

* Less than 10% of revenue

The following table sets forth major customers accounting for 10% or more of our accounts receivable balance:

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| | December 31, 2012 | June 30, 2012 |
|---|---|---|
| Ericsson AB | 16 % | 21 % |
| Scansource Inc. | 11 % | * |
| Westcon Group Inc. | * | 16 % |

* Less than 10% of accounts receivable

## 4. Fair Value Measurements

The Company measures certain financial assets and liabilities at fair value on a recurring basis, including cash equivalents, available-for-sale securities, trading securities and foreign currency derivatives. Fair value is measured based on a fair value hierarchy following three levels of inputs, of which the first two are considered observable and the last unobservable:

- Level 1 — Quoted prices in active markets for identical assets or liabilities;
- Level 2 — Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; and
- Level 3 — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The following table presents the Company's fair value hierarchy for its financial assets and liabilities measured at fair value on a recurring basis:

| December 31, 2012 | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| | (In thousands) | | | |
| Assets | | | | |
| Investments: | | | | |
| Federal agency notes | $— | $7,513 | $— | $7,513 |
| Money market funds | 59,110 | — | — | 59,110 |
| Corporate notes/bonds | — | 98,899 | — | 98,899 |
| Foreign currency forward contracts | $— | $10 | $— | $10 |
| Total | $59,110 | $106,422 | $— | $165,532 |

| June 30, 2012 | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| | (In thousands) | | | |
| Assets | | | | |
| Investments: | | | | |
| Municipal bonds | $— | $2,736 | $— | $2,736 |
| Federal agency notes | — | 11,234 | — | 11,234 |
| Money market funds | 36,141 | — | — | 36,141 |

| | | | | |
|---|---|---|---|---|
| Corporate notes/bonds | — | 84,949 | — | 84,949 |
| Foreign currency forward contracts | — | 179 | — | 179 |
| Total | $36,141 | $99,098 | $— | $135,239 |

Level 2 investment valuations are based on inputs such as quoted market prices of similar instruments, dealer quotations or valuations provided by alternative pricing sources supported by observable inputs. These generally include U.S. government and sovereign obligations, most government agency securities, investment-grade corporate bonds, and state, municipal and provincial

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obligations. There were no transfers of assets or liabilities between Level 1 and Level 2 during the three months ended December 31, 2012 and January 1, 2012.

## 5. Share-based Compensation

Share-based compensation expense recognized in the condensed consolidated financial statements by line item caption is as follows (in thousands):

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | December 31, 2012 | January 1, 2012 | December 31, 2012 | January 1, 2012 |
| Cost of product revenue | $121 | $135 | $295 | $291 |
| Cost of service revenue | 85 | 30 | 244 | 144 |
| Research and development | 288 | 280 | 720 | 752 |
| Sales and marketing | 567 | 323 | 1,295 | 819 |
| General and administrative | 555 | 513 | 1,230 | 1,170 |
| Total share-based compensation expense | $1,616 | $1,281 | $3,784 | $3,176 |

During the three and six months ended December 31, 2012 and January 1, 2012, the Company did not capitalize any stock-based compensation expense in inventory, as the amounts were immaterial. The income tax benefit for share-based compensation expense was immaterial in the three and six months ended December 31, 2012 and January 1, 2012.

The weighted-average grant-date per share fair value of options granted during the three months ended December 31, 2012 and January 1, 2012 were $1.73 and $1.54, respectively. The weighted-average estimated per share fair value of shares purchased under the Company’s 1999 Employee Stock Purchase Plan (“ESPP”) during the three months ended December 31, 2012 and January 1, 2012 were $0.91 and $1.03, respectively.

The weighted-average grant-date per share fair value of options granted during the six months ended December 31, 2012 and January 1, 2012 were $1.81 and $1.66, respectively. The weighted-average estimated per share fair value of shares purchased under the ESPP during the six months ended December 31, 2012 and January 1, 2012 were $0.89 and $0.99, respectively.

The following table summarizes stock option activity under all plans for the six months ended December 31, 2012:

| | Number of Shares (000’s) | Weighted-Average Exercise Price Per Share | Weighted-Average Remaining Contractual Term (years) | Aggregate Intrinsic Value (000’s) |
|---|---|---|---|---|
| Options outstanding at June 30, 2012 | 9,006 | $3.68 | | |
| Granted | 1,830 | $3.49 | | |
| Exercised | (454) | $2.86 | | $314 |
| Canceled | (633) | $3.69 | | |
| Options outstanding at December 31, 2012 | 9,749 | $3.68 | 4.79 | $3,104 |
| Exercisable at December 31, 2012 | 5,742 | $3.89 | 4.03 | $2,036 |
| Vested and expected to vest at December 31, 2012 | 9,257 | $3.70 | 4.73 | $2,984 |

### Stock Awards

Stock awards may be granted under the 2005 Plan on terms approved by the Board of Directors. Stock awards generally provide for the issuance of restricted stock which vests over a fixed period.

The following table summarizes stock award activity for the six months ended December 31, 2012:

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| | Number of Shares (000's) | Weighted-Average Grant-Date Fair Value | Aggregate Fair Market Value ($000's) |
|---|---|---|---|
| Non-vested stock outstanding at June 30, 2012 | 1,078 | $2.35 | |
| Granted | 2,589 | $3.47 | |
| Vested | (647) | $3.37 | $2,181 |
| Cancelled | (83) | $3.32 | |
| Non-vested stock outstanding at December 31, 2012 | 2,937 | $3.09 | |

The fair value of each option award and share purchase option under the Company's ESPP is estimated on the date of grant using the Black-Scholes-Merton option valuation model with the weighted average assumptions noted in the following table. The expected term of options granted is derived from historical data on employee exercise and post-vesting employment termination behavior. The expected term of ESPP represents the contractual life of the ESPP purchase period. The risk-free rate based upon the estimated life of the option and ESPP is based on the U.S. Treasury yield curve in effect at the time of grant. Expected volatility is based on both the implied volatilities from traded options on the Company's stock and historical volatility on the Company's stock.

| | Stock Option Plan | | Employee Stock Purchase Plan | | Stock Option Plan | | Employee Stock Purchase Plan | |
|---|---|---|---|---|---|---|---|---|
| | Three Months Ended | | Three Months Ended | | Six Months Ended | | Six Months Ended | |
| | December 31, 2012 | January 1, 2012 | December 31, 2012 | January 1, 2012 | December 31, 2012 | January 1, 2012 | December 31, 2012 | January 1, 2012 |
| Expected life | 4 years | 5 years | 0.25 years | 0.25 years | 5 years | 5 years | 0.25 years | 0.25 years |
| Risk-free interest rate | 0.57 % | 1.00 % | 0.04 % | 0.04 % | 0.71 % | 1.09 % | 0.05 % | 0.04 % |
| Volatility | 63 % | 61 % | 50 % | 79 % | 64 % | 59 % | 59 % | 70 % |
| Dividend yield | — % | — % | — % | — % | — % | — % | — % | — % |

The Company is required to estimate the expected forfeiture rate and only recognize expense on a straight-line method for those shares expected to vest.

## 6. Common Stock Repurchases and Retirement

### Retirement of Treasury Stock

On September 5, 2012, the Company retired 39,631,836 shares of treasury stock. The retired shares had a carrying value of approximately $149.7 million, and the Company reduced additional paid-in capital by approximately $149.7 million upon the formal retirement of the shares. The retired shares are now included in the Company's authorized but unissued shares.

### Common Stock Repurchases

On September 28, 2012, the Company's Board of Directors approved a share repurchase program for a maximum of $75 million which may be purchased over a three year period in the open market or in privately negotiated transactions. All repurchased shares will be retired and included in the Company's authorized but unissued shares. During the three months ended December 31, 2012, the Company repurchased 1.9 million shares of common stock at a total cost of $6.7 million.

## 7. Commitments and Contingencies

### Purchase Commitments

The Company currently has arrangements with contract manufacturers and suppliers for the manufacture of its products. The arrangements allow them to procure long lead-time component inventory based upon a rolling production forecast provided by the Company. The Company is obligated to the purchase of long lead-time component inventory that its contract manufacturer procures in accordance with the forecast, unless the Company gives notice of order cancellation outside of applicable component lead-times. As of December 31, 2012, the Company had non-cancelable commitments to purchase approximately $21.8 million of such inventory.

Legal Proceedings

The Company may from time to time be party to litigation arising in the course of its business, including, without limitation, allegations relating to commercial transactions, business relationships or intellectual property rights. Such claims, even if not meritorious, could result in the expenditure of significant financial and managerial resources. Litigation in general, and intellectual property and securities litigation in particular, can be expensive and disruptive to normal business operations. Moreover, the results of legal proceedings are difficult to predict.

In accordance with applicable accounting guidance, the Company records accruals for certain of its outstanding legal proceedings, investigations or claims when it is probable that a liability will be incurred and the amount of loss can be reasonably estimated. The Company evaluates, at least on a quarterly basis, developments in legal proceedings, investigations or claims that could affect the amount of any accrual, as well as any developments that would result in a loss contingency to become both probable and reasonably estimable. When a loss contingency is not both probable and reasonably estimable, the Company does not record a loss accrual. However, if the loss (or an additional loss in excess of any prior accrual) is at least a reasonable possibility and material, then the Company would disclose an estimate of the possible loss or range of loss, if such estimate can be made, or disclose that an estimate cannot be made. The assessment whether a loss is probable or a reasonable possibility, and whether the loss or a range of loss is estimable, involves a series of complex judgments about future events. Even if a loss is reasonably possible, the Company may not be able to estimate a range of possible loss, particularly where (i) the damages sought are substantial or indeterminate, (ii) the proceedings are in the early stages, or (iii) the matters involve novel or unsettled legal theories or a large number of parties. In such cases, there is considerable uncertainty regarding the ultimate resolution of such matters, including the amount of any possible loss, fine or penalty. Accordingly, for current proceedings, the Company is currently unable to estimate any reasonably possible loss or range of possible loss. However, an adverse resolution of one or more of such matters could have a material adverse effect on the Company's results of operations in a particular quarter or fiscal year.

Intellectual Property Litigation

Enterasys Networks

On June 21, 2005, Enterasys Networks ("Enterasys") filed suit against Extreme and Foundry Networks, Inc. (“Foundry”) in the United States District Court for the District of Massachusetts, Civil Action No. 05-11298 DPW. The complaint alleges willful infringement of U.S. Patent Nos. 5,251,205; 5,390,173; 6,128,665; 6,147,995; 6,539,022; and 6,560,236, and seeks: a) a judgment that the Company willfully infringes each of the patents; (b) a permanent injunction from infringement, inducement of infringement and contributory infringement of each of the six patents; (c) damages and a “reasonable royalty” to be determined at trial; (d) treble damages; (e) attorneys' fees, costs and interest; and (f) equitable relief at the Court's discretion. Petitions for reexamination were filed challenging five of the patents at issue to the U.S. Patent and Trademark Office, and a stay of the case was entered. Following the reexamination proceedings, Enterasys withdrew its allegations of infringement as to two of the patents, U.S. Patent Nos. 6,539,022 and 6,560,236. The stay was lifted on May 21, 2010, and the Court held claim construction hearings in December 2010. Fact discovery is ongoing. No trial date has been set. The Company intends to defend the lawsuit vigorously, but, due to the inherent uncertainties of litigation, it cannot predict the ultimate outcome of the matter at this time.

