

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

**Form 10-Q**

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

For the quarterly period ended September 30, 2016

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 1-13449

**QUANTUM CORPORATION**

**Delaware**

(State or other jurisdiction of incorporation or organization)

**224 Airport Parkway, Suite 300, San Jose, California**

(Address of principal executive offices)

**94-2665054**

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

**95110**

(Zip Code)

**(408) 944-4000**

(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

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

As of the close of business on October 28, 2016, there were 271,184,262 shares of Quantum Corporation's common stock issued and outstanding.

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PART I—FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

**QUANTUM CORPORATION**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
(In thousands, except par value)  
(Unaudited)

| <b>Assets</b>   | <b>September 30, 2016</b> | <b>March 31, 2016</b> |
|---|---------------------------|-----------------------|
| <b>Current assets:</b>  |                           |                       |
| Cash and cash equivalents   | \$ 29,528                 | \$ 33,870             |
| Restricted cash   | 2,801                     | 2,788                 |
| Accounts receivable, net of allowance for doubtful accounts of \$16 and \$22, respectively  | 107,910                   | 105,959               |
| Manufacturing inventories   | 36,242                    | 40,614                |
| Service parts inventories   | 20,422                    | 21,407                |
| Other current assets  | 6,967                     | 6,953                 |
| Total current assets  | <u>203,870</u>            | <u>211,591</u>        |
| <b>Long-term assets:</b>  |                           |                       |
| Property and equipment, less accumulated depreciation   | 12,353                    | 12,939                |
| Intangible assets, less accumulated amortization  | 355                       | 451                   |
| Other long-term assets  | 4,320                     | 4,565                 |
| Total long-term assets  | <u>17,028</u>             | <u>17,955</u>         |
|   | <u>\$ 220,898</u>         | <u>\$ 229,546</u>     |
| <b>Liabilities and Stockholders' Deficit</b>  |                           |                       |
| <b>Current liabilities:</b>   |                           |                       |
| Accounts payable  | \$ 50,859                 | \$ 46,136             |
| Accrued warranty  | 3,371                     | 3,430                 |
| Deferred revenue, current   | 82,421                    | 88,919                |
| Accrued restructuring charges, current  | 1,784                     | 1,621                 |
| Long-term debt, current   | —                         | 3,000                 |
| Accrued compensation  | 23,806                    | 22,744                |
| Other accrued liabilities   | 11,510                    | 13,806                |
| Total current liabilities   | <u>173,751</u>            | <u>179,656</u>        |
| <b>Long-term liabilities:</b>   |                           |                       |
| Deferred revenue, long-term   | 32,763                    | 35,427                |
| Accrued restructuring charges, long-term  | 734                       | 1,116                 |
| Long-term debt  | 60,250                    | 62,709                |
| Convertible subordinated debt, long-term, net of unamortized debt issuance costs of \$517 and \$747, respectively   | 69,483                    | 69,253                |
| Other long-term liabilities   | 7,340                     | 8,324                 |
| Total long-term liabilities   | <u>170,570</u>            | <u>176,829</u>        |
| <b>Stockholders' deficit:</b>   |                           |                       |
| Common stock, \$0.01 par value; 1,000,000 shares authorized; 271,171 and 266,209 shares issued and outstanding at September 30, 2016 and March 31, 2016, respectively | 2,712                     | 2,662                 |
| Capital in excess of par  | 468,132                   | 464,549               |
| Accumulated deficit   | (597,963)                 | (597,994)             |
| Accumulated other comprehensive income  | 3,696                     | 3,844                 |
| Total stockholders' deficit   | <u>(123,423)</u>          | <u>(126,939)</u>      |
|   | <u>\$ 220,898</u>         | <u>\$ 229,546</u>     |

See accompanying Notes to Condensed Consolidated Financial Statements.

**QUANTUM CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
(In thousands, except per share data)  
(Unaudited)

|   | Three Months Ended |                    | Six Months Ended   |                    |
|---|--------------------|--------------------|--------------------|--------------------|
|   | September 30, 2016 | September 30, 2015 | September 30, 2016 | September 30, 2015 |
| Product revenue                               | \$ 88,575          | \$ 71,057          | \$ 160,401         | \$ 133,776         |
| Service revenue                               | 36,620             | 37,247             | 72,438             | 75,186             |
| Royalty revenue                               | 9,547              | 8,721              | 18,187             | 18,919             |
| Total revenue                                 | 134,742            | 117,025            | 251,026            | 227,881            |
| Cost of product revenue                       | 64,352             | 53,073             | 114,484            | 100,037            |
| Cost of service revenue                       | 14,910             | 17,635             | 30,691             | 34,562             |
| Total cost of revenue                         | 79,262             | 70,708             | 145,175            | 134,599            |
| Gross margin                                  | 55,480             | 46,317             | 105,851            | 93,282             |
| Operating expenses:                           |                    |                    |                    |                    |
| Research and development                      | 11,401             | 13,370             | 22,459             | 26,693             |
| Sales and marketing                           | 26,146             | 28,043             | 52,513             | 55,648             |
| General and administrative                    | 12,572             | 14,136             | 25,532             | 28,122             |
| Restructuring charges                         | 15                 | 387                | 2,067              | 645                |
| Total operating expenses                      | 50,134             | 55,936             | 102,571            | 111,108            |
| Income (loss) from operations                 | 5,346              | (9,619)            | 3,280              | (17,826)           |
| Other income                                  | 10                 | 714                | 166                | 428                |
| Interest expense                              | (1,485)            | (1,975)            | (2,993)            | (3,898)            |
| Income (loss) before income taxes             | 3,871              | (10,880)           | 453                | (21,296)           |
| Income tax provision                          | 45                 | 347                | 422                | 686                |
| Net income (loss)                             | \$ 3,826           | \$ (11,227)        | \$ 31              | \$ (21,982)        |
| Basic and diluted net income (loss) per share | \$ 0.01            | \$ (0.04)          | \$ 0.00            | \$ (0.08)          |
| Weighted average shares:                      |                    |                    |                    |                    |
| Basic   | 270,432            | 263,058            | 268,396            | 260,766            |
| Diluted                                       | 272,382            | 263,058            | 269,593            | 260,766            |

See accompanying Notes to Condensed Consolidated Financial Statements.

**QUANTUM CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**  
(In thousands)  
(Unaudited)

|  | Three Months Ended |                    | Six Months Ended   |                    |
|--|--------------------|--------------------|--------------------|--------------------|
|  | September 30, 2016 | September 30, 2015 | September 30, 2016 | September 30, 2015 |
| Net income (loss)  | \$ 3,826           | \$ (11,227)        | \$ 31              | \$ (21,982)        |
| Other comprehensive income (loss), net of taxes:                             |                    |                    |                    |                    |
| Foreign currency translation adjustments                                     | 206                | (340)              | (133)              | 101                |
| Net unrealized gain (loss) on revaluation of long-term intercompany balances | (57)               | 207                | (15)               | 121                |
| Total other comprehensive income (loss)                                      | 149                | (133)              | (148)              | 222                |
| Total comprehensive income (loss)  | <u>\$ 3,975</u>    | <u>\$ (11,360)</u> | <u>\$ (117)</u>    | <u>\$ (21,760)</u> |

See accompanying Notes to Condensed Consolidated Financial Statements.

**QUANTUM CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(Unaudited)  
(In thousands)

|  | Six Months Ended   |                    |
|--|--------------------|--------------------|
|  | September 30, 2016 | September 30, 2015 |
| <b>Cash flows from operating activities:</b>   |                    |                    |
| Net income (loss)  | \$ 31              | \$ (21,982)        |
| Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities: |                    |                    |
| Depreciation   | 2,710              | 3,361              |
| Amortization of intangible assets  | 96                 | 185                |
| Amortization of debt issuance costs  | 336                | 648                |
| Service parts lower of cost or market adjustment   | 2,659              | 3,050              |
| Deferred income taxes  | 17                 | 35                 |
| Share-based compensation   | 3,648              | 5,100              |
| Changes in assets and liabilities:   |                    |                    |
| Accounts receivable  | (1,951)            | 31,896             |
| Manufacturing inventories  | 2,429              | 10,050             |
| Service parts inventories  | (766)              | (526)              |
| Accounts payable   | 4,875              | 1,624              |
| Accrued warranty   | (59)               | (746)              |
| Deferred revenue   | (9,162)            | (16,429)           |
| Accrued restructuring charges  | (219)              | (2,017)            |
| Accrued compensation   | 1,049              | (10,871)           |
| Other assets and liabilities   | (3,112)            | (5,723)            |
| Net cash provided by (used in) operating activities  | 2,581              | (2,345)            |
| <b>Cash flows from investing activities:</b>   |                    |                    |
| Purchases of property and equipment  | (1,249)            | (1,611)            |
| Change in restricted cash  | (5)                | (110)              |
| Net cash used in investing activities  | (1,254)            | (1,721)            |
| <b>Cash flows from financing activities:</b>   |                    |                    |
| Borrowings of long-term debt, net  | 6,300              | —                  |
| Repayments of long-term debt   | (11,959)           | —                  |
| Restricted cash used to repay convertible subordinated debt  | —                  | (16,280)           |
| Payment of taxes due upon vesting of restricted stock  | (673)              | (3,101)            |
| Proceeds from issuance of common stock   | 658                | 1,740              |
| Net cash used in financing activities  | (5,674)            | (17,641)           |
| Effect of exchange rate changes on cash and cash equivalents                                       | 5                  | (12)               |
| Net decrease in cash and cash equivalents  | (4,342)            | (21,719)           |
| Cash and cash equivalents at beginning of period   | 33,870             | 67,948             |
| Cash and cash equivalents at end of period   | \$ 29,528          | \$ 46,229          |
| <b>Supplemental disclosure of cash flow information:</b>   |                    |                    |
| Purchases of property and equipment included in accounts payable                                   | \$ 217             | \$ 1,136           |

See accompanying Notes to Condensed Consolidated Financial Statements.

**QUANTUM CORPORATION**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

**NOTE 1: BASIS OF PRESENTATION**

Quantum Corporation (“Quantum”, the “Company”, “us” or “we”), founded in 1980 and reincorporated in Delaware in 1987, is a leading expert in scale-out storage, archive and data protection, providing solutions for capturing, sharing, managing and preserving digital assets over the entire data lifecycle. Our customers, ranging from small businesses to large/multi-national enterprises, trust us to address their most demanding data workflow challenges. Our end-to-end tiered storage solutions enable users to maximize the value of their data by making it accessible whenever and wherever needed, retaining it indefinitely and reducing total cost and complexity. We work closely with a broad network of distributors, value-added resellers (“VARs”), direct marketing resellers (“DMRs”), original equipment manufacturers (“OEMs”) and other suppliers to meet customers’ evolving needs. Our stock is traded on the New York Stock Exchange under the symbol QTM.

The accompanying unaudited Condensed Consolidated Financial Statements include the accounts of Quantum and our wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated. The interim financial statements reflect all adjustments, consisting of normal recurring adjustments that, in the opinion of management, are necessary for a fair statement of the results for the periods shown. The results of operations for such periods are not necessarily indicative of the results expected for the full fiscal year. The Condensed Consolidated Balance Sheet as of March 31, 2016 has been derived from the audited financial statements at that date, but it does not include all disclosures required by accounting principles generally accepted in the United States for complete financial statements. The accompanying financial statements should be read in conjunction with the audited Consolidated Financial Statements for the fiscal year ended March 31, 2016 included in our Annual Report on Form 10-K, filed with the Securities and Exchange Commission (“SEC”) on June 3, 2016, as amended by Amendment No. 1 to Form 10-K, filed with the SEC on July 27, 2016 (together, the “Form 10-K”).

***Recently Adopted Accounting Pronouncements***

In April 2015, the FASB issued ASU No. 2015-05, *Customer's Accounting for Fees Paid in a Cloud Computing Arrangement* (“ASU 2015-05”). ASU 2015-05 requires that customers apply the same criteria as vendors to determine whether a cloud computing arrangement (“CCA”) contains a software license or is solely a service contract. Under ASU 2015-05, fees paid by a customer in a CCA will be within the scope of internal-use software guidance if both of the following criteria are met: 1) the customer has the contractual right to take possession of the software at any time without significant penalty and 2) it is feasible for the customer to run the software on its own hardware (or to contract with another party to host the software). We adopted ASU 2015-05 in the first quarter of fiscal 2017 and adoption did not impact our statements of financial condition, results of operations, cash flows and financial statement disclosures.

***Recent Accounting Pronouncements***

In August 2014, the FASB issued ASU No. 2014-15, *Presentation of Financial Statements – Going Concern (Topic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern* (“ASU 2014-15”). ASU 2014-15 requires that management assess an entity’s ability to continue as a going concern by incorporating and expanding upon certain principles that are currently in U.S. auditing standards. ASU 2014-15 is effective for annual periods ending after December 15, 2016, and for annual periods and interim periods thereafter. We plan to adopt ASU 2014-15 as of the end of our fiscal year ending March 31, 2017. We are currently evaluating the guidance to determine the potential impact on our financial condition, results of operations, cash flows and financial statement disclosures.

In July 2015, the FASB issued ASU No. 2015-11, *Inventory (Topic 330)* (“ASU 2015-11”). ASU 2015-11 requires that an entity measure all inventory at the lower of cost and net realizable value, except for inventory that is measured using last-in, first-out (LIFO) or the retail inventory method. ASU 2015-11 will become effective for us beginning April 1, 2017, or fiscal 2018. We are currently evaluating the guidance to determine the potential impact on our financial condition, results of operations, cash flows and financial statement disclosures.

In January 2016, the FASB issued ASU No. 2016-01, *Financial Instruments - Overall (Topic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities* (“ASU 2016-01”). ASU 2016-01 addresses certain aspects of recognition, measurement, presentation and disclosures of financial instruments. ASU 2016-01 will become effective for us beginning April 1, 2018, or fiscal 2019. We are currently evaluating the guidance to determine the potential impact on our financial condition, results of operations, cash flows and financial statement disclosures.

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In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)* ("ASU 2016-02"). ASU 2016-02 provides a new comprehensive model for lease accounting. Under ASU 2016-02, lessees and lessors should apply a "right-of-use" model in accounting for all leases and eliminate the concept of operating leases and off-balance sheet leases. ASU 2016-02 will become effective for us beginning April 1, 2019, or fiscal 2020. We are currently evaluating the guidance to determine the potential impact on our financial condition, results of operations, cash flows and financial statement disclosures.

In March 2016, the FASB issued ASU No. 2016-09, *Compensation - Stock compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting* ("ASU 2016-09"). ASU 2016-09 simplifies several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities and classification on the statement of cash flows. ASU 2016-09 will become effective for us beginning April 1, 2017, or fiscal 2018. We are currently evaluating the guidance to determine the potential impact on our financial condition, results of operations, cash flows and financial statement disclosures.

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Receipts and Cash Payments* ("ASU 2016-15"). ASU 2016-15 provides guidance on the following eight specific cash flow issues: 1) debt prepayment or debt extinguishment costs, 2) settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing, 3) contingent consideration payments made after a business combination, 4) proceeds from the settlement of insurance claims, 5) proceeds from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies, 6) distributions received from equity method investees, 7) beneficial interests in securitization transactions and 8) separately identifiable cash flows and application of the predominance principle. ASU 2016-15 will become effective for us beginning April 1, 2018, or fiscal 2019. We are currently evaluating the guidance to determine the potential impact on our cash flows.

The FASB issued the following accounting standard updates related to its revenue convergence project :

- ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)* ("ASU 2014-09") in May 2014. ASU 2014-09 requires entities to recognize revenue through the application of a five-step model, which includes identification of the contract, identification of the performance obligations, determination of the transaction price, allocation of the transaction price to the performance obligations and recognition of revenue as the entity satisfies the performance obligations.
- ASU No. 2016-08, *Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)* ("ASU 2016-08") in March 2016. ASU 2016-08 does not change the core principle of revenue recognition in Topic 606 but clarifies the implementation guidance on principal versus agent considerations.
- ASU No. 2016-10, *Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing* ("ASU 2016-10") in April 2016. ASU 2016-10 does not change the core principle of revenue recognition in Topic 606 but clarifies the implementation guidance on identifying performance obligations and the licensing implementation guidance, while retaining the related principles for those areas.
- ASU No. 2016-11, *Revenue Recognition (Topic 605) and Derivatives and Hedging (Topic 815): Rescission of SEC Guidance Because of Accounting Standards Updates 2014-09 and 2014-16 Pursuant to Staff Announcements at the March 3, 2016 EITF Meeting (SEC Update)* ("ASU 2016-11") in May 2016. ASU 2016-11 rescinds SEC paragraphs pursuant to two SEC Staff Announcements at the March 3, 2016 EITF meeting. The SEC Staff is rescinding SEC Staff Observer comments that are codified in Topic 605 and Topic 932, effective upon adoption of Topic 606.
- ASU No. 2016-12, *Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients* in May 2016. ASU 2016-12 does not change the core principle of revenue recognition in Topic 606 but clarifies the implementation guidance on a few narrow areas and adds some practical expedients to the guidance.

