

VERIFONE SYSTEMS, INC.

Form 10-Q

June 07, 2016

Table of Contents

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended April 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: 001-32465

VERIFONE SYSTEMS, INC.

(Exact name of registrant as specified in its charter)

Delaware 04-3692546

(State or other jurisdiction of (I.R.S. Employer incorporation or organization) Identification No.)

88 West Plumeria Drive

San Jose, CA 95134

(Address of principal executive offices with zip code)

(408) 232-7800

(Registrant's telephone number, including area code)

N/A

(Former name, former address and former fiscal year, if changed since last report)

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

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

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

Large accelerated filer  Accelerated filer

Non-accelerated filer  Smaller reporting company

(Do not check if a 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

The number of shares outstanding of each of the issuer's classes of common stock, as of the close of business on May 31, 2016

Class

Number of  
shares  
Common  
Stock,  
\$0.01  
par  
value  
per  
share

110,549,555
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Table of Contents

VERIFONE SYSTEMS, INC.

TABLE OF CONTENTS

PART I — FINANCIAL INFORMATION

Item 1. <u>Financial Statements:</u>	<u>3</u>
<u>Condensed Consolidated Statements of Operations</u>	<u>3</u>
<u>Condensed Consolidated Statements of Comprehensive Loss</u>	<u>4</u>
<u>Condensed Consolidated Balance Sheets</u>	<u>5</u>
<u>Condensed Consolidated Statements of Cash Flows</u>	<u>6</u>
<u>Notes to Condensed Consolidated Financial Statements</u>	<u>7</u>
Item 2. <u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>31</u>
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>51</u>
Item 4. <u>Controls and Procedures</u>	<u>51</u>
PART II — OTHER INFORMATION	
Item 1. <u>Legal Proceedings</u>	<u>52</u>
Item 1A. <u>Risk Factors</u>	<u>52</u>
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>81</u>
Item 3. <u>Defaults Upon Senior Securities</u>	<u>81</u>
Item 4. <u>Mine Safety Disclosures</u>	<u>81</u>
Item 5. <u>Other Information</u>	<u>81</u>
Item 6. <u>Exhibits</u>	<u>82</u>
<u>Signatures</u>	<u>82</u>
<u>Exhibit Index</u>	<u>83</u>

## PART I — FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS (Unaudited)

## VERIFONE SYSTEMS, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended April 30,		Six Months Ended April 30,	
	2016	2015	2016	2015
	(Unaudited, in thousands, except per share data)			
Net revenues:				
Systems	\$342,443	\$324,300	\$680,035	\$637,700
Services	183,835	165,844	359,782	338,670
Total net revenues	526,278	490,144	1,039,817	976,370
Cost of net revenues:				
Systems	200,544	188,972	395,349	374,640
Services	115,355	97,269	218,804	198,657
Total cost of net revenues	315,899	286,241	614,153	573,297
Total gross margin	210,379	203,903	425,664	403,073
Operating expenses:				
Research and development	54,715	47,579	106,383	96,482
Sales and marketing	59,027	55,371	113,976	112,781
General and administrative	54,884	49,457	107,710	96,807
Litigation settlement and loss contingency expense	—	1,213	—	1,213
Amortization of purchased intangible assets	21,974	20,567	41,600	42,899
Total operating expenses	190,600	174,187	369,669	350,182
Operating income	19,779	29,716	55,995	52,891
Interest expense, net	(8,543 )	(7,432 )	(16,847 )	(15,327 )
Other income (expense), net	(4,809 )	(3,169 )	(6,989 )	(2,926 )
Income before income taxes	6,427	19,115	32,159	34,638
Income tax provision	3,087	1,449	5,086	2,844
Consolidated net income	3,340	17,666	27,073	31,794
Net income attributable to noncontrolling interests	(441 )	(102 )	(673 )	(382 )
Net income attributable to VeriFone Systems, Inc. stockholders	\$2,899	\$17,564	\$26,400	\$31,412
Net income per share attributable to VeriFone Systems, Inc. stockholders:				
Basic	\$0.03	\$0.15	\$0.24	\$0.28
Diluted	\$0.03	\$0.15	\$0.24	\$0.27
Weighted average number of shares used in computing net income per share attributable to VeriFone Systems, Inc. stockholders:				
Basic	110,314	113,940	110,808	113,688
Diluted	111,314	115,900	111,889	115,727

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

Table of Contents

## VERIFONE SYSTEMS, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

	Three Months Ended April 30,		Six Months Ended April 30,	
	2016	2015	2016	2015
	(Unaudited, in thousands)			
Consolidated net income	\$3,340	\$17,666	\$27,073	\$31,794
Other comprehensive income (loss):				
Foreign currency translation adjustments	60,279	(30,260 )	22,050	(164,164 )
Unrealized gain (loss) on derivatives designated as cash flow hedges				
Change in unrealized loss on derivatives designated as cash flow hedges, net of tax	(374 )	(213 )	(2,061 )	(4,400 )
Amounts reclassified from Accumulated other comprehensive loss, net of tax	952	872	2,114	1,572
Net change in unrealized gain (loss) on derivatives designated as cash flow hedges	578	659	53	(2,828 )
Net change in other	25	27	51	54
Other comprehensive income (loss)	60,882	(29,574 )	22,154	(166,938 )
Total comprehensive income (loss)	64,222	(11,908 )	49,227	(135,144 )
Less: net income attributable to noncontrolling interests	(441 )	(102 )	(673 )	(382 )
Comprehensive income (loss) attributable to VeriFone Systems, Inc. stockholders	\$63,781	\$(12,010)	\$48,554	\$(135,526)

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

Table of ContentsVERIFONE SYSTEMS, INC.  
CONDENSED CONSOLIDATED BALANCE SHEETS

	April 30, 2016	October 31, 2015
	(Unaudited, in thousands, except par value)	
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 156,569	\$ 208,870
Accounts receivable, net of allowances of \$12,280 and \$8,752, respectively	397,429	361,988
Inventories	154,575	129,716
Prepaid expenses and other current assets	132,041	81,690
Total current assets	840,614	782,264
Property and equipment, net	217,177	190,965
Purchased intangible assets, net	368,017	317,517
Goodwill	1,164,744	1,084,031
Deferred tax assets, net	37,964	35,896
Other long-term assets	79,870	62,389
Total assets	\$ 2,708,386	\$ 2,473,062
<b>LIABILITIES AND EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 217,493	\$ 189,354
Accruals and other current liabilities	228,501	229,900
Deferred revenue, net	112,922	82,899
Short-term debt	55,296	39,088
Total current liabilities	614,212	541,241
Long-term deferred revenue, net	61,711	55,322
Deferred tax liabilities, net	113,508	102,921
Long-term debt	899,456	760,241
Other long-term liabilities	88,142	78,896
Total liabilities	1,777,029	1,538,621
Commitments and contingencies		
Stockholders' equity:		
Preferred stock: \$0.01 par value, 10,000 shares authorized, no shares issued and outstanding	—	—
Common stock: \$0.01 par value, 200,000 shares authorized, 110,525 and 112,684 shares issued and outstanding as of April 30, 2016 and October 31, 2015, respectively	1,105	1,125
Additional paid-in capital	1,749,369	1,726,416
Accumulated deficit	(582,658 )	(535,716 )
Accumulated other comprehensive loss	(270,167 )	(292,321 )
Total VeriFone Systems, Inc. stockholders' equity	897,649	899,504
Noncontrolling interests in subsidiaries	33,708	34,937
Total equity	931,357	934,441
Total liabilities and equity	\$ 2,708,386	\$ 2,473,062

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

Table of ContentsVERIFONE SYSTEMS, INC.  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Six Months Ended April 30,	
	2016	2015
	(Unaudited, in thousands)	
Cash flows from operating activities		
Consolidated net income	\$27,073	\$31,794
Adjustments to reconcile consolidated net income to net cash provided by operating activities:		
Depreciation and amortization, net	85,581	86,336
Stock-based compensation expense	22,039	21,027
Deferred income taxes, net	(5,103)	(7,216)
Other	6,227	10,019
Net cash provided by operating activities before changes in operating assets and liabilities	135,817	141,960
Changes in operating assets and liabilities:		
Accounts receivable, net	(12,602)	(35,249)
Inventories	(23,416)	(11,665)
Prepaid expenses and other assets	(24,221)	(19,295)
Accounts payable	26,015	17,331
Deferred revenue, net	30,882	12,656
Other current and long-term liabilities	(18,371)	(8,320)
Net change in operating assets and liabilities	(21,713)	(44,542)
Net cash provided by operating activities	114,104	97,418
Cash flows from investing activities		
Capital expenditures	(58,345)	(48,873)
Acquisition of businesses, net of cash acquired	(169,712)	(10,944)
Other investing activities, net	83	60
Net cash used in investing activities	(227,974)	(59,757)
Cash flows from financing activities		
Proceeds from debt, net of issuance costs	380,363	30,000
Repayments of debt	(238,616)	(70,204)
Proceeds from issuance of common stock through employee equity incentive plans	2,458	9,477
Stock repurchases	(79,866)	—
Other financing activities, net	(3,389)	(2,215)
Net cash provided by (used in) financing activities	60,950	(32,942)
Effect of foreign currency exchange rate changes on cash and cash equivalents	619	(20,687)
Net decrease in cash and cash equivalents	(52,301)	(15,968)
Cash and cash equivalents, beginning of period	208,870	250,187
Cash and cash equivalents, end of period	\$156,569	\$234,219

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





Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Unaudited

Note 1. Principles of Consolidation and Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited Condensed Consolidated Financial Statements include the accounts of VeriFone Systems, Inc. and our wholly-owned and majority-owned subsidiaries and have been prepared in accordance with U.S. GAAP for interim financial information and with the instructions on Form 10-Q pursuant to the rules and regulations of the U.S. Securities and Exchange Commission. The Condensed Consolidated Balance Sheet at October 31, 2015 has been derived from the audited Consolidated Balance Sheet at that date. All significant inter-company accounts and transactions have been eliminated. In accordance with the rules and regulations, we have omitted certain information and notes normally provided in our annual consolidated financial statements. In the opinion of management, the unaudited Condensed Consolidated Financial Statements contain all adjustments, consisting only of normal recurring items, necessary for the fair presentation of our financial position and results of operations for the interim periods. These unaudited Condensed Consolidated Financial Statements should be read in conjunction with the audited Consolidated Financial Statements and Notes thereto included in our Annual Report on Form 10-K for the fiscal year ended October 31, 2015. The results of operations for the three and six months ended April 30, 2016 are not necessarily indicative of the results expected for the entire fiscal year.

During December 2015, our Chief Executive Officer realigned the company's organizational structure to focus on two global product lines: Verifone Systems and Verifone Services. Verifone Systems delivers point of sale electronic payment devices that run our unique operating systems, security and encryption software, and certified payment software for both payments and commerce. Verifone Services delivers device related leasing and maintenance, payment transaction routing and reporting, and commerce based services such as advertising on digital screens. As a result of this organizational change, our reportable segments shifted from geographic-based segments to two global product segments effective for the first quarter of 2016. We determine our operating segments considering our overall management structure, how forecasts are approved, how executive compensation is determined, our organizational chart, as well as how our Chief Executive Officer, who is our chief operating decision maker, regularly reviews our operating results, assesses performance, allocates resources, and makes decisions regarding VeriFone's operations. Our reportable segments are the same as our operating segments. All prior period amounts reported by geographic segment have been reclassified to conform to the current presentation. See Note 12, Segment Information, in the Notes to Condensed Consolidated Financial Statements of this Quarterly Report on Form 10-Q for additional information.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires us to make estimates and assumptions about future events that affect the amounts reported in our consolidated financial statements and accompanying notes. We evaluate our estimates on an ongoing basis when updated information related to such estimates becomes available. We base our estimates on historical experience and information available to us at the time these estimates are made. Actual results could differ materially from these estimates.

Significant Accounting Policies

During the three and six months ended April 30, 2016, there have been no changes in our significant accounting policies as described in our Annual Report on Form 10-K for the fiscal year ended October 31, 2015.



Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Concentrations of Credit Risk

For the three and six months ended April 30, 2016 and 2015, no single customer accounted for more than 10% of our total Net revenues. As of April 30, 2016 and October 31, 2015 no single customer accounted for more than 10% of our total Accounts receivable, net.

Recent Accounting Pronouncements

During May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers, as amended by ASU 2015-14, 2016-08, 2016-10, and 2016-12, which provides new guidance on the recognition of revenue and states that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The standard is effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Early adoption is permitted as of reporting periods beginning after December 15, 2016. We are currently evaluating our adoption timing, the transition method we will use and the impact of this new pronouncement on our consolidated financial position and results of operations.

During January 2016, the FASB issued ASU 2016-01, Financial Instruments - Overall: Recognition and Measurement of Financial Assets and Financial Liabilities, which provides new guidance on the recognition, measurement, presentation, and disclosure of financial assets and liabilities. The standard is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Early adoption is permitted only for certain provisions. We are currently in the process of evaluating the impact of this new pronouncement on our consolidated financial position and results of operations.

During February 2016, the FASB issued ASU 2016-02, Leases, which increases transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. In connection with this new guidance, the FASB created Topic 842, Leases, which supersedes Topic 840, Leases. The standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. The new standard must be adopted using a modified retrospective transition, and provides for certain practical expedients. Transition will require application of the new guidance at the beginning of the earliest comparative period presented. We are currently in the process of evaluating the impact of this new pronouncement on our consolidated financial position and results of operations.

During March 2016, the FASB issued ASU 2016-07, Investments - Equity Method and Joint Ventures, which eliminates the requirement to retrospectively apply the equity method in previous periods when an investor initially obtains significant influence over a previously held investment and requires the investor to apply the equity method prospectively from the date the investment qualifies for the equity method. The standard is effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. Early adoption is permitted for any interim and annual financial statements that have not yet been issued. We are currently in the process of evaluating the impact of this new pronouncement on our consolidated financial position and results of operations.

During March 2016, the FASB issued ASU 2016-09, Compensation - Stock Compensation, to simplify various aspects related to how share-based payments are accounting for and presented in the financial statements, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The standard is effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. Early adoption is permitted for any interim and annual financial statements that have not yet

been issued, however, all of the guidance must be adopted in the same period. The new standard must be adopted either prospectively, retrospectively, or using a modified retrospective transition method, depending on the area covered in this ASU. We are currently in the process of evaluating the impact of this new pronouncement on our consolidated financial position and results of operations.

Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Note 2. Business Combinations

Fiscal Year 2016 Acquisitions

On December 23, 2015, we acquired InterCard AG, a leading payment services provider in Germany, in exchange for 85.0 million Euro in cash paid on the acquisition date (approximately \$92.4 million at the foreign exchange rate on the acquisition date) plus 1.2 million Euro (approximately \$1.4 million at the foreign exchange rate as of April 30, 2016), that is due in the third quarter of fiscal 2016. The acquisition was accounted for using the acquisition method of accounting, and the results of InterCard are included in our financial results as of the acquisition date. We acquired InterCard to expand our services offerings in Germany. Tangible assets acquired, net of liabilities assumed, totaled \$3.5 million. Purchased intangible assets, which have a weighted-average amortization useful life of 8.7 years, totaled \$42.7 million related to customer relationships, \$7.8 million related to developed and core technology, and \$2.2 million related to other intangible assets. Goodwill from the acquisition totaled \$37.6 million, was assigned to our Verifone Services reportable segment, and will not be deductible for income tax purposes. The primary areas of the preliminary purchase price allocation that have not yet been finalized are the fair value of income and non-income based taxes, and residual goodwill.

On February 2, 2016, we acquired AJB Software Design Inc., a Toronto-based provider of payment gateway and switching solutions for large merchants in the U.S. and Canada, for purchase consideration totaling approximately \$87.5 million in cash and tax liabilities incurred, subject to certain upward adjustments, plus up to \$10.0 million of additional contingent consideration with a fair value of \$1.4 million at the acquisition date. This acquisition was accounted for using the acquisition method of accounting, and the results of AJB are included in our financial results as of the acquisition date. We acquired AJB to expand our suite of services offerings. Tangible assets acquired, net of liabilities assumed, totaled \$17.4 million. Purchased intangible assets, which have a weighted-average amortization useful life of 4.5 years, totaled \$27.6 million related to customer relationships, \$13.1 million related to developed software technology, and \$0.4 million related to other intangible assets. Goodwill from the acquisition totaled \$30.4 million, was assigned to our Verifone Services reportable segment, and is partially deductible for income tax purposes. The primary areas of the preliminary purchase price allocation that have not yet been finalized are the fair value of income and non-income based taxes, and residual goodwill.

Fiscal Year 2015 Acquisitions

In fiscal year 2015, we completed five business combinations for consideration totaling \$29.6 million, including \$22.1 million of cash paid on the relevant acquisition date, \$5.7 million in future consideration and contingent consideration with a fair value of \$1.8 million at the relevant acquisition date. Each acquisition was accounted for using the acquisition method of accounting. These acquisitions were completed to augment our existing service offerings. Purchased intangible assets totaled \$9.0 million related to developed and core technology, \$2.8 million related to customer relationships, and \$0.5 million related to other intangible assets. Goodwill from these acquisitions totaled \$16.6 million, of which \$5.1 million will be deductible for income tax purposes.

Note 3. Net Income per Share of Common Stock

Basic net income per share of common stock is computed by dividing net income attributable to VeriFone Systems, Inc. stockholders by the weighted average number of shares of common stock outstanding for the period. Diluted net income per share of common stock is computed using the weighted average number of shares of common stock outstanding plus the effect of common stock equivalents, unless the common stock equivalents are anti-dilutive. The potential dilutive shares of our common stock resulting from assumed exercises of equity related instruments are

determined using the treasury stock method. Under the treasury stock method, an increase in the fair market value of our common stock will result in a greater number of dilutive securities.

Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The following table presents the computation of net income per share of common stock (in thousands, except per share data):

	Three Months Ended April 30, 2016		Six Months Ended April 30, 2015	
Basic and diluted net income per share attributable to VeriFone Systems, Inc. stockholders:				
Numerator:				
Net income attributable to VeriFone Systems, Inc. stockholders	\$2,899	\$17,564	\$26,400	\$31,412
Denominator:				
Weighted average shares attributable to VeriFone Systems, Inc. stockholders - basic	110,314	113,940	110,808	113,688
Weighted average effect of dilutive securities:				
Stock options, RSUs and RSAs	1,000	1,960	1,081	2,039
Weighted average shares attributable to VeriFone Systems, Inc. stockholders - diluted	111,314	115,900	111,889	115,727
Net income per share attributable to VeriFone Systems, Inc. stockholders:				
Basic	\$0.03	\$0.15	\$0.24	\$0.28
Diluted	\$0.03	\$0.15	\$0.24	\$0.27

For the three and six months ended April 30, 2016, equity incentive awards representing 2.6 million shares of common stock were excluded from the calculation of weighted average shares for diluted net income per share as they were anti-dilutive. For the three and six months ended April 30 2015, equity incentive awards representing 1.3 million shares of common stock were excluded from the calculation of weighted average shares for diluted net income per share as they were anti-dilutive. Anti-dilutive awards, which include stock options, RSUs and RSAs, could impact future calculations of diluted net income per share if the fair market value of our common stock increases.

**Note 4. Stock Repurchase Program**

In September 2015, our Board of Directors authorized a program to repurchase shares of our common stock with an aggregate value of up to \$200.0 million, with no expiration from the date of authorization. Shares may be repurchased from time to time in the open market, private purchases, through forward, derivative, accelerated repurchase or automatic repurchase transactions or otherwise. Certain of our share repurchases have been and may from time to time be effected through Exchange Act Rule 10b5-1 repurchase plans. The timing and actual amount of the share repurchases will depend on several factors including price, capital availability, regulatory requirements, alternative investment opportunities, including mergers and acquisitions, market conditions and other factors. We are not obligated to repurchase any specific number of shares under the program and the repurchase program may be modified, suspended or discontinued at any time.

During the six months ended April 30, 2016, we repurchased approximately 2.6 million shares of our common stock on the open market at an average repurchase price of \$28.02 per share. There were no stock repurchase activities during the three months ended April 30, 2016. As of April 30, 2016, there was approximately \$50.0 million remaining available for stock repurchases under this program.

Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Note 5. Income Taxes

We recorded tax provisions totaling \$3.1 million and \$1.4 million for the three months ended April 30, 2016 and 2015, respectively. The income tax provisions for the three months ended April 30, 2016 and 2015 are primarily related to foreign taxes and other discrete activity. We recorded tax provisions totaling \$5.1 million and \$2.8 million for the six months ended April 30, 2016 and 2015, respectively. The income tax provisions for the six months ended April 30, 2016 were primarily related to foreign taxes and other discrete activity. The income tax provisions for the six months ended April 30, 2015 were primarily related to foreign taxes offset by the reversal of unrecognized tax benefits where statutes of limitations expired and audits were settled.

Our total unrecognized tax benefits were approximately \$110.8 million as of April 30, 2016. The amount of unrecognized tax benefits could be reduced upon closure of tax examinations or if the statute of limitations on certain tax filings expires without assessment from the relevant tax authorities. We believe that it is reasonably possible that there could be an immaterial reduction in unrecognized tax benefits due to statute of limitation expirations in multiple tax jurisdictions during the next 12 months. Interest and penalties accrued on these uncertain tax positions will also be released upon the expiration of the applicable statute of limitations.

U.S. Internal Revenue Service Tax Audit Assessment

We were audited by the U.S. Internal Revenue Service for fiscal years 2005 through 2010 related to our five year net operating loss carry back for fiscal year 2010. In December 2014 we received a Notice of Proposed Adjustment indicating the denial of our worthless stock deduction of \$154.3 million, related to the insolvency of one of our UK subsidiaries, recorded on our 2010 tax return. The impact of the Notice of Proposed Adjustment was the denial of the loss carryback to 2005 and 2006 which resulted in an approximately \$25.0 million cash refund and the disallowance of approximately \$29.0 million of future tax benefits residing in the NOL carryover which are offset with a valuation allowance. We filed a protest to the Notice of Proposed Assessment in April 2015. In June 2016 we reached a final settlement with the U.S. Internal Revenue Service sustaining our worthless stock deduction at 75% of the originally claimed value. The impact of this settlement will be a reduction in our net operating loss carryforward of \$38.6 million and an offsetting reduction of our valuation allowance against the deferred tax asset. The net result will not have a material impact on our financial position or results of operations.



Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

## Israel Tax Audit Assessment

We are currently under audit by the Israeli Tax Authorities for fiscal years 2008 through 2009, and 2011 through 2013. The Israeli Tax Authorities issued a tax assessment in October 2014 for fiscal year 2009 or alternatively for fiscal year 2008 claiming there was a business restructuring that resulted in a transfer of some functions, assets and risks from VeriFone Israel Ltd. to the U.S. parent company that the Israeli Tax Authorities claim was a sale valued at 1.36 billion New Israeli Shekels (approximately \$363.5 million at the foreign exchange rate as of April 30, 2016). The Israeli Tax Authorities argued that the claim applies to fiscal year 2009 or alternatively to fiscal year 2008. We filed our objection to the tax assessment in January 2015 and received the Israeli Tax Authorities decision through an Order (a second stage assessment) in January 2016. The Order increased the value of the sale to 2.20 billion New Israeli Shekels in fiscal year 2009 (approximately \$587.6 million at the foreign exchange rate as of April 30, 2016) or alternatively 2.23 billion New Israeli Shekels in fiscal year 2008 (approximately \$594.4 million at the foreign exchange rate as of April 30, 2016) and contended secondary adjustments relating to a deemed dividend and/or interest.

Based on the Order, these and other claims result in a tax liability and deficiency penalty assessment in the amount of 1.25 billion New Israeli Shekels (approximately \$333.1 million at the foreign exchange rate as of April 30, 2016), if the claim was assessed for fiscal year 2009, to 1.47 billion New Israeli Shekels (approximately \$391.7 million at the foreign exchange rate as of April 30, 2016) if the claim was assessed for fiscal year 2008, including interest, the required Israeli price index adjustments (referred to as the linkage differentials) and deficiency fines (as applicable) through April 30, 2016. The Israeli Tax Authorities' contention regarding secondary adjustments relating to deemed dividend was not quantified by them.

We continue to believe the Israeli Tax Authorities' assessment position is without merit and plan on appealing the assessment to the district court. We have agreed with the Israeli Tax Authorities to repay our \$69.0 million intercompany loan from VeriFone Israel Ltd. to the extent of the amount of a final agreed tax assessment concerning fiscal year 2008 and fiscal year 2009 or a judgment of a district court in an appeal on the decision of the Israeli Tax Authorities in the objection, if any.

## Note 6. Balance Sheet and Statement of Operations Details

## Inventories

Inventories consisted of the following (in thousands):

	April 30, 2016	October 31, 2015
Raw materials	\$33,578	\$30,297
Work-in-process	1,516	2,588
Finished goods	119,481	96,831
Total inventories	\$154,575	\$129,716

Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

## Accruals and Other Current Liabilities

Accruals and other current liabilities consisted of the following (in thousands):

	April 30, October 31,	
	2016	2015
Accrued expenses	\$80,990	\$ 85,973
Accrued compensation	60,751	69,174
Other current liabilities	86,760	74,753
Total accruals and other current liabilities	\$228,501	\$ 229,900

Other current liabilities were comprised primarily of sales and value-added taxes payable and accrued warranty.

## Accrued Warranty

Activity related to accrued warranty consisted of the following (in thousands):

	Six Months Ended	
	April 30,	
	2016	2015
Balance at beginning of period	\$16,320	\$15,411
Warranty charged to Cost of net revenues	7,156	5,977
Utilization of warranty accrual	(7,348 )	(5,434 )
Other	124	(869 )
Balance at end of period	16,252	15,085
Less: current portion	(12,918 )	(12,824 )
Long-term portion	\$3,334	\$2,261

## Deferred Revenue, Net

Deferred revenue, net of related costs consisted of the following (in thousands):

	April 30, October 31,	
	2016	2015
Deferred revenue	\$192,831	\$157,747
Deferred cost of revenue	(18,198 )	(19,526 )
Deferred revenue, net	174,633	138,221
Less: current portion	(112,922 )	(82,899 )
Long-term portion	\$61,711	\$55,322

## Other Long-Term Liabilities

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

	April 30, October 31,	
	2016	2015
Unrecognized tax benefits liability, net	\$37,663	\$ 35,860
Contingent consideration payable	11,760	10,776
Other long-term liabilities	38,719	32,260
Total other long-term liabilities	\$88,142	\$ 78,896



Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

## Stock-Based Compensation Expense

The following table presents the stock-based compensation expense recognized in our Condensed Consolidated Statements of Operations (in thousands):

	Three Months		Six Months	
	Ended April 30,		Ended April 30,	
	2016	2015	2016	2015
Cost of net revenues	\$880	\$409	\$1,692	\$1,128
Research and development	1,886	1,208	3,794	3,952
Sales and marketing	3,840	3,499	7,099	7,579
General and administrative	4,973	3,756	9,454	8,368
Total stock-based compensation expense	\$11,579	\$8,872	\$22,039	\$21,027

## Accumulated Other Comprehensive Loss

Activity related to Accumulated other comprehensive loss consisted of the following (in thousands):

	Foreign currency translation adjustments	Unrealized loss on derivatives designated as cash flow hedges <sup>(1)</sup>	Other <sup>(2)</sup>	Total
Balance at October 31, 2015	\$ (286,662 )	\$ (4,409 )	\$ (1,250)	\$ (292,321)
Gains (losses) before reclassifications, net of tax	22,050	(2,061 )	—	19,989
Amounts reclassified from Accumulated other comprehensive loss, net of tax	—	2,114	51	2,165
Other comprehensive gain	22,050	53	51	22,154
Balance at April 30, 2016	\$ (264,612 )	\$ (4,356 )	\$ (1,199)	\$ (270,167)

(1) Amounts reclassified from Accumulated other comprehensive loss, net of tax, were recorded in Interest expense, net in the Condensed Consolidated Statements of Operations. The related tax impacts were insignificant.