On April 20, 2007, the Company filed suit against Enterasys in the United States District Court for the Western District of Wisconsin, Civil Action No. 07-C-0229-C. The complaint alleged willful infringement of U.S. Patents Nos. 6,104,700, 6,678,248, and 6,859,438, and sought injunctive relief against Enterasys' continuing sale of infringing goods and monetary damages. Enterasys responded to the complaint on May 30, 2007, and also filed counterclaims alleging infringement of three U.S. patents owned by Enterasys. On April 9, 2008, the Court dismissed Enterasys' counterclaims on one of its patents with prejudice. On May 5, 2008, the Court granted the Company's motion for summary judgment, finding that it does not infringe Enterasys' two remaining patents and dismissing all of Enterasys' remaining counterclaims with prejudice. On May 30, 2008, a jury found that Enterasys infringed all three of the

Company's patents and awarded the Company damages in the amount of $0.2 million. The Court also ruled in the Company's favor on Enterasys' challenge to the validity of the Company's patents. On October 29, 2008, the Court denied Enterasys' post-trial motion for judgment as a matter of law, and granted Extreme Network's motion for a permanent injunction against Enterasys. The injunction order permanently enjoins Enterasys from manufacturing, using, offering to sell, selling in the U.S. and importing into the U.S. the Enterasys products accused of infringing Extreme Network's three patents. On March 16, 2009, the Court also denied Enterasys' motion for a new trial, but granted Enterasys' motion for a stay of the injunction pending appeal. On April 17, 2009, Enterasys filed its notice of appeal and on May 1, 2009, the Company filed its cross appeal. On September 30, 2010, the U.S. Court of Appeals for the Federal Circuit upheld the jury verdict of infringement by Enterasys of the Company's patents and the Districts Court's summary judgment of non-infringement by the Company of Enterasys' '727 patent. The Federal Circuit reversed the judgment of non-infringement by the Company of Enterasys '181 patent, holding that the District Court Judge applied an incorrect claim construction and reversed the District Court's denial of the Company's request for attorneys' fees as premature.

On November 4, 2011, a jury returned a verdict of non-infringement by the Company of the '181 patent and found the patent to be valid. Both parties filed post-trial motions, including motions for a new trial, for judgment as a matter of law and for attorneys' fees, all of which the Court denied on July 11, 2012. Enterasys did not file a notice of appeal by the August 10, 2012 deadline.

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Consequently, the judgment of non-infringement in favor of the Company in the second trial is final. During the fourth quarter of fiscal 2012, Enterasys paid the Company $0.6 million related to the judgment. During the quarter ended December 31, 2012, the Company received payments from Enterasys totaling approximately $0.4 million for the Court's award for damages, supplemental damages, pre and post judgment interests, costs from the first trial and second trial, plus the amount Enterasys agreed to release for damages held in escrow that accrued during the stay of the injunction post-trial and on appeal.

Chrimar Systems

On October 31, 2011, Chrimar Systems, Inc. dba CMS Technologies, and Chrimar Holding Company filed suit against the Company, Cisco Systems, Inc., and Cisco Consumer Products LLC. Cisco-Linksys LLC, Hewlett-Packard Company, 3Com Corporation and Avaya, Inc. in the United States District Court for the District of Delaware, Civil Action No. 11-1050 (the "Delaware action"). The complaint alleges infringement of U.S. Patent No. 7,457,250. The Delaware action has been stayed pursuant to 28 USC Section 1659(a) pending final determination of the International Trade Commission action described below, based on the fact that the allegations in both cases relate to the same patent.

On November 1, 2011, Chrimar filed a complaint with the International Trade Commission, pursuant to Section 337 of the Tariff Act of 1930, as amended, alleging that the Company imports into the United States, sells for importation and/or sells within the United States after importation of products and/or systems infringing U.S. Patent No. 7,457,250 patent, the same patent asserted in the Delaware action. On December 2, 2011, the International Trade Commission instituted an investigation of these allegations (the "ITC action"). The complaint in the ITC action seeks a permanent order excluding from entry into the United States all infringing articles that are manufactured, imported or sold by the Company that infringe U.S. Patent No. 7,457,250. On July 20, 2012, Chrimar filed a motion to withdraw its complaint in the ITC action and the motion was granted on August 1, 2012 by the presiding administrative law judge. On August 27, 2012, the Commission determined not to review the administrative law judge's decision, rendering that decision final.

During the fourth quarter of the fiscal 2012, the Company engaged in settlement discussions with Chrimar Systems Inc. As part of the negotiations the Company determined that it is reasonably possible that a range of loss could be between $0.3 million and $1.4 million which is dependent on a number of factors including whether mutually acceptable settlement terms can be reached. As of December 31, 2012 and through the date of the filing of this Form 10-Q, this matter was still pending. However, during the quarter ended June 30, 2012 the Company recorded a charge of $0.3 million based on its best estimate of the probable loss.

Reefedge Networks

On September 17, 2012, Reefedge Networks, LLC filed suit against the Company in the United States District Court for the District of Delaware, Civil Action No. 12-1148. The complaint alleges wrongful use, making, selling, and/or offering to sell products that infringe U.S. Patent Nos. 6,633.761; 6,975,864; and 7,197,308 and seeks unspecified monetary damages and a permanent injunction for products originating from a single supplier to which the Company has submitted an indemnification request. Given the preliminary nature of the claims, it is premature to assess the likelihood of a particular outcome. An answer was filed on December 10, 2012. The Company plans to vigorously defend itself.

Indemnification Obligations

Subject to certain limitations, the Company may be obligated to indemnify its current and former directors, officers and employees. These obligations arise under the terms of its certificate of incorporation, its bylaws, applicable contracts, and Delaware and California law. The obligation to indemnify, where applicable, generally means that the Company is required to pay or reimburse, and in certain circumstances the Company has paid or reimbursed, the individuals' reasonable legal expenses and possibly damages and other liabilities incurred in connection with these matters. It is not possible to estimate the maximum potential amount under these indemnification agreements due to the limited history of these claims. The cost to defend the Company and the named individuals could have a material adverse effect on its consolidated financial position, results of operations and cash flows in the future. Recovery of such costs under its directors and officers insurance coverage is uncertain. As of December 31, 2012, the Company had no outstanding indemnification claims

8. Income Taxes

The Company recorded an income tax provision of $0.4 million and $0.2 million for the three months ended December 31, 2012 and January 1, 2012, respectively. The Company recorded an income tax provision of $1.0 million and $0.7 million for the six months ended December 31, 2012 and January 1, 2012 respectively.

The income tax provisions for the three and six months ended December 31, 2012 and January 1, 2012 consisted primarily of taxes on foreign income and U.S. state income taxes. The income tax provisions for both fiscal years were calculated based on the results of operations for the three and six months ended December 31, 2012 and January 1, 2012, and may not reflect the annual effective rate.

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The Company recognizes deferred tax assets and liabilities based on the differences between the financial statement carrying amounts and the tax bases of assets and liabilities. Significant management judgment is required in determining the Company's deferred tax assets and liabilities and any valuation allowance recorded against the Company's net deferred tax assets. The Company makes an assessment of the likelihood that the Company's net deferred tax assets will be recovered from future taxable income, and to the extent that recovery is not believed to be likely, a valuation allowance is established.

The Company has a full valuation allowance against its U.S. net deferred tax assets. The valuation allowance was calculated by assessing both negative and positive evidence when measuring the need for a valuation allowance. Negative evidence, such as the Company's current quarter financial performance, the Company's significant restructuring in the current quarter, and the unfavorable macroeconomic climate were given more weight than our expectations of future profitability, which are inherently uncertain. Our current U.S. loss along with these negative factor represented sufficient negative evidence to require a full valuation allowance against our U.S. federal and state net deferred tax assets. This valuation allowance will be evaluated periodically and can be reversed partially or totally if business results have sufficiently improved to support realization of the Company's U.S. deferred tax assets.

The sale of the Company's buildings and land in Santa Clara, California during the quarter ended September 30, 2012 resulted in a tax loss that increased the amount of the Company's deferred tax assets with a corresponding increase to the related valuation allowance.

The Company had $25.8 million of unrecognized tax benefits as of December 31, 2012. The future impact of the unrecognized tax benefit of $25.8 million, if recognized, is as follows: approximately $0.5 million would impact the effective tax rate, and approximately $25.3 million would result in adjustments to deferred tax assets and corresponding adjustments to the valuation allowance. It is reasonably possible that the amount of unrealized tax benefit could decrease by approximately $0.2 million during the next twelve months due to the expiration of the statute of limitations in certain foreign jurisdictions.

Estimated interest and penalties related to the underpayment of income taxes are classified as a component of tax expense in the Consolidated Statements of Income and were immaterial for both the three months and six months periods ended December 31, 2012. Accrued interest and penalties were $0.1 million and $0.2 million as of December 31, 2012 and January 1, 2012, respectively.

In general, the Company's U.S. federal income tax returns are subject to examination by tax authorities for fiscal years 1998 forward due to net operating losses and the Company's state income tax returns are subject to examination for fiscal years 2001 forward due to net operating losses.

9. Net (Loss) Income Per Share

Basic earnings (loss) per share is calculated by dividing net income (loss) by the weighted average number of common shares outstanding during the period, less shares subject to repurchase, and excludes any dilutive effects of options, warrants and unvested restricted stock. Dilutive earnings per share is calculated by dividing net income by the weighted average number of common shares used in the basic earnings per share calculation plus the dilutive effect of shares subject to repurchase, options, warrants and unvested restricted stock. The following table presents the calculation of basic and diluted net income(loss) per share (in thousands, except per share data):

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | December 31, 2012 | January 1, 2012 | December 31, 2012 | January 1, 2012 |
| Net (loss) income | $(4,206) | $4,107 | $8,709 | $5,689 |
| Weighted-average shares used in per share calculation – basic | 94,501 | 93,247 | 94,619 | 92,978 |

| | | | | |
|---|---|---|---|---|
| Incremental shares using the treasury stock method: | | | | |
| Stock options | — | 282 | 418 | 299 |
| Restricted stock units | — | 471 | 370 | 645 |
| Employee Stock Purchase Plan | — | 118 | 107 | 134 |
| Weighted -average share used in per share calculation – diluted | 94,501 | 94,118 | 95,514 | 94,056 |
| Net income (loss) per share – basic | (0.04 ) | 0.04 | 0.09 | 0.06 |
| Net income (loss) per share – diluted | (0.04 ) | 0.04 | 0.09 | 0.06 |

Potentially dilutive common shares from employee incentive plans are determined by applying the treasury stock method to the assumed exercise of outstanding stock options, the assumed vesting of outstanding restricted stock units, and the assumed issuance of common stock under the stock purchase plan. Weighted stock options outstanding with an exercise price higher than the Company's average stock price for the periods presented are excluded from the calculation of diluted net income per share since the effect of including them would have been anti-dilutive due to the net income position of the Company during the periods presented. For the three and six months ended December 31, 2012, the Company excluded 7.3 million and 7.0 million outstanding weighted average stock options, respectively, from the calculation of diluted earnings per common share because they would have been anti-dilutive. The Company excluded 8.8 million and 8.7 million outstanding weighted average stock options from the calculation of diluted earnings per common share in the three and six months ended January 1, 2012 because they would have been anti-dilutive.