These ASUs will become effective for us beginning April 1, 2018, or fiscal 2019. We are currently evaluating the guidance to determine the potential impact on our financial condition, results of operations, cash flows and financial statement disclosures.

## NOTE 2: FAIR VALUE

Our assets measured and recorded at fair value on a recurring basis consist of money market funds, which are included in cash and cash equivalents in our Condensed Consolidated Balance Sheets and are valued using quoted market prices (level 1 fair value measurements) at the respective balance sheet dates (in thousands):

|                    | As of              |                |
|--------------------|--------------------|----------------|
|                    | September 30, 2016 | March 31, 2016 |
| Money market funds | \$ 3,646           | \$ 1,640       |



We did not record impairments to any non-financial assets in thesecond quarter or first six months of fiscal 2017 or fiscal 2016. We do not have any non-financial liabilities measured and recorded at fair value on a non-recurring basis.

Our financial liabilities were comprised primarily of convertible subordinated debt and long-term debt aSeptember 30, 2016 and March 31, 2016. The carrying value and fair value of our convertible subordinated debt and long-term debt were as follows (in thousands):

|  | As of              |            |                |            |
|--|--------------------|------------|----------------|------------|
|  | September 30, 2016 |            | March 31, 2016 |            |
|  | Carrying Value     | Fair Value | Carrying Value | Fair Value |
| Convertible subordinated debt <sup>(1)</sup> | \$ 69,483          | \$ 66,333  | \$ 69,253      | \$ 51,686  |
| Long-term debt <sup>(2)</sup>                | \$ 60,250          | \$ 60,247  | \$ 65,709      | \$ 65,741  |

<sup>(1)</sup> Fair value based on quoted market prices in less active markets (level 2).

<sup>(2)</sup> Fair value based on outstanding borrowings and market interest rates (level 2).

**NOTE 3: INVENTORIES**

Manufacturing inventories and service parts inventories consisted of the following (in thousands):

|                                   | As of              |                  |
|-----------------------------------|--------------------|------------------|
|                                   | September 30, 2016 | March 31, 2016   |
| <b>Manufacturing inventories:</b> |                    |                  |
| Finished goods                    | \$ 19,591          | \$ 22,127        |
| Work in process                   | 447                | 665              |
| Materials and purchased parts     | 16,204             | 17,822           |
|                                   | <u>\$ 36,242</u>   | <u>\$ 40,614</u> |
| <b>Service parts inventories:</b> |                    |                  |
| Finished goods                    | \$ 15,709          | \$ 16,381        |
| Component parts                   | 4,713              | 5,026            |
|                                   | <u>\$ 20,422</u>   | <u>\$ 21,407</u> |

**NOTE 4: INTANGIBLE ASSETS**

We evaluate our amortizable and indefinite-lived intangible assets (“long-lived assets”) for impairment whenever indicators of impairment exist. We concluded the carrying amount of our long-lived assets was recoverable and there was no impairment in the second quarter or first six months of fiscal 2017 or fiscal 2016. The following provides a summary of the carrying value of our long-lived assets (in thousands):

|                      | As of              |                          |               |                   |                          |               |
|----------------------|--------------------|--------------------------|---------------|-------------------|--------------------------|---------------|
|                      | September 30, 2016 |                          |               | March 31, 2016    |                          |               |
|                      | Gross Amount       | Accumulated Amortization | Net Amount    | Gross Amount      | Accumulated Amortization | Net Amount    |
| Purchased technology | \$ 178,292         | \$ (177,937)             | \$ 355        | \$ 178,292        | \$ (177,841)             | \$ 451        |
| Trademarks           | 3,900              | (3,900)                  | —             | 3,900             | (3,900)                  | —             |
| Customer lists       | 64,701             | (64,701)                 | —             | 64,701            | (64,701)                 | —             |
|                      | <u>\$ 246,893</u>  | <u>\$ (246,538)</u>      | <u>\$ 355</u> | <u>\$ 246,893</u> | <u>\$ (246,442)</u>      | <u>\$ 451</u> |

**NOTE 5: ACCRUED WARRANTY**

The changes in the accrued warranty balance were (in thousands):

|   | Three Months Ended |                    | Six Months Ended   |                    |
|---|--------------------|--------------------|--------------------|--------------------|
|   | September 30, 2016 | September 30, 2015 | September 30, 2016 | September 30, 2015 |
| Beginning balance                                       | \$ 3,444           | \$ 3,600           | \$ 3,430           | \$ 4,219           |
| Additional warranties issued                            | 1,626              | 1,523              | 3,606              | 3,130              |
| Adjustments for warranties issued in prior fiscal years | 243                | 298                | 401                | (69)               |
| Settlements   | (1,942)            | (1,948)            | (4,066)            | (3,807)            |
| Ending balance  | \$ 3,371           | \$ 3,473           | \$ 3,371           | \$ 3,473           |

We warrant our products against certain defects for one to three years. A provision for estimated future costs and estimated returns for repair or replacement relating to warranty is recorded when products are shipped and revenue is recognized. Our estimate of future costs to satisfy warranty obligations is primarily based on historical trends and, if believed to be significantly different from historical trends, estimates of future failure rates and future costs of repair. Future costs of repair include materials consumed in the repair, labor and overhead amounts necessary to perform the repair. If we determine in a future period that either actual failure rates or actual costs of repair were to differ from our estimates, we record the impact of those differences in that future period.

**NOTE 6: DEBT***Wells Fargo Credit Agreement*

On April 15, 2016, our credit agreement with Wells Fargo (as amended, the "WF credit agreement") was amended to modify the maturity date, increase the excess availability requirement over time and reduce the maximum amount of intellectual property assets that may be included in the borrowing base over time.

Under the WF credit agreement, we had the ability to borrow the lesser of \$75 million or the amount of the monthly borrowing base under a senior secured revolving credit facility, which matures August 10, 2017. As of September 30, 2016, we had a \$60.3 million outstanding balance on the line of credit at a weighted average interest rate of 3.04%. In addition, we had letters of credit totaling \$1.0 million and an excess availability requirement of \$8.0 million, reducing the maximum amount available to borrow to \$5.7 million as of September 30, 2016. Quarterly, we were required to pay a 0.375% commitment fee on undrawn amounts under the revolving credit facility.

The WF credit agreement contained financial covenants and customary events of default for such securities, including cross-payment default and cross-acceleration to other material indebtedness for borrowed money which require notice from the trustee or holders of at least 25% of the notes and were subject to a cure period upon receipt of such notice. As of September 30, 2016, and during the first six months of fiscal 2017, we were in compliance with all covenants.

On October 21, 2016, our WF credit agreement was refinanced through the use of proceeds obtained from our new credit facility as further discussed within Note 12 "Subsequent Event" of the Notes to the Condensed Consolidated Financial Statements. As such, a \$60.3 million outstanding balance under our WF credit agreement was classified as long-term in the Condensed Consolidated Balance Sheets as of September 30, 2016.

**NOTE 7: RESTRUCTURING CHARGES***Fiscal 2017 April Restructuring Plan*

In April 2016, we approved a plan ("Fiscal 2017 April Restructuring Plan") to eliminate 29 positions in the U.S. and internationally to reduce investments in various functions of our business to improve operational efficiencies. The costs associated with these actions consist of restructuring charges related to severance and benefits. These actions were completed by the second quarter of fiscal 2017, with the majority having occurred by June 30, 2016. For the first six months of fiscal 2017, we incurred and paid \$1.5 million of restructuring charges under this plan.

**Summary of Restructuring Expense**

The types of restructuring expense for the three and six months ended September 30, 2016 and September 30, 2015 were (in thousands):

|                        | Three Months Ended |                    | Six Months Ended   |                    |
|------------------------|--------------------|--------------------|--------------------|--------------------|
|                        | September 30, 2016 | September 30, 2015 | September 30, 2016 | September 30, 2015 |
| Severance and benefits | \$ (39)            | \$ 155             | \$ 1,450           | \$ 227             |
| Facilities             | 54                 | 232                | 617                | 418                |
| Total                  | \$ 15              | \$ 387             | \$ 2,067           | \$ 645             |

For the first six months of fiscal 2017, restructuring charges were largely due to \$1.5 million of severance and benefits costs incurred as a result of the Fiscal 2017 April Restructuring Plan. We also approved a plan to vacate certain leased space in the U.S. primarily used for administration and research and development in the first quarter of fiscal 2017 and recorded \$0.4 million of restructuring charges related to facilities costs in the first six months of fiscal 2017. The accrued facility restructuring charges, net of estimated sublease amounts, will be paid in accordance with the facility lease terms through November 2018.

For the second quarter of fiscal 2016, restructuring charges were largely due to facilities costs incurred as a result of a change in the estimate of lease payments for our facilities in the U.S. Additionally, for the first six months of fiscal 2016, we incurred restructuring charges related to facilities costs as a result of further consolidating our facilities in the U.S.

**Accrued Restructuring Charges**

The following tables show the activity and the estimated timing of future payouts for accrued restructuring charges (in thousands):

|                                  | Six Months Ended September 30, 2016 |            |          |
|----------------------------------|-------------------------------------|------------|----------|
|                                  | Severance and Benefits              | Facilities | Total    |
| Balance as of March 31, 2016     | \$ 354                              | \$ 2,383   | \$ 2,737 |
| Restructuring costs              | 1,489                               | 480        | 1,969    |
| Adjustment of prior estimates    | (39)                                | 137        | 98       |
| Cash payments                    | (1,664)                             | (664)      | (2,328)  |
| Other non-cash                   | —                                   | 42         | 42       |
| Balance as of September 30, 2016 | \$ 140                              | \$ 2,378   | \$ 2,518 |

|                                     | As of September 30, 2016 |            |          |
|-------------------------------------|--------------------------|------------|----------|
|                                     | Severance and Benefits   | Facilities | Total    |
| Estimated timing of future payouts: |                          |            |          |
| Next twelve months                  | \$ 140                   | \$ 1,644   | \$ 1,784 |
| October 2017 through December 2021  | —                        | 734        | 734      |
|                                     | \$ 140                   | \$ 2,378   | \$ 2,518 |

Accrued facility restructuring charges will be paid in accordance with the respective facility lease terms and amounts above are net of estimated sublease amounts.

**NOTE 8: STOCK INCENTIVE PLANS AND SHARE-BASED COMPENSATION**

***Share-Based Compensation***

The following table summarizes share-based compensation (in thousands):

|  | Three Months Ended |                    | Six Months Ended   |                    |
|--|--------------------|--------------------|--------------------|--------------------|
|  | September 30, 2016 | September 30, 2015 | September 30, 2016 | September 30, 2015 |
| Share-based compensation:                  |                    |                    |                    |                    |
| Cost of revenue                            | \$ 234             | \$ 331             | \$ 514             | \$ 693             |
| Research and development                   | 333                | 492                | 736                | 1,041              |
| Sales and marketing                        | 606                | 839                | 1,218              | 1,709              |
| General and administrative                 | 477                | 785                | 1,180              | 1,657              |
|  | <u>\$ 1,650</u>    | <u>\$ 2,447</u>    | <u>\$ 3,648</u>    | <u>\$ 5,100</u>    |
| Share-based compensation by type of award: |                    |                    |                    |                    |
| Stock options                              | \$ —               | \$ —               | \$ —               | \$ 2               |
| Restricted stock units                     | 1,511              | 2,167              | 3,347              | 4,597              |
| Stock purchase plan                        | 139                | 280                | 301                | 501                |
|  | <u>\$ 1,650</u>    | <u>\$ 2,447</u>    | <u>\$ 3,648</u>    | <u>\$ 5,100</u>    |

***Stock Incentive Plans - Grants and Fair Value***

Stock Options

No stock options were granted during thesecond quarter or first six months of fiscal 2017 or fiscal 2016.

Restricted Stock Units

The fair value of restricted stock units (“RSUs”) granted is the intrinsic value as of the respective grant date since the RSUs are granted at no cost to the employee. The weighted-average grant date fair values of RSUs granted during the second quarter and first six months of fiscal 2017 were \$0.42 and \$0.43, respectively. The weighted-average grant date fair values of RSUs granted during the second quarter and first six months of fiscal 2016 were \$1.63 and \$1.64 per share, respectively.

During the second quarter of fiscal 2017, we granted 3.3 million RSUs with performance conditions (“2017 performance RSUs”), and the total fair value of 2017 performance RSUs at the grant date was \$1.4 million. These RSUs will become eligible for vesting based on Quantum achieving a certain revenue target through the end of fiscal 2017. Share-based compensation expense for 2017 performance RSUs is recognized when it is probable that the performance conditions will be achieved. As of September 30, 2016, \$0.2 million of share-based compensation expense was recognized for these performance RSUs.

Stock Purchase Plan

Under the Stock Purchase Plan, rights to purchase shares are typically granted during the second and fourth quarter of each fiscal year. The value of rights to purchase shares granted in the second quarter and first six months of fiscal 2017 and fiscal 2016, respectively, was estimated at the date of grant using the Black-Scholes option pricing model. The weighted-average grant date fair values and the assumptions used in calculating fair values for the three and six month periods ended September 30, 2016 and September 30, 2015 were as follows:

|  | Three and Six Months Ended |                    |
|--|----------------------------|--------------------|
|  | September 30, 2016         | September 30, 2015 |
| Option life (in years)                           | 0.5                        | 0.5                |
| Risk-free interest rate                          | 0.40%                      | 0.09%              |
| Stock price volatility                           | 81.88%                     | 64.61%             |
| Weighted-average grant date fair value per share | \$ 0.23                    | \$ 0.38            |

**Stock Incentive Plans - Activity**

Stock Options

A summary of activity relating to our stock options follows (options and aggregate intrinsic value in thousands):

|   | Options | Weighted-Average Exercise Price | Weighted-Average Remaining Contractual Term | Aggregate Intrinsic Value |
|---|---------|---------------------------------|---|---------------------------|
| Outstanding as of March 31, 2016                  | 4,131   | \$ 1.52                         |   |                           |
| Forfeited   | (301)   | 1.02                            |   |                           |
| Expired   | (2,355) | 0.99                            |   |                           |
| Outstanding as of September 30, 2016              | 1,475   | \$ 2.49                         | 1.43  | \$ 2,107                  |
| Vested and expected to vest at September 30, 2016 | 1,475   | \$ 2.49                         | 1.43  | \$ 2,107                  |
| Exercisable as of September 30, 2016              | 1,475   | \$ 2.49                         | 1.43  | \$ 2,107                  |

Restricted Stock Units

A summary of activity relating to our restricted stock units follows (shares in thousands):

|                                 | Shares  | Weighted-Average Grant Date Fair Value Per Share |
|---------------------------------|---------|--|
| Nonvested at March 31, 2016     | 11,109  | \$ 1.39  |
| Granted                         | 8,042   | 0.43   |
| Vested                          | (4,825) | 1.38   |
| Forfeited                       | (767)   | 1.44   |
| Nonvested at September 30, 2016 | 13,559  | \$ 0.82  |

**NOTE 9: INCOME TAXES**

Income tax provisions for the second quarter and first six months of fiscal 2017 were less than \$0.1 million and \$0.4 million, respectively. Income tax provisions for the second quarter and first six months of fiscal 2016 were \$0.3 million and \$0.7 million, respectively. Income tax provisions for each of these periods reflect expenses for foreign income taxes and state taxes. We have provided a full valuation allowance against our U.S. net deferred tax assets due to our history of net losses, difficulty in predicting future results and our conclusion that we cannot rely on projections of future taxable income to realize the deferred tax assets. Significant management judgment is required in determining our deferred tax assets and liabilities and valuation allowances for purposes of assessing our ability to realize any future benefit from our net deferred tax assets. We intend to maintain this valuation allowance until sufficient positive evidence exists to support a reversal or decrease in this allowance. Future income tax expense will be reduced to the extent that we have sufficient positive evidence to support a reversal of, or decrease in, our valuation allowance.