(2) Amounts reclassified from Accumulated other comprehensive loss, net of tax, were recorded in General and administrative expenses in the Condensed Consolidated Statements of Operations. The related tax impacts were insignificant.

## Note 7. Financial Instruments

## Fair Value Measurements

## Assets and Liabilities Measured and Recorded at Fair Value on a Recurring Basis

Our financial assets and liabilities consist principally of cash, accounts receivable, accounts payable, debt, foreign exchange forward contracts, interest rate swaps, and contingent consideration payable. We measure and record certain of our financial assets and liabilities at fair value on a recurring basis. The estimated fair value of cash, accounts receivable, and accounts payable approximates their carrying value. The estimated fair value of our debt approximates the carrying value because the interest rate on such debt adjusts to market rates on a periodic basis. Contingent

consideration payable, interest rate swaps, and foreign exchange forward contracts are recorded at estimated fair value.

Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The following tables present our significant assets and liabilities that are measured at fair value on a recurring basis and their classification within the fair value hierarchy (in thousands). There were no transfers between levels of fair value hierarchy in the six months ended April 30, 2016 and the fiscal year ended October 31, 2015.

	April 30, 2016			October 31, 2015				
	Carrying Value	Level 1	Level 2	Level 3	Carrying Value	Level 1	Level 2	Level 3
<b>Assets</b>								
Other current and long-term assets:								
Derivative financial instruments	\$23	\$	-\$23	\$—	\$53	\$	-\$53	\$—
Total assets measured and recorded at fair value	\$23	\$	-\$23	\$—	\$53	\$	-\$53	\$—
<b>Liabilities</b>								
Other current and long-term liabilities:								
Contingent consideration payable	\$14,657	\$	-\$—	\$14,657	\$12,786	\$	-\$—	\$12,786
Derivative financial instruments	4,477	—	4,477	—	4,784	—	4,784	—
Total liabilities measured and recorded at fair value	\$19,134	\$	-\$4,477	\$14,657	\$17,570	\$	-\$4,784	\$12,786

## Fair Value of Contingent Consideration Payable

The following table presents changes in our contingent consideration payable which is categorized in Level 3 of the fair value hierarchy for the six months ended April 30, 2016 (in thousands):

Balance at beginning of period	\$12,786
Additions	1,389
Payments	(207 )
Changes in estimates, included in Other income (expense), net	(317 )
Interest expense, net	1,006
Balance at end of period	\$14,657

Contingent consideration payable is comprised substantially of amounts payable for acquired media contracts. The contingent consideration payable is classified as Level 3 because we use significant unobservable inputs to determine the expected payments and an appropriate discount rate to calculate the fair value. The significant unobservable inputs we use include our estimate of the future net revenues we expect to generate from the acquired media contracts, the probability of achieving those revenues, and the revenue share rate for a media contract. The discount rate used to determine the fair value of the contingent consideration payable is 18.5%. The maximum liability on contingent consideration payable is indeterminate because it is based on future revenues generated from the acquired business. We evaluate changes in the assumptions used to calculate the fair value of contingent consideration payable at the end of each period.

Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

## Derivative Financial Instruments

## Interest Rate Swap Agreements Designated as Cash Flow Hedges

We use interest rate swap agreements to hedge the variability in cash flows related to interest payments. As of April 30, 2016, we had outstanding interest rate swap agreements to effectively convert \$500.0 million of the term A loan from a floating rate plus applicable margin to a 1.20% fixed rate plus applicable margin. The principal amount under the term A loan covered by the new interest rate swap agreements will decrease to \$450.0 million from April 1, 2017 through September 30, 2017, and \$400.0 million from October 1, 2017 through March 30, 2018. The swap agreements expire March 30, 2018.

The interest rate swaps qualify for hedge accounting treatment as cash flow hedges. The notional amounts of interest rate swap agreements outstanding as of April 30, 2016 and October 31, 2015 were each \$500.0 million.

Gains and losses arising from the effective portion of interest rate swap agreements are recorded in Accumulated other comprehensive loss, and are subsequently reclassified into earnings in the period or periods during which the underlying transactions affect earnings. As of April 30, 2016, the estimated net derivative loss related to our cash flow hedges included in Accumulated other comprehensive loss that will be reclassified into earnings in the next 12 months is \$3.0 million.

## Foreign Exchange Forward Contracts Not Designated as Hedging Instruments

We arrange and maintain foreign exchange forward contracts so as to yield gains or losses to offset changes in foreign currency denominated assets or liabilities due to changes in foreign exchange rates, with the objective to mitigate the volatility associated with foreign currency transaction gains or losses. Our foreign currency exposures are predominantly inter-company receivables and payables arising from product sales and loans from one of our entities to another. Our foreign exchange forward contracts generally mature within 90 days. The notional amounts of such contracts outstanding as of April 30, 2016 and October 31, 2015 were \$184.1 million and \$219.6 million, respectively.

We recognized the following gains (losses) on foreign exchange forward contracts not designated as cash flow hedges (in thousands):

	Three Months Ended April 30, 2016		Six Months Ended April 30, 2015	
Gains (losses) recognized in Other income (expense), net in our Condensed Consolidated Statements of Operations	\$(2,689)	\$(631)	\$1,621	\$10,903

## Note 8. Goodwill and Purchased Intangible Assets

## Goodwill

Activity related to goodwill by reportable segment for the six months ended April 30, 2016 consisted of the following (in thousands):

	Verifone Systems	Verifone Services	Total
Balance at beginning of period	\$512,182	\$571,849	\$1,084,031
Acquisitions	—	68,010	68,010

Other adjustments	—	(762	) (762	)
Currency translation adjustments	4,946	8,519	13,465	
Balance at end of period	\$517,128	\$647,616	\$1,164,744	



Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

As a result of the change to our two new operating segments in December 2015, we have realigned our reporting units. Verifone Systems represents one reporting unit, and Verifone Services is comprised of two reporting units, Taxi Solutions and Verifone Payment Services. In connection with this reporting unit realignment, during the three months ended January 31, 2016, we also updated our goodwill impairment assessment based on a quantitative analysis. We first evaluated the goodwill of our reporting units immediately prior the realignment and concluded that there was no impairment. We then allocated our goodwill to the new reporting units using a relative fair value approach, and re-confirmed that there is no impairment.

Based on our review for potential indicators of impairment performed during the three months ended April 30, 2016 and the fiscal year ended October 31, 2015, there were no indicators of impairment. During the fourth quarter of fiscal year 2016, we will perform our annual goodwill impairment assessment.

## Purchased Intangible Assets, Net

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

	April 30, 2016			October 31, 2015		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Customer relationships	\$662,417	\$(333,778)	\$328,639	\$591,930	\$(298,812)	\$293,118
Other	105,606	(66,228)	39,378	115,143	(90,744)	24,399
Total	\$768,023	\$(400,006)	\$368,017	\$707,073	\$(389,556)	\$317,517

Other intangible assets, net, were comprised primarily of developed and core technology and trade names.

Activity related to purchased intangible assets during the six months ended April 30, 2016 includes a \$12.2 million currency translation adjustment to Gross carrying amount and a \$6.0 million currency translation adjustment to Accumulated amortization.

Amortization of purchased intangible assets was allocated as follows (in thousands):

	Three Months Ended April 30, 2016		Six Months Ended April 30, 2015	
	2016	2015	2016	2015
Included in Cost of net revenues	\$3,820	\$4,609	\$7,809	\$9,269
Included in Operating expenses	21,974	20,567	41,600	42,899
Total amortization of purchased intangible assets	\$25,794	\$25,176	\$49,409	\$52,168

Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Total future amortization expense for purchased intangible assets that have finite lives, based on our existing intangible assets and their current estimated useful lives as of April 30, 2016, is estimated as follows (in thousands):

	Cost of Net Revenues	Operating Expenses	Total
Fiscal Years Ending October 31:			
Remaining of fiscal year 2016	\$ 7,667	\$44,853	\$52,520
2017	8,379	66,555	74,934
2018	6,205	59,906	66,111
2019	4,911	56,306	61,217
2020	3,248	39,012	42,260
Thereafter	3,464	67,511	70,975
Total future amortization expense	\$ 33,874	\$334,143	\$368,017

## Note 9. Financings

Amounts outstanding under our financing arrangements consisted of the following (in thousands):

	April 30, 2016	October 31, 2015
Credit Agreement		
Term A loan	\$547,500	\$562,500
Term B loan	196,500	197,500
Revolving loan	218,237	54,000
Capital leases and other debt	5,435	342
Total principal payments due	967,672	814,342
Less: original issue discount and debt issuance cost	(12,920 )	(15,013 )
Total amounts outstanding	954,752	799,329
Less: current portion	(55,296 )	(39,088 )
Long-term portion	\$899,456	\$760,241

## Credit Agreement

Key terms of our credit agreement include financial maintenance covenants and certain representations, warranties, covenants, and conditions that are customarily required for similar financings. We were in compliance with all financial covenants under our credit agreement as of April 30, 2016.

Borrowings under the credit agreement may be “Base Rate Borrowings” or “Eurodollar Borrowings” at our option. As of April 30, 2016, we have elected the Eurodollar option for all of our borrowings. Eurodollar loans bear interest at a monthly market interest rate plus a margin according to the credit agreement. As of April 30, 2016, the monthly market interest rate was 0.44% for our term A and revolver loans, and 0.75% for our term B loan, and the margins were 1.75% for our term A and revolver loans and 2.75% for our term B loan. Accordingly, as of April 30, 2016, the interest rate was 2.19% for the term A and revolving loans and 3.50% for the term B loan.

Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

We have a number of interest rate swap agreements under which we pay banks a fixed rate of 1.20% and receive a monthly floating rate, which effectively converts \$500.0 million of the term A loan from a floating interest rate to a fixed interest rate as of April 30, 2016.

As of April 30, 2016, the commitment fee for the unused portion of the revolving loan was 0.250% per annum, payable quarterly in arrears, and the amount available to draw under the revolving loan was \$281.8 million.

## Capital Lease

In February 2016, we entered into a \$15.0 million capital leasing facility. As of April 30, 2016, we leased approximately \$4.5 million under this arrangement.

## Note 10. Restructurings

As part of cost optimization and corporate transformation initiatives, our management has approved, committed to and initiated restructuring plans to reduce headcount, and consolidate facilities and data centers. Plans initiated in 2014 and 2015 are expected to be substantially complete by the end of fiscal year 2016.

Activity related to our restructuring plans for the six months ended April 30, 2016 consisted of the following (in thousands):

	Restructuring Plans			
	June 2014 Plan		July 2015 Plan	
	Employee Involuntary Termination Benefits	Facilities Related Costs	Employee Involuntary Termination Benefits	Total
Balance at October 31, 2015	\$1,027	\$ 5	\$ 5,090	\$6,122
Charges, net of adjustments	734	—	(256 )	478
Cash payments	(567 )	(5 )	(3,168 )	(3,740 )
Balance at April 30, 2016	\$1,194	\$ —	\$ 1,666	\$2,860
Cumulative costs to date	\$12,957	\$ 853	\$ 7,087	

The following table presents the restructuring expense recognized in our Condensed Consolidated Statements of Operations (in thousands):

	Three Months Ended April 30,		Six Months Ended April 30,	
	2016	2015	2016	2015
Cost of net revenues	\$(28 )	\$(48 )	\$(89 )	\$35
Research and development	595	32	628	154
Sales and marketing	(13 )	108	(483 )	793
General and administrative	21	69	422	552
Total restructuring expense	\$575	\$161	\$478	\$1,534



Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Note 11. Commitments and Contingencies

Commitments

There have been no material changes to our leases and manufacturing agreements since October 31, 2015.

Bank Guarantees

We have issued bank guarantees with maturities ranging from two months to six years to certain of our customers and vendors as required in some countries to support certain performance obligations under our service or other agreements with those parties. As of April 30, 2016, the maximum amount that may become payable under these guarantees was \$11.9 million, of which \$1.4 million was collateralized by restricted cash deposits.

Contingencies

We evaluate the circumstances regarding outstanding and potential litigation and other contingencies on a quarterly basis to determine whether there is at least a reasonable possibility that a loss exists requiring accrual or disclosure, and if so, whether an estimate of the possible loss or range of loss can be made, or whether such an estimate cannot be made. When a loss is probable and reasonably estimable, we accrue for such amount based on our estimate of the probable loss considering information available at the time. When a loss is reasonably possible, we disclose the estimated possible loss or range of loss in excess of amounts accrued if material. Except as otherwise disclosed below, we do not believe that material losses were probable or that there was a reasonable possibility that a material loss may have been incurred with respect to the matters disclosed.

Brazilian Tax Assessments

State Value-Added Tax

The Brazilian subsidiary we acquired as part of our acquisition of Hypercom in August 2011 received an unfavorable administrative decision on a tax enforcement action against it filed by the São Paulo State Revenue Department for collection of state sales taxes related to purported sales of software for the 1998 and 1999 tax years. In 2004, an appeal against this unfavorable administrative decision was filed in a judicial proceeding. The first level decision in the judicial proceeding was issued in our favor. The São Paulo State Revenue Department filed an appeal of this decision. The second level administrative decision ordered that the case be returned to the lower court in order to allow the production of further evidence. Based on our current understanding of the underlying facts of this matter, we believe it is reasonably possible that we may receive an unfavorable decision in this proceeding. The tax assessment including estimated interest through April 30, 2016 for this matter totals approximately 8.8 million Brazilian reais (approximately \$2.5 million at the foreign exchange rate as of April 30, 2016). As of April 30, 2016, we have not accrued for this matter, but we have posted a bank bond as a guaranty.

Federal Tax Assessments

Brazilian Federal Tax Amnesty

In December 2013, without admitting any fault or liability, we elected to enroll certain of our pending Brazilian tax assessments in the Brazilian Federal Tax Amnesty Program created by Law n. 11.941/2009 in 2009 and reopened for enrollment from October 2013 to December 2013, known as the “REFIS Amnesty.” The REFIS Amnesty is a program

administered by the Brazilian tax authorities and allows entities charged with tax assessments that fall within the program's scope to voluntarily settle such assessments with certain discounts applied to the amounts due. After conducting an evaluation of our existing Brazilian federal tax assessments and the terms offered by the REFIS Amnesty, we determined to voluntarily settle a number of our pending assessments.

Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Tax assessment matters that fall within the REFIS Amnesty's scope are generally listed in the program's web-based portal for enrollment. Although no formal acceptance by the tax authorities is issued at the time of our enrollment of a matter, we expect the tax authorities to confirm our enrollment as they complete their process to formally consolidate the matters we enrolled in the REFIS Amnesty. In connection with our enrollment of the tax assessments into the REFIS Amnesty, we were required to forgo any further legal defense or proceedings with respect to the merits of such assessments. In exchange, the enrolled assessments were closed and we were granted discounts on our payment of the related accrued interest and penalties and are able to pay under an installment plan, subject to our compliance with the terms of the program. For certain assessments, existing net operating loss carryforwards, or net operating losses, may be used to satisfy a portion of the settlement obligation. Under the terms of the REFIS Amnesty, our right to fund the settlement through the installment payment plan would be canceled after three instances of our not timely paying the installment amounts as scheduled, in which case the full amounts of the original tax debts, including interest and penalties without the benefit of discount, would become immediately due and payable. We have included the terms and amounts below for those assessments that we have placed into the REFIS Amnesty.

Federal Tax Assessments related to Brazilian Subsidiaries from Lipman Acquisition

Two of our Brazilian subsidiaries that were acquired as a part of the November 2006 acquisition of Lipman Electronic Engineering Ltd. ("Lipman") were notified of assessments regarding Brazilian customs penalties that relate to alleged infractions in the importation of goods. The assessments were issued by the Federal Revenue Department in the City of Vitória, the City of São Paulo, and the City of Itajai. In each of these cases, the tax authorities allege that the structure used for the importation of goods was simulated with the objective of evading taxes levied on the importation by under-invoicing the imported goods. The tax authorities allege that the simulation was created through an interposition of parties and that the real sellers and buyers of the imported goods were hidden. In February 2013, the São Paulo assessment was canceled following a favorable second level decision that was not appealed.

In the Vitória tax assessment, the fines were reduced from 4.7 million Brazilian reais (approximately \$1.3 million at the foreign exchange rate as of April 30, 2016) to 1.5 million Brazilian reais (approximately \$410,000 at the foreign exchange rate as of April 30, 2016) on a first level administrative decision on January 26, 2007. Both we and the tax authorities filed appeals of the first level administrative decision. In this appeal, we argued that the tax authorities did not have enough evidence to determine that the import transactions were indeed fraudulent and that, even if there were some irregularities in such importations, they could not be deemed to be our responsibility since all the transactions were performed by the third-party importer of the goods. On June 30, 2010, the Taxpayers Administrative Council of Tax Appeals decided to reinstate the original claim amount of 4.7 million Brazilian reais (approximately \$1.3 million at the foreign exchange rate as of April 30, 2016) against us. On February 27, 2013, the Taxpayers Administrative Council of Tax Appeals issued its formal ruling reinstating the original claim amount. On May 31, 2013, we filed a motion to clarify such ruling, which is pending a decision.

In the Itajai tax assessment, we were notified on January 18, 2008, of a first level administrative decision rendered that maintained the total fine of 2.0 million Brazilian reais (approximately \$560,000 at the foreign exchange rate as of April 30, 2016) as imposed, excluding interest. On May 27, 2008, we appealed the first level administrative decision to the Taxpayers Council. This matter is pending second level decision.

Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

In December 2013, we sought to enroll the entire amount of tax liabilities in dispute for both the Vitória and Itajai assessments in the REFIS Amnesty. However, because we are named as a jointly-liable party rather than as the primary defendant in these matters, these assessments were not listed in the REFIS Amnesty web-based portal as available for election under the REFIS Amnesty. We believe these matters qualify for inclusion in the REFIS Amnesty and have filed the required notifications to our local tax office and commenced payments to indicate our decision to enroll these matters in the REFIS Amnesty. We expect the tax authorities' confirmation that these matters have been included in the REFIS Amnesty once they complete their procedures to consolidate the enrolled assessments. We elected to make the amnesty payments for these matters in monthly installments over a 30-month period for total payments, inclusive of interest and penalties, of 7.6 million Brazilian reais (approximately \$2.1 million at the foreign exchange rate as of April 30, 2016). We accrued the full amount of the payments, plus estimated interest, under the REFIS Amnesty for these matters in December 2013 when we enrolled in the program, and made our first payment on December 26, 2013. As of April 30, 2016, we have remaining installment payments totaling 0.3 million Brazilian reais (approximately \$70,000 at the foreign exchange rate as of April 30, 2016).

We had previously accrued the estimated liability for both the Vitória and Itajai assessments. Based on our understanding of the underlying facts of these matters, we believe it is probable we may receive an unfavorable decision for each of these assessments unless we are able to resolve these matters through the REFIS Amnesty. Upon confirmation of acceptance of these matters into the REFIS Amnesty, we will reduce our accrued liabilities related to these matters to reflect the discounted amounts due under the REFIS Amnesty. As of April 30, 2016, we have accruals totaling 12.3 million Brazilian reais (approximately \$3.5 million at the foreign exchange rate as of April 30, 2016).

#### Federal Tax Assessments related to Brazilian Subsidiary from Hypercom Acquisition

The Brazilian subsidiary we acquired as part of our acquisition of Hypercom in August 2011 is the subject of outstanding tax assessments by the federal tax authorities alleging unpaid IRPJ, CSL, COFINS and PIS taxes from 2002 and 2003. The 2002 assessments are the subject of an administrative proceeding and the 2003 assessments are the subject of a civil enforcement action. Three of the four claims for the 2002 assessments were previously settled prior to our acquisition of Hypercom. The first level administrative court issued an unfavorable decision for the remaining claim related to the 2002 tax assessments. Our appeal to the Administrative Tax Appeals Council was denied in December 2013. With respect to the 2003 tax assessments, we received a partially favorable ruling, and our appeal for the remaining assessments is pending decision in the civil courts. In December 2013, we elected to enroll the tax liability for the remaining 2002 assessment in dispute and the portion of the 2003 assessments for which we received an unfavorable ruling in the REFIS Amnesty.

For the 2002 assessment, we applied available net operating losses, to the extent permitted, toward the interest and penalties portion of the settlement obligation under the REFIS Amnesty. For the remaining balance, we elected to make the amnesty payments in monthly installments over a 90-month period for total payments of 2.2 million Brazilian reais (approximately \$630,000 at the foreign exchange rate as of April 30, 2016). We accrued the full amount of the payments, plus estimated interest, under the REFIS Amnesty for this matter in December 2013 when we enrolled in the program, and made our first payment on December 26, 2013. In the first quarter of fiscal year 2015, based on new provisions made available under the REFIS Amnesty, we elected to pay all remaining outstanding amounts due under the REFIS Amnesty in relation to the 2002 assessment, and settled such payments using cash and additional available net operating losses.



Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

For the 2003 assessments, we applied available net operating losses, to the extent permitted, toward the interest and penalties portion of the settlement obligation under the REFIS Amnesty. At the time we initially appealed the 2003 assessments to the civil courts, we were required to make a deposit of 2.8 million Brazilian reais (approximately \$800,000 at the foreign exchange rate as of April 30, 2016) to the court in order to perfect our appeal. In light of our enrollment of certain of the 2003 assessments in the REFIS Amnesty, we have notified the civil court of our enrollment and requested the release of the portion of the deposit for the assessments enrolled in the REFIS Amnesty, which totals 675,000 Brazilian reais (approximately \$190,000 at the foreign exchange rate as of April 30, 2016). Once approved by the court, the released funds will be applied against the settlement obligation under the REFIS Amnesty. Approximately 2.2 million Brazilian reais (approximately \$610,000 at the foreign exchange rate as of April 30, 2016) will remain deposited in connection with the 2003 assessments that will continue in the civil courts and which deposits will be released to the prevailing party after resolution of the underlying assessments.

Excluding the assessments that have been enrolled in the REFIS Amnesty for this matter, which have been accrued as described above, and excluding the net operating losses still at issue, the remaining assessments total approximately 3.1 million Brazilian reais (approximately \$870,000 at the foreign exchange rate as of April 30, 2016), including estimated penalties and interest, as of April 30, 2016. Based on our current understanding of the underlying facts of this matter, we believe it is reasonably possible we may receive an unfavorable decision related to these remaining assessments.

We also elected to enroll a number of outstanding tax offset requests that were previously applied for by the Brazilian subsidiary we acquired as part of our acquisition of Hypercom in August 2011 in the REFIS Amnesty. These outstanding tax offset requests relate to different tax debts, primarily for IRPJ, PIS and COFINS for past tax years, and total approximately 2.5 million Brazilian reais (approximately \$710,000 at the foreign exchange rate as of April 30, 2016), including estimated penalties and interest. We applied available net operating losses toward the interest and penalties portion of the settlement obligation under the REFIS Amnesty. For the remaining balance, we elected to make the amnesty payments in monthly installments over a 90-month period for total payments of 1.3 million Brazilian reais (approximately \$380,000 at the foreign exchange rate as of April 30, 2016). We accrued the full amount of the payments, plus estimated interest, under the REFIS Amnesty for these matters in December 2013 when we enrolled in the program, and made our first payment on December 26, 2013. After further review, the tax authorities agreed with our positions in certain of these cases and reduced our liabilities under the REFIS Amnesty. In the first quarter of fiscal year 2015, based on new provisions made available under the REFIS Amnesty, we elected to pay all remaining outstanding amounts due under the REFIS Amnesty in relation to the remaining tax offset requests, and settled such payments using cash and additional available net operating losses.

Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Municipality Services Tax Assessments

In December 2009, one of the Brazilian subsidiaries that was acquired as part of the Lipman acquisition was notified of a tax assessment regarding alleged nonpayment of tax on services rendered for the period from September 2004 to December 2004. This assessment was issued by the municipality of São Paulo (the "municipality"), and asserts a services tax deficiency and related penalties totaling 875,000 Brazilian reais (approximately \$250,000 at the foreign exchange rate as of April 30, 2016), excluding interest. The municipality claims that the Brazilian subsidiary rendered certain services within the municipality of São Paulo but simulated that those services were rendered in another city. At the end of December 2010 the municipality issued further tax assessments alleging the same claims for 2005 through June 2007. These additional subsequent claims assert services tax deficiencies and related penalties totaling 5.9 million Brazilian reais (approximately \$1.7 million at the foreign exchange rate as of April 30, 2016), excluding interest. We received unfavorable decisions from the administrative courts, which ruled to maintain the tax assessments for each of these matters. No further grounds of appeal are available to us for these assessments within the administrative courts. In October 2012, as a result of the decision at the administrative level, the tax authorities filed an enforcement action in the civil courts to collect on the services tax assessments amounts awarded by the administrative court, and seeking other related costs and fees. On March 6, 2013, we filed our defensive claims in the civil courts in response to the tax authorities' enforcement action. In February 2013 the tax authorities filed an additional enforcement action in the civil courts to collect on the penalties related to the services tax assessments amounts awarded by the administrative courts. Based on our understanding of the underlying facts of this matter and our evaluation of the potential outcome at the judicial level, we believe it is reasonably possible that our Brazilian subsidiary will be required to pay some amount of the alleged tax assessments and penalties related to these matters, as well as amounts of interest and certain costs and fees imposed by the court related thereto. As of April 30, 2016, the amount of the alleged tax assessments and penalties related to these matters was approximately 23.3 million Brazilian reais (approximately \$6.6 million at the foreign exchange rate as of April 30, 2016), including interest, costs and fees related thereto.

The Brazilian subsidiary we acquired as part of our acquisition of Hypercom in August 2011 received an unfavorable administrative decision on a tax enforcement action against it filed by the municipality of Curitiba for collection of alleged services tax deficiency. An appeal against this unfavorable administrative decision was filed in a judicial proceeding and currently the case is pending the municipality of Curitiba's compliance with the writ of summons. As of April 30, 2016, the underlying assessment, including estimated interest, was approximately 5.4 million Brazilian reais (approximately \$1.5 million at the foreign exchange rate as of April 30, 2016). Based on our current understanding of the underlying facts of this matter, we believe it is reasonably possible that we may receive an unfavorable decision in this proceeding.