10. Restructuring Charges

As part of the Company's on-going restructuring efforts, during the three months ended December 31, 2012, the Company initiated a plan to reduce its worldwide headcount by 13%, consolidate specific global administrative functions, and shift certain operating costs to lower cost regions, among other actions. Restructuring expense was $5.2 million in both the three and six months ended December 31, 2012 and $0.4 million and $1.4 million in the three and six months ended January 1, 2012, respectively.

The following table summarizes restructuring activities for the six months ended December 31, 2012:

| | Termination Benefits (1) | Excess Facilities (2) | Other Cost | Total |
|---|---|---|---|---|
| Balance at July 1, 2012 | $359 | $93 | $11 | $463 |
| Period charges | 5,065 | 16 | 110 | 5,191 |
| Period reversals | (24) | — | — | (24) |
| Period payments | (477) | (109) | (12) | (598) |
| Restructuring liabilities at December 31, 2012 | $4,923 | $— | $109 | $5,032 |

(1) Termination benefits generally include severance, outplacement services and health insurance coverage.
(2) Excess facilities costs generally include rent expense less expected sublease income, lease termination costs and asset abandonment costs.

11. Foreign Exchange Forward Contracts

The Company uses derivative financial instruments to manage exposures to foreign currency. The Company’s objective for holding derivatives is to use the most effective methods to minimize the impact of these exposures. The Company does not enter into derivatives for speculative or trading purposes. The Company records all derivatives on the balance sheet as Other Assets, Net at fair value. Changes in the fair value of derivatives are recognized in earnings as Other Income (Expense). The Company enters into foreign exchange forward contracts to mitigate the effect of gains and losses generated by the foreign currency forecasted transactions related to certain operating expenses and re-measurement of certain assets and liabilities denominated in Japanese Yen, the Euro, the Swedish Krona, the Indian Rupee and the British Pound. These derivatives do not qualify as hedges. At December 31, 2012, these forward foreign currency contracts had a notional principal amount of $9.5 million and an immaterial unrealized gain on foreign exchange contracts. These contracts have maturities of less than 60 days. Changes in the fair value of these foreign exchange forward contracts are offset largely by re-measurement of the underlying assets and liabilities. Foreign currency transaction gains and losses from operations were a $0.4 million gain for the three months ended December 31, 2012 and a $0.1 million loss for the three months ended January 1, 2012. Foreign currency transaction gains and losses were a $0.1 million gain for the six months ended December 31, 2012 and an immaterial loss for the six months ended January 1, 2012.

12. Disclosure about Segments of an Enterprise and Geographic Areas

Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision makers with respect to the allocation of resources and performance.

The Company operates in one segment, the development and marketing of network infrastructure equipment. The Company conducts business globally and is managed geographically. Revenue is attributed to a geographical area based on the location of the customers. The Company operates in three geographical areas: Americas, which includes the United States, Canada, Mexico, Central America and South America; EMEA, which includes Europe, Middle East and Africa; and APAC which includes Asia Pacific, South Asia, Japan, and Australia.

The Company attributes revenues to geographic regions primarily based on the customer's ship-to location.

Information regarding geographic areas is as follows (in thousands):

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| Net Revenues: | Three Months Ended December 31, 2012 | Three Months Ended January 1, 2012 | Six Months Ended December 31, 2012 | Six Months Ended January 1, 2012 |
|---|---|---|---|---|
| Americas: | | | | |
| United States | $22,731 | $26,588 | $47,935 | $52,389 |
| Other | 10,767 | 11,307 | 20,545 | 19,511 |
| Total Americas | 33,498 | 37,895 | 68,480 | 71,900 |
| EMEA | 28,700 | 31,335 | 57,220 | 60,815 |
| APAC | 13,353 | 13,582 | 25,978 | 28,991 |
| Total net revenues | $75,551 | $82,812 | $151,678 | $161,706 |

Substantially all of the Company’s assets were attributable to North America operations at December 31, 2012 and January 1, 2012.

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

This quarterly report on Form 10-Q, including the following sections, contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, including in particularly, our expectations regarding market demands, customer requirements and the general economic environment, and future results of operations, and other statements that include words such as “may” “expect” or “believe” . These forward-looking statements involve risks and uncertainties. We caution investors that actual results may differ materially from those projected in the forward-looking statements as a result of certain risk factors identified in the section entitled “Risk Factors” in this Report, our Quarterly Report on Form 10-Q for the second quarter of fiscal 2013, our Annual Report on Form 10-K for the fiscal year ended June 30, 2012, and other filings we have made with the Securities and Exchange Commission. These risk factors, include, but are not limited to: fluctuations in demand for our products and services; a highly competitive business environment for network switching equipment; our effectiveness in controlling expenses; the possibility that we might experience delays in the development or introduction of new technology and products; customer response to our new technology and products; the timing of any recovery in the global economy; risks related to pending or future litigation; and a dependency on third parties for certain components and for the manufacturing of our products.

Business Overview

We are a leading provider of network infrastructure equipment and services for enterprises, data centers, and service providers. We were incorporated in California in May 1996 and reincorporated in Delaware in March 1999. Our corporate headquarters are located in Santa Clara, California. We develop and sell network infrastructure equipment to our enterprise, data center and telecommunications service provider customers.

We conduct our sales and marketing activities on a worldwide basis through a distribution channel utilizing distributors, resellers and our field sales organization. We primarily sell our products through an ecosystem of channel partners who combine our Ethernet products with their offerings to create compelling information technology solutions for end user customers. We utilize our field sales organization to support our channel partners and to sell direct to end-user customers, including some large global accounts. Our customers include businesses, hospitals, schools, hotels, telecommunications companies and government agencies around the world.

We outsource the majority of our manufacturing and supply chain management operations as part of our strategy to maintain global manufacturing capabilities and to reduce our costs. We conduct quality assurance, manufacturing engineering, document control and test development in Santa Clara, California and Research Triangle Park, North

Carolina. This approach enables us to reduce fixed costs and to flexibly respond to changes in market demand
The market for network infrastructure equipment is highly competitive and dominated by a few large companies. The current economic climate has further driven consolidation of vendors within the Ethernet networking market and with vendors from adjacent markets, including storage, security, wireless and voice applications. We believe that the underpinning technology for all of these adjacent markets is Ethernet. As a result, independent Ethernet switch vendors are being acquired or merged with larger, adjacent market vendors to enable them to deliver complete and broad solutions. As a result, we believe that, as an independent Ethernet switch vendor, we must provide products that, when combined with the products of our large strategic partners, create compelling solutions for end user customers. Our approach is to focus on the intelligence and automation layer that spans our hardware products and that facilitates end-to-end solutions, as opposed to positioning Extreme Networks as a low-cost-vendor with point products.

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We believe that continued success in our marketplace is dependent upon a variety of factors that includes, but is not limited to, our ability to design, develop and distribute new and enhanced products employing leading-edge technology.

Results of Operations

During the second quarter of fiscal 2013, we achieved the following results:

- Net revenues of $75.6 million compared to net revenues of $82.8 million in the second quarter of fiscal 2012.
- Product revenues of $60.3 million compared to product revenues of $68.1 million in the second quarter of fiscal 2012.
- Service revenues of $15.3 million compared to service revenues of $14.7 million in the second quarter of fiscal 2012.
- Total gross margin of 54% of net revenues compared to total gross margin of 56% of net revenues in the second quarter of fiscal 2012.
- Operating loss of $3.8 million (including restructuring charges of $5.2 million) compared to operating income of $4.1 million (including restructuring charges of $0.4 million) in the second quarter of fiscal 2012.
- Net loss of $4.2 million compared to net income of $4.1 million in the second quarter of fiscal 2012.
- Cash flow provided by operating activities of $8.1 million compared to cash flow provided by operating activities of $4.0 million in the first six months of fiscal 2012.
- Cash and cash equivalents, short-term investments and marketable securities increased by $42.7 million to $196.2 million from $153.5 million as of June 30, 2012, primarily due to cash provided by operating and investing activities, including the sale of buildings and land.

We operate in three regions: Americas, which includes the United States, Canada, Mexico, Central America and South America; EMEA, which includes Europe, Middle East, and Africa; and APAC which includes Asia Pacific, South Asia, Japan, and Australia. The following table presents the total net revenue geographically for the three and six months ended December 31, 2012 and January 1, 2012, respectively (dollars in thousands):

| Net Revenue | Three Months Ended December 31, 2012 | Three Months Ended January 1, 2012 | $ Change | % Change | Six Months Ended December 31, 2012 | Six Months Ended January 1, 2012 | $ Change | % Change |
|---|---|---|---|---|---|---|---|---|
| Americas: | | | | | | | | |
| United States | $22,731 | $26,588 | $(3,857) | (14.5)% | $47,935 | $52,389 | $(4,454) | (8.5)% |
| Other | 10,767 | 11,307 | (540) | (4.8)% | 20,545 | 19,511 | 1,034 | 5.3% |
| Total Americas | 33,498 | 37,895 | (4,397) | (11.6)% | 68,480 | 71,900 | (3,420) | (4.8)% |
| Percentage of net revenue | 44.3% | 45.8% | | | 45.1% | 44.5% | | |
| EMEA | 28,700 | 31,335 | (2,635) | (8.4)% | 57,220 | 60,815 | (3,595) | (5.9)% |
| Percentage of net revenue | 38.0% | 37.8% | | | 37.7% | 37.6% | | |
| APAC | 13,353 | 13,582 | (229) | (1.7)% | 25,978 | 28,991 | (3,013) | (10.4)% |
| Percentage of net revenue | 17.7% | 16.4% | | | 17.1% | 17.9% | | |
| Total net revenues | $75,551 | $82,812 | $(7,261) | (8.8)% | $151,678 | $161,706 | $(10,028) | (6.2)% |

Net Revenues

The following table presents net product and service revenue for the three and six months ended December 31, 2012 and January 1, 2012, respectively (dollars in thousands):

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| | Three Months Ended | | | | Six Months Ended | | | |
|---|---|---|---|---|---|---|---|---|
| | December 31, 2012 | January 1, 2012 | $ Change | % Change | December 31, 2012 | January 1, 2012 | $ Change | % Change |
| Net Revenue: | | | | | | | | |
| Product | $60,259 | $68,094 | $(7,835) | (11.5)% | $121,378 | $131,307 | $(9,929) | (7.6)% |
| Percentage of net revenue | 79.8% | 82.2% | | | 80.0% | 81.2% | | |
| Service | 15,292 | 14,718 | 574 | 3.9% | 30,300 | 30,399 | (99) | (0.3)% |
| Percentage of net revenue | 20.2% | 17.8% | | | 20.0% | 18.8% | | |
| Total net revenue | $75,551 | $82,812 | $(7,261) | (8.8)% | $151,678 | $161,706 | $(10,028) | (6.2)% |

Product revenue decreased by $7.8 million or 11.5% in the second quarter of fiscal 2013, and decreased by $9.9 million or 7.6% in the first six months of fiscal 2013, compared to the corresponding periods of fiscal 2012 primarily due to lower sales volume in the Americas and EMEA regions. In the first two quarters of fiscal 2013, we experienced weaker than expected demand from our public sector and enterprise customers in the U.S. and we continued to experience weak demand from our strategic customers and distributors in the EMEA region attributable to the persistent macroeconomic challenges in Europe.