**NOTE 10: NET INCOME (LOSS) PER SHARE**

The following is the computation of basic and diluted net income (loss) per share (in thousands, except per share data):

|   | Three Months Ended |                    | Six Months Ended   |                    |
|---|--------------------|--------------------|--------------------|--------------------|
|   | September 30, 2016 | September 30, 2015 | September 30, 2016 | September 30, 2015 |
| Numerator:                                    |                    |                    |                    |                    |
| Net income (loss)                             | \$ 3,826           | \$ (11,227)        | \$ 31              | \$ (21,982)        |
| Denominator:                                  |                    |                    |                    |                    |
| Weighted average shares:                      |                    |                    |                    |                    |
| Basic   | 270,432            | 263,058            | 268,396            | 260,766            |
| Dilutive shares from stock plans              | 1,950              | —                  | 1,197              | —                  |
| Diluted                                       | <u>272,382</u>     | <u>263,058</u>     | <u>269,593</u>     | <u>260,766</u>     |
| Basic and diluted net income (loss) per share | <u>\$ 0.01</u>     | <u>\$ (0.04)</u>   | <u>\$ 0.00</u>     | <u>\$ (0.08)</u>   |

Dilutive and potentially dilutive common shares from the Stock Incentive Plans are determined by applying the treasury stock method to the assumed exercise of outstanding options and the assumed vesting of outstanding restricted stock units. The dilutive impact related to our convertible subordinated notes is determined by applying the if-converted method, which includes adding the related weighted average shares to the denominator and the related interest expense to net income.

The computations of diluted net income (loss) per share for the periods presented exclude the following because the effect would have been anti-dilutive:

- For the second quarter and first six months of fiscal 2017 and fiscal 2016, 42.5 million weighted average shares related to our 4.50% convertible subordinated notes were excluded. For the second quarter of fiscal 2017 and fiscal 2016, \$0.9 million of related interest expense was excluded. For the first six months of fiscal 2017 and fiscal 2016, \$1.8 million of related interest expense was excluded.
- For the second quarter and first six months of fiscal 2016, 19.3 million weighted average shares related to our 3.50% convertible subordinated notes were excluded. For the second quarter and first six months of fiscal 2016, \$0.9 million and \$1.8 million, respectively, of related interest expense was excluded.
- For the second quarter of fiscal 2017 and fiscal 2016, options to purchase 1.6 million and 4.6 million, respectively, weighted average shares were excluded. For the first six months of fiscal 2017 and fiscal 2016, options to purchase 2.8 million and 4.7 million, respectively, weighted average shares were excluded.
- For the second quarter of fiscal 2017 and fiscal 2016, unvested RSUs of 3.5 million and 12.1 million, respectively, weighted average shares were excluded. For the first six months of fiscal 2017 and fiscal 2016, unvested RSUs of 6.6 million and 12.6 million, respectively, weighted average shares were excluded.

**NOTE 11: COMMITMENTS AND CONTINGENCIES**

**Commitments to Purchase Inventory**

We use contract manufacturers for our manufacturing operations. Under these arrangements, the contract manufacturer procures inventory to manufacture products based upon our forecast of customer demand. We have similar arrangements with certain other suppliers. We are responsible for the financial impact on the supplier or contract manufacturer of any reduction or product mix shift in the forecast relative to materials that the third party had already purchased under a prior forecast. Such a variance in forecasted demand could require a cash payment for inventory in excess of current customer demand or for costs of excess or obsolete inventory. As of September 30, 2016 and March 31, 2016, we issued non-cancelable commitments for \$48.0 million and \$42.2 million, respectively, to purchase inventory from our contract manufacturers and suppliers.

## Legal Proceedings

### Crossroads

On February 18, 2014, Crossroads Systems, Inc. (“Crossroads”) filed a patent infringement lawsuit against Quantum in the U.S. District Court for the Western District of Texas, alleging infringement of U.S. patents 6,425,035 and 7,934,041. An amended complaint filed on April 15, 2014 also alleged infringement of U.S. patent 7,051,147. Crossroads asserts that we have incorporated Crossroads' patented technology into our StorNext QX and Q-Series lines of disk array products and into our Scalar libraries. Crossroads seeks unspecified monetary damages and injunctive relief. Crossroads has already dismissed all claims of infringement with respect to the StorNext QX and Q-Series products. In July and September of 2014, we filed for inter partes review of all three asserted Crossroads patents before the Patent Trial and Appeal Board and a review has been initiated for all claims. On June 16, 2015, the U.S. District Court, Western District of Texas stayed the Crossroads trial proceedings pending resolution of the inter partes review proceedings. On January 29, 2016, the Patent Trial and Appeal Board issued decisions on the inter partes reviews for U.S. patents 6,425,035 and 7,051,147, ordering all claims of both patents to be unpatentable. On March 17, 2016, the Patent Trial and Appeal Board issued a decision on the inter partes review for U.S. patent 7,934,041, ordering all claims to be unpatentable. On March 31, 2016, Crossroads filed Notices of Appeal in each of the inter partes review decisions. We believe the probability that this lawsuit will have a material adverse effect on our business, operating results or financial condition is remote.

### Realtime Data

On July 22, 2016, Realtime Data LLC d/b/a IXO (“Realtime Data”) filed a patent infringement lawsuit against Quantum in the U.S. District Court for the Eastern District of Texas, alleging infringement of U.S. patents 7,161,506, 7,378,992, 7,415,530, 8,643,513, 9,054,728 and 9,116,908. Realtime Data asserts that we have incorporated Realtime Data's patented technology into our compression products and services. Realtime Data seeks unspecified monetary damages and other relief that the Court deems appropriate. We believe the probability that this lawsuit will have a material adverse effect on our business, operating results or financial condition is remote.

## NOTE 12: SUBSEQUENT EVENT

On October 21, 2016 (“closing date”), we entered into a secured credit facility (“credit facility”) which consisted of a revolving loan and credit agreement (“revolving loan”) and a term loan and credit agreement (“term loan”). The credit facility allows for maximum borrowings of up to \$170 million, including \$100 million under the revolving loan, \$50 million under the term loan, and \$20 million under a delayed draw term loan (“DDTL”). Borrowings under the DDTL are restricted to only be used to redeem our 4.50% convertible subordinated notes (“4.50% notes”), and available from the closing date through December 31, 2017. The revolving loan and term loan mature on October 21, 2021, subject to conversion or repayment of our 4.50% notes. Borrowings under the term loan bear interest at rates ranging from 7.00% to 8.25%, which is adjusted quarterly, and is dependent on applicable senior net leverage ratio parameters. Borrowings under the revolving loan will typically bear interest at LIBOR plus a margin that fluctuates from 1.50% to 2.50% depending upon availability under the facility.

We borrowed \$76.0 million which included proceeds from the term loan and funds drawn on the revolving loan at closing. These funds were used to pay off the outstanding balance on our Wells Fargo credit agreement and letters of credit in the amount of \$61.4 million, \$10.0 million to fund the restricted reserve requirements for the revolving loan of \$20.0 million and pay transaction fees and other expenses totaling \$4.6 million.

Fees incurred under the credit facility include debt issuance costs and loan commitment fees. Debt issuance costs will be included as an offset to long-term debt in future reporting periods and will be amortized to interest expense over the life of the credit facility using the effective interest method. Loan commitment fees will be recorded as an asset and amortized ratably over the term of the underlying agreement.

The credit facility contains customary covenants, customary events of default and financial covenants, including fixed charge coverage ratio, senior net leverage ratio and total leverage ratio as defined within the credit facility. The credit facility is collateralized by substantially all of our assets.

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

### FORWARD-LOOKING STATEMENT

This report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Forward-looking statements in this report usually contain the words "will," "estimate," "anticipate," "expect," "believe," "project" or similar expressions and variations or negatives of these words. All such forward-looking statements including, but not limited to, (1) our goals, strategy and expectations for future operating performance including increasing market share and shareholder value, continuing to add customers and increasing revenue and delivering on operating profit goals; (2) our expectations and beliefs regarding the storage market and the other markets in which we compete; (3) our belief that our existing cash and capital resources will be sufficient to meet all currently planned expenditures, debt service and sustain our operations for at least the next 12 months; (4) our expectations regarding our ongoing efforts to control our cost structure; (5) our expectations regarding the outcome of any litigation in which we are involved; and (6) our business goals, objectives, key focuses, opportunities and prospects, are inherently uncertain as they are based on management's expectations and assumptions concerning future events, and they are subject to numerous known and unknown risks and uncertainties. Readers are cautioned not to place undue reliance on these forward-looking statements, about which we speak only as of the date hereof. As a result, our actual results may differ materially from the forward-looking statements contained herein. Factors that could cause actual results to differ materially from those described herein include, but are not limited to: (1) the amount of orders received in future periods; (2) our ability to timely ship our products; (3) uncertainty regarding information technology spending and the corresponding uncertainty in the demand for our products and services; (4) our ability to maintain supplier relationships; (5) general economic, political and fiscal conditions in the U.S. and internationally; (6) our ability to successfully introduce new products; (7) our ability to capitalize on market demand; (8) our ability to achieve anticipated gross margin levels and (9) those factors discussed under "Risk Factors" in Part II, Item 1A. Our forward-looking statements are not guarantees of future performance. We disclaim any obligation to update information in any forward-looking statement.

### OVERVIEW

We believe our combination of expertise, innovation and platform independence enables us to solve scale-out storage and data protection challenges more easily, cost-effectively and securely than competitive offerings. We earn our revenue from the sale of products, systems and services through an array of channel partners and our sales force. Our products are sold under both the Quantum brand name and the names of various OEM customers. Our scale-out storage solutions include StorNext® software, StorNext appliances (which include StorNext disk storage, StorNext-related tape storage and Xcellis™), StorNext Pro™ Solutions, Lattus™ extended online storage systems, Q-Cloud® Archive and Q-Cloud Vault. These products are designed to help customers manage large unstructured data sets in an information workflow, encompassing high-performance ingest, real-time collaboration, scalable processing, intelligent protection and high-value monetization. Our data protection solutions include DXi® deduplication backup systems and Scalar® automated tape libraries that optimize backup and recovery, simplify management and lower cost. Our vmPRO™ virtual server backup and disaster recovery offerings protect virtual environments while minimizing the impact on servers and storage. In addition, we offer software for cloud backup and disaster recovery of physical and virtual servers. We have a full range of services and the global scale and scope to support our worldwide customer base.

Our goal for fiscal 2017 is to increase shareholder value by growing our scale-out storage revenue and investing to drive future growth in our scale-out business while also delivering on our operating profit goals. We continue to focus on building our momentum in three main broad categories of scale-out storage: media and entertainment, video surveillance and technical workflows with large unstructured data. Outside of our scale-out storage, our strategy is to continue leveraging our technology leadership, our extensive customer base and our channel and technology partnerships to generate profits and cash from our offerings.

On October 21, 2016 ("closing date"), we entered into a secured credit facility ("credit facility") which consisted of a revolving loan and credit agreement ("revolving loan") and a term loan and credit agreement ("term loan"). The credit facility allows for maximum borrowings of up to \$170 million, including \$100 million under the revolving loan, \$50 million under the term loan and \$20 million under a delayed draw term loan ("DDTL"). Borrowings under the DDTL are restricted to only be used to redeem our 4.50% convertible subordinated notes ("4.50% notes"), and available from the closing date through December 31, 2017.



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We borrowed \$76.0 million which included proceeds from the term loan and funds drawn on the revolving loan at closing. These funds were used to pay off the outstanding balance on our credit agreement with Wells Fargo and letters of credit in the amount of \$61.4 million, \$10.0 million to fund the restricted reserve requirements for the revolving loan of \$20.0 million and pay transaction fees and other expenses totaling \$4.6 million. Refer to Note 12 "Subsequent event" of the Notes to the Condensed Consolidated Financial Statements for further information regarding our refinance details.

**Results**

We had total revenue of \$134.7 million in the second quarter of fiscal 2017, a \$17.7 million increase from the second quarter of fiscal 2016, primarily due to increased product revenue from scale-out storage solutions and devices and media, partially offset by decreased product revenue from tape automation systems. Our branded product and service revenue increased by 20% from the second quarter of fiscal 2016. Our focus on our branded business continues to be reflected in the proportion of non-royalty revenue from branded business, which was 93% in the second quarter of fiscal 2017 compared to 90% in the second quarter of fiscal 2016.

Our gross margin percentage increased by 160 basis points to 41.2% from the second quarter of fiscal 2016 primarily due to a combination of improved leverage on fixed costs from increased product revenue and a decrease in compensation and benefits from lower staffing levels as a result of the cost reduction actions we took in the second half of fiscal 2016 and the first half of fiscal 2017 ("cost reduction actions").

Operating expenses decreased \$5.8 million, or 10%, from the second quarter of fiscal 2016 primarily due to the cost reduction actions described above. The largest spending decrease compared to the second quarter of fiscal 2016 was for compensation and benefits from lower staffing levels. We also had a decrease in legal fees related to the Crossroads lawsuit. For further information, refer to Note 11 "Commitments and Contingencies" of the Notes to the Condensed Consolidated Financial Statements.

Our operating results improved \$15.0 million, from a \$9.6 million loss from operations in the second quarter of fiscal 2016 to \$5.3 million of income from operations in the second quarter of fiscal 2017.

We generated \$2.6 million in cash from operations in the first six months of fiscal 2017 compared to \$2.3 million of cash used in operations in the first six months of fiscal 2016. We ended the quarter with \$32.3 million in cash, cash equivalents and restricted cash.

**RESULTS OF OPERATIONS****Revenue**

| (Dollars in thousands) | Three Months Ended |              |                    |              |           |          |
|------------------------|--------------------|--------------|--------------------|--------------|-----------|----------|
|                        | September 30, 2016 | % of revenue | September 30, 2015 | % of revenue | Change    | % Change |
| Product revenue        | \$ 88,575          | 65.7%        | \$ 71,057          | 60.7%        | \$ 17,518 | 24.7 %   |
| Service revenue        | 36,620             | 27.2%        | 37,247             | 31.8%        | (627)     | (1.7)%   |
| Royalty revenue        | 9,547              | 7.1%         | 8,721              | 7.5%         | 826       | 9.5 %    |
| Total revenue          | \$ 134,742         | 100.0%       | \$ 117,025         | 100.0%       | \$ 17,717 | 15.1 %   |

| (Dollars in thousands) | Six Months Ended   |              |                    |              |           |          |
|------------------------|--------------------|--------------|--------------------|--------------|-----------|----------|
|                        | September 30, 2016 | % of revenue | September 30, 2015 | % of revenue | Change    | % Change |
| Product revenue        | \$ 160,401         | 63.9%        | \$ 133,776         | 58.7%        | \$ 26,625 | 19.9 %   |
| Service revenue        | 72,438             | 28.9%        | 75,186             | 33.0%        | (2,748)   | (3.7)%   |
| Royalty revenue        | 18,187             | 7.2%         | 18,919             | 8.3%         | (732)     | (3.9)%   |
| Total revenue          | \$ 251,026         | 100.0%       | \$ 227,881         | 100.0%       | \$ 23,145 | 10.2 %   |

Total revenue increased in the second quarter of fiscal 2017 compared to the prior year period primarily due to increased product revenue from scale-out storage solutions and devices and media, partially offset by decreased product revenue from tape automation systems. Total revenue increased in the first six months of fiscal 2017 compared to the prior year period primarily due to increased product revenue from scale-out storage solutions, disk backup systems and devices and media, partially offset by a decrease in service revenue.

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We believe the changes in our product and service revenue continue to be driven by the changing storage environment, including increased market demand for scale-out storage solutions and changes in demand for data protection tape products. Revenue from branded scale-out storage solutions and services increased \$16.8 million, or 56%, from the second quarter of fiscal 2016 and \$19.8 million, or 34%, from the first six months of fiscal 2016 due to increased sales of our StorNext appliances. Our scale-out storage solutions include StorNext software, StorNext appliances (which include StorNext disk storage, StorNext-related tape storage and Xcellis), StorNext Pro Solutions, Lattus extended online storage systems, Q-Cloud Archive and Q-Cloud Vault. Revenue from branded data protection products and services increased \$2.4 million, or 4%, from the second quarter of fiscal 2016 primarily due to increased media revenue, which was partially offset by a decrease in tape automation systems revenue. Revenue from branded data protection products and services increased \$5.8 million, or 4%, from the first six months of fiscal 2016 primarily due to increased media and disk backup systems revenue, which was partially offset by a decrease in tape automation systems revenue. Data protection products include our tape automation systems, disk backup systems and devices and media offerings. OEM product and service revenue, which primarily is comprised of data protection tape automation systems, decreased \$2.4 million and \$1.8 million from the second quarter and first six months of fiscal 2016, respectively.