Patent Infringement Claims

Cardsoft, Inc. et al v. VeriFone Holdings, Inc., VeriFone, Inc., Hypercom Corporation, et al.

On March 6, 2008, Cardsoft, Inc. and Cardsoft (Assignment for the Benefit of Creditors), LLC (collectively, "Cardsoft") commenced an action in the United States District Court for the Eastern District of Texas, Marshall Division, against us and Hypercom Corporation, among others, alleging infringement of U.S. Patents No. 6,934,945 and No. 7,302,683 purportedly owned by Cardsoft. Cardsoft sought, in its complaint, a judgment of infringement, an injunction against further infringement, damages, interest and attorneys' fees. On June 8, 2012, the jury returned an unfavorable verdict finding that Cardsoft's patents were valid and were infringed by the accused VeriFone and Hypercom devices, and further determined that a royalty rate of \$3 per unit should be applied. Accordingly, the jury awarded Cardsoft infringement damages and royalties of approximately \$15.4 million covering past sales of the accused devices by

VeriFone and Hypercom. The jury concluded there was no willful infringement by either VeriFone or Hypercom.

Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Following the jury's verdict, we determined that it was probable we would incur a loss on this litigation based on the jury's verdict and the status of the litigation proceedings at that time. Accordingly, we accrued for the full amount of the jury's verdict plus estimated pre-judgment interest and, effective from July 31, 2012, we began accruing estimated ongoing royalties of \$3 per unit of accused device to Cost of net revenues. During the fiscal quarter ended October 31, 2012, we completed redesigns of the terminals subject to the jury's verdict specifically to address the Cardsoft allegations, and implemented such redesigns in the U.S. We further obtained the legal opinion of independent intellectual property counsel that our terminals, as redesigned, do not infringe the Cardsoft patents-in-suit. We concluded based on the procedures taken and legal reviews obtained, that it was not probable that an ongoing royalty based on the jury's verdict applies to our terminals as redesigned, and ceased accruing an ongoing royalty.

On October 30, 2013, the District Court issued judgment upholding the jury's verdict that the patent was valid and infringed. The judgment confirmed the jury's award of infringement damages and royalties of approximately \$15.4 million covering past sales of the VeriFone and Hypercom accused devices, plus pre-judgment interest, post-judgment interest and costs. The court also ruled that an ongoing royalty should be applied for sales of the accused devices after the verdict date and ordered the parties to mediate on the issue of an ongoing royalty rate. The parties participated in mediation but were unable to reach a resolution. In March 2014, Cardsoft filed a motion requesting the court to set an ongoing royalty rate. We opposed, arguing (among other things) that no ongoing royalty applies in light of our redesigns of the products subject to the District Court's infringement ruling.

We appealed the District Court's judgment to the U.S. Court of Appeals for the Federal Circuit. On October 17, 2014, a three-judge panel of the Federal Circuit issued a unanimous opinion in our favor. The Federal Circuit ruling reversed the District Court's judgment and, further, concluded that our products did not infringe the Cardsoft patents as a matter of law. As a result, the District Court's finding of infringement and order of past and ongoing royalties, as well as related interest and costs, have been reversed. Previously, based on our assessment and the status of this matter before the District Court, we had accrued a total estimated loss of approximately \$20.0 million, including estimated pre-judgment interest, potential ongoing royalties and statutory post-judgment interest related to this litigation. As a result of the Federal Circuit's favorable opinion reversing the District Court's judgment and ruling that our products do not infringe as a matter of law, in October 2014, we reversed the total estimated loss previously accrued.

On December 22, 2014, the Federal Circuit denied Cardsoft's petition for rehearing by the panel and hearing en banc, and issued its mandate on December 29, 2014. On March 23, 2015, Cardsoft filed a petition for certiorari with the U.S. Supreme Court, requesting the Court to grant its petition, vacate the Federal Circuit's decision and remand for the Federal Circuit to review using a more deferential standard of review of the District Court's claim construction. On June 29, 2015, the U.S. Supreme Court granted Cardsoft's petition, vacated the Federal Circuit's decision and remanded the case to the Federal Circuit for reconsideration under a more deferential standard of review of the District Court's claim construction. On August 24, 2015, both parties submitted briefs regarding this more deferential standard of review and its applicability to the case.

Cardsoft also filed motions before the District Court claiming that it was entitled to a new trial to allege infringement under the doctrine of equivalents and seeking to reopen the case before the District Court. We opposed these motions and filed a cross motion to dismiss this matter in its entirety.

On December 2, 2015, the Federal Circuit again granted judgment in our favor of no infringement as a matter of law. Cardsoft did not timely file another petition for certiorari with the U.S. Supreme Court. On April 28, 2016, the District Court entered a Stipulation of Dismissal, and this matter is now concluded.



Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Class Action and Derivative Lawsuits

In re VeriFone Holdings, Inc. Shareholder Derivative Litigation Proceedings

Beginning on December 13, 2007, several actions were filed against certain current and former directors and officers derivatively on our behalf. These derivative lawsuits were filed in: (1) the U.S. District Court for the Northern District of California, as In re VeriFone Holdings, Inc. Shareholder Derivative Litigation, Lead Case No. C 07-6347 MHP, which consolidates King v. Bergeron, et al. (Case No. 07-CV-6347), Hilborn v. VeriFone Holdings, Inc., et al. (Case No. 08-CV-1132), Patel v. Bergeron, et al. (Case No. 08-CV-1133), and Lemmond, et al. v. VeriFone Holdings, Inc., et al. (Case No. 08-CV-1301); and (2) the Superior Court of California, County of Santa Clara, as In re VeriFone Holdings, Inc. Derivative Litigation, Lead Case No. 1-07-CV-100980, which consolidates Catholic Medical Mission Board v. Bergeron, et al. (Case No. 1-07-CV-100980) and Carpel v. Bergeron, et al. (Case No. 1-07-CV-101449). We prevailed in our motion to dismiss the federal derivative claims before the U.S. District Court for the Northern District of California and, on November 28, 2011, in ruling on lead plaintiff's appeal against the district court's judgment dismissing lead plaintiff's derivative claims, the Ninth Circuit issued judgment affirming the dismissal of lead plaintiff's complaint against us. The time period for the lead plaintiff to appeal the Ninth Circuit's judgment has expired.

On October 31, 2008, the state derivative plaintiffs filed their consolidated derivative complaint in the Superior Court of California, County of Santa Clara naming us as a nominal defendant and bringing claims for insider selling, breach of fiduciary duty, unjust enrichment, waste of corporate assets and aiding and abetting breach of fiduciary duty against certain of our current and former officers and directors and our largest stockholder as of October 31, 2008, GTCR Golder Rauner LLC. On February 18, 2009, plaintiff Catholic Medical Mission Board voluntarily dismissed itself from the action. In November 2008, we filed a motion to stay the state court action pending resolution of the parallel federal actions, and the parties agreed by stipulation to delay briefing on the motion to stay until after the issue of demand futility was resolved in the federal derivative case. On June 2, 2011, the court entered a stipulated order requiring the parties to submit a case status report on August 1, 2011 and periodically thereafter. The parties submitted status reports to the court through February 1, 2013 as requested by the court. On January 30, 2013, counsel for plaintiff informed us that Mr. Carpel, the nominal plaintiff, had sold his shares in the company and therefore no longer had standing to maintain a derivative action against us. On February 15, 2013, plaintiff filed a motion for leave to publish notice to our stockholders seeking a new nominal plaintiff. On May 10, 2013, the court adopted its tentative order granting the motion to publish notice, which was formally entered on May 17, 2013. Under the terms of the order, the parties were ordered to publish notice of the potential dismissal of the action and any qualifying shareholder who wishes to intervene must notify the court within ninety days from the formal entry of the order. Otherwise, the action will be dismissed. On August 14, 2013, counsel for the former nominal plaintiff, Mr. Carpel, filed a notice of intent to substitute a new nominal plaintiff, Joel Gerber, into the action. On September 16, 2013, counsel for former plaintiff Carpel filed a motion to substitute a new plaintiff, Joel Gerber, into the action. On October 16, 2013, the court granted the motion and deemed the amended complaint filed as of the same date. Our demurrer to the amended complaint was filed on April 7, 2014. On May 23, 2014, plaintiff filed a statement of non-opposition to our demurrer and filed a motion to stay the action to allow plaintiff to make a demand on our current Board of Directors. We filed our opposition to the motion to stay on June 18, 2014 and plaintiff filed his reply on July 25, 2014.

On December 3, 2014, the Court issued an order sustaining our demurrer and granting plaintiff's motion to stay. Plaintiff made a demand on the Board of Directors on December 23, 2014.

On June 11, 2015, the parties entered into a stipulation of settlement, pursuant to which we agreed to implement certain non-monetary corporate governance reforms and to provide support for plaintiff's request for attorneys' fees. On

December 9, 2015, the Court entered an order and final judgment approving the settlement. The deadline for us to implement the non-monetary corporate governance reforms will be August 5, 2016, unless an appeal is timely filed.

Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

## Israel Securities Class Actions

On January 27, 2008, a class action complaint was filed against us in the Central District Court in Tel Aviv, Israel on behalf of purchasers of our stock on the Tel Aviv Stock Exchange. The complaint sought compensation for damages allegedly incurred by the class of plaintiffs due to the publication of erroneous financial reports. We filed a motion to stay the action, in light of the proceedings already filed in the U.S., on March 31, 2008. A hearing on the motion was held on May 25, 2008. Further briefing in support of the stay motion, specifically with regard to the threshold issue of applicable law, was submitted on June 25, 2008. On September 11, 2008, the Israeli District Court ruled in our favor, holding that U.S. law would apply in determining our liability. On October 7, 2008, plaintiffs filed a motion for leave to appeal the Israeli District Court's ruling to the Israeli Supreme Court. Our response to plaintiffs' appeal motion was filed on January 21, 2009. The Israeli District Court stayed its proceedings until the Israeli Supreme Court rules on plaintiffs' motion for leave to appeal. On January 27, 2010, after a hearing before the Israeli Supreme Court, the court dismissed the plaintiffs' motion for leave to appeal and addressed the case back to the Israeli District Court. The Israeli Supreme Court instructed the Israeli District Court to rule whether the Israel class action should be stayed, under the assumption that the applicable law is U.S. law. Plaintiffs subsequently filed an application for reconsideration of the Israeli District Court's ruling that U.S. law is the applicable law. Following a hearing on plaintiffs' application, on April 12, 2010, the parties agreed to stay the proceedings pending resolution of the U.S. securities class action, without prejudice to plaintiffs' right to appeal the Israeli District Court's decision regarding the applicable law to the Israeli Supreme Court. On May 24, 2010, plaintiff filed a motion for leave to appeal the decision regarding the applicable law with the Israeli Supreme Court. In August 2010, plaintiff filed an application to the Israeli Supreme Court arguing that the U.S. Supreme Court's decision in *Morrison et al. v. National Australia Bank Ltd.*, 561 U.S. 247, 130 S. Ct. 2869 (2010), may affect the outcome of the appeal currently pending before the Court and requesting that this authority be added to the Court's record. Plaintiff concurrently filed an application with the Israeli District Court asking that court to reverse its decision regarding the applicability of U.S. law to the Israel class action, as well as to cancel its decision to stay the Israeli proceedings in favor of the U.S. class action in light of the U.S. Supreme Court's decision in *Morrison*. On August 25, 2011, the Israeli District Court issued a decision denying plaintiff's application and reaffirming its ruling that the law applicable to the Israel class action is U.S. law. The Israeli District Court also ordered that further proceedings in the case be stayed pending the decision on appeal in the U.S. class action.

On November 13, 2011, plaintiff filed an amended application for leave to appeal addressing the Israeli District Court's ruling. We filed an amended response on December 28, 2011. On January 1, 2012, the Israeli Supreme Court ordered consideration of the application by three justices. On July 2, 2012, the Israeli Supreme Court ordered us to file an updated notice on the status of the proceedings in the U.S. securities class action then pending in the U.S. Court of Appeals for the Ninth Circuit by October 1, 2012. On October 11, 2012, we filed an updated status notice in the Israeli Supreme Court on the proceedings in the U.S. securities class action pending at the time in the U.S. Court of Appeals for the Ninth Circuit. On January 9, 2013, the Israeli Supreme Court held a further hearing on the status of the appeal in the U.S. Court of Appeals for the Ninth Circuit and recommended that the parties meet and confer regarding the inclusion of the Israeli plaintiffs in the federal class action pending in the U.S. On February 10, 2013, the Israeli Supreme Court issued an order staying the case pursuant to the joint notice submitted to the court by the parties on February 4, 2013. The plaintiff and putative class members in this action are included in the stipulated settlement of the federal securities class action, *In re VeriFone Holdings, Inc.*, disclosed above unless an individual plaintiff opts out. Following the February 25, 2014 judgment and orders by the U.S. court, on May 1, 2014, the parties in the Israel class action filed a joint motion requesting that the Israeli Supreme Court renew the proceedings on appeal concerning the determination of the applicable law. A hearing was held on June 23, 2014 concerning whether the Israel class action should proceed in light of the settlement in the U.S. class action. On July 27, 2014, the plaintiff filed a supplemental pleading at the court's request. We filed our reply pleading on August 21, 2014, and plaintiff filed a further response pleading on September 4, 2014. On April 2, 2015, the Israeli Supreme Court ruled that the Israeli



class action is estopped by the U.S. class action settlement and dismissed the case.

On May 12, 2015, a new class action complaint was filed against us in Israel alleging similar claims as the dismissed Israeli class action, and alleging that Israeli shareholders were deprived of due process in the U.S. class action settlement proceedings. We are opposing the new class action on substantially the same grounds on which the previous case was dismissed.

Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

On June 29, 2015, the plaintiff in the 2008 Israel Securities Class Action filed a motion for award of compensation and attorneys' fees based on the amount of settlement compensation received by Israelis in the U.S. class action. On January 14, 2016, the Israeli District Court denied this motion. Plaintiff has not timely appealed, and this ruling is now final.

*In re VeriFone Securities Litigation*

On March 7, 2013, a putative securities class action was filed in the U.S. District Court for the Northern District of California against us, certain of our former officers and one of our current officers and alleged claims in connection with our February 20, 2013 announcement of preliminary financial results for the fiscal quarter ended January 31, 2013. The action, captioned *Sanders v. VeriFone Systems, Inc. et al.*, Case No. C 13-1038, and subsequently re-captioned *In re VeriFone Securities Litigation*, was initially brought on behalf of a putative class of purchasers of VeriFone securities between December 14, 2011 and February 19, 2013 and asserted claims under the Securities Exchange Act Sections 10(b) and 20(a) and SEC Rule 10b-5 for securities fraud and control person liability. The claims were based on allegations that we and the individual defendants made false or misleading public statements regarding our business, operations, and financial controls during the putative class period. The complaint sought unspecified monetary damages and other relief. Two additional class actions related to the same matter (*Laborers Local 235 Benefit Funds v. VeriFone Systems, Inc. et al.*, Case No. CV 13-1676 and *Bland v. VeriFone Systems, Inc. et al.*, Case No. CV 13-1853) were filed in April 2013. On May 6, 2013, several putative plaintiffs and plaintiffs' law firms filed motions to consolidate these three securities class actions and requesting appointment as lead plaintiff and lead counsel, respectively. The plaintiffs in *Laborers Local 235 Benefit Funds v. VeriFone Systems, Inc. et al.* and *Bland v. VeriFone Systems, Inc. et al.* voluntarily dismissed their respective actions, without prejudice, on July 10, 2013 and July 17, 2013, respectively, and filed motions to be appointed lead plaintiff in the action previously captioned *Sanders v. VeriFone Systems, Inc. et al.* On October 7, 2013, the court entered an order appointing the Selz Funds as lead plaintiffs and appointing Gold Bennett Cera & Sidener LLP as lead counsel. Lead plaintiffs' first amended complaint was filed on December 16, 2013. The first amended complaint expanded the putative class period to December 14, 2011 and February 20, 2013, inclusive, and removed the current officer who was named in the original complaint from the action. We filed our motion to dismiss the amended complaint on February 14, 2014, lead plaintiffs filed their opposition on April 15, 2014 and we filed our reply on May 16, 2014. On May 27, 2014, the court took the motion to dismiss under submission without oral argument. On August 8, 2014, the court dismissed the amended complaint, with leave to amend. Lead plaintiffs filed their second amended complaint on October 7, 2014. On March 29, 2016, the Court granted our motion to dismiss the second amended complaint, finding it insufficiently pled, and granted leave to amend by June 3, 2016. Instead of filing a third amended complaint, lead plaintiffs are stipulating to a judgment of dismissal with prejudice so they can appeal the court's dismissal of their second amended complaint.

*Dolled v. Bergeron et al.*

On April 19, 2013, a derivative action, *Dolled v. Bergeron et al.*, Case No. 113-CV-245056, was filed in the Superior Court of California, County of Santa Clara in connection with our February 20, 2013 announcement of preliminary financial results for the fiscal quarter ended January 31, 2013. The action, brought derivatively on behalf of VeriFone, names VeriFone as a nominal defendant and brings claims for insider selling, breach of fiduciary duty and unjust enrichment variously against certain of our current and former officers and directors. The complaint seeks unspecified monetary damages, restitution and disgorgement of profits and compensation paid to defendants, injunctive relief directing us to reform its corporate governance, and payment of the plaintiff's costs and attorneys' fees. On May 30, 2013, the court entered the parties' stipulation and proposed order, which appointed plaintiff and plaintiff's counsel as lead plaintiff and lead counsel, respectively, in the consolidated action, captioned *In re VeriFone Systems, Inc.*

Derivative Litigation. The next case management conference is scheduled for September 23, 2016.

Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Zoumboulakis v. McGinn et al.

On May 24, 2013, a federal derivative action, Zoumboulakis v. McGinn et al., Case No. 13-CV-02379, was filed in the U.S. District Court for the Northern District of California against certain current and former directors and officers derivatively on our behalf. The complaint, which names us as a nominal defendant, alleges breach of fiduciary duty and abuse of control and asserts claims under Section 14(a) of the Securities Exchange Act of 1934 for false or misleading financial statements and proxy statement disclosures. The complaint seeks unspecified monetary damages, including exemplary damages, restitution from defendants, injunctive relief directing us to make certain corporate governance reforms, and payment of the plaintiff's costs and attorneys' fees. On August 12, 2013, the court entered defendants' motion seeking to relate this action to the pending shareholder class action, Sanders v. VeriFone Systems, Inc. et al. On October 31, 2013, the court entered a stipulation and order setting a December 31, 2013 deadline for the filing of an amended complaint and setting a January 30, 2014 deadline for defendants to move or answer. An initial case management conference was held on January 17, 2014. On January 21, 2014, plaintiff filed an amended complaint, which removed one of our former officers from the action and added an additional former director as a defendant. The amended complaint brings claims against the defendants for breach of fiduciary duty, abuse of control, violations of Securities Exchange Act Section 14(a), and unjust enrichment. The amended complaint also brings claims for insider trading against three of the named former and current directors. We filed our motion to dismiss the amended complaint on March 7, 2014, plaintiff filed an opposition on April 23, 2014, and we filed our reply on May 16, 2014. On May 27, 2014, the court took the motion to dismiss under submission without oral argument. On August 7, 2014, the court dismissed the amended complaint, with leave to amend. Plaintiff filed a second amended complaint on October 17, 2014. We filed a motion to dismiss the second amended complaint on December 18, 2014. On December 3, 2015, the court granted our motion to dismiss, with leave to amend. On January 20, 2016, plaintiff filed a third amended complaint alleging demand futility with respect to the current Board. We filed our motion to dismiss on March 1, 2016, which motion is scheduled for hearing on September 29, 2016.

If any of these class action or derivative lawsuits is resolved adversely to us, it could have a material adverse effect on our business, financial condition, results of operations, and cash flows.

Antitrust Investigation

The Competition Commission of India ("CCI") investigated certain complaints made against us alleging unfair practices based on certain provisions in our software development license arrangements in India. We cooperated with requests by the CCI in its investigation. In March 2014, the director general of the CCI investigating the allegations issued a report rejecting certain of the allegations, but also finding that certain provisions of our licenses may constitute unfair business practices. VeriFone India Sales Pvt. Ltd. filed objections to that report.

In April 2015, the CCI issued rulings directing Verifone India to cease and desist from engaging in the alleged anti-competitive conduct and imposing a penalty, the amount of which is not material to our results of operations. We have deposited 10% of this penalty amount and accrued the balance while we appeal these rulings.

On June 15, 2015, we filed appeals and interim applications to stay the CCI orders. The appellate court has granted our interim applications to stay all proceedings at least until the final appellate hearing, which commenced on January 19, 2016, continued on January 29, March 28, and April 28, 2016, and is scheduled to continue on August 4, 2016.

The CCI's rulings reserved the right to pursue additional proceedings against individuals that it deems responsible for the alleged conduct. We are unable to make any estimate of potential loss for any further proceedings the CCI may pursue but do not expect it to be material to our results of operations.



Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

## Other Litigation

Certain of the foregoing cases are still in the preliminary stages, and we are not able to quantify the extent of our potential liability, if any, other than as described above. Further, the outcome of litigation is inherently unpredictable and subject to significant uncertainties. If any of these matters are resolved adversely to us, this could have a material adverse effect on our business, financial condition, results of operations, and cash flows. In addition, defending these legal proceedings is likely to be costly, which may have a material adverse effect on our financial condition, results of operations and cash flows, and may divert management's attention from the day-to-day operations of our business. We are subject to various other legal proceedings related to commercial, customer, and employment matters that have arisen during the ordinary course of business. The outcome of such legal proceedings is inherently unpredictable and subject to significant uncertainties. Although there can be no assurance as to the ultimate disposition of these matters, our management has determined, based upon the information available at the date of these financial statements, including anticipated expected availability of insurance coverage, that the expected outcome of these matters, individually or in the aggregate, will not have a material adverse effect on our consolidated financial position, results of operations or cash flows.

## Income Tax Uncertainties

As of April 30, 2016, the amount payable for unrecognized tax benefits was \$37.7 million, including accrued interest and penalties, none of which is expected to be paid within one year. This amount is included in Other long-term liabilities in our Condensed Consolidated Balance Sheet as of April 30, 2016. We are unable to make a reasonably reliable estimate as to when cash settlement with a taxing authority may occur.

## Note 12. Segment Information

In December 2015, we realigned our organizational structure and changed our reportable segments to be Verifone Systems and Verifone Services. Net revenues and operating income of each segment reflect net revenues and expenses that are directly attributable to that segment. Net revenues and expenses not allocated to segment net revenues and segment operating income include amortization of purchased intangible assets, amortization of step-down in deferred services net revenues and associated costs of net revenues at acquisition, restructuring expenses, stock-based compensation, as well as general and administrative and corporate research and development expense. We do not separately evaluate assets by segment, and therefore assets by segment are not presented below.

The following table sets forth net revenues for our reportable segments and reconciles segment net revenues to total net revenues (in thousands):

	Three Months Ended April 30,		Six Months Ended April 30,	
	2016	2015	2016	2015
Segment net revenues:				
Verifone Systems	\$342,443	\$324,300	\$680,035	\$637,700
Verifone Services	189,913	165,966	365,877	339,480
Total segment net revenues	532,356	490,266	1,045,912	977,180
Amortization of step down in deferred services net revenues at acquisition	(6,078)	(122)	(6,095)	(810)
Total net revenues	\$526,278	\$490,144	\$1,039,817	\$976,370

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The following table sets forth operating income for our reportable segments and reconciles segment operating income to consolidated operating income (in thousands):

	Three Months Ended April 30,		Six Months Ended April 30,	
	2016	2015	2016	2015
Operating income by segment:				
Verifone Systems	\$77,969	\$78,592	\$158,870	\$151,005
Verifone Services	46,446	38,535	88,575	81,351
Total segment operating income	124,415	117,127	247,445	232,356
Items not attributable to segment operating income:				
Amortization of step down in deferred services gross margin at acquisition	(4,408 )	(122 )	(4,425 )	(810 )
Unallocated general and administrative expenses	(49,891 )	(45,632 )	(97,835 )	(87,887 )
Unallocated research and development expenses	(4,705 )	(5,215 )	(9,593 )	(10,476 )
Other unallocated costs	(7,684 )	(1,020 )	(7,671 )	(4,350 )
Amortization of purchase intangible assets	(25,794 )	(25,176 )	(49,409 )	(52,168 )
Stock-based compensation expense	(11,579 )	(8,872 )	(22,039 )	(21,027 )
Litigation settlement and loss contingency expense	—	(1,213 )	—	(1,213 )
Restructuring expense	(575 )	(161 )	(478 )	(1,534 )
Total operating income	\$19,779	\$29,716	\$55,995	\$52,891

Table of Contents

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

This section should be read in conjunction with our consolidated financial statements and related notes included in our 2015 Annual Report on Form 10-K and the Condensed Consolidated Financial Statements and Notes included in Part I, Item I of this Quarterly Report on Form 10-Q. This section and other parts of this Quarterly Report on Form 10-Q and certain information incorporated by reference herein contain forward-looking statements that involve risks and uncertainties. In some cases, forward-looking statements can be identified by words such as "may," "should," "expect," "plan," "intend," "anticipate," "believe," "estimate," "predict," "potential," or "continue," the negative of such terms, or comparable terminology. Such forward-looking statements are based on current expectations, estimates, and projections about our industry and management's beliefs and assumptions, and do not reflect the potential impact of any mergers, acquisitions, or other business combinations or divestitures that have not been completed.

Forward-looking statements are not guarantees of future performance, and our actual results may differ materially from the results expressed or implied in the forward-looking statements. Factors that might cause such differences include, but are not limited to, those discussed in Part I, Item 1A, Risk Factors, in our 2015 Annual Report on Form 10-K and in Part II, Item 1A, Risk Factors, of this Quarterly Report on Form 10-Q, and elsewhere in these reports, including our disclosures of Critical Accounting Policies and Estimates in Part II, Item 7 in our 2015 Annual Report on Form 10-K and in Part I, Item 2 of this Quarterly Report on Form 10-Q, and our disclosures in Part II, Item 7A, Quantitative and Qualitative Disclosures About Market Risk in our 2015 Annual Report on Form 10-K and in Part I, Item 3, Quantitative and Qualitative Disclosures About Market Risk of this Quarterly Report on Form 10-Q, as well as in our Condensed Consolidated Financial Statements and Notes thereto. We are under no duty to update any of the forward-looking statements after the date of this Quarterly Report on Form 10-Q to conform such statements to actual results or to changes in expectations. We assume no obligation to revise or update any forward-looking statements for any reason, except as required by law.

In this Quarterly Report on Form 10-Q, each of the terms "VeriFone," "Company," "us," "we," and "our" refers to VeriFone Systems, Inc. and its consolidated subsidiaries.

Our Management's Discussion and Analysis of Financial Condition and Results of Operations is provided in addition to our Condensed Consolidated Financial Statements and accompanying notes to assist readers in understanding our results of operations, financial condition, and cash flows. This section is organized as follows:

Overview: Discussion of our business, significant matters, and financial results highlights for the periods presented.

Results of Operations:

Consolidated Results of Operations: An analysis and discussion of our financial results comparing our consolidated results of operations for the three and six months ended April 30, 2016 to the three and six months ended April 30, 2015.

Segment Results of Operations: An analysis and discussion of our financial results comparing the results of operations for each of our two reportable segments, Verifone Systems and Verifone Services, for the three and six months ended April 30, 2016 to the three and six months ended April 30, 2015.

Financial Outlook: A discussion of our expectations regarding certain trends that may affect our financial condition and results of operations.

Liquidity and Capital Resources: An analysis of changes in our balance sheets and cash flows, and discussion of our financial condition and potential sources of liquidity.

Contractual Obligations and Off-Balance Sheet Arrangements: Disclosures related to our contractual obligations, contingent liabilities, commitments, and off-balance-sheet arrangements, as of April 30, 2016.

Critical Accounting Policies and Estimates: A discussion of the accounting policies and estimates that we believe are most important to understanding the assumptions and judgments incorporated in our reported financial results and forecasts, as well as recent accounting pronouncements that have had or are expected to have a material impact on our results of operations.





## Table of Contents

### Overview

### Our Business

We are a global leader in payments and commerce solutions. We provide expertise, solutions and services that reduce risk and add value at the retail point-of-sale (POS), and enable innovative forms of commerce. For over 30 years, we have been a leader in designing, manufacturing, marketing and supplying a broad range of innovative payment devices and complementary services that enable secure electronic payment transactions and value-added services at the POS. We focus on delivering increasingly innovative POS payment capabilities, value-added services that increase merchant revenues and enhance the consumer experience, and solutions that enrich the interaction between merchants and consumers. For example, during April 2016 we introduced the first of a new family of integrated POS systems, known as Verifone Carbon, that we expect will provide more scalable solutions for our clients globally. Key industries in which we operate include financial services, retail, petroleum, restaurant, hospitality, taxi, transportation, and healthcare.

During December 2015 our Chief Executive Officer realigned the company's organizational structure to focus on two global product lines: Verifone Systems and Verifone Services. Verifone Systems delivers point of sale electronic payment devices that run our unique operating systems, security and encryption software, and certified payment software for payments and commerce. Verifone Services delivers device related leasing and maintenance, payment transaction routing and reporting, and commerce based services such as advertising on digital screens. As a result of this organizational change, effective for the first quarter of 2016, our reportable segments are Verifone Systems and Verifone Services. All prior period amounts reported by geographic segment have been reclassified to conform to the current presentation.

The markets in which we operate are highly competitive. We compete based on various factors, including product functions and features, pricing, product quality and reliability, design innovation, interoperability with third-party systems and brand reputation. We also compete based on product availability and certifications, as well as service offerings and support. We continue to experience intense competition in Verifone Systems from traditional POS terminal providers and we also see new companies entering our markets, including entrants offering various forms of mobile device based payment options. In certain geographic markets, such as China and Brazil, we see customers requiring a choice of offerings for a lower cost. This trend has increased competition and pricing pressures. Our competitors are introducing increasingly aggressive pricing in these markets and clients are relying more on pricing for their purchase decisions.

### Verifone Systems

Sales of our point of sale electronic payment devices and systems by our Verifone Systems business comprise approximately 65.1% and 65.4% of our net revenues in the three and six months ended April 30, 2016, respectively. Our point of sale electronic payment devices run our unique operating systems, security and encryption software, and certified payment software, and are designed to suit our clients' needs in a variety of environments, including traditional multi-lane and countertop implementations, self-service and unattended environments, in-vehicle and portable deployments, as well as mobile commerce. Our systems can securely process a wide range of payment types including signature and PIN-based debit cards, credit cards, NFC/contactless/radio frequency identification cards, or RFID cards, smart cards, pre-paid gift and other stored-value cards, electronic bill payment, signature capture and electronic benefits transfer, or EBT. Our unique architecture enables multiple value-added applications, including third-party applications, such as gift card and loyalty card programs, healthcare insurance eligibility, and time and attendance tracking, and allows these applications to reside on the same system without requiring recertification upon the addition of new applications. With our newest line of Verifone Engage payment solutions, we will be able to deliver richer media and more complex commerce enablement services on our payment terminals to our merchant

clients. Security continues to be an important factor for our clients and we have experienced increasing demand for Europay, MasterCard and Visa, or "EMV", capable terminal solutions.

## Table of Contents

### Verifone Services

Verifone Services drives an important part of our business and revenues, accounting for approximately 34.9% and 34.6% of our net revenues in the three and six months ended April 30, 2016, respectively. Our service offerings fall into four main product lines: (i) device-related services, (ii) payment-related services, (iii) commerce-related services, and (iv) omni-commerce services. Device-related services include mechanical and support services such as terminal leasing, “break fix” maintenance work, and call center support. Payment-related services include transaction routing, software development and licensing, and security services, such as encryption, tokenization, and our Secure Commerce Architecture. Commerce-related services include our digital media business, which delivers advertising and marketing content to over 100,000 screens, and taxi related services such as mobile hailing. Omni-commerce services bring together payments and commerce both in-store and online.

### Timing of Revenue

The timing of our customer orders may cause our revenue to vary from period to period. Specifically, revenues recognized in our fiscal quarters can vary significantly when larger customers or our distributors delay orders due to regulatory and industry standards compliance, budget considerations, product feature availability, dual vendor sourcing requirements, technology refresh cycles, economic conditions or other concerns that impact their business or purchasing decisions. For example, the timing of customer orders is often impacted by the timing of technology refreshes or the timing of completed product certifications by a particular customer or in a particular market. Customer purchases have also been impacted by regulatory factors such as new or pending banking regulations and government initiatives to drive cashless transactions.

In addition, revenues can be back-end weighted when we receive sales orders and deliver a higher proportion of our systems toward the end of our fiscal quarters. This variability and back-end weighting of orders may adversely affect our results of operations in a number of ways, and could negatively impact revenues and profits. First, the product mix of orders may not align with manufacturing forecasts, which could result in a shortage of the components needed for production. Second, existing manufacturing capacity may not be sufficient to deliver the desired volume of orders in a concentrated time when they are received. Third, back-end weighted demand could negatively impact gross margins through higher labor, delivery, and other manufacturing and distribution costs. If, on the other hand, we were to seek to manage the fulfillment of back-end weighted orders through holding increased inventory levels, we would risk higher inventory obsolescence charges if our sales fall short of our expectations.

Because our revenue recognition depends on, among other things, the timing of product shipments, decisions we make about product shipments, particularly toward the end of a fiscal quarter, may impact our reported revenues. The timing of product shipments may depend on a number of factors, including costs of air shipments if required, the delivery date requested by customers, and our operating capacity to fill orders and ship products, as well as our own long and short-term business planning and supply chain management. These factors may affect timing of shipments and consequently revenues recognized for a particular period.

### Significant Matters

#### Business Combinations

On December 23, 2015, we acquired InterCard AG, a leading payment-related services provider in Germany, in exchange for 85.0 million Euro in cash paid on the acquisition date (approximately \$92.4 million at the foreign exchange rate on the acquisition date) plus 1.2 million Euro (approximately \$1.4 million at the foreign exchange rate as of April 30, 2016), that will be paid in the third quarter of fiscal 2016. We acquired InterCard to expand our payment-related services offerings in Germany. This acquisition was accounted for using the acquisition method of

accounting, and the results of InterCard were included in our Results of Operations since the acquisition date.

## Table of Contents

On February 2, 2016, we acquired AJB Software Design Inc., a Toronto-based provider of payment gateway and switching solutions for large merchants in the U.S. and Canada, for cash payments totaling approximately \$87.5 million, subject to certain upward adjustments, plus up to \$10.0 million of additional contingent consideration with a fair value of \$1.4 million at the acquisition date. We acquired AJB to expand our suite of services offerings. This acquisition was accounted for using the acquisition method of accounting, and the results of AJB were included in our Results of Operations since the acquisition date.

### Stock Repurchase Program

In September 2015, our Board of Directors authorized a program to repurchase shares of our common stock with an aggregate value of up to \$200.0 million, with no expiration from the date of authorization. During the six months ended April 30, 2016, we repurchased approximately 2.6 million shares of our common stock on the open market at an average repurchase price of \$28.02 per share. There were no stock repurchase activities during the three months ended April 30, 2016. As of April 30, 2016, there was approximately \$50.0 million remaining available for stock repurchases under this program.

Pursuant to this program, shares may be repurchased from time to time in the open market, private purchases, through forward, derivative, accelerated repurchase or automatic repurchase transactions or otherwise. The timing and actual amount of the share repurchases will depend on several factors including price, capital availability, regulatory requirements, alternative investment opportunities, including mergers and acquisitions, market conditions and other factors. We are not obligated to repurchase any specific number of shares under the program and the repurchase program may be modified, suspended or discontinued at any time. See Note 4, Stock Repurchase Program, in the Notes to Condensed Consolidated Financial Statements of this Quarterly Report on Form 10-Q for additional information regarding this stock repurchase program.

### Financial Results Highlights

#### Overall

Consolidated net revenues for the three months ended April 30, 2016 were \$526.3 million, compared to \$490.1 million for the three months ended April 30, 2015, up 7.4% year over year, despite a \$26.2 million unfavorable foreign currency impact.

Gross margins for the three months ended April 30, 2016 were \$210.4 million or 40.0% compared to \$203.9 million or 41.6% for the three months ended April 30, 2015, up \$6.5 million or 3.2%, but down 1.6 points.

Net cash provided by operating activities for the three months ended April 30, 2016 totaled \$50.9 million.

Table of Contents

## Results of Operations

## Consolidated Results of Operations

## Three Months Ended April 30, 2016 compared to April 30, 2015

	Three Months Ended April 30, 2016		Three Months Ended April 30, 2015	
		% of Net revenues <sup>(1)</sup>		% of Net revenues <sup>(1)</sup>
	(in thousands, except percentages)			
Net revenues:				
Systems	\$342,443	65.1%	\$324,300	66.2%
Services	183,835	34.9%	165,844	33.8%
Total net revenues	526,278	100.0%	490,144	100.0%
Gross margin:				
Systems	141,899	41.4%	135,328	41.7%
Services	68,480	37.3%	68,575	41.3%
Total gross margin	210,379	40.0%	203,903	41.6%
Operating expenses:				
Research and development	54,715	10.4%	47,579	9.7%
Sales and marketing	59,027	11.2%	55,371	11.3%
General and administrative	54,884	10.4%	49,457	10.1%
Litigation settlement and loss contingency expense	—	—%	1,213	0.2%
Amortization of purchased intangible assets	21,974	4.2%	20,567	4.2%
Total operating expenses	190,600	36.2%	174,187	35.5%
Operating income	19,779	3.8%	29,716	6.1%
Interest expense, net	(8,543)	(1.6)%	(7,432)	(1.5)%
Other income (expense), net	(4,809)	(0.9)%	(3,169)	(0.6)%
Income before income taxes	6,427	1.2%	19,115	3.9%
Income tax provision	3,087	0.6%	1,449	0.3%
Consolidated net income	\$3,340	0.6%	\$17,666	3.6%

(1) Systems and Services gross margin as a percentage of net revenues is computed as a percentage of the corresponding Systems and Services net revenues.

Net revenues for the three months ended April 30, 2016 were \$526.3 million, compared to \$490.1 million for the three months ended April 30, 2015, up \$36.2 million or 7.4%, net of a \$26.2 million negative foreign currency impact. Systems net revenues increased \$18.2 million due primarily to increased demand for EMV capable products in North America. Services net revenues increased \$18.0 million due primarily to the benefit of acquired businesses and sales of additional services on increased device sales. The foreign currency impact was due primarily to a decrease in the value of the Brazilian real, the Argentine peso, the South African rand, and the Australian dollar. (See further discussion of revenues by segment and geography below.)

Table of Contents

## Net Revenues by Geography

Three Months Ended April 30,  
2016      % of net revenues    2015      % of net revenues  
(in thousands, except percentages)

## Net Revenues

North America	\$209,338	39.8%	\$192,970	39.4%
Latin America	69,788	13.3%	68,054	13.9%
EMEA	196,982	37.4%	179,531	36.6%
Asia-Pacific	50,170	9.5%	49,589	10.1%
Total	\$526,278	100.0%	\$490,144	100.0%

North America net revenues increased \$16.4 million year over year, due primarily to increased demand for our EMV capable products, including petroleum customers upgrading to products that support EMV requirements and increasing adoption of EMV capable devices by small and medium businesses, which outpaced the prior year revenues from EMV implementations by Tier 1 retailers.

Latin America net revenues increased \$1.7 million year over year, despite \$16.3 million of unfavorable foreign currency fluctuations. Net revenue increases throughout Latin America markets were offset by a \$11.3 million decrease in net revenues in Brazil that was influenced by factors such as economic weakness and competitive pricing pressures.

EMEA net revenues increased \$17.5 million year over year, due primarily to \$12.7 million in net revenues from InterCard, which was acquired in December 2015. Net revenues also increased due to the timing of product certifications in certain countries, for example, increased demand for our products due to government fiscalization requirements in Turkey. EMEA net revenues include a \$6.2 million negative impact due to unfavorable foreign currency fluctuations.

Asia-Pacific net revenues remained relatively flat year over year. Increases in net revenues in some Asia-Pacific markets were almost entirely offset by a \$6.0 million decrease in net revenues in China, where we have not yet released a lower cost suite of products to meet customer preferences in that market. Net revenues include a \$3.5 million negative impact due to unfavorable foreign currency fluctuations.

Gross margin for the three months ended April 30, 2016 was \$210.4 million or 40.0% of total net revenues, compared to \$203.9 million or 41.6% of total net revenues, for the three months ended April 30, 2015, up \$6.5 million but down 1.6 percentage points. Gross margin in dollars increased due primarily to the increase in net revenues. Gross margin as a percentage of net revenues decreased due primarily to changes in product, geographic and customer mix. For example, we experienced competitive pricing pressures in several markets, particularly Latin America, that have resulted in lower margins year over year. In addition, in North America net revenues have shifted to more purchases by our distributors and petroleum customers in the current year compared to net revenues from higher margin large customers completing substantial EMV roll outs in the prior year.

Research and development for the three months ended April 30, 2016 was \$54.7 million compared to \$47.6 million for the three months ended April 30, 2015, up \$7.1 million or 14.9%, due primarily to an increase in personnel related and outside contractor expenses, which reflects our ongoing investment in additional resources to develop and bring next generation products and solutions to market.



Sales and marketing for the three months ended April 30, 2016 was \$59.0 million, compared to \$55.4 million for the three months ended April 30, 2015, up \$3.6 million or 6.5%, due primarily to costs associated with the recent acquisitions of InterCard and AJB.

General and administrative for the three months ended April 30, 2016 was \$54.9 million, compared to \$49.5 million for the three months ended April 30, 2015, up \$5.4 million or 10.9%, due primarily to costs associated with the recent acquisitions of InterCard and AJB.

Amortization of purchased intangible assets for the three months ended April 30, 2016 was \$22.0 million, compared to \$20.6 million for the three months ended April 30, 2015, up \$1.4 million or 6.8%, due primarily to an increase in purchased intangible assets associated with recently acquired businesses.

Interest expense, net for the three months ended April 30, 2016 was \$8.5 million, compared to \$7.4 million for the three months ended April 30, 2015, up \$1.1 million or 14.9%, due primarily to higher loan balances related to new borrowings for acquisitions.

Table of Contents

Income tax provision for the three months ended April 30, 2016 was \$3.1 million, compared to \$1.4 million for the three months ended April 30, 2015, up \$1.7 million or 117.3%. The income tax provisions for the three months ended April 30, 2016 and 2015 were primarily related to foreign taxes and other discrete activities.

## Six Months Ended April 30, 2016 compared to April 30, 2015

	Six Months Ended April 30,			
	2016	% of net revenues <sup>(1)</sup>	2015	% of net revenues <sup>(1)</sup>
	(in thousands, except percentages)			
Net revenues:				
Systems	\$680,035	65.4%	\$637,700	65.3%
Services	359,782	34.6%	338,670	34.7%
Total net revenues	1,039,817	100.0%	976,370	100.0%
Gross margin:				
Systems	284,686	41.9%	263,060	41.3%
Services	140,978	39.2%	140,013	41.3%
Total gross margin	425,664	40.9%	403,073	41.3%
Operating expenses:				
Research and development	106,383	10.2%	96,482	9.9%
Sales and marketing	113,976	11.0%	112,781	11.6%
General and administrative	107,710	10.4%	96,807	9.9%
Litigation settlement and loss contingency expense (benefit)	—	—%	1,213	0.1%
Amortization of purchased intangible assets	41,600	4.0%	42,899	4.4%
Total operating expenses	369,669	35.6%	350,182	35.9%
Operating income	55,995	5.4%	52,891	5.4%
Interest expense, net	(16,847)	(1.6)%	(15,327)	(1.6)%
Other income (expense), net	(6,989)	(0.7)%	(2,926)	(0.3)%
Income before income taxes	32,159	3.1%	34,638	3.5%
Income tax provision	5,086	0.5%	2,844	0.3%
Consolidated net income	\$27,073	2.6%	\$31,794	3.3%

(1) Systems and Services gross margin as a percentage of net revenues is computed as a percentage of the corresponding Systems and Services net revenues.

Net revenues for the six months ended April 30, 2016 were \$1.04 billion, compared to \$976.4 million for the six months ended April 30, 2015, up \$63.4 million or 6.5%, net of a \$62.8 million negative foreign currency impact. Systems net revenues increased \$42.3 million due primarily to increased demand for EMV capable products in North America. Services net revenues increased \$21.0 million due primarily to the benefit of acquired businesses and sales of additional services on increased device sales. The foreign currency impact was due primarily to a decrease in the values of the Brazilian real, the Argentine peso, the Euro, and the South African rand. (See further discussion of revenues by segment and geography below.)

Table of Contents

## Net Revenues by Geography

	Six Months Ended April 30,			
	2016	% of net revenues	2015	% of net revenues
	(in thousands, except percentages)			
Net Revenues				
North America	\$445,034	42.8%	\$353,267	36.2%
Latin America	124,568	12.0%	139,150	14.3%
EMEA	367,370	35.3%	359,564	36.8%
Asia-Pacific	102,845	9.9%	124,389	12.7%
Total	\$1,039,817	100.0%	\$976,370	100.0%

North America net revenues increased \$91.8 million, due primarily to increased demand for our EMV capable products, including petroleum customers upgrading to products that support EMV requirements and increasing adoption of EMV capable devices by small and medium businesses, which outpaced the prior year revenues from EMV implementations by Tier 1 retailers.

Latin America net revenues decreased \$14.6 million, due primarily to the timing of purchase decisions by large customers. Decreased net revenues in Brazil, which were influenced by factors such as economic weakness and competitive pricing pressures, were partially offset by increases throughout Latin American markets. Net revenues include a \$29.4 million negative impact due to unfavorable foreign currency fluctuations.

EMEA net revenues increased \$7.8 million, due primarily to \$17.0 million in net revenues from InterCard, which was acquired in December 2015. Revenue also increased in the rest of EMEA due primarily to timing of product certifications in certain countries, for example, increased demand for our products due to government fiscalization requirements in Turkey. Net revenues include a \$23.4 million negative impact due to unfavorable foreign currency fluctuations.

Asia-Pacific net revenues decreased \$21.5 million, primarily in China, where we have not yet released a lower cost suite of products to meet customer preferences in that market. Net revenues include a \$9.3 million negative impact due to the unfavorable foreign currency fluctuations.

Gross margin for the six months ended April 30, 2016 was \$425.7 million or 40.9% of net revenues, compared to \$403.1 million, or 41.3% of net revenues, for the six months ended April 30, 2015, up \$22.6 million but down 0.4 percentage points. Gross margin in dollars increased due primarily to the increase in net revenues. Gross margin as a percentage of net revenues decreased due primarily to changes in geographic and customer mix. For example, we experienced competitive pricing pressures in several markets, particularly China and Latin America, that have resulted in lower margins year over year. In addition, in North America net revenues have shifted to more purchases by our distributors and Petro customers in the current year compared to net revenues from higher margin large customers completing substantial EMV roll outs in the prior year.

Research and development for the six months ended April 30, 2016 was \$106.4 million compared to \$96.5 million for the six months ended April 30, 2015, up \$9.9 million or 10.3%, due primarily to an increase in personnel related and outside contractor expenses, which reflects our ongoing investment in additional resources to develop and bring next generation products and solutions to market.

Sales and marketing for the six months ended April 30, 2016 was \$114.0 million, compared to \$112.8 million for the six months ended April 30, 2015, up \$1.2 million or 1.1%, due primarily to costs associated with the recent

acquisitions of InterCard and AJB.

General and administrative for the six months ended April 30, 2016 was \$107.7 million compared to \$96.8 million for the six months ended April 30, 2015, up \$10.9 million or 11.3%, due primarily to costs associated with the recent acquisitions of InterCard and AJB.

Amortization of purchased intangible assets for the six months ended April 30, 2016 was \$41.6 million compared to \$42.9 million for the six months ended April 30, 2015, down \$1.3 million or 3.0%, due primarily to the devaluation of the Euro, Swedish krona, South African rand, and Norwegian krone against the U.S. dollar year over year, as most of our purchased intangible assets are denominated in these currencies. The devaluation was partially offset by an increase in purchased intangible assets associated with recently acquired businesses.

Table of Contents

Interest expense, net for the six months ended April 30, 2016 was \$16.8 million compared to \$15.3 million for the six months ended April 30, 2015, up \$1.5 million or 9.8%, due primarily to higher loan balances related to new borrowings for acquisitions and stock repurchases and lower cash balances.

Income tax provision for the six months ended April 30, 2016 was \$5.1 million, compared to \$2.8 million for the six months ended April 30, 2015, up \$2.3 million or 82.1%. The income tax provision for the six months ended April 30, 2016 was primarily related to foreign taxes and other discrete activities. The income tax provision for the six months ended April 30, 2015 was primarily related to foreign taxes offset by the reversal of unrecognized tax benefits where statutes of limitations expired and audits were settled.

Table of Contents

## Segment Results of Operations

In December 2015, we realigned our organizational structure and changed our reportable segments to be Verifone Systems and Verifone Services. Net revenues and operating income of each segment reflect net revenues and expenses that are directly attributable to that segment. Net revenues and expenses not allocated to segment net revenues and segment operating income include amortization of purchased intangible assets, amortization of step-down in deferred services net revenues and associated costs of net revenues at acquisition, restructuring expenses, stock-based compensation, as well as general and administrative and corporate research and development expense.

## Verifone Systems Net Revenues and Operating Income

Our Verifone Systems business delivers point of sale electronic payment devices that run our unique operating systems, security and encryption software, and certified payment software globally, for both payments and commerce.

## Three Months Ended April 30, 2016 compared to April 30, 2015

	Three Months Ended April 30,			
	2016	% of net revenues	2015	% of net revenues
	(in thousands, except percentages)			
Net revenues	\$342,443	64.3 %	\$324,300	66.2 %
Operating income	\$77,969	22.8 %	\$78,592	24.2 %

Net revenues for the three months ended April 30, 2016 were \$342.4 million, compared to \$324.3 million for the three months ended April 30, 2015, up \$18.2 million or 5.6%, net of a \$17.1 million negative impact due to unfavorable foreign currency fluctuations.

Net revenues from the sale of desktop devices increased \$14.8 million, due primarily to increased demand related to the release of new products and certifications received in certain markets, for example, due to government fiscalization requirements in Turkey, as well as due to the timing of purchase decisions by customers.

Net revenues from the sale of multi-lane devices and our Petroleum product family increased \$5.7 million, due primarily to increased demand for EMV compatible devices. Increased net revenues from customers in the North American petroleum market and small to medium businesses outpaced the decreased demand from North America Tier 1 retailers that rolled out EMV compatible devices in the prior year.

Operating income for the three months ended April 30, 2016 was \$78.0 million or 22.8% of net revenues, compared to \$78.6 million or 24.2% of net revenues for the three months ended April 30, 2015, down \$0.6 million or 1.4 percentage points.

Operating income in dollars decreased due primarily to changes in geographic and product mix, competitive pricing pressures in certain markets, as well as an increased research and development spend, which reflects our ongoing investment in additional resources to bring next generation products and solutions to market.

Operating income as a percentage of net revenues decreased due primarily to changes in geographic and product mix, as well as competitive pricing pressures.



Table of Contents

Six Months Ended April 30, 2016 compared to April 30, 2015

	Six Months Ended April 30,			
	2016	% of net revenues	2015	% of net revenues
	(in thousands, except percentages)			
Net revenues	\$680,035	65.0 %	\$637,700	65.3 %
Operating income	\$158,870	23.4 %	\$151,005	23.7 %

Net revenues for the six months ended April 30, 2016 were \$680.0 million, compared to \$637.7 million for the six months ended April 30, 2015, up \$42.3 million or 6.6%, net of a \$36.3 million negative impact due to unfavorable foreign currency fluctuations.

Net revenues from the sale of desktop devices increased \$28.8 million, due primarily to increased demand related to the release of new products and certifications received in certain markets, for example, due to government fiscalization requirements in Turkey, as well as due to the timing of purchase decisions by customers.

Net revenues from the sale of multi-lane devices and our Petroleum product family increased \$23.3 million, due primarily to increased demand for EMV compatible devices. Increased net revenues from customers in the North American petroleum market and small to medium businesses outpaced the decreased demand from North America Tier 1 retailers that rolled out EMV compatible devices in the prior year.

Net revenues from the sale of portable devices decreased \$12.2 million, primarily in Latin America due to the timing of purchase decisions by large customers, which were influenced, in part, by economic weakness, as well as the impact of foreign currency fluctuations.

Operating income for the six months ended April 30, 2016 was \$158.9 million or 23.4% of net revenues, compared to \$151.0 million or 23.7% of net revenues for the six months ended April 30, 2015, up \$7.9 million but down 0.3 percentage points.

Operating income in dollars increased due primarily to increases in net revenues.

Operating income as a percentage of net revenues decreased due primarily to changes in geographic and customer mix during the six months ended April 30, 2016, as well as an increased research and development spend, which reflects our ongoing investment in additional resources to bring next generation products and solutions to market.



Table of Contents

## Verifone Services Net Revenues and Operating Income

Verifone Services delivers a variety of service solutions that are designed to be complimentary to our systems. These solutions ensure secure electronic payment transactions, provide value-added services to our merchants and enhance the consumer experience. Device-related services include mechanical and support services such as terminal leasing, “break fix” maintenance work, and call center support. Payment-related services include transaction routing, software development and licensing, and security services, such as encryption, tokenization, and our Secure Commerce Architecture. Commerce-related services include our digital media business, which delivers advertising and marketing content to over 100,000 screens, and taxi related services such as mobile hailing.

## Three Months Ended April 30, 2016 compared to April 30, 2015

	Three Months Ended April 30,			
	2016	% of net revenues	2015	% of net revenues
	(in thousands, except percentages)			
Net revenues	\$189,913	35.7 %	\$165,966	33.9 %
Operating income	\$46,446	24.5 %	\$38,535	23.2 %

Net revenues for the three months ended April 30, 2016 were \$189.9 million compared to \$166.0 million for the three months ended April 30, 2015, up \$23.9 million or 14.4%, net of a \$9.1 million negative impact due to unfavorable foreign currency fluctuations.

Net revenues increased \$12.7 million from the acquisition of InterCard in December 2015 and \$6.7 million from the acquisition of AJB in February 2016.

The remaining increase in net revenues is due to growing demand for device-related and payment-related services, particularly in Australia and New Zealand, as additional devices are sold globally.

Operating income for the three months ended April 30, 2016 was \$46.4 million or 24.5% of net revenues, compared to \$38.5 million or 23.2% of net revenues for the three months ended April 30, 2015, up \$7.9 million or 1.3 percentage points.

Operating income in dollars increased due primarily to increases in net revenues.

Operating income as a percentage of net revenues increased due primarily to changes in geographic mix and the higher margins from our recently acquired businesses, InterCard and AJB.

Table of Contents

Six Months Ended April 30, 2016 compared to April 30, 2015

	Six Months Ended April 30,			
	2016	% of net revenues	2015	% of net revenues
	(in thousands, except percentages)			
Net revenues	\$365,877	35.0 %	\$339,480	34.8 %
Operating income	\$88,575	24.2 %	\$81,351	24.0 %

Net revenues for the six months ended April 30, 2016 were \$365.9 million compared to \$339.5 million for the six months ended April 30, 2015, up \$26.4 million or 7.8%, net of a \$26.5 million negative impact due to unfavorable foreign currency fluctuations.

Net revenues increased \$17.0 million from the acquisition of InterCard in December 2015 and \$6.7 million from the acquisition of AJB in February 2016.

The remaining increase in net revenues is due primarily to growing demand for device-related and payment related services solutions as additional devices are sold globally.

Operating income for the six months ended April 30, 2016 was \$88.6 million or 24.2% of net revenues, compared to \$81.4 million or 24.0% of net revenues for the six months ended April 30, 2015, up \$7.2 million or 0.2 percentage points.

Operating income in dollars increased due primarily to increases in net revenues.

Operating income as a percentage of net revenues increased due primarily to changes in geographic mix and the higher margins from our recently acquired businesses, InterCard and AJB.

## Table of Contents

### Financial Outlook

#### Overview

We expect the timing and amount of overall revenue growth to continue to be impacted by factors such as macroeconomic conditions, increased competition and pricing pressures, the timing of new product releases and certifications, the timing of our customers' technology refresh cycles, changes in distribution and distributor inventory levels, and continued uncertain political conditions in certain markets.

#### Global Markets and Competition

As a result of our global customer base, we expect that our net revenues will continue to be impacted by macroeconomic conditions such as foreign currency fluctuations, economic sanctions and other trade restrictions, and changing global oil prices, particularly in certain markets such as Argentina, Brazil, Russia, the Middle East, and Africa. We expect that continued uncertain political conditions in certain markets will have a negative impact on our ability to do business or operate at a desired level.

We expect that the markets in which we conduct our business will remain highly competitive, characterized by changing technologies, evolving industry standards and government regulations that may favor one product or technology over others, and increased demand for new functionality, premium services, mobility, and security. In particular, we expect that there will be continued demand for lower priced products in certain emerging markets, such as Brazil, China and India. We expect the pricing pressures and/or aggressive pricing by competitors that we have seen in recent periods may have significant impact on our net revenues in the future. Market disruptions caused by new technologies, the entry of new competitors, mobile order and pay, the presence of strong local competition, consolidations among our customers and competitors, changes in regulatory requirements, timing of electronic payments initiatives that create demand for our products in emerging markets, new technology entrants, and other factors, can introduce volatility into our business.

#### Our Business and Focus

We continue to focus on expanding our Services offerings globally. We are investing in select markets in order to expand our payment-related services solutions into new countries and to improve the functionality of our payment-related services solutions in existing markets. We also continue to invest in digital media expansion and on commerce enablement solutions, using our consumer-facing point of sale terminals to offer services complementary to our payment solutions that facilitate commerce between merchants and consumers. We expect continued growth in Services net revenues as a result of these efforts. As we transition to more service oriented arrangements, we may experience a shift in the timing of Systems net revenues as revenue recognition will depend on when all of our performance obligations are complete.

We expect the timing of new product releases to continue to have a significant impact on our net revenues. Net revenues can vary significantly when larger customers or distributors cancel or delay orders due to changes in regulatory and industry standards, budget considerations, product feature availability, dual vendor sourcing requirements, technology refresh cycles, economic conditions or other concerns that impact their business or purchasing decisions. Also, demand for electronic payment systems may eventually reach a saturation point, at which time customers might slow or end expansion projects. We expect to generate additional net revenues in the U.S. related to the continued adoption of EMV standards in the future, particularly by the petroleum market and small and medium businesses, and increased desire for mobile payment devices, although the timing of any related revenues will depend on the timing of decisions by merchants. We expect growth in emerging markets as economic conditions improve and those markets make efforts to modernize to cashless payment systems.

As part of our transformation initiatives, we continue to focus on research and development activities and expect to continue at current spend levels as we focus on platform development efforts and gateway consolidation in order to increase standardization, shorten our product development life-cycle and time to market, and also ensure timely certification of our products in each market.

Table of Contents

We plan to continue efforts to improve our cost structure and streamline all aspects of our business, including a strategic review of under-performing products and businesses, as well as consolidating and upgrading some of our global suppliers. In connection with our transformation efforts, we have approved restructuring plans under which we have reduced headcount and closed facilities. We expect to incur additional costs under the previously approved plans and expect to approve additional plans and make strategic changes with regard to some under-performing businesses before our transformation efforts are complete. Our existing and future restructuring plans may generate ongoing savings, some of which will continue to be reinvested into growth initiatives as part of our transformation program. Overall, spending may increase further depending on the costs of any future restructuring plans, costs associated with new acquisitions or ongoing integration of past acquisitions, costs to exit under-performing businesses, as well as costs related to resolving legal and tax matters.

## Table of Contents

### Liquidity and Capital Resources

Our primary liquidity and capital resource needs are to finance working capital, pay for contractual commitments, service our debt, and make capital expenditures and investments. As of April 30, 2016, our primary sources of liquidity were \$156.6 million of cash and cash equivalents, as well as amounts available to us under the revolving loan that is part of our 2011 Credit Agreement.

Cash and cash equivalents as of April 30, 2016 included \$156.4 million held by our foreign subsidiaries. If we decide to distribute or use the cash and cash equivalents held by our foreign subsidiaries outside those foreign jurisdictions, including a distribution to the U.S., we may be subject to additional taxes or costs, or face regulatory restrictions on the amount of cash that can be distributed out of some countries.

We also held \$10.6 million in restricted cash as of April 30, 2016, which was mainly comprised of pledged deposits.

As of April 30, 2016, our outstanding borrowings consisted of a \$547.5 million term A loan, \$196.5 million term B loan, \$218.2 million drawn against a revolving loan commitment, and \$5.4 million under capital leases and other debt. In addition, \$281.8 million was available for draw on the revolving loan commitment, subject to covenant requirements. See Note 9, Financings, in the Notes to Condensed Consolidated Financial Statements of this Quarterly Report on Form 10-Q for additional information regarding our borrowings. We were in compliance with all financial covenants under our credit agreement as of April 30, 2016.

As of April 30, 2016, we had outstanding interest rate swap agreements to effectively convert \$500.0 million of the term A loan from a floating rate plus applicable margin to a 1.20% fixed rate plus applicable margin. The principal amount under the term A loan covered by the new interest rate swap agreements will decrease to \$450.0 million from April 1, 2017 through September 30, 2017, and \$400.0 million from October 1, 2017 through March 30, 2018. See Note 7, Financial Instruments, in the Notes to Condensed Consolidated Financial Statements of this Quarterly Report on Form 10-Q for additional information regarding the swap agreements.

In September 2015, our Board of Directors authorized a program to repurchase shares of our common stock with an aggregate value of up to \$200.0 million, with no expiration from the date of authorization. During the six months ended April 30, 2016 we repurchased approximately 2.6 million shares of our common stock on the open market at an average repurchase price of \$28.02 per share. As of April 30, 2016, there was approximately \$50.0 million remaining available for stock repurchases. The timing and actual amount of the share repurchases will depend on several factors including price, capital availability, regulatory requirements, alternative investment opportunities, including mergers and acquisitions, market conditions and other factors. We are not obligated to repurchase any specific number of shares under the program and the repurchase program may be modified, suspended or discontinued at any time.

On December 23, 2015, in connection with the acquisition of InterCard AG, we paid 85.0 million Euro in cash (approximately \$92.4 million at the foreign exchange rate on the acquisition date.) We will also pay 1.2 million Euro (approximately \$1.4 million at the foreign exchange rate as of April 30, 2016), related to this acquisition during the third quarter of fiscal 2016.

During February 2016 we made cash payments totaling approximately \$87.5 million in connection with the acquisition of AJB.

Our future capital requirements may vary significantly from prior periods as well as from those capital requirements we have currently planned. These requirements will depend on a number of factors, including operating factors such as our terms and payment experience with customers, the timing of annual recurring billings in some markets, the resolution of any legal proceedings against us or settlement of litigation in an amount in excess of our insurance

coverage, costs related to acquisitions, restructuring expenses, stock repurchases and investments we may make in infrastructure, product or market development, or to expand our revenue generating asset base as well as timing and availability of financing. Based upon our current level of operations, we believe that we have the financial resources to meet our business requirements for the next year, including capital expenditures, working capital requirements, future strategic investments and debt servicing costs, stock repurchases, and to maintain compliance with our financial covenants.

Table of Contents

## Bank Guarantees

We have issued bank guarantees with maturities ranging from two months to six years to certain of our customers and vendors as required in some countries to support certain performance obligations under our service or other agreements with those parties. As of April 30, 2016, the maximum amount that may become payable under these guarantees was \$11.9 million, of which \$1.4 million was collateralized by restricted cash deposits.

## Statement of Cash Flows

The net decrease in cash and cash equivalents are summarized in the following table (in thousands):

	Six Months Ended April 30,		
	2016	2015	Change
Net cash provided by (used in):			
Operating activities	\$114,104	\$97,418	\$16,686
Investing activities	(227,974 )	(59,757 )	(168,217 )
Financing activities	60,950	(32,942 )	93,892
Effect of foreign currency exchange rate changes on cash and cash equivalents	619	(20,687 )	21,306
Net decrease in cash and cash equivalents	\$(52,301 )	\$(15,968 )	\$(36,333)

## Operating Activities

Net cash provided by operating activities for the six months ended April 30, 2016 was \$114.1 million, up \$16.7 million from \$97.4 million in cash provided during the six months ended April 30, 2015, primarily due to a \$21.4 million improvement as a result of better working capital management, partially offset by a \$4.7 million decrease in consolidated net income.

## Investing Activities

Net cash used in investing activities for the six months ended April 30, 2016 was \$228.0 million, compared to \$59.8 million for the six months ended April 30, 2015, up \$168.2 million, due primarily to \$158.8 million payments for acquired businesses and a \$9.5 million increase in capital expenditures during the six months ended April 30, 2016, as we invested in additional revenue generating assets to support our services businesses.

## Financing Activities

Net cash provided by financing activities for the six months ended April 30, 2016 was \$61.0 million, compared to \$32.9 million of cash used for the six months ended April 30, 2015, up \$93.9 million, due primarily to \$182.0 million additional borrowings for business acquisitions and stock repurchases, which was partially offset by stock repurchases totaling \$79.9 million during the six months ended April 30, 2016.



## Table of Contents

### Contractual Obligations

As of April 30, 2016, our contractual obligations consist of obligations under debt, capital leases, operating leases, purchase commitments, and other contractual obligations. There have been no material changes to these obligations outside the ordinary course of business during the three months ended April 30, 2016 compared to the contractual obligations disclosed in Management's Discussion and Analysis of Financial Condition and Results of Operations, as described in our Annual Report in Part II, Item 7 of Form 10-K for the fiscal year ended October 31, 2015.

As of April 30, 2016, the amount payable for unrecognized tax benefits was \$37.7 million, including accrued interest and penalties, none of which is expected to be paid within one year. This amount is included in Other long-term liabilities in our Condensed Consolidated Balance Sheets as of April 30, 2016. We are unable to make a reasonably reliable estimate as to when cash settlement with the applicable taxing authorities may occur.

### Off-Balance Sheet Arrangements

We have no off-balance sheet arrangements, as defined in Item 303(a)(4)(ii) of Regulation S-K.

### Critical Accounting Policies and Estimates

#### General

Management's Discussion and Analysis of Financial Condition and Results of Operations is based upon our Condensed Consolidated Financial Statements, which have been prepared in accordance with U.S. GAAP. Our significant accounting policies are more fully described in Note 1, Principles of Consolidation and Summary of Significant Accounting Policies, in the Notes to Consolidated Financial Statements of our 2015 Annual Report on Form 10-K. There were no changes to our significant accounting policies during the six months ended April 30, 2016.

An accounting policy is deemed to be critical if it requires an accounting estimate to be made based on assumptions about matters that are highly uncertain at the time the estimate is made, and if different estimates that reasonably could have been used, or changes in the accounting estimates that are reasonably likely to occur periodically, could materially impact our Condensed Consolidated Financial Statements. Our critical accounting policies include our more significant estimates and assumptions used in the preparation of our Condensed Consolidated Financial Statements. Our critical accounting policies are described in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations of our 2015 Annual Report on Form 10-K.

On an ongoing basis, we evaluate our critical accounting policies and estimates, including those related to revenue recognition, inventory valuation, allowance for doubtful accounts, warranty reserves, contingencies and litigation, income taxes, accounting for goodwill and long-lived assets, stock-based compensation, business combinations, restructuring and contingent consideration. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

The accounting policies that reflect our more significant estimates, judgments and assumptions and which we believe are the most critical to aid in fully understanding and evaluating our reported financial results for the six months ended April 30, 2016 are discussed below.



## Table of Contents

### Business Combinations

We are required to estimate the fair values assigned to assets acquired and liabilities assumed of acquired companies.

Critical estimates in valuing acquired assets and assumed liabilities include but are not limited to: future expected cash flows from customer contracts, customer lists, distribution agreements, acquired developed technologies, and patents; expected costs to complete development of in process research and development into commercially viable products and estimating the cash flows from those projects when completed; brand awareness and market position, as well as assumptions about the period of time the brand will continue to be used in our product portfolio; customer attrition rates and discount rates.

Future expected cash flow to be generated from an acquired business is estimated based on the current financial performance of the business, then adjusted for expected market participant synergies that can be realized, the expected timing of future cash flows of all of the acquired business' products and services, the expected customer attrition rates, and the future growth rates. The higher the projected cash flows, the higher the value of intangible assets.

Discount rates reflect the nature of our investment and the perceived risk of the underlying cash flows.

### Goodwill

We review the goodwill of our reporting units for impairment annually on August 1 and whenever events or changes in circumstances indicate its carrying amount may not be recoverable.

As a result of the realignment of our business into two new operating segments, Verifone Systems and Verifone Services, we realigned our reporting units during the first quarter of 2016. Verifone Systems represents one reporting unit, and Verifone Services is comprised of two reporting units, Taxi Solutions and Verifone Payment Services. In connection with this reporting unit realignment, during the first quarter of 2016 we also updated our goodwill impairment assessment based on a quantitative analysis. We first evaluated the goodwill of our reporting units immediately prior the realignment and concluded that there was no impairment. We then allocated our goodwill to the new reporting units using a relative fair value approach, and re-confirmed that there is no impairment. Our Taxi Solutions reporting unit, which was allocated \$48.8 million of goodwill, had a fair value approximately 10% above carrying value. The other reporting units, which were each allocated approximately \$500 million of goodwill, had fair values approximately double or more than their carrying values.

Consistent with prior periods, in performing our goodwill impairment assessment, we selected the income approach, specifically the discounted cash flow method, to determine the fair value of each report unit. The DCF method calculates fair value by discounting estimated after-tax cash flows to a present value, using a risk-adjusted discount rate. We believe this method is the most meaningful in conducting our goodwill assessment because we believe it most appropriately measures our income-producing assets. In applying this approach to our accounting for goodwill, we make certain assumptions as to the amount and timing of future expected cash flows, terminal value growth rates, and appropriate discount rates. The amount and timing of future cash flows used in our DCF analysis is based on our most recent long-term forecasts and the expected future financial performance of each reporting unit, including projections of net revenues, cost of net revenues, operating expenses, income taxes, working capital requirements, and capital expenditures. We based our fair value estimates on assumptions we believe to be reasonable, but the future impact of such assumptions is unpredictable and inherently uncertain. Actual future results may differ from those estimates. In addition, we make judgments and assumptions in allocating shared assets and liabilities to determine the carrying values for each of our reporting units. Different judgments or assumptions could result in different carrying values. Considering the sensitivity of the analysis performed, we evaluated the impact of a hypothetical 10% decrease in the estimated fair value of our reporting units and concluded that the estimated fair value of our Taxi Solutions

reporting unit in excess of its carrying value would be approximately nil, and the fair value of our other reporting units remain substantially in excess of their carrying value.

## Table of Contents

Significant changes to our financial outlook, a sustained decline in our stock price, weakening of macroeconomic conditions, or additional changes in our management structure or business strategies could result in changes to our reporting units or goodwill impairment assessment in the future.

In accordance with our accounting policies, during each quarter we perform an interim review for potential impairment indicators. During the second quarter of fiscal year 2016 we concluded that there were no potential impairment indicators for any of our reporting units. However, during the third quarter of fiscal year 2016 management has begun a detailed review of under-performing products and businesses. If, as a result of this review, we decide to change business strategies, particularly in our Taxi Solutions business, which has a fair value approximately 10% above carrying value, it is possible that we could trigger a goodwill impairment.

During the fourth quarter of fiscal year 2016, we will perform our annual goodwill impairment assessment. See further discussion in Note 8, Goodwill and Purchased Intangible Assets, in the Notes to Condensed Consolidated Financial Statements of this Quarterly Report on Form 10-Q.

## Income Taxes

Deferred tax assets and liabilities are recognized for the expected tax consequences of temporary differences between the tax bases of assets and liabilities and their reported amounts using enacted tax rates in effect for the year the differences are expected to reverse. In evaluating our ability to recover our deferred tax assets we consider all available positive and negative evidence including our past operating results, the existence of cumulative losses in past fiscal years, and our forecast of future taxable income in the jurisdictions in which we have operations.

We have placed a valuation allowance on the U.S. deferred tax assets and certain non-U.S. deferred tax assets, because realization of these tax benefits through future taxable income does not meet the more-likely-than-not threshold. We intend to maintain the valuation allowances until sufficient positive evidence exists to support the reversal of the valuation allowances. Due to improvements in the U.S. operating results over the past two years, management believes a reasonable possibility exists that, in the next 12 to 24 months, sufficient positive evidence may become available to reach a conclusion that all or a portion of the U.S. valuation allowance will no longer be needed.

The calculation of our tax liabilities involves dealing with uncertainties in the application of complex tax laws. Our estimate for the potential outcome of any uncertain tax issue is based on the detailed facts and circumstances of each issue. For example, during the fourth quarter of fiscal 2014, the Israeli Tax Authorities issued a tax assessment for 2008 or 2009 claiming there was a business restructuring that resulted in a transfer of some functions, assets and risks from Israel to the U.S. parent company treated as an equity sale. We are appealing the tax assessment and believe the Israeli Tax Authority's assessment position is without merit. We intend to continue to challenge the Israeli Tax Authorities position vigorously. If this matters is litigated and the Israeli Tax Authorities are able to successfully sustain their position, our results of operations and financial condition could be materially and adversely affected. See further discussion in Note 5, Income Taxes, in the Notes to Condensed Consolidated Financial Statements of this Quarterly Report on Form 10-Q.

## Recent Accounting Pronouncements

Information with respect to recent accounting pronouncements may be found in Note 1, Principles of Consolidation and Summary of Significant Accounting Policies, in the Notes to Condensed Consolidated Financial Statements of this Quarterly Report on Form 10-Q.



Table of Contents

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

We are exposed to market risk related to changes in interest rates and foreign currency exchange rates. These exposures may change over time as business practices evolve, and could have a material adverse impact on our financial results. Our exposures to market risk have not changed materially since October 31, 2015.

As of April 30, 2016, we had outstanding interest rate swap agreements to effectively convert \$500.0 million of the term A loan from a floating rate to plus applicable margin to a 1.20% fixed rate plus applicable margin. These interest rate swap agreements will decrease in the future and effectively convert \$450.0 million of the term A loan from a floating rate to a 1.20% fixed rate plus applicable margin from April 1, 2017 through September 30, 2017, and \$400.0 million from October 1, 2017 through March 30, 2018. The swap agreements expire March 30, 2018.

For quantitative and qualitative disclosures about market risk, see Part II Item 7A, Quantitative and Qualitative Disclosures About Market Risk, in our Annual Report on Form 10-K for the fiscal year ended October 31, 2015.

**ITEM 4. CONTROLS AND PROCEDURES**

**Evaluation of Disclosure Controls and Procedures**

Our management, with the participation of our CEO and CFO, has evaluated the effectiveness of our disclosure controls and procedures pursuant to Rule 13a-15 under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on that evaluation, our CEO and CFO have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act), are designed to and are effective to provide reasonable assurance that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in Securities and Exchange Commission rules and forms, and is accumulated and communicated to management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure.

**Changes in Internal Control over Financial Reporting**

There were no changes to our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**Inherent Limitations on Effectiveness of Controls**

Our management, including the CEO and the CFO, does not expect that our disclosure controls or our internal control over financial reporting will prevent or detect all error and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. The design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Further, because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, have been detected. The design of any system of controls is based in part on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Projections of any evaluation of the effectiveness of controls to future periods are subject to risks. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures. Our disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in Securities and Exchange Commission rules and forms, and is accumulated and communicated to

management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure.



Table of Contents

PART II — OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Information with respect to legal proceedings may be found in Note 11, Commitments and Contingencies, in the Notes to Condensed Consolidated Financial Statements of this Quarterly Report on Form 10-Q, which section is incorporated herein by reference.

ITEM 1A. RISK FACTORS

The risks set forth below include risks related to our business and operations, market, economic and political conditions, our legal and regulatory environment, and our capital structure, and may adversely affect our business, financial condition, results of operations and cash flows. In addition to the risks set forth below and the factors affecting specific business operations identified with the description of these operations elsewhere in this report, there may also be risks of which we are currently not aware, or that we currently regard as immaterial based on the information available to us, that later prove to be or become material.

Risks Related to Our Business

If we do not continually enhance our existing solutions and develop and market new solutions and enhancements responsive to technological advancements and customer or end user demand in a timely manner or at all, our net revenues and income will be adversely affected.

The market for electronic payment systems is characterized by:

- rapid technological advancements;
- frequent product introductions and enhancements;
- local certification requirements and product customizations;
- evolving industry and government performance and security standards and regulatory requirements;
- introductions of competitive products, including products that customers may perceive as having better functions and features, and alternative payment solutions, such as mobile payments and processing, at the POS; and
- rapidly changing customer and end user preferences or requirements.

In addition, our competitors have been increasingly aggressive in introducing products and lowering prices. Because of these factors, we must continually enhance our existing solutions and develop and market new solutions, and we must anticipate and respond timely to these industry, customer and regulatory changes in order to remain competitive, all of which have become increasingly challenging as competition intensifies. If we cannot develop new solutions or enhancements to our existing solutions that satisfy customer or end user demand, or if our new solutions or enhancements do not meet local certification requirements or experience delays in the certification process or meet resistance from clients or merchants or are inhibited by third parties' intellectual property rights, we will not be able to timely and adequately respond to competitive challenges and technological advancements, and our net revenues and results of operations will be adversely affected. These efforts require management attention and significant investment in research and development as well as increased costs of manufacturing and distributing our systems, and ultimately may not be successful. We may not necessarily be able to increase or maintain prices to account for these costs, which will negatively impact our profitability, cash flows and results of operations. Our business has been in the past and continues to be adversely affected by our failure to timely obtain local certifications or develop software in some

markets for certain of our products. In particular, our business would be adversely affected if we are unable to timely obtain certifications or develop software for our Verifone Engage line of products.

## Table of Contents

We cannot be sure that we will successfully and timely complete the development and introduction of new solutions or enhancements or that our new solutions will satisfy customer or end user demand or be accepted in the marketplace. If we fail in either case, we may lose market share to existing or new competitors and competing technologies, our solutions could become obsolete and our net revenues, income and profitability will suffer.

We continue to experience significant and increasing levels of competition from existing and new competitors and a variety of technologies.

The markets for our systems and services are highly competitive and rapidly evolving, and we have been and expect to continue to be subject to significant and increasing competition from existing and new competitors and a variety of technologies. Traditionally, we have competed with other large manufacturers and distributors of electronic POS payment solutions, suppliers of cash registers that provide built-in electronic payment capabilities and producers of software that facilitates electronic payment over the Internet. In certain areas, we also compete with smaller companies that have been able to develop strong local or regional customer bases. We compete with companies that are more established, benefit from greater name recognition in particular countries, and have greater resources within those countries than we do. In addition, some of these competitors compete with aggressive pricing. We face downward pressures on prices in many markets. For example, price competition is increasingly intense for us in countries and regions such as China, Southeast Asia, Brazil, Mexico, Russia and India from both global and local competitors. In addition, pricing is increasingly an important factor in our ability to penetrate new markets. Any decrease in our selling prices in order to become and remain competitive in these markets could negatively impact our net revenues, gross margins and results of operations.

We also face competition from alternative payment solutions, such as mobile device-based card payment and processing solutions that offer customers the ability to pay on mobile devices through a variety of payment methods. Some of these alternative solutions enable payment and processing at the POS without use of traditional payment terminals, such as those we manufacture and sell. In addition, some of these alternative solutions are offered by companies that are significantly larger than we are. Competition from these alternative solutions could reduce demand for our traditional payment terminals and our services offerings and have an adverse effect on our results of operations.

As discussed in “If we are unsuccessful in executing on our implementation of the Payment-as-a-Service model and obtaining and maintaining customer acceptance of our service offerings, our net revenues, income and profitability will be adversely affected”, the competitive environment for services offerings is complex and very different in each market and, in some markets, our competitors include certain of our customers that distribute our terminals. Some of our competitors may offer more services, have better name recognition in that market or have a longer or more established relationship with customers in that market than we do. Some of our competitors also control other products and services that are important to our success, including e-commerce and omni-channel platforms or may develop exclusive strategic relationships with key distributors upon whom we previously relied.

We expect to continue to experience significant and increasing competition. Our net revenues, income and profitability will be negatively impacted if we do not effectively compete with existing competitors and new market entrants. If we cannot develop and offer, in a timely and cost-effective manner, technological features our customers desire or offer alternative solutions that align with shifts to payment on devices other than the traditional POS terminal, we may lose customers and market share, experience price reductions and/or reduced margins, or, in some cases, cease to participate in the market at all. Furthermore, as we respond to changes in the competitive environment, we may, from time to time, make pricing, product offering or service decisions or acquisitions that may lead to dissatisfaction among our customers and partners and harm our revenues and/or profitability.



Table of Contents

Security is vital to our customers and end users, and breaches in the security of our solutions could adversely affect our reputation and results of operations.

We operate in an industry that makes us a target of cyber- and other attacks on our systems as well as at our payment solutions. Our business involves the collection, transmission, storage and use of proprietary data or personally-identifying information of our customers, business partners and employees, as well as, in certain cases, end-users of our products or services. We rely on electronic networks, computers, systems, including our gateways, programs to run our business and operations, our employees and third party technology and IT infrastructure providers and, as a result, are exposed to risks of third-party security breaches, criminal hackers, industrial espionage, employee or third party error or malfeasance, or other irregularities or compromises on our systems which could result in the loss or misappropriation of sensitive data, corruption of business data or other disruption to our operations. Outside parties may also attempt to fraudulently induce our employees, customers, business partners, service providers and other users of our solutions to disclose information in order to gain access to sensitive data and our solutions. As we expand our solutions and services, we may handle increasing volumes of sensitive data, in which case we would expect to increasingly become a target of security breach attempts. We have devoted significant resources to security measures, processes and technologies to protect and secure our networks and systems, but they cannot provide absolute security, especially in light of rapid advances in computer capabilities and cryptography. For example, an increasing number of companies have disclosed breaches of their security systems, some of which have involved sophisticated and highly targeted attacks on their network infrastructure. Because the techniques used to breach security safeguards change frequently, such techniques may be difficult to detect for a long period of time and often are not recognized until launched against a target. Certain efforts may also be state sponsored and supported by significant financial and technological resources, potentially making them even more difficult to detect. As a result, we may be unable to anticipate these techniques or to implement adequate preventative measures.

In addition, overall payment network security depends upon a number of factors outside our control, including the merchant or service provider network environment in which our systems are installed, the merchant's or service provider's adherence to security protocols in the installation, use and operation of our solutions and implementation of and adherence to compliant security processes and practices for its network. Even if there is no compromise to our solutions, any security breach or compromise in any part of a merchant's or service provider's network could result in negative media and/or reputational harm to us, or other costs or damages to us, all of which could have a material adverse impact on our results of operations.

We have in the past experienced and may in the future experience security breaches related to unauthorized access to sensitive customer information. If the security of our solutions is compromised, our reputation and marketplace acceptance of our solutions will be adversely affected, which would cause our business to suffer. We may also be subject to damages claims, lost sales, fines, investigations or lawsuits, which could lead to restrictions imposed on our business and otherwise adversely affect our results of operations. Furthermore, the costs associated with preventing breaches in the security of our solutions, such as investment in technology and related personnel and costs associated with the testing and verification of the security of our solutions, could adversely impact our financial condition and results of operations. Additionally, our insurance policies carry low coverage limits, which may not be adequate to reimburse us for losses caused by security breaches and we may not be able to fully collect, if at all, under these insurance policies.

Our quarterly operating results may fluctuate significantly as a result of factors outside of our control, which could cause the market price of our stock to decline.

We expect our net revenues and operating results to vary from quarter to quarter. As a consequence, our operating results in any single quarter may not meet the expectations of securities analysts and investors, which could cause the price of our stock to decline. Factors that may affect our operating results include:

the type, timing, and size of orders and shipments;

delays in the implementation, including obtaining certifications, delivery and customer acceptance of our products and services, which may impact the timing of our recognition, and amount, of net revenues;

54

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Table of Contents

•delays in customer purchases in anticipation of product or service enhancements or due to uncertainty in economic conditions;

•demand for and acceptance of our new offerings;

•changes in competitive conditions, including from traditional payment solution providers and from alternative payment solution providers;

•the rate at which we transition customers to our services model;

•decisions by our distributors and other customers relating to the overall channel inventories of our products held in a particular quarter;

•concentration in certain of our customer bases;

•changes in economic or market conditions, such as fluctuations in foreign currency exchange rates;

•variations in product and service mix and cost during any period;

development of new customer and distributor relationships or new types of customers, penetration of new markets and

•maintenance and enhancement of existing relationships with customers, distributors and strategic partners, as well as the mix of customers in a particular quarter;

•component supply, manufacturing, or distribution difficulties;

•timing of commencement, execution, or completion of major product or service implementation projects;

•timing of governmental, statutory and industry association requirements, such as PCI compliance deadlines or EMV adoption in the U.S. or elsewhere;

•the relative geographic mix of net revenues;

•the fixed nature of many of our expenses;

changes in credit card interchange and assessment fees, which are set by the credit card networks and are a component

•of the cost of providing some of our product offerings, including the Payment-as-a-Service solution and in-taxi payments solutions;

the introduction of new or stricter laws and regulations in jurisdictions where we operate, such as data protection and

•privacy laws and regulations, laws and regulations covering hazardous substances, or employment laws and regulations, that may cause us to incur additional compliance or implementation costs and/or costs to alter our business operations;

the introduction of new laws and regulations, or changes in implementation of existing laws and regulations, in

•jurisdictions where we operate that may create uncertainty regarding the business operations of our customers or distributors, which may in turn lead to deferred or reduced orders from our customers or distributors; and

business and operational disruptions or delays caused by political, social or economic instability and unrest, such as

•the ongoing significant civil, political and economic disturbances in Russia, Turkey, Ukraine and their spillover effect on surrounding areas as well as the political and military conditions in Israel and the Palestinian territories.

No single factor above is dominant, and any of the foregoing factors could have an adverse effect on our operating results.

In addition, we have experienced in the past and may continue to experience periodic variations in sales in our key vertical and geographical markets. In particular, differences in relative growth rates among our businesses in the U.S. and other regions may cause significant fluctuation in our quarterly operating results, especially our quarterly gross profit margins, because net revenues generated from international markets tend to carry lower margins. Furthermore, adoption of standards such as EMV in the United States, could cause revenues to increase but it may not be possible to sustain or increase those revenues in future periods. These periodic variations occur throughout the year and may lead to fluctuations in our quarterly operating results depending on the impact of any given market during that quarter and could lead to volatility in our stock price.

Table of Contents

We may suffer losses due to fraudulent activities.

We are expanding our service solutions offerings. Some of our service solutions offerings include our gateway services for credit card transactions. We may be subject to losses in the provision of such services in the event of fraudulent activities or errors in connection with such transactions. As we expand such service solutions offerings, we may increasingly become a target of fraudulent activities and our exposure to the risk of losses from such activities may increase, which may adversely impact our business, results of operations and financial condition. Further, the occurrence of fraud perpetrated on our solutions may result in negative publicity and user sentiment which could harm our brand and reputation and impair our ability to retain or attract users of our solutions.

A majority of our net revenues are generated outside the U.S.; accordingly, fluctuations in currency exchange rates may adversely affect our results of operations.

A substantial portion of our business consists of sales made to customers outside the U.S. For example, during the six months ended April 30, 2016, approximately 57.0% of our net revenues were generated outside of the U.S. A portion of the net revenues we receive from such sales is denominated in currencies other than the U.S. dollar, primarily the Euro, the Brazilian real, the British Pound, the Chinese renminbi and the Swedish Krona. Additionally, portions of our cost of net revenues and our other operating expenses are incurred by our international operations and denominated in local currencies, primarily the Euro, the Brazilian real, the British Pound, and the Swedish Krona. Our net revenues, cost of net revenues and operating expenses denominated in the Euro and the Swedish Krona have increased with the Point and Hypercom acquisitions. Fluctuations in the value of these net revenues, costs and expenses as measured in U.S. dollars have historically affected our results of operations, and adverse currency exchange rate fluctuations may have a material impact in the future. Further, changes in exchange rates that strengthen the U.S. dollar could increase the price of our U.S. dollar-denominated products in the local currencies of the foreign markets we serve, making our products relatively more expensive than products that are denominated in local currencies, which could lead to a reduction in our sales and profitability in those markets. For example, in recent periods, the U.S. dollar has strengthened, in some cases significantly, against certain major currencies in which we transact, such as the Euro, the Brazilian real, and the Argentina Peso, impacting negatively our results of operations. In addition, our balance sheet contains monetary assets and liabilities denominated in currencies other than the U.S. dollar, such as cash, intercompany balances, trade receivables and payables, and fluctuations in the exchange rates for these currencies could adversely affect our results of operations.

We have entered into foreign exchange forward contracts intended to hedge a portion of our balance sheet exposure to adverse fluctuations in exchange rates. These hedging arrangements can be costly and may not always be effective, particularly in the event of imprecise forecasts of non-U.S. dollar denominated assets and liabilities. In addition, we may be unable to hedge currency risk for some transactions due to cost or because of a high level of uncertainty or the inability to reasonably estimate our foreign exchange exposures. For some currencies in which we do business, hedging instruments may not be available on any terms.

We have also effectively priced our systems products in U.S. dollars in certain countries. Additionally, our efforts to effectively price products in U.S. dollars may have disadvantages as they may affect demand for our products if the local currency strengthens relative to the U.S. dollar. We could be adversely affected when the U.S. dollar strengthens relative to the local currency between the time of a sale and the time we receive payment, which would be collected in the devalued local currency. Accordingly, if there is an adverse movement in one or more exchange rates, we might suffer significant losses and our results of operations may otherwise be adversely affected. Uncertainty in global market conditions has resulted in and may continue to cause significant volatility in foreign currency exchange rates which could increase these risks. As our international operations expand, our exposure to these risks also increases.





## Table of Contents

We intend to continue to expand our operations internationally, and our results of operations could suffer if we are unable to manage our international expansion effectively.

The percentage of our net revenues generated outside of the U.S. is significant and may increase over time. In particular, our acquisition of Point significantly increased our business in the Nordic regions and elsewhere in Northern Europe and our acquisition of Hypercom significantly increased our business in the EMEA region and Asia. Part of our strategy is to expand our penetration in existing foreign markets and to enter new foreign markets, particularly emerging markets where we expect to see growth in electronic payments and related services. Our ability to penetrate some international markets may be limited due to different technical standards, protocols or product requirements. For example, we have lost market share and business in China because we have not been able to provide products and solutions that meet the requirements of the Chinese market. Expansion of our international operations will require significant management attention and financial resources. Certain emerging markets, including those in the Middle East and Africa, may require longer lead times to develop distribution channels, may involve distribution channels with greater business and operational risk due to their relatively shorter operating histories, may be dependent upon the timing and success of local electronic payments initiatives and related infrastructure investments in such markets, as well as require additional time and effort to obtain product certifications and gain market acceptance for our products. Our international net revenues will depend on our success in a number of areas, including:

- securing commercial relationships to help establish or increase our presence in new and existing international markets;
- hiring and training personnel capable of marketing, installing and integrating our solutions, supporting customers, and effectively managing operations in foreign countries;
- adapting our solutions to meet local requirements and regulations, and to target the specific needs and preferences of foreign customers, which may differ from our traditional customer base in the markets we currently serve;
- building our brand name and awareness of our services in new and existing international markets;
- enhancing our business infrastructure to enable us to efficiently manage the higher costs of operating across a larger span of geographic regions and international jurisdictions; and
- implementing effective systems, procedures, and controls to monitor and manage our operations across our international markets.

As discussed more extensively under “If we fail to address the challenges and risks associated with international operations, including those through expansion and acquisitions, we may encounter difficulties implementing our strategy, which could impede our growth or harm our operating results”, if we cannot effectively manage our international expansion, our results of operations could suffer.

If we fail to address the challenges and risks associated with international operations, including those through expansion and acquisitions, we may encounter difficulties implementing our strategy, which could impede our growth or harm our operating results.

We are subject to risks and costs associated with operating in foreign countries which could negatively impact our results of operations or cash flows. In addition, if we are not able to effectively manage these risks, our strategy of international expansion will be negatively impacted.

Our international operations expose us to a number of risks, including:

- multiple, changing, and often inconsistent enforcement of laws and regulations;
- local regulatory or industry imposed requirements, including security or other certification requirements;
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competition from existing market participants, including strong global or local competitors that may have a longer history in and greater familiarity with the international markets we enter;  
tariffs and trade barriers, including the imposition of new or enforcement of existing import restrictions in jurisdictions in which we do business;

57

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Table of Contents

higher costs and complexities of compliance with international and U.S. laws and regulations such as import and trade regulations and embargoes, trade sanctions, export requirements and local tax laws;

laws and business practices that may favor local competitors;

restrictions on the repatriation of funds, including remittance of dividends by foreign subsidiaries, foreign currency exchange restrictions, and currency exchange rate fluctuations;

pricing sensitivities, less favorable payment terms and increased difficulty in collecting accounts receivable and developing payment histories that support collectability of accounts receivable and revenue recognition;

different and/or more stringent labor laws and practices, such as the mandated use of workers' councils and labor unions, or laws that provide for broader definitions of employer/employee relationships;

different and/or more stringent data protection, privacy and other laws;

antitrust and competition regulations;

infrastructure challenges;

changes or instability in a specific country's or region's political or economic conditions; and

greater difficulty in safeguarding intellectual property, including in areas such as China, India, Russia, and Latin America.

Many of these factors typically become more prevalent during periods of economic stress, such as recent fluctuations in the Chinese economy, the ongoing weakness in the economies of the euro zone countries and Latin America countries and volatility in global financial markets that have caused declines in the value of the euro and other currencies impacted by the European sovereign debt crisis, or disruptive events such as natural or man-made disasters or military or terrorist actions. The occurrence or persistence of weakened global economic conditions in one or more regions where we do business may exacerbate certain of these risks. Additionally, these risks and costs associated with operating in foreign countries are heightened with respect to our international expansion into emerging or developing markets, which, for example, tend to experience more economic and political instability or have less developed or sophisticated distribution channels.

We are subject to foreign currency risk including that from economic and political instability which can lead to significant and unpredictable volatility in currency rates, including as a result of significant currency devaluations, which may negatively impact our net revenues, gross margins, results of operations and financial position. Although we engage in some hedging of our foreign currency exposures, we do not hedge all such exposures and our hedging arrangements may not always be effective. The uncertainty with respect to the ability of certain European countries to continue to service their sovereign debt obligations and the related European financial restructuring efforts may cause the value of the Euro to fluctuate. The current political situation in Ukraine, the sanctions imposed against Russia by certain European nations and the U.S., and Russia's response to these sanctions may further increase the economic uncertainty in the affected regions and lead to further fluctuation in the value of foreign currencies, such as the Euro and Russian ruble, used in these regions. Similarly, an economic downturn in China or a further decrease in economic growth in China could lead to currency fluctuations that impact us. See "A majority of our net revenues are generated outside the U.S.; accordingly, fluctuations in currency exchange rates may adversely affect our results of operations" and Part II, Item 7A, Quantitative and Qualitative Disclosures About Market Risk--Foreign Currency Transaction Risk in our Annual Report on Form 10-K for the fiscal year ended October 31, 2015.

Table of Contents

In addition, compliance with foreign and U.S. laws and regulations, including changes and additions to such laws and regulations, that are applicable to our international operations is complex and may increase our cost of doing business in international jurisdictions. Our international operations could expose us to fines and penalties if we fail to comply with these regulations. These laws and regulations include import and export requirements, trade restrictions and embargoes, exchange control regulations, data privacy requirements, labor laws, tax laws, anti-competition regulations, U.S. laws such as the Foreign Corrupt Practices Act, and local laws prohibiting corrupt payments to governmental officials and other improper payments or inducements, such as the U.K. Bribery Act. Although we have implemented policies, procedures and training designed to ensure compliance with these laws and regulations, there can be no assurance that our employees, contractors, distributors, suppliers and agents will not take actions in violation of our policies, particularly as we expand our operations through organic growth and acquisitions, including acquisitions of businesses that were not previously subject to and may not have familiarity with U.S. and other laws and regulations applicable to us or compliance policies similar to ours. For example, as described under the caption “Disclosures of Iranian Activities under Section 13(r) of the Securities Exchange Act of 1934” in Part I, Item 1, Business, of our Annual Report on Form 10-K filed with the SEC for the fiscal year ended October 31, 2013, in early 2013, we submitted a voluntary disclosure to the U.S. Department of Treasury's Office of Foreign Assets Control in connection with certain unauthorized activities by employees of one of our non-U.S. subsidiaries that involved potential violations of sanctions regulations. Any violations of sanctions or export control regulations or other laws could subject us to civil or criminal penalties, including the imposition of substantial fines and interest or prohibitions on our ability to offer our products and services to one or more countries, and could also materially damage our reputation, our brand, our international expansion efforts and our business, and negatively impact our operating results.

Our international operations tend to carry solutions with lower average selling prices, may be subject to greater downward pressure on prices in some markets and may be associated with higher costs and lower gross margins, which may promote volatility in our results of operations and may adversely impact future growth in our earnings.

Our international sales of systems tend to carry lower average selling prices and therefore have lower gross margins than our sales in the U.S. We also face increasing downward pressure on prices in certain international markets such as China and Southeast Asia, where competition from local low-cost and global competitors has increased significantly, Brazil, where competition has intensified, and India where we continue to work to expand our business. In these and certain other markets, some customers increasingly seek lower-cost solutions suited to their markets that may have similar, different, and in some cases, better features and functionality. In addition, the costs associated with international trade may be higher as a result of the importation costs, duties and trade requirements or other import or export control laws and regulations imposed by some jurisdictions where we do business. As a result, any improvement in our results of operations from our international expansion will likely not be as favorable or profitable as an expansion of similar magnitude in the U.S. In addition, we are unable to predict for any future period our proportion of net revenues that will result from international sales versus sales in the U.S. Variations in this proportion from period to period may lead to volatility in our results of operations and may adversely impact future growth in our earnings.

Table of Contents

Macroeconomic conditions and economic volatility have in the past and could in future periods materially and adversely affect our business and results of operations.

Our operations and performance depend significantly on global and regional economic conditions. For example, the current continued and prolonged weak macro-economic conditions in Europe and in some euro zone countries have resulted in a slowdown, and in some cases deferrals, of orders by customers, which has adversely impacted our business, financial condition and results of operations. Similarly, the significant slowdown and volatility in the U.S. and international economy and financial markets which began in the latter half of 2008 resulted in reduced demand for our products and adversely affected our business, financial condition and results of operations. The lower-than-expected growth rates in certain emerging market economies in which we operate have also had an adverse effect on our results of operations in these regions. More recently, the decreases in oil prices have resulted in, and may continue to result in, decline in demand and overall weaker market conditions in countries and regions heavily dependent on oil revenues, such as Russia, Venezuela, Mexico, and the Middle East. In particular, the slowdown and volatility in the global markets resulted in softer demand in the financial and retail sectors, pricing pressures and more conservative purchasing decisions by customers, including a tendency toward lower-priced products and lower volume of purchases. In some countries where we do business, the weakened economy has resulted in economic instability which has had negative effects, including a decrease in purchasing power due to currency devaluations. If these weak macro-economic conditions continue or if any economic recovery remains slow and fragile or is not sustained, our net revenues, business, financial condition and results of operations could be adversely impacted.

We expect certain markets where we conduct business, including parts of Europe and Brazil, to continue to experience weakened or uncertain economic conditions in the near term, and some of our customers, prospective customers, suppliers, distributors and partners will continue to be negatively impacted by the continued global weakness in the economy. We cannot predict the extent and duration of the negative impact that global and regional economic volatility may have on our business, operating results and financial condition. There is no assurance that governments and central banks will take actions to further stimulate the economy or that any such actions will have positive or lasting impacts. Existing stimulus measures may also be withdrawn or reduced, introducing greater economic uncertainty or volatility. Further, conditions such as political situations or terrorist actions in other parts of the world, such as Europe and parts of Asia, the continued uncertainty related to economic conditions in the U.S., any potential, additional congressional actions regarding the national debt ceiling and federal budget deficit, the potential effect of any future federal government shutdown, and additional taxes related to changes in the health care law, as well as continued high unemployment rates in the U.S. and some other regions, may negatively impact global economic conditions, including corporate and consumer spending, and liquidity of capital markets. Continued volatility in market conditions, such as fluctuations in foreign currency rates relative to the U.S. dollar, makes it difficult to forecast our financial guidance and/or to meet such guidance. If we fail to meet our financial guidance or the expectations of investment analysts or investors in any period, the market price of our stock could decline.

Table of Contents

Sanctions against Russia, and Russia's response to those sanctions, including the imposition of sanctions by Russia, could materially adversely affect our business, results of operations and financial condition.

In March 2014, the Crimean region of Ukraine was annexed by Russia. In response, other nations, including the U.S., have imposed or are considering imposing, economic sanctions on Russia. Recently, concerns related to the political and military conditions in the region have prompted stringent restrictions by the U.S. and EU, and increasing levels of economic sanctions, targeting certain Russian companies in the finance, energy and defense industries and additional Russian nationals, as well as imposing restrictions on trading and access to capital markets. In response, Russia announced its own trading sanctions against nations that implemented or supported the anti-Russia sanctions, including the U.S. and some European Union nations. Russia has also recently announced potential sanctions against Turkey in response to a military incident between Turkey and Russia in November 2015. A portion of our net revenues are from Russia and its surrounding areas, including Ukraine and Turkey. Economic sanctions imposed by the U.S., the European Union, Russia, Turkey or the world community may result in serious economic challenges in Ukraine, Turkey, Russia and the surrounding areas, and imposition of trade restrictions may delay or prevent shipment of products to or services performed in those countries, which could have an adverse effect on our results of operations. In addition, to the extent it is more difficult for some of our customers to obtain financing or access U.S. dollar currency, due to restrictions on access to international capital markets as a result of the sanctions, our customers' ability to pay could be adversely affected, which could have a material adverse impact on our business, cash flows, results of operations and financial condition. Further, current and any future retaliatory measures by Russia in response to anti-Russia sanctions could adversely affect European and Middle East economic conditions, which could in turn affect our business in Europe, Turkey and elsewhere. Accordingly, sanctions against or by Russia and the responses to sanctions, including potential responses by Turkey to sanctions imposed by Russia, could have a material adverse effect on our business, results of operation and financial condition.

Our solutions may have defects or experience field failures that could delay sales, harm our brand, increase costs and result in product recalls and additional warranty and other expense.

We offer complex solutions that are susceptible to undetected hardware and software errors or failures. Our solutions may experience failures when first introduced, as new versions or enhancements are released, or at any time during their lifecycle. Despite our testing procedures and controls over manufacturing quality, errors may be found in our products. Field failure may result from usage with third-party issued payment cards, for example, if such usage generates excess electrostatic discharge. Defects may also arise from third-party components that are incorporated into our products, such as hardware modules, chipsets, wireless modules or battery cells. Our customers may also run third-party software applications on our electronic payment systems. Errors in such third-party applications could adversely affect the performance of our solutions or cause the loss of data. Any product recalls or delays in implementation of our products as a result of, or perceived to be resulting from, our errors or failures could result in the loss of customers, fines incurred by our customers due to failure to comply with payment system rules for which we may be obligated to compensate our customers, loss of or delays in market acceptance of our solutions, diversion of the attention of our research and development personnel from product development efforts and harm to our credibility and relationships with our customers, adversely affect our business and reputation, and increase our product costs which could negatively impact our margins, profitability, and results of operations. Any significant returns or warranty claims for any of our products, including products from acquisitions, could result in significant additional costs to us, such as costs to implement modifications to correct defects, recall and replace products, and defend against litigation related to defective products or related property damage or personal injury, and could adversely affect our results of operations.

Identifying and correcting defects can be time-consuming, costly and in some circumstances extremely difficult. It may take several months to correct software errors, and even longer for hardware defects. The delays in correcting product defects could exacerbate the adverse impact product defects or failures may have on our business, results of

operations, financial condition and reputation.

61

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Table of Contents

Disruptions in our services could reduce our net revenues, increase costs, harm our reputation and result in loss of customers.

The performance of our services may from time to time be disrupted due to equipment malfunctions, technical performance failures, and connection problems, among other things, including disruptions caused by factors outside our control, such as telecommunication network failures. Service disruptions may result in our customers' inability to process transactions using our terminals or gateways and lead to loss of net revenues for us. We may have to spend resources to detect and fix defects that caused such disruptions, and we cannot guarantee that we will be able to detect and fix all such defects. In addition, we may be required to reimburse or indemnify our customers for losses and fines or penalties due to such service disruptions. Our brand may be harmed by service disruptions and we may lose customers to our competitors, which could result in financial or reputational harm to our business.

Changes to our management and strategic business plan and restructuring activities may cause uncertainty regarding the future of our business, and may adversely impact employee hiring and retention, our stock price, our customer relationships, and our results of operations and financial condition.

We have experienced, and may experience in the future, changes in our management team. In 2013, the Board appointed Mr. Paul Galant as our CEO and Mr. Marc E. Rothman as our new CFO. Further, in recent years, we announced certain other sales, technology, marketing, human resources, and operations management changes. During this time of transition, our new executive leadership and our continuing executives have been designing and implementing changes to our strategic business plans, in order to better position the company for strategic growth and long-term profitability. In addition, we have initiated certain restructuring activities in accordance with our approved restructuring plans, reducing the number of employees and contractors in certain areas and reassigning certain employee duties, and consolidating excess facilities. Our management changes, changes to our strategic business plan, and restructuring activities, as well as the potential for additional changes or activities in the future, may introduce uncertainty regarding our business prospects and may result in disruption of our business and our customer relationships. In addition, these changes and measures could distract our employees, decrease employee morale, result in failure in meeting operational targets due to the loss of employees and make it more difficult to retain and hire new talent, increase our expenses in terms of severance payments and facility exit costs, both of which could be significant, expose us to increased risk of legal claims by terminated employees, and harm our reputation. These changes and activities could also increase the volatility of our stock price. If we are unable to mitigate these or other similar risks, our business, results of operations, and financial condition may be adversely affected.

We may not successfully implement our transformation initiatives or fully realize the anticipated benefits from our restructuring efforts.

We are in the process of implementing a number of strategic, transformation initiatives intended to redefine our global product management process and portfolio, re-engineer our research and development function and improve our cost structure. As part of these transformation initiatives, during fiscal year 2014, fiscal 2015 and fiscal year 2016, our management approved restructuring plans to better align our business organization, operations and product lines to achieve long-term sustainable growth and value, including through workforce reduction and facility consolidations. We cannot assure you that we will be able to successfully implement our transformation initiatives. Further, our ability to achieve the anticipated benefits, including the anticipated levels of cost savings and efficiency, of such transformation initiatives and the restructuring plans within expected timeframes is subject to many estimates and assumptions, which are, in turn, subject to significant economic, market, competitive and other uncertainties, some of which are beyond our control. Further restructuring or reorganization activities may also be required in the future beyond what is currently planned, which could further enhance the risks associated with these activities. There is no assurance that we will successfully implement, or fully realize the anticipated positive impact of, our transformation initiatives and the restructuring plans, in the timeframes we desire or at all.



Table of Contents

If we are unsuccessful in executing on our implementation of the Payment-as-a-Service model and obtaining and maintaining customer acceptance of our service offerings, our net revenues, income and profitability will be adversely affected.

A central part of our strategic plan is to increase services offerings so that we can derive higher overall net revenues and margins, develop deeper relationships with our customers and drive more predictable financial results. Following our acquisition of Point, we have been implementing Point's Payment-as-a-Service model in multiple jurisdictions. Implementing a new services model is difficult and involves management focus, upfront local infrastructure and capital costs and other resources that could otherwise be utilized in research and development of other hardware and software product offerings, and the build-out of local service and support teams. In addition, the competitive environment for services is very different in each market, and the bundle of services being offered must be customized to compete effectively. Markets may take longer to adopt a Payment-as-a-Service model than we anticipate or may choose not to adopt this model at all. We may also be competing against others, including certain of our customers that distribute our terminals, who already offer similar services. Continued weakness in the global economy may also negatively impact our ability to implement our Payment-as-a-Service model within the time frames we desire and to achieve the benefits we anticipate. If we are unsuccessful in executing on our implementation of the Payment-as-a-Service model and obtaining and maintaining customer acceptance of our service offerings or are unable to implement the model while also maintaining focus on other key areas of our business or if we are unable to maintain the expected level of margins associated with these service offerings, we may not be able to generate sufficient returns on our investments in the services business and our net revenues, income and profitability will be adversely affected.

We have experienced rapid and significant growth in our operations in recent years, and if we cannot manage our expanded operations and also effectively execute on our business strategy, our results of operations will suffer.

We have experienced rapid and significant growth in our operations in recent years, both organically and from acquisitions. If we cannot manage our expanded operations to align with our business strategy, which includes maintaining streamlined and efficient operations while effectively meeting the needs of our broader customer base, managing a competitive portfolio of products, and growing our payment services globally in a cost-effective manner, our results of operations will suffer. In particular, we may not be able to attain desired cost-efficiencies and remain competitive, and any measures we may need to undertake to further align our operations with our business strategy may be costly and could adversely impact our results of operations. If we are unable to successfully execute on our business strategy, our results of operations may also be adversely affected. Furthermore, we cannot be sure that we have made adequate allowances for the costs and risks associated with supporting our expanded operations. Any delay in implementing, or transitioning to, new or enhanced systems, procedures, processes or controls to adequately support our expanded operations, including our expansion into a number of additional international markets, including emerging markets, and our growth in payment services globally may adversely affect our ability to meet customer requirements, manage our product inventory, and record and report financial and management information on a timely and accurate basis.

## Table of Contents

From time to time, we engage in acquisitions, divestitures, and other strategic transactions that involve numerous enterprise risks and could disrupt our ongoing business and harm our results of operations. We may not be able to address these risks without substantial expense, delay or other operational or financial problems, and may not realize the expected benefits of our acquisitions.

In pursuing our business strategy, we, from time to time, conduct discussions, evaluate opportunities, and complete acquisitions or strategic investments in related businesses, technologies, or products.

The integration of our acquisitions, particularly those that are international in scope, is complex, time-consuming and expensive, and has disrupted, and may continue to disrupt, our business or divert the attention of our management. Achieving the expected benefits of our acquisitions depends in large part on our successful integration of the acquired businesses' operations and personnel with our own in a timely and efficient manner. We cannot ensure that all of our integration efforts will be completed as quickly as expected or that our past or future acquisitions will achieve any of the expected benefits. These challenges and risks, which are heightened due to the number, size and varying scope of our recently completed acquisitions, include, but are not limited to:

- the need to integrate the operations, business systems, and personnel of the acquired business, technology or product, including coordinating the efforts of the sales operations, in a cost-effective manner;
- the challenge of managing acquired lines of business, particularly those lines of business with which we have limited operational experience;
- the occurrence of multiple product lines or services offerings as a result of acquisitions, that are offered, priced or supported differently, potentially leading to integration delays and customer impact;
- the need to integrate or migrate the information technology infrastructures of acquired operations into our information technology systems and resources in an effective and timely manner;
- the need to migrate our acquired businesses to our common enterprise resource planning information system and integrating all operations, sales, accounting, human resources and administrative activities for the combined company, all in a scalable, cost-effective and timely manner;
- the need to coordinate research and development and support activities across our existing and newly acquired products and services in a cost-effective manner;
- the challenges of incorporating acquired technologies, products and service offerings into our next generation of products and solutions in an effective and timely manner;
- the potential disruption of our ongoing business, including the diversion of management attention to issues related to integration and administration;
- entering markets in which we have limited prior experience;
- in the case of international acquisitions, the need to integrate operations across different jurisdictions, cultures and languages and to address the particular economic, foreign currency, political, legal, compliance and regulatory risks, including with respect to countries where we previously had limited operations;
- the possible inability to realize the desired financial and strategic benefits from any or all of our acquisitions or investments in the time frame expected, or at all;
- the loss of all or part of our investment;
- the loss of customers and partners of acquired businesses;
- the failure to retain employees from acquired businesses;
- the need to integrate each company's accounting, legal, management, information, human resource and other administrative systems to enable effective management, and the lack of control if such integration is delayed or unsuccessful;
- the need to implement controls, procedures and policies appropriate for a larger public company at companies that prior to acquisition had lacked such controls, procedures and policies and the potential stress on our existing controls, particularly in integrating multiple acquired companies;
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the risk that increasing complexity inherent in operating a larger global business and managing a broader range of solutions and service offerings may impact the effectiveness of our internal controls and adversely affect our financial reporting processes;

Table of Contents

the failure to adequately identify or assess the magnitude of certain liabilities, shortcomings or other circumstances prior to acquiring a company, which could result in unexpected litigation, unanticipated liabilities, additional costs, unfavorable accounting treatment or other adverse effects; and the dependency on the retention and performance of key management and employees of acquired businesses for the day-to-day management and future operating results of these businesses.

Our operating results or financial condition may be adversely impacted by pre-existing claims or liabilities, both known and unknown, of these acquired companies, including claims from current or former customers, terminated employees or other third parties; pre-existing contractual relationships of an acquired company that may contain unfavorable terms or that have unfavorable revenue recognition or accounting treatment; and intellectual property claims or disputes. In addition, the integration process may strain the combined company's financial and managerial controls and reporting systems and procedures and may result in the diversion of management and financial resources from the combined company's core business objectives. There can be no assurance that we will successfully integrate our businesses or that we will realize the anticipated benefits of the acquisitions after we complete our integration efforts.

These risks are heightened and more prevalent in acquisitions of larger businesses, in the event of multiple concurrent acquisitions and integrations, or in businesses involving geographies or business lines in which we may have less experience. Future acquisitions and investments could also result in substantial cash expenditures, potentially dilutive issuances of our equity securities and incurrence of additional debt, contingent liabilities and amortization expenses related to other intangible assets that could adversely affect our business, operating results, and financial condition.

We may not be able to attract, integrate, manage, and retain qualified personnel.

Our success depends to a significant degree upon the continued contributions of our key senior management, engineering, sales and marketing, supply chain, and other specialized personnel, many of whom would be difficult to replace. In addition, our future success depends on our ability to attract, integrate, manage, and retain highly skilled employees throughout our business. Competition for some of these personnel is intense in certain markets, especially in the Silicon Valley where our corporate headquarters are located, and competitive pressures in such markets can drive up wages, impacting our profitability. In the past we have had difficulty hiring, in our desired time frame and in our desired markets, employees that have the specific qualifications required for a particular position. In particular, we may be unsuccessful in attracting and retaining personnel as a result of the workforce reduction measures we have implemented or may implement in the future. To help attract, retain and motivate qualified personnel, we use share-based incentive awards, such as employee stock options and restricted stock units as well as cash-based incentive awards tied to our performance. If the Company's overall performance is poor, the value of our stock awards does not appreciate as measured by the performance of the price of our common stock, or if our share-based compensation otherwise ceases to be viewed as a valuable benefit, employee incentive awards and morale could be negatively impacted and our ability to attract, retain and motivate personnel could be weakened. The loss of the services of any of our key personnel, the inability to attract or retain qualified personnel in the future, or delays in hiring required personnel, particularly engineers and sales personnel, could make it difficult for us to manage our business and meet key objectives, such as timely product introductions, and our business and profitability may suffer.

Table of Contents

We depend on distributors and resellers to sell a significant portion of our solutions. If we do not effectively manage our relationships with them, our net revenues and results of operations could suffer.

We sell a significant portion of our solutions through third-party resellers such as independent distributors, ISOs, value-added resellers, and payment processors. We depend on their active marketing and sales efforts. These resellers also provide after-sales support and related services to end user customers, and generally have valuable knowledge and experience with the customer base in the territories they serve. These resellers also provide critical services of developing and supporting the software applications to run on our various electronic payment systems and, internationally, in obtaining requisite certifications in the markets in which they are active. Accordingly, the pace at which we are able to introduce new solutions in markets in which these resellers are active depends in part on the resources they dedicate to these tasks. Moreover, our arrangements with these resellers typically do not prevent them from selling products of other companies, including our competitors, and such resellers may elect to market our competitors' products and services in preference to our system solutions. In addition, we may offer similar services as those offered by certain of our resellers as we introduce our Payment-as-a-Service offerings. If one or more of our major resellers terminate their relationship with us, are acquired by one of our competitors or one of our competitor's resellers, or otherwise adversely change their relationship with us, we may be unsuccessful in replacing such relationship. The loss of any of our major resellers could impair our ability to sell our solutions and result in lower net revenues and income. It could also be time-consuming and expensive to replicate, either directly or through other resellers, the certifications and the applications developed by these resellers.

In addition, orders from our distributors and resellers depend on their sales volumes and inventory management decisions. We have experienced, and may in future periods experience, a significant decrease in our net revenues based on the timing of orders from our distributors, which generally varies based on distributor decisions on managing inventory levels, desired product mix and timing of new product introductions. Declines or deferrals of orders could materially and adversely affect our net revenues, operating results and cash flows.

We depend on a limited number of customers, including distributors and resellers, for a large percentage of our net revenues. If we do not effectively manage our relationships with them, our net revenues and operating results could suffer.

A significant percentage of our net revenues is attributable to a limited number of customers, including distributors and ISOs. If we are not able to adequately and timely respond to demands for new or additional products or features from any of our large customers, that customer may decide to reduce its order or not to purchase from us at all, which could have a material adverse effect on our business and results of operations. Our net revenues are dependent in part on the timing of purchases by our large customers. If any of our large customers significantly reduces or delays purchases from us or if we are required to sell products to them at reduced prices or on other terms less favorable to us, our net revenues, profitability, cash flows and net income could be materially and adversely affected.

Table of Contents

Timing for orders for our products and services can be back-end weighted within the fiscal quarter, which can make our net revenues difficult to predict and can negatively impact our business and results of operations.

The timing of our customer orders and related net revenues are often back-end weighted, meaning that during a particular fiscal quarter, a substantial portion of sales orders may be received, substantial product may be shipped, and substantial revenue may be recognized in the last month of the fiscal quarter. Timing of customer orders and related net revenues often become more back-end weighted during economic downturns or periods of uncertainty, as well as in markets where there is uncertainty related to acceptance and/or implementation of our products, such as that related to changes or potential changes in regulations or other local requirements that impact deployment of our products. These effects can also be exacerbated in markets where we depend on a limited number of customers, and where one or a few customers' decisions can have a significant impact on our results of operations in the fiscal quarter. Such back-end loading can also adversely affect our business and results of operations due to a number of additional factors including the following:

- the manufacturing processes at our third-party contract manufacturers could become concentrated in a shorter time period. This concentration of manufacturing could increase manufacturing costs, such as costs associated with the expediting of orders, and negatively impact our gross margins. The risk of higher levels of obsolete or excess inventory write-offs would also increase if we were to hold higher inventory levels to counteract this effect; the higher concentration of orders may make it difficult to accurately forecast component requirements and, as a result, we could experience a shortage of the components needed for production, possibly delaying shipments and causing lost orders;
- if we are unable to fill orders at the end of a quarter, shipments may be delayed. This could cause us to fail to meet our revenue and operating profit expectations for a particular quarter and could increase the fluctuation of quarterly results if shipments are delayed from one fiscal quarter to the next or orders are canceled by customers; and
- in order to fulfill orders at the end of a quarter, we may be forced to deliver our products using air freight which would result in increased distribution costs.

These factors can cause our net revenues to fluctuate and be difficult to predict in any given fiscal quarter. Any failure to meet our or analysts' revenue or operating profit expectations for a particular quarter could cause the market price of our stock to decline.



## Table of Contents

If we do not accurately forecast customer demand and effectively manage our product mix and inventory levels, we may lose sales from having too few or the wrong mix of products or incur costs associated with excess inventory.

If we inaccurately forecast demand for our products, we could end up with either excess or insufficient inventory to satisfy demand. This problem is exacerbated because our products are offered in a number of different configurations and with a variety of optional features, and we generally receive a significant volume of customer orders towards the end of each fiscal quarter which leaves us little room to adjust inventory mix to match demand, as discussed under “Timing for orders for our products and services can be back-end weighted within the fiscal quarter, which can make our net revenues difficult to predict and can negatively impact our business and results of operations.” During the transition from an existing product to a new replacement product, we must accurately predict the demand for the existing and the new product. Furthermore, introducing new products into our current markets or existing products into new markets involves the uncertainty of whether the market will adopt our product in the volumes and time frames that we anticipate or at all. Our inability to properly manage our inventory levels could lead to increased expenses associated with writing off excessive or obsolete inventory, additional shipping costs to meet immediate demand and a corresponding decline in gross margins, or lost sales. If we do not accurately predict demand, we could also incur increased expenses associated with binding commitments to certain third-party contract manufacturers and suppliers which would negatively impact our gross margins and operating results. For example, as of October 31, 2015, the amount of purchase commitments issued to contract manufacturers and component suppliers totaled approximately \$178.4 million. Of this amount, \$10.4 million has been recorded in Accruals and other current liabilities in our Consolidated Balance Sheets because these commitments are not expected to have future value to us. For additional information regarding our commitments to third-party manufacturers and suppliers, see Note 12, Commitments and Contingencies, in the Notes to Consolidated Financial Statements of our Annual Report on Form 10-K filed with the SEC for the fiscal year ended October 31, 2015. During times of economic uncertainty, such as the global economic recession that continues to impact certain parts of Europe and economic fluctuations in China, it becomes more difficult to accurately forecast demand and manage our inventory levels. Deteriorating market conditions have in the past and can in future periods cause us to incur additional costs associated with excess and obsolete inventory, scrap, and excess inventory held by our contract manufacturers.

We may accumulate excess or obsolete inventory that could result in unanticipated price reductions and write-downs and adversely affect our financial condition.

In formulating our solutions, we have focused our efforts on providing our customers with solutions that have high levels of functionality, which requires us to develop and incorporate new and evolving technologies. This approach tends to increase the risk of obsolescence for products and components we hold in inventory and may compound the difficulties posed by other factors that affect our inventory levels, including the following:

- maintaining significant inventory of components that are in limited supply;
- buying components in bulk for better pricing;
  - entering into purchase commitments based on early estimates of quantities for longer lead time components;
- responding to the unpredictable demand for products;
- cancellation of customer orders;
- responding to customer requests for quick delivery schedules; and
- timing of end-of-life decisions regarding products.

The accumulation of excess or obsolete inventory has in the past resulted in and may in future periods result in price reductions and inventory write-downs and scrap, which could, sometimes materially, adversely affect our business, results of operations and financial condition. For example, as a result of the expiration of PCI 1.3 standards in April 2014, we can no longer sell our products that are only compliant with PCI 1.3 or earlier standards except under limited

circumstances, primarily as one-for-one in-kind replacements of devices for repair and replacement. For the fiscal year ended October 31, 2013, we incurred costs for obsolete inventory, scrap, and purchase commitments for excess components at contract manufacturers of \$26.5 million, an increase of \$13.7 million compared to those for the fiscal year ended October 31, 2012, due to lower-than-anticipated systems sales volumes and potential obsolescence because of the PCI 1.3 standard expiration.

Table of Contents

We are exposed to credit risk with some of our customers and to credit exposures and currency controls in certain markets, which could result in material losses.

A significant portion of our net revenues are on an open credit basis, with typical payment terms of up to 60 days in the U.S. and longer in some international markets due to local customs or conditions. In the past, there have been bankruptcies among our customer base. Credit risks may be higher and collections may be more difficult to enforce in emerging markets where we conduct business, including for example where the market for our products and solutions is still developing and their acceptance uncertain, and future losses, if incurred, could harm our business and have a material adverse effect on our operating results and financial condition. Also, certain customers that are invoiced in U.S. dollars, such as those based in Venezuela and Nigeria and other countries whose economies are significantly impacted by the price of oil, have experienced, and may continue to experience, difficulties in obtaining U.S. dollars due to local currency controls, and therefore may not be able to remit timely payment to us. Additionally, instability or uncertainty in global or regional economic, political or military conditions may make it more difficult for some customers to obtain financing or access U.S. dollar currency, and their ability to pay could be adversely impacted, which in turn could have a material adverse impact on our business, cash flows, operating results and financial condition.

We depend upon third parties to manufacture our systems and to supply the components necessary to manufacture our products, and in some cases we are dependent upon sole source suppliers to manufacture our systems.

We utilize a limited number of third parties to manufacture our hardware products pursuant to our specifications and rely upon these contract manufacturers to produce and deliver products on a timely basis and at an acceptable cost or to otherwise meet our product demands. Further, a material portion of these third-party manufacturing activities are concentrated in China. Disruptions to the business, financial stability or operations, including due to strikes, labor disputes or other disruptions to the workforce, of these contract manufacturers, or to their ability to produce the products we require in accordance with our and our customers' requirements, and particularly disruptions to the manufacturing operations in China including due to geological disruptions such as earthquakes, could significantly affect our ability to fulfill customer demand on a timely basis which could materially harm our net revenues and results of operations. Substantially all of our manufacturing is currently handled by our third-party contract manufacturers and our dependency on our third-party contract manufacturers could exacerbate these risks.

Components such as application specific integrated circuits, or ASICs, microprocessors, wireless modules, modems, and printer mechanisms that are necessary to manufacture and assemble our systems are sourced either directly by us or on our behalf by our contract manufacturers from a variety of component suppliers selected by us. Certain of the components are specifically customized for use in our products and are obtained from sole source suppliers on a purchase order basis. Disruptions to the business, financial stability or operations, including due to strikes, labor disputes or other disruptions to the workforce, of our suppliers, and particularly sole source suppliers, or to the distribution and transportation of our products may also impact the availability of components to us in the quantities or within the timeframe we require. Any prolonged component shortage could materially and adversely affect our business and results of operations. Component shortages have resulted in increased costs for certain components and continued cost increases could negatively impact our gross margins and profitability. If our suppliers are unable or unwilling to deliver the quantities that we require within the timeframe that we require, we would be faced with a shortage of components. We also experience from time to time an increase in the lead time for delivery of some of our key components. We may not be able to find alternative sources in a timely manner if suppliers of our key components become unwilling or unable to provide us with adequate supplies of these key components when we need them or if they increase their prices. If we are unable to obtain sufficient key required components, or to develop alternative sources if and as required in the future, or to replace our component and factory tooling for our products in a timely manner if they are damaged or destroyed, we could experience delays or reductions in product shipments. This could harm our relationships with our customers and cause our net revenues to decline. Even if we are able to

secure alternative sources or replace our tooling in a timely manner, our costs could increase. Any of these events could adversely affect our results of operations.

Table of Contents

Shipments of electronic payment systems may be delayed by factors outside of our control, which can harm our reputation and our relationships with our customers.

The shipment of payment systems requires us or our manufacturers, distributors, or other agents to obtain customs or other government certifications and approvals, and, on occasion, to submit to physical inspection of our systems in transit. Failure to satisfy these requirements, and the very process of trying to satisfy them, can lead to lengthy delays in the delivery of our solutions to our direct or indirect customers. Because we depend upon third-party carriers for the timely delivery of our products we may face delays in delivery due to reasons outside our control. Delays and unreliable delivery by us may harm our reputation in the industry and our relationships with our customers and result in canceled orders, any of which could adversely affect our results of operations and business.

We may be subject to future impairment charges due to potential declines in the fair value of our assets.

As a result of our acquisitions, particularly that of Lipman in November 2006, Hypercom in August 2011 and Point in December 2011, we have recorded significant goodwill and intangible assets on our balance sheet. We test goodwill and intangible assets for impairment on a periodic basis as required, and whenever events or changes in circumstances indicate that the carrying value may not be recoverable. The events or changes that could require us to test our goodwill and intangible assets for impairment include a reduction in our stock price and market capitalization and changes in our estimated future cash flows or changes in rates of growth in our industry or in any of our reporting units or lines of business.

During the first quarter of 2016, we realigned our organizational structure and changed our reportable segments to be Verifone Systems and Verifone Services. As a result of this change, we have realigned our reporting units to be Verifone Systems, Taxi Solutions, and Verifone Payment Services. In connection with this reporting unit realignment, we also updated our goodwill impairment assessment based on a quantitative analysis and concluded that there was no impairment.

Our evaluation of potential impairment of goodwill is subjective, requires significant judgment and could be negatively affected by a variety of factors, including declines in our stock price, failure to meet our internal forecasts, and weakening of macroeconomic conditions or significant changes in management structure or business strategies. If we determine in the future that there is potential further impairment in any of our reporting units, we may be required to record additional charges to earnings, which could materially and adversely affect our financial results and could also materially and adversely affect our business. See Note 8, Goodwill and Purchased Intangible Assets, in the Notes to Condensed Consolidated Financial Statements and Part I, Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations - Critical Accounting Policies and Estimates -- Goodwill, of this Quarterly Report on Form 10-Q for additional information related to impairment of goodwill and intangible assets.

We have operations in Israel and therefore our results of operations may be adversely affected by political or economic instability or military operations in or around Israel.

We have offices and personnel in Israel. Therefore, political, economic, and military conditions in Israel directly affect our operations. The outcome of peace efforts between Israel and its Arab neighbors remains uncertain. Any armed conflicts, such as ongoing military conflict in the Gaza Strip, or further political instability in the region is likely to negatively affect business conditions and materially harm our results of operations. Furthermore, several countries continue to restrict or ban business with Israel, Israeli companies and companies with significant Israeli operations. These restrictive laws and policies may seriously limit our ability to make sales in those countries.

In addition, many employees in Israel are obligated to perform between 30 to 40 days of military reserve duty annually and are subject to being called for active duty under emergency circumstances. If a military conflict arises,

these individuals could be required to serve in the military for extended periods of time. Our operations in Israel could be disrupted by the absence for a significant period of one or more key employees or a significant number of other employees due to military service. Any disruption in our operations in Israel could materially and adversely affect our business.

Table of Contents

Force majeure events, such as terrorist attacks, other acts of violence or war and political instability may adversely affect us.

Terrorist attacks, war, and international political instability may disrupt our ability to generate net revenues. Such events may negatively affect our ability to maintain net revenues and to develop new business relationships. Because a substantial and growing part of our net revenues is derived from sales and services to customers outside of the U.S. and we have our electronic payment systems manufactured outside the U.S., terrorist attacks, war, and international political instability anywhere may decrease international demand for our products and inhibit customer development opportunities abroad, disrupt our supply chain, and impair our ability to deliver our electronic payment systems, which could materially and adversely affect our net revenues or results of operations. Economic and political instability, particularly in the Middle East or OPEC member countries, may also disrupt the production or supply of fuel which could increase our costs related to shipment and distribution of our products. Any of these events may also disrupt global financial markets and precipitate a decline in the price of our stock. See also "Sanctions against Russia, and Russia's response to those sanctions, including the imposition of sanctions by Russia, could materially adversely affect our business, results of operations and financial condition" and "We have operations in Israel and therefore our results of operations may be adversely affected by political or economic instability or military operations in or around Israel."

Natural or man-made disasters, business interruptions and health epidemics could delay our ability to receive or ship our products or provide our services, or otherwise disrupt our business.

Our worldwide operations could be subject to earthquakes, power shortages, telecommunications failures, water shortages, tsunamis, floods, hurricanes, typhoons, fires, extreme weather conditions, health epidemics, and other natural or man-made disasters or business interruptions, all of which could impact our ability to conduct vital business operations, including the ability of our employees to access work sites or customer sites where urgent or time critical repairs are needed. The occurrence of any of these business disruptions could seriously harm our business, our revenue and financial condition, and increase our costs and expenses. If our or our manufacturers' facilities are damaged or destroyed, we would be unable to distribute our products or provide our services on a timely basis, which could harm our business. Our corporate headquarters, and a portion of our research and development activities, are located in California, and other critical business operations and some of our suppliers are located in California and Asia, near major earthquake faults. Certain key servers and information systems as well as a shared services center are located in Florida, which has in the past experienced major hurricanes and similar extreme weather. Any disruption of our operations in these areas could materially affect our operations and harm our business. In addition, we increasingly rely on our computer systems and servers to conduct our business. For example, much of our order fulfillment process is automated and the order information is stored on our servers. If our computer systems and servers are impaired or cease functioning, even for a short period, our ability to serve our customers and fulfill orders would be disrupted, our reputation could be damaged and our net revenues could be materially and adversely affected. Moreover, if our computer information systems or communication systems, or those of our vendors or customers, are subject to hacker attacks or other disruptions, our business could suffer. Although we have established and tested back-up systems and facilities to run our critical business operations in case of a business interruption, all of our systems and facilities are not yet fully redundant or fully tested. We are still in the process of formalizing a comprehensive disaster recovery plan and continue to rely on regional disaster recovery plans in some cases. In addition, our back-up operations may be inadequate under certain circumstances and our business interruption insurance may not be enough to compensate us for any losses that we may incur, which could adversely affect our business, results of operations and financial condition, as well as harm our reputation, and could cause our stock price to decline significantly.

Table of Contents

Risks Related to Our Legal and Regulatory Environment

Our results of operations will suffer if we cannot comply with industry and government regulations and standards, or if changing standards do not continue to drive upgrade cycles.

Our systems must meet industry standards imposed by payment systems standards setting organizations such as EMVCo LLC, credit card associations such as Visa, MasterCard, and other credit card associations and standard setting organizations such as PCI SSC, Intermec and the U.K. Cards Association and other local organizations. New standards are continually being adopted or proposed as a result of worldwide anti-fraud initiatives, encryption of cardholder data, the increasing need for system compatibility and technology developments such as wireless and wireline IP communication. Our solutions also must comply with government regulations, including those imposed by telecommunications authorities and independent standards groups worldwide regarding emissions, radiation, and connections with telecommunications and radio networks, as well as data privacy laws and regulations which regulate the collection, compilation, aggregation, sharing or use of consumer information. We cannot be sure that we will be able to design our solutions to comply with future standards or regulations on a timely basis, if at all. Compliance with these standards could increase the cost of developing or producing our solutions. New products designed to meet any new standards need to be introduced to the market and ordinarily need to be certified by the credit card associations and our customers and, in some cases, local certification bodies, before being purchased. These certification processes are costly and time consuming and increase the amount of time it takes to introduce new products and sell our products. Our business has been in the past and continues to be adversely affected by our failure to timely obtain local certifications in some markets for certain of our products. Moreover, certain uses of our products may subject us to additional regulations and licensing requirements. For example, use of our products in taxis requires additional licensing and may subject us to certain taxi business regulations in the various jurisdictions we operate in. At the same time, as ridesharing companies and other taxi alternative companies expand, depending on regulatory outcomes and developments, the market for our taxi products could be negatively impacted. Various aspects of our services business also are or may be subject to additional regulations and licensing requirements as we expand into new areas. Our business, net revenues and financial condition could be adversely affected if we cannot comply with new or existing industry standards, or obtain or retain necessary regulatory approval or certifications in a timely fashion, or if compliance results in increasing costs of our products. Selling products that are non-compliant may result in fines against us or our customers, which we may be liable to pay. In addition, even if our products are designed to be compliant, compliance with certain security standards is determined based on the merchant's or service provider's network environment in which our systems are installed and, therefore, is dependent upon a number of additional factors such as proper installation of the components of the environment including our systems, compliance of software and system components provided by other vendors, implementation of compliant security processes and business practices and adherence to such processes and practices. Our business and financial condition, as well as our reputation and market share, could be adversely affected if we do not comply with new or existing industry standards and regulations, or obtain or retain necessary regulatory approval or certifications in a timely fashion, or if compliance results in increasing costs of our products.

On the other hand, our business also benefits from changes in industry standards and government regulations as well as technological changes, which are large drivers of customer upgrade cycles. For example, as EMV standards are implemented in the U.S., we expect that our business could benefit as customers move to upgrade their systems. Nevertheless, if these or other standards are not implemented on the timeline we expect, or at all, or if they are implemented but we cannot deliver products that comply with these standards in a timely manner or at all, our business will suffer. If customers do not continue to upgrade their terminals due to technological changes or changes in standards or government regulations, demand for our offerings could reach a saturation point, which would adversely affect our results of operations.





Table of Contents

Changes in laws and regulations of privacy and protection of user data could adversely affect our business.

We are subject to data privacy and protection laws and regulations that apply to the collection, transmission, storage and use of proprietary information and personally-identifying information. The regulatory environment surrounding information security and data privacy varies from jurisdiction to jurisdiction and is constantly evolving and increasingly demanding. The restrictions imposed by such laws continue to develop and may require us to incur substantial costs, adopt additional compliance measures, such as notification requirements and corrective actions in the event of a security breach, and/or change our current or planned business models. For example, in the U.S., legislation is pending regarding restrictions on the use of geolocation information collected by mobile devices without consumer consent. If adopted, such legislation or any other restrictions imposed on use of location-based information or geolocation tracking could impact our implementation of mobile-based payments solutions that utilize such information or technology. In addition, we are already subject to strict data privacy laws in the European Union and other jurisdictions governing the collection, transmission, storage and use of employee data and personally-identifying information. Such regulations increase our compliance and administrative burden significantly.

If our current security measures and data protection policies and controls are found to be non-compliant with relevant laws or regulations in any jurisdiction where we conduct business, we may be subject to penalties and fines, and may need to expend significant resources to implement additional data protection measures. In addition, we may be required to modify the features and functionality of our system offerings in a way that is less attractive to customers.

We are party to a number of lawsuits and tax assessments and we may be named in additional litigation and assessments, all of which are likely to require significant management time and attention and expenses and may result in unfavorable outcomes that could have a material adverse effect on our business, financial condition, results of operations and cash flows.

We are currently a party in several litigation proceedings. If any of these proceedings are resolved adversely to us, this could have a material adverse effect on our business, financial condition, results of operations or cash flows. For example, in connection with the restatement of our historical interim financial statements during fiscal year 2007, a number of securities class action complaints were filed against us and certain of our officers, and purported derivative actions were also filed against certain of our current and former directors and officers. As described in Part I, Item 3, Legal Proceedings, of our Annual Report on Form 10-K for the fiscal year ended October 31, 2014, we settled with the plaintiffs in the securities class action case captioned *In re VeriFone Holdings, Inc. Securities Litigation* for a total of \$95.0 million. In fiscal year 2013, we recorded a total expense of \$61.2 million for this securities class action, which represents the amount of the settlement that was not covered by insurance.

We are also subject to a number of pending tax assessment matters, particularly in Brazil where such assessments can be difficult to defend and result in substantial losses, and in Israel, where we are currently under audit by the Israel Tax Authority for fiscal years 2008 through 2013 and subject to a substantial potential tax liability and deficiency penalty assessment in the range of several hundred million dollars. While we continue to believe the Israel Tax Authority assessment is without merit and plan on appealing the assessment, we cannot be sure of the outcome and our ultimate aggregate exposure. See Note 5, Income Taxes and Note 11, Commitments and Contingencies, in the Notes to Condensed Consolidated Financial Statements of this Quarterly Report on Form 10-Q for additional information related to tax assessment matters.

Further, our operating results or financial condition may also be adversely impacted by claims or liabilities that we assume from an acquired company or that are otherwise related to an acquisition. For example, in connection with our acquisition of Hypercom, we have, except for certain matters related to the businesses divested by Hypercom, generally assumed all of Hypercom's litigation proceedings and tax assessments, and may also be liable for certain matters arising after closing of the Hypercom divestitures but related to pre-closing operations.



Table of Contents

We also are subject to the risk of additional litigation and regulatory proceedings or actions in connection with the restatement of our financial statements. We have responded to inquiries and provided information and documents related to the restatement to the SEC, the U.S. Department of Justice, the New York Stock Exchange, and the Chicago Board Options Exchange. We were the subject of a Wells Notice from the SEC stating that the staff of the SEC's Division of Enforcement intended to recommend that the SEC bring a civil injunctive action against us, alleging violations of the federal securities laws arising from the restatement, which we settled in November 2009. Although we have settled this matter with the SEC, additional regulatory inquiries may also be commenced by other U.S. federal, state or foreign regulatory agencies. In addition, we may in the future be subject to additional litigation or other proceedings or actions arising in relation to the restatement of our historical interim financial statements.

Furthermore, we are, and in the future may be, involved in various litigation and regulatory matters, such as commercial disputes and labor and employment claims, that arise in the ordinary course of business.

Our insurance policies may not cover certain claims that are filed against us or may not be sufficient to cover all of our costs for defending such actions or paying any damages in the event of an unfavorable outcome. In addition, we may be obligated to indemnify (and advance legal expenses to) both current and former officers, employees and directors in connection with the securities class action and derivative action matters. Although we currently hold insurance policies for the benefit of our directors and officers, such insurance coverage may not be sufficient in some or all of these matters. Furthermore, our insurance carriers may seek to deny coverage in some or all of these matters, in which case we may have to fund the indemnification amounts owed to such directors and officers ourselves. Because we have a number of pending litigation matters, these amounts may be material.

The amount of time and resources required to resolve these lawsuits is unpredictable, and defending ourselves is likely to divert management's attention from the day-to-day operations of our business, which could adversely affect our business, financial condition, and results of operations. We have in the past incurred and expect to continue to incur significant expenses in connection with these matters. Many members of our senior management team and our Board of Directors have devoted and may be required to devote additional time to our pending litigation matters. Certain of these individuals are named defendants in the litigation related to the restatement actions. If our senior management is unable to devote sufficient time in the future to developing and pursuing our strategic business initiatives and running ongoing business operations, there may be a material adverse effect on our business, financial condition and results of operations.

The outcome of litigation and tax assessments is inherently difficult to predict. If any such litigation or tax assessment is resolved adversely to us (whether as a result of a court judgment or a decision by us to settle litigation to avoid the distraction, expense and inherent risks of continued litigation), this could have a material adverse effect on our business, financial condition, results of operations and cash flows. Furthermore, even when we are able to reasonably estimate the probable loss and thus record an accrual for such probable and reasonably estimable loss contingency, the accrual may change due to new developments or changes in our estimates or the amount of our liability could exceed the accrual. For a description of our material pending litigation, see Part II, Item 1, Legal Proceedings, of this Quarterly Report on Form 10-Q.

Our business may suffer if we are sued for infringing the intellectual property rights of third parties, or if we are unable to obtain rights to third-party intellectual property on which we depend.

Third parties have in the past asserted and may in the future assert claims that our products and services infringe their proprietary rights. Such infringement claims, even if meritless, may cause us to incur significant costs in defending against or settling those claims, whether directly or as a result of indemnification obligations. We may be required to discontinue using and selling any infringing technology and services, to expend resources to develop non-infringing technology or to purchase licenses or pay royalties for other technology. Similarly, we depend on our ability to license

intellectual property from third parties. The third parties from whom we license technology may become unwilling to license to us on acceptable terms intellectual property that is necessary to our business. In addition, we may be unable to acquire licenses for other technology necessary for our business on reasonable commercial terms or at all. As a result, we may be unable to continue to offer the solutions and services upon which our business depends.

## Table of Contents

We have received, and have currently pending, third-party infringement claims and may receive additional notices of claims of infringement in the future. As we expand into other payment technologies and as competition in this area increases, it is possible that the rate at which third parties bring claims will increase. Infringement claims may cause us to incur significant costs in defending against those claims or to settle claims to avoid costly or protracted litigation even if we believe those claims are without merit. Claims may result in additional protracted and costly litigation. There can be no assurance that we will prevail in any such actions or that any license required under any such patent or other intellectual property would be made available on commercially acceptable terms, if at all. An unfavorable outcome in any such litigation could result in a significant judgment of damages against us, which could materially and adversely impact our operating results, financial condition and cash flows. See Note 11, Commitments and Contingencies, in the Notes to Condensed Consolidated Financial Statements of this Quarterly Report on Form 10-Q.

Our proprietary technology is difficult to protect and unauthorized use of our proprietary technology by third parties may impair our ability to compete effectively.

We may not be able to protect our proprietary technology, which could enable competitors to develop services that compete with our own. We rely on patent, copyright, trademark, and trade secret laws, as well as confidentiality, licensing and other contractual arrangements to establish and protect the proprietary aspects of our solutions. Institution of legal proceedings to enforce our intellectual property rights could be costly and divert the efforts and attention of our management and technical personnel from other business operations. In addition, there can be no assurance that such proceedings would be determined in our favor. We do not have patent protection for certain important aspects of our current solutions. The laws of some countries in which we sell our solutions and services may not protect software and intellectual property rights to the same extent as the laws in the U.S. If we are unable to prevent misappropriation of our proprietary technology, competitors or others may be able to use and adapt such technology, which could diminish our competitive advantage and cause us to lose customers to competitors.

Our business and results of operations may be adversely affected if we do not comply with legal and regulatory requirements that apply to our products, including environmental laws and regulations that regulate substances contained in our products.

We may be subject to various other legal and regulatory requirements related to the manufacture and sale of our products, such as a European Union directive that places restrictions on the use of hazardous substances (RoHS and RoHS2) in electronic equipment, a European Union directive on WEEE, the European Union's REACH, and the environmental regulations under China RoHS. RoHS and RoHS2 sets a framework for producers' obligations in relation to manufacturing (including the amounts of named hazardous substances contained in products sold) and WEEE sets a framework for treatment, labeling, recovery, and recycling of electronic products in the European Union which may require us to alter the manufacturing of the physical devices that include our solutions and/or require active steps to promote recycling of materials and components. REACH imposes chemicals regulation and controls including requirements for registration of chemicals on the European Union market. In addition, similar legislation could be enacted in other jurisdictions, including in the U.S. where many states have already enacted state-level programs and requirements for recycling of certain electronic goods. In addition, climate change legislation in the U.S. is a significant topic of discussion and may generate federal or other regulatory responses in the near future. If we do not comply with environmental law and regulations, we may suffer a loss of revenue, be unable to sell in certain markets or countries, be subject to penalties and enforced fees, and/or suffer a competitive disadvantage. Customers may impose certain requirements or levels of compliance due to these regulations and programs that may increase our costs of doing business. Furthermore, the costs to comply with RoHS, RoHS2, WEEE, REACH and China RoHS, or with current and future environmental and worker health and safety laws may have a material adverse effect on our business, results of operations and financial condition.



Table of Contents

In 2012, the SEC adopted rules pursuant to Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act requiring disclosure of the use of certain minerals that are mined from the Democratic Republic of Congo and adjoining countries. We filed our most recent report under the disclosure requirement in June 2015 for the 2014 calendar year. Because our supply chain is complex, in preparation of such report, we were dependent on the implementation of diligence procedures we put in place to determine the sources of conflict minerals that may be used or are necessary to the production of our products and, if applicable, potential changes to products, processes or sources of supply in response to the findings resulting from such verification activities, as well as information provided by many of our suppliers. To the extent the information we received from our suppliers is inaccurate or inadequate or our processes in obtaining such information do not satisfy the SEC's diligence requirements, we may be unable to sufficiently verify the origins of conflict minerals used in our products and could face reputational risks. In addition, we have incurred and expect to continue to incur costs associated with complying with these disclosure requirements, including for conducting diligence procedures. Moreover, these rules could adversely affect the sourcing, supply and pricing of materials used in our products, particularly if the number of suppliers offering minerals identified as "conflict minerals" that are sourced from locations other than the Democratic Republic of Congo and adjoining countries is limited. We may also suffer reputational harm if we determine that certain of our products contain minerals not determined to be conflict-free yet are unable to alter our products, processes or sources of supply to avoid such materials.

Changes in our effective tax rate could adversely affect our results of operations.

Our effective tax rate could be adversely affected by a number of factors, including shifts in the mix of pretax profits and losses by tax jurisdiction, loss or cessation of tax holidays or other tax benefits, our ability to generate tax credits, our ability to utilize net operating loss carryforwards, the tax impact of nondeductible compensation, and changes in accounting rules, tax laws and regulations, and related interpretations, in the jurisdictions in which we operate. The U.S., countries in the European Union and other countries where we do business have been considering changes in tax laws applicable to multinational corporations. These potential changes in tax laws could have an adverse effect on our effective tax rate.

We are subject to ongoing tax audits in various jurisdictions. Although we regularly assess the likely outcomes of such audits in order to determine the appropriateness of our tax provision, such assessments involve significant judgment and there can be no assurance that we will accurately predict the outcomes of these audits, and the actual outcomes of these audits could have a material impact on our net income or financial condition. We have not provided for U.S. federal and state income taxes or foreign withholding taxes that may result from future remittances of undistributed earnings of our foreign subsidiaries. Any changes to these factors could have an adverse effect on our results of operations.

We have previously received tax benefits related to our operations in Israel and Singapore. Our subsidiary in Israel (formerly Lipman) previously received tax benefits under Israeli law for capital investments that were designated as "Approved Enterprises" through October 31, 2009. To the extent that these prior year earnings are distributed or deemed distributed, our Israeli subsidiary could be required to remit corporate income tax on these earnings at the applicable rate, between 12.5% and 36.25%. In addition, our subsidiary in Singapore previously received tax benefits under the Singapore Pioneer Tax Holiday provision (the "Tax Holiday") which expired on October 31, 2012. Our effective tax rate could be adversely affected to the extent that tax authorities in Singapore challenge our Tax Holiday.



Table of Contents

The value of our deferred tax assets may not be realizable to the extent our future profits are less than we have projected and we may be required to record valuation allowances against previously-booked deferred tax assets, which may have a material adverse effect on our results of operations and our financial condition.

Our income tax expense includes deferred income taxes arising from temporary differences between the financial reporting and tax bases of assets and liabilities, capital loss carry-forwards and net operating losses. We evaluate the realizability of our deferred income tax assets and assess the need for a valuation allowance on an ongoing basis. In evaluating our deferred income tax assets, we consider whether it is more likely than not that the deferred income tax assets will be realized. The ultimate realization of our deferred income tax assets depends upon generating sufficient future taxable income during the periods in which our temporary differences become deductible and before our capital loss carry-forwards and net operating losses expire. Our assessment of the realizability of our deferred income tax assets requires significant judgment. If we fail to achieve our projections or if we need to lower our projections, we may not have sufficient evidence of our ability to realize our deferred tax assets, and we may need to increase our valuation allowance. For example, for the fiscal year ended October 31, 2013 we recorded a \$245.0 million valuation allowance against a significant portion of our deferred tax assets, primarily in the U.S., because our three year cumulative U.S. pretax losses raised uncertainty about the likelihood of realization of those deferred tax assets. For further information regarding this valuation allowance, see Note 6, Income Taxes, in the Notes to Consolidated Financial Statements of our Annual Report on Form 10-K for the fiscal year ended October 31, 2015. There is no assurance that we will not record a valuation allowance in future periods against previously-booked deferred tax assets. Any increase in the valuation allowance would result in additional income tax expense which could have a material adverse effect on our results of operations and financial condition.

Our internal processes and control over financial reporting have in prior periods been deemed inadequate.

In certain prior periods we reported material weaknesses in our internal control over financial reporting, which we have remedied. These material weaknesses in our internal control over financial reporting contributed to our need to restate previously reported interim financial information for each of the first three quarters of our fiscal year ended October 31, 2007, and to the delays in the filing of our Annual Report on Form 10-K for fiscal year 2007. We also were unable to file our quarterly reports on Form 10-Q for our fiscal quarters ended January 31, 2008 and April 30, 2008 on a timely basis.

Although we have implemented improved controls and remedied these material weaknesses, these controls may not be sufficient to detect or prevent errors in financial reporting in future periods and will require continued enhancement to accommodate our rapid growth in operations both organically and from acquisitions. We may hire additional employees and may also engage additional consultants in these and other key areas. Competition for qualified financial control and accounting professionals in the geographic areas in which we operate is intense and there can be no assurance that we will be able to hire and retain these individuals.

Our business could be adversely impacted if we have deficiencies in our disclosure controls and procedures or internal control over financial reporting.

The design and effectiveness of our disclosure controls and procedures and internal control over financial reporting may not prevent all errors, misstatements or misrepresentations. While management continually reviews the effectiveness of our disclosure controls and procedures and internal control over financial reporting, there can be no guarantee that our internal control over financial reporting will be effective in accomplishing all control objectives all of the time. Deficiencies, including any material weakness, in our internal control over financial reporting that may occur in the future could result in misstatements of our results of operations, restatements of our financial statements, a decline in the price of our securities, or otherwise materially adversely affect our business, reputation, results of operations, financial condition or liquidity.



Table of Contents

Risks Related to Our Capital Structure

Our secured credit facility contains restrictive and financial covenants. If we are unable to comply with these covenants, we will be in default. A default could result in the acceleration of our outstanding indebtedness, which would have an adverse effect on our business and stock price.

We have senior secured credit facilities pursuant to a credit agreement as described in Note 9, Financings, in the Notes to Condensed Consolidated Financial Statements to this Quarterly Report on Form 10-Q, with outstanding loan balances of \$962.2 million as of April 30, 2016.

The 2011 Credit Agreement contains customary covenants that require maintenance of certain specified financial ratios and restricts the ability of certain of our subsidiaries to make certain distributions with respect to their capital stock, prepay other debt, encumber their assets, incur additional indebtedness, make capital expenditures above specified levels, engage in certain business combinations, or undertake various other corporate activities. Therefore, as a practical matter, these covenants restrict our ability to engage in or benefit from such activities. Further, VeriFone, Inc. must limit its leverage ratio and maintain its interest coverage ratio at or above specified thresholds. In addition, we have, in order to secure our repayment obligations under the 2011 Credit Agreement, pledged a substantial amount of our assets and properties. This pledge may reduce our operating flexibility because it restricts our ability to dispose of these secured assets or engage in other transactions that may be beneficial to us.

If we are unable to comply with the covenants in the 2011 Credit Agreement, we will be in default, which could result in the acceleration of our outstanding indebtedness. If acceleration occurs, we may not be able to repay our debt and we may not be able to borrow sufficient additional funds to refinance our debt. In addition, under the terms of the 2011 Credit Agreement, increases in our leverage ratio could result in increased interest rates and, therefore, higher debt service costs. If we were to default in performance under the 2011 Credit Agreement, we may pursue an amendment or waiver from our lenders, but there can be no assurance that the lenders would grant such an amendment or waiver and, in light of current credit market conditions, any such amendment or waiver requested is likely to be on terms, including additional fees, as well as increased interest rates and other more stringent terms and conditions that would be materially disadvantageous to us.

See Note 9, Financings, in the Notes to Condensed Consolidated Financial Statements of this Quarterly Report on Form 10-Q for additional information regarding the 2011 Credit Agreement.

Our indebtedness and debt service obligations under our 2011 Credit Agreement are substantial and may adversely affect our cash flow, cash position, and stock price.

Our outstanding indebtedness and debt service obligations are substantial. As of April 30, 2016, we had total indebtedness outstanding of \$962.2 million related to the 2011 Credit Agreement, payable in quarterly installments through July 8, 2021. Outstanding amounts may be subject to mandatory prepayment with the proceeds of certain asset sales and debt issuances and, for certain of the loan balances, from a portion of annual excess cash flows (as determined in the 2011 Credit Agreement) depending on our total net leverage ratio. See Note 10, Financings, in the Notes to Consolidated Financial Statements of our Annual Report on Form 10-K for the fiscal year ended October 31, 2015 for a schedule of the principal payments due under our financings.

Table of Contents

We intend to fulfill our debt service obligations from existing cash and cash from operations. A substantial portion of our cash balances and cash generated from operations are held by our foreign subsidiaries. If we decide to distribute or use such cash and cash equivalents outside those foreign jurisdictions, including a distribution to the U.S. we may be subject to additional taxes or costs. In the future, if we are unable to generate or raise additional cash sufficient to meet our debt service obligations and need to use more of our existing cash than planned or to liquidate investments in order to fund these obligations, we may have to delay or curtail the development and/or the sales and marketing of new payment systems and reduce the amount of expected cash flow available for other purposes, including capital expenditures, investments, acquisitions and dividends. If we are unable to generate sufficient cash flows or other sources of liquidity to meet our debt service requirements, our lenders may declare a default on the 2011 Credit Agreement which could result in the termination of commitments under the 2011 Credit Agreement, the declaration that all outstanding loans are immediately due and payable in whole or in part, and the requirement of cash collateral deposits in respect of outstanding letters of credit.

Interest rates applicable to our debt are expected to fluctuate based on economic and market factors that are beyond our control. In particular, all of the outstanding debt under the 2011 Credit Agreement has a floating interest rate. Although we have entered into a swap arrangement that converts the floating interest rate to a fixed interest rate for a substantial portion of the principal amount under the 2011 Credit Agreement through March 2018, any significant increase in market interest rates, and in particular the short-term LIBOR rates, could result in a significant increase in interest expense on the portion of our debt not covered by such swap arrangement and during periods after the expiration of such swap arrangement, which could negatively impact our net income and cash flows.

Our indebtedness could have significant additional negative consequences, including, without limitation:

- increasing our vulnerability to general adverse economic conditions;
- limiting our ability to obtain additional financing on acceptable terms; and
- placing us at a possible competitive disadvantage to less-leveraged competitors and competitors that have better access to capital resources.

The conditions of the U.S. and international capital markets may have an adverse effect on other financial transactions.

Deterioration in the U.S. and international capital markets has in the past had an adverse effect on certain of our financial transactions. If financial institutions that have extended credit commitments to us, including under the 2011 Credit Agreement, or have entered into hedge, insurance or similar transactions with us, are adversely affected by the conditions of the U.S. and international capital markets, they may become unable to fund borrowings under their credit commitments to us or otherwise fulfill their obligations under the relevant transactions, which could have a material and adverse impact on our financial condition and our ability to borrow additional funds, if needed, for working capital, capital expenditures, acquisitions, and other corporate purposes.

Table of Contents

Some provisions of our certificate of incorporation and bylaws may delay or prevent transactions that many stockholders may favor.

Some provisions of our certificate of incorporation and bylaws may have the effect of delaying, discouraging or preventing a merger or acquisition that our stockholders may consider favorable, including transactions in which stockholders might receive a premium for their shares. These provisions include:

- authorization of the issuance of “blank check” preferred stock without the need for action by stockholders;
- the amendment of our organizational documents only by the affirmative vote of the holders of two-thirds of the shares of our capital stock entitled to vote at an election of directors;
- provision that any vacancy on the board of directors, however occurring, including a vacancy resulting from an enlargement of the board, may only be filled by vote of the directors then in office;
- inability of stockholders to call special meetings of stockholders; and
- advance notice requirements for board nominations and proposing matters to be acted on by stockholders at annual stockholder meetings.

Our share price has been volatile and we expect that the price of our stock may continue to fluctuate substantially.

Our stock price has fluctuated substantially since our initial public offering in 2005, for example, due to the announcement of our restatement of certain financial statements in December 2007, during the recent turmoil in the worldwide financial markets, and due to the announcement of our preliminary results for the first fiscal quarter of 2013. In addition to fluctuations related to company-specific factors, broad market and industry factors may adversely affect the market price of our stock, regardless of our actual operating performance. Factors that could cause fluctuations in our stock price may include, among other things:

- actual or anticipated variations in quarterly operating results;
- changes in our financial guidance or financial estimates by any securities analysts who might cover our stock, or our failure to meet our financial guidance or the estimates made by securities analysts;
- uncertainty about current global or regional economic conditions;
- changes in the market valuations of other companies operating in our industry;
- the rate at which we return capital to our shareholders;
- announcements by us or our competitors related to significant acquisitions, strategic partnerships, or divestitures;
- business disruptions, costs and future events related to shareholder activism;
- additions or departures of key personnel;
- sales or purchases of our stock, including sales or purchases of our stock by our directors and officers or by significant stockholders; and
- repurchases of our stock by us pursuant to our share repurchase program.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None.

81

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Table of Contents

VERIFONE SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

ITEM 6. EXHIBITS

The following documents are filed as Exhibits to this report:

Exhibit Number	Description
31.1*	Certification of the Chief Executive Officer, as required by Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of the Chief Financial Officer, as required by Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Certification of the Chief Executive Officer and the Chief Financial Officer as required by 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.

XBRL (eXtensible Business Reporting Language) information is furnished and not filed or a part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, is deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, and otherwise is not subject to liability under these sections.

SIGNATURES

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

VERIFONE SYSTEMS, INC.

By: /S/ PAUL S. GALANT  
Paul S. Galant  
Chief Executive Officer

By: /S/ MARC E. ROTHMAN  
Marc E. Rothman  
Executive Vice President and Chief Financial Officer

Date: June 7, 2016





Table of Contents

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