Service revenue increased by $0.6 million, or 3.9% in the second quarter of fiscal 2013, and was flat in the first six months of fiscal 2013, compared to the corresponding periods of fiscal 2012, reflecting our continued stable levels of service contract renewals.

Cost of Revenue and Gross Profit

The following table presents the gross profit on product and service revenue and the gross profit percentage of product and service revenue for the three and six months ended December 31, 2012 and January 1, 2012 (in thousands):

| | Three Months Ended | | | | Six Months Ended | | | |
|---|---|---|---|---|---|---|---|---|
| | December 31, 2012 | January 1, 2012 | $ Change | % Change | December 31, 2012 | January 1, 2012 | $ Change | % Change |
| Gross profit: | | | | | | | | |
| Product | $30,882 | $37,273 | $(6,391) | (17.1)% | $61,525 | $71,008 | $(9,483) | (13.4)% |
| Percentage of product revenue | 51.3% | 54.7% | | | 50.7% | 54.1% | | |
| Service | 9,857 | 8,995 | 862 | 9.6% | 19,189 | 18,796 | 393 | 2.1% |
| Percentage of service revenue | 64.5% | 61.1% | | | 63.3% | 61.8% | | |
| Total gross profit | $40,739 | $46,268 | $(5,529) | (11.9)% | $80,714 | $89,804 | $(9,090) | (10.1)% |
| Percentage of net revenue | 53.9% | 55.9% | | | 53.2% | 55.5% | | |

Cost of product revenue includes costs of materials, amounts paid to third-party contract manufacturers, costs related to warranty obligations, charges for excess and obsolete inventory, royalties under technology license agreements, and internal costs associated with manufacturing overhead, including management, manufacturing engineering, quality assurance, development of test plans, and document control. We outsource substantially all of our manufacturing and supply chain management operations, and we conduct quality assurance, manufacturing engineering, document control and distribution in Santa Clara, California, China, and Taiwan. Accordingly, a significant portion of our cost of product revenue consists of payments to our primary contract manufacturer, Alpha Networks, located in Hsinchu, Taiwan. In addition, we OEM our wireless product line from Motorola.

Product gross margin decreased to 51.3% from 54.7% in the second quarter of fiscal 2013, and decreased to 50.7% from 54.1% in the first six months of fiscal 2013, compared to the corresponding periods of fiscal 2012. The decreases in product gross margin were primarily due to higher discounting and an increase in charges for excess and obsolete inventory.

Our cost of service revenue consists primarily of labor, overhead, repair and freight costs and the cost of spares used in providing support under customer service contracts. Service gross margin increased to 64.5% from 61.1% in the second quarter of fiscal 2013 and increased to 63.3% from 61.8% in the first six months of fiscal 2013. The increases in service gross margin were primarily due to lower material costs.

Operating Expenses

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The following table presents operating expenses and operating income (in thousands, except percentages):

| | Three Months Ended | | | | Six Months Ended | | | |
|---|---|---|---|---|---|---|---|---|
| | December 31, 2012 | January 1, 2012 | $ Change | % Change | December 31, 2012 | January 1, 2012 | $ Change | % Change |
| Research and development | $11,007 | $11,082 | $(75) | (0.7)% | $21,573 | $23,490 | $(1,917) | (8.2)% |
| Sales and marketing | 22,093 | 22,734 | (641) | (2.8)% | 44,120 | 44,855 | (735) | (1.6)% |
| General and administrative | 6,644 | 7,954 | (1,310) | (16.5)% | 12,003 | 14,224 | (2,221) | (15.6)% |
| Restructuring charge, net of reversals | 5,176 | 437 | 4,739 | 1,084.4 % | 5,167 | 1,392 | 3,775 | 271.2 % |
| Litigation settlement | (421) | — | (421) | (100.0)% | (421) | — | (421) | (100.0)% |
| Gain on sale of campus | — | — | — | — % | (11,539) | — | (11,539) | (100.0)% |
| Total operating expenses | $44,499 | $42,207 | $2,292 | 5.4 % | $70,903 | $83,961 | $(13,058) | (15.6)% |
| Operating income | $(3,760) | 4,061 | $(7,821) | (192.6)% | $9,811 | $5,843 | $3,968 | 67.9 % |

The following table highlights our operating expenses and operating income as a percentage of net revenues:

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | December 31, 2012 | January 1, 2012 | December 31, 2012 | January 1, 2012 |
| Research and development | 14.6 % | 13.4 % | 14.2 % | 14.5 % |
| Sales and marketing | 29.2 % | 27.5 % | 29.1 % | 27.7 % |
| General and administrative | 8.8 % | 9.6 % | 7.9 % | 8.8 % |
| Restructuring charge, net of reversals | 6.9 % | 0.5 % | 3.4 % | 0.9 % |
| Litigation settlement | (0.6)% | — % | (0.3)% | — % |
| Gain on sale of campus | — % | — % | (7.6)% | — % |
| Total operating expenses | 58.9 % | 51.0 % | 46.7 % | 51.9 % |
| Operating income | (5.0)% | 4.9 % | 6.5 % | 3.6 % |

Research and Development Expenses

Research and development expenses consist primarily of salaries and related personnel expenses, consultant fees and prototype expenses related to the design, development, and testing of our products.

Research and development expenses decreased by $0.1 million, or 1% in the second quarter of fiscal 2013 and decreased by $1.9 million, or 8.2% in the first six months of fiscal 2013, compared to the corresponding periods of fiscal 2012. The decreases in research and development expenses primarily resulted from lower spending on engineering project expenses due to differences in the timing and pattern of planned engineering project spending in the first two quarters of fiscal 2013 when compared to the same period last year.

Sales and Marketing Expenses

Sales and marketing expenses consist of salaries, commissions and related expenses for personnel engaged in marketing and sales functions, as well as trade shows and promotional expenses.

Sales and marketing expenses decreased by $0.6 million, or 2.8% in the second quarter of fiscal 2013 and decreased by $0.7 million, or 1.6% in the first six months of fiscal 2013, compared to the corresponding periods of fiscal 2012. The decreases in sales and marketing expenses were primarily due to decreases of $1.3 million and $1.5 million in commissions in the three and six months ended December 31, 2012, respectively, partially offset by small increases in various marketing related expenses.

General and Administrative Expenses

General and administrative expenses decreased by $1.3 million, or 16.5% in the second quarter of fiscal 2013 and decreased by $2.2 million, or 15.6% in the six months of fiscal 2013, compared to the corresponding periods of fiscal 2012. The decreases in general and administrative expenses were primarily due to decreases of $1.6 million and $2.7 million in legal expenses in the three and six months ended December 31, 2012, respectively, mainly attributable to the resolution of certain legal matters.

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Restructuring Charge, Net of Reversals

Restructuring charges increased by $4.7 million in the second quarter of fiscal 2013 and increased by $3.8 million in the first six months of fiscal 2013, compared to the corresponding periods of fiscal 2012. During the second quarter of fiscal 2013, we further reduced costs through targeted restructuring activities intended to reduce operating costs and realign our organization in the current competitive environment. As part of our restructuring efforts in the second quarter, we initiated a plan to reduce our worldwide headcount by 13%, consolidate specific global administrative functions, and shift certain operating costs to lower cost regions, among other actions. As of December 31, 2012, we had restructuring liabilities of $5.0 million, which we anticipate paying by the end of fiscal 2013. We anticipate incurring restructuring charges of approximately $1.0 million to $2.0 million in the second half of fiscal 2013.

Litigation Settlement

During the second quarter of fiscal 2013, we recognized a litigation award of $0.4 million related to a favorable verdict on a trial.

Gain on Campus Sale

During the first quarter of fiscal 2013, we completed the sale of our corporate campus and accompanying 16 acres of land in Santa Clara, California for net cash proceeds of approximately $44.7 million. We realized a gain of $11.5 million in connection with this transaction.

Other Income (Expense), net

Other expense, net increased by approximately $0.3 million in the second quarter of fiscal 2013 and increased by $0.7 million in the first six months of fiscal 2013, compared to the corresponding periods of fiscal 2012. The changes in other income (expense), net in the first half of fiscal 2013, as compared to the same period in fiscal 2012, was insignificant. The increases in other expense, net were primarily due to gains from the revaluation of certain assets and liabilities denominated in foreign currencies into U.S. dollars.

Provision for Income Taxes

We recorded an income tax provision of $0.4 million and $0.2 million for the three months ended December 31, 2012 and January 1, 2012, respectively. We recorded an income tax provision of $1.0 million and $0.7 million for the six months ended December 31, 2012 and January 1, 2012, respectively. The income tax provision for the second quarter of fiscal 2013 consisted primarily of taxes on foreign income and U.S state income taxes. The income tax provision for the second quarter of fiscal 2012 consisted primarily of taxes on foreign income and U.S. state income taxes. The income tax provisions for both quarters were calculated based on the results of operations for the three and six months ended December 31, 2012 and January 1, 2012, and may not reflect the annual effective rate.

We have provided a full valuation allowance for our U.S. net deferred tax assets after assessing both negative and positive evidence when measuring the need for a valuation allowance. For the current quarter, negative evidence, such as the Company's current quarter financial performance, the Company's significant restructuring in the current quarter, and the unfavorable macroeconomic climate were given more weight than our expectations of future profitability, which are inherently uncertain. Accordingly, we believe that there is sufficient negative evidence to maintain a full valuation allowance against our U.S. federal and state net deferred tax assets. This valuation allowance will be evaluated periodically and can be reversed partially or totally if business results have sufficiently improved to support realization of our U.S. deferred tax assets.

The sale of our buildings and land in Santa Clara, California during the quarter ended September 30, 2012 resulted in a tax loss that increased the amount of our deferred tax assets with a corresponding increase to the related valuation allowance.

Critical Accounting Policies and Estimates

Our unaudited condensed consolidated financial statements and the related notes included elsewhere in this report are prepared in accordance with accounting principles generally accepted in the United States. The preparation of these unaudited condensed consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, costs and expenses, and related disclosures. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. In many instances, we could have reasonably used different accounting estimates, and in other instances changes in the accounting estimates are reasonably likely to occur from period to period. Accordingly, actual results could differ significantly from the estimates made by our management. On an ongoing basis, we evaluate our estimates and assumptions. To the extent that there are material differences

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between these estimates and actual results, our future financial statement presentation, financial condition, results of operations and cash flows will be affected.

As discussed in Part II, Item 7, “Management's Discussion and Analysis of Financial Condition and Results of Operations” of our Annual Report on Form 10-K for the year ended June 30, 2012, we consider the following accounting policies to be the most critical in understanding the judgments that are involved in preparing our consolidated financial statements:

- Revenue Recognition
- Inventory Valuation
- Long Lived Assets
- Allowance for Doubtful Accounts
- Deferred Tax Valuation Allowance
- Accounting for Uncertainty in Income Taxes
- Share-Based Compensation
- Legal Contingencies
- Restructuring Costs

There have been no changes to our critical accounting policies since the filing of our last Annual Report on Form 10-K.