**Product Revenue**

Total product revenue, which includes sales of our hardware and software products sold through both our Quantum branded and OEM channels, increased \$17.5 million and \$26.6 million in the second quarter and first six months of fiscal 2017, respectively, compared to the prior year periods. Revenue from sales of branded products increased 32% and 24% and revenue from sales of products to OEM customers decreased 18% and 3% in the second quarter and first six months of fiscal 2017, respectively, compared to the prior year periods.

| (Dollars in thousands)      | Three Months Ended |              |                    |              |            |          |
|-----------------------------|--------------------|--------------|--------------------|--------------|------------|----------|
|                             | September 30, 2016 | % of revenue | September 30, 2015 | % of revenue | Change     | % Change |
| Tape automation systems     | \$ 23,844          | 17.7%        | \$ 25,414          | 21.7%        | \$ (1,570) | (6.2)%   |
| Disk backup systems         | 10,023             | 7.4%         | 9,874              | 8.4%         | 149        | 1.5 %    |
| Devices and media           | 14,564             | 10.8%        | 11,525             | 9.8%         | 3,039      | 26.4 %   |
| Scale-out storage solutions | 40,144             | 29.8%        | 24,244             | 20.8%        | 15,900     | 65.6 %   |
| Total product revenue       | \$ 88,575          | 65.7%        | \$ 71,057          | 60.7%        | \$ 17,518  | 24.7 %   |

| (Dollars in thousands)      | Six Months Ended   |              |                    |              |           |          |
|-----------------------------|--------------------|--------------|--------------------|--------------|-----------|----------|
|                             | September 30, 2016 | % of revenue | September 30, 2015 | % of revenue | Change    | % Change |
| Tape automation systems     | \$ 45,282          | 18.0%        | \$ 46,036          | 20.2%        | \$ (754)  | (1.6)%   |
| Disk backup systems         | 23,506             | 9.4%         | 18,568             | 8.1%         | 4,938     | 26.6 %   |
| Devices and media           | 27,318             | 10.9%        | 22,429             | 9.8%         | 4,889     | 21.8 %   |
| Scale-out storage solutions | 64,295             | 25.6%        | 46,743             | 20.6%        | 17,552    | 37.6 %   |
| Total product revenue       | \$ 160,401         | 63.9%        | \$ 133,776         | 58.7%        | \$ 26,625 | 19.9 %   |

Revenue from tape automation systems decreased in the second quarter of fiscal 2017 compared to the prior year period primarily due to a decrease of \$1.7 million in OEM tape automation systems largely driven by decreased sales of enterprise systems. Revenue from tape automation systems decreased in the first six months of fiscal 2017 compared to the prior year period primarily due to a decrease of \$0.5 million in OEM tape automation systems driven by decreased sales in enterprise and entry-level systems, partially offset by increased sales of midrange systems.

Revenue from disk backup systems in the second quarter of fiscal 2017 was relatively flat compared to the prior year period. Revenue from disk backup systems increased in the first six months of fiscal 2017 compared to the prior year period primarily due to increased sales of midrange systems, partially offset by decreased sales of entry-level systems.

Product revenue from devices, which includes tape drives and removable hard drives, and non-royalty media sales increased during the second quarter and first six months of fiscal 2017 compared to the prior year periods primarily due to higher sales of branded media.

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Our scale-out storage solutions revenue increased during the second quarter of fiscal 2017 compared to the prior year period primarily due to increased sales of StorNext appliances. Our scale-out storage solutions revenue increased during the first six months of fiscal 2017 compared to the prior year period primarily due to increased sales of StorNext appliances, partially offset by a decrease in revenue from StorNext Pro Solutions and Lattus extended online storage systems.

Service Revenue

Service revenue is primarily comprised of hardware service contracts, which are typically purchased by our customers to extend the warranty, to provide faster service response time, or both. Service revenue decreased during the second quarter of fiscal 2017 due to decreased service revenue from our OEM repair services. Service revenue decreased during the first six months of fiscal 2017 due to decreased service revenue from our data protection products, partially offset by an increase in revenue from branded service contracts for our StorNext appliances.

Royalty Revenue

Royalty revenue increased during the second quarter of fiscal 2017 compared to the prior year period primarily due to increased media royalties from LTO 6 and recently-introduced LTO 7, partially offset by decreased media royalties from LTO generation 1 through 5. In fiscal 2016, we began offering LTO-7 to our tiered storage portfolio. Royalty revenue decreased during the first six months of fiscal 2017 compared to the prior year period primarily due to decreased media royalties from LTO generation 1 through 5, partially offset by increased media royalties from LTO 7.

**Gross Margin**

|                      | Three Months Ended |                |                    |                |                 | Basis point change |
|----------------------|--------------------|----------------|--------------------|----------------|-----------------|--------------------|
|                      | September 30, 2016 | Gross margin % | September 30, 2015 | Gross margin % | Change          |                    |
| Product gross margin | \$ 24,223          | 27.3%          | \$ 17,984          | 25.3%          | \$ 6,239        | 200                |
| Service gross margin | 21,710             | 59.3%          | 19,612             | 52.7%          | 2,098           | 660                |
| Royalty gross margin | 9,547              | 100.0%         | 8,721              | 100.0%         | 826             | —                  |
| Gross margin         | <u>\$ 55,480</u>   | <u>41.2%</u>   | <u>\$ 46,317</u>   | <u>39.6%</u>   | <u>\$ 9,163</u> | <u>160</u>         |

|                      | Six Months Ended   |                |                    |                |                  | Basis point change |
|----------------------|--------------------|----------------|--------------------|----------------|------------------|--------------------|
|                      | September 30, 2016 | Gross margin % | September 30, 2015 | Gross margin % | Change           |                    |
| Product gross margin | \$ 45,917          | 28.6%          | \$ 33,739          | 25.2%          | \$ 12,178        | 340                |
| Service gross margin | 41,747             | 57.6%          | 40,624             | 54.0%          | 1,123            | 360                |
| Royalty gross margin | 18,187             | 100.0%         | 18,919             | 100.0%         | (732)            | —                  |
| Gross margin         | <u>\$ 105,851</u>  | <u>42.2%</u>   | <u>\$ 93,282</u>   | <u>40.9%</u>   | <u>\$ 12,569</u> | <u>130</u>         |

Gross margin percentage increased during the second quarter and first six months of fiscal 2017 compared to the prior year periods primarily due to a combination of improved leverage on fixed costs from increased product revenue and a decrease in compensation and benefits from lower staffing levels as a result of the cost reduction actions described above.

Product Margin

Product gross margin increased 200 basis points and 340 basis points during the second quarter and first six months of fiscal 2017, respectively, compared to the prior year periods primarily due to improved leverage on fixed costs from increased product revenue.

Service Margin

Service gross margin increased 660 basis points and 360 basis points in the second quarter and first six months of fiscal 2017, respectively, compared to the prior year periods. The increase in basis points for both periods was primarily due to the cost reduction actions described above, which resulted in a decrease in compensation and benefits from lower staffing levels and lower external repair expense.

**Royalty Margin**

Royalties typically do not have related cost of sales and have a 100% gross margin percentage. Therefore, royalty gross margin dollars vary directly with royalty revenue.

**Research and Development Expenses**

| (Dollars in thousands)   | Three Months Ended |              |                    |              |            |          |
|--------------------------|--------------------|--------------|--------------------|--------------|------------|----------|
|                          | September 30, 2016 | % of revenue | September 30, 2015 | % of revenue | Change     | % Change |
| Research and development | \$ 11,401          | 8.5%         | \$ 13,370          | 11.4%        | \$ (1,969) | (14.7)%  |

| (Dollars in thousands)   | Six Months Ended   |              |                    |              |            |          |
|--------------------------|--------------------|--------------|--------------------|--------------|------------|----------|
|                          | September 30, 2016 | % of revenue | September 30, 2015 | % of revenue | Change     | % Change |
| Research and development | \$ 22,459          | 8.9%         | \$ 26,693          | 11.7%        | \$ (4,234) | (15.9)%  |

The decrease in research and development expense in thesecond quarter and first six months of fiscal 2017 compared to the prior year periods was primarily due to the cost reduction actions described above. The largest spending reductions in the second quarter and first six months of fiscal 2017 compared to the prior year periods were decreases of \$0.9 million and \$2.7 million, respectively, in compensation and benefits from lower staffing levels, followed by a decrease of \$0.4 million in each period in external service provider expense. Additionally, we had decreases of \$0.2 million and \$0.4 million in depreciation expense due to lower capital expenditures in the second quarter and first six months of fiscal 2017, respectively, compared to the prior year periods.

**Sales and Marketing Expenses**

| (Dollars in thousands) | Three Months Ended |              |                    |              |            |          |
|------------------------|--------------------|--------------|--------------------|--------------|------------|----------|
|                        | September 30, 2016 | % of revenue | September 30, 2015 | % of revenue | Change     | % Change |
| Sales and marketing    | \$ 26,146          | 19.4%        | \$ 28,043          | 24.0%        | \$ (1,897) | (6.8)%   |

| (Dollars in thousands) | Six Months Ended   |              |                    |              |            |          |
|------------------------|--------------------|--------------|--------------------|--------------|------------|----------|
|                        | September 30, 2016 | % of revenue | September 30, 2015 | % of revenue | Change     | % Change |
| Sales and marketing    | \$ 52,513          | 20.9%        | \$ 55,648          | 24.4%        | \$ (3,135) | (5.6)%   |

The decrease in sales and marketing expense in the second quarter and first six months of fiscal 2017 compared to the prior year periods was primarily due to the cost reduction actions described above. The largest spending reductions in the second quarter and first six months of fiscal 2017 compared to the prior year periods were decreases of \$1.4 million and \$2.7 million, respectively, in compensation and benefits from lower staffing levels, followed by decreases of \$0.3 million and \$0.5 million, respectively, in external service provider expense. These decreases were partially offset by increases of \$0.4 million and \$0.6 million in commission expense related to increased branded product revenue in the second quarter and first six months of fiscal 2017, respectively, compared to the prior year periods.

**General and Administrative Expenses**

| (Dollars in thousands)     | Three Months Ended |              |                    |              |            |          |
|----------------------------|--------------------|--------------|--------------------|--------------|------------|----------|
|                            | September 30, 2016 | % of revenue | September 30, 2015 | % of revenue | Change     | % Change |
| General and administrative | \$ 12,572          | 9.3%         | \$ 14,136          | 12.1%        | \$ (1,564) | (11.1)%  |

| (Dollars in thousands)     | Six Months Ended   |              |                    |              |            |          |
|----------------------------|--------------------|--------------|--------------------|--------------|------------|----------|
|                            | September 30, 2016 | % of revenue | September 30, 2015 | % of revenue | Change     | % Change |
| General and administrative | \$ 25,532          | 10.2%        | \$ 28,122          | 12.3%        | \$ (2,590) | (9.2)%   |

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The decrease in general and administrative expense in thesecond quarter and first six months of fiscal 2017 compared to the prior year periods was largely due to decreases of \$0.8 million and \$1.5 million, respectively, in legal fees related to the Crossroads lawsuits as disclosed in Note 11 "Commitments and Contingencies" of the Notes to the Condensed Consolidated Financial Statements and \$0.5 million and \$0.7 million, respectively, in compensation and benefits from lower staffing levels as a result of the cost reduction actions.

**Restructuring Charges**

| (Dollars in thousands) | Three Months Ended |              |                    |              |          |          |
|------------------------|--------------------|--------------|--------------------|--------------|----------|----------|
|                        | September 30, 2016 | % of revenue | September 30, 2015 | % of revenue | Change   | % Change |
| Restructuring charges  | \$ 15              | 0.0%         | \$ 387             | 0.3%         | \$ (372) | (96.1)%  |

| (Dollars in thousands) | Six Months Ended   |              |                    |              |          |          |
|------------------------|--------------------|--------------|--------------------|--------------|----------|----------|
|                        | September 30, 2016 | % of revenue | September 30, 2015 | % of revenue | Change   | % Change |
| Restructuring charges  | \$ 2,067           | 0.8%         | \$ 645             | 0.3%         | \$ 1,422 | 220.5 %  |

For the first six months of fiscal 2017, restructuring charges were largely due to \$1.5 million of severance and benefits costs incurred in the first quarter of fiscal 2017 as a result of our Fiscal 2017 April Restructuring Plan. We also approved a plan to vacate certain leased space in the U.S. primarily used for administration and research and development in the first quarter of fiscal 2017 and recorded \$0.4 million of restructuring charges related to facilities costs in the first six months of fiscal 2017. The accrued facility restructuring charges, net of estimated sublease amounts, will be paid in accordance with the facility lease terms through November 2018.

For the second quarter of fiscal 2016, restructuring charges were largely due to facilities costs incurred as a result of a change in the estimate of lease payments for our facilities in the U.S. Additionally, for the first six months of fiscal 2016, we incurred restructuring charges related to facilities costs as a result of further consolidating our facilities in the U.S.

For further information regarding our restructuring actions, refer to Note 7 "Restructuring Charges" of the Notes to the Condensed Consolidated Financial Statements.

**Other Income**

| (Dollars in thousands) | Three Months Ended |              |                    |              |          |          |
|------------------------|--------------------|--------------|--------------------|--------------|----------|----------|
|                        | September 30, 2016 | % of revenue | September 30, 2015 | % of revenue | Change   | % Change |
| Other income           | \$ 10              | 0.0%         | \$ 714             | 0.6%         | \$ (704) | (98.6)%  |

| (Dollars in thousands) | Six Months Ended   |              |                    |              |          |          |
|------------------------|--------------------|--------------|--------------------|--------------|----------|----------|
|                        | September 30, 2016 | % of revenue | September 30, 2015 | % of revenue | Change   | % Change |
| Other income           | \$ 166             | 0.1%         | \$ 428             | 0.2%         | \$ (262) | (61.2)%  |

The decrease in other income and expense in the second quarter of fiscal 2017 compared to the prior year period was primarily due to a change in net foreign exchange gains and losses. We had \$0.1 million of net foreign exchange losses in the second quarter of fiscal 2017 compared to \$0.4 million of net foreign exchange gains in the second quarter of fiscal 2016.

**Interest Expense**

|                        | Three Months Ended |              |                    |              |          |          |
|------------------------|--------------------|--------------|--------------------|--------------|----------|----------|
|                        | September 30, 2016 | % of revenue | September 30, 2015 | % of revenue | Change   | % Change |
| (Dollars in thousands) |                    |              |                    |              |          |          |
| Interest expense       | \$ 1,485           | 1.1%         | \$ 1,975           | 1.7%         | \$ (490) | (24.8)%  |

|                        | Six Months Ended   |              |                    |              |          |          |
|------------------------|--------------------|--------------|--------------------|--------------|----------|----------|
|                        | September 30, 2016 | % of revenue | September 30, 2015 | % of revenue | Change   | % Change |
| (Dollars in thousands) |                    |              |                    |              |          |          |
| Interest expense       | \$ 2,993           | 1.2%         | \$ 3,898           | 1.7%         | \$ (905) | (23.2)%  |

The decrease in interest expense for the second quarter and first six months of fiscal 2017 compared to the prior year periods was primarily due to the payments of \$83.7 million of aggregate principal amount of 3.50% notes in fiscal 2016, partially offset by an increase in interest expense incurred from the outstanding balance on the line of credit under the WF credit agreement.

**Income Taxes**

|                        | Three Months Ended |                     |                    |                   |          |          |
|------------------------|--------------------|---------------------|--------------------|-------------------|----------|----------|
|                        | September 30, 2016 | % of pre-tax income | September 30, 2015 | % of pre-tax loss | Change   | % Change |
| (Dollars in thousands) |                    |                     |                    |                   |          |          |
| Income tax provision   | \$ 45              | 1.2%                | \$ 347             | (3.2)%            | \$ (302) | (87.0)%  |

|                        | Six Months Ended   |                     |                    |                   |          |          |
|------------------------|--------------------|---------------------|--------------------|-------------------|----------|----------|
|                        | September 30, 2016 | % of pre-tax income | September 30, 2015 | % of pre-tax loss | Change   | % Change |
| (Dollars in thousands) |                    |                     |                    |                   |          |          |
| Income tax provision   | \$ 422             | 93.2%               | \$ 686             | (3.2)%            | \$ (264) | (38.5)%  |

The income tax provision for the second quarter and first six months of both fiscal 2017 and fiscal 2016 reflects expenses for foreign income taxes and state taxes. We have provided a full valuation allowance against our U.S. net deferred tax assets due to our history of net losses, difficulty in predicting future results and our conclusion that we cannot rely on projections of future taxable income to realize the deferred tax assets.

Significant management judgment is required in determining our deferred tax assets and liabilities and valuation allowances for purposes of assessing our ability to realize any future benefit from our net deferred tax assets. We intend to maintain this valuation allowance until sufficient positive evidence exists to support a reversal or decrease in this allowance. Future income tax expense will be reduced to the extent that we have sufficient positive evidence to support a reversal of, or decrease in, our valuation allowance.

**Share-based Compensation**

The following table summarizes share-based compensation expense within our Condensed Consolidated Statements of Operations (dollars in thousands):

|                            | Three Months Ended |                    | Change          | % Change       |
|----------------------------|--------------------|--------------------|-----------------|----------------|
|                            | September 30, 2016 | September 30, 2015 |                 |                |
| Cost of revenue            | \$ 234             | \$ 331             | \$ (97)         | (29.3)%        |
| Research and development   | 333                | 492                | (159)           | (32.3)%        |
| Sales and marketing        | 606                | 839                | (233)           | (27.8)%        |
| General and administrative | 477                | 785                | (308)           | (39.2)%        |
|                            | <u>\$ 1,650</u>    | <u>\$ 2,447</u>    | <u>\$ (797)</u> | <u>(32.6)%</u> |

|                            | Six Months Ended   |                    | Change            | % Change       |
|----------------------------|--------------------|--------------------|-------------------|----------------|
|                            | September 30, 2016 | September 30, 2015 |                   |                |
| Cost of revenue            | \$ 514             | \$ 693             | \$ (179)          | (25.8)%        |
| Research and development   | 736                | 1,041              | (305)             | (29.3)%        |
| Sales and marketing        | 1,218              | 1,709              | (491)             | (28.7)%        |
| General and administrative | 1,180              | 1,657              | (477)             | (28.8)%        |
|                            | <u>\$ 3,648</u>    | <u>\$ 5,100</u>    | <u>\$ (1,452)</u> | <u>(28.5)%</u> |

The decrease in share-based compensation expense in the second quarter and first six months of fiscal 2017 compared to the prior year periods was primarily due to decreases of \$0.7 million and \$1.3 million, respectively, in share-based compensation expense of restricted stock units from a decrease in fair value.

**LIQUIDITY AND CAPITAL RESOURCES****Capital Resources and Financial Condition**

As of September 30, 2016, we had \$29.5 million of cash and cash equivalents, which is comprised of money market funds and cash deposits.

We continue to focus on improving our operating performance, including efforts to increase revenue and to control costs in order to improve margins, return to consistent profitability and generate positive cash flows from operating activities. We believe that our existing cash and capital resources will be sufficient to meet all currently planned expenditures, debt service and contractual obligations and to sustain operations for at least the next 12 months. This belief is dependent upon our ability to achieve gross margin projections and to control operating expenses in order to provide positive cash flow from operating activities. Should we be unable to meet our gross margin or expense objectives, it would likely have a material negative effect on our cash balances and capital resources.

The following is a description of our existing capital resources including outstanding balances, funds available to borrow and primary repayment terms including interest rates.

As of September 30, 2016, we had \$70.0 million of 4.50% convertible subordinated debt outstanding due November 15, 2017 (“4.50% notes”), excluding unamortized debt issuance costs. The 4.50% notes require semi-annual interest payments paid on May 15 and November 15 of each year and have no early call provisions. We paid \$1.6 million of interest on the 4.50% notes in the first six months of fiscal 2017. In addition, we had a \$60.3 million outstanding balance on a line of credit under the WF credit agreement at a weighted average interest rate of 3.04% as of September 30, 2016. We paid \$1.1 million of interest on the WF credit agreement during the first six months of fiscal 2017.

The WF credit agreement contains financial covenants and customary events of default for such securities, including cross-payment default and cross-acceleration to other material indebtedness for borrowed money which require notice from the trustee or holders of at least 25% of the notes and are subject to a cure period upon receipt of such notice. As of September 30, 2016, and during the first six months of fiscal 2017, we were in compliance with all covenants.

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On October 21, 2016 (“closing date”), we entered into a secured credit facility (“credit facility”) which consisted of a revolving loan and credit agreement (“revolving loan”) and a term loan and credit agreement (“term loan”). The credit facility allows for maximum borrowings of up to \$170 million, including \$100 million under the revolving loan, \$50 million under the term loan, and \$20 million under a delayed draw term loan (“DDTL”). Borrowings under the DDTL are restricted to only be used to redeem our 4.50% convertible subordinated notes (“4.50% notes”), and available from the closing date through December 31, 2017. The revolving loan and term loan mature on October 21, 2021, subject to conversion or repayment of our 4.50% notes. Borrowings under the term loan bear interest at rates ranging from 7.00% to 8.25%, which is adjusted quarterly, and is dependent on applicable senior net leverage ratio parameters. Borrowings under the revolving loan will typically bear interest at LIBOR plus a margin that fluctuates from 1.50% to 2.50% depending upon availability under the facility.

We borrowed \$76.0 million which included proceeds from the term loan and funds drawn on the revolving loan at closing. These funds were used to pay off the outstanding balance on our WF credit agreement and letters of credit in the amount of \$61.4 million, \$10.0 million to fund the restricted reserve requirements for the revolving loan of \$20.0 million and pay transaction fees and other expenses totaling \$4.6 million.

Fees incurred under the credit facility include debt issuance costs and loan commitment fees. Debt issuance costs will be included as an offset to long-term debt in future reporting periods and will be amortized to interest expense over the life of the credit facility using the effective interest method. Loan commitment fees will be recorded as an asset and amortized ratably over the term of the underlying agreement.

The credit facility contains customary covenants, customary events of default and financial covenants, including fixed charge coverage ratio, senior net leverage ratio and total leverage ratio as defined within the credit facility. The credit facility is collateralized by substantially all of our assets.

Generation of positive cash flow from operating activities has historically been, and will continue to be, an important source of cash to fund operating needs and meet our current and long-term obligations. We may choose to raise additional capital if strategically advantageous to the company. We can provide no assurance that such additional financing would be available to us on commercially acceptable terms or at all.

We have taken many actions in recent years and are continuing to take such actions to offset the negative impact of economic uncertainty and slow economic growth and their impact on the data protection and scale-out storage markets. We cannot provide assurance that the actions we have taken in the past or any actions we may take in the future will ensure a consistent, sustainable and sufficient level of net income and positive cash flow from operating activities to fund, sustain or grow our business. Certain events that are beyond our control, including prevailing economic, competitive and industry conditions, as well as various legal and other disputes, may prevent us from achieving these financial objectives. Any inability to achieve consistent and sustainable net income and cash flow could result in:

- (i) Restrictions on our ability to manage or fund our existing operations, which could result in a material and adverse effect on our future results of operations and financial condition.
- (ii) Unwillingness on the part of the lenders to:
  - Provide a waiver or amendment for any covenant violations we may experience in future periods, thereby triggering a default under, or termination of, the revolving credit line, or
  - Approve any amendments to the credit facility we may seek to obtain in the future.

Any lack of renewal, waiver or amendment, if needed, could result in the revolving credit line becoming unavailable to us and any amounts outstanding becoming immediately due and payable.

- (iii) Further impairment of our financial flexibility, which could require us to raise additional funding in the capital markets sooner than we otherwise would, and on terms less favorable to us, if available at all.

In addition, the credit facility is collateralized by a pledge of all of our assets. If we were to default and were unable to obtain a waiver for such default, the lenders would have the right to foreclose on our assets in order to satisfy our obligations under these agreements.

Any of the above mentioned items, individually or in combination, could have a material and adverse effect on our results of operations, available cash and cash flows, financial condition, access to capital and liquidity.



**Cash Flows**

Following is a summary of cash flows from operating, investing and financing activities (in thousands):

|   | Six Months Ended   |                    |
|---|--------------------|--------------------|
|   | September 30, 2016 | September 30, 2015 |
| Net income (loss)                                   | \$ 31              | \$ (21,982)        |
| Net cash provided by (used in) operating activities | 2,581              | (2,345)            |
| Net cash used in investing activities               | (1,254)            | (1,721)            |
| Net cash used in financing activities               | \$ (5,674)         | \$ (17,641)        |

**Six Months Ended September 30, 2016**

The \$2.6 million difference between net income and net cash provided by operating activities during the six months ended September 30, 2016 was primarily due to \$9.5 million in non-cash items, the largest of which were share-based compensation, depreciation and service parts lower of cost or market adjustment, and a \$4.9 million increase in accounts payable. These were partially offset by a \$9.2 million decrease in deferred revenue. The increase in accounts payable was primarily due to the timing of payments. The decrease in deferred revenue was largely due to a decrease in deferred service contracts revenue, primarily driven by seasonality. The majority of our service contracts renew in our third and fourth fiscal quarters.

Cash used in investing activities was primarily due to \$1.2 million of property and equipment purchases. Equipment purchases were primarily for engineering equipment for additional IT infrastructure upgrades and equipment for product development.

Cash used in financing activities was primarily due to \$5.5 million of net repayments of borrowings under the WF credit agreement.

**Six Months Ended September 30, 2015**

The \$19.6 million difference between net loss and net cash used in operating activities during the six months ended September 30, 2015 was primarily due to a \$31.9 million decrease in accounts receivable and \$12.4 million in non-cash items, the largest of which were share-based compensation, depreciation and service parts lower of cost or market adjustment, partially offset by a \$16.4 million decrease in deferred revenue and a \$10.9 million decrease in accrued compensation. The decrease in accounts receivable was due to lower revenue in the second quarter of fiscal 2016 compared to the fourth quarter of fiscal 2015 and the timing of cash collections. The decrease in deferred revenue was largely due to a decrease in deferred service contracts revenue, primarily driven by seasonality. The decrease in accrued compensation was primarily due to payment of a profit sharing bonus accrued in fiscal 2015 and a lower commission accrual related to lower branded revenue.

Cash used in investing activities was primarily due to \$1.6 million of property and equipment purchases. Equipment purchases were primarily for engineering equipment for product development, IT servers and firewall upgrades and leasehold improvements in our Colorado Springs facility.

Cash used in financing activities was primarily due to the transfer of \$16.3 million from cash to restricted cash that was required by our WF credit agreement to be held in a Wells Fargo controlled account to repay the 3.50% notes.

**Off Balance Sheet Arrangements****Commitments to Purchase Inventory**

We use contract manufacturers for our manufacturing operations. Under these arrangements, the contract manufacturer procures inventory to manufacture products based upon our forecast of customer demand. We have similar arrangements with certain other suppliers. We are responsible for the financial impact on the supplier or contract manufacturer of any reduction or product mix shift in the forecast relative to materials that the third party had already purchased under a prior forecast. Such a variance in forecasted demand could require a cash payment for inventory in excess of current customer demand or for costs of excess or obsolete inventory. As of September 30, 2016 and March 31, 2016, we issued non-cancelable commitments for \$48.0 million and \$42.2 million, respectively, to purchase inventory from our contract manufacturers and suppliers.

## **CRITICAL ACCOUNTING ESTIMATES AND POLICIES**

Our discussion and analysis of the financial condition and results of operations are based on the accompanying unaudited Condensed Consolidated Financial Statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these statements requires us to make significant estimates and judgments about future uncertainties that affect reported assets, liabilities, revenues and expenses and related disclosures. We base our estimates on historical experience and on various other assumptions believed to be reasonable under the circumstances. In the event that estimates or assumptions prove to be different from actual results, adjustments are made in subsequent periods to reflect more current information. The accounting estimates requiring our most difficult, subjective or complex judgments because these matters are inherently uncertain are unchanged. These critical accounting estimates and policies have been disclosed in our Annual Report on Form 10-K for the year ended March 31, 2016 filed with the Securities and Exchange Commission ("SEC") on June 3, 2016, as amended by Amendment No. 1 to Form 10-K, filed with the SEC on July 27, 2016 (together, the "Form 10-K").

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

### **Interest Rate Risk**

Changes in interest rates affect interest income earned on our cash equivalents, which consisted solely of money market funds during the first six months of fiscal 2017. During the first six months of fiscal 2017, interest rates on these funds were under 1.0%, and we earned negligible amounts in interest income, thus a hypothetical 100 basis point decrease in interest rates would have an insignificant impact on interest income.

In addition, changes in interest rates affect interest expense on our borrowings under the revolving loan and the term loan. Under the revolving loan and the term loan, we had \$50.0 million and \$26.0 million outstanding borrowings, respectively, at an interest rate of 8.50% and 3.03%, respectively, as of October 21, 2016 ("closing date"). A hypothetical 100 basis point would result in an approximate \$0.8 million change in our annual interest expense on our outstanding borrowings as of the closing date.

Our convertible subordinated notes have a fixed interest rate, thus a hypothetical 100 basis point have no impact on our interest expense during the first six months of fiscal 2017.

For a further description of our outstanding debt, see the section captioned "Liquidity and Capital Resources" in Part I, Item 2 "Management's Discussion and Analysis of Financial Condition and Results of Operations."

### **Foreign Exchange Risk**

We conduct business in certain international markets, primarily in the European Union. Because we operate in international markets, we have exposure to different economic climates, political arenas, tax systems and regulations that could affect foreign exchange rates. Our primary exposure to foreign currency risk relates to transacting in foreign currency and recording the activity in U.S. dollars. Changes in exchange rates between the U.S. dollar and these other currencies will result in transaction gains or losses, which we recognize in our Condensed Consolidated Statements of Operations.

To the extent practicable, we minimize our foreign currency exposures by maintaining natural hedges between our assets and liabilities and revenues and expenses denominated in foreign currencies. We have entered into foreign currency option contracts in the past and we may enter into foreign exchange derivative contracts or other economic hedges in the future. Our goal in managing our foreign exchange risk is to reduce to the extent practicable our potential exposure to the changes that exchange rates might have on our earnings. We make a number of estimates in conducting hedging. In the event those estimates differ significantly from actual results, we could experience greater volatility as a result of our hedges.

**ITEM 4. CONTROLS AND PROCEDURES**

- (a) *Evaluation of disclosure controls and procedures.* We evaluated the effectiveness of the design and operation of our disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act as of the end of the period covered by the Quarterly Report on Form 10-Q. This control evaluation was performed under the supervision and with the participation of management, including our CEO and our CFO. Disclosure controls and procedures are designed to ensure that information required to be disclosed in our reports filed under the Exchange Act, such as this Quarterly Report on Form 10-Q, is recorded, processed, summarized and reported within the time periods specified by the SEC. Disclosure controls are also designed to ensure that such information is accumulated and communicated to our management, including the CEO and CFO, as appropriate, to allow timely decisions regarding the required disclosure. Based on the controls evaluation, our CEO and CFO have concluded that as of the end of the period covered by this Quarterly Report on Form 10-Q, our disclosure controls were effective.
- (b) *Changes in internal control over financial reporting.* There was no change in our internal control over financial reporting that occurred during the fiscal quarter covered by this Quarterly Report on Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## PART II—OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

#### Crossroads

On February 18, 2014, Crossroads Systems, Inc. (“Crossroads”) filed a patent infringement lawsuit against Quantum in the U.S. District Court for the Western District of Texas, alleging infringement of U.S. patents 6,425,035 and 7,934,041. An amended complaint filed on April 15, 2014 also alleged infringement of U.S. patent 7,051,147. Crossroads asserts that we have incorporated Crossroads' patented technology into our StorNext QX and Q-Series lines of disk array products and into our Scalar libraries. Crossroads seeks unspecified monetary damages and injunctive relief. Crossroads has already dismissed all claims of infringement with respect to the StorNext QX and Q-Series products. In July and September of 2014, we filed for inter partes review of all three asserted Crossroads patents before the Patent Trial and Appeal Board and a review has been initiated for all claims. On June 16, 2015, the U.S. District Court, Western District of Texas stayed the Crossroads trial proceedings pending resolution of the inter partes review proceedings. On January 29, 2016, the Patent Trial and Appeal Board issued decisions on the inter partes reviews for U.S. patents 6,425,035 and 7,051,147, ordering all claims of both patents to be unpatentable. On March 17, 2016, the Patent Trial and Appeal Board issued a decision on the inter partes review for U.S. patent 7,934,041, ordering all claims to be unpatentable. On March 31, 2016, Crossroads filed Notices of Appeal in each of the inter partes review decisions. We believe the probability that this lawsuit will have a material adverse effect on our business, operating results or financial condition is remote.

#### Realtime Data

On July 22, 2016, Realtime Data LLC d/b/a IXO (“Realtime Data”) filed a patent infringement lawsuit against Quantum in the U.S. District Court for the Eastern District of Texas, alleging infringement of U.S. patents 7,161,506, 7,378,992, 7,415,530, 8,643,513, 9,054,728 and 9,116,908. Realtime Data asserts that we have incorporated Realtime Data's patented technology into our compression products and services. Realtime Data seeks unspecified monetary damages and other relief that the Court deems appropriate. We believe the probability that this lawsuit will have a material adverse effect on our business, operating results or financial condition is remote.

### ITEM 1A. RISK FACTORS

YOU SHOULD CAREFULLY CONSIDER THE RISKS DESCRIBED BELOW, TOGETHER WITH ALL OF THE OTHER INFORMATION INCLUDED IN THIS QUARTERLY REPORT ON FORM 10-Q. THE RISKS AND UNCERTAINTIES DESCRIBED BELOW ARE NOT THE ONLY ONES FACING QUANTUM. ADDITIONAL RISKS AND UNCERTAINTIES NOT PRESENTLY KNOWN TO US OR THAT ARE CURRENTLY DEEMED IMMATERIAL MAY ALSO IMPAIR OUR BUSINESS AND OPERATIONS. THIS QUARTERLY REPORT ON FORM 10-Q CONTAINS “FORWARD-LOOKING” STATEMENTS THAT INVOLVE RISKS AND UNCERTAINTIES. PLEASE SEE “MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS” FOR ADDITIONAL DISCUSSION OF THESE FORWARD-LOOKING STATEMENTS.

**We derive significant revenue from products incorporating tape technology. Our future results of operations depend in part on continued market acceptance and use of products employing tape technology, and decreases in the market have materially and adversely impacted our business, financial condition and results of operations. In addition, if we are unable to compete with new or alternative storage technologies, our business, financial condition and results of operations could be materially and adversely affected.**

We currently derive significant revenue from products that incorporate some form of tape technology, and we expect to continue to derive significant revenue from these products in the next several years. As a result, our future results of operations depend in part on continued market acceptance and use of products employing tape technology. We believe that the storage environment is changing, including reduced demand for tape products. Decreased market acceptance or use of products employing tape technology has materially and adversely impacted our business, financial condition and results of operations and we expect that our revenues from tape products will continue to decline, which could materially and adversely impact our business, financial condition and results of operations in the future.

Disk products as well as various software solutions and alternative technologies continue to gain broader market acceptance. We expect that, over time, many of our tape customers will continue to migrate toward these products and solutions and that revenue from these products and solutions will generate a greater proportion of our revenue. While we are making targeted investments in software, disk backup systems and other alternative technologies, these markets are characterized by rapid innovation, evolving customer demands and strong competition, including competition with several companies who are also significant customers. If we are not successful in our efforts, we may not be able to retain customers or attract new customers and our business, financial condition and results of operations could be materially and adversely affected.

**We have significant indebtedness, which imposes upon us debt service obligations, and our credit facility contains various operating and financial covenants that limit our discretion in the operation of our business. If we are unable to generate sufficient cash flows from operations and overall results of operations to meet these debt obligations or remain in compliance with the covenants, our business, financial condition and results of operations could be materially and adversely affected.**

Our level of indebtedness presents significant risks to our business and investors, both in terms of the constraints that it places on our ability to operate our business and because of the possibility that we may not generate sufficient cash and results of operations to remain in compliance with our covenants and pay the principal and interest on our indebtedness as it becomes due. For further description of our outstanding debt, see the section captioned "Liquidity and Capital Resources" in Part I, Item 2 "Management's Discussion and Analysis of Financial Condition and Results of Operations."

As a result of our indebtedness:

- Our ability to invest in the growth areas of our business is constrained by the financial covenants contained in our credit facility, which require us to maintain a minimum fixed charge coverage ratio and liquidity levels;
- We must dedicate a portion of our cash flow from operations and other capital resources to debt service, thereby reducing our ability to fund working capital, capital expenditures, research and development and other cash requirements;
- Our flexibility in planning for, or reacting to, changes and opportunities in the markets in which we compete may be limited, including our ability to engage in mergers and acquisitions activity, which may place us at a competitive disadvantage;
- We are subject to mandatory field audits and control of cash receipts by the lenders if we do not maintain liquidity above certain thresholds;
- We may be more vulnerable to adverse economic and industry conditions;
- We may be unable to make payments on other indebtedness or obligations;
- We may be unable to incur additional debt or refinance our existing debt on acceptable terms, if at all.

Our credit facility contains restrictive covenants that require us to comply with and maintain certain liquidity levels and a minimum fixed charge coverage ratio, as well as restrict our ability, subject to certain thresholds, to:

- Incur debt;
- Incur liens;
- Make acquisitions of businesses or entities or sell certain assets;
- Make investments, including loans, guarantees and advances;
- Engage in transactions with affiliates;
- Pay dividends or engage in stock repurchases;
- Enter into certain restrictive agreements.

The recent weakness we have seen in the general storage and backup market, and the resulting underperformance of our data protection business, which is the primary driver of our overall cash flow and operating income, has placed increased pressure on our ability to meet our liquidity and fixed charge coverage ratio covenants. We have taken steps and are making changes to our business designed to ensure that our results of operations are sufficient to meet these covenants, but if we are not successful in implementing these changes or our results turn out to be lower than expected, we may violate a covenant, which could result in a default under our credit facility agreements.

Our credit facility is collateralized by a pledge of all of our assets. If we were to default and were unable to obtain a waiver for such a default, the lenders would have a right to foreclose on our assets in order to satisfy our obligations under these agreements. Any such action on the part of the lenders against us could have a materially adverse impact on our business, financial condition and results of operations.

**We rely on indirect sales channels to market and sell our branded products. Therefore, the loss of or deterioration in our relationship with one or more of our resellers or distributors, or our inability to establish new indirect sales channels to drive growth of our branded revenue, especially for disk backup systems and scale-out storage solutions, could negatively affect our results of operations.**

We sell the majority of our branded products to distributors such as Ingram Micro, Inc. and others, value-added resellers ("VARs") and direct marketing resellers ("DMRs") such as CDW Corporation, who in turn sell our products to end users. The success of these sales channels is hard to predict, particularly over time, and we have no purchase commitments or long-term orders from them that assure us of any baseline sales through these channels. Several of our resellers carry competing product lines that they may promote over our products. A reseller might not continue to purchase our products or market them effectively, and each reseller determines the type and amount of our products that it will purchase from us and the pricing of the products that it sells to end user customers. Establishing new indirect sales channels is an important part of our strategy to drive growth of our branded revenue.

As we introduce new products and solutions, our relationship with channel partners that historically have sold other products and solutions that now compete with our new offerings could be adversely impacted. For example, we introduced QXS hybrid storage beginning in fiscal 2016 causing us to more directly compete for primary storage sales with channel partners that sold other primary storage products.

Certain of our contracts with customers contain "most favored nation" pricing provisions mandating that we offer our products to these customers at the lowest price offered to other similarly situated customers. In addition, sales of our enterprise products, and the revenue associated with the on-site service of those products, are somewhat concentrated in specific customers, including government agencies and government-related companies. Any failure of such customers and agencies to continue purchasing products in the same quantities and in the same time frames as they have in the past could affect our results of operations. Our results of operations could be adversely affected by any number of factors including:

- A change in competitive strategy that adversely affects a reseller's willingness or ability to distribute our products;
- The reduction, delay or cancellation of orders or the return of a significant amount of products;
- Our inability to gain traction in developing new indirect sales channels for our branded products;
- The loss of one or more of such distributors or resellers;
- Any financial difficulties of such distributors or resellers that result in their inability to pay amounts owed to us; or
- Changes in requirements or programs that allow our products to be sold by third parties to government customers.

**If our products fail to meet our or our customers' specifications for quality and reliability, we may face liability and reputational or financial harm which may adversely impact our results of operations and our competitive position may suffer.**

Although we place great emphasis on product quality, we may from time to time experience problems with the performance of our products, which could result in one or more of the following:

- Increased costs related to fulfillment of our warranty obligations;
- The reduction, delay or cancellation of orders or the return of a significant amount of products;
- Focused failure analysis causing distraction of the sales, operations and management teams; or
- The loss of reputation in the market and customer goodwill.

These factors could cause our business, financial condition and results of operations to be materially and adversely affected.

In addition, we face potential liability for performance problems of our products because our end users employ our storage technologies for the storage and backup of important data and to satisfy regulatory requirements. We could potentially face claims for product liability from our customers if our products cause property damage or bodily injury. Although we maintain technology errors and omissions liability and general liability insurance, our insurance may not cover potential claims of these types or may not be adequate to indemnify us for all liability that may be imposed. Any imposition of liability or litigation costs that is not covered by insurance or is in excess of our insurance coverage could harm our business.

**A large percentage of our sales are to a few customers, some of which are also competitors, and these customers generally have no minimum or long-term purchase commitments. The loss of, or a significant reduction in demand from, one or more key customers could materially and adversely affect our business, financial condition and results of operations.**

Our sales have been and continue to be concentrated among a few customers because under our business model, we sell to OEMs, distributors, VARs and DMRs to reach end user customers. Furthermore, customers are not obligated to purchase any minimum product volume, and our relationships with customers are terminable at will. Revenue from OEM customers has decreased in recent years. If we experience further declines in revenue from OEM customers or any of our other large customers, our business, financial condition and results of operations could be materially and adversely affected. In addition, certain of our large customers are also our competitors, and such customers could decide to reduce or terminate their purchases of our products for competitive reasons.

Some of our tape and disk products are incorporated into larger storage systems or solutions that are marketed and sold to end users by large OEM customers as well as VARs, channel partners and other distributors. Because of this, we have limited market access to these end users, limiting our ability to reach and influence their purchasing decisions. These market conditions further our reliance on these OEM and other large customers such as distributors and VARs. Thus if they were to significantly reduce, cancel or delay their orders with us, our results of operations could be materially and adversely affected.

A portion of our sales are to various agencies and departments of the U.S. federal government, and funding cuts to federal spending can adversely impact our revenue. The American Taxpayer Relief Act of 2012 implemented automatic spending cuts beginning March 1, 2013. Between October 1 and October 16, 2013, the U.S. government partial shutdown caused reductions, cancellations and delayed orders. Future spending cuts by the U.S. federal government could decrease revenue from sales to the federal government that could materially and adversely affect our results of operations.

**Our results of operations depend on a limited number of products and on new product introductions, which may not be successful, in which case our business, financial condition and results of operations may be materially and adversely affected.**

A limited number of products comprise a significant majority of our sales, and due to rapid technological change in the industry, our future results of operations depend on our ability to develop and successfully introduce new products. To compete effectively, we must continually improve existing products and introduce new ones. We have devoted and expect to continue to devote considerable management and financial resources to these efforts. We cannot provide assurance that:

- We will introduce new products in the time frame we are forecasting;
- We will not experience technical, quality, performance-related or other difficulties that could prevent or delay the introduction and market acceptance of new products;
- Our new products will achieve market acceptance and significant market share, or that the markets for these products will continue or grow as we have anticipated;
- Our new products will be successfully or timely qualified with our customers by meeting customer performance and quality specifications which must occur before customers will place large product orders; or
- We will achieve high volume production of these new products in a timely manner, if at all.

If we are not successful in timely completion of our new product qualifications and then ramping sales to our key customers, our revenue and results of operations could be adversely impacted. In addition, if the quality of our products is not acceptable to our customers, this could result in customer dissatisfaction, lost revenue and increased warranty and repair costs.

**We continue to face risks related to economic uncertainty and slow economic growth.**

Uncertainty about economic conditions poses a risk as businesses may further reduce or postpone spending in response to reduced budgets, tightening of credit markets, negative financial news and declines in income or asset values which could adversely affect our business, financial condition and results of operations. The slow economic growth in recent years along with periods of economic uncertainty in various countries around the world has had a material and adverse impact on our business and our financial condition.

In particular, we have experienced reduced demand for IT products and services overall and more specifically for products with tape technology in the data protection market. We continue to face risks related to economic conditions in Europe, including concerns about sovereign debt, and uncertainty related to the United Kingdom's exit from the European Union and related political matters, which could negatively impact the U.S. and global economies and adversely affect our financial results. In addition, our ability to access capital markets may be restricted, which could have an impact on our ability to react to changing economic and business conditions and could also adversely affect our results of operations and financial condition.

**Competition may intensify in the data protection market as a result of competitors introducing products based on new technology standards and merger and acquisition activity, which could materially and adversely affect our business, financial condition and results of operations.**

Our competitors in the data protection market for disk backup systems and virtual machine solutions are aggressively trying to advance and develop new technologies and products to compete against our technologies and products and we face the risk that customers could choose competitor products over ours. Competition in our markets is characterized by technological innovation and advancement. As a result of competition and new technology standards, our sales or gross margins could decline, which could materially and adversely affect our business, financial condition and results of operations.

Technological developments and competition over the years in the tape automation market and in the storage market in general have resulted in decreased prices for tape automation products and product offerings. Pricing pressure is more pronounced in the tape automation market for entry-level products and less pronounced for enterprise products. Over time, the prices of our products and competitor products have decreased, but such products often incorporate new and/or different features and technologies than in prior years. We face risks that customers could choose competitor products over ours due to these features and technologies or due to pricing differences. We have managed pricing pressure by reducing production costs and/or adding features to increase value to maintain a certain level of gross margin for our tape automation systems. However, certain of our costs are fixed in the short term, so we may not be able to offset price decreases or reductions in demand sufficiently to maintain our profitability. In addition, if competition further intensifies, or if there is additional industry consolidation, our sales and gross margins for tape automation systems could decline, which could materially and adversely affect our business, financial condition and results of operations.

Industry consolidation and competing technologies with device products, which include tape drives and removable hard drives, have resulted in decreased prices and increasingly commoditized device products. We have exited certain portions of the device market and have anticipated decreased sales of devices. We face risk of reduced shipments of our devices beyond our plans and could have reduced margins on these products, which could adversely impact our business, financial condition and results of operations.

Additionally, the competitive landscape could change due to merger and acquisition activity in the data protection market. Such transactions may impact us in a number of ways. For instance, they could result in:

- Competitors consolidating, having greater resources and becoming more competitive with us;
- Companies that we have not historically competed against entering into one or more of our primary markets and increasing competition in such market(s);
- Customers that are also competitors becoming more competitive with us and/or reducing their purchase of our products; and
- Competitors acquiring our current suppliers or business partners and negatively impacting our business model.

These transactions also create uncertainty and disruption in the market because whether a pending transaction will be completed, the timing of such a transaction and its degree of impact are often unknown. Given these factors and others, such merger and acquisition activity may materially and adversely impact our business, financial condition and results of operations.

**Competition may intensify in the scale-out storage market as a result of competitors introducing products based on new technology standards and market consolidation, which could materially and adversely affect our business, financial condition and results of operations.**

Competition in the scale-out storage market is characterized by technological innovation and advancement, including performance and scale features, and our competitors are aggressively trying to advance and develop new technologies and solutions. If we are unable to compete effectively in these markets and develop solutions that have features and technologies that our customers desire, including new technology standards, our sales from software solutions and appliances could decline, which could materially and adversely affect our business, financial condition and results of operations.

Additionally, the competitive landscape could change due to mergers and acquisitions among our competitors, customers and partners. Transactions such as these may impact us in a number of ways. For instance, they could result in:

- Competitors consolidating, having greater resources and becoming more competitive with us;
- Companies that we have not historically competed against entering into one or more of our primary markets and increasing competition in such market(s);
- Customers that are also competitors becoming more competitive with us and/or reducing their purchase of our products; and
- Competitors acquiring our current suppliers or business partners and negatively impacting our business model.



These transactions also create uncertainty and disruption in the market, because whether a pending transaction will be completed, the timing of such a transaction and its degree of impact are often unknown. Given these factors and others, such merger and acquisition activity may materially and adversely impact our business, financial condition and results of operations.

**A significant decline in our media royalty or branded software revenues could materially and adversely affect our business, financial condition and results of operations.**

Our media royalties or branded software revenues are relatively profitable and can significantly impact total company profitability. We receive media royalty revenue based on tape media cartridges sold by various tape media manufacturers and resellers. Under our license agreements with these companies, each of the licensees determines the pricing and number of units of tape media cartridges that it sells. Our media royalty revenue varies depending on the level of sales of the various media cartridge offerings sold by the licensees and other factors, including:

- The size of the installed base of devices and similar products that use tape media cartridges;
- The performance of our strategic licensing partners, which sell tape media cartridges;
- The relative growth in units of newer device products, since the associated media cartridges for newer products typically sell at higher prices than the media cartridges associated with older products;
- The media consumption habits and rates of end users;
- The pattern of device retirements;
- and
- The level of channel inventories.

Our media royalties depend on royalty rates and the quantity of media consumed in the market. We do not control licensee sales of these tape media cartridges. Reduced royalty rates, or a reduced installed device base using tape media cartridges, would result in further reductions in our media royalty revenue and could reduce gross margins. This could materially and adversely affect our business, financial condition and results of operations.

Our branded software revenues are also dependent on many factors, including the success of competitive offerings, our ability to execute on our product roadmap and our effectiveness at marketing and selling our branded software solutions directly or through our channel partners. Disruptions to any one of these factors could reduce our branded software revenues, which could adversely affect our business, financial condition and results of operations.

**Some of our products contain licensed, third-party technology that provides important product functionality and features. The loss or inability to obtain any such license could have a material adverse effect on our business.**

Certain of our products contain technology licensed from third parties that provides important product functionality and features. We have contractual protections within our license agreements to help mitigate against the risks of incorporating this third-party technology into our products. However, there remains a risk that we may not have continued access to this technology, for instance, if the licensing company ceased to exist, either from bankruptcy, dissolution or purchase by a competitor. In some cases, we may seek to enforce our contractual protections via litigation against the licensing company itself, which may cause us to incur significant legal or other costs and may not be resolved in our favor. Other legal actions, such as intellectual property actions, brought against the licensing company could also impact our future access to the technology. We also have limited control of the technology roadmap and cannot ensure that the licensing company will advance the roadmap of the licensed technology in the manner best for Quantum. Any of these actions could negatively impact our technology licensing, thereby reducing the functionality and/or features of our products, and adversely affect our business, financial condition and results of operations. We also face the risk of not being able to quickly implement a replacement technology or otherwise mitigate the risks associated with not having access to this licensed technology, which may adversely affect our business, financial condition and results of operations.

**We have taken considerable steps towards reducing our cost structure and may take further cost reduction actions. The steps we have taken and may take in the future may not reduce our cost structure to a level appropriate in relation to our future sales and therefore, these anticipated cost reductions may be insufficient to result in consistent profitability.**

In the last several years, we have recorded significant restructuring charges and made cash payments in order to reduce our cost of sales and operating expenses to respond to adverse economic and industry conditions, from strategic management decisions and to rationalize our operations following acquisitions. In the third quarter of fiscal 2016 and the first quarter of fiscal 2017, we implemented restructuring plans, which we refer to as the Fiscal 2016 Restructuring Plan and the Fiscal 2017 April Restructuring Plan, respectively to eliminate certain positions in the U.S. and internationally. These restructuring plans may result in decreases to our revenues or adversely affect our ability to grow our business in the future. Workforce reductions may also adversely affect employee morale and our ability to retain our employees. We may take future steps to further reduce our operating costs, including future cost reduction steps or restructurings in response to strategic decisions, adverse changes in our business or industry or future acquisitions. We may be unable to reduce our cost of sales and operating expenses at a rate and to a level appropriate in relation to our future sales, which may adversely affect our business, financial condition and results of operations.

In addition, our ability to achieve the anticipated cost savings and other benefits from these restructuring plans within the expected time frame is subject to many estimates and assumptions. These estimates and assumptions are subject to significant economic, competitive and other uncertainties, some of which are beyond our control. If these estimates and assumptions are incorrect, if we experience delays, or if other unforeseen events occur, our business, financial condition and results of operations could be adversely affected.

**If we are unable to attract and retain skilled employees, our business could be adversely impacted.**

We may be subject to increased turnover in our employee base or the inability to fill open headcount requisitions due to competition, concerns about our operational performance or other factors. In addition, we may need to rely on the performance of employees whose skill sets are not sufficiently developed to fulfill their expected job responsibilities. Either of these situations could impair or delay our ability to realize operational and strategic objectives and cause increased expenses and lost sales opportunities.

Additionally, over the last several years, we made certain changes in our strategic direction focusing on key technology segments. As part of this change in focus, we reduced costs of revenue and other operating expenses. Executing on this new strategic direction as well as the ongoing efficiency initiatives across the company, such as the Fiscal 2016 Restructuring Plan and the Fiscal 2017 April Restructuring Plan could adversely affect our ability to retain and hire key personnel and may result in reduced productivity by our employees. Further, our stock price has declined in recent years, reducing the retentive value of our equity compensation. If employees and potential employees do not view our equity compensation as valuable, we may have difficulty retaining or hiring key personnel.

The loss of the services of any of our key employees, the inability to attract or retain qualified talent in the future, or delays in hiring required talent, particularly sales and engineering talent, could delay the development and introduction of our products or services and/or negatively affect our ability to sell our products or services.

**Third party intellectual property infringement claims could result in substantial liability and significant costs, and, as a result, our business, financial condition and result of operations may be materially and adversely affected.**

From time to time, third parties allege our infringement of and need for a license under their patented or other proprietary technology, such as our current litigation with Crossroads Systems, Inc. and Realtime Data LLC d/b/a IXO described in Part II, Item 1 "Legal Proceedings." While we currently believe the amount of ultimate liability, if any, with respect to any such actions will not materially affect our financial condition, results of operations or liquidity, the ultimate outcome of any license discussion or litigation is uncertain. Adverse resolution of any third party infringement claim could subject us to substantial liabilities and require us to refrain from manufacturing and selling certain products. In addition, the costs incurred in intellectual property litigation can be substantial, regardless of the outcome. As a result, our business, financial condition and results of operations could be materially and adversely affected.

In addition, certain products or technologies acquired or developed by us may include “open source” software. Open source software is typically licensed for use at no initial charge. Certain open source software licenses, however, require users of the open source software to license to others any software that is based on, incorporates or interacts with, the open source software under the terms of the open source license. Although we endeavor to comply fully with such requirements, third parties could claim that we are required to license larger portions of our software than we believe we are required to license under open source software licenses. If such claims were successful, they could adversely impact our competitive position and financial results by providing our competitors with access to sensitive information that may help them develop competitive products. In addition, our use of open source software may harm our business and subject us to intellectual property claims, litigation or proceedings in the future because:

- Open source license terms may be ambiguous and may subject us to unanticipated obligations regarding our products, technologies and intellectual property;
- Open source software generally cannot be protected under trade secret law; and
- It may be difficult for us to accurately determine the origin of the open source code and whether the open source software infringes, misappropriates or violates third party intellectual property or other rights.

**As a result of our global manufacturing and sales operations, we are subject to a variety of risks related to our business outside of the U.S., any of which could, individually or in the aggregate, have a material adverse effect on our business.**

A significant portion of our manufacturing and sales operations and supply chain occurs in countries other than the U.S. We also have sales outside the U.S. We utilize contract manufacturers to produce and fulfill orders for our products and have suppliers for various components, several of which have operations located in foreign countries including China, Hungary, Japan, Malaysia, Singapore, Mexico, the Philippines and Thailand. Because of these operations, we are subject to a number of risks including:

- Reduced or limited protection of our intellectual property;
- Compliance with multiple and potentially conflicting regulatory requirements and practices;
- Commercial laws that favor local businesses;
- Exposure to economic fluctuations including inflationary risk and continuing sovereign debt risk;
- Shortages in component parts and raw materials;
- Import, export and trade regulation changes that could erode our profit margins or restrict our ability to transport our products;
- The burden and cost of complying with foreign and U.S. laws governing corporate conduct outside the U.S. including the Foreign Corrupt Practices Act, the United Kingdom Bribery Act and other similar regulations;
- Adverse movement of foreign currencies against the U.S. dollar (the currency in which our results are reported) and uncertain global economic conditions generally;
- Inflexible employee contracts and employment laws that may make it difficult to terminate or change the compensation structure for employees in some foreign countries in the event of business downturns;
- Recruiting employees in highly competitive markets and wage inflation in certain markets;
- Potential restrictions on the transfer of funds between countries;
- Political, military, social and infrastructure risks, especially in emerging or developing economies;
- Import and export duties and value-added taxes;
- Natural disasters, including earthquakes, flooding, typhoons and tsunamis; and
- Cultural differences that affect the way we do business.

Any or all of these risks could have a material adverse effect on our business.

**Our quarterly results of operations have fluctuated significantly, and past quarterly results of operations should not be used to predict future performance.**

Our quarterly results of operations have fluctuated significantly in the past and could fluctuate significantly in the future. As a result, our quarterly results of operations should not be used to predict future performance. Quarterly results of operations could be materially and adversely affected by a number of factors, including, but not limited to:

- Fluctuations in IT spending as a result of economic conditions or fluctuations in U.S. federal government spending;
- Failure by our contract manufacturers to complete shipments in the last month of a quarter during which a substantial portion of our products are typically shipped;
- Customers canceling, reducing, deferring or rescheduling significant orders as a result of excess inventory levels, weak economic conditions or other factors;
- Seasonality, including customer fiscal year-ends and budget availability impacting customer demand for our products;
- Declines in large orders (defined as orders greater than \$200,000);
- Declines in royalty or software revenues;
- Product development and ramp cycles and product performance or quality issues of ours or our competitors;
- Poor execution of and performance against expected sales and marketing plans and strategies;
- Reduced demand from our OEM or distribution, VAR, DMR and other large customers;
- Increased competition which may, among other things, increase pricing pressure or reduce sales;
- Failure to meet the expectations of investors or analysts;
- Restructuring actions or unexpected costs; and
- Foreign exchange fluctuations.

If we fail to meet our projected quarterly results, our business, financial condition and results of operations may be materially and adversely affected.

**If we fail to protect our intellectual property or if others use our proprietary technology without authorization, our competitive position may suffer.**

Our future success and ability to compete depends in part on our proprietary technology. We rely on a combination of copyright, patent, trademark and trade secrets laws and nondisclosure agreements to establish and protect our proprietary technology. However, we cannot provide assurance that patents will be issued with respect to pending or future patent applications that we have filed or plan to file or that our patents will be upheld as valid or will prevent the development of competitive products or that any actions we have taken will adequately protect our intellectual property rights. We generally enter into confidentiality agreements with our employees, consultants, customers, potential customers, contract manufacturers and others as required, in which we strictly limit access to, and distribution of, our software and further limit the disclosure and use of our proprietary information.

Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy or otherwise obtain or use our products or technology. Enforcing our intellectual property rights can sometimes only be accomplished through the use of litigation. Our competitors may also independently develop technologies that are substantially equivalent or superior to our technology. In addition, the laws of some foreign countries do not protect our proprietary rights to the same extent as the laws of the U.S.

**Because we may order components from suppliers in advance of receipt of customer orders for our products that include these components, we could face a material inventory risk if we fail to accurately forecast demand for our products or manage production, which could have a material and adverse effect on our results of operations and cash flows.**

Although we use third parties to manufacture our products, in some cases we may retain the responsibility to purchase component inventory to support third party manufacturing activities, which presents a number of risks that could materially and adversely affect our financial condition. For instance, as part of our component planning, we may place orders with or pay certain suppliers for components in advance of receipt of customer orders. We may occasionally enter into negotiated orders with vendors early in the manufacturing process of our products to ensure that we have sufficient components for our products to meet anticipated customer demand. Because the design and manufacturing process for these components can be complicated, it is possible that we could experience a design or manufacturing flaw that could delay or even prevent the production of the components for which we previously committed to pay. We also face the risk of ordering too many components, or conversely, not enough components, since supply orders are generally based on forecasts of customer orders rather than actual customer orders. In addition, in some cases, we may make non-cancelable order commitments to our suppliers for work-in-progress, supplier's finished goods, custom sub-assemblies, discontinued (end-of-life) components and Quantum-unique raw materials that are necessary to meet our lead times for finished goods. If we cannot change or be released from supply orders, we could incur costs from the purchase of unusable components, either due to a delay in the production of the components or other supplies or as a result of inaccurately predicting supply orders in advance of customer orders. These same risks exist with our third party contract manufacturing partners. Our business and results of operations could be materially and adversely affected if we incur increased costs or are unable to fulfill customer orders.

**Our manufacturing, component production and service repair are outsourced to third party contract manufacturers, component suppliers and service providers. If we cannot obtain products, parts and services from these third parties in a cost effective and timely manner that meets our customers' expectations, this could materially and adversely impact our business, financial condition and results of operations.**

Many aspects of our supply chain and operational results are dependent on the performance of third party business partners. We increased the use of third party contract manufacturers, service providers and/or product integrators in fiscal 2014 in connection with our transition to an outsourced manufacturing model. We face a number of risks as a result of these relationships, including, among others:

- *Sole source of product supply*  
In many cases, our business partner may be the sole source of supply for the products or parts they manufacture, or the services they provide, for us. Because we are relying on one supplier, we are at greater risk of experiencing shortages, reduced production capacity or other delays in customer deliveries that could result in customer dissatisfaction, lost sales and increased expenses, each of which could materially damage customer relationships and result in lost revenue.
- *Cost and purchase commitments*  
We may not be able to control the costs for the products our business partners manufacture for us or the services they provide to us. They procure inventory to build our products based upon a forecast of customer demand that we provide. We could be responsible for the financial impact on the contract manufacturer, supplier or service provider of any reduction or product mix shift in the forecast relative to materials that they had already purchased under a prior forecast. Such a variance in forecasted demand could require us to pay them for finished goods in excess of current customer demand or for excess or obsolete inventory and generally incur higher costs. As a result, we could experience reduced gross margins and operating losses based on these purchase commitments. With respect to service providers, although we have contracts for most of our third party repair service vendors, the contract period may not be the same as the underlying service contract with our customer. In such cases, we face risks that the third party service provider may increase the cost of providing services over subsequent periods contracted with our customer.
- *Financial condition and stability*  
Our third party business partners may suffer adverse financial or operational results or may be negatively impacted by global and local economic conditions. Therefore, we may face interruptions in the supply of product components or service as a result of financial or other volatility affecting our supply chain. We could suffer production downtime or increased costs to procure alternate products or services as a result of the possible inadequate financial condition of one or more of our business partners.

- *Quality and supplier conduct*

We have limited control over the quality of products and components produced and services provided by our supply chain and third party contract manufacturing and service business partners. Therefore, the quality of the products, parts or services may not be acceptable to our customers and could result in customer dissatisfaction, lost revenue and increased warranty costs. In addition, we have limited control over the manner in which our business partners conduct their business. Sub-tier suppliers selected by the primary third party could have process control issues or could select components with latent defects that manifest over a longer period of time. We may face negative consequences or publicity as a result of a third party's failure to comply with applicable compliance, trade, environmental or employment regulations.

Any or all of these risks could have a material adverse effect on our business. In the past we have successfully transitioned products or component supply from one supplier or manufacturing location to another without significant financial or operational impact, but there is no guarantee of our continued ability to do so.

**If we do not successfully manage the changes that we have made and may continue to make to our infrastructure and management, our business could be disrupted, and that could adversely impact our results of operations and financial condition.**

Managing change is an important focus for us. In recent years, we have implemented several significant initiatives involving our sales and marketing, engineering and operations organizations, aimed at increasing our efficiency and better aligning these groups with our corporate strategy. In addition, we have reduced headcount to streamline and consolidate our supporting functions as appropriate in response to market or competitive conditions and following past acquisitions and have increased our reliance on certain third party business relationships. If we are unable to successfully manage the changes that we implement and detect and address issues as they arise, our business could be disrupted and our results of operations and financial condition could be materially and adversely impacted.

**Because we rely heavily on distributors and other resellers to market and sell our products, if one or more distributors were to experience a significant deterioration in its financial condition or its relationship with us, this could disrupt the distribution of our products and reduce our revenue, which could materially and adversely affect our business, financial condition and results of operations.**

We heavily utilize distributors and VARs to perform the functions necessary to market and sell our products in certain product and geographic segments. To fulfill this role, the distributor must maintain an acceptable level of financial stability, creditworthiness and the ability to successfully manage business relationships with the customers it serves directly. Under our distributor agreements with these companies, each of the distributors determines the type and amount of our products that it will purchase from us and the pricing of the products that it sells to its customers. If the distributor is unable to perform in an acceptable manner, we may be required to reduce the amount of sales of our product to the distributor or terminate the relationship. We may also incur financial losses for product returns from distributors or for the failure or refusal of distributors to pay obligations owed to us. Either scenario could result in fewer of our products being available to the affected market segments, reduced levels of customer satisfaction and/or increased expenses, which could in turn have a material and adverse impact on our business, results of operations and financial condition.

**Our stock price has been volatile and such volatility could increase based on the trading activity of our institutional investors. In addition, there are other factors and events that could affect the trading prices of our common stock.**

A small number of institutional investors have owned a significant portion of our common stock at various times in recent years. If any or all of these investors were to decide to purchase significant additional shares or to sell significant amounts or all of the common shares they currently own, or if there is a perception that those sales may occur, that may cause our stock price to be more volatile. For example, there have been instances in the past where a shareholder with a significant equity position began to sell shares, putting downward pressure on our stock price for the duration of their selling activity. In these situations, selling pressure outweighed buying demand and our stock price declined. This situation has occurred due to our stock price falling below institutional investors' price thresholds and our volatility increasing beyond investors' volatility parameters, causing even greater selling pressure.

Trading prices of our common stock may fluctuate in response to a number of events and factors, such as:

- General economic conditions;
- Changes in interest rates;
- Fluctuations in the stock market in general and market prices for technology companies in particular;
- Quarterly variations in our results of operations;
- Failure to meet our expectations or the expectations of securities analysts and investors;
- New products, services, innovations and strategic developments by our competitors or us, or business combinations and investments by our competitors or us;
- Changes in financial estimates by us or securities analysts and recommendations by securities analysts;
- Changes in our capital structure, including issuance of additional debt or equity to the public; and
- Strategic acquisitions.

Any of these events and factors may cause our stock price to rise or fall and may adversely affect our business and financing opportunities.

**Our operation and design processes are subject to safety and environmental regulations which could lead to increased costs, or otherwise adversely affect our business, financial condition and results of operations.**

We are subject to a variety of laws and regulations relating to, among other things, the use, storage, discharge and disposal of materials and substances used in our facilities as well as the safety of our employees and the public. Current regulations in the U.S. and various international jurisdictions restrict the use of certain potentially hazardous materials used in electronic products and components (including lead and some flame retardants), impose a “take back” obligation on manufacturers for the financing of the collection, recovery and disposal of electrical and electronic equipment and require extensive investigation into and disclosure regarding certain minerals used in our supply chain. We have implemented procedures and will likely continue to introduce new processes to comply with current and future safety and environmental legislation. However, measures taken now or in the future to comply with such legislation may adversely affect our costs or product sales by requiring us to acquire costly equipment or materials, redesign processes or to incur other significant expenses in adapting our waste disposal and emission management processes. Furthermore, safety or environmental claims or our failure to comply with present or future regulations could result in the assessment of damages or imposition of fines against us or the suspension of affected operations, which could have an adverse effect on our business, financial condition and results of operations.

**We are subject to many laws and regulations, and violation of or changes in those requirements could materially and adversely affect our business.**

We are subject to numerous U.S. and international laws and requirements regarding corporate conduct, fair competition, corruption prevention and import and export practices, including laws applicable to U.S. government contractors. In addition, the SEC has adopted disclosure rules related to the supply of certain minerals originating from the conflict zones of the Democratic Republic of Congo or adjoining countries, and we have incurred costs to comply with such regulations and may realize other costs relating to the sourcing and availability of minerals used in our products. While we maintain a rigorous corporate ethics and compliance program, we may be subject to increased regulatory scrutiny, significant monetary fines or penalties, suspension of business opportunities or loss of jurisdictional operating rights as a result of any failure to comply with those requirements. If we were to be subject to a compliance investigation, we may incur increased personnel and legal costs. Our supply and distribution models may be reliant upon the actions of our third party business partners and we may also be exposed to potential liability resulting from their violation of these or other compliance requirements. Further, our U.S. and international business models are based on currently applicable regulatory requirements and exceptions. Changes in those requirements or exceptions could necessitate changes to our business model. Any of these consequences could materially and adversely impact our business and results of operations.

**A cybersecurity breach could adversely affect our ability to conduct our business, harm our reputation, expose us to significant liability or otherwise damage our financial results.**

A cybersecurity breach could negatively affect our reputation as a trusted provider of scale-out storage, archive and data protection products by adversely affecting the market’s perception of the security or reliability of our products and services. Many of our customers and partners store sensitive data on our products, and a cybersecurity breach related to our products could harm our reputation and potentially expose us to significant liability.

We also maintain sensitive data related to our employees, strategic partners and customers, including intellectual property, proprietary business information and personally identifiable information on our own systems. We employ sophisticated security measures; however, we may face threats across our infrastructure including unauthorized access, security breaches and other system disruptions.

It is critical to our business that our employees', strategic partners' and customers' sensitive information remains secure and that our customers perceive that this information is secure. A cybersecurity breach could result in unauthorized access to, loss of, or unauthorized disclosure of such information. A cybersecurity breach could expose us to litigation, indemnity obligations, government investigations and other possible liabilities. Additionally, a cyber-attack, whether actual or perceived, could result in negative publicity which could harm our reputation and reduce our customers' confidence in the effectiveness of our solutions, which could materially and adversely affect our business and results of operations. A breach of our security systems could also expose us to increased costs including remediation costs, disruption of operations or increased cybersecurity protection costs that may have a material adverse effect on our business.

**Our actual or perceived failure to adequately protect personal data could adversely affect our business, financial condition and results of operations.**

A variety of state, national, foreign, and international laws and regulations apply to the collection, use, retention, protection, disclosure, transfer and other processing of personal data. These privacy- and data protection-related laws and regulations are evolving, with new or modified laws and regulations proposed and implemented frequently and existing laws and regulations subject to new or different interpretations. Compliance with these laws and regulations can be costly and can delay or impede the development of new products.

For example, we historically relied upon adherence to the U.S. Department of Commerce's Safe Harbor Privacy Principles and compliance with the U.S.-EU Safe Harbor Framework agreed to by the U.S. Department of Commerce and the EU. The U.S.-EU Safe Harbor Framework, which established means for legitimizing the transfer of personal data by U.S. companies from the European Economic Area, or EEA, to the U.S., was invalidated in October 2015 by a decision of the European Court of Justice, or the ECJ. In light of the ECJ's decision, we have made certain changes to our personal data handling in an effort to cause our transfer and receipt of EEA residents' personal data to be legitimized under applicable European law. In February 2016, U.S. and EU authorities reached agreement on new means for legitimizing personal data transfers from the EU to the U.S., the EU-U.S. Privacy Shield. We have self-certified our compliance with its requirements. Additionally, the European Commission has adopted a general data protection regulation that, when effective in May 2018, will supersede current EU data protection legislation, impose more stringent EU data protection requirements and provide for greater penalties for noncompliance. Our actual or alleged failure to comply with applicable laws and regulations, or to protect personal data, could result in enforcement actions and significant penalties against us, which could result in negative publicity, increase our operating costs, subject us to claims or other remedies and have a material adverse effect on our business, financial condition, and results of operations.

**We must maintain appropriate levels of service parts inventories. If we do not have sufficient service parts inventories, we may experience increased levels of customer dissatisfaction. If we hold excessive service parts inventories, we may incur financial losses.**

We maintain levels of service parts inventories to satisfy future warranty obligations and also to earn service revenue by providing enhanced and extended warranty and repair service during and beyond the warranty period. We estimate the required amount of service parts inventories based on historical usage and forecasts of future warranty and extended warranty requirements, including estimates of failure rates and costs to repair, and out of warranty revenue. Given the significant levels of judgment inherently involved in the process, we cannot provide assurance that we will be able to maintain appropriate levels of service parts inventories to satisfy customer needs and to avoid financial losses from excess service parts inventories. If we are unable to maintain appropriate levels of service parts inventories, our business, financial condition and results of operations may be materially and adversely impacted.

**From time to time we have made acquisitions. The failure to successfully integrate future acquisitions could harm our business, financial condition and results of operations.**

As a part of our business strategy, we have in the past and may make acquisitions in the future, subject to certain debt covenants. We may also make significant investments in complementary companies, products or technologies. If we fail to successfully integrate such acquisitions or significant investments, it could harm our business, financial condition and results of operations. Risks that we may face in our efforts to integrate any recent or future acquisitions include, among others:

- Failure to realize anticipated synergies from the acquisition;
- Difficulties in assimilating and retaining employees;
- Potential incompatibility of business cultures or resistance to change;
- Coordinating geographically separate organizations;
- Diversion of management's attention from ongoing business concerns;
- Coordinating infrastructure operations in a rapid and efficient manner;
- The potential inability to maximize our financial and strategic position through the successful incorporation of acquired technology and rights into our products and services;



- Failure of acquired technology or products to provide anticipated revenue or margin contribution;
- Insufficient revenues to offset increased expenses associated with the acquisition;
- Costs and delays in implementing or integrating common systems and procedures;
- Reduction or loss of customer orders due to the potential for market confusion, hesitation and delay;
- Impairment of existing customer, supplier and strategic relationships of either company;
- Insufficient cash flows from operations to fund the working capital and investment requirements;
- Difficulties in entering markets in which we have no or limited direct prior experience and where competitors in such markets have stronger market positions;
- The possibility that we may not receive a favorable return on our investment, the original investment may become impaired, and/or we may incur losses from these investments;
- Dissatisfaction or performance problems with the acquired company;
- The assumption of risks of the acquired company that are difficult to quantify, such as litigation;
- The cost associated with the acquisition, including restructuring actions, which may require cash payments that, if large enough, could materially and adversely affect our liquidity; and
- Assumption of unknown liabilities or other unanticipated adverse events or circumstances.

Acquisitions present many risks, and we may not realize the financial and strategic goals that were contemplated at the time of any transaction. We cannot provide assurance that we will be able to successfully integrate any business, products, technologies or personnel that we may acquire in the future, and our failure to do so could negatively impact our business, financial condition and results of operations.

**We were notified by the New York Stock Exchange (“NYSE”) that we did not meet its continued listing requirements, and we potentially face delisting if we do not comply with NYSE standards.**

We received notification from the NYSE on October 2, 2015 that we are not in compliance with the NYSE’s continued listing standard requiring that our stock trade at a minimum average closing price of \$1.00 for thirty consecutive trading days. In order to regain compliance, we expect that we will need to take actions, such as a reverse stock split, which will require shareholder action at our annual shareholder meeting for fiscal year 2016. If shareholders do not approve the actions we propose to regain compliance, or we are unable to otherwise regain compliance with the NYSE listing requirements, our common stock will be delisted from the NYSE, and, as a result, we would likely have our common stock quoted on the Over-the-Counter Bulletin Board, or the OTC BB. Securities that trade on the OTC BB generally have less liquidity and greater volatility than securities that trade on the NYSE. In addition, because issuers whose securities trade on the OTC BB are not subject to the corporate governance and other standards imposed by the NYSE, our reputation may suffer, which could result in a decrease in the trading price of our shares. The market price of our common stock has historically fluctuated and is likely to fluctuate in the future.

**If the future outcomes related to the estimates used in recording tax liabilities to various taxing authorities result in higher tax liabilities than estimated, then we would have to record tax charges, which could be material.**

We have provided amounts and recorded liabilities for probable and estimable tax adjustments that may be proposed by various taxing authorities in the U.S. and foreign jurisdictions. If events occur that indicate payments of these amounts will be less than estimated, then reversals of these liabilities would create tax benefits recognized in the periods when we determine the liabilities have reduced. Conversely, if events occur which indicate that payments of these amounts will be greater than estimated, then tax charges and additional liabilities would be recorded. In particular, various foreign jurisdictions could challenge the characterization or transfer pricing of certain intercompany transactions. In the event of an unfavorable outcome of such challenge, there exists the possibility of a material tax charge and adverse impact on the results of operations in the period in which the matter is resolved or an unfavorable outcome becomes probable and estimable.

Certain changes in stock ownership could result in a limitation on the amount of net operating loss and tax credit carryovers that can be utilized each year. Should we undergo such a change in stock ownership, it would severely limit the usage of these carryover tax attributes against future income, resulting in additional tax charges, which could be material.

**We are exposed to fluctuations in foreign currency exchange rates, and an adverse change in foreign currency exchange rates relative to our position in such currencies could have a material adverse impact on our business, financial condition and results of operations.**

We do not currently use derivative financial instruments for speculative purposes. We have used in the past, and may use in the future, foreign currency forward contracts and derivative instruments to hedge our exposure to foreign currency exchange rates. To the extent that we have assets or liabilities denominated in a foreign currency that are inadequately hedged or not hedged at all, we may be subject to foreign currency losses, which could be significant.

Our international operations can act as a natural hedge when both operating expenses and sales are denominated in local currencies. In these instances, although an unfavorable change in the exchange rate of a foreign currency against the U.S. dollar would result in lower sales when translated to U.S. dollars, operating expenses would also be lower in these circumstances. An increase in the rate at which a foreign currency is exchanged for U.S. dollars would require more of that particular foreign currency to equal a specified amount of U.S. dollars than before such rate increase. In such cases, and if we were to price our products and services in that particular foreign currency, we would receive fewer U.S. dollars than we would have received prior to such rate increase for the foreign currency. Likewise, if we were to price our products and services in U.S. dollars while competitors priced their products in a local currency, an increase in the relative strength of the U.S. dollar would result in our prices being uncompetitive in those markets. Such fluctuations in currency exchange rates could materially and adversely affect our business, financial condition and results of operations.

**The Company faces various risks associated with activist stockholders, including a potential proxy contest at our next annual meeting of stockholders.**

On June 3, 2016, VIEX Capital Advisors, LLC (“VIEX”) delivered a letter to us nominating five director candidates, for election to the Board at the 2016 annual meeting of stockholders (“annual meeting”).

On September 23, 2016, we entered into an agreement (“VIEX agreement”) with VIEX pursuant to which we have granted Board observer rights to two persons named in the VIEX agreement until December 1, 2016, subject to certain conditions. Under the VIEX agreement, we agreed to use our reasonable best efforts to hold the Annual Meeting on January 31, 2017, or another date mutually agreed by the parties, and VIEX agreed to abide by certain standstill provisions related to the solicitation of proxies and other matters until December 1, 2016, subject to earlier termination under certain circumstances.

Notwithstanding the VIEX agreement, VIEX may pursue a proxy contest at the annual meeting. A proxy contest would require us to incur significant legal fees and proxy solicitation expenses and require significant time and attention by management and the Board. Further, any perceived uncertainties as to our future direction and control could result in the loss of potential business opportunities and may make it more difficult to attract and retain qualified personnel and business partners, any of which could adversely affect our business, financial condition and results of operations. Depending on certain circumstances, including how many nominees VIEX seeks to elect, it is possible that VIEX nominated directors could constitute a majority of the Board following the annual meeting.

Under certain circumstances arising out of or related to a proxy contest or threatened proxy contest or the nomination of directors by a stockholder, a change in the composition of the Board may result in a change of control under the severance and change of control agreements we have with our management. Pursuant to the severance and change in control agreements, certain severance payments may be triggered following a change of control, but only upon there being a qualifying termination that occurs within twelve months of any such change of control. Under certain circumstances arising out of or related to a proxy contest or threatened proxy contest or the nomination of directors by a stockholder, a change in the composition of the Board may also result in a change of control under certain contracts with third parties, including our directors’ and officers’ liability insurance, if we are unable to secure appropriate waivers or amendments to any such contracts. The occurrence of any of the foregoing events could adversely affect our business.

**ITEM 6. EXHIBITS**

The Exhibit Index beginning on page 42 of this report sets forth a list of exhibits and is hereby incorporated by reference.

**SIGNATURE**

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

QUANTUM CORPORATION

/s/ FUAD AHMAD

Fuad Ahmad

Chief Financial Officer

(Principal Financial and Principal Accounting Officer)

Date: November 4, 2016

**EXHIBIT INDEX**

| <b><u>Exhibit Number</u></b> | <b><u>Exhibit Description</u></b>  |
|------------------------------|--|
| 10.1                         | Agreement between the Company and VIEX Capital Advisors, LLC and its affiliates dated September 23, 2016 (incorporated by reference to the Company's Current Report on Form 8-K filed on September 26, 2016) |
| 31.1                         | Certification of the Chief Executive Officer pursuant to Section 302(a) of the Sarbanes-Oxley Act of 2002. ‡   |
| 31.2                         | Certification of the Chief Financial Officer pursuant to Section 302(a) of the Sarbanes-Oxley Act of 2002. ‡   |
| 32.1                         | Certification of Chief Executive Officer pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley act of 2002. †   |
| 32.2                         | Certification of Chief Financial Officer pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley act of 2002. †   |
| 101.INS                      | XBRL Instance Document.  |
| 101.SCH                      | XBRL Taxonomy Extension Schema Document.   |
| 101.CAL                      | XBRL Taxonomy Extension Calculation Linkbase Document.   |
| 101.DEF                      | XBRL Taxonomy Extension Definition Linkbase Document.  |
| 101.LAB                      | XBRL Taxonomy Extension Label Linkbase Document.   |
| 101.PRE                      | XBRL Taxonomy Extension Presentation Linkbase Document.  |

‡ Filed herewith.

† Furnished herewith.

\* Indicates management contract or compensatory plan, contract or arrangement.

CERTIFICATION PURSUANT TO SECTION 302(a)  
OF THE SARBANES-OXLEY ACT OF 2002

I, Jon W. Gacek, certify that:

- 1) I have reviewed this quarterly report on Form 10-Q of Quantum Corporation;
- 2) Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
- 3) Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
- 4) The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this report based on such evaluation; and
  - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
- 5) The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 4, 2016

/s/ JON W. GACEK

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Jon W. Gacek  
President and Chief Executive Officer  
(Principal Executive Officer)

CERTIFICATION PURSUANT TO SECTION 302(a)  
OF THE SARBANES-OXLEY ACT OF 2002

I, Fuad Ahmad, certify that:

- 1) I have reviewed this quarterly report on Form 10-Q of Quantum Corporation;
- 2) Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
- 3) Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
- 4) The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this report based on such evaluation; and
  - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
- 5) The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 4, 2016

/s/ FUAD AHMAD

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Fuad Ahmad

Chief Financial Officer

(Principal Financial Officer)

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

I, Jon W. Gacek, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report of Quantum Corporation, on Form 10-Q for the quarterly period ended September 30, 2016 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, and that information contained in such Quarterly Report on Form 10-Q fairly presents in all material respects the financial condition and results of operations of Quantum Corporation.

Date: November 4, 2016

QUANTUM CORPORATION

/s/ JON W. GACEK

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Jon W. Gacek  
President and Chief Executive Officer  
(Principal Executive Officer)

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

I, Fuad Ahmad, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report of Quantum Corporation, on Form 10-Q for the quarterly period ended September 30, 2016, fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, and that information contained in such Quarterly Report on Form 10-Q fairly presents in all material respects the financial condition and results of operations of Quantum Corporation.

Date: November 4, 2016

QUANTUM CORPORATION

/s/ FUAD AHMAD

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Fuad Ahmad

Chief Financial Officer

(Principal Financial Officer)