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

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2013

or

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from ______ to ______

Commission file number: 001-34511

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

Delaware	**77-0560389**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
1090 Kifer Road **Sunnyvale, California**	**94086**
(Address of principal executive offices)	**(Zip Code)**

(408) 235-7700
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§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 x No o

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

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

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

As of July 31, 2013, there were 162,586,517 shares of the registrant's common stock outstanding.

FORTINET, INC.

QUARTERLY REPORT ON FORM 10-Q

For the Quarter Ended June 30, 2013

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Part I

ITEM 1. Financial Statements

FORTINET, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited, in thousands, except per share amounts)

	June 30, 2013	December 31, 2012
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 123,468	$ 122,975
Short-term investments	379,229	290,719
Accounts receivable—Net	108,907	107,642
Inventory	33,317	21,060
Prepaid expenses and other current assets	27,479	26,878
Total current assets	672,400	569,274
PROPERTY AND EQUIPMENT—Net	27,047	25,638
LONG-TERM INVESTMENTS	311,713	325,892
GOODWILL AND OTHER INTANGIBLE ASSETS—Net	9,539	2,117
DEFERRED TAX ASSETS—Non-current	61,764	48,525
OTHER ASSETS	3,283	4,051
TOTAL ASSETS	$ 1,085,746	$ 975,497
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 35,964	$ 20,816
Accrued liabilities	28,091	22,263
Accrued payroll and compensation	30,787	28,957
Deferred revenue	265,639	247,268
Total current liabilities	360,481	319,304
DEFERRED REVENUE—Non-current	124,043	115,917
INCOME TAXES PAYABLE—Non-current	32,628	28,778
OTHER LIABILITIES	1,409	564
Total liabilities	518,561	464,563
COMMITMENTS AND CONTINGENCIES (Note 7)		
STOCKHOLDERS' EQUITY:		
Common stock, $0.001 par value — 300,000 shares authorized; 163,773 and 161,757 shares issued and 162,364 and 160,348 shares outstanding as of June 30, 2013 and December 31, 2012, respectively	164	162
Additional paid-in capital	437,837	400,075
Treasury stock	(2,995)	(2,995)
Accumulated other comprehensive income	350	3,091
Retained earnings	131,829	110,601
Total stockholders' equity	567,185	510,934
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 1,085,746	$ 975,497

See notes to condensed consolidated financial statements.

FORTINET, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited, in thousands, except per share amounts)

	Three Months Ended		Six Months Ended	
	June 30, 2013	June 30, 2012	June 30, 2013	June 30, 2012
REVENUE:				
Product	$ 66,525	$ 61,692	$ 124,475	$ 114,896
Services	79,668	65,412	155,564	127,550
Ratable and other revenue	1,235	1,858	3,209	3,763
Total revenue	147,428	128,962	283,248	246,209
COST OF REVENUE:				
Product	26,948	23,935	49,906	43,003
Services	16,259	12,467	31,833	23,680
Ratable and other revenue	501	725	1,097	1,487
Total cost of revenue	43,708	37,127	82,836	68,170
GROSS PROFIT:				
Product	39,577	37,757	74,569	71,893
Services	63,409	52,945	123,731	103,870
Ratable and other revenue	734	1,133	2,112	2,276
Total gross profit	103,720	91,835	200,412	178,039
OPERATING EXPENSES:				
Research and development	25,158	20,388	48,492	40,055
Sales and marketing	55,997	44,259	105,973	86,295
General and administrative	8,788	6,238	16,779	12,023
Total operating expenses	89,943	70,885	171,244	138,373
OPERATING INCOME	13,777	20,950	29,168	39,666
INTEREST INCOME	1,337	1,203	2,706	2,287
OTHER (EXPENSE) INCOME—Net	(100)	73	115	3
INCOME BEFORE INCOME TAXES	15,014	22,226	31,989	41,956
PROVISION FOR INCOME TAXES	6,035	8,276	10,761	13,833
NET INCOME	$ 8,979	$ 13,950	$ 21,228	$ 28,123
Net income per share:				
Basic	$ 0.06	$ 0.09	$ 0.13	$ 0.18
Diluted	$ 0.05	$ 0.08	$ 0.13	$ 0.17
Weighted-average shares outstanding:				
Basic	162,247	157,474	161,767	156,742
Diluted	168,042	166,061	168,033	165,808

See notes to condensed consolidated financial statements.

FORTINET, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited, in thousands)

	Three Months Ended		Six Months Ended	
	June 30, 2013	June 30, 2012	June 30, 2013	June 30, 2012
Net income	$ 8,979	$ 13,950	$ 21,228	$ 28,123
Other comprehensive (loss) income, net of reclassification adjustments:				
Foreign currency translation losses	(861)	(783)	(1,813)	(225)
Unrealized (losses) gains on investments	(1,468)	(326)	(1,426)	1,473
Unrealized gains on cash flow hedges	—	19	—	19
Tax benefit (provision) related to items of other comprehensive income or loss	513	114	498	(515)
Other comprehensive (loss) income, net of tax	(1,816)	(976)	(2,741)	752
Comprehensive income	$ 7,163	$ 12,974	$ 18,487	$ 28,875

See notes to condensed consolidated financial statements.

FORTINET, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited, in thousands)

	Six Months Ended	
	June 30, 2013	June 30, 2012
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 21,228	$ 28,123
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	7,322	5,077
Amortization of investment premiums	5,889	6,528
Stock-based compensation expense	20,006	15,098
Excess tax benefit from employee stock option plans	(1,894)	(5,158)
Other non-cash items, net	(925)	31
Changes in operating assets and liabilities:		
Accounts receivable—Net	(801)	171
Inventory	(16,375)	(7,952)
Prepaid expenses and other current assets	(243)	(152)
Other assets	(12,442)	1,461
Accounts payable	14,255	4,337
Accrued payroll and compensation	2,287	3,119
Accrued and other liabilities	(257)	(115)
Deferred revenue	25,943	36,492
Income taxes payable	11,339	5,743
Net cash provided by operating activities	75,332	92,803
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of investments	(275,029)	(355,025)
Sales of investments	16,691	44,255
Maturities of investments	176,378	209,242
Purchases of property and equipment	(3,569)	(3,855)
Payments made in connection with acquisitions, net of cash acquired	(5,985)	(550)
Net cash used in investing activities	(91,514)	(105,933)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of common stock	15,590	17,650
Excess tax benefit from employee stock option plans	1,894	5,158
Net cash provided by financing activities	17,484	22,808
EFFECT OF EXCHANGE RATES ON CASH AND CASH EQUIVALENTS	(809)	(442)
NET INCREASE IN CASH AND CASH EQUIVALENTS	493	9,236
CASH AND CASH EQUIVALENTS—Beginning of period	122,975	71,990
CASH AND CASH EQUIVALENTS—End of period	$ 123,468	$ 81,226
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid for income taxes	$ 11,640	$ 6,380
NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Purchase of property and equipment not yet paid	$ 1,056	$ 580
Liability incurred in connection with business acquisition	$ —	$ 400

See notes to condensed consolidated financial statements.

FORTINET, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation and Preparation

The unaudited condensed consolidated financial statements of Fortinet, Inc. and its wholly owned subsidiaries (collectively, "we," "us," or "our") have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information as well as the instructions to Form 10-Q and the rules and regulations of the U.S. Securities and Exchange Commission ("SEC"). Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements, and should be read in conjunction with our audited consolidated financial statements as of and for the fiscal year ended December 31, 2012, contained in our Annual Report on Form 10-K ("Form 10-K") filed with the SEC on February 27, 2013. In the opinion of management, all adjustments, including normal recurring accruals, considered necessary for a fair presentation have been included. All intercompany balances, transactions and cash flows have been eliminated. The results of operations for the three and six months ended June 30, 2013 are not necessarily indicative of the operating results for any subsequent quarter, for the full year or for any future periods. The condensed consolidated balance sheets as of December 31, 2012 are derived from the audited consolidated financial statements for the year ended December 31, 2012.

The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in the condensed consolidated financial statements and accompanying notes. Actual results could differ materially from those estimates.

There have been no material changes in our significant accounting policies as of and for the three and six months ended June 30, 2013, as compared to the significant accounting policies described in the Form 10-K, except for the inclusion of policies related to goodwill and other indefinite-lived assets.

Goodwill and other indefinite-lived intangible assets

Goodwill represents the excess of purchase consideration over the estimated fair value of net assets of businesses acquired in a business combination. Goodwill and other indefinite-lived intangible assets such as in-process research and development acquired in a business combination are not amortized, but instead tested for impairment at least annually during the fourth quarter. We perform our annual goodwill impairment analysis at the reporting unit level. As of June 30, 2013, we had one reporting unit.

In reviewing goodwill for impairment we have the option to (i) assess qualitative factors to determine whether it is more-likely-than-not that the fair value of the reporting unit is less than its carrying amount or (ii) bypass the qualitative assessment and proceed directly to a quantitative assessment. If we opt to perform a qualitative assessment, the factors we may review include, but are not limited to (a) macroeconomic conditions; (b) industry and market considerations; (c) cost factors; (d) overall financial performance; (e) other relevant entity-specific events such as changes in management, strategy, customers, or litigation; (f) events affecting the reporting unit; or (g) or sustained decrease in share price. If we believe, as a result of the qualitative assessment, that it is more-likely-than-not that the fair value of the reporting unit is less than its carrying amount, the quantitative impairment test will be required. Otherwise, no further testing will be required. A quantitative assessment utilizes a two-step process. In the first step, the fair value of the reporting unit is determined, and is compared against its carrying amount, including goodwill. We consider a combination of an income-based approach using projected discounted cash flows and a market-based approach using multiples of comparable companies to determine the fair value. The fair value of the reporting unit is estimated using significant judgment based on a combination of the income and the market approaches. Under the income approach, we estimate fair value of the reporting unit based on the present value of forecasted future cash flows that the reporting unit is expected to generate over its remaining life. Under the market approach, we estimate fair value of our reporting unit based on an analysis that compares the value of the reporting unit to values of other companies in similar lines of business. If the fair value of the reporting unit does not exceed its carrying value, then we perform the second step to measure the amount of impairment loss. The amount of impairment is determined by comparing the implied fair value of reporting unit goodwill to the carrying value of the goodwill. When the carrying value of the reporting unit's goodwill exceeds its implied fair value, we record an impairment loss equal to the difference.

Determining the fair value of the reporting unit is highly judgmental in nature and involves the use of significant estimates and assumptions. These estimates and assumptions include revenue growth rates and operating margins used to calculate projected future cash flows, operating trends, risk-adjusted discount rates, future economic and market conditions and determination of appropriate market comparables. We base our fair value estimates on assumptions we believe to be reasonable but that are unpredictable and inherently uncertain. Actual future results may differ from those estimates. We may also test goodwill and other intangible assets for impairment between annual tests in the presence of impairment indicators. Acquired in-process research and development assets are classified as indefinite-lived intangible assets until the successful completion or abandonment of the associated research and development efforts. Upon successful completion of the associated research and development efforts, the useful life of the asset is determined and the asset is amortized over its useful life. If the associated research and development efforts are abandoned, an impairment loss is recognized for the carrying value of the related asset.

Certain prior period amounts have been combined on the condensed consolidated balance sheets and statements of cash flows to conform to the current period presentation.

Recent Accounting Pronouncements

In February 2013, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update No. 2013-02, *Comprehensive Income (Topic 220)—Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income* (“ASU 2013-02”). ASU 2013-02 requires an entity to report the effect of significant reclassifications out of accumulated other comprehensive income on the respective line items in net income if the amount being reclassified is required under GAAP to be reclassified in its entirety to net income. For other amounts that are not required under GAAP to be reclassified in their entirety to net income in the same reporting period, an entity is required to cross-reference other disclosures required under GAAP that provide additional detail about those amounts. We adopted ASU 2013-02 on January 1, 2013, and presented the effects within Note 15, *Accumulated Other Comprehensive Income*.

In July 2013, the FASB issued ASU No. 2013-11, *Income Taxes (Topic 740)-Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists* (“ASU 2013-11”). ASU 2013-11 provides guidance on the financial statement presentation of an unrecognized tax benefit when a net operating loss carryforward, similar tax loss, or tax credit carryforward exists. This new standard requires the netting of unrecognized tax benefits (“UTBs”) against a deferred tax asset for a loss or other carryforward that would apply in settlement of the uncertain tax positions. UTBs will be netted against all available same-jurisdiction loss or other tax carryforwards that would be utilized, rather than only against carryforwards that are created by the UTBs. ASU 2013-11 will be effective for us beginning in the first quarter of fiscal 2014. Early adoption is permitted. Since ASU 2013-11 only impacts financial statement disclosure requirements for unrecognized tax benefits, we do not expect its adoption to have an impact on our financial position or results of operations.

2. FINANCIAL INSTRUMENTS AND FAIR VALUE

The following table summarizes our investments ($ amounts in 000's):

	June 30, 2013			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Corporate debt securities	576,447	1,188	(919)	576,716
Commercial paper	71,844	15	(7)	71,852
Municipal bonds	34,387	63	(12)	34,438
Certificates of deposit and term deposits	7,933	4	(1)	7,936
Total available-for-sale securities	690,611	1,270	(939)	690,942

	December 31, 2012			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Corporate debt securities	529,738	1,814	(161)	531,391
Commercial paper	39,229	22	(6)	39,245
Municipal bonds	36,787	83	—	36,870
Certificates of deposit and term deposits	9,099	6	—	9,105
Total available-for-sale securities	614,853	1,925	(167)	616,611

The following table shows the gross unrealized losses and the related fair values of our investments that have been in a continuous unrealized loss position, as of June 30, 2013 ($ amounts in 000's):

	Less Than 12 Months		12 Months or Greater		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Corporate debt securities	262,379	(919)	—	—	262,379	(919)
Commercial paper	18,372	(7)	—	—	18,372	(7)
Municipal bonds	10,370	(12)	—	—	10,370	(12)
Certificate of deposit	1,000	(1)	—	—	1,000	(1)
Total available-for-sale securities	292,121	(939)	—	—	292,121	(939)

The following table shows the gross unrealized losses and the related fair values of our investments that have been in a continuous unrealized loss position, as of December 31, 2012 ($ amounts in 000's):

	Less Than 12 Months		12 Months or Greater		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Corporate debt securities	133,006	(156)	5,010	(5)	138,016	(161)
Commercial paper	8,464	(6)	—	—	8,464	(6)
Total available-for-sale securities	141,470	(162)	5,010	(5)	146,480	(167)

The contractual maturities of our investments were as follows ($ amounts in 000's)

	June 30, 2013	December 31, 2012
Due within one year	379,229	290,719
Due within one to three years	311,713	325,892
Total	690,942	616,611

Realized gains or losses from the sale of available-for-sale securities were not significant for any of the periods presented.

The following table presents the fair value of our financial assets measured at fair value on a recurring basis as of June 30, 2013 and December 31, 2012 ($ amounts in 000's):

	June 30, 2013			December 31, 2012		
	Aggregate Fair Value	Quoted Prices in Active Markets For Identical Assets (Level 1)	Significant Other Observable Remaining Inputs (Level 2)	Aggregate Fair Value	Quoted Prices in Active Markets For Identical Assets (Level 1)	Significant Other Observable Remaining Inputs (Level 2)
Assets:						
Corporate debt securities	576,716	—	576,716	531,391	—	531,391
Commercial paper	75,977	—	75,977	41,994	—	41,994
Municipal bonds	34,438	—	34,438	36,870	—	36,870
Certificates of deposit and term deposits	7,936	—	7,936	9,105	—	9,105
Money market funds	6,674	6,674	—	39,871	39,871	—
Total	701,741	6,674	695,067	659,231	39,871	619,360
Reported as:						
Cash equivalents	10,799			42,620		
Short-term investments	379,229			290,719		
Long-term investments	311,713			325,892		
Total	701,741			659,231		

We did not hold financial assets or liabilities which were recorded at fair value using inputs in the Level 3 category as of June 30, 2013 or December 31, 2012. There were no transfers between Level 1 and Level 2 of the fair value hierarchy during the three and six months ended June 30, 2013.

3. INVENTORY

Inventory consisted of the following ($ amounts in 000's):

	June 30, 2013	December 31, 2012
Raw materials	6,625	4,958
Finished goods	26,692	16,102
Inventory	33,317	21,060

4. PROPERTY AND EQUIPMENT—Net

Property and equipment consisted of the following ($ amounts in 000's):

	June 30, 2013	December 31, 2012
Land	13,895	13,895
Building and building improvements	610	610
Evaluation units	21,154	18,322
Computer equipment and software	20,478	17,176
Furniture and fixtures	1,666	1,501
Leasehold improvements and tooling	5,368	5,354
Total property and equipment	63,171	56,858
Less: accumulated depreciation	(36,124)	(31,220)
Property and equipment—net	27,047	25,638

Depreciation expense was $3.4 million and $2.4 million for the three months ended June 30, 2013 and June 30, 2012, respectively. Depreciation expense was $6.6 million and $4.5 million for the six months ended June 30, 2013 and June 30, 2012, respectively.

5. NET INCOME PER SHARE

Basic net income per share is computed by dividing net income by the weighted-average number of shares of common stock outstanding during the period. Diluted net income per share is computed by dividing net income by the weighted-average number of shares of common stock outstanding, plus the dilutive effects of stock options, restricted stock units ("RSUs"), and the employee stock purchase plan ("ESPP"). Potentially dilutive shares of common stock are determined by applying the treasury stock method.

A reconciliation of the numerator and denominator used in the calculation of basic and diluted net income per share is as follows ($ and share amounts in 000's, except per share amounts):

	Three Months Ended		Six Months Ended	
	June 30, 2013	June 30, 2012	June 30, 2013	June 30, 2012
Numerator:				
Net income	8,979	13,950	21,228	28,123
Denominator:				
Basic shares:				
Weighted-average common stock outstanding-basic	162,247	157,474	161,767	156,742
Diluted shares:				
Weighted-average common stock outstanding-basic	162,247	157,474	161,767	156,742
Effect of potentially dilutive securities:				
Stock options	5,734	8,576	6,152	9,043
RSUs	32	—	46	—
ESPP	29	11	68	23
Weighted-average shares used to compute diluted net income per share	168,042	166,061	168,033	165,808
Net income per share:				
Basic	0.06	0.09	0.13	0.18
Diluted	0.05	0.08	0.13	0.17

The following weighted-average shares of common stock were excluded from the computation of diluted net income per share for the periods presented, as their effect would have been antidilutive (in 000's):

	Three Months Ended		Six Months Ended	
	June 30, 2013	June 30, 2012	June 30, 2013	June 30, 2012
Stock options	7,472	7,475	7,483	6,767
RSUs	2,554	—	1,804	—
ESPP	434	311	395	298
	10,460	7,786	9,682	7,065

6. DEFERRED REVENUE

Deferred revenue consisted of the following ($ amounts in 000's):

	June 30, 2013	December 31, 2012
Product	4,611	5,411
Services	378,453	348,548
Ratable and other revenue	6,618	9,226
Total deferred revenue	389,682	363,185
Reported As:		
Short-term	265,639	247,268
Long-term	124,043	115,917
Total deferred revenue	389,682	363,185

7. COMMITMENTS AND CONTINGENCIES

Leases—We lease certain facilities under various non-cancelable operating leases, which expire through 2020. Rent expense was $2.4 million and $2.2 million for the three months ended June 30, 2013 and June 30, 2012, respectively. Rent expense was $4.7 million and $4.4 million for the six months ended June 30, 2013 and June 30, 2012, respectively. Rent expense is recognized using the straight-line method over the term of the lease. The aggregate future non-cancelable minimum rental payments on operating leases as of June 30, 2013 are as follows ($ amounts in 000's):

	Rental Payment
Fiscal Years:	
2013 (remainder)	4,325
2014	5,974
2015	4,384
2016	3,968
2017	3,632
Thereafter	7,544
Total	29,827

Contract Manufacturer and Other Commitments—Our independent contract manufacturers procure components and build our products based on our forecasts. These forecasts are based on estimates of future demand for our products, which are in turn based on historical trends and an analysis from our sales and marketing organizations, adjusted for overall market conditions. In order to reduce manufacturing lead times and plan for adequate component supply, we issue non-cancelable purchase orders to some of our independent contract manufacturers. As of June 30, 2013, we had $39.8 million of open purchase orders with our independent contract manufacturers that may not be cancelable.

In addition to commitments with contract manufacturers, we have open purchase orders and contractual obligations in the ordinary course of business for which we have not received goods or services. As of June 30, 2013, we had $9.1 million in other purchase commitments.

Warranties—We generally provide a 1-year warranty on hardware products and a 90-day warranty on software.

Accrued warranty activities are summarized as follows ($ amounts in 000's):

	For The Six Months Ended	
	June 30, 2013	June 30, 2012
Accrued warranty balance—beginning of the period	2,309	2,582
Warranty costs incurred	(1,744)	(1,141)
Provision for warranty	2,204	764
Changes in prior period estimates	208	(265)
Accrued warranty balance—end of the period	2,977	1,940

Litigation—In August 2009, Enhanced Security Research, LLC and Security Research Holdings LLC (collectively "ESR"), a non-practicing entity, filed a complaint against us in the United States District Court for the District of Delaware alleging infringement by us and other defendants of two patents. The plaintiffs are claiming unspecified damages and requesting an injunction against the alleged infringement. In June 2010, the Court granted our motion to stay pending the outcome of reexamination proceedings in the U.S. Patent and Trademark Office ("PTO") on both asserted patents. The PTO rejected all of the claims of the patents in the suit and ESR appealed this result to the Board of Patent Appeals and Interferences ("BPAI"). In August 2012, the BPAI completed its review of both reexamination proceedings, and, after the BPAI's review, all claims of the asserted ESR patents remain rejected. In October 2012, ESR filed an additional appeal of the BPAI decision with the United States Court of Appeal for the Federal Circuit. That appeal is still pending. We have determined that, as of this time, there is not a reasonable possibility that a loss has been incurred. The litigation related to ESR is no longer material to us, and we will no longer report on this case.

In July 2010, Network Protection Sciences, LLC ("NPS"), a non-practicing entity, filed a complaint in the United States District Court for the Eastern District of Texas alleging patent infringement by us and other defendants. NPS is claiming unspecified damages, including treble damages for willful infringement, and requests an injunction against such alleged infringement. In December 2011, the United States District Court for the Eastern District of Texas ordered the case to be transferred to the Northern District of California. In June 2012, the United States District Court for the Northern District of California dismissed the other defendants for misjoinder, and the case is proceeding with Fortinet as the sole defendant. We have filed a motion to dismiss the case and a separate motion for summary judgment, both of which are pending. This case is currently scheduled for a jury trial starting in September 2013. We have determined that, as of this time, there is not a reasonable possibility that a loss has been incurred.

In June 2012, we received a letter from SRI International, ("SRI") claiming that we infringed certain SRI patents. Subsequently, we filed a complaint in the United States District Court for the Northern District of California seeking declaratory relief and a judgment that the SRI patents were invalid, unenforceable and not infringed by any of our products or services. The case is proceeding in the United States District Court for the Northern District of California. The case is currently in the early stages, and we have determined that, as of this time, there is not a reasonable possibility that a loss has been incurred.

Indemnification—Under the indemnification provisions of our standard sales contracts, we agree to defend our customers against third-party claims asserting infringement of certain intellectual property rights, which may include patents, copyrights, trademarks, or trade secrets, and to pay judgments entered on such claims. Our exposure under these indemnification provisions is generally limited by the terms of our contracts to the total amount paid by our customer under the agreement. However, certain agreements include indemnification provisions that could potentially expose us to losses in excess of the amount received under the agreement. To date, there have been no claims under such indemnification provisions.

8. STOCKHOLDERS' EQUITY

Employee Stock Options

The following table summarizes the weighted-average assumptions relating to our employee stock options:

	Three Months Ended	Six Months Ended
	June 30, 2012	June 30, 2012
Expected term in years	4.6	4.6
Volatility (%)	46.4	46.4 - 51.9
Risk-free interest rate (%)	0.9	0.7 - 0.9
Dividend rate (%)	—	—

There were no stock options granted during the three and six months ended June 30, 2013.

The following table summarizes the stock option activity and related information for the periods presented below (in 000's, except per share amounts, exercise prices and contractual life):

	Options Outstanding			
	Number of Shares	Weighted-Average Exercise Price ($)	Weighted-Average Remaining Contractual Life (Years)	Aggregate Intrinsic Value ($)
Balance—December 31, 2012	18,571	12.40		
Forfeited	(464)	21.54		
Exercised	(1,687)	5.36		
Balance—June 30, 2013	16,420	12.86		117,043
Options vested and expected to vest—June 30, 2013	16,405	12.86	3.7	117,034
Options exercisable—June 30, 2013	11,657	9.30	3.2	112,038

The aggregate intrinsic value represents the pre-tax difference between the exercise price of stock options and the quoted market price of our common stock on June 30, 2013, for all in-the-money options. As of June 30, 2013, total compensation expense related to unvested stock options granted to employees but not yet recognized was $51.2 million, net of estimated forfeitures. This expense is expected to be amortized on a straight-line basis over a weighted-average period of 2.1 years.

Additional information related to our stock options is summarized below ($ amounts in 000's, except per share amounts):

	Three Months Ended		Six Months Ended	
	June 30, 2013	June 30, 2012	June 30, 2013	June 30, 2012
Weighted-average fair value per share granted	—	9.62	—	10.94
Intrinsic value of options exercised	3,058	12,588	29,117	50,690
Fair value of options vested	5,486	4,881	16,489	13,074

Restricted Stock Units

The following table summarizes the activity and related information for RSUs for the period presented below (in 000's, except per share amounts):

	Restricted Stock Units Outstanding	
	Number of Shares	Weighted-Average Grant-Date Fair Value per Share ($)
Balance—December 31, 2012	830	23.73
Granted	2,711	22.12
Forfeited	(170)	23.36
Balance—June 30, 2013	3,371	22.35
RSUs expected to vest—June 30, 2013	3,097	22.36

As of June 30, 2013, total compensation expense related to unvested RSUs that were granted to employees and non-employees, but not yet recognized, was $71.2 million, net of estimated forfeitures. This expense is expected to be amortized on a straight-line basis over a weighted-average vesting period of 3.5 years.

Employee Stock Purchase Plan

In determining the fair value of the shares subject to our ESPP, we use the Black-Scholes option pricing model that employs the following weighted-average assumptions:

	Six Months Ended	
	June 30, 2013	June 30, 2012
Expected term in years	0.5	0.5
Volatility (%)	48	58
Risk-free interest rate (%)	0.1	0.2
Dividend rate (%)	—	—

Additional information related to our ESPP is provided below (in 000's, except per share amounts):

	Six Months Ended	
	June 30, 2013	June 30, 2012
Weighted-average fair value per share granted ($)	7.02	8.08
Shares issued under the ESPP	329	288
Weighted-average price per share issued ($)	19.91	17.51

There were no ESPP shares granted or issued during the three months ended June 30, 2013 and June 30, 2012.

Stock-based Compensation Expense

Stock-based compensation expense is included in costs and expenses as follows ($ amounts in 000's):

	Three Months Ended		Six Months Ended	
	June 30, 2013	June 30, 2012	June 30, 2013	June 30, 2012
Cost of product revenue	96	88	186	152
Cost of services revenue	1,226	941	2,246	1,686
Research and development	3,291	2,292	6,057	4,249
Sales and marketing	4,594	3,475	8,712	6,918
General and administrative	1,500	1,056	2,805	2,093
Total stock-based compensation expense	10,707	7,852	20,006	15,098

The following table summarizes stock-based compensation expense by award type ($ amounts in 000's)

	Three Months Ended		Six Months Ended	
	June 30, 2013	June 30, 2012	June 30, 2013	June 30, 2012
Stock options	1,215	6,681	6,701	12,997
RSUs	4,357	—	5,496	—
ESPP	5,135	1,171	7,809	2,101
Total stock-based compensation expense	10,707	7,852	20,006	15,098

Total income tax benefit from employee stock option plans that is recognized in the consolidated statements of operations is as follows ($ amounts in 000's):

	Three Months Ended		Six Months Ended	
	June 30, 2013	June 30, 2012	June 30, 2013	June 30, 2012
Income tax benefit from employee stock option plans	2,794	3,713	6,381	10,387

9. INCOME TAXES

The effective tax rate was 40% for the three months ended June 30, 2013, compared to an effective tax rate of 37% for the three months ended June 30, 2012. The effective tax rate was 34% for the six months ended June 30, 2013, compared to an effective tax rate of 33% for the six months ended June 30, 2012. The provision for income taxes for the periods presented is comprised of foreign income taxes, U.S. federal and state taxes, and withholding tax.

As of June 30, 2013 and December 31, 2012, unrecognized tax benefits were $31.2 million and $27.8 million, respectively. The total amount of $30.8 million in unrecognized tax benefits, if recognized, would favorably impact the effective tax rate.

It is our policy to classify accrued interest and penalties related to unrecognized tax benefits in the provision for income taxes. As of June 30, 2013, we had accrued approximately $2.2 million for estimated interest related to uncertain tax provisions.

The State of California has been conducting an audit of our state income tax returns for fiscal 2010 and fiscal 2011. We do not expect this audit to have a significant detrimental effect on our income tax liability nor have a material impact on our results of operations.

10. EMPLOYEE BENEFIT PLAN

The 401(k) tax-deferred savings plan (the “401(k) Plan”) permits participants to make contributions by salary deduction pursuant to Section 401(k) of the Internal Revenue Code of 1986, as amended. Under the 401(k) Plan, participating employees may defer a portion of their pre-tax earnings, up to the annual contribution limit specified by the Internal Revenue Service (“IRS”). In Canada, we have a Group Registered Retirement Savings Plan program (the “RRSP”) which permits participants to make tax deductible contributions up to the maximum contribution limits under the Income Tax Act. Our matching contributions to the 401(k) Plan and RRSP were $0.5 million for each of the three months ended June 30, 2013 and June 30, 2012. Our matching contributions to the 401(k) Plan and RRSP were $1.1 million and $0.9 million for the six months ended June 30, 2013 and June 30, 2012, respectively.

11. SEGMENT AND SIGNIFICANT CUSTOMER INFORMATION

The following tables set forth revenue and property and equipment by geographic region ($ amounts in 000’s):

	Three Months Ended		Six Months Ended	
Revenue	**June 30, 2013**	**June 30, 2012**	**June 30, 2013**	**June 30, 2012**
Americas:				
United States	38,815	34,190	73,603	65,309
Other Americas	21,211	17,732	39,050	33,044
Total Americas	60,026	51,922	112,653	98,353
Europe, Middle East and Africa (“EMEA”)	50,801	43,664	98,127	84,550
Asia Pacific and Japan (“APAC”)	36,601	33,376	72,468	63,306
Total revenue	147,428	128,962	283,248	246,209

During the three and six months ended June 30, 2013, one distributor, Exclusive Networks Group, accounted for 11% and 12% of revenue, respectively. During the three and six months ended June 30, 2012, one distributor, Exclusive Networks Group, accounted for 11% and 12% of total revenue, respectively.

Property and Equipment	June 30, 2013	December 31, 2012
Americas:		
United States	19,704	18,764
Canada	4,268	4,376
Other Americas	61	87
Total Americas	24,033	23,227
EMEA	1,402	1,213
APAC	1,612	1,198
Total property and equipment—net	27,047	25,638

12. FOREIGN CURRENCY DERIVATIVES

The notional amounts of forward exchange contracts to hedge balance sheet accounts as of June 30, 2013 and December 31, 2012 were ($ amounts in 000’s):

	Buy/Sell	Notional
Balance Sheet Contracts:		
Currency - As of June 30, 2013		
CAD	Buy	23,025
Currency - As of December 31, 2012		
CAD	Buy	17,968

13. BUSINESS COMBINATIONS

On March 21, 2013, we acquired all of the outstanding equity securities of Coyote Point Systems, Inc. (“Coyote”), a provider of application delivery, load balancing and acceleration solutions, for $6.0 million in cash. The acquisition also includes a contingent obligation for up to $5.5 million in future earn-out payments to former stockholders of Coyote, if specified future operational objectives, service conditions and financial results are met within two years of the acquisition date. Of the maximum $5.5 million in contingent earn-out payments, up to $3.5 million will be payable after eighteen months from the acquisition date, and up to $2.0 million will be payable after two years from the acquisition date. As the future earn-out payments are also contingent upon one of Coyote's former stockholder's employment during the earn-out period, these contingent obligations are being recorded as compensation expense ratably over the earn-out periods.

We accounted for this acquisition as a purchase of a business and, accordingly, the total purchase price was allocated to Coyote’s identifiable tangible and intangible assets acquired and liabilities assumed based on their estimated fair values as of the acquisition date. The fair value assigned to the intangible assets acquired was determined using the income approach which discounts expected cash flows to present value using our estimates and assumptions.

The following table summarizes the fair value of assets acquired and liabilities assumed as of the acquisition date ($ amounts in 000's):

Cash and cash equivalents	206
Other current assets	501
Finite-lived intangible assets	2,800
Indefinite-lived intangible assets	2,600
Goodwill	2,766
Other assets	88
Total assets acquired	8,961
Current liabilities	1,078
Long-term liabilities	1,898
Total liabilities assumed	2,976
Total purchase price	5,985

Of the total acquired identified intangible assets, we allocated $2.3 million to developed technology, $0.5 million to customer relationships, and $2.6 million to in-process research and development. Identified finite-lived intangible assets consist of developed technology and customer relationships that will be amortized as cost of revenue and sales and marketing expense, respectively, ratably on a straight-line basis, each over an estimated useful life of 6 years. Identified indefinite-lived intangible assets consist of in-process research and development. The goodwill of $2.8 million represents the premium we paid over the fair value of the net tangible liabilities assumed and identified intangible assets acquired. We paid this premium for a number of reasons, primarily for acquiring developed and in-process technology. None of the goodwill recognized as a result of the acquisition is deductible for income tax purposes. The financial results of this acquisition were considered immaterial for purposes of pro-forma financial disclosures.

On December 7, 2012, we completed the acquisition of XDN, Inc., a provider of cloud-based content delivery solutions, for a total consideration of $0.5 million. We accounted for this acquisition as a purchase of a business and, accordingly, the total purchase price was allocated to identifiable intangible assets acquired based on their estimated fair market value as of the acquisition date. The purchase price allocation resulted in purchased identifiable intangible assets of $0.5 million. Identifiable intangible assets consist of developed technology. The fair value assigned to identifiable intangible assets acquired was determined using the market approach, which compares the value of the purchased assets to similar assets in similar lines of business. Purchased identifiable intangible assets are being amortized as cost of revenue ratably over three years. The financial results of this acquisition were considered immaterial for purposes of pro forma financial disclosures.

On March 8, 2012, we completed the acquisition of IntruGuard Devices, Inc. ("IntruGuard"), a supplier of Distributed Denial of Services ("DDoS"), prevention products, for a total consideration of $1.0 million. Of the total consideration, $0.4 million was withheld in escrow as security for IntruGuard's indemnification obligations. We accounted for this acquisition as a purchase of a business and, accordingly, the total purchase price was allocated to tangible and identifiable intangible assets acquired and liabilities assumed based on their estimated fair market values as of the acquisition date. The purchase price allocation resulted in purchased tangible assets of $53,000 and liabilities of $43,000, and purchased identifiable intangible assets of $0.9 million. Identifiable intangible assets consist of purchased technology. The fair value assigned to identifiable intangible assets acquired was determined using the income approach, which discounts expected future cash flows to present value using estimates and assumptions determined by us. Purchased identifiable intangible assets are being amortized as cost of revenue ratably over three years. Of the $0.4 million previously withheld in escrow, $0.2 million and $0.2 million were released to the selling stockholders during the three months ended September 30, 2012 and the three months ended March 31, 2013, respectively. The financial results of this acquisition were considered immaterial for purposes of pro forma financial disclosures.

14. GOODWILL AND OTHER INTANGIBLE ASSETS—NET

We acquired $2.8 million of goodwill during the six months ended June 30, 2013, which approximated the carrying value as of June 30, 2013.

We acquired $2.3 million of developed technology, $0.5 million of customer relationships, and $2.6 million of in-process research and development during the six months ended June 30, 2013. The following tables present other intangible assets ($ amounts in 000's):

	June 30, 2013		
	Gross	Accumulated Amortization	Net
Finite-lived other intangible assets:			
Developed technology	5,784	2,090	3,694
Customer relationships	500	21	479
	6,284	2,111	4,173
Indefinite-lived other intangible assets:			
In-process research and development	2,600	—	2,600
Total other intangible assets	8,884	2,111	6,773

	December 31, 2012		
	Gross	Accumulated Amortization	Net
Finite-lived other intangible assets:			
Developed technology	3,541	1,424	2,117
Total other intangible assets	3,541	1,424	2,117

Amortization expense was $0.4 million and $0.3 million for the three months ended June 30, 2013 and June 30, 2012, respectively. Amortization expense was $0.7 million and $0.6 million for the six months ended June 30, 2013 and June 30, 2012, respectively. The following table summarizes estimated future amortization expense of other intangible assets with finite lives for future fiscal years ($ amounts in 000's):

	Amount
Fiscal Years:	
2013 (remainder)	758
2014	1,154
2015	738
2016	472
2017	467
Thereafter	584
Total	4,173

15. ACCUMULATED OTHER COMPREHENSIVE INCOME

The following table summarizes the changes in accumulated balances of other comprehensive income for the six months ended June 30, 2013 ($ amounts in 000's):

	Foreign Currency Translation Gains and Losses	Unrealized Gains and Losses on Investments	Tax benefit or provision related to items of other comprehensive income or loss	Total
Beginning balance	1,948	1,758	(615)	3,091
Other comprehensive income before reclassifications	(1,813)	(1,421)	496	(2,738)
Amounts reclassified from accumulated other comprehensive income	—	(5)	2	(3)
Net current-period other comprehensive income	(1,813)	(1,426)	498	(2,741)
Ending balance	135	332	(117)	350

The following table provides details about the reclassification out of accumulated other comprehensive income for the six months ended June 30, 2013 ($ amounts in 000s):

Details about Accumulated Other Comprehensive Income Components	Amount Reclassified from Accumulated Other Comprehensive Income	Affected Line Item in the Statement Where Net Income is Presented
Unrealized gains on investments	(5)	Other (expense) income, net
Tax provision related to items of other comprehensive income or loss	2	Provision for income taxes
Total reclassification for the period	(3)	

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

In addition to historical information, this Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended ("Exchange Act"). These statements include, among other things, statements concerning our expectations regarding:

- *variability in sales in certain product categories from year to year and between quarters;*
- *expected impact of sales of certain products;*
- *continued sales into large enterprises and service providers;*
- *the significance of stock-based compensation as an expense;*
- *the proportion of our revenue that consists of our product and service revenues, and the mix of billings between products and services;*
- *the impact of our product innovation strategy;*
- *trends in revenue, costs of revenue, and gross margin;*
- *trends in our operating expenses, including personnel costs, research and development expense, sales and marketing expense and general and administrative expense, and expectations regarding these expenses as a percentage of revenue;*
- *our effective tax rate;*
- *the sufficiency of our existing cash, cash equivalents and investments to meet our cash needs for at least the next 12 months; and*
- *as well as other statements regarding our future operations, financial condition and prospects and business strategies.*

These forward-looking statements are subject to certain risks and uncertainties that could cause our actual results to differ materially from those reflected in the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those discussed in this Quarterly Report on Form 10-Q and, in particular, the risks discussed under the heading "Risk Factors" included in Part II, Item 1A. Risk Factors and elsewhere in this Quarterly Report on Form 10-Q and in our other SEC filings, including the Form 10-K. We undertake no obligation to revise or publicly release the results of any revision to these forward-looking statements. Given these risks and uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements.

Business Overview

We provide network security solutions, which enable broad, integrated and high performance protection against dynamic security threats while simplifying the IT security infrastructure for enterprises, service providers and governmental entities worldwide. From inception through June 30, 2013, we shipped over 1,250,000 appliances via more than 15,000 channel partners to more than 160,000 end-customers worldwide, including a majority of the 2012 Fortune Global 100.

Our core Unified Threat Management ("UTM")/Next Generation Firewall ("NGFW") product line of FortiGate physical and virtual appliances ships with a set of security and networking capabilities, including firewall, VPN, application control, anti-malware, intrusion prevention, Web filtering, anti-spam and WAN acceleration functionality. We derive a substantial majority of product sales from our FortiGate appliances, which range from the FortiGate-20, designed for small businesses, to the FortiGate-5000 series for large enterprises, telecommunications carriers, and service providers. Our UTM/NGFW solution also includes our FortiGuard security subscription services, which end-customers can subscribe to in order to obtain access to dynamic updates to intrusion prevention, application control, anti-malware, Web filtering, vulnerability management and anti-spam functionality included in our appliances. End-customers can also choose to purchase FortiCare technical support services for our products. End-customers also often use FortiManager and FortiAnalyzer products in conjunction with a FortiGate deployment to provide centralized management, analysis and reporting capabilities.

We complement our core FortiGate product line with other appliances and software that offer additional protection from security threats to other critical areas of the enterprise, such as messaging, Web application firewalls, databases, protection against DDoS, endpoint security for employee computers and mobile devices and wireless access point. Although sales of these complementary products have grown in recent quarters, these products still represent less than 10% of our total revenue.

Financial Highlights

- We recorded total revenue of $147.4 million and $283.2 million during the three and six months ended June 30, 2013, respectively. This represents an increase of 14% and 15% during the three and six months ended June 30, 2013, respectively, compared to the same periods last year. Product revenue was $66.5 million and $124.5 million during the three and six months ended June 30, 2013, respectively, an increase of 8% during each of the periods, compared to the same periods last year. Services revenue was $79.7 million and $155.6 million during the three and six months ended June 30, 2013, respectively, an increase of 22% during each of the periods, compared to the same periods last year.

- We generated cash flows from operating activities of $75.3 million during the six months ended June 30, 2013, a decrease of 19% compared to the same period last year.

- Cash, cash equivalents and investments were $814.4 million as of June 30, 2013, an increase of $74.8 million from December 31, 2012.

- Deferred revenue was $389.7 million as of June 30, 2013, an increase of $26.5 million from December 31, 2012.

During the three and six months ended June 30, 2013, revenue grew as a result of our sales efforts and product offerings. We also continued to gain traction with several recently introduced products, including new FortiGate entry-level appliances such as the FG-60D with its WIFI counterparts; the FG-800C mid-range appliance; and the FG-3600C and FG-5001C for large enterprises and service providers.

We continue to invest in research and development to strengthen our technology leadership position, as well as sales and marketing to expand brand awareness, strengthen our value proposition, and expand our global sales team and distribution channels. During the three and six months ended June 30, 2013, we experienced higher sales volume in our FortiGate product family, particularly entry-level products, wireless security and access point products, which contributed to the largest portion of the growth during this period. Although we experienced a decline in deals valued at greater than $500,000 during the six months ended June 30, 2013 when compared to the same period last year, during the three and six months ended June 30, 2013, we experienced an increase in the number of deals involving sales greater than $250,000 and deals greater than $100,000 when compared to the same periods last year. Specifically, the number of deals involving sales greater than $500,000 was 20 and 33 in the three and six months ended June 30, 2013, respectively, compared to 19 and 38 in the three and six months ended June 30, 2012, respectively. The number of deals involving sales greater than $250,000 was 58 and 113 in the three and six months ended June 30, 2013, respectively, compared to 55 and 102 in the three and six months ended June 30, 2012, respectively. The number of deals involving sales greater than $100,000 was 190 and 360 in the three and six months ended June 30, 2013, respectively, compared to 168 and 321 in the three and six months ended June 30, 2012, respectively. We expect some variability in this metric, and remain focused on investing in our sales and marketing and research and development resources in order to expand our reach into new high-growth verticals and emerging markets. Moreover, such investments will allow us to meet increasing customer expectations about the quality and functionality of our products, as we continue to sell to large enterprises and service providers. While we have experienced some success selling to large enterprises, across key verticals, including service provider, government, retail, financial services and education, we experienced slower sales in the U.S. service provider sector during the three and six months ended June 30, 2013, and there can be no assurance we will be successful selling into these vertical customer segments.

During the three and six months ended June 30, 2013, operating expenses increased by 27% and 24% compared to the same periods last year. The increase was primarily driven by additional headcount as we continued to invest in the development of new products and expand our sales coverage. Headcount increased to 2,182 as of June 30, 2013 from 1,762 as of June 30, 2012. Our accelerated pace of hiring continued during the three and six months ended June 30, 2013, particularly in sales and marketing, research and development, and technical support.

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Key Metrics

We monitor the key financial metrics set forth below to help us evaluate growth trends, establish budgets, measure the effectiveness of our sales and marketing efforts, and assess operational efficiencies. Our total deferred revenue increased by $13.3 million from $376.4 million as of March 31, 2013 to $389.7 million as of June 30, 2013. Revenue recognized plus the change in deferred revenue from the beginning to the end of the period less any deferred revenue balances acquired from business combination(s) is a useful metric that management identifies as billings. Billings for services drive deferred revenue, which is an important indicator of the health and visibility of our business, and has historically represented a majority of the revenue that we recognize in a typical quarter. As of June 30, 2013, we had $814.4 million in cash, cash equivalents and investments and have had positive cash flow from operations every fiscal year since 2005. We discuss revenue, gross margin, and the components of operating income and margin below under "—Results of Operations," and we discuss our cash, cash equivalents, and investments under "—Liquidity and Capital Resources." Deferred revenue and cash flow from operations are discussed immediately below the following table.

	Three Months Ended Or As Of	
	June 30, 2013	**June 30, 2012**
	($ amounts in 000's)	
Revenue	147,428	128,962
Gross margin	70%	71%
Operating income [1]	13,777	20,950
Operating margin	9%	16%
Total deferred revenue	389,682	331,368
Increase in total deferred revenue	13,268	16,796
Cash, cash equivalents and investments	814,410	644,398
Cash provided by operating activities	37,221	44,285
Free cash flow (Non-GAAP)[2]	35,186	42,054

(1) Includes:

Stock-based compensation expense	10,707	7,852
Patent settlement income	478	478

(2) See "—Cash flow from operations" below for a definition of free cash flow.

Deferred revenue. Our deferred revenue consists of amounts that have been invoiced but that have not yet been recognized as revenue. The majority of our deferred revenue balance consists of the unamortized portion of services revenue from subscription and support service contracts. We monitor our deferred revenue balance because it represents a significant portion of revenue to be recognized in future periods. We define billings as revenue recognized during a period plus the change in deferred revenue from the beginning to the end of the period less any deferred revenue balances acquired from business combination(s) during the period. The following table reflects the reconciliation of billings to revenue. For a discussion of the limitations of non-GAAP financial measures, see "—Other Non-GAAP Financial Measures" below.

	Three Months Ended	
	June 30, 2013	**June 30, 2012**
	($ amounts in 000's)	
Billings:		
Revenue	147,428	128,962
Add increase in deferred revenue	13,268	16,796
Total billings (Non-GAAP)	160,696	145,758

Cash flow from operations. We monitor cash flow from operations as a measure of our overall business performance. Our cash flow from operations is driven in large part by our billings growth, profitability, and our ability to successfully manage our working capital. Monitoring cash flow from operations and free cash flow enables us to analyze our financial performance excluding the non-cash effects of certain items such as depreciation, amortization and stock-based compensation expenses, thereby allowing us to better understand and manage the cash needs of our business. Free cash flow, an alternative non-GAAP financial measure of liquidity, is defined as net cash provided by operating activities less capital expenditures. The following table provides a reconciliation of free cash flow to cash provided by operating activities. For a discussion of the limitations of non-GAAP financial measures, see "—Other Non-GAAP Financial Measures" below.

	Three Months Ended	
	June 30, 2013	June 30, 2012
	($ amounts in 000's)	
Free Cash Flow:		
Net cash provided by operating activities	37,221	44,285
Less purchases of property and equipment	(2,035)	(2,231)
Free cash flow (Non-GAAP)	35,186	42,054

Other Non-GAAP Financial Measures

To supplement our consolidated financial statements presented in accordance with GAAP, we consider certain financial measures that are not prepared in accordance with GAAP, including billings and free cash flow discussed above as well as non-GAAP gross margin, non-GAAP operating income, non-GAAP operating margin, non-GAAP operating expenses, and non-GAAP net income. These non-GAAP financial measures are not based on any standardized methodology prescribed by GAAP and are not necessarily comparable to similar measures presented by other companies.

We use these non-GAAP financial measures internally in analyzing our financial results and believe they are useful to investors, as a supplement to GAAP measures, in evaluating our ongoing operational performance and enhancing an overall understanding of our past financial performance, as they help illustrate underlying trends in our business that could otherwise be masked by the effect of the expenses that we exclude in these non-GAAP financial measures. Furthermore, we use many of these measures to establish budgets and operational goals for managing our business and evaluating our performance. We also believe that the use of these non-GAAP financial measures provides an additional tool for investors to use in comparing our recurring core business operating results over multiple periods with other companies in our industry, many of which present similar non-GAAP financial measures to investors.

These non-GAAP financial measures should not be considered in isolation from, or as a substitute for, financial information prepared in accordance with GAAP. There are a number of limitations related to the use of these non-GAAP financial measures versus the nearest GAAP equivalent of these financial measures. First, these non-GAAP financial measures exclude certain recurring, non-cash charges such as stock-based compensation expense, offset by patent settlement income. Effective second quarter of fiscal 2013, our non-GAAP financial measures will include amortization expense of certain intangible assets. Prior period amounts have been adjusted to conform to current period presentation. Stock-based compensation expense has been, and will continue to be, for the foreseeable future, a significant recurring expense in our business and is an important part of our employees' overall compensation. Second, the expenses that we exclude in our calculation of these non-GAAP financial measures may differ from the expenses, if any, that our peer companies may exclude when they report their results of operations. We compensate for these limitations by providing the nearest GAAP equivalents of these non-GAAP financial measures and describing these GAAP equivalents in the section entitled "—Results of Operations" below.

Non-GAAP gross margin represents gross margin as reported in our consolidated statements of operations, excluding the impact of stock-based compensation expense and amortization expense of certain intangible assets, both of which are non-cash charges. Non-GAAP operating income is operating income, as reported on our consolidated statements of operations, excluding the impact of stock-based compensation expense, amortization expense of certain intangible assets, and the income we received from a patent settlement. Non-GAAP operating margin is non-GAAP operating income divided by revenue. The following table reconciles GAAP gross profit, GAAP gross margin, GAAP operating income, and GAAP operating margin to non-GAAP gross margin, non-GAAP operating income, and non-GAAP operating margin for the three months ended June 30, 2013 and June 30, 2012.

	Three Months Ended			
	June 30, 2013		**June 30, 2012**	
	Amount ($)	**% of Revenue**	**Amount ($)**	**% of Revenue**
	($ amounts in 000's)			
Total revenue	147,428		128,962	
GAAP gross profit and margin	103,720	70	91,835	71
Stock-based compensation expense	1,322	1	1,029	1
Amortization expense of certain intangible assets (1)	354	—	226	—
Non-GAAP gross profit and margin	105,396	71	93,090	72
GAAP operating income and margin	13,777	9	20,950	16
Stock-based compensation expense:				
Cost of revenue	1,322	1	1,029	1
Research and development	3,291	2	2,292	2
Sales and marketing	4,594	3	3,475	2
General and administrative	1,500	1	1,056	1
Total stock-based compensation expense	10,707	7	7,852	6
Amortization expense of certain intangible assets (1)	354	—	226	—
Patent settlement income	(478)	—	(478)	—
Non-GAAP operating income and margin	24,360	16	28,550	22

(1) Effective second quarter of fiscal 2013, amortization expense of certain intangible assets is excluded from GAAP gross profit and margin, and GAAP operating income and margin to reconcile to non-GAAP financial metrics. Prior period amounts have been adjusted to conform to current period presentation.

Non-GAAP operating expenses represent operating expenses, as reported in our condensed consolidated statements of operations, excluding the impact of stock-based compensation expense and the income from a patent settlement. The following table reconciles GAAP operating expenses to non-GAAP operating expenses for the three months ended June 30, 2013 and June 30, 2012.

	Three Months Ended			
	June 30, 2013		June 30, 2012	
	Amount ($)	% of Revenue	Amount ($)	% of Revenue
	($ amounts in 000's)			
Operating Expenses:				
Research and development expenses:				
GAAP research and development expenses	25,158	17	20,388	16
Stock-based compensation expense	(3,291)	(2)	(2,292)	(2)
Non-GAAP research and development expenses	21,867	15	18,096	14
Sales and marketing expenses:				
GAAP sales and marketing expenses	55,997	38	44,259	34
Stock-based compensation expense	(4,594)	(3)	(3,475)	(2)
Non-GAAP sales and marketing expenses	51,403	35	40,784	32
General and administrative expenses:				
GAAP general and administrative expenses	8,788	6	6,238	5
Stock-based compensation expense	(1,500)	(1)	(1,056)	(1)
Patent settlement income	478	—	478	—
Non-GAAP general and administrative expenses	7,766	5	5,660	4
Total operating expenses:				
GAAP operating expenses	89,943	61	70,885	55
Stock-based compensation expense	(9,385)	(6)	(6,823)	(5)
Patent settlement income	478	—	478	—
Non-GAAP operating expenses	81,036	55	64,540	50

Non-GAAP net income represents net income, as reported in our condensed consolidated statements of operations, excluding the impact of stock-based compensation expense, amortization expense of certain intangible assets, and income from a patent settlement. The following table reconciles GAAP net income to non-GAAP net income for the three months ended June 30, 2013 and June 30, 2012.

	Three Months Ended	
	June 30, 2013	June 30, 2012
	($ and share amounts in 000's, except per share amounts)	
Net Income:		
GAAP net income	8,979	13,950
Stock-based compensation expense [(1)]	10,707	7,852
Amortization expense of certain intangible assets [(2)]	354	226
Patent settlement income [(3)]	(478)	(478)
Provision for income taxes [(4)]	6,035	8,276
Non-GAAP income before provision for income taxes	25,597	29,826
Non-GAAP provision for income taxes [(5)]	(8,447)	(10,141)
Non-GAAP net income	17,150	19,685
Non-GAAP net income per share—diluted	0.10	0.12
Shares used in per share calculation—diluted	168,042	166,061

(1) Stock-based compensation expense is excluded from GAAP net income to reconcile to non-GAAP income before provision for income taxes.
(2) Effective second quarter of fiscal 2013, amortization expense of certain intangible assets is excluded from GAAP net income to reconcile to non-GAAP income before provision for income taxes. Prior period amounts have been adjusted to conform to current period presentation.
(3) The patent settlement income is excluded from GAAP net income to reconcile to non-GAAP income before provision for income taxes.
(4) Provision for income taxes is our GAAP tax provision that must included in GAAP net income to reconcile to non-GAAP income before provision for income taxes.
(5) We used non-GAAP effective tax rates of 33% and 34%, which could differ from the GAAP tax rates, to calculate non-GAAP net income for the three months ended June 30, 2013 and June 30, 2012, respectively.

Critical Accounting Policies and Estimates

Our discussion and analysis of our financial condition and results of operations are based upon our financial statements, which have been prepared in accordance with GAAP. These principles require us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses, cash flow and related disclosure of contingent assets and liabilities. Our estimates include those related to revenue recognition, stock-based compensation expense, valuation of inventory, warranty liabilities and accounting for income taxes. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. Actual results may differ from these estimates. To the extent that there are material differences between these estimates and our actual results, our future financial statements will be affected.

There have been no material changes in our significant accounting policies since the fiscal year ended December 31, 2012, except for the inclusion of policies related to goodwill and other indefinite-lived intangible assets.

Goodwill and other indefinite-lived intangible assets

Goodwill represents the excess of purchase consideration over the estimated fair value of net assets of businesses acquired in a business combination. Goodwill and other indefinite-lived intangible assets such as in-process research and development acquired in a business combination are not amortized, but instead tested for impairment at least annually during the fourth quarter. We perform our annual goodwill impairment analysis at the reporting unit level. As of June 30, 2013, we had one reporting unit.

In reviewing goodwill for impairment we have the option to (i) assess qualitative factors to determine whether it is more-likely-than-not that the fair value of the reporting unit is less than its carrying amount or (ii) bypass the qualitative assessment and proceed directly to a quantitative assessment. If we opt to perform a qualitative assessment, the factors we may review include, but are not limited to (a) macroeconomic conditions; (b) industry and market considerations; (c) cost factors; (d) overall financial performance; (e) other relevant entity-specific events such as changes in management, strategy, customers, or litigation; (f) events affecting the reporting unit; or (g) or sustained decrease in share price. If we believe, as a result of the qualitative assessment, that it is more-likely-than-not that the fair value of the reporting unit is less than its carrying amount, the quantitative impairment test will be required. Otherwise, no further testing will be required. A quantitative assessment utilizes a two-step process. In the first step, the fair value of the reporting unit is determined, and is compared against its carrying amount, including goodwill. We consider a combination of an income-based approach using projected discounted cash flows and a market-based approach using multiples of comparable companies to determine the fair value. The fair value of the reporting unit is estimated using significant judgment based on a combination of the income and the market approaches. Under the income approach, we estimate fair value of the reporting unit based on the present value of forecasted future cash flows that the reporting unit is expected to generate over its remaining life. Under the market approach, we estimate fair value of our reporting unit based on an analysis that compares the value of the reporting unit to values of other companies in similar lines of business. If the fair value of the reporting unit does not exceed its carrying value, then we perform the second step to measure the amount of impairment loss. The amount of impairment is determined by comparing the implied fair value of reporting unit goodwill to the carrying value of the goodwill. When the carrying value of the reporting unit's goodwill exceeds its implied fair value, we record an impairment loss equal to the difference.

Determining the fair value of the reporting unit is highly judgmental in nature and involves the use of significant estimates and assumptions. These estimates and assumptions include revenue growth rates and operating margins used to calculate projected future cash flows, operating trends, risk-adjusted discount rates, future economic and market conditions and determination of appropriate market comparables. We base our fair value estimates on assumptions we believe to be reasonable but that are unpredictable and inherently uncertain. Actual future results may differ from those estimates. We may also test goodwill and other intangible assets for impairment between annual tests in the presence of impairment indicators. Acquired in-process research and development assets are classified as indefinite-lived intangible assets until the successful completion or abandonment of the associated research and development efforts. Upon successful completion of the associated research and development efforts, the useful life of the asset is determined and the asset is amortized over its useful life. If the associated research and development efforts are abandoned, an impairment loss is recognized for the carrying value of the related asset.

Recent Accounting Pronouncements

In February 2013, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2013-02, *Comprehensive Income (Topic 220)-Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income* (“ASU 2013-02”). ASU 2013-02 requires an entity to report the effect of significant reclassifications out of accumulated other comprehensive income on the respective line items in net income if the amount being reclassified is required under GAAP to be reclassified in its entirety to net income. For other amounts that are not required under GAAP to be reclassified in their entirety to net income in the same reporting period, an entity is required to cross-reference other disclosures required under GAAP that provide additional detail about those amounts. We adopted ASU 2013-02 on January 1, 2013, and presented the effects within Note 15, *Accumulated Other Comprehensive Income*, of the notes to our condensed consolidated financial statements.

In July 2013, the FASB issued ASU No. 2013-11, *Income Taxes (Topic 740)-Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists* (“ASU 2013-11”). ASU 2013-11 provides guidance on the financial statement presentation of an unrecognized tax benefit when a net operating loss carryforward, similar tax loss, or tax credit carryforward exists. This new standard requires the netting of unrecognized tax benefits (“UTBs”) against a deferred tax asset for a loss or other carryforward that would apply in settlement of the uncertain tax positions. UTBs will be netted against all available same-jurisdiction loss or other tax carryforwards that would be utilized, rather than only against carryforwards that are created by the UTBs. ASU 2013-11 will be effective for us beginning in the first quarter of fiscal 2014. Early adoption is permitted. Since ASU 2013-11 only impacts financial statement disclosure requirements for unrecognized tax benefits, we do not expect its adoption to have an impact on our financial position or results of operations.

Results of Operations

Three months ended June 30, 2013 and June 30, 2012

Revenue

	Three Months Ended					
	June 30, 2013		June 30, 2012			
	Amount ($)	**% of Total Revenue**	**Amount ($)**	**% of Total Revenue**	**Change**	**% Change**
			($ amounts in 000's)			
Revenue:						
Product	66,525	45	61,692	48	4,833	8
Services	79,668	54	65,412	51	14,256	22
Ratable and other revenue	1,235	1	1,858	1	(623)	(34)
Total revenue	147,428	100	128,962	100	18,466	14
Revenue by geography:						
Americas	60,026	41	51,922	40	8,104	16
Europe, Middle East and Africa (“EMEA”)	50,801	34	43,664	34	7,137	16
Asia Pacific and Japan (“APAC”)	36,601	25	33,376	26	3,225	10
Total revenue	147,428	100	128,962	100	18,466	14

Total revenue increased by $18.5 million, or 14%, during the three months ended June 30, 2013 compared to the same period last year. All three regions experienced growth in revenue by 10% or more compared to the same period last year, with the Americas and EMEA regions each growing 16%. Product revenue increased by $4.8 million, or 8%, compared to the same period last year. The increase in product revenue was primarily driven by greater sales volume in our FortiGate product family, particularly with our entry-level products, wireless security and access point products, which contributed the largest portion of the growth. Services revenue increased by $14.3 million, or 22%, in the three months ended June 30, 2013 compared to the same period last year due to the recognition of revenue from our growing deferred revenue balance consisting of subscription and support contracts sold to a larger customer base.

Cost of revenue and gross margin

	Three Months Ended			
	June 30, 2013	June 30, 2012	Change	% Change
	($ amounts in 000's)			
Cost of revenue:				
Product	26,948	23,935	3,013	13
Services	16,259	12,467	3,792	30
Ratable and other revenue	501	725	(224)	(31)
Total cost of revenue	43,708	37,127	6,581	18
Gross margin (%):				
Product	59.5	61.2	(1.7)	
Services	79.6	80.9	(1.3)	
Ratable and other revenue	59.4	61.0	(1.6)	
Total gross margin	70.4	71.2	(0.8)	

Total gross margin decreased by 0.8 percentage points in the three months ended June 30, 2013 compared to the same period last year, as both product and services gross margins declined. Product gross margin decreased by 1.7 percentage points in the three months ended June 30, 2013 compared to the same period last year primarily as a result of the higher mix of entry-level products and higher overhead costs. Services gross margin decreased by 1.3 percentage points during the three months ended June 30, 2013 primarily due to our continued investments in our technical support organization to accommodate our expanding customer base and higher service level expectations from our enterprise customers. In addition, we experienced growth in our professional consulting services which have lower gross margins than our support and subscription businesses. Cost of services revenue increased by $3.8 million primarily due to a $2.8 million increase in cash-based personnel costs related to an increase in headcount, a $0.3 million increase in stock-based compensation expense, a $0.4 million increase in warranty-related costs and a $0.3 million increase in travel and depreciation expenses.

Operating expenses

	Three Months Ended					
	June 30, 2013		June 30, 2012			
	Amount ($)	% of Total Revenue	Amount ($)	% of Total Revenue	Change	% Change
	($ amounts in 000's)					
Operating expenses:						
Research and development	25,158	17	20,388	16	4,770	23
Sales and marketing	55,997	38	44,259	34	11,738	27
General and administrative	8,788	6	6,238	5	2,550	41
Total operating expenses	89,943	61	70,885	55	19,058	27

Research and development expense

Research and development expense increased by $4.8 million, or 23%, in the three months ended June 30, 2013 compared to the same period last year, primarily due to an increase of $3.1 million in cash-based personnel costs and $1.0 million in stock-based compensation expense as a result of increased headcount to support the development of new products and continued enhancements of our existing products. Other costs, including earn-out payments to former stockholders of Coyote, also increased by $0.7 million. We intend to continue to invest in our research and development organization, but we currently expect research and development expense as a percentage of total revenue to remain at approximately comparable levels during the remainder of fiscal 2013.

Sales and marketing expense

Sales and marketing expense increased by $11.7 million, or 27%, in the three months ended June 30, 2013 compared to the same period last year, primarily due to an increase of $6.1 million in cash-based personnel costs as we continued to increase our sales headcount in order to expand our global footprint. In addition, we incurred increases in marketing-related expenses of $1.6 million, travel expenses of $1.4 million, stock-based compensation expense of $1.1 million and, depreciation expenses of $0.6 million. As a percentage of total revenue, sales and marketing expenses increased as we continued to invest in our sales force to support future growth. We intend to continue to make investments in our sales resources and infrastructure which are critical to support sustainable growth, but we currently expect sales and marketing expense as a percentage of total revenue to remain at approximately comparable levels during the remainder of fiscal 2013.

General and administrative expense

General and administrative expense increased by $2.6 million, or 41%, in the three months ended June 30, 2013 compared to the same period last year. Cash-based personnel costs increased by $1.0 million and stock-based compensation expense increased by $0.4 million. In addition, we incurred $0.9 million of higher legal and accounting fees. We currently expect general and administrative expense as a percentage of total revenue to remain at approximately comparable levels during the remainder of fiscal 2013.

Interest income and other (expense) income, net

	Three Months Ended			
	June 30, 2013	June 30, 2012	Change	% Change
	($ amounts in 000's)			
Interest income	1,337	1,203	134	11
Other (expense) income, net	(100)	73	(173)	(237)

The $0.1 million increase in interest income in the three months ended June 30, 2013 compared to the same period last year was primarily due to interest earned on higher invested balances of cash, cash equivalents and investments. The change in other (expense) income, net, for the three months ended June 30, 2013 was the result of foreign exchange losses compared to foreign exchange gains in the same period last year.

Provision for income taxes

	Three Months Ended			
	June 30, 2013	June 30, 2012	Change	% Change
	($ amounts in 000's)			
Provision for income taxes	6,035	8,276	(2,241)	(27)
Effective tax rate (%)	40	37	3	

Our effective tax rate was 40% in the three months ended June 30, 2013, compared to an effective tax rate of 37% in the same period last year. The provision for income taxes for the periods presented is comprised of foreign income taxes, U.S. federal and state taxes, and withholding tax. The increase in the effective tax rate was primarily due to a reduction in tax benefits from stock options related to our foreign subsidiaries and an increase in non-deductible stock-based compensation expense.

As of June 30, 2013 and December 31, 2012, unrecognized tax benefits were $31.2 million and $27.8 million, respectively. The total amount of $30.8 million in unrecognized tax benefits, if recognized, would favorably impact the effective tax rate.

It is our policy to classify accrued interest and penalties related to unrecognized tax benefits in the provision for income taxes. As of June 30, 2013, we had accrued approximately $2.2 million for estimated interest related to uncertain tax provisions.

The State of California has been conducting an audit of our state income tax returns for fiscal 2010 and fiscal 2011. We do not expect this audit to have a significant detrimental effect on our income tax liability nor have a material impact on our results of operations.

Within the next twelve months, it is possible our uncertain tax benefit will decrease up to $1.1 million. This possible decrease in our uncertain tax benefit may be a result of several factors, including a lapse of statute of limitations, provided no tax authority conducts a new examination. This may impact our future effective tax rate.

Six months ended June 30, 2013 and June 30, 2012

Revenue

	Six Months Ended					
	June 30, 2013		June 30, 2012			
	Amount ($)	% of Total Revenue	Amount ($)	% of Total Revenue	Change	% Change
	($ amounts in 000's)					
Revenue:						
Product	124,475	44	114,896	47	9,579	8
Services	155,564	55	127,550	52	28,014	22
Ratable and other revenue	3,209	1	3,763	1	(554)	(15)
Total revenue	283,248	100	246,209	100	37,039	15
Revenue by geography:						
Americas	112,653	40	98,353	40	14,300	15
EMEA	98,127	35	84,550	34	13,577	16
APAC	72,468	25	63,306	26	9,162	14
Total revenue	283,248	100	246,209	100	37,039	15

Total revenue increased by $37.0 million, or 15%, during the six months ended June 30, 2013 compared to the same period last year. All three regions contributed comparable growth on a percentage basis. Product revenue increased by $9.6 million, or 8%, compared to the same period last year. The increase in product revenue was primarily driven by greater sales volume in our FortiGate product family, particularly entry-level products, wireless security and access point products, which contributed the largest portion of the growth. Services revenue increased by $28.0 million, or 22%, in the six months ended June 30, 2013 compared to the same period last year due to the recognition of revenue from our growing deferred revenue balance consisting of subscription and support contracts sold to a larger customer base.

Cost of revenue and gross margin

	Six Months Ended			
	June 30, 2013	June 30, 2012	Change	% Change
	($ amounts in 000's)			
Cost of revenue:				
Product	49,906	43,003	6,903	16
Services	31,833	23,680	8,153	34
Ratable and other revenue	1,097	1,487	(390)	(26)
Total cost of revenue	82,836	68,170	14,666	22
Gross margin (%):				
Product	59.9	62.6	(2.7)	
Services	79.5	81.4	(1.9)	
Ratable and other revenue	65.8	60.5	5.3	
Total gross margin	70.8	72.3	(1.5)	

Total gross margin decreased by 1.5 percentage points in the six months ended June 30, 2013 compared to the same period last year, as both product and services gross margins declined. Product gross margin decreased by 2.7 percentage points in the six months ended June 30, 2013 compared to the same period last year primarily as a result of the higher mix of entry-level products and higher overhead costs. Services gross margin decreased by 1.9 percentage points during the six months ended June 30, 2013 primarily due to our continued investments in our technical support organization to accommodate our expanding customer base and higher service level expectations from our enterprise customers. In addition, we experienced growth in our professional consulting services which have lower gross margins than our support and subscription businesses. Cost of services revenue increased by $8.2 million primarily due to a $5.9 million increase in cash-based personnel costs related to an increase in headcount, a $0.6 million increase in stock-based compensation expense, a $0.7 million increase in warranty-related costs and freight, and a $0.5 million increase in each of the professional services and depreciation expenses.

Operating expenses

	Six Months Ended					
	June 30, 2013		June 30, 2012			
	Amount ($)	% of Total Revenue	Amount ($)	% of Total Revenue	Change	% Change
	($ amounts in 000's)					
Operating expenses:						
Research and development	48,492	17	40,055	16	8,437	21
Sales and marketing	105,973	37	86,295	35	19,678	23
General and administrative	16,779	6	12,023	5	4,756	40
Total operating expenses	171,244	60	138,373	56	32,871	24

Research and development expense

Research and development expense increased by $8.4 million, or 21%, in the six months ended June 30, 2013 compared to the same period last year, primarily due to an increase of $6.0 million in cash-based personnel costs and $1.8 million in stock-based compensation expense as a result of increased headcount to support the development of new products and continued enhancements of our existing products.

Sales and marketing expense

Sales and marketing expense increased by $19.7 million, or 23%, in the six months ended June 30, 2013 compared to the same period last year, primarily due to an increase of $11.0 million in cash-based personnel costs as we continued to increase our sales headcount in order to expand our global footprint. In addition, we incurred increases in travel expenses of $2.3 million, stock-based compensation expense of $1.8 million, trade shows and promotional expenses of $1.6 million and depreciation expenses of $1.3 million. As a percentage of total revenue, sales and marketing expenses increased as we accelerated the investment in our sales force to support future growth.

General and administrative expense

General and administrative expense increased by $4.8 million, or 40%, in the six months ended June 30, 2013 compared to the same period last year. Cash-based personnel costs increased by $1.7 million and stock-based compensation expense increased by $0.7 million. In addition, we incurred $1.9 million of higher legal and accounting fees.

Interest income and other (expense) income, net

	Six Months Ended			
	June 30, 2013	June 30, 2012	Change	% Change
	($ amounts in 000's)			
Interest income	2,706	2,287	419	18
Other (expense) income, net	115	3	112	3,733

The $0.4 million increase in interest income in the six months ended June 30, 2013 compared to the same period last year, was primarily due to interest earned on higher invested balances of cash, cash equivalents and investments. The change in other (expense) income, net, for the six months ended June 30, 2013 was the result of higher foreign exchange gains compared to the same period last year.

Provision for income taxes

	Six Months Ended			
	June 30, 2013	June 30, 2012	Change	% Change
	($ amounts in 000's)			
Provision for income taxes	10,761	13,833	(3,072)	(22)
Effective tax rate (%)	34	33	1	

Our effective tax rate was 34% in the six months ended June 30, 2013, compared to an effective tax rate of 33% in the same period last year. The provision for income taxes for the periods presented is comprised of foreign income taxes, U.S. federal and state taxes, and withholding tax. The increase in the effective tax rate was primarily due to a reduction in tax benefits from the stock options related to our foreign subsidiaries and an increase in non-deductible stock based compensation expense. Further, in January 2013, the American Taxpayer Relief Act of 2012 reinstated the U.S. Federal Research and Development Tax Credit retroactive to January 1, 2012. As a result, the U.S. Federal Research and Development Tax Credit benefit was recorded in the six months ended June 30, 2013.

Liquidity and Capital Resources

	June 30, 2013	December 31, 2012
	($ amounts in 000's)	
Cash and cash equivalents	123,468	122,975
Investments	690,942	616,611
Total cash, cash equivalents and investments	814,410	739,586
Working capital	311,919	249,970

The following table presents a summary of our cash flows:

	Six months ended June 30, 2013	Six months ended June 30, 2012
	($ amounts in 000's)	
Cash provided by operating activities	75,332	92,803
Cash used in investing activities	(91,514)	(105,933)
Cash provided by financing activities	17,484	22,808
Effect of exchange rates on cash and cash equivalents	(809)	(442)
Net increase in cash and cash equivalents	493	9,236

As of June 30, 2013, our cash, cash equivalents, and investments of $814.4 million were held for working-capital purposes and were invested primarily in money market funds, commercial paper, corporate debt securities, municipal bonds and certificates of deposit and term deposits. As of June 30, 2013, $63.6 million of our cash was held by certain international subsidiaries and is not immediately available to fund domestic operations unless the cash is repatriated. While we do not intend to do so, should this amount be repatriated, it would be subject to U.S. federal income tax which would be partially offset by foreign tax credits. We do not enter into investments for trading or speculative purposes. We believe that our existing cash, cash equivalents and investments will be sufficient to meet our anticipated cash needs for at least the next 12 months. Our future capital requirements will depend on many factors including our growth rate, the timing and extent of spending to support development efforts, the expansion of sales and marketing activities, the introduction of new and enhanced products and services offerings, the costs to ensure access to adequate manufacturing capacity and the continuing market acceptance of our products. Historically, we have required capital principally to fund our working capital needs, capital expenditures, and acquisition activities. In the event that additional financing is required from outside sources, we may not be able to raise it on terms acceptable to us or at all. If we are unable to raise additional capital when desired, our business, operating results and financial condition would be adversely affected.

The following table presents our cash flows from operating activities:

	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
	($ amounts in 000's)	
Net income	21,228	28,123
Adjustments for non-cash charges [(1)]	30,398	21,576
Net income before non-cash charges	51,626	49,699
Increase in deferred revenue	25,943	36,492
(Increase) decrease in accounts receivable—net	(801)	171
Increase in accounts payable and accrued liabilities, net [(2)]	13,998	4,222
Increase in income taxes payable [(2)]	11,339	5,743
(Increase) decrease in other assets [(2)]	(12,442)	1,461
Increase in inventory	(16,375)	(7,952)
Increase in accrued payroll and compensation	2,287	3,119
Increase in prepaid expenses and other current assets [(2)]	(243)	(152)
Net cash provided by operating activities	75,332	92,803

(1) Non-cash charges consist of stock-based compensation expense, depreciation and amortization, amortization of investment premiums, an excess tax benefit from our employee stock option plans, and other non-cash items, net.

(2) Certain prior period amounts have been combined to conform to current period presentation.

Operating Activities

Cash generated by operating activities is our primary source of liquidity. Our operating activities during the six months ended June 30, 2013, provided $75.3 million in cash as a result of our billings growth, profitability, and our ability to successfully manage our working capital. Net income was $21.2 million, increased by adjustments for non-cash charges of $30.4 million and sources of cash of $53.6 million, partially offset by uses of cash of $29.9 million from changes in operating assets and liabilities. Adjustments for non-cash charges consisted of stock-based compensation expense of $20.0 million, amortization of investment premiums of $5.9 million, depreciation and amortization of $7.3 million, partially offset by an excess tax benefit from stock option exercises of $1.9 million and other non-cash items, net, of $0.9 million. Sources of cash were related to a $25.9 million increase in deferred revenue which was attributable primarily to increased sales of our subscription and support services, which have yet to be recognized in income, a $14.0 million increase in accounts payable and accrued liabilities related to timing of payments, a $11.3 million increase in income taxes payable due to our continued profitability and timing of tax payments, and a $2.3 million increase in accrued payroll and compensation primarily related to increased headcount and employer taxes related to the exercise of stock options. Uses of cash were related to a $16.4 million increase in inventory to ensure an adequate level of inventory to support high-turnover channel driven products to reduce the risk of product stockouts, a $12.4 million increase in other assets, a $0.8 million increase in accounts receivable due to timing of collections, and a $0.2 million increase in prepaid expenses and other current assets.

Our operating activities during the six months ended June 30, 2012 provided $92.8 million in cash as a result of net income of $28.1 million, increased by adjustments for non-cash charges of $21.6 million and sources of cash of $51.2 million partially offset by uses of cash of $8.1 million. Adjustments for non-cash charges consisted of stock-based compensation of $15.1 million, amortization of investment premiums of $6.5 million, and depreciation and amortization of $5.1 million, offset partially by an excess tax benefit from stock option exercises of $5.2 million. Sources of cash were related to a $36.5 million increase in deferred revenue which was attributable primarily to increased sales of our subscription and support services, which have yet to be recognized as income, a $4.2 million increase in accounts payable and accrued liabilities, a $3.1 million increase in accrued payroll and compensation, a $5.7 million increase in income taxes payable, a $1.5 million decrease in other assets, and a $0.2 million decrease in accounts receivable, net. Uses of cash were primarily related to an $8.0 million increase in inventory to ensure an adequate level of inventory to support high-turnover channel driven products to reduce the risk of product stockouts and a $0.2 million decrease in prepaid expenses and other current assets.

Investing Activities

Our investing activities during the six months ended June 30, 2013 consisted primarily of purchases and sales of investments, and to a much lesser extent, acquisitions and capital expenditures. The $91.5 million of cash used by investing activities was due to net purchases of investments of $82.0 million, acquisition of Coyote for $6.0 million and purchases of property and equipment of $3.6 million.

Our investing activities during the six months ended June 30, 2012 consisted primarily of purchases, sales and maturities of investments, and to a lesser extent capital expenditures and acquisitions. The $105.9 million of cash used in investing activities during the six months ended June 30, 2012 was primarily due to net purchases of investments of $101.5 million, purchases of property and equipment of $3.9 million, and our acquisition of IntruGuard for $0.6 million.

Financing Activities

Our financing activities during the six months ended June 30, 2013 resulted in net cash provided of $17.5 million as a result of receiving proceeds of $9.1 million and $6.5 million from the issuance of common stock under our stock option plans and ESPP, respectively, and an excess tax benefit from employee stock option exercises of $1.9 million.

Our financing activities during the six months ended June 30, 2012 resulted in net cash provided of $22.8 million as a result of proceeds of $12.7 million and $5.0 million, from the issuance of common stock under our stock option plans and ESPP, respectively, and an excess tax benefit from employee stock option exercises of $5.2 million.

Contractual Obligations and Commitments

There have been no significant changes during the six months ended June 30, 2013, to the contractual obligations and commitments disclosed in Management's Discussion and Analysis of Financial Condition and Results of Operations, set forth in Part II, Item 7, of the Form 10-K, other than the following which summarizes the specified contractual obligations as of June 30, 2013:

	Payments Due by Period				
	Total	**Less than 1 year**	**1 - 3 years**	**3 - 5 years**	**More than 5 years**
	($ amounts in 000's)				
Operating leases (1)	29,827	4,325	14,326	6,869	4,307
Purchase commitments (2)	39,803	39,803	—	—	—
Total (3)	69,630	44,128	14,326	6,869	4,307

(1) Consists of contractual obligations from non-cancelable office space under operating leases. In March 2013, we extended the operating lease for one of our existing facilities in Canada through 2020. The total incremental lease payments are $14.3 million.

(2) Consists of minimum purchase commitments with independent contract manufacturers. As of June 30, 2013, we had $39.8 million of open purchase orders with our independent contract manufacturers that may not be cancelable compared to $30.0 million as of December 31, 2012. The increase is required to replenish current inventory and to ensure adequate future inventory related to new product releases and product lead-times for certain products.

(3) No tax liabilities related to uncertain tax positions have been included in the table. As of June 30, 2013, we had $33.4 million of long-term tax liabilities, including interest, related to uncertain tax positions. Because of the high degree of uncertainty regarding the settlement of these liabilities, we are unable to estimate the years in which future cash outflows may occur.

Off-Balance Sheet Arrangements

As of June 30, 2013, we did not have any relationships with unconsolidated organizations or financial partnerships, such as structured finance or special purpose entities that would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

There have been no material changes in our market risk during the six months ended June 30, 2013, compared to the disclosures in Part II, Item 7A of the Form 10-K.

ITEM 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) or 15d-15(e) under the Exchange Act) as of June 30, 2013. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints and that management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs.

Based on that evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures were effective as of June 30, 2013, to provide reasonable assurance that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, and that such information is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate, to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) or 15d-15(f) under the Exchange Act) during the three months ended June 30, 2013 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Part II

ITEM 1. Legal Proceedings

In August 2009, ESR, a non-practicing entity, filed a complaint against us in the United States District Court for the District of Delaware alleging infringement by us and other defendants of two patents. The plaintiffs are claiming unspecified damages and requesting an injunction against the alleged infringement. In June 2010, the Court granted our motion to stay pending the outcome of reexamination proceedings in the U.S. Patent and Trademark Office ("PTO") on both asserted patents. The PTO rejected all of the claims of the patents in the suit and ESR appealed this result to the BPAI. In August 2012, the BPAI completed its review of both reexamination proceedings, and, after the BPAI's review, all claims of the asserted ESR patents remain rejected. In October 2012, ESR filed an additional appeal of the BPAI decision with the United States Court of Appeal for the Federal Circuit. That appeal is still pending. The litigation related to ESR is no longer material to us, and we will no longer report on this case.

In July 2010, NPS, a non-practicing entity, filed a complaint in the United States District Court for the Eastern District of Texas alleging patent infringement by us and other defendants. NPS is claiming unspecified damages, including treble damages for willful infringement, and requests an injunction against such alleged infringement. In December 2011, the United States District Court for the Eastern District of Texas ordered the case to be transferred to the Northern District of California. In June 2012, the United States District Court for the Northern District of California dismissed the other defendants for misjoinder, and the case is proceeding with Fortinet as the sole defendant. We have filed a motion to dismiss the case and a separate motion for summary judgment, both of which are pending. This case is currently scheduled for a jury trial starting in September 2013.

In June 2012, we received a letter from SRI claiming that we infringed certain SRI patents. Subsequently, we filed a complaint in the United States District Court for the Northern District of California seeking declaratory relief and a judgment that the SRI patents were invalid, unenforceable and not infringed by any of our products or services. The case is proceeding in the United States District Court for the Northern District of California.

We do not currently believe that any of the foregoing litigation matters will have a material adverse effect on our business.

ITEM 1A. Risk Factors

Investing in our common stock involves a high degree of risk. You should carefully consider the following risks and all other information contained in this Quarterly Report on Form 10-Q, including our condensed consolidated financial statements and the related notes, before investing in our common stock. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties that we are unaware of, or that we currently believe are not material, also may become important factors that affect us. If any of the following risks materialize, our business, financial condition and results of operations could be materially harmed. In that case, the trading price of our common stock could decline, and you may lose some or all of your investment.

Risks Related to Our Business

Our quarterly operating results are likely to vary significantly and be unpredictable.

Our operating results have historically varied from period to period, and we expect that they will continue to do so as a result of a number of factors, many of which are outside of our control and may be difficult to predict, including:

- the level of demand for our products and services;
- the timing of channel partner and end-customer orders and our reliance on a concentration of shipments at the end of the quarter;
- the timing of shipments, which may depend on many factors such as inventory levels and logistics, our ability to ship new products on schedule and to accurately forecast inventory requirements, and potential delays in the manufacturing process;
- inventory imbalances, such as those related to new products and the end of life of existing products;

- the mix of products sold, the mix of revenue between products and services and the degree to which products and services are bundled and sold together for a package price;
- the budgeting cycles and purchasing practices of our channel partners and end-customers;
- seasonal buying patterns of our end-customers;
- the timing of revenue recognition for our sales, which may be affected by both the mix of sales by our “sell-in” versus our “sell-through” channel partners, and by the extent to which we bring on new distributors;
- the accuracy and timing of point of sale reporting by our sell-through distributors, which impacts our ability to recognize revenue;
- the level of perceived threats to network security, which may fluctuate from period to period;
- changes in end-customer, distributor or reseller requirements or market needs and buying practices and patterns;
- changes in the growth rate of the network security or UTM markets;
- the timing and success of new product and service introductions by us or our competitors or any other change in the competitive landscape of our industry, including consolidation among our competitors or end-customers;
- deferral of orders from end-customers in anticipation of new products or product enhancements announced by us or our competitors;
- increases or decreases in our expenses caused by fluctuations in foreign currency exchange rates, as a significant portion of our expenses are incurred and paid in currencies other than the U.S. dollar;
- decisions by potential end-customers to purchase network security solutions from larger, more established security vendors or from their primary network equipment vendors;
- price competition, and increased competitiveness in general in our market;
- changes in customer renewal rates for our services;
- changes in the payment terms of services contracts or the length of services contracts sold;
- increased expenses, unforeseen liabilities or write-downs and any impact on results of operations from any acquisition consummated;
- insolvency or credit difficulties confronting our customers, affecting their ability to purchase or pay for our products and services;
- disruptions in our channel or termination of our relationship with important channel partners;
- insolvency or credit difficulties confronting our key suppliers, which could disrupt our supply chain;
- general economic conditions, both in our domestic and foreign markets; and
- future accounting pronouncements or changes in our accounting policies.

Any one of the factors above or the cumulative effect of some of the factors referred to above may result in significant fluctuations in our quarterly financial and other operating results, including fluctuations in our key metrics. This variability and unpredictability could result in our failing to meet our internal operating plan or the expectations of securities analysts or investors for any period. If we fail to meet or exceed such expectations for these or any other reasons, the market price of our shares could fall substantially and we could face costly lawsuits, including securities class action suits. In addition, a significant percentage of our operating expenses are fixed in nature and based on forecasted revenue trends. Accordingly, in the event of revenue shortfalls, we are generally unable to mitigate the negative impact on margins in the short term.

Our billings and revenue growth may slow or may not continue.

Billings and revenue growth may slow, or we may experience a decrease in billings and revenue, for a number of reasons, including a slowdown in demand for our products or services, an increase in competition, a decrease in the growth of our overall market, softness in demand in certain geographies, or if we fail for any reason to continue to capitalize on growth opportunities. For example, we experienced lower than expected billings during the first quarter of 2013 due to a number of factors, including decreased sales in the service provider market and slower sales in Latin America and EMEA. Our expenses as a percentage of total revenue may be higher than expected if our revenue is lower than expectations, and we may not be able to sustain profitability in future periods if we fail to increase billings, revenue or deferred revenue, do not appropriately manage our cost structure, or encounter unanticipated liabilities. Any failure by us to maintain profitability and continue our billings and revenue growth could cause the price of our common stock to materially decline.

Reliance on a concentration of shipments at the end of the quarter could cause our billings and revenue to fall below expected levels.

As a result of customer-buying patterns and the efforts of our sales force and channel partners to meet or exceed quarterly quotas, we have historically received a substantial portion of each quarter's sales orders and generated a substantial portion of each quarter's billings and revenue during the last two weeks of the quarter. For example, on average over the past eight quarters, our shipments during the last two weeks of each quarter accounted for approximately 37% of aggregate billings for each quarter. If expected orders at the end of any quarter are delayed for any reason, including the failure of anticipated purchase orders to materialize, our logistics partners' inability to ship products prior to quarter-end to fulfill purchase orders received near the end of the quarter, our failure to manage inventory to meet demand, our inability to release new products on schedule, any failure of our systems related to order review and processing, or any delays in shipments based on trade compliance requirements, our billings and revenue for that quarter could fall below our expectations or those of securities analysts and investors, resulting in a decline in our stock price.

We rely significantly on revenue from subscription and support services which may decline, and because we recognize revenue from subscription and support services over the term of the relevant service period, downturns or upturns in sales of subscription and support services are not immediately reflected in full in our operating results.

Our subscription and support services revenue has historically accounted for a significant percentage of our total revenue. Sales of new or renewal subscription and support services contracts may decline and fluctuate as a result of a number of factors, including end-customers' level of satisfaction with our products and services, the prices of our products and services, the prices of products and services offered by our competitors or reductions in our customers' spending levels. If our sales of new or renewal subscription and support services contracts decline, our revenue and revenue growth may decline and our business will suffer. In addition, in the event significant customers require payment terms for subscription or support services in arrears or for shorter periods of time than annually, such as monthly or quarterly, this may negatively impact subscription and support billing. Furthermore, we recognize subscription and support services revenue monthly over the term of the relevant service period, which is typically one year but has been as long as five years. As a result, much of the subscription and support services revenue we report each quarter is the recognition of deferred revenue from subscription and support services contracts entered into during previous quarters. Consequently, a decline in new or renewed subscription or support services contracts in any one quarter will not be fully reflected in revenue in that quarter but will negatively affect our revenue in future quarters. Accordingly, the effect of significant downturns in new or renewed sales of our subscriptions or support services is not reflected in full in our statements of operations until future periods. Our subscription and support services revenue also makes it difficult for us to rapidly increase our revenue through additional service sales in any period, as revenue from new and renewal services contracts must be recognized over the applicable service period.

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

Managing our inventory is complex. Our channel partners may increase orders during periods of product shortages, cancel orders if their inventory is too high, return products or take advantage of price protection (if any is available to the particular partner), or delay orders in anticipation of new products. They also may adjust their orders in response to the supply of our products and the products of our competitors that are available to them and in response to seasonal fluctuations in end-customer demand. Furthermore, if the time required to manufacture certain products or ship products increases for any reason, this could result in inventory shortfalls. Management of our inventory is further complicated by the significant number of different products and models that we sell.

In addition, for those channel partners that have rights of return, inventory held by such channel partners affects our results of operations. Our inventory management systems and related supply chain visibility tools may be inadequate to enable us to effectively manage inventory. Inventory management remains an area of focus as we balance the need to maintain inventory levels that are sufficient to ensure competitive lead times against the risk of inventory obsolescence because of rapidly changing technology and customer requirements. If we ultimately determine that we have excess inventory, we may have to reduce our prices and write-down inventory, which in turn could result in lower gross margins. Alternatively, insufficient inventory levels may lead to shortages that result in delayed revenue or loss of sales opportunities altogether as potential end-customers turn to competitors' products that are readily available. For example, we experienced inventory shortages in the first quarter of 2013 due to more demand for certain products than we had forecasted. If we are unable to effectively manage our inventory and that of our channel partners, our results of operations could be adversely affected.

We rely on third-party channel partners to generate substantially all of our revenue. If our partners fail to perform, our ability to sell our products and services will be limited, and if we fail to optimize our channel partner model going forward, our operating results will be harmed.

Substantially all of our revenue is generated through sales by our channel partners, which include distributors and resellers. We depend upon our channel partners to generate sales opportunities and manage the sales process. To the extent our channel partners are unsuccessful in selling our products, or we are unable to enter into arrangements with, and retain, a sufficient number of high quality channel partners in each of the regions in which we sell products, and keep them motivated to sell our products, our ability to sell our products and operating results will be harmed. The termination of our relationship with any significant channel partner may adversely impact our sales and operating results.

We provide sales channel partners with specific programs to assist them in selling our products, but there can be no assurance that these programs will be effective. In addition, our channel partners may be unsuccessful in marketing, selling and supporting our products and services. Our channel partners generally do not have minimum purchase requirements. They may also market, sell and support products and services that are competitive with ours, and may devote more resources to the marketing, sales and support of such products. They may also have incentives to promote our competitors' products to the detriment of our own. They may cease selling our products altogether. We cannot assure you that we will retain these channel partners or that we will be able to secure additional or replacement partners or that existing channel partners will continue to perform. The loss of one or more of our significant channel partners or the failure to obtain and ship a number of large orders each quarter through them could harm our operating results. In addition, any new sales channel partner will require extensive training and may take several months or more to achieve productivity. Our channel partner sales structure could subject us to lawsuits, potential liability and reputational harm if, for example, any of our channel partners misrepresent the functionality of our products or services to end-customers or our channel partners violate laws or our corporate policies. If we fail to optimize our channel partner model or fail to manage existing sales channels, our business will be seriously harmed.

If we are not successful in continuing to execute our strategy to increase our sales to larger end-customers, our results of operations may suffer.

An important part of our growth strategy is to increase sales of our products to large enterprises, service providers and governmental entities. Sales to enterprises, service providers and governmental entities involve risks that may not be present (or that are present to a lesser extent) with sales to small-to-mid-sized entities. These risks include:

- increased competition from competitors, such as Cisco Systems, Inc. ("Cisco"), Sourcefire, Inc. ("Sourcefire") (acquired by Cisco) Check Point Software Technologies Ltd. ("Check Point"), McAfee, Inc. ("McAfee") (acquired by Intel Corporation ("Intel")), Blue Coat Systems, Inc. ("Blue Coat"), Palo Alto Networks, Inc. ("Palo Alto Networks"), SonicWALL, Inc. ("SonicWALL") (acquired by Dell Inc. ("Dell")), Juniper Networks, Inc. ("Juniper"), and Stonesoft Corporation ("Stonesoft") (acquired by McAfee) that traditionally target enterprises, service providers and governmental entities and that may already have purchase commitments from those end-customers;

- increased purchasing power and leverage held by large end-customers in negotiating contractual arrangements;

- unanticipated changes in the capital resources of or purchasing behavior of large end-customers, including changes in the volume and frequency of their purchases;

- more stringent support requirements in our support service contracts, including stricter support response times, more complex customer requirements, and increased penalties for any failure to meet support requirements; and
- longer sales cycles and the associated risk that substantial time and resources may be spent on a potential end-customer that elects not to purchase our products and services.

Large enterprises, service providers and governmental entities often undertake a significant evaluation process that results in a lengthy sales cycle, in some cases over 12 months. Although we have a channel sales model, our sales representatives typically engage in direct interaction with our distributors and resellers in connection with sales to larger end-customers. Due to the lengthy nature, the size and scope, and stringent requirements of these evaluations, we typically provide evaluation products to these customers. We may spend substantial time, effort and money in our sales efforts without being successful in producing any sales. If we are unsuccessful in converting these evaluations into sales, we may experience an increased inventory of used products and potentially increased write-offs. In addition, product purchases by enterprises, service providers and governmental entities are frequently subject to budget constraints, multiple approvals, and unplanned administrative, processing and other delays. Finally, enterprises, service providers and governmental entities typically have longer implementation cycles, require greater product functionality and scalability and a broader range of services, including design services, demand that vendors take on a larger share of risks, sometimes require acceptance provisions that can lead to a delay in revenue recognition, and expect greater payment flexibility from vendors. All these factors can add further risk to business conducted with these customers. If sales expected from a large end-customer for a particular quarter are not realized in that quarter or at all, our business, operating results and financial condition could be materially and adversely affected.

The average sales prices of our products may decrease, which may reduce our gross profits and adversely impact our financial results and the trading price of our common stock.

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

Actual, possible or perceived defects or vulnerabilities in our products or services, the failure of our products or services to prevent a virus or security breach, or misuse of our products could harm our reputation and divert resources.

Because our products and services are complex, they have contained and may contain defects or errors that are not detected until after their commercial release and deployment by our customers. Defects or vulnerabilities may impede or block network traffic or cause our products or services to be vulnerable to electronic break-ins or cause them to fail to help secure networks. Because the techniques used by computer hackers to access or sabotage networks change frequently and generally are not recognized until launched against a target, we may be unable to anticipate these techniques. In addition, defects or errors in our FortiGuard subscription updates or our FortiGate appliances could result in a failure of our FortiGuard services to effectively update end-customers' FortiGate appliances and thereby leave customers vulnerable to attacks. Furthermore, our solutions may also fail to detect or prevent viruses, worms or similar threats due to a number of reasons such as the evolving nature of such threats and the continual emergence of new threats that we may fail to add to our FortiGuard databases in time to protect our end-customers' networks. Our FortiGuard or FortiCare data centers and networks may also experience technical failures and downtime, and may fail to distribute appropriate updates, or fail to meet the increased requirements of a growing customer base. Any such technical failure, downtime, or failures in general may temporarily or permanently expose our end-customers' networks, leaving their networks unprotected against the latest security threats.

An actual, possible or perceived security breach or infection of the network of one of our end-customers, regardless of whether the breach is attributable to the failure of our products or services to prevent the security breach, could adversely affect the market's perception of our security products and services. We may not be able to correct any security flaws or vulnerabilities promptly, or at all. Our products may also be misused by end-customers or third parties who obtain access to our products. For example, our products could be used to censor private access to certain information on the Internet. Such use of our products for censorship could result in negative press coverage and negatively affect our reputation, even if we take reasonable measures to prevent any improper shipment of our products or if our products are provided by an unauthorized third-party. Any actual, possible, or perceived defects, errors or vulnerabilities in our products, or misuse of our products, could result in:

- expenditure of significant financial and product development resources in efforts to analyze, correct, eliminate or work-around errors or defects or to address and eliminate vulnerabilities;
- loss of existing or potential end-customers or channel partners;
- delayed or lost revenue;
- delay or failure to attain market acceptance;
- negative publicity, which will harm our reputation; and
- litigation, regulatory inquiries or investigations that may be costly and harm our reputation.

Our business and operations have experienced growth, and if we do not appropriately manage any future growth, or are unable to improve our systems and processes, our operating results will be negatively affected.

Our business has grown over the last several years. We rely heavily on information technology systems to help manage critical functions such as order processing, revenue recognition, financial forecasts, inventory and supply chain management and trade compliance reviews. However, we have been slow to adopt and implement certain automated functions, like Electronic Data Interchange, which could have a negative impact on our business. For example, a large part of our order processing relies on the manual processing of emails internally and from our customers. Combined with the fact that we may receive a majority of our orders in the last few weeks of any given quarter, a significant interruption in our email service or other systems could result in delayed order fulfillment and decreased revenue for that quarter. To manage any future growth effectively, we must continue to improve and expand our information technology and financial infrastructure, operating and administrative systems and controls, and continue to manage headcount, capital and processes in an efficient manner. We may not be able to successfully implement improvements to these systems and processes in a timely or efficient manner. For example, we are in the planning stages for an upgrade to our enterprise resource planning system and such change may cause disruption and additional cost. In addition, our systems and processes may not prevent or detect all errors, omissions or fraud. Our failure to improve our systems and processes, or their failure to operate in the intended manner, may result in our inability to manage the growth of our business and to accurately forecast our revenue, expenses and earnings, or to prevent certain losses. Our productivity and the quality of our products and services may be adversely affected if we do not integrate and train our new employees quickly and effectively. Any future growth would add complexity to our organization and require effective coordination throughout our organization. Failure to manage any future growth effectively could result in increased costs and harm our results of operations.

If our estimates or judgments relating to our critical accounting policies are based on assumptions that change or prove to be incorrect, our operating results could fall below expectations of securities analysts and investors, resulting in a decline in our stock price.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, as provided in “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in this Quarterly Report on Form 10-Q, 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. Our operating results may be adversely affected if our assumptions change or if actual circumstances differ from those in our assumptions, which could cause our operating results to fall below the expectations of securities analysts and investors, resulting in a decline in our stock price. Significant assumptions and estimates used in preparing our consolidated financial statements include those related to revenue recognition, stock-based compensation expense, valuation of inventory, warranty liabilities, and accounting for income taxes.

We offer retroactive price protection to certain of our major distributors, and if we fail to balance their inventory with end-customer demand for our products, our allowance for price protection may be inadequate, which could adversely affect our results of operations.

We provide certain of our major distributors with price protection rights for inventories of our products held by them. If we reduce the list price of our products, certain distributors receive refunds or credits from us that reduce the price of such products held in their inventory based upon the new list price. Future credits for price protection will depend on the percentage of our price reductions for the products in inventory and our ability to manage the levels of our major distributors' inventories. If future price protection adjustments are higher than expected, our future results of operations could be materially and adversely affected.

If we are unable to hire, retain and motivate qualified personnel, our business will suffer.

Our future success depends, in part, on our ability to continue to attract and retain highly skilled personnel. The loss of the services of any of our key personnel, the inability to attract or retain qualified personnel, or delays in hiring required personnel, particularly in engineering and sales, may seriously harm our business, financial condition and results of operations. From time to time, we have experienced turnover in our management-level personnel. None of our key employees has an employment agreement for a specific term, and any of our employees may terminate their employment at any time. Our ability to continue to attract and retain highly skilled personnel will be critical to our future success. Competition for highly-skilled personnel is frequently intense, especially in the locations where we have a substantial presence and need for highly-skilled personnel: the San Francisco Bay Area, Vancouver, Canada and Beijing, China. We may not be successful in attracting, assimilating or retaining qualified personnel to fulfill our current or future needs. Also, to the extent we hire personnel from competitors, we may be subject to allegations that they have been improperly solicited or divulged proprietary or other confidential information.

We are dependent on the continued services and performance of our senior management, the loss of any of whom could adversely affect our business, operating results and financial condition.

Our future performance depends on the continued services and continuing contributions of our senior management to execute on our business plan, and to identify and pursue new opportunities and product innovations. The loss of services of members of senior management, particularly Ken Xie, our Co-founder, President and Chief Executive Officer and Michael Xie, our Co-founder, Vice President of Engineering and Chief Technology Officer, and any of our senior sales leaders or functional area leaders, could significantly delay or prevent the achievement of our development and strategic objectives. We recently hired a new Chief Financial Officer and Chief Operating Officer, and it will take time for this executive officer to become fully integrated in his new role. In addition, key personnel may be distracted by activities unrelated to our business. The loss of the services, or distraction, of our senior management for any reason could adversely affect our business, financial condition and results of operations.

Adverse economic conditions or reduced information technology spending may adversely impact our business.

Our business depends on the overall demand for information technology and on the economic health of our current and prospective customers. In addition, the purchase of our products is often discretionary and may involve a significant commitment of capital and other resources. Weak global economic conditions, weak economic conditions in certain geographies, or a reduction in information technology spending regardless of macro-economic conditions, could adversely impact our business, financial condition and results of operations in a number of ways, including longer sales cycles, lower prices for our products and services, higher default rates among our channel partners, reduced unit sales and lower or no growth.

Because we depend on several third-party manufacturers to build our products, we are susceptible to manufacturing delays that could prevent us from shipping customer orders on time, if at all, and may result in the loss of sales and customers, and third-party manufacturing cost increases could result in lower gross margins.

We outsource the manufacturing of our security appliance products to a variety of contract manufacturing partners and original design manufacturing partners.

Our reliance on our third-party manufacturers reduces our control over the manufacturing process, exposing us to risks, including reduced control over quality assurance, product costs and product supply and timing. Any manufacturing disruption by our third-party manufacturers could impair our ability to fulfill orders. If we are unable to manage our relationships with these third-party manufacturers effectively, or if these third-party manufacturers experience delays, increased manufacturing lead-times, disruptions, capacity constraints or quality control problems in their manufacturing operations, or fail to meet our future requirements for timely delivery, our ability to ship products to our customers could be impaired and our business would be seriously harmed.

These manufacturers fulfill our supply requirements on the basis of individual purchase orders. We have no long-term contracts or arrangements with certain of our third-party manufacturers that guarantee capacity, the continuation of particular payment terms or the extension of credit limits. Accordingly, they are not obligated to continue to fulfill our supply requirements, and the prices we are charged for manufacturing services could be increased on short notice. If we are required to change third-party manufacturers, our ability to meet our scheduled product deliveries to our customers would be adversely affected, which could cause the loss of sales and existing or potential customers, delayed revenue or an increase in our costs which could adversely affect our gross margins. Our individual product lines are generally manufactured by only one manufacturing partner. Any production interruptions for any reason, such as a natural disaster, epidemic, capacity shortages, or quality problems, at one of our manufacturing partners would severely affect sales of our product lines manufactured by that manufacturing partner. Furthermore manufacturing cost increases for any reason could result in lower gross margins.

Our proprietary FortiASIC, which is the key to the performance of our appliances, is fabricated by contract manufacturers in foundries operated by United Microelectronics Corporation (“UMC”) and Taiwan Semiconductor Manufacturing Company Limited (“TSMC”). Faraday Technology Corporation (“Faraday”) (using UMC’s foundry), Kawasaki Microelectronics America, Inc. (“K-Micro”) (using TSMC’s foundry) and Renesas Electronics Corporation (“Renesas”) (using UMC’s foundry) manufacture our Application-Specific Integrated Circuits (“ASICs”) on a purchase order basis, and these foundries do not guarantee any capacity and could reject orders from Faraday, K-Micro or Renesas or try to increase pricing. Accordingly, the foundries are not obligated to continue to fulfill our supply requirements, and due to the long lead time that a new foundry would require, we could suffer temporary or long term inventory shortages of our FortiASIC as well as increased costs. Our suppliers may also prioritize orders by other companies that order higher volumes of products. If any of these suppliers materially delays its supply of ASICs or specific product models to us, or requires us to find an alternate supplier and we are not able to do so on a timely and reasonable basis, or if these foundries materially increase their prices for fabrication of our ASICs or specific product models, our business would be harmed.

In addition, our reliance on third-party manufacturers and foundries limits our control over environmental regulatory requirements such as the hazardous substance content of our products and therefore our ability to ensure compliance with the European Union’s (“EU”) Restriction of Hazardous Substances Directive (“RoHS”) and other similar laws. It also exposes us to the risk that certain minerals and metals that originated in the Democratic Republic of Congo or an adjoining country, known as “conflict minerals,” are contained within our products. Under the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, the SEC adopted new disclosure requirements for public companies using conflict minerals in their products. Under these rules, we are required to perform due diligence, disclose and report our efforts to prevent the sourcing of such conflict minerals. As a result of these new rules, we expect to incur additional costs to comply with the disclosure requirements, including costs related to determining the source of any of the conflict minerals that may be used in our products. Moreover, the implementation of these new requirements could adversely affect the sourcing, availability, and pricing of materials used in the manufacture of our products to the extent that there may be only a limited number of suppliers offering “conflict free” minerals that can be used in our products. There can be no assurance that we will be able to obtain such minerals in sufficient quantities or at competitive prices. We may also encounter customers who require that all of the components of our products be certified as conflict free. If we are not able to meet customer requirements, such customers may choose to not purchase our products, which could impact our sales and the value of portions of our inventory.

Because some of the key components in our products come from limited sources of supply, we are susceptible to supply shortages, long lead times for components, and supply changes, each of which could disrupt or delay our scheduled product deliveries to our customers, result in inventory shortage, and may result in the loss of sales and customers, and increased component costs may result in lower gross margins.

We and our contract manufacturers currently purchase several key parts and components used in the manufacture of our products from limited sources of supply. We are therefore subject to the risk of shortages and long lead times in the supply of these components and the risk that component suppliers discontinue or modify components used in our products. We have in the past experienced, and are currently experiencing, shortages and long lead times for certain components. Certain of our limited source components for particular appliances and suppliers of those components include: specific types of central processing units from Intel, Advanced Micro Devices, Inc., RMI/Netlogic Corporation, network chips from Broadcom Corporation, Marvell Technology Group Ltd. and Intel, and hard drives from Western Digital Technologies, Inc. The introduction by component suppliers of new versions of their products, particularly if not anticipated by us or our contract manufacturers, could require us to expend significant resources to incorporate these new components into our products. In addition, if these suppliers were to discontinue production of a necessary part or component, we would be required to expend significant resources and time in locating and integrating replacement parts or components from another vendor. Qualifying additional suppliers for limited source parts or components can be time-consuming and expensive.

Our manufacturing partners have experienced long lead times for the purchase of components incorporated into our products. Lead times for components may be adversely impacted by factors outside of our control, such as natural disasters and other factors. Our reliance on a limited number of suppliers involves several additional risks, including:

- a potential inability to obtain an adequate supply of required parts or components when required;
- financial or other difficulties faced by our suppliers;
- infringement or misappropriation of our intellectual property;
- price increases;
- failure of a component to meet environmental or other regulatory requirements;
- failure to meet delivery obligations in a timely fashion; and
- failure in component quality.

The occurrence of any of these would be disruptive to us and could seriously harm our business. Any interruption or delay in the supply of any of these parts or components, or the inability to obtain these parts or components from alternate sources at acceptable prices and within a reasonable amount of time, would harm our ability to meet our scheduled product deliveries to our distributors, resellers and end-customers. This could harm our relationships with our channel partners and end-customers and could cause delays in shipment of our products and adversely affect our results of operations. In addition, increased component costs could result in lower gross margins.

We are exposed to fluctuations in currency exchange rates, which could negatively affect our financial condition and results of operations.

A majority of our operating expenses is incurred outside the United States. These expenses are denominated in foreign currencies and are subject to fluctuations due to changes in foreign currency exchange rates, particularly changes in the Euro and Canadian dollar. Although we have been hedging currency exposures relating to certain balance sheet accounts and have periodically entered into cash flow hedges relating to certain operating expenses incurred outside of the United States, if we stop hedging against any of these risks or if our attempts to hedge against these currency exposures are not successful, our financial condition and results of operations could be adversely affected. In addition, our sales contracts are primarily denominated in U.S. dollars and therefore substantially all of our revenue is not subject to foreign currency risk. However, a strengthening of the U.S. dollar could increase the real cost of our products to our customers outside of the United States, which could also adversely affect our financial condition and results of operations.

We generate a majority of revenue from sales to distributors, resellers and end-customers outside of the United States, and we are therefore subject to a number of risks associated with international sales and operations.

We market and sell our products throughout the world and have established sales offices in many parts of the world. Therefore, we are subject to risks associated with having worldwide operations. We are also subject to a number of risks typically associated with international sales and operations, including:

- economic or political instability in foreign markets;
- greater difficulty in enforcing contracts, accounts receivable collection and longer collection periods;
- changes in regulatory requirements;
- difficulties and costs of staffing and managing foreign operations;
- the uncertainty of protection for intellectual property rights in some countries;

- costs of compliance with foreign policies, laws and regulations and the risks and costs of non-compliance with such policies, laws and regulations;

- costs of complying with U.S. laws and regulations for foreign operations, including the Foreign Corrupt Practices Act, import and export control laws, tariffs, trade barriers, and economic sanctions;

- other regulatory or contractual limitations on our ability to sell our products in certain foreign markets, and the risks and costs of non-compliance;

- heightened risks of unfair or corrupt business practices in certain geographies and of improper or fraudulent sales arrangements that may result in disruption in the sales team and may adversely impact financial results as compared to those already reported or the forecasted results and result in restatements of financial statements and irregularities in financial statements;

- the potential for political unrest, terrorism, hostilities or war;

- management communication and integration problems resulting from cultural differences and geographic dispersion; and

- multiple and possibly overlapping tax structures.

Product and service sales may be subject to foreign governmental regulations, which vary substantially from country to country. Further, we may be unable to keep up-to-date with changes in government requirements as they change from time to time. Failure to comply with these regulations could result in adverse effects to our business. In many foreign countries it is common for others to engage in business practices that are prohibited by our internal policies and procedures or U.S. regulations applicable to us. Although we implemented policies and procedures designed to ensure compliance with these laws and policies, there can be no assurance that all of our employees, contractors, channel partners and agents will comply with these laws and policies. Violations of laws or key control policies by our employees, contractors, channel partners or agents could result in delays in revenue recognition, financial reporting misstatements, fines, penalties, or the prohibition of the importation or exportation of our products and services and could have a material adverse effect on our business and results of operations.

We are subject to governmental export and import controls that could subject us to liability or impair our ability to compete in international markets.

Because we incorporate encryption technology into our products, certain of our products are subject to U.S. export controls and may be exported outside the U.S. only with the required export license or through an export license exception. If we were to fail to comply with U.S. export licensing, U.S. Customs regulations and import regulations, U.S. economic sanctions and other countries' import and export laws, we could be subject to substantial civil and criminal penalties, including fines for the company and incarceration for responsible employees and managers, and the possible loss of export or import privileges. In addition, if our channel partners fail to obtain appropriate import, export or re-export licenses or permits, we may also be adversely affected through reputational harm and penalties. Obtaining the necessary export license for a particular sale may be time-consuming and may result in the delay or loss of sales opportunities.

Furthermore, U.S. export control laws and economic sanctions prohibit the shipment of certain products to U.S. embargoed or sanctioned countries, governments and persons. Even though we take precautions to prevent our product from being shipped to U.S. sanctions targets, our products could be shipped to those targets by our channel partners, despite such precautions. Any such shipment could have negative consequences including government investigations and penalties and reputational harm. In addition, various countries regulate the import of certain encryption technology, including import permitting/licensing requirements, and have enacted laws that could limit our ability to distribute our products or could limit our customers' ability to implement our products in those countries. Changes in our products or changes in export and import regulations may create delays in the introduction of our products in international markets, prevent our customers with international operations from deploying our products globally or, in some cases, prevent the export or import of our products to certain countries, governments or persons altogether. Any change in export or import regulations, economic sanctions or related legislation, shift in the enforcement or scope of existing regulations, or change in the countries, governments, persons or technologies targeted by such regulations, could result in decreased use of our products by, or in our decreased ability to export or sell our products to, existing or potential customers with international operations. Any decreased use of our products or limitation on our ability to export or sell our products would likely adversely affect our business, financial condition and results of operations.

If we fail to comply with environmental requirements, our business, financial condition, operating results and reputation could be adversely affected.

We are subject to various environmental laws and regulations including laws governing the hazardous material content of our products and laws relating to the recycling of electrical and electronic equipment. The laws and regulations to which we are subject include the EU, RoHS and the EU Waste Electrical and Electronic Equipment Directive ("WEEE Directive") as well as the implementing legislation of the EU member states. Similar laws and regulations have been passed or are pending in China, South Korea, Norway and Japan and may be enacted in other regions, including in the United States, and we are, or may in the future be, subject to these laws and regulations.

The EU RoHS and the similar laws of other jurisdictions ban the use of certain hazardous materials such as lead, mercury and cadmium in the manufacture of electrical equipment, including our products. We have incurred costs to comply with these laws, including research and development costs, costs associated with assuring the supply of compliant components and costs associated with writing off noncompliant inventory. We expect to incur more of these costs in the future. With respect to the EU RoHS, we and our competitors rely on an exemption for lead in network infrastructure equipment. It is possible this exemption will be revoked in the near future. If this exemption is revoked, if there are other changes to these laws (or their interpretation) or if new similar laws are passed in other jurisdictions, we may be required to reengineer our products to use components compatible with these regulations. This reengineering and component substitution could result in additional costs to us or disrupt our operations or logistics.

The EU has also adopted the WEEE Directive, which requires electronic goods producers to be responsible for the collection, recycling and treatment of such products. Although currently our EU international channel partners are responsible for the requirements of this directive as the importer of record in most of the European countries in which we sell our products, changes in interpretation of the regulations may cause us to incur costs or have additional regulatory requirements in the future to meet in order to comply with this directive, or with any similar laws adopted in other jurisdictions.

Our failure to comply with these and future environmental rules and regulations could result in reduced sales of our products, increased costs, substantial product inventory write-offs, reputational damage, penalties and other sanctions.

A portion of our revenue is generated by sales to governmental entities, which are subject to a number of challenges and risks.

Sales to U.S. and foreign federal, state and local governmental agency end-customers have accounted for a portion of our revenue in past periods, and we may in the future increase sales to governmental entities. Sales to governmental entities are subject to a number of risks. Selling to governmental entities can be highly competitive, expensive and time consuming, often requiring significant upfront time and expense without any assurance that we will win a sale.

Government demand, sales, and payment for our products and services may be negatively impacted by numerous factors and requirements unique to selling to government agencies, such as:

- public sector budgetary cycles,
- funding authorizations and requirements unique to government agencies, with funding or purchasing reductions or delays adversely affecting public sector demand for our products,
- geopolitical matters, and
- rules and regulations applicable to certain government sales.

The rules and regulations applicable to government sales may also negatively impact sales to non-governmental entities. To date we have had limited traction in sales to U.S. federal government agencies, and any future sales to governmental entities is uncertain. All of our sales to governmental entities have been made indirectly through our distribution channel. Governmental entities may have contractual or other legal rights to terminate contracts with our distributors and resellers for convenience or due to a default, and any such termination may adversely impact our future results of operations. For example, if the distributor receives a significant portion of its revenue from sales to such governmental entity, the financial health of the distributor could be substantially harmed, which could negatively affect our future sales to such distributor. Governments routinely investigate and audit government contractors' administrative processes, and any unfavorable audit could result in the government refusing to continue buying our products and services, a reduction of revenue or fines or civil or criminal liability if the audit uncovers improper or illegal activities. Any such penalties could adversely impact our results of operations in a material way. Finally, purchases by the U.S. government may require certain products to be manufactured in the United States and other high cost manufacturing locations, and we may not manufacture all products in locations that meet the requirements of the U.S. government.

False detection of viruses or security breaches or false identification of spam or spyware could adversely affect our business.

Our antivirus and our intrusion prevention services may falsely detect viruses or other threats that do not actually exist. This risk is heightened by the inclusion of a “heuristics” feature in our products, which attempts to identify viruses and other threats not based on any known signatures but based on characteristics or anomalies that may indicate that a particular item is a threat. When our end-customers enable the heuristics feature in our products, the risk of falsely identifying viruses and other threats significantly increases. These false positives, while typical in the industry, may impair the perceived reliability of our products and may therefore adversely impact market acceptance of our products. Also, our anti-spam and anti-malware services may falsely identify emails or programs as unwanted spam or potentially unwanted programs, or alternatively fail to properly identify unwanted emails or programs, particularly as spam emails or spyware are often designed to circumvent anti-spam or spyware products. Parties whose emails or programs are blocked by our products may seek redress against us for labeling them as spammers or spyware, or for interfering with their business. In addition, false identification of emails or programs as unwanted spam or potentially unwanted programs may reduce the adoption of our products. If our system restricts important files or applications based on falsely identifying them as malware or some other item that should be restricted, this could adversely affect end-customers’ systems and cause material system failures. Any such false identification of important files or applications could result in negative publicity, loss of end-customers and sales, increased costs to remedy any problem, and costly litigation.

If our internal network system is compromised by computer hackers, public perception of our products and services will be harmed.

We will not succeed unless the marketplace is confident that we provide effective network security protection. Because we provide network security products, we may be a more attractive target for attacks by computer hackers. Although we have not experienced significant damages from unauthorized access by a third party of our internal network, if an actual or perceived breach of network security occurs in our internal systems it could adversely affect the market perception of our products and services. In addition, such a security breach could impair our ability to operate our business, including our ability to provide subscription and support services to our end-customers. If this happens, our revenue could decline and our business could suffer.

Our ability to sell our products is dependent on the quality of our technical support services, and our failure to offer high quality technical support services would have a material adverse effect on our sales and results of operations.

Once our products are deployed within our end-customers’ networks, our end-customers depend on our technical support services, as well as the support of our channel partners, to resolve any issues relating to our products. If we or our channel partners do not effectively assist our customers in deploying our products, succeed in helping our customers quickly resolve post-deployment issues, and provide effective ongoing support, our ability to sell additional products and services to existing customers would be adversely affected and our reputation with potential customers could be damaged. Many large end-customers, service provider and governmental entity end-customers require higher levels of support than smaller end-customers because of their more complex deployments. If we fail to meet the requirements of our larger end-customers, it may be more difficult to execute on our strategy to increase our penetration with enterprises, service providers and governmental entities.

As a result, our failure to maintain high quality support services would have a material adverse effect on our business, financial condition and results of operations.

Changes in our provision for income taxes or adverse outcomes resulting from examination of our income tax returns could adversely affect our results.

Our provision for income taxes is subject to volatility and could be adversely affected by several factors, many of which are outside of our control, including:

- earnings being lower than anticipated in countries that have lower tax rates and higher than anticipated in countries that have higher tax rates;

- changes in the valuation of our deferred tax assets and liabilities;
- expiration of, or lapses in the research and development tax credit laws;
- transfer pricing adjustments including the effect of acquisitions on our intercompany research and development and legal structure;
- an increase in non-deductible expenses for tax purposes, including certain stock-based compensation expense, write-offs of acquired in-process research and development, and impairment of goodwill;
- a decrease in the stock option exercises by our employees in some of our foreign subsidiaries that can cause an adverse transfer pricing adjustment;
- tax costs related to intercompany realignments;
- tax assessments resulting from income tax audits or any related tax interest or penalties that could significantly affect our income tax provision for the period in which the settlement takes place;
- a change in our decision to indefinitely reinvest foreign earnings;
- changes in accounting principles; or
- changes in tax laws and regulations including possible changes in the United States to the taxation of earnings of our foreign subsidiaries, and the deductibility of expenses attributable to foreign income, or the foreign tax credit rules, or changes to the U.S. income tax rate, which would necessitate a revaluation of our deferred tax assets and liabilities.

Significant judgment is required to determine the recognition and measurement attribute prescribed in the FASB standard. In addition, the standard applies to all income tax positions, including the potential recovery of previously paid taxes, which if settled unfavorably could adversely impact our provision for income taxes or additional paid-in capital. Further, as a result of certain of our ongoing employment and capital investment actions and commitments, our income in certain foreign countries is subject to reduced tax rates and in some cases is wholly exempt from tax. Our failure to meet these commitments could adversely impact our provision for income taxes. In addition, we are subject to the examination of our income tax returns by the IRS and other tax authorities. For example, the California Franchise Tax Board is examining our tax returns for 2010 and 2011. We regularly assess the likelihood of adverse outcomes resulting from these examinations to determine the adequacy of our provision for income taxes. There can be no assurance that the outcomes from these continuous examinations will not have an adverse effect on our results of operations.

Although we currently do not have a valuation allowance, we may in the future be required to establish one. We will continue to assess the need for a valuation allowance on the deferred tax asset by evaluating both positive and negative evidence that may exist.

Forecasting our estimated annual effective tax rate is complex and subject to uncertainty, and there may be material differences between our forecasted and actual tax rates.

Forecasts of our income tax position and effective tax rate are complex and subject to uncertainty because our income tax position for each year combines the effects of a mix of profits earned and losses incurred by us in various tax jurisdictions with a broad range of income tax rates, as well as changes in the valuation of deferred tax assets and liabilities, the impact of various accounting rules and changes to these rules and tax laws, the results of examinations by various tax authorities, and the impact of any acquisition, business combination or other reorganization or financing transaction. To forecast our global tax rate, we estimate our pre-tax profits and losses by jurisdiction and forecast our tax expense by jurisdiction. If the mix of profits and losses, our ability to use tax credits, or effective tax rates by jurisdiction is different than those estimated, our actual tax rate could be materially different than forecasted, which could have a material impact on our results of business, financial condition and results of operations.

As a multinational corporation, we conduct our business in many countries and are subject to taxation in many jurisdictions. The taxation of our business is subject to the application of multiple and sometimes conflicting tax laws and regulations as well as multinational tax conventions. Our effective tax rate is highly dependent upon the geographic distribution of our worldwide earnings or losses, the tax regulations and tax holidays in each geographic region, the availability of tax credits and carryforwards, and the effectiveness of our tax planning strategies. The application of tax laws and regulations is subject to legal and factual interpretation, judgment and uncertainty. Tax laws themselves are subject to change as a result of changes in fiscal policy, changes in legislation, and the evolution of regulations and court rulings. Consequently, taxing authorities may impose tax assessments or judgments against us that could materially impact our tax liability and/or our effective income tax rate.

In addition, we may be subject to examination of our income tax returns by the IRS and other tax authorities. If tax authorities challenge the relative mix of U.S. and international income, our future effective income tax rates could be adversely affected. While we regularly assess the likelihood of adverse outcomes from such examinations and the adequacy of our provision for income taxes, there can be no assurance that such provision is sufficient and that a determination by a tax authority will not have an adverse effect on our business, financial condition and results of operations.

Our inability to acquire and integrate other businesses, products or technologies could seriously harm our competitive position.

In order to remain competitive, we may seek to acquire additional businesses, products, or technologies and intellectual property, such as patents. If we identify an appropriate acquisition candidate, we may not be successful in negotiating the terms of the acquisition, financing the acquisition, or effectively integrating the acquired business, product, technology or intellectual property into our existing business and operations. We may have difficulty incorporating acquired technologies, intellectual property or products with our existing product lines and maintaining uniform standards, controls, procedures and policies. Our due diligence may fail to identify all of the problems, liabilities or other shortcomings or challenges of an acquired business, product or technology, including issues with intellectual property, product quality or product architecture, regulatory compliance practices, revenue recognition or other accounting practices or employee or customer issues, and we may not accurately forecast the financial impact of an acquisition. In addition, any acquisitions we are able to complete may be dilutive to revenue growth and earnings and may not result in any synergies or other benefits we had expected to achieve, which could result in write-offs that could be substantial. Acquisitions during a quarter may result in increased operating expenses and adversely affect our results of operations for that period or future periods compared to the results that we have previously forecasted or achieved. Further, completing a potential acquisition and integrating acquired businesses, products, technologies or intellectual property could significantly divert management time and resources.

Our business is subject to the risks of warranty claims, product returns, product liability and product defects.

Our products are very complex and, despite testing prior to their release, have contained and may contain undetected defects or errors, especially when first introduced or when new versions are released. Product errors have affected the performance of our products and could delay the development or release of new products or new versions of products, adversely affect our reputation and our end-customers' willingness to buy products from us, and adversely affect market acceptance or perception of our products. Any such errors or delays in releasing new products or new versions of products or allegations of unsatisfactory performance could cause us to lose revenue or market share, increase our service costs, cause us to incur substantial costs in redesigning the products, cause us to lose significant end-customers, subject us to liability for damages and divert our resources from other tasks, any one of which could materially and adversely affect our business, results of operations and financial condition. Our products must successfully interoperate with products from other vendors. As a result, when problems occur in a network, it may be difficult to identify the sources of these problems. The occurrence of hardware and software errors, whether or not caused by our products, could delay or reduce market acceptance of our products, and have an adverse effect on our business and financial performance, and any necessary revisions may cause us to incur significant expenses. The occurrence of any such problems could harm our business, financial condition and results of operations.

Although we have limitation of liability provisions in our standard terms and conditions of sale, they may not fully or effectively protect us from claims as a result of federal, state or local laws or ordinances or unfavorable judicial decisions in the United States or other countries. The sale and support of our products also entail the risk of product liability claims. We maintain insurance to protect against certain claims associated with the use of our products, but our insurance coverage may not adequately cover any claim asserted against us. In addition, even claims that ultimately are unsuccessful could result in our expenditure of funds in litigation and divert management's time and other resources.

Our business is subject to the risks of earthquakes, fire, power outages, floods and other catastrophic events, and to interruption by manmade problems such as civil unrest and terrorism.

A significant natural disaster, such as an earthquake, fire, a flood, or significant power outage could have a material adverse impact on our business, operating results and financial condition. Our corporate headquarters are located in the San Francisco Bay Area, a region known for seismic activity. In addition, natural disasters could affect our manufacturing vendors, suppliers or logistics providers' ability to perform services such as obtaining product components and manufacturing products on a timely basis and assisting with shipments on a timely basis. In the event our or our service providers' information technology systems or manufacturing or logistics abilities are hindered by any of the events discussed above, shipments could be delayed, resulting in us missing financial targets, such as revenue and shipment targets, for a particular quarter. In addition, regional instability, acts of terrorism and other geo-political unrest could cause disruptions in our business or the business of our manufacturers, logistics providers, partners, or end-customers or the economy as a whole. Given our typical concentration of sales at each quarter end, any disruption in the business of our manufacturers, logistics providers, partners or end-customers that impacts sales at the end of our quarter could have a significant adverse impact on our quarterly results. All of the aforementioned risks may be augmented if the disaster recovery plans for us and our suppliers prove to be inadequate. To the extent that any of the above results in delays or cancellations of customer orders, or the delay in the manufacture, deployment or shipment of our products, our business, financial condition and results of operations would be adversely affected.

Risks Related to Our Industry

The network security market is rapidly evolving and the complex technology incorporated in our products makes them difficult to develop. If we do not accurately predict, prepare for and respond promptly to technological and market developments and changing end-customer needs, our competitive position and prospects will be harmed.

The network security market is expected to continue to evolve rapidly. Moreover, many of our end-customers operate in markets characterized by rapidly changing technologies and business plans, which require them to add numerous network access points and adapt increasingly complex enterprise networks, incorporating a variety of hardware, software applications, operating systems and networking protocols. In addition, computer hackers and others who try to attack networks employ increasingly sophisticated techniques to gain access to and attack systems and networks. The technology in our products is especially complex because it needs to effectively identify and respond to new and increasingly sophisticated methods of attack, while minimizing the impact on network performance. Additionally, some of our new products and enhancements may require us to develop new hardware architectures and ASICs that involve complex, expensive and time consuming research and development processes. Although the market expects rapid introduction of new products or product enhancements to respond to new threats, the development of these products is difficult and the timetable for commercial release and availability is uncertain and there can be long time periods between releases and availability of new products. We have in the past and may in the future experience unanticipated delays in the availability of new products and services and fail to meet previously announced timetables for such availability. If we do not quickly respond to the rapidly changing and rigorous needs of our end-customers by developing and releasing and making available on a timely basis new products and services or enhancements that can respond adequately to new security threats, our competitive position and business prospects will be harmed.

Our URL database for our Web filtering service may fail to keep pace with the rapid growth of URLs and may not categorize websites in accordance with our end-customers' expectations.

The success of our Web filtering service depends on the breadth and accuracy of our URL database. Although our URL database currently catalogs millions of unique URLs, it contains only a portion of the URLs for all of the websites that are available on the Internet. In addition, the total number of URLs and software applications is growing rapidly, and we expect this rapid growth to continue in the future. Accordingly, we must identify and categorize content for our security risk categories at an extremely rapid rate. Our database and technologies may not be able to keep pace with the growth in the number of websites, especially the growing amount of content utilizing foreign languages and the increasing sophistication of malicious code and the delivery mechanisms associated with spyware, phishing and other hazards associated with the Internet. Further, the ongoing evolution of the Internet and computing environments will require us to continually improve the functionality, features and reliability of our Web filtering function. Any failure of our databases to keep pace with the rapid growth and technological change of the Internet could impair the market acceptance of our products, which in turn could harm our business, financial condition and results of operations.

In addition, our Web filtering service may not be successful in accurately categorizing Internet and application content to meet our end-customers' expectations. We rely upon a combination of automated filtering technology and human review to categorize websites and software applications in our proprietary databases. Our end-customers may not agree with our determinations that particular URLs should be included or not included in specific categories of our databases. In addition, it is possible that our filtering processes may place material that is objectionable or that presents a security risk in categories that are generally unrestricted by our customers' Internet and computer access policies, which could result in such material not being blocked from the network. Conversely, we may miscategorize websites such that access is denied to websites containing information that is important or valuable to our customers. Any miscategorization could result in customer dissatisfaction and harm our reputation. Any failure to effectively categorize and filter websites according to our end-customers' and channel partners' expectations could impair the growth of our business.

If our new products and product enhancements do not achieve sufficient market acceptance, our results of operations and competitive position will suffer.

We spend substantial amounts of time and money to research and develop new products and enhanced versions of our existing products to incorporate additional features, improved functionality or other enhancements in order to meet our customers' rapidly evolving demands for network security in our highly competitive industry. When we develop a new product or an enhanced version of an existing product, we typically incur expenses and expend resources upfront to market, promote and sell the new offering. Therefore, when we develop and introduce new or enhanced products, they must achieve high levels of market acceptance in order to justify the amount of our investment in developing and bringing them to market.

Our new products or product enhancements could fail to attain sufficient market acceptance for many reasons, including:

- delays in releasing our new products or enhancements to the market;
- failure to accurately predict market demand in terms of product functionality and to supply products that meet this demand in a timely fashion;
- failure of our sales force and partners to focus on selling new products;
- inability to interoperate effectively with the networks or applications of our prospective end-customers;
- inability to protect against new types of attacks or techniques used by hackers;
- actual or perceived defects, vulnerabilities, errors or failures;
- negative publicity about their performance or effectiveness;
- introduction or anticipated introduction of competing products by our competitors;
- poor business conditions for our end-customers, causing them to delay IT purchases;
- easing of regulatory requirements around security; and
- reluctance of customers to purchase products incorporating open source software.

If our new products or enhancements do not achieve adequate acceptance in the market, our competitive position will be impaired, our revenue will be diminished and the effect on our operating results may be particularly acute because of the significant research, development, marketing, sales and other expenses we incurred in connection with the new product or enhancement.

Unless we continue to develop better market awareness of our company and our products, our revenue may not continue to grow.

Increased market awareness of our capabilities and products is essential to our continued growth and our success in all of our markets, particularly for the large enterprise, service provider and governmental entities markets. We have historically had relatively low spending on certain marketing activities, and, if our marketing programs are not successful in creating market awareness of our company and products, our business, financial condition and results of operations will be adversely affected, and we will not be able to achieve sustained growth.

Demand for UTM products may be limited by market perception that UTM products are inferior to network security solutions from multiple vendors.

Sales of most of our products depend on increased demand for UTM products. If the UTM market fails to grow as we anticipate, our business will be seriously harmed. Target customers may view UTM “all-in-one” solutions as inferior to security solutions from multiple vendors because of, among other things, their perception that UTM products provide security functions from only a single vendor and do not allow users to choose “best-of-breed” defenses from among the wide range of dedicated security applications available. Target customers might also perceive that, by combining multiple security functions into a single platform, UTM solutions create a “single point of failure” in their networks, which means that an error, vulnerability or failure of the UTM product may place the entire network at risk. In addition, the market perception that UTM solutions may be suitable only for small and medium sized businesses because UTM lacks the performance capabilities and functionality of other solutions may harm our sales to large enterprise, service provider, and governmental entity end-customers. If the foregoing concerns and perceptions become prevalent, even if there is no factual basis for these concerns and perceptions, or if other issues arise with the UTM market in general, demand for UTM products could be severely limited, which would limit our growth and harm our business, financial condition and results of operations. Further, a successful and publicized targeted attack against us or another well known UTM vendor exposing a “single point of failure” could significantly increase these concerns and perceptions and may harm our business and results of operations.

We face intense competition in our market and we may lack sufficient financial or other resources to maintain or improve our competitive position.

The market for network security products is intensely competitive, and we expect competition to intensify in the future. Our competitors include networking companies such as Cisco and Juniper, security vendors such as Check Point, McAfee (acquired by Intel), Sourcefire (acquired by Cisco), Stonesoft (acquired by McAfee), SonicWALL (acquired by Dell), Blue Coat, and Palo Alto Networks, and other point solution security vendors.

Many of our existing and potential competitors enjoy substantial competitive advantages such as:

- greater name recognition and longer operating histories;
- larger sales and marketing budgets and resources;
- broader distribution and established relationships with distribution partners and end-customers;
- access to larger customer bases;
- greater customer support resources;
- greater resources to make acquisitions;
- lower labor and development costs; and
- substantially greater financial, technical and other resources.

In addition, some of our larger competitors have substantially broader product offerings and leverage their relationships based on other products or incorporate functionality into existing products in a manner that discourages users from purchasing our products. These larger competitors often have broader product lines and market focus and are in a better position to withstand any significant reduction in capital spending by end-customers in these markets. Therefore, these competitors will not be as susceptible to downturns in a particular market. Also, many of our smaller competitors that specialize in providing protection from a single type of network security threat are often able to deliver these specialized network security products to the market more quickly than we can. Some of our smaller competitors are using third-party chips designed to accelerate performance. Conditions in our markets could change rapidly and significantly as a result of technological advancements or continuing market consolidation. Our current and potential competitors may also establish cooperative relationships among themselves or with third parties that may further enhance their resources. In addition, current or potential competitors may be acquired by third parties with greater available resources, such as Juniper’s acquisition of NetScreen Technologies Inc., Intel’s acquisition of McAfee, McAfee's acquisition of Stonesoft, Check Point’s acquisition of Nokia Corporations’ security appliance business and Dell’s acquisition of SonicWALL. As a result of such acquisitions, our current or potential competitors might be able to adapt more quickly to new technologies and customer needs, devote greater resources to the promotion or sale of their products and services, initiate or withstand substantial price competition, take advantage of acquisition or other opportunities more readily or develop and expand their product and service offerings more quickly than we do. In addition, our competitors may bundle products and services competitive with ours with other products and services. Customers may accept these bundled products and services rather than separately purchasing our products and services. Due to budget constraints or economic downturns, organizations may be more willing to incrementally add solutions to their existing network security infrastructure from competitors than to replace it with our solutions. These competitive pressures in our market or our failure to compete effectively may result in price reductions, fewer customer orders, reduced revenue and gross margins and loss of market share.

If functionality similar to that offered by our products is incorporated into existing network infrastructure products, organizations may decide against adding our appliances to their network, which would have an adverse effect on our business.

Large, well-established providers of networking equipment such as Cisco and Juniper offer, and may continue to introduce, network security features that compete with our products, either in stand-alone security products or as additional features in their network infrastructure products. The inclusion of, or the announcement of an intent to include, functionality perceived to be similar to that offered by our security solutions in networking products that are already generally accepted as necessary components of network architecture may have an adverse effect on our ability to market and sell our products. Furthermore, even if the functionality offered by network infrastructure providers is more limited than our products, a significant number of customers may elect to accept such limited functionality in lieu of adding appliances from an additional vendor such as us. Many organizations have invested substantial personnel and financial resources to design and operate their networks and have established deep relationships with other providers of networking products, which may make them reluctant to add new components to their networks, particularly from other vendors such as us. In addition, an organization’s existing vendors or new vendors with a broad product offering may be able to offer concessions that we are not able to match because we currently offer only network security products and have fewer resources than many of our competitors. If organizations are reluctant to add additional network infrastructure from new vendors or otherwise decide to work with their existing vendors, our business, financial condition and results of operations will be adversely affected.

Risks Related to Intellectual Property

Our proprietary rights may be difficult to enforce, which could enable others to copy or use aspects of our products without compensating us.

We rely primarily on patent, trademark, copyright and trade secrets laws, confidentiality procedures and contractual provisions to protect our technology. Valid patents may not issue from our pending applications, and the claims eventually allowed on any patents may not be sufficiently broad to protect our technology or products. Any issued patents may be challenged, invalidated or circumvented, and any rights granted under these patents may not actually provide adequate defensive protection or competitive advantages to us. Patent applications in the United States are typically not published until at least 18 months after filing, or, in some cases, not at all, and publications of discoveries in industry-related literature lag behind actual discoveries. We cannot be certain that we were the first to make the inventions claimed in our pending patent applications or that we were the first to file for patent protection. Additionally, the process of obtaining patent protection is expensive and time-consuming, and we may not be able to prosecute all necessary or desirable patent applications at a reasonable cost or in a timely manner. In addition, recent changes to the patent laws in the United States may bring into question the validity of certain software patents and may make it more difficult and costly to prosecute patent applications. As a result, we may not be able to obtain adequate patent protection or effectively enforce our issued patents.

Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy aspects of our products or obtain and use information that we regard as proprietary. We generally enter into confidentiality or license agreements with our employees, consultants, vendors and customers, and generally limit access to and distribution of our proprietary information. However, we cannot assure you that the steps taken by us will prevent misappropriation of our technology. Policing unauthorized use of our technology or products is difficult. In addition, the laws of some foreign countries do not protect our proprietary rights to as great an extent as the laws of the United States, and many foreign countries do not enforce these laws as diligently as government agencies and private parties in the United States. From time to time, legal action by us may be necessary to enforce our patents and other intellectual property rights, to protect our trade secrets, to determine the validity and scope of the proprietary rights of others or to defend against claims of infringement or invalidity. Such litigation could result in substantial costs and diversion of resources and could negatively affect our business, operating results and financial condition. If we are unable to protect our proprietary rights (including aspects of our software and products protected other than by patent rights), we may find ourselves at a competitive disadvantage to others who need not incur the additional expense, time and effort required to create the innovative products that have enabled us to be successful to date.

Our products contain third-party open source software components, and failure to comply with the terms of the underlying open source software licenses could restrict our ability to sell our products.

Our products contain software modules licensed to us by third-party authors under “open source” licenses, including the GNU Public License, the GNU Lesser Public License (LGPL), the BSD License, the Apache License and others. From time to time, there have been claims against companies that distribute or use open source software in their products and services, asserting that open source software infringes the claimants’ intellectual property rights. We could be subject to suits by parties claiming infringement of intellectual property rights in what we believe to be licensed open source software. Use and distribution of open source software may entail greater risks than use of third-party commercial software, as open source licensors generally do not provide warranties or other contractual protections regarding infringement claims or the quality of the code. Some open source licenses contain requirements that we make available source code for modifications or derivative works we create based upon the type of open source software we use. If we combine our proprietary software with open source software in a certain manner, we could, under certain open source licenses, be required to release the source code of our proprietary software to the public. This would allow our competitors to create similar products with lower development effort and time and ultimately could result in a loss of product sales for us.

Although we monitor our use of open source software to avoid subjecting our products to conditions we do not intend, the terms of many open source licenses have not been interpreted by United States courts, and there is a risk that these licenses could be construed in a way that could impose unanticipated conditions or restrictions on our ability to commercialize our products. In this event, we could be required to seek licenses from third parties to continue offering our products, to make generally available, in source code form, our proprietary code, to re-engineer our products, or to discontinue the sale of our products if re-engineering could not be accomplished on a timely basis, any of which could adversely affect our business, operating results and financial condition.

Claims by others that we infringe their proprietary technology or other litigation matters could harm our business.

Patent and other intellectual property disputes are common in the network security industry. Third parties have asserted and may in the future assert claims of infringement of intellectual property rights against us. They may also assert such claims against our end-customers or channel partners whom we typically indemnify against claims that our products infringe the intellectual property rights of third parties. As the number of products and competitors in our market increases and overlaps occur, infringement claims may increase. Any claim of infringement by a third-party, even those without merit, could cause us to incur substantial costs defending against the claim and could distract our management from our business. In addition, litigation may involve patent holding companies or other adverse patent owners who have no relevant product revenue and against whom our own patents may therefore provide little or no deterrence or protection.

Although third parties may offer a license to their technology, the terms of any offered license may not be acceptable, and the failure to obtain a license or the costs associated with any license could cause our business, financial condition and results of operations to be materially and adversely affected. In addition, some licenses may be non-exclusive, and therefore our competitors may have access to the same technology licensed to us.

Alternatively, we may be required to develop non-infringing technology, which could require significant time, effort and expense and may ultimately not be successful. Furthermore, a successful claimant could secure a judgment or we may agree to a settlement that prevents us from distributing certain products or performing certain services or that requires us to pay substantial damages (including treble damages if we are found to have willfully infringed such claimant’s patents or copyrights), royalties or other fees. Any of these events could seriously harm our business, financial condition and results of operations.

From time to time we are subject to lawsuits claiming patent infringement, and there are lawsuits claiming patent infringement currently pending, as discussed in the section entitled “Legal Proceedings” in Part II, Item 1 of this Quarterly Report on Form 10-Q. We are also subject to other litigation in addition to patent infringement claims, such as employment-related litigation and disputes, general commercial litigation, and other forms of litigation and disputes, including stockholder litigation. If we are unsuccessful in defending any such claims, our operating results and financial condition and results may be materially and adversely affected. For example, we may be required to pay substantial damages and could be prevented from selling certain of our products. Litigation, with or without merit, could negatively impact our business, reputation, and sales in a material fashion. In addition to the lawsuits described in “Legal Proceedings,” several other non-practicing patent holding companies have sent us letters proposing that we license certain of their patents, and given this and the proliferation of lawsuits in our industry and other similar industries by both non-practicing entities and operating entities, we expect that we will be sued for patent infringement in the future, regardless of the merits of any such lawsuits. The cost to defend such lawsuits and any adverse result in such lawsuits could have a material adverse effect on our results of operations and financial condition.

We rely on the availability of third-party licenses.

Many of our products include software or other intellectual property licensed from third parties. It may be necessary in the future to renew licenses relating to various aspects of these products or to seek new licenses for existing or new products. There can be no assurance that the necessary licenses would be available on acceptable terms, if at all. The inability to obtain certain licenses or other rights or to obtain such licenses or rights on favorable terms, or the need to engage in litigation regarding these matters, could result in delays in product releases until equivalent technology can be identified, licensed or developed, if at all, and integrated into our products and may have a material adverse effect on our business, operating results, and financial condition. Moreover, the inclusion in our products of software or other intellectual property licensed from third parties on a nonexclusive basis could limit our ability to differentiate our products from those of our competitors.

Risks Related to Ownership of our Common Stock

As a public company, we are subject to compliance initiatives that will require substantial time from our management and result in significantly increased costs that may adversely affect our operating results and financial condition.

The Sarbanes-Oxley Act of 2002, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, as well as other rules implemented by the SEC and The NASDAQ Stock Market, impose various requirements on public companies, including requiring changes in corporate governance practices. These and proposed corporate governance laws and regulations under consideration may further increase our compliance costs. If compliance with these various legal and regulatory requirements diverts our management’s attention from other business concerns, it could have a material adverse effect on our business, financial condition and results of operations. The Sarbanes-Oxley Act requires, among other things, that we assess the effectiveness of our internal control over financial reporting annually and disclosure controls and procedures quarterly. Although our most recent assessment, testing and evaluation resulted in our conclusion that as of December 31, 2012, our internal controls over financial reporting were effective, we cannot predict the outcome of our testing in 2013 or future periods. If our internal controls or disclosure controls are ineffective in future periods, our business and reputation could be harmed. We may incur additional expenses and commitment of management’s time in connection with further evaluations, both of which could materially increase our operating expenses and accordingly reduce our operating results.

Changes in financial accounting standards may cause adverse unexpected fluctuations and affect our reported results of operations.

A change in accounting standards or practices and varying interpretations of existing accounting pronouncements, such as changes to standards related to the increased use of fair value measure, financial instruments, and the potential requirement that U.S. registrants prepare financial statements in accordance with International Financial Reporting Standards, could have a significant effect on our reported financial results or the way we conduct our business. If we do not ensure that our systems and processes are aligned with the new standards, we could encounter difficulties generating quarterly and annual financial statements in a timely manner, which would have an adverse effect on our business and our ability to meet our reporting obligations.

If securities or industry analysts stop publishing research or publish inaccurate or unfavorable research about our business, our stock price and trading volume could decline.

The trading market for our common stock will depend in part on the research and reports that securities or industry analysts publish about us or our business. If we do not maintain adequate research coverage or if one or more of the analysts who covers us downgrades our stock or publishes inaccurate or unfavorable research about our business, our stock price would likely decline. If one or more of these analysts ceases coverage of our company or fails to publish reports on us regularly, demand for our stock could decrease, which could cause our stock price and trading volume to decline.

The trading price of our common stock is likely to be volatile.

The market price of our common stock is subject to wide fluctuations in response to, among other things, the risk factors described in this periodic report, and other factors such as rumors or fluctuations in the valuation of companies perceived by investors to be comparable to us. For example, in the six months ended June 30, 2013, the closing price of our common stock ranged from $16.53 to $25.00.

Furthermore, the stock markets have experienced price and volume fluctuations that have affected and continue to affect the market prices of equity securities of many companies. These fluctuations often have been unrelated or disproportionate to the operating performance of those companies. These broad market and industry fluctuations, as well as general economic, political, and market conditions, such as recessions, interest rate changes or international currency fluctuations, may negatively affect the market price of our common stock.

In the past, many companies that have experienced volatility in the market price of their stock have been subject to securities class action litigation. We may be the target of this type of litigation in the future. Securities litigation against us could result in substantial costs and divert our management's attention from other business concerns, which could seriously harm our business.

Anti-takeover provisions contained in our certificate of incorporation and bylaws, as well as provisions of Delaware law, could impair a takeover attempt.

Our certificate of incorporation, bylaws and Delaware law contain provisions that could have the effect of rendering more difficult, delaying or preventing an acquisition deemed undesirable by our board of directors. Our corporate governance documents include provisions:

- providing for a classified board of directors whose members serve staggered three-year terms;
- authorizing "blank check" preferred stock, which could be issued by the board without stockholder approval and may contain voting, liquidation, dividend and other rights superior to our common stock;
- limiting the liability of, and providing indemnification to, our directors and officers;
- limiting the ability of our stockholders to call and bring business before special meetings;
- requiring advance notice of stockholder proposals for business to be conducted at meetings of our stockholders and for nominations of candidates for election to our board of directors;
- controlling the procedures for the conduct and scheduling of board and stockholder meetings; and
- providing the board of directors with the express power to postpone previously scheduled annual meetings and to cancel previously scheduled special meetings.

These provisions, alone or together, could delay or prevent hostile takeovers and changes in control or changes in our management.

As a Delaware corporation, we are also subject to provisions of Delaware law, including Section 203 of the Delaware General Corporation law, which prevents some stockholders holding more than 15% of our outstanding common stock from engaging in certain business combinations without approval of the holders of a substantial majority of all of our outstanding common stock.

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

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

Not applicable.

ITEM 3. Defaults Upon Senior Securities

Not applicable.

ITEM 4. Mine Safety Disclosures

Not applicable.

ITEM 5. Other Information

None.

ITEM 6. Exhibits

The exhibits listed in the accompanying Exhibit Index are filed or incorporated by reference as part of this Quarterly Report on Form 10-Q.

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.

Date: August 6, 2013

FORTINET, INC.

By: /s/ AHMED RUBAIE

Ahmed Rubaie
Chief Financial Officer and Chief Operating Officer (Principal Financial and Accounting Officer) (Duly Authorized Officer)

EXHIBIT INDEX

Exhibit Number	Description	Incorporated by reference herein		
		Form	Date	Exhibit Number
10.1†	Offer Letter, dated as of April 16, 2013, between Registrant and Ahmed Rubaie	Current report on Form 8-K (File No. 001-34511)	April 19, 2013	99.1
10.2 †	Change of Control Severance Agreement, dated as of April 16, 2013, between Registrant and Ahmed Rubaie	Current Report on Form 8-K (File No. 001-34511)	April 19, 2013	99.2
31.1*	Certification of Chief Executive Officer pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002			
31.2*	Certification of Chief Financial Officer pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002			
32.1*	Certifications of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002			
99.1†*	2009 Equity Incentive Plan Performance Stock Unit Award Agreement			
101.SCH*	XBRL Taxonomy Extension Schema Document			
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document			
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document			
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document			
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document			
101.INS*	XBRL Instance Document			

† Indicates management compensatory plan, contract or arrangement.

* Filed herewith.

Exhibit 31.1

CERTIFICATION

I, Ken Xie, certify that:

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

Date: August 6, 2013

/s/ Ken Xie

Ken Xie

President, Chief Executive Officer and Chairman of the Board of Directors
(Principal Executive Officer)

Exhibit 31.2

CERTIFICATION

I, Ahmed Rubaie, certify that:

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

Date: August 6, 2013

/s/ Ahmed Rubaie

Ahmed Rubaie

Chief Financial Officer and Chief Operating Officer
(Principal Financial Officer)

Exhibit 32.1

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

I, Ken Xie, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report on Form 10-Q of Fortinet, Inc. for the quarterly period ended June 30, 2013 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and that information contained in this Quarterly Report on Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of Fortinet, Inc.

Date:	August 6, 2013	By:	
		Name:	Ken Xie
		Title:	President, Chief Executive Officer and Chairman of the Board of Directors (Principal Executive Officer)

I, Ahmed Rubaie, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report on Form 10-Q of Fortinet, Inc. for the quarterly period ended June 30, 2013 fully complies with the requirements of Section 13(a) or 15(d) of the Exchange Act and the information contained in this Quarterly Report on Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of Fortinet, Inc.

Date:	August 6, 2013	By:	/s/ Ahmed Rubaie
		Name:	Ahmed Rubaie
		Title:	Chief Financial Officer and Chief Operating Officer (Principle Financial Officer)

This certification is being furnished pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and will not be deemed “filed” for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section. This certification will not be incorporated by reference into any filing under the Securities Act of 1933, as amended, or the Exchange Act, except as shall be expressly set forth by specific reference in such a filing.

FORTINET, INC.

2009 EQUITY INCENTIVE PLAN

PERFORMANCE STOCK UNIT AWARD AGREEMENT

Unless otherwise defined herein, the terms defined in the Fortinet, Inc. 2009 Equity Incentive Plan (the "Plan") will have the same defined meanings in this Performance Stock Unit Award Agreement (the "Award Agreement").

I. **NOTICE OF PERFORMANCE STOCK UNIT GRANT**

Participant Name:

Address:

You have been granted the right to receive an Award of Performance Stock Units, the vesting of which is based on the attainment of performance goals related to the Total Shareholder Return of the Company ("PSUs"), subject to the terms and conditions of the Plan, the Fortinet, Inc. Cash and Equity Incentive Plan (the "Performance Award Plan" and, collectively with the Plan, the "Plans") and this Award Agreement, as follows:

Grant Number

Date of Grant

Performance Period Start Date

Target Number of PSUs:

For Two-Year Performance Period

For Three-Year Performance Period

Total Target Number

Vesting Conditions:

Subject to any acceleration provisions contained in the Plans or in this Award Agreement, any Earned PSUs (as defined in the Performance Goal and Pay-Out Matrix that is attached hereto as Exhibit B) for the Two-Year Performance Period will vest on the first business day following the end of the Two-Year Performance Period and any Earned PSUs for the Three-Year Performance Period will vest on the first business day following the end of the Three-Year Performance Period, provided Participant remains a Service Provider from the Date of Grant through the last day of the respective Performance Period.

As soon as reasonably practicable after the completion of each Performance Period, the Administrator shall determine the actual level of attainment of the performance goal (the "Performance Goal") which determines the number of Earned PSUs, if any, provided, however, that in the case of PSUs intended to constitute "qualified performance-based compensation," as described in Section 162(m)(4)(C) of the Code ("Qualified Performance-Based Compensation"), the determination of the level of attainment of the Performance Goal shall be certified in writing in accordance with the requirements of Section 162(m) of the Code by the Administrator, which shall be comprised of "outside directors" within the meaning of Section 162(m) of the Code. On the basis of the determination or certified level of attainment of the Performance Goal, the number of PSUs that are eligible to vest shall be calculated. In the case of PSUs that are intended to constitute Qualified Performance-Based Compensation, the Administrator may not increase the number of PSUs that may be eligible to vest to a number that is greater than the number of PSUs determined in accordance with the foregoing sentence, but it retains the sole discretion to reduce the number of PSUs that would otherwise be eligible to vest based on the attainment level of the Performance Goal. For PSUs that are intended to constitute Qualified Performance-Based Compensation, the Performance Goal may not be adjusted except as specified in Exhibit B in accordance with the requirements of Section 162(m) of the Code. For PSUs that are not intended to constitute Qualified Performance-Based Compensation, the Administrator may make such adjustment to the Performance Goal as the Administrator in its sole discretion deems appropriate.

Except as otherwise provided in the Plans or in this Award Agreement, in the event Participant ceases to be a Service Provider for any or no reason before Participant vests in the PSUs, the PSUs and Participant's right to acquire any Shares hereunder will immediately terminate.

By Participant's signature and the signature of the representative of the Company on the signature page that follows, Participant and the Company agree that this Award of PSUs is granted under and governed by the terms and conditions of the Plans and this Award Agreement, including the Terms and Conditions of Performance Stock Unit Grant, attached hereto as Exhibit A, the Performance Goal and Pay-Out Matrix attached hereto as Exhibit B and the Addendum with additional country-specific terms and conditions (the "Addendum") attached hereto as Exhibit C, all of which are made a part of this Award Agreement. Participant has reviewed the Plans and this Award Agreement in their entirety, has had an opportunity to obtain the advice of counsel prior to accepting this Award Agreement and fully understands all provisions of the Plans and Award Agreement. Participant hereby agrees to accept as binding, conclusive and final all decisions or interpretations of the Administrator upon any questions relating to the Plans and Award Agreement. Participant further agrees to notify the Company upon any change in the residence address indicated below.

[Signature page follows]

PARTICIPANT:	FORTINET, INC.
Signature	By
Print Name	Title

Residence Address:

EXHIBIT A

TERMS AND CONDITIONS OF PERFORMANCE STOCK UNIT GRANT

1. Grant. The Company hereby grants to the individual named in the Notice of Grant attached as Part I of this Award Agreement (the "Participant") under the Plans an Award of PSUs, the vesting of which is based on the attainment of the Performance Goal set forth in the Performance Goal and Pay-Out Matrix (attached as Exhibit B), subject to all of the terms and conditions in this Award Agreement and the Plans, which are incorporated herein by reference. Capitalized terms not defined herein shall have the meanings ascribed to such terms in the Notice of Grant and the Plans.

If Participant is or may be a "covered employee" (within the meaning of Section 162(m) of the Code, and the regulations promulgated thereunder), the PSUs are intended to constitute Qualified Performance-Based Compensation.

Subject to Section 19 of the Plan, in the event of a conflict between the terms and conditions of the Plans and the terms and conditions of this Award Agreement, the terms and conditions of the Plans will prevail; provided, however, that to the extent the PSUs are intended to constitute Qualified Performance-Based Compensation, the provisions of the Performance Award Plan will prevail to the extent necessary to ensure that the PSUs will be treated as Qualified Performance-Based Compensation.

2. Company's Obligation to Pay. Unless and until the PSUs will have vested in the manner set forth in Section 3, Participant will have no right to payment of any such PSUs. Prior to actual payment of any vested PSUs, such PSU will represent an unsecured obligation of the Company, payable (if at all) only from the general assets of the Company. Any PSUs that vest in accordance with Sections 3 or 4 will be paid to Participant (or in the event of Participant's death, to his or her estate) in whole Shares, subject to Participant satisfying any Tax-Related Items as defined and as set forth in Section 8. Subject to the provisions of Section 4, such vested PSUs will be paid in Shares as soon as practicable after vesting, but in each such case within the period ending no later than the date that is two and one-half (2½) months from the end of the Company's tax year that includes the vesting date.

3. Vesting Conditions. Except as provided in Section 4, and subject to Section 6, the PSUs awarded by this Award Agreement will vest in accordance with the vesting provisions set forth in the Notice of Grant. PSUs scheduled to vest on a certain date or upon the occurrence of a certain condition will not vest in Participant in accordance with any of the provisions of this Award Agreement, unless Participant will have been continuously a Service Provider from the Date of Grant until the date such vesting occurs, as further described in Section 6.

4. Administrator Discretion. The Administrator, in its discretion, may accelerate the vesting of the balance, or some lesser portion of the balance, of the unvested PSUs at any time, subject to the terms of the Plans, provided, however, that the vesting of PSUs that are intended to constitute Qualified Performance-Based Compensation shall not be accelerated to the extent that any such vesting acceleration would cause the PSUs to fail to constitute Qualified Performance-Based Compensation. If so accelerated, such PSUs will be considered as having vested as of the date specified by the Administrator.

Notwithstanding anything in the Plans or this Award Agreement to the contrary, if the vesting and payment of the balance, or some lesser portion of the balance, of the PSUs that constitute nonqualified deferred compensation subject to Section 409A is accelerated in connection with Participant's termination as a Service Provider (provided that such termination is a "separation from service" within the meaning of Section 409A, as determined by the Company) other than due to death**,** and if (x) Participant is a U.S. taxpayer and "specified employee" within the meaning of Section 409A at the time of such termination as a Service Provider and (y) the payment of such accelerated PSUs will result in the imposition of additional tax under Section 409A if paid to Participant on or within the six (6) month period following Participant's termination as a Service Provider, then the payment of such accelerated PSUs will not be made until the date six (6) months and one (1) day following the date of Participant's termination as a Service Provider, unless Participant dies following his or her termination as a Service Provider, in which case, the PSUs will be paid in Shares to the Participant's estate not more than ninety (90) days following his or her death. It is the intent of this Award Agreement to comply with the requirements of Section 409A so that none of the PSUs provided under this Award Agreement or Shares issuable thereunder will be subject to the additional tax imposed under Section 409A, and any ambiguities herein will be interpreted to so comply. For purposes of this Award Agreement, "Section 409A" means Section 409A of the Code, and any proposed, temporary or final Treasury Regulations and Internal Revenue Service guidance thereunder, as each may be amended from time to time. Section 409A applies to and is relevant only for Participants who are U.S. taxpayers.

5. Dividend Equivalents. Participant shall be entitled to receive the equivalent value (in cash or Shares) of any dividends paid on each Share for each Earned PSU (as such term is defined in Exhibit B) (a "Dividend Equivalent"). Any Dividend Equivalent that becomes payable shall be paid at the same time that the underlying PSU is paid pursuant to Section 2.

6. Forfeiture upon Termination of Status as a Service Provider. Except as otherwise provided in the Plans or this Award Agreement, the balance of the PSUs that have not vested as of the time of Participant's termination as a Service Provider, for any or no reason and Participant's right to acquire any Shares hereunder, will immediately terminate upon Participant's termination as a Service Provider. For purposes of the PSUs, Participant's status as a Service Provider will be considered terminated as of the date Participant is no longer actively providing services to the Company or any Parent or Subsidiary (regardless of the reason for such termination and whether or not later to be found invalid or in breach of employment laws in the jurisdiction where Participant is employed or rendering services or the terms of Participant's employment or service agreement, if any), and Participant's right to vest in the PSUs under the Plans, if any, will terminate as of such date and will not be extended by any notice period (e.g., Participant's period of service would not include any contractual notice period or any period of "garden leave" or similar period mandated under employment laws in the jurisdiction where Participant is employed or rendering services or the terms of Participant's employment or service agreement, if any); the Administrator shall have the exclusive discretion to determine when Participant is no longer actively providing services for purposes of the PSU grant (including whether Participant may still be considered to be a Service Provider while on a leave of absence).

7. Death of Participant. Any distribution or delivery to be made to Participant under this Award Agreement will, if Participant was a U.S. resident and is then deceased, be made to Participant's designated beneficiary, or if no beneficiary survives Participant, the administrator or executor of Participant's estate. Any distribution or delivery to be made to Participant under this Award Agreement will, if Participant was not a U.S. resident and is then deceased, be made to the administrator or executor of Participant's estate. Any such transferee must furnish the Company with (a) written notice of his or her status as transferee, and (b) evidence satisfactory to the Company to establish the validity of the transfer and compliance with any laws or regulations pertaining to said transfer.

8. Withholding of Taxes. Participant acknowledges that, regardless of any action taken by the Company or, if different, the Parent or Subsidiary retaining or employing Participant (the "Employer") the ultimate liability for all income tax, social insurance, payroll tax, fringe benefits tax, payment on account or other tax-related items related to Participant's participation in the Plans and legally applicable to Participant ("Tax-Related Items"), is and remains Participant's responsibility and may exceed the amount actually withheld by the Company or the Employer. Participant further acknowledges that the Company and/or the Employer (1) make no representations or undertakings regarding the treatment of any Tax-Related Items in connection with any aspect of the PSUs, including, but not limited to, the grant, vesting or settlement of the PSUs, the subsequent sale of Shares acquired pursuant to such settlement and the receipt of any dividends or dividend equivalents; and (2) do not commit to and are under no obligation to structure the terms of the grant or any aspect of the PSUs to reduce or eliminate Participant's liability for Tax-Related Items or achieve any particular tax result. Further, if Participant is subject to Tax-Related Items in more than one jurisdiction between the Date of Grant and the date of any relevant taxable or tax withholding event, as applicable, Participant acknowledges that the Company and/or the Employer (or former employer, as applicable) may be required to withhold or account for Tax-Related Items in more than one jurisdiction.

Prior to any relevant taxable or tax withholding event, as applicable, Participant agrees to make adequate arrangements satisfactory to the Company and/or the Employer to satisfy all Tax-Related Items. Notwithstanding any contrary provision of this Award Agreement, no certificate representing the Shares will be issued to Participant, unless and until satisfactory arrangements (as determined by the Administrator) will have been made by Participant with respect to the payment of Tax-Related Items which the Company determines must be withheld with respect to such Shares.

The Administrator, in its sole discretion and pursuant to such procedures as it may specify from time to time, may satisfy any Tax-Related Items, in whole or in part (without limitation) by (a) withholding from Participant's wages or other cash compensation payable to Participant by the Company and/or any Parent or Subsidiary, (b) withhold otherwise deliverable Shares, or (c) selling a sufficient number of such Shares otherwise deliverable to Participant through such means as the Company may determine in its sole discretion (whether through a broker or otherwise). Depending on the withholding method, the Company may withhold or account for Tax-Related Items by considering applicable minimum statutory withholding rates or other applicable withholding rates, including maximum applicable rates, in which case Participant will receive a refund of any over-withheld amount in cash and will have no entitlement to the Share equivalent.

To the extent determined appropriate by the Company in its discretion, it will have the right (but not the obligation) to satisfy any Tax-Related Items by reducing the number of Shares otherwise deliverable to Participant. In this case, for tax purposes, Participant will be deemed to have been issued the full number of Shares subject to the vested PSUs, notwithstanding that a number of the Shares are held back solely for the purpose of paying the Tax-Related Items.

If Participant is a Section 16 officer of the Company under the Exchange Act, then the Company will withhold in Shares upon the relevant taxable or tax withholding event, as applicable, unless the Company determines that such withholding method is problematic under Applicable Laws. In this case, Participant may elect the form of withholding from the alternatives above.

Finally, Participant agrees to pay to the Company or the Employer any amount of Tax-Related Items that the Company or the Employer may be required to withhold or account for as a result of Participant's participation in the Plans that cannot be satisfied by the means previously described. If Participant fails to make satisfactory arrangements for the payment of any required Tax-Related Items obligations hereunder at the time any applicable PSUs otherwise are scheduled to vest pursuant to Sections 3 or 4, Participant will permanently forfeit such PSUs and any right to receive Shares thereunder and the PSUs will be returned to the Company at no cost to the Company.

9. Rights as Stockholder. Neither Participant nor any person claiming under or through Participant will have any of the rights or privileges of a stockholder of the Company in respect of any Shares deliverable hereunder unless and until certificates representing such Shares will have been issued, recorded on the records of the Company or its transfer agents or registrars, and delivered to Participant. After such issuance, recordation and delivery, Participant will have all the rights of a stockholder of the Company with respect to voting such Shares and receipt of dividends and distributions on such Shares.

10. No Guarantee of Continued Service. PARTICIPANT ACKNOWLEDGES AND AGREES THAT THE VESTING OF THE PSUs PURSUANT TO THE VESTING CONDITIONS HEREOF IS EARNED ONLY BY CONTINUING AS AN ACTIVE SERVICE PROVIDER, AND NOT THROUGH THE ACT OF BEING HIRED, BEING GRANTED THIS AWARD OF PSUs OR ACQUIRING SHARES HEREUNDER. PARTICIPANT FURTHER ACKNOWLEDGES AND AGREES THAT THIS AWARD AGREEMENT, THE TRANSACTIONS CONTEMPLATED HEREUNDER AND THE VESTING CONDITIONS SET FORTH HEREIN DO NOT CONSTITUTE AN EXPRESS OR IMPLIED PROMISE OF CONTINUED ENGAGEMENT AS A SERVICE PROVIDER FOR THE PERFORMANCE PERIOD, FOR ANY PERIOD, OR AT ALL, AND WILL NOT INTERFERE IN ANY WAY WITH PARTICIPANT'S RIGHT OR THE RIGHT OF THE COMPANY (OR THE EMPLOYER) TO TERMINATE PARTICIPANT'S RELATIONSHIP AS A SERVICE PROVIDER AT ANY TIME, WITH OR WITHOUT CAUSE.

11. Change in Control.

(a) In the event of a Change in Control prior to the last date of any Performance Period, (i) the affected Performance Period(s) shall be truncated so that it ends on the closing date of the Change in Control, (ii) the Company TSR (as defined in the Performance Goal and Pay-Out Matrix attached hereto as Exhibit B) shall be determined based on the per share transaction consideration attributed to the Common Stock in connection with the Change in Control, and (iii) the NASDAQ Composite Index TSR shall be determined based on the average share price of the applicable stock during the ninety (90) trading days prior to and including the closing date of the Change in Control.

(b) As of the closing date of the Change in Control, Participant shall vest in a number of PSUs equal to the product of (A) the Earned PSUs, as determined subject to subsection (a) above, multiplied by (B) a fraction, the numerator of which is equal to the number of days that have elapsed between the Date of Grant and the closing date of the Change in Control and the denominator of which is equal to (i) the total number of days during the Two-Year Peformance Period in case the closing date of the Change in Control occurs during the Two-Year Peformance Period, or (ii) the total number of days during the Three-Year Performance Period in case the closing date of the Change in Control occurs during the last year of the Three-Year Peformance Period (the "CIC Vested PSUs").

(c) The number of PSUs equal to the difference, in any, between (i) the Target Number of PSUs for each Performance Period and (ii) the CIC Vested PSUs for each Performance Period shall be converted into time-vested Restricted Stock Units and vest in equal monthly installments over the period commencing on the closing date of the Change in Control and ending on the last day of the respective Performance Period (the "Time-Based RSUs"), provided, however, that, in accordance with the provisions of the Plans, if the Time-Based RSUs are not assumed by the successor corporation in connection with the Change in Control, the Time-Based RSUs shall vest in full immediately prior to closing date of the Chante in Control.

(d) Any Time-Based RSUs shall be subject to the terms of the Plans, this Award Agreement (except for the terms pertaining to the attainment of Performance Goals) and to any Change in Control agreement entered into between Participant, the Company or any Parent or Subsidiary.

12. Nature of Grant. In accepting the Award, Participant acknowledges, understands and agrees that:

a. the grant of the PSUs is voluntary and occasional and does not create any contractual or other right to receive future grants of PSUs, or benefits in lieu of PSUs, even if PSUs have been granted in the past;

b. all decisions with respect to future PSUs or other grants, if any, will be at the sole discretion of the Company;

c. Participant is voluntarily participating in the Plans;

d. the PSUs and the Shares subject to the PSUs are not intended to replace any pension rights or compensation;

e. the PSUs and the Shares subject to the PSUs, and the income and value of same, are not part of normal or expected compensation for purposes of calculating any severance, resignation, termination, redundancy, dismissal, end-of-service payments, bonuses, long-service awards, pension or retirement or welfare benefits or similar payments;

f. the future value of the underlying Shares is unknown, indeterminable and cannot be predicted with certainty;

g. no claim or entitlement to compensation or damages shall arise from forfeiture of the PSUs resulting from the termination of Participant's status as a Service Provider for any reason whatsoever whether or not later found to be invalid or in breach of employment laws in the jurisdiction where Participant is employed or rendering services or the terms of Participant's employment or service agreement, if any), and in consideration of the grant of the PSUs to which Participant is otherwise not entitled, Participant irrevocably agrees never to institute any claim against the Company, any Parent or Subsidiary or the Employer, waives his or her ability, if any, to bring any such claim, and releases the Company, any Parent or Subsidiary and the Employer from any such claim; if, notwithstanding the foregoing, any such claim is allowed by a court of competent jurisdiction, then, by participating in the Plans, Participant shall be deemed irrevocably to have agreed not to pursue such claim and agrees to execute any and all documents necessary to request dismissal or withdrawal of such claim; and

h. unless otherwise provided in the Plans or by the Company in its discretion, the PSUs and the benefits evidenced by this Award Agreement do not create any entitlement to have the PSUs or any such benefits transferred to, or assumed by, another company nor be exchanged, cashed out or substituted for, in connection with any corporate transaction affecting the Shares; and

i. the following provisions apply only if Participant is providing services outside the United States:

(i) the PSUs and the Shares subject to the PSUs are not part of normal or expected compensation or salary for any purpose; and

(ii) Participant acknowledges and agrees that neither the Company, the Employer nor any Parent or Subsidiary shall be liable for any foreign exchange rate fluctuation between Participant's local currency and the United States Dollar that may affect the value of the PSUs or of any amounts due to Participant pursuant to the settlement of the PSUs or the subsequent sale of any Shares acquired upon settlement.

13. No Advice Regarding Grant. The Company is not providing any tax, legal or financial advice, nor is the Company making any recommendations regarding Participant's participation in the Plans, or Participant's acquisition or sale of the underlying Shares. Participant is hereby advised to consult with his or her own personal tax, legal and financial advisors regarding his or her participation in the Plans before taking any action related to the Plans.

14. **DATA PRIVACY**. ***Participant hereby explicitly and unambiguously consents to the collection, use and transfer, in electronic or other form, of Participant's personal data as described in this Award Agreement and any other PSU grant materials by and among, as applicable, the Employer, the Company and any Parent or Subsidiary for the exclusive purpose of implementing, administering and managing Participant's participation in the Plans.***

Participant understands that the Company and the Employer may hold certain personal information about Participant, including, but not limited to, Participant's name, home address and telephone number, date of birth, social insurance number or other identification number, salary, nationality, job title, any shares of stock or directorships held in the Company, details of all PSUs or any other entitlement to shares of stock awarded, canceled, exercised, vested, unvested or outstanding in Participant's favor ("Data"), for the exclusive purpose of implementing, administering and managing the Plans.

Participant understands that Data will be transferred to Charles Schwab & Co., Inc., or such other stock plan service provider as may be selected by the Company in the future, which is assisting the Company with the implementation, administration and management of the Plans. Participant understands that the recipients of the Data may be located in the United States or elsewhere, and that the recipients' country (e.g., the United States) may have different data privacy laws and protections than Participant's country. Participant understands that if he or she resides outside the United States, he or she may request a list with the names and addresses of any potential recipients of the Data by contacting his or her local human resources representative. Participant authorizes the Company, its broker and any other possible recipients which may assist the Company (presently or in the future) with implementing, administering and managing the Plans to receive, possess, use, retain and transfer the Data, in electronic or other form, for the sole purpose of implementing, administering and managing his or her participation in the Plans. Participant understands that Data will be held only as long as is necessary to implement, administer and manage Participant's participation in the Plans. Participant understands if he or she resides outside the United States, he or she may, at any time, view Data, request additional information about the storage and processing of Data, require any necessary amendments to Data or refuse or withdraw the consents herein, in any case without cost, by contacting in writing his or her local human resources representative. Further, Participant understands that he or she is providing the consents herein on a purely voluntary basis. If Participant does not consent, or if Participant later seeks to revoke his or her consent, his or her employment status or service and career with the Employer will not be adversely affected; the only adverse consequence

of refusing or withdrawing Participant's consent is that the Company would not be able to grant Participant PSUs or other Awards or administer or maintain such Awards. Therefore, Participant understands that refusing or withdrawing his or her consent may affect Participant's ability to participate in the Plans. For more information on the consequences of Participant's refusal to consent or withdrawal of consent, Participant understands that he or she may contact his or her local human resources representative.

15. Address for Notices. Any notice to be given to the Company under the terms of this Award Agreement will be addressed to the Company, in care of Stock Administration at Fortinet, Inc., at 1090 Kifer Road, Sunnyvale, CA 94086, or at such other address as the Company may hereafter designate in writing.

16. Grant is Not Transferable. Except to the limited extent provided in Section 7, this grant and the rights and privileges conferred hereby will not be transferred, assigned, pledged or hypothecated in any way (whether by operation of law or otherwise) and will not be subject to sale under execution, attachment or similar process. Upon any attempt to transfer, assign, pledge, hypothecate or otherwise dispose of this grant, or any right or privilege conferred hereby, or upon any attempted sale under any execution, attachment or similar process, this grant and the rights and privileges conferred hereby immediately will become null and void.

17. Binding Agreement. Subject to the limitation on the transferability of this grant contained herein, this Award Agreement will be binding upon and inure to the benefit of the heirs, legatees, legal representatives, successors and assigns of the parties hereto.

18. Additional Conditions to Issuance of Stock. If at any time the Company will determine, in its discretion, that the listing, registration or qualification of the Shares upon any securities exchange or under any U.S. state or federal or foreign law, or the consent or approval of any governmental regulatory authority is necessary or desirable as a condition to the issuance of Shares to Participant (or his or her estate or beneficiary, if applicable), such issuance will not occur unless and until such listing, registration, qualification, consent or approval will have been effected or obtained free of any conditions not acceptable to the Company. Where the Company determines that the delivery of the payment of any Shares will violate U.S. federal securities laws or other Applicable Laws, the Company will defer delivery until the earliest date at which the Company reasonably anticipates that the delivery of Shares will no longer cause such violation.

19. Plan Governs. This Award Agreement is subject to all terms and provisions of the Plans. In the event of a conflict between one or more provisions of this Award Agreement and one or more provisions of the Plan or the Performance Award Plan, the provisions of the Plan will govern; provided, however, that to the extent the PSUs are intended to constitute Qualified Performance-Based Compensation, the provisions of the Performance Award Plan will prevail to the extent necessary to ensure that the PSUs will be treated as Qualified Performance-Based Compensation.

20. Administrator Authority. The Administrator will have the power to interpret the Plans and this Award Agreement and to adopt such rules for the administration, interpretation and application of the Plans as are consistent therewith and to interpret or revoke any such rules (including, but not limited to, the determination of whether or not any PSUs have vested). All actions taken and all interpretations and determinations made by the Administrator in good faith will be final and binding upon Participant, the Company and all other interested persons. No member of the Administrator will be personally liable for any action, determination or interpretation made in good faith with respect to the Plans or this Award Agreement.

21. Electronic Delivery. The Company may, in its sole discretion, decide to deliver any documents related to PSUs awarded under the Plans or future PSUs that may be awarded under the Plans by electronic means or request Participant's consent to participate in the Plans by electronic means. Participant hereby consents to receive such documents by electronic delivery and agrees to participate in the Plans through any on-line or electronic system established and maintained by the Company or a third party designated by the Company.

22. Captions. Captions provided herein are for convenience only and are not to serve as a basis for interpretation or construction of this Award Agreement.

23. Agreement Severable. In the event that any provision in this Award Agreement will be held invalid or unenforceable, such provision will be severable from, and such invalidity or unenforceability will not be construed to have any effect on, the remaining provisions of this Award Agreement.

24. Modifications to the Agreement. This Award Agreement constitutes the entire understanding of the parties on the subjects covered. Participant expressly warrants that he or she is not accepting this Award Agreement in reliance on any promises, representations, or inducements other than those contained herein. Modifications to this Award Agreement or the Plans

can be made only in an express written document executed by a duly authorized officer of the Company. Notwithstanding anything to the contrary in the Plans or this Award Agreement, the Company reserves the right to revise this Award Agreement as it deems necessary or advisable, in its sole discretion and without the consent of Participant, to comply with Section 409A or to otherwise avoid imposition of any additional tax or income recognition under Section 409A in connection to this Award of PSUs, but the Company shall not be under any obligation to make any such revision. Furthermore, nothing in this Award Agreement or the Plans shall provide a basis for any person to take action against the Company or any Parent or Subsidiary based on matters covered by Section 409A, including the tax treatment of any PSU settled or amount paid or PSUs granted under this Award Agreement, and neither the Company nor any Parent or Subsidiary shall under any circumstances have any liability to Participant or his or her estate or any other party for any taxes, penalties or interest due on amounts paid or payable under this Award Agreement, including taxes, penalties or interest imposed under Section 409A.

25. Amendment, Suspension or Termination of the Plan. By accepting this Award, Participant expressly warrants that he or she has received an Award of PSUs under the Plans, and has received, read and understood a description of the Plans. Participant understands that the Plans are discretionary in nature and may be amended, suspended or terminated by the Company at any time.

26. Governing Law and Venue. This Award Agreement will be governed by the laws of the State of California, without giving effect to the conflict of law principles thereof. For purposes of litigating any dispute that arises under this Award of Restricted Stock or this Award Agreement, the parties hereby submit to and consent to the jurisdiction of the State of California**,** and agree that such litigation will be conducted in the courts of Santa Clara County, California**,** or the federal courts for the United States for the Northern District of California, and no other courts, where this Award of Restricted Stock is made and/or to be performed.

27. Language. If Participant has received this Award Agreement or any other document related to the Plans translated into a language other than English and if the meaning of the translated version is different than the English version, the English version will control.

28. Addendum. Notwithstanding any provisions in the Award Agreement, the PSU grant shall be subject to any special terms and conditions set forth in the Addendum, attached as Exhibit C, for Participant's country. Moreover, if Participant relocates to one of the countries included in the Addendum, the special terms and conditions for such country will apply to Participant, to the extent the Company determines that the application of such terms and conditions is necessary or advisable for legal or administrative reasons. The Addendum constitutes part of the Award Agreement.

29. Imposition of Other Requirements. The Company reserves the right to impose other requirements on Participant's participation in the Plans, on the PSU and on any Shares acquired under the Plans, to the extent the Company determines it is necessary or advisable for legal or administrative reasons, and to require Participant to sign any additional agreements or undertakings that may be necessary to accomplish the foregoing.

30. Waiver. Participant acknowledges that a waiver by the Company of breach of any provision of this Award Agreement shall not operate or be construed as a waiver of any other provision of this Award Agreement, or of any subsequent breach by Participant or any other Participant.

*** * ***

Exhibit B

Performance Goal and Pay-Out Matrix

Performance Stock Unit Award Agreement

1. Performance Periods:

Two-Year Performance Period: [January 1, 2013 - December 31, 2014]

Three-Year Performance Period: [January 1, 2013 - December 31, 2015]

2. Performance Goal/Calculation of Earned PSUs. The Performance Goal shall be based on a comparison of the Company TSR (defined below) relative to the NASDAQ Composite Index TSR, which shall be equal to the Company TSR minus the NASDAQ Composite Index TSR during the applicable Performance Period ("Relative TSR").

Total Shareholder Return ("TSR") means the average share price for the applicable stock during the final ninety (90) trading days of the Performance Period divided by the average share price of the applicable stock during the ninety (90) trading days ending on the trading day prior to the first day of the Performance Period. The value of share price of the applicable stock in the calculation of TSR shall include the value attributable to reinvestment of dividends, if any.

The number of PSUs that vest shall be equal to the Target Number of PSUs subject to the applicable Performance Period, multiplied by the Award Multiplier for the applicable Performance Period (the "Earned PSUs").

Relative TSR Performance	Award Multiplier
+25% or greater	150%
+12.5%	125%
0%	100%
-16.7%	50%
-33.3% TSR or less	0%

If the Earned PSUs for the Two-Year Performance Period are below the Target Number of PSUs subject to the Two-Year Performance Period, the difference between Earned PSUs and the Target Number of PSUs subject to the Two-Year Performance Period will be added to the Target Number of PSUs applicable to the Three-Year Performance Period. The additional PSUs, if any, that are added to the Target Number of PSUs subject to the Three-Year Performance Period shall be subject to the same vesting conditions applicable to the PSUs subject to the Three-Year Performance Period.

3. Adjustment to Performance Goal. The Administrator shall specify the manner of adjustment of the Performance Goal to the extent necessary to prevent dilution or enlargement of any Award as a result of extraordinary events or circumstances, as determined by the Administrator, or to exclude the effects of extraordinary, unusual, or non-recurring items, changes in applicable laws, regulations, or accounting principles, currency fluctuations, discontinued operations, non-cash items, such as amortization, depreciation, or reserves, asset impairment or any recapitalization, restructuring, reorganization, merger, acquisition, divestiture, consolidation, spin-off, split-up, combination, liquidation, dissolution, sale of assets, or other similar corporate transaction, but only to the extent such adjustments would be permitted under Section 162(m) of the Code.

Exhibit C

Addendum to

Performance Stock Unit Award Agreement

Terms and Conditions

This Addendum includes additional terms and conditions that govern the PSUs granted to Participant under the Plans if Participant resides and/or works in one of the countries listed below. This Addendum forms part of the Award Agreement. Capitalized terms used but not defined herein shall have the meanings set forth in the Plans, the Notice of Grant and/or the Terms and Conditions of PSU Grant.

If Participant is a citizen or resident of a country other than the one in which Participant is currently working, is considered a resident of another country for local law purposes or transfers employment and/or residency between countries after the Date of Grant, the Company shall, in its sole discretion, determine to what extent the additional terms and conditions included herein will apply to Participant under these circumstances.

Notifications

This Addendum also includes notices regarding exchange controls and certain other issues of which Participant should be aware with respect to Participant's participation in the Plans. The information is based on the securities, exchange control and other laws in effect in Participant's country as of July 2013. Such laws are often complex and change frequently. As a result, the Company strongly recommends that Participant not rely on the information noted herein as the only source of information relating to the consequences of Participant's participation in the Plans because the information may be out of date at the time Participant vests in the PSUs or sells Shares acquired under the Plans.

In addition, the information contained herein is general in nature and may not apply to Participant's particular situation, and the Company is not in a position to assure Participant of any particular result. Accordingly, Participant is advised to seek appropriate professional advice as to how the relevant laws in Participant's country may apply to Participant's situation.

Finally, if Participant is a citizen or resident of a country other than the one in which Participant is currently working, is considered a resident of another country for local law purposes or transfers employment and/or residency between countries after the Date of Grant, the information contained herein may not be applicable in the same manner to Participant.

Argentina

Notifications

Securities Law Information. Neither the PSUs nor the underlying Shares are publicly offered or listed on any stock exchange in Argentina. The offer is private and not subject to the supervision of any Argentine governmental authority.

Exchange Control Information. In the event that Participant transfers proceeds from the sale of Shares or the receipt of any dividends paid on such Shares into Argentina within 10 days of receipt (*i.e.*, the proceeds have not been held in the offshore bank or brokerage account for at least 10 days prior to transfer), Participant must deposit 30% of the proceeds into a non-interest bearing account in Argentina for 365 days. If Participant has satisfied the 10-day holding obligation, the Argentine bank handling the transaction may request certain documentation in connection with Participant's request to transfer proceeds into Argentina, including evidence of the sale or dividend payment and proof that no funds were remitted out of Argentina to acquire the Shares. If the bank determines that the 10-day rule or any other rule or regulation promulgated by the Argentine Central Bank has not been satisfied, it will require that 30% of the proceeds be placed in a non-interest bearing dollar denominated mandatory deposit account for a holding period of 365 days. Please note that exchange control regulations in Argentina are subject to frequent change. Participant should consult with Participant's personal legal advisor regarding any exchange control obligations Participant may have in connection with Participant's participation in the Plans.

Tax Reporting Information. If Participant holds Shares as of December 31 of any year, Participant is required to report the holding of the Shares on his or her personal tax return for the relevant year.

Australia

Notifications

Securities Law Information. If Participant acquires Shares under the Plans and Participant offers such Shares for sale to a person or entity resident in Australia, the offer may be subject to disclosure requirements under Australian law. Participant should obtain legal advice as to Participant's disclosure obligations prior to making any such offer.

Austria

Notifications

Exchange Control Information. If Participant holds Shares acquired under the Plans outside of Austria, Participant must submit a report to the Austrian National Bank. An exemption applies if the value of the Shares as of any given quarter does not exceed €30,000,000 or as of December 31 does not exceed €5,000,000. If the former threshold is exceeded, quarterly obligations are imposed, whereas if the latter threshold is exceeded, annual reports must be given. The annual reporting date is December 31 and the deadline for filing the annual report is January 31 of the following year.

When Participant sells Shares acquired under the Plans or receives a dividend payment, there may be exchange control obligations if the cash proceeds are held outside of Austria. If the transaction volume of all accounts abroad exceeds €3,000,000, the movements and balances of all accounts must be reported monthly, as of the last day of the month, on or before the fifteenth day of the following month, on the prescribed form (*Meldungen SI-Forderungen und/oder SI-Verpflichtungen*).

Belgium

Notifications

Tax Reporting Information. Participant is required to report any security or bank account opened and maintained outside Belgium on Participant's annual tax return.

Brazil

Notifications

Compliance with Law. By accepting the PSUs, Participant acknowledges his or her agreement to comply with applicable Brazilian laws and to pay any and all applicable taxes associated with the vesting of the PSUs, and the sale of Shares acquired under the Plans and the receipt of any dividends.

Exchange Control Information. If Participant is resident or domiciled in Brazil, Participant will be required to submit annually a declaration of assets and rights held outside of Brazil to the Central Bank of Brazil if the aggregate value of such assets and rights is equal to or greater than US$100,000. Assets and rights that must be reported include Shares acquired under the Plans.

Cambodia

There are no country-specific provisions.

Canada

Terms and Conditions

PSUs Payable Only in Shares. Notwithstanding any discretion in the Plans or anything to the contrary in the Award Agreement, the grant of PSUs does not provide any right for Participant to receive a cash payment, and the PSUs are payable in Shares only.

Termination of Service. The following provision replaces Section 6 of the Award Agreement:

Except as otherwise provided in the Planss or the Award Agreement, the balance of the PSUs that have not vested as of the time of Participant's termination as a Service Provider (for any or no reason and whether or not later found to be invalid or in breach of Canadian laws or the terms of the Participant's employment or service agreement, if any), and Participant's right to acquire any Shares hereunder, will immediately terminate upon Participant's termination as a Service Provider. For purposes of the preceding sentence, the Participant's right to vest in the PSUs will terminate effective as of the date that is the earlier of (1) the date Participant's status as a Service Provider is terminated, (2) the date Participant receives notice of termination of service from the Employer, or (3) the date the Participant is no longer actively providing service. The right to vest in the PSUs will not be extended by any notice period (e.g., active service would not include any contractual notice period or any period of "garden leave" or similar period mandated under Canadian laws or the terms of the Participant's employment or service agreement, if any); the Administrator shall have the exclusive discretion to determine when the Participant is no longer actively providing service for purposes of the PSU grant (including whether Participant may still be considered to be a Service Provider while on a leave of absence).

<u>The following provisions will apply if Participant is a resident of Quebec</u>:

Language Consent. The parties acknowledge that it is their express wish that this Award Agreement, as well as all documents, notices and legal proceedings entered into, given or instituted pursuant hereto or relating directly or indirectly hereto, be drawn up in English.

Les parties reconnaissent avoir expressement souhaité que la convention ["Award Agreement"], ainsi que tous les documents, avis et procédures judiciaries, éxecutés, donnés ou intentés en vertu de, ou lié, directement ou indirectement à la présente convention, soient rédigés en langue anglaise.

Data Privacy Notice and Consent. This provision supplements Section 13 of the Award Agreement:

Participant hereby authorizes the Company and the Company's representatives to discuss with and obtain all relevant information from all personnel, professional or not, involved in the administration and operation of the Plans. Participant further authorizes the Company and any Parent or Subsidiary and the administrator of the Plans to disclose and discuss the Plans with their advisors. Participant further authorizes the Company and any Parent or Subsidiary to record such information and to keep such information in Participant's file.

Notifications

Securities Law Information. Participant is permitted to sell Shares acquired under the Plans through the designated broker appointed under the Plans, if any, provided the resale of Shares acquired under the Plans takes place outside of Canada through the facilities of a stock exchange on which the Shares are listed. The Shares are currently listed on the NASDAQ.

Tax Reporting Information. Participant is required to report any foreign assets (including Shares) with a value exceeding C$100,000 on Form T1135 (Foreign Income Verification Statement). The statement is due at the same time as Participant's annual tax return.

Chile

Notifications

Securities Law Information. Neither the Company, the PSUs nor the Shares issued upon vesting of the PSUs are registered with the Chilean Registry of Securities or under the control of the Chilean Superintendence of Securities.

Exchange Control and Tax Information. Participant is not required to repatriate proceeds obtained from the sale of Shares or from dividends to Chile; however, if Participant decides to repatriate proceeds from the sale of Shares and/or dividends and the amount of the proceeds to be repatriated exceeds US$10,000, Participant acknowledges that he or she must effect such repatriation through the Formal Exchange Market (i.e., a commercial bank or registered foreign exchange office).

Further, if the value of Participant's aggregate investments held outside of Chile exceed US$5,000,000 (including the value of Shares acquired under the Plans), Participant must report the status of such investments annually to the Central Bank using Annex 3.1 of Chapter XII of the Foreign Exchange Regulations.

Finally, if Participant holds Shares acquired under the Plans outside of Chile, he or she must inform the Chilean Internal Revenue Service (the "CIRS") of the details of his or her investment in the Shares by Filing Tax Form 1851 "Annual Sworn Statement Regarding Investments Held Abroad". Further, if Participant wishes to receive credit against Participant's Chilean income taxes for any taxes paid abroad, Participant must report the payment of taxes abroad to the CIRS by filing Tax Form 1853 "Annual Sworn Statement Regarding Credits for Taxes Paid Abroad". These statements must be submitted electronically through the CIRS website before March 15 of each year: www.sii.cl.

China

Terms and Conditions

<u>The following provisions will apply to Participants who are subject to PRC exchange control restrictions, as determined by the Company in its sole discretion</u>:

Immediate Sale Restriction. Notwithstanding anything to the contrary in the Plans or Award Agreement, due to exchange control laws in China, Participant agrees that any Shares acquired at vesting of the PSUs may be immediately sold at vesting or, at the Company's discretion, at a later time (including when Participant's status as a Service Provider terminates). If, however, the sale of the Shares is not permissible under the Company's insider trading policy, or if any requisite exchange control approval for the Plans in China has not been obtained, the Company retains the discretion to postpone the issuance of the Shares subject to Participant's vested PSUs until such time that the sale is again permissible and to then immediately sell the Shares subject to the PSUs. Participant further agrees that the Company is authorized to instruct its designated broker to assist with the mandatory sale of the Shares (on Participant's behalf pursuant to this authorization), and Participant expressly authorizes such broker to complete the sale of such Shares. Participant acknowledges that the Company's designated broker is under no obligation to arrange for the sale of the Shares at any particular price. Upon the sale of the Shares, the Company agrees to pay the cash proceeds from the sale, less any brokerage fees or commissions, to Participant in accordance with applicable exchange control laws and regulations and provided any liability for Tax-Related Items resulting from the vesting of the PSUs has been satisfied. Due to fluctuations in the Share price and/or the US dollar exchange rate between the vesting date and (if later) the date on which the Shares are sold, the sale proceeds may be more or less than the market value of the Shares on the vesting date (which is the amount relevant to determining Participant's tax liability). Participant understands and agrees that the Company is not responsible for the amount of any loss Participant may incur and that the Company assumes no liability for any fluctuations in the Share price and/or US dollar exchange rate.

Exchange Control Information. Participant understands and agrees that, to facilitate compliance with exchange control laws in China, Participant may be required to immediately repatriate to China the cash proceeds from the sale of any Shares acquired at vesting of the PSUs and any dividends received in relation to the Shares. Participant further understands that, under local law, such repatriation of the cash proceeds may need to be effectuated through a special exchange control account established by the Company or any Parent or Subsidiary, and Participant hereby consents and agrees that the proceeds from the sale of Shares acquired under the Plans and any dividends received in relation to the Shares may be transferred to such special account prior to being delivered to Participant.

The proceeds may be paid to Participant in U.S. dollars or local currency at the Company's discretion. In the event the proceeds are paid to Participant in U.S. dollars, Participant understands that Participant will be required to set up a U.S. dollar bank account in China and provide the bank account details to the Employer and/or the Company so that the proceeds may be deposited into this account.

Participant agrees to bear any currency fluctuation risk between the time the Shares are sold or dividends are paid and the time the proceeds are distributed to Participant through any such special account.

Participant further agrees to comply with any other requirements that may be imposed by the Company in the future in order to facilitate compliance with exchange control requirements in China.

Colombia

Terms and Conditions

Labor Laws Acknowledgement. The following provision supplements Section 12 of the Award Agreement:

Participants acknowledges that pursuant to Article 128 of the Colombian Labor Code, the Plans and related benefits do not constitute a component of "salary" for any purpose.

Notifications

Exchange Control Information. Investment and assets (such as Shares) held abroad must be registered with the Central Bank (*Banco de la Republica*) if the value of Participant's aggregate investments and assets abroad (as of December 31 of the relevant fiscal year) equals or exceeds US$500,000. In addition, when Participant sells or otherwise disposes of any Shares acquired under the Plans, if the investment was registered with the Central Bank, Participant must cancel the registration no later than March 31 of the year following the year in which the Shares were sold. If Participant does not cancel the registration by the above-mentioned deadline, Participant will be subject to a fine.

Costa Rica

There are no country-specific provisions.

Czech Republic

Notifications

Exchange Control Information. The Czech National Bank may require Participant to fulfill certain notification duties in relation to the opening and maintenance of a foreign account.

Because exchange control regulations change frequently and without notice, Participant should consult his or her personal legal advisor prior to the sale of Shares to ensure compliance with current regulations. It is Participant's responsibility to comply with Czech exchange control laws, and neither the Company nor any Parent or Subsidiary will be liable for any resulting fines or penalties.

Dominican Republic

There are no country-specific provisions.

Egypt

Notifications

Exchange Control Information. If Participant transfers funds into Egypt in connection with the sale of Shares, Participant is required to do so through a registered bank in Egypt.

Finland

There are no country-specific provisions.

France

Terms and Conditions

French Language Provision. By accepting the Award Agreement providing for the terms and conditions of Participant's grant, Participant confirms having read and understood the documents relating to this grant (the Plans and the Award Agreement) which were provided in English language. Participant accepts the terms of those documents accordingly.

En acceptant le Contrat d'Attribution décrivant les termes et conditions de l'attribution, le participant confirme ainsi avoir lu et compris les documents relatifs à