Liquidity and Capital Resources

The following summarizes information regarding our cash, investments, and working capital (in thousands):

| | December 31, 2012 | June 30, 2012 |
|---|---|---|
| Cash and cash equivalent | $89,766 | $54,596 |
| Short-term investments | 35,204 | 23,358 |
| Marketable securities | 71,208 | 75,561 |
| Total cash and investments | $196,178 | $153,515 |
| Working capital | $102,982 | $72,361 |

As of December 31, 2012, our principal sources of liquidity consisted of cash, cash equivalents and investments of $196.2 million and net accounts receivable of $42.6 million. Historically, our principal uses of cash have consisted of the purchase of finished goods inventory from our contract manufacturers, payroll and other operating expenses related to the development, marketing of our products and purchases of property and equipment and repurchases of our common stock. We believe that our $196.2 million of cash and cash equivalents and investments at December 31, 2012 will be sufficient to fund our operating requirements, stock repurchase program, and restructuring expenses for at least the next 12 months.

Key Components of Cash Flows and Liquidity

A summary of the sources and uses of cash and cash equivalents is as follows (in thousands):

| | Six Months Ended | |
|---|---|---|
| | December 31, 2012 | January 1, 2012 |
| Net cash provided by operating activities | $8,077 | $3,954 |
| Net cash provided by (used in) investing activities | $31,181 | $(3,945) |
| Net cash (used in) provided by financing activities | $(4,557) | $698 |
| Foreign currency effect on cash | $469 | $(1,260) |
| Net increase (decrease) in cash and cash equivalents | $35,170 | $(553) |

Net Cash Provided by Operating Activities

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Cash flows from operations increased by $4.1 million in the first six months of fiscal 2013 compared to the corresponding period of fiscal 2012, primarily due to purposeful reduction of inventory spending to bring inventory levels in line with the anticipated near-term demand for our products.

Net Cash Provided by Investing Activities

Cash flow provided by investing activities in the first six months of fiscal 2013 was $31.2 million, comprised of proceeds of $42.7 million from the sale of buildings and land in Santa Clara California, proceeds of $17.8 million from the sale and maturities of investments, offset by $25.9 million used to purchase investment securities and $3.0 million used to purchase property and equipment.

Net Cash Used in Financing Activities

Cash flow used in financing activities in the first six months of fiscal 2013 was $4.6 million, comprised of $6.2 used to repurchase shares of our common stock, offset by $1.6 million of proceeds from the exercise of stock options and purchases of shares of our common stock under the ESPP, net of taxes paid on vested and released stock awards.

Contractual Obligations

The following summarizes our contractual obligations at December 31, 2012, and the effect such obligations are expected to have on our liquidity and cash flow in future periods (in thousands):

| | Total | Less than 1 Year | 1-3 years | 3-5 years | More than 5 years |
|---|---|---|---|---|---|
| Contractual Obligations: | | | | | |
| Non-Cancellable Inventory purchase commitments | $21,823 | $21,823 | $— | $— | $— |
| Non-cancellable operating lease obligations | 36,332 | 4,224 | 9,239 | 7,593 | 15,276 |
| Total contractual cash obligations | $58,155 | $26,047 | $9,239 | $7,593 | $15,276 |

Non-cancelable inventory purchase commitments represent the purchase of long lead-time component inventory that our contract manufacturers procure in accordance with our forecast. Inventory purchase commitments were $21.8 million as of December 31, 2012, a decrease of $17.0 million from $38.8 million as of June 30, 2012. We expect to honor the inventory purchase commitments within the next 12 months.

The amounts in the table above exclude $0.5 million of income tax liabilities related to uncertain tax positions as we are unable to reasonably estimate the timing of settlement.

We did not have any material commitments for capital expenditures as of December 31, 2012.

Off-Balance Sheet Arrangements

We did not have any off-balance sheet arrangements as of December 31, 2012.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Interest Rate Sensitivity

The primary objective of our investment activities is to preserve principal while at the same time maximize the income we receive from our investments without significantly increasing risk. Some of the securities that we have invested in may be subject to market risk. This means that a change in prevailing interest rates may cause the principal amount of the investment to fluctuate. For example, if we hold a security that was issued with a fixed interest rate at the then-prevailing rate and the prevailing interest rate later rises, the principal amount of our investment will probably decline. To minimize this risk, we maintain our portfolio of cash equivalents and short-term investments in a variety of securities, including commercial paper, other non-government debt securities and money market funds.

The valuation of our investment portfolio is subject to uncertainties that are difficult to predict. Factors that may impact its valuation include changes to credit ratings of the securities, discount rates and ongoing strength and quality of market credit and liquidity.

If the current market conditions deteriorate further, or the anticipated recovery in market values does not occur, we may be required to record impairment charges in future quarters.

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The following table presents the amounts of our cash equivalents, short-term investments and marketable securities that are subject to market risk by range of expected maturity and weighted-average interest rates as of December 31, 2012. This table does not include money market funds because those funds are generally not subject to market risk.

| | Maturing in Three months or less (In thousands) | Three months to one year | Greater than one year | Total | Fair Value |
|---|---|---|---|---|---|
| December 31, 2012 | | | | | |
| Included in cash and cash equivalent | $4.601 | $— | $— | $4.601 | $4.601 |
| Weighted average interest rate | 1.35 % | — | — | | |
| Included in short-term investments | $— | $30,602 | $— | $30,602 | $30,602 |
| Weighted average interest rate | — % | 0.77 % | — | | |
| Included in marketable securities | $— | $— | $71,208 | $71,208 | $71,208 |
| Weighted average interest rate | — | — | 0.72 % | | |

The following tables present hypothetical changes in fair value of the financial instruments held at December 31, 2012 that are sensitive to changes in interest rates:

| Unrealized gain given a decrease in interest rate of X bps | | Fair value as of | Unrealized loss given an increase in interest rate of X bps | |
|---|---|---|---|---|
| (100 bps) | (50 bps) | December 31, 2012 | 100 bps | 50 bps |
| (In thousands) | | | | |
| $1,536 | $763 | $106,412 | $(1,494) | $(752) |

Exchange Rate Sensitivity

Currently, substantially all of our sales and the majority of our expenses are denominated in United States dollars. While we conduct some sales transactions and incur certain operating expenses in foreign currencies and expect to continue to do so, we do not anticipate that foreign exchange gains or losses will be significant, in part because of our foreign exchange risk management process discussed below.

Foreign Exchange Forward Contracts

We record all derivatives on the balance sheet at fair value. Changes in the fair value of derivatives are recognized in earnings as Other Income (Expense). We enter into foreign exchange forward contracts to mitigate the effect of gains and losses generated by the foreign currency forecasted transactions related to certain operating expenses and re-measurement of certain assets and liabilities denominated in Japanese Yen, the Euro, the Swedish Krona, the Indian Rupee and the British Pound. These derivatives do not qualify as hedges. At December 31, 2012, these forward foreign currency contracts had a notional principal amount of $9.5 million and an immaterial unrealized gain on foreign exchange contracts. These contracts have maturities of less than 60 days. Changes in the fair value of these foreign exchange forward contracts are offset largely by re-measurement of the underlying assets and liabilities. Foreign currency transaction gains and losses from operations were a $0.4 million loss for the three months ended December 31, 2012 and a $0.1 million loss for the three months ended January 1, 2012. Foreign currency transaction gains and losses from operations were $0.1 million for the six months ended December 31, 2012, and an immaterial loss for the six months ended January 1, 2012.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Disclosure controls and procedures are controls and procedures designed to reasonably assure that information required to be disclosed in our reports filed under the Securities Exchange Act of 1934 as amended, such as this Report, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and to reasonably assure that such information is accumulated and communicated to our management, including the Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO"), as appropriate to allow timely decisions regarding required disclosure. Under the supervision and with the participation of our management, including our CEO and CFO, we evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this Report. Based on this evaluation, our CEO and CFO concluded that our disclosure controls and procedures were effective as of the end of the period covered by this Report.

Management's Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over our financial reporting. There are inherent limitations in the effectiveness of any system of internal control, including the possibility of human error and the circumvention or overriding of controls. Accordingly, even effective internal controls can provide only reasonable assurances with respect to financial statement preparation. Further because of changes in conditions, the effectiveness of internal control may vary over time.

We assessed the effectiveness of our internal control over financial reporting as of the end of the period covered by this Report. In making this assessment, we used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control-Integrated Framework.

Based on our assessment using those criteria, we concluded that, as of the end of the period covered by this Report, our internal control over financial reporting is effective.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting during the quarter ended December 31, 2012 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Inherent Limitations on Effectiveness of Controls

Our management, including the CEO and CFO, does not expect that our disclosure controls or our internal control over financial reporting will prevent or detect all error and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. Our controls and procedures are designed to provide reasonable assurance that our control system's objective will be met and our CEO and CFO have concluded that our disclosure controls and procedures are effective at the reasonable assurance level. The design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Further, because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, within Extreme Networks have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple error or mistake. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part on certain assumptions about the likelihood of future events. Projections of any evaluation of the effectiveness of controls in future periods are subject to risks. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures. Notwithstanding these limitations, our disclosure controls and procedures are designed to provide reasonable assurance of achieving their objectives. Our CEO and CFO have concluded that our disclosure controls and procedures are, in fact, effective at the "reasonable assurance" level.

## PART II. Other Information

### Item 1. Legal Proceedings

For information regarding litigation matters that we deem significant, refer to Part I, Item 3, Legal Proceedings of our Annual Report on Form 10-K for the fiscal year ended June 30, 2012 and Note 7 to our Notes to Condensed Consolidated Financial Statements, included in Part I, Item 1 of this Report which are incorporated herein by reference.

### Item 1A. Risk Factors

The following is a list of risks and uncertainties which may have a material and adverse effect on our business, financial condition or results of operations. The risks and uncertainties set out below are not the only risks and uncertainties we face, and some are endemic to the networking industry.

We cannot assure you that we will be profitable in the future because a number of factors could negatively affect our financial results.

We have a limited history of profitability and have reported losses in some of our prior fiscal years. In addition, in years when we reported profits, we were not profitable in each quarter during those years. We anticipate continuing to incur significant sales and marketing, product development and general and administrative expenses. Any delay in generating or recognizing revenue could result in a loss for a quarter or full year. Even if we are profitable, our operating results may fall below our expectations and those of our investors, which could cause the price of our stock to fall.

We may experience challenges or delays in generating or recognizing revenue for a number of reasons and our revenue and operating results have varied significantly in the past and may vary significantly in the future due to a number of factors, including, but not limited to, the following:

- we are dependent upon obtaining orders during a quarter and shipping those orders in the same quarter to achieve our revenue objectives;
- decreases in the prices of the products that we sell;
- the mix of products sold and the mix of distribution channels through which products are sold;
- acceptance provisions in customer contracts;
- our ability to deliver installation or inspection services by the end of the quarter;
- changes in general and/or specific economic conditions in the networking industry;
- seasonal fluctuations in demand for our products and services;
- a disproportionate percentage of our sales occurring in the last month of the quarter;
- our ability to ship products by the end of a quarter;
- reduced visibility into the implementation cycles for our products and our customers' spending plans;
- our ability to forecast demand for our products, which in the case of lower-than-expected sales, may result in excess or obsolete inventory in addition to non-cancelable purchase commitments for component parts;
- sales to the telecommunications service provider market, which represent a significant source of large product orders, are especially volatile and difficult to forecast;
- product returns or the cancellation or rescheduling of orders;
- announcements and new product introductions by our competitors;
- our ability to develop and support relationships with enterprise customers, service providers and other potential large customers;
- our ability to achieve targeted cost reductions;
- fluctuations in warranty or other service expenses actually incurred;
- our ability to obtain sufficient supplies of sole- or limited-source components for our products on a timely basis;
- increases in the prices of the components that we purchase.

Due to the foregoing factors, period-to-period comparisons of our operating results should not be relied upon as an indicator of our future performance.

Intense competition in the market for networking equipment could prevent us from increasing revenue and maintaining profitability.

The market for network switching solutions is intensely competitive and dominated primarily by Brocade Communications Systems, Inc., Cisco Systems Inc., Hewlett-Packard Company, Huawei, and Juniper Networks, Inc. Most of our competitors have longer operating histories, greater name recognition, larger customer bases, broader product lines and substantially greater financial, technical, sales, marketing and other resources. As a result, these competitors are able to devote greater resources to the development, promotion, sale and support of their products. In addition, they have larger distribution channels, stronger brand names, access to more customers, a larger installed customer base and a greater ability to make attractive offers to channel partners and customers than we do. For example, we have encountered, and expect to continue to encounter, many potential customers who are confident in and committed to the product offerings of our principal competitors. Accordingly, these potential customers may not consider or evaluate our products. When such potential customers have considered or evaluated our products, we have in the past lost, and

expect in the future to lose, sales to some of these customers as large competitors have offered significant price discounts to secure these sales.

The pricing policies of our competitors impact the overall demand for our products and services. Some of our competitors are capable of operating at significant losses for extended periods of time, increasing pricing pressure on our products and services. If we do not maintain competitive pricing, the demand for our products and services, as well as our market share, may decline. From time to time, we may lower the prices of our products and services in response to competitive pressure. When this happens, if we are unable to reduce our component costs or improve operating efficiencies, our revenue and margins will be adversely affected.

We may not fully realize the anticipated positive impacts to future financial results from our restructuring efforts.

We are currently undergoing restructuring efforts to streamline operations and reduce operating expenses. Our ability to achieve the anticipated cost savings and other benefits from our restructuring efforts within expected time frames is subject to many estimates and assumptions, and may vary materially based on factors such as market conditions and the effect of our restructuring efforts on our work force. These estimates and assumptions are subject to significant economic, competitive and other uncertainties, some of which are beyond our control. There can be no assurance that we will fully realize the anticipated positive impacts to future financial results from our current or future restructuring efforts. If our estimates and assumptions are incorrect or if other unforeseen events occur, we may not achieve the cost savings expected from such restructurings, and our business and results of operations could be adversely affected.

Industry consolidation may lead to stronger competition and may harm our operating results.

There has been a trend toward industry consolidation in our markets for several years. We expect this trend to continue as companies attempt to strengthen or hold their market positions in an evolving industry and as companies are acquired or are unable to continue operations. For example, some of our current and potential competitors for enterprise data center business have made acquisitions, or announced new strategic alliances, designed to position them with the ability to provide end-to-end technology solutions for the enterprise data center. Companies that are strategic alliance partners in some areas of our business may acquire or form alliances with our competitors, thereby reducing their business with us. We believe that industry consolidation may result in stronger competitors that are better able to compete as sole-source vendors for customers. This could lead to more variability in our operating results and could have a material adverse effect on our business, operating results, and financial condition. Furthermore, particularly in the service provider market, rapid consolidation will lead to fewer customers, with the effect that loss of a major customer could have a material impact on results not anticipated in a customer marketplace composed of more numerous participants.

We intend to invest in engineering, sales, service, marketing and manufacturing on a long term basis, and delays or inability to attain the expected benefits may result in unfavorable operating results.

While we intend to focus on managing our costs and expenses, over the long term, we also intend to invest in personnel and other resources related to our engineering, sales, service, marketing and manufacturing functions as we focus on our foundational priorities, such as leadership in our core products and solutions and architectures for business transformation. We are likely to recognize the costs associated with these investments earlier than some of the anticipated benefits and the return on these investments may be lower, or may develop more slowly, than we expect. If we do not achieve the benefits anticipated from these investments, or if the achievement of these benefits is delayed, our operating results may be adversely affected.

We expect the average selling prices of our products to decrease, which may reduce gross margin and/or revenue.

The network equipment industry has traditionally experienced an erosion of average selling prices due to a number of factors, including competitive pricing pressures, promotional pricing and technological progress. We anticipate that the average selling prices of our products will decrease in the future in response to competitive pricing pressures, excess inventories, increased sales discounts and new product introductions by us or our competitors. We may experience decreases in future operating results due to the erosion of our average selling prices. To maintain our gross margin, we must develop and introduce on a timely basis new products and product enhancements and continually reduce our product costs. Our failure to do so would likely cause our revenue and gross margin to decline.

Our success is dependent on our ability to continually introduce new products and features that achieve broad market acceptance.

The network equipment market is characterized by rapid technological progress, frequent new product introductions, changes in customer requirements and evolving industry standards. If we do not regularly introduce new products in this dynamic environment, our product lines will become obsolete. These new products must be compatible and inter-operate with products and architectures offered by other vendors. We have and may in the future experience delays in product development and releases, and such delays have and could in the future adversely affect our ability to compete and our operating results.

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When we announce new products or product enhancements or end of sale existing products that have the potential to replace or shorten the life cycle of our existing products, customers may defer or cancel orders for our existing products. These actions could have a material adverse effect on our operating results by unexpectedly decreasing sales, increasing inventory levels of older products and exposing us to greater risk of product obsolescence.

Even if we introduce new switching products, alternative technologies could achieve widespread market acceptance and displace the Ethernet technology on which we have based our product architecture. For example, developments in routers and routing software could significantly reduce demand for our products. As a result, we may not be able to achieve widespread market acceptance of our current or future new products.

The unfavorable economic environment has and may continue to negatively impact our business and operating results.

The challenges and uncertainty currently affecting global economic conditions may negatively impact our business and operating results in the following ways:

- customers may delay or cancel plans to purchase our products and services;
- customers may not be able to pay, or may delay payment of, the amounts that they owe us which may adversely affect our cash flow, the timing of our revenue recognition and the amount of revenue;
- increased pricing pressure may result from our competitors aggressively discounting their products;
- accurate budgeting and planning will be difficult due to low visibility into future sales;
- forecasting customer demand will be more difficult, increasing the risk of either excess and obsolete inventory if our forecast is too high or insufficient inventory to meet customer demand if our forecast is too low; and
- our component suppliers and contract manufacturers have been negatively affected by the economy which may result in product delays and changes in pricing and service levels.

If global economic conditions do not show continued improvement, we believe that we could experience material adverse impacts to our business and operating results.

Claims of infringement by others may increase and the resolution of such claims may adversely affect our operating results.

Our industry is characterized by the existence of a large number of patents and frequent claims and related litigation regarding patents, copyrights (including rights to “open source” software), and other intellectual property rights. Because of the existence of a large number of patents in the networking field, the secrecy of some pending patents and the issuance of new patents at a rapid pace, it is not possible to determine in advance if a product or component might infringe the patent rights of others. Because of the potential for courts awarding substantial damages and the lack of predictability of such awards, it is not uncommon for companies in our industry to settle even potentially unmeritorious claims for very substantial amounts. Further, the entities with whom we have or could have disputes or discussions include entities with extensive patent portfolios and substantial financial assets. These entities are actively engaged in programs to generate substantial revenue from their patent portfolios and are seeking or may seek significant payments or royalties from us and others in our industry.

Litigation resulting from claims that we are infringing the proprietary rights of others has resulted and could in the future result in substantial costs and a diversion of resources, and could have a material adverse effect on our business, financial condition and results of operations. We have received notices from entities alleging that we may be infringing their patents, and we are currently parties to patent litigation as described under Part I, Item 3, Legal Proceedings. Without regard to the merits of these or any other claims, an adverse court order or a settlement could require us, among other actions, to:

- stop selling our products that incorporate the challenged intellectual property;
- obtain a royalty bearing license to sell or use the relevant technology, and that license may not be available on reasonable terms or available at all;
- pay damages; or
- redesign those products that use the disputed technology.

In addition, our products include so-called “open source” software. Open source software is typically licensed for use at no initial charge, but imposes on the user of the open source software certain requirements to license to others both the open source software as well as modifications to the open source software. Our use of open source software subjects us to certain additional risks for the following reasons:

- open source license terms may be ambiguous and may result in unanticipated obligations regarding our products;

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- open source software cannot be protected under trade secret law;
- suppliers of open-source software do not provide the warranty, support and liability protections typically provided by vendors who offer proprietary software; and
- it may be difficult for us to accurately determine the developers of the open source code and whether the acquired software infringes third-party intellectual property rights.

We believe that even if we do not infringe the rights of others, we will incur significant expenses in the future due to disputes or licensing negotiations, though the amounts cannot be determined. These expenses may be material or otherwise adversely affect our operating results.

Our operating results may be negatively affected by defending or pursuing claims or lawsuits.

We have and may in the future pursue or be subject to claims or lawsuits in the normal course of our business. In addition to the intellectual property lawsuits described above, we are currently parties to securities and contract litigation as described in "Item 3. Legal Proceedings." Regardless of the result, litigation can be expensive, lengthy and disruptive to normal business operations. Moreover, the results of complex legal proceedings are difficult to predict. An unfavorable resolution of a lawsuit in which we are a defendant could result in a court order against us or payments to other parties that would have an adverse effect on our business, results of operations, or financial condition. Even if we are successful in prosecuting claims and lawsuits, we may not recover damages sufficient to cover our expenses incurred to manage, investigate and pursue the litigation. In addition, subject to certain limitations, we may be obligated to indemnify our current and former directors, officers and employees in certain lawsuits. We do not maintain insurance coverage which will cover all of our litigation costs and liabilities.

If we fail to protect our intellectual property, our business could suffer.

We rely on a combination of patent, copyright, trademark and trade secret laws and restrictions on disclosure to protect our intellectual property rights. However, we cannot ensure that the actions we have taken will adequately protect our intellectual property rights or that other parties will not independently develop similar or competing products that do not infringe on our patents. We generally enter into confidentiality or license agreements with our employees, consultants and corporate partners, and control access to and distribution of our intellectual property and other proprietary information. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy or otherwise misappropriate or use our products or technology, which would adversely affect our business.

When our products contain undetected errors, we may incur significant unexpected expenses and could lose sales.

Network products frequently contain undetected errors when new products or new versions or updates of existing products are released to the marketplace. In the past, we have experienced such errors in connection with new products and product updates. We have experienced component problems in prior years that caused us to incur higher than expected warranty, service costs and expenses, and other related operating expenses. In the future, we expect that, from time to time, such errors or component failures will be found in new or existing products after the commencement of commercial shipments. These problems may have a material adverse effect on our business by causing us to incur significant warranty, repair and replacement costs, diverting the attention of our engineering personnel from new product development efforts, delaying the recognition of revenue and causing significant customer relations problems. Further, if products are not accepted by customers due to such defects, and such returns exceed the amount we accrued for defective returns based on our historical experience, our operating results would be adversely affected.

Our products must successfully interoperate with products from other vendors. As a result, when problems occur in a network, it may be difficult to identify the sources of these problems. The occurrence of system errors, whether or not caused by our products, could result in the delay or loss of market acceptance of our products and any necessary revisions may cause us to incur significant expenses. The occurrence of any such problems would likely have a material adverse effect on our business, operating results and financial condition.

We purchase several key components for products from single or limited sources and could lose sales if these suppliers fail to meet our needs.

We currently purchase several key components used in the manufacture of our products from single or limited sources and are dependent upon supply from these sources to meet our needs. Certain components such as tantalum capacitors, SRAM, DRAM, and printed circuit boards, have been in the past, and may in the future be, in short supply. We have encountered, and are likely in the future to encounter, shortages and delays in obtaining these or other components, and this could have a material adverse effect on our ability to meet customer orders. Our principal sole-source components include:

- ASICs;
- Merchant silicon;

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- microprocessors;
- programmable integrated circuits;
- selected other integrated circuits;
- custom power supplies; and
- custom-tooled sheet metal.

Our principal limited-source components include:

- flash memory;
- DRAMs and SRAMs;
- printed circuit boards; and
- CAMs.

We use our forecast of expected demand to determine our material requirements. Lead times for materials and components we order vary significantly, and depend on factors such as the specific supplier, contract terms and demand for a component at a given time. If forecasts exceed orders, we may have excess and/or obsolete inventory, which could have a material adverse effect on our operating results and financial condition. If orders exceed forecasts, we may have inadequate supplies of certain materials and components, which could have a material adverse effect on our ability to meet customer delivery requirements and to recognize revenue.

Generally, we do not have agreements fixing long-term prices or minimum volume requirements from suppliers. From time to time we have experienced shortages and allocations of certain components, resulting in delays in filling orders. Qualifying new suppliers to compensate for such shortages may be time-consuming and costly, and may increase the likelihood of errors in design or production. In addition, during the development of our products, we have experienced delays in the prototyping of our chipsets, which in turn has led to delays in product introductions. Similar delays may occur in the future. Furthermore, the performance of the components as incorporated in our products may not meet the quality requirements of our customers.

Our dependence on one manufacturer for our manufacturing requirements could harm our operating results.

We primarily rely on one manufacturing partner, Alpha Networks, Inc. headquartered in Hsinchu, Taiwan, to manufacture our products. We have experienced delays in product shipments from our manufacturing partner in the past, which in turn delayed product shipments to our customers. These or similar problems may arise in the future, such as delivery of products of inferior quality, delivery of insufficient quantity of products, or the interruption or discontinuance of operations of a manufacturer, any of which could have a material adverse effect on our business and operating results. In addition, any natural disaster or business interruption to our manufacturing partner could significantly disrupt our business. While we maintain strong relationships with our manufacturing partner, our agreements with this manufacturer are generally of limited duration and pricing, quality and volume commitments are negotiated on a recurring basis. The failure to maintain continuing agreements with our manufacturing partner could adversely affect our business. We intend to introduce new products and product enhancements, which will require that we rapidly achieve volume production by coordinating our efforts with those of our suppliers and contract manufacturer.

As part of our cost-reduction efforts, we will need to realize lower per unit product costs from our manufacturing partner by means of volume efficiencies and the utilization of manufacturing sites in lower-cost geographies. However, we cannot be certain when or if such price reductions will occur. The failure to obtain such price reductions would adversely affect our gross margins and operating results.

Our dependence on an OEM for all of our wireless products could harm our operating results.

We rely on Motorola to provide our wireless products. If we experience delays in product shipments from our OEM or if they experience delays from their suppliers, which in turn delays product shipments to our customers, our financial results could be negatively impacted. Problems such as delivery of products of inferior quality, delivery of insufficient quantity of products, or the interruption or discontinuance of operations of our OEM, may arise in the future, any of which could have a material adverse effect on our business and operating results.

We may engage in future acquisitions that dilute the ownership interests of our stockholders, cause us to incur debt and assume contingent liabilities.

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As part of our business strategy, we review acquisition and strategic investment prospects that we believe would complement our current product offerings, augment our market coverage or enhance our technical capabilities, or otherwise offer growth opportunities. In the event of any future acquisitions, we could:

- issue equity securities which would dilute current stockholders' percentage ownership;
- incur substantial debt;
- assume contingent liabilities; or
- expend significant cash.

These actions could have a material adverse effect on our operating results or the price of our common stock. Moreover, even if we do obtain benefits in the form of increased sales and earnings, these benefits may be recognized much later than the time when the expenses associated with an acquisition are incurred. This is particularly relevant in cases where it would be necessary to integrate new types of technology into our existing portfolio and new types of products may be targeted for potential customers with which we do not have pre-existing relationships. Acquisitions and investment activities also entail numerous risks, including:

- difficulties in the assimilation of acquired operations, technologies and/or products;
- unanticipated costs associated with the acquisition or investment transaction;
- the diversion of management's attention from other business concerns;
- adverse effects on existing business relationships with suppliers and customers;
- risks associated with entering markets in which we have no or limited prior experience;
- the potential loss of key employees of acquired organizations; and
- substantial charges for the amortization of certain purchased intangible assets, deferred stock compensation or similar items.

We may not be able to successfully integrate any businesses, products, technologies, or personnel that we might acquire in the future, and our failure to do so could have a material adverse effect on our business, operating results and financial condition.

We depend upon international sales for a significant portion of our revenue which imposes a number of risks on our business.

International sales constitute a significant portion of our net revenue. Our ability to grow will depend in part on the expansion of international sales. Our international sales primarily depend on the success of our resellers and distributors. The failure of these resellers and distributors to sell our products internationally would limit our ability to sustain and grow our revenue. There are a number of risks arising from our international business, including:

- longer accounts receivable collection cycles;
- difficulties in managing operations across disparate geographic areas;
- difficulties associated with enforcing agreements through foreign legal systems;
- higher credit risks requiring cash in advance or letters of credit;
- difficulties in safeguarding intellectual property;
- political and economic turbulence;
- terrorism, war or other armed conflict;
- natural disasters and epidemics;
- potential adverse tax consequences;
- compliance with regulatory requirements of foreign countries, including compliance with rapidly evolving environmental regulations;
- compliance with U.S. laws and regulations pertaining to the sale and distribution of products to customers in foreign countries, including export controls and the Foreign Corrupt Practices Act; and
- the payment of operating expenses in local currencies, which exposes us to risks of currency fluctuations.

All of our international sales are U.S. dollar-denominated. Future increases in the value of the U.S. dollar relative to foreign currencies could make our products less competitive in international markets. In the future, we may elect to invoice

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some of our international customers in local currency, which would expose us to fluctuations in exchange rates between the U.S. dollar and the particular local currency. If we do so, we may decide to engage in hedging transactions to minimize the risk of such fluctuations.

We have entered into foreign exchange forward contracts to offset the impact of payment of operating expenses in local currencies to some of our operating foreign subsidiaries. However, if we are not successful in managing these foreign currency transactions, we could incur losses from these activities.

We must continue to develop and increase the productivity of our indirect distribution channels to increase net revenue and improve our operating results.

Our distribution strategy focuses primarily on developing and increasing the productivity of our indirect distribution channels. If we fail to develop and cultivate relationships with significant channel partners, or if these channel partners are not successful in their sales efforts, sales of our products may decrease and our operating results could suffer. Many of our channel partners also sell products from other vendors that compete with our products. Our channel partners may not continue to market or sell our products effectively or to devote the resources necessary to provide us with effective sales, marketing and technical support. We may not be able to successfully manage our sales channels or enter into additional reseller and/or distribution agreements. Our failure to do any of these could limit our ability to grow or sustain revenue.

Our operating results for any given period have and will continue to depend to a significant extent on large orders from a relatively small number of channel partners and other customers. However, we do not have binding purchase commitments from any of them. A substantial reduction or delay in sales of our products to a significant reseller, distributor or other customer could harm our business, operating results and financial condition because our expense levels are based on our expectations as to future revenue and to a large extent are fixed in the short term. Under specified conditions, some third-party distributors are allowed to return products to us and unexpected returns could adversely affect our results.

The sales cycle for our products is long and we may incur substantial non-recoverable expenses or devote significant resources to sales that do not occur when anticipated.

Our products represent a significant strategic decision by a customer regarding its communications infrastructure. The decision by customers to purchase our products is often based on the results of a variety of internal procedures associated with the evaluation, testing, implementation and acceptance of new technologies. Accordingly, the product evaluation process frequently results in a lengthy sales cycle, typically ranging from three months to longer than a year, and as a result, our ability to sell products is subject to a number of significant risks, including risks that:

- budgetary constraints and internal acceptance reviews by customers will result in the loss of potential sales;
- there may be substantial variation in the length of the sales cycle from customer to customer, making decisions on the expenditure of resources difficult to assess;
- we may incur substantial sales and marketing expenses and expend significant management time in an attempt to initiate or increase the sale of products to customers, but not succeed;
- if a sales forecast from a specific customer for a particular quarter is not achieved in that quarter, we may be unable to compensate for the shortfall, which could harm our operating results; and
- downward pricing pressures could occur during the lengthy sales cycle for our products.

To successfully manage our business or achieve our goals, we must attract, retain, train, motivate, develop and promote key employees, and failure to do so can harm us.

Our success depends to a significant degree upon the continued contributions of our key management, engineering, sales and marketing, service and operations personnel, many of whom would be difficult to replace. We do not have employment contracts with these individuals that mandate that they render services for any specific term, nor do we carry life insurance on any of our key personnel. We have experienced and may in the future experience significant turnover in our executive personnel. In addition, retention has generally become more difficult for us, in part because of our restructuring efforts and in part due to the exercise price of most of the stock options granted to many of our employees is below the market price. As a result, we experienced high levels of attrition. We believe our future success will also depend in large part upon our ability to attract and retain highly skilled managerial, engineering, sales and marketing, service, finance and operations personnel. The market for these personnel is competitive, and we

have had difficulty in hiring employees, particularly engineers, in the time-frame we desire.
Companies in the networking industry whose employees accept positions with competitors frequently claim that competitors have engaged in unfair hiring practices. We have from time to time been involved in claims like this with other

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companies and, although to date they have not resulted in material litigation, we do not know whether we will be involved in additional claims in the future. We could incur substantial costs in litigating any such claims, regardless of the merits.

Failure to successfully expand our sales and support teams or educate them in regard to technologies and our product families may harm our operating results.

The sale of our products and services requires a concerted effort that is frequently targeted at several levels within a prospective customer's organization. We may not be able to increase net revenue unless we expand our sales and support teams in order to address all of the customer requirements necessary to sell our products.

We cannot assure you that we will be able to successfully integrate employees into our company or to educate current and future employees in regard to rapidly evolving technologies and our product families. A failure to do so may hurt our revenue growth and operating results.

Failure of our products to comply with evolving industry standards and complex government regulations may adversely impact our business.

If we do not comply with existing or evolving industry standards and government regulations, we may not be able to sell our products where these standards or regulations apply. The network equipment industry in which we compete is characterized by rapid changes in technology and customers' requirements and evolving industry standards. As a result, our success depends on:

- the timely adoption and market acceptance of industry standards, and timely resolution of conflicting U.S. and international industry standards; and
- our ability to influence the development of emerging industry standards and to introduce new and enhanced products that are compatible with such standards.

In the past, we have introduced new products that were not compatible with certain technological standards, and in the future, we may not be able to effectively address the compatibility and interoperability issues that arise as a result of technological changes and evolving industry standards.

Our products must also comply with various U.S. federal government regulations and standards defined by agencies such as the Federal Communications Commission, standards established by governmental authorities in various foreign countries and recommendations of the International Telecommunication Union. In some circumstances, we must obtain regulatory approvals or certificates of compliance before we can offer or distribute our products in certain jurisdictions or to certain customers. Complying with new regulations or obtaining certifications can be costly and disruptive to our business.

If we do not comply with existing or evolving industry standards or government regulations, we will not be able to sell our products where these standards or regulations apply, which may prevent us from sustaining our net revenue or achieving profitability.

Changes in the effective tax rate including from the release of the valuation allowance recorded against our net U.S. deferred tax assets, or adverse outcomes resulting from examination of our income or other tax returns or change in ownership, could adversely affect our results.

Our future effective tax rates may be volatile or adversely affected by changes in our business or U.S. or foreign tax laws, including: the partial or full release of the valuation allowance recorded against our net U.S. deferred tax assets; expiration of or lapses in the research and development tax credit laws; transfer pricing adjustments; tax effects of stock-based compensation; or costs related to restructurings. In addition, we are subject to the examination of our income tax returns by the Internal Revenue Service and other tax authorities. Although we regularly assess the likelihood of adverse outcomes resulting from these examinations to determine the adequacy of our provision for income taxes, there is no assurance that such determinations by us are in fact adequate. Changes in our effective tax rates or amounts assessed upon examination of our tax returns may have a material, adverse impact on our cash flows and our financial condition.

Our future effective tax rate in particular could be adversely affected by a change in ownership pursuant to U.S. Internal Revenue Code Section 382. If a change in ownership occurs, it may limit our ability to utilize our net operating losses to offset our U.S. taxable income. If U.S. taxable income is greater than the change in ownership limitation, we will pay a higher rate of tax with respect to the amount of taxable income that exceeds the

limitation. This could have a material adverse impact on our results of operations. On April 26, 2012, we adopted an amended and restated Shareholder Rights plan to help protect our assets. The plan is effective through April 30, 2013.
If we do not adequately manage and evolve our financial reporting and managerial systems and processes, our ability to manage and grow our business may be harmed.

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Our ability to successfully implement our business plan and comply with regulations requires an effective planning and management process. We need to continue improving our existing, and implement new, operational and financial systems, procedures and controls. Any delay in the implementation of, or disruption in the transition to, new or enhanced systems, procedures or controls, could harm our ability to record and report financial and management information on a timely and accurate basis, or to forecast future results.

Compliance with laws, rules and regulations relating to corporate governance and public disclosure may result in additional expenses.

Federal securities laws, rules and regulations, as well as NASDAQ rules and regulations, require companies to maintain extensive corporate governance measures, impose comprehensive reporting and disclosure requirements, set strict independence and financial expertise standards for audit and other committee members and impose civil and criminal penalties for companies and their Chief Executive Officers, Chief Financial Officers and directors for securities law violations. These laws, rules and regulations and the interpretation of these requirements are evolving, and we are making investments to evaluate current practices and to continue to achieve compliance.

Our headquarters and some significant supporting businesses are located in northern California and other areas subject to natural disasters that could disrupt our operations and harm our business.

Our corporate headquarters are located in Silicon Valley in Northern California. Historically, this region as well as our R&D center in North Carolina has been vulnerable to natural disasters and other risks, such as earthquakes, fires, floods and tropical storms, which at times have disrupted the local economy and posed physical risks to our property. We have contract manufacturers located in Taiwan where similar natural disasters and other risks may disrupt the local economy and pose physical risks to our property and the property of our contract manufacturer.

In addition, the continued threat of terrorism and heightened security and military action in response to this threat, or any future acts of terrorism, may cause further disruptions to the economies of the U.S. and other countries. If such disruptions result in delays or cancellations of customer orders for our products, our business and operating results will suffer.

We currently do not have redundant, multiple site capacity in the event of a natural disaster, terrorist act or other catastrophic event. In the event of such an occurrence, our business would suffer.

Our stock price has been volatile in the past and our stock price may significantly fluctuate in the future.

In the past, our common stock price has fluctuated significantly. This could continue as we or our competitors announce new products, our results or those of our customers or competition fluctuate, conditions in the networking or semiconductor industry change, or when investors, change their sentiment toward stocks in the networking technology sector.

In addition, fluctuations in our stock price and our price-to-earnings multiple may make our stock attractive to momentum, hedge or day-trading investors who often shift funds into and out of stock rapidly, exacerbating price fluctuations in either direction, particularly when viewed on a quarterly basis.

Provisions in our charter documents and Delaware law and our adoption of a stockholder rights plan may delay or prevent an acquisition of Extreme, which could decrease the value of our Common Stock.

Our certificate of incorporation and bylaws and Delaware law contain provisions that could make it more difficult for a third party to acquire us without the consent of our Board of Directors. Delaware law also imposes some restrictions on mergers and other business combinations between us and any holder of 15% or more of our outstanding common stock. In addition, our Board of Directors has the right to issue preferred stock without stockholder approval, which could be used to dilute the stock ownership of a potential hostile acquirer. Although we believe these provisions of our certificate of incorporation and bylaws and Delaware law and our stockholder rights plan, which is described below, will provide for an opportunity to receive a higher bid by requiring potential acquirers to negotiate with our Board of Directors, these provisions apply even if the offer may be considered beneficial by some of our stockholders.

Our Board of Directors adopted a stockholder rights plan, under which we declared and paid a dividend of one right for each share of common stock held by stockholders of record as of May 14, 2001. Under the plan, each right will entitle stockholders to purchase a fractional share of our preferred stock for $150.00. Each such fractional share of the new preferred stock has terms designed to make it substantially the economic equivalent of one share of common stock. Initially the rights will not be exercisable and will trade with our common stock. Generally, the rights may become exercisable if a person or group acquires beneficial ownership of 4.95% or more of our common stock or commences a tender or exchange offer upon consummation of which such person or group would beneficially own 4.95% or more of our common stock. When the rights become exercisable, our Board of Directors has the right to authorize the issuance of one share of our common stock in exchange for each right that is then exercisable.

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We rely on the availability of third-party licenses

Some of our products are designed to include software or other intellectual property licensed from third parties. It may be necessary in the future to seek or renew licenses relating to various aspects of these products. There can be no assurance that the necessary licenses would be available on acceptable terms, if at all. The inability to obtain certain licenses or other rights or to obtain such licenses or rights on favorable terms, or the need to engage in litigation regarding these matters, could have a material adverse effect on our business, operating results, and financial condition. Moreover, the inclusion in our products of software or other intellectual property licensed from third parties on a nonexclusive basis could limit our ability to protect our proprietary rights in our products.

Market conditions and changes in the industry could lead to discontinuation of our products or businesses resulting in asset impairments

In response to changes in industry and market conditions, we may be required to strategically realign our resources and consider restructuring, disposing of, or otherwise exiting businesses in the future. Any future decision to limit investment in or dispose of or otherwise exit businesses may result in the recording of special charges, such as inventory and technology-related write-offs, workforce reduction costs, charges relating to consolidation of excess facilities, or claims from third parties who were resellers or users of discontinued products. Our estimates with respect to the useful life or ultimate recoverability of our carrying basis of assets, including purchased intangible assets, could change as a result of such assessments and decisions. Although in certain instances, our supply agreements allow us the option to cancel, reschedule, and adjust our requirements based on our business needs prior to firm orders being placed, our loss contingencies may include liabilities for contracts that we cannot cancel with contract manufacturers and suppliers. Further, our estimates relating to the liabilities for excess facilities are affected by changes in real estate market conditions.

If our products do not effectively inter-operate with our customers’ networks and result in cancellations and delays of installations our business could be harmed.

Our products are designed to interface with our customers’ existing networks, each of which have different specifications and utilize multiple protocol standards and products from other vendors. Many of our customers’ networks contain multiple generations of products that have been added over time as these networks have grown and evolved. Our products must inter-operate with many or all of the products within these networks as well as future products in order to meet our customers’ requirements. If we find errors in the existing software or defects in the hardware used in our customers’ networks, we may need to modify our software or hardware to fix or overcome these errors so that our products will inter-operate and scale with the existing software and hardware, which could be costly and could negatively affect our business, financial condition, and results of operations. In addition, if our products do not inter-operate with those of our customers’ networks, demand for our products could be adversely affected or orders for our products could be cancelled. This could hurt our operating results, damage our reputation, and seriously harm our business and prospects.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds - Not applicable

Item 3. Defaults Upon Senior Securities - Not applicable

Item 4. Mine Safety Disclosure - Not Applicable

Item 5. Other Information

Item 6. Exhibits

(a) Exhibits:

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| Exhibit Number | Description of Document | Incorporated by Reference | | | Filed Herewith |
|---|---|---|---|---|---|
| | | Form | Filing Date | Number | |
| 10.1 | Lease Agreement by and between RDU Center III LLC and Extreme Networks, Inc. dated October 15, 2012. | 8-K | 10/19/2012 | 10.1 | |
| 10.2 | First Amendment to Lease Agreement by and between RDU Center III LLC and Extreme Networks, Inc. dated December 31, 2012. | 8-K | 1/7/2013 | 10.1 | |
| 10.3 | Office Space Lease Agreement by and between W3 Ridge Rio Robles Property LLC and Extreme Networks, Inc., dated December 31, 2012. | 8-K | 1/7/2013 | 10.2 | |
| 31.1 | Section 302 Certification of Chief Executive Officer | | | | X |
| 31.2 | Section 302 Certification of Chief Financial Officer | | | | X |
| 32.1 | Section 906 Certification of Chief Executive Officer | | | | X |
| 32.2 | Section 906 Certification of Chief Financial Officer | | | | X |
| 101.INS | XBRL Instance Document.* | | | | |
| 101.SCH | XBRL Taxonomy Extension Schema Document.* | | | | |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document.* | | | | |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document.* | | | | |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document.* | | | | |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document* | | | | |

* Pursuant to Rule 406T of Regulation S-T, these interactive data files are furnished and not filed or a part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, as amended; are deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, as amended; and otherwise are not subject to liability under these sections.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

EXTREME NETWORKS, INC.
(Registrant)

/S/ JOHN KURTZWEIL
JOHN KURTZWEIL
Senior Vice President, Chief Financial Officer, and Chief Accounting Officer
January 31, 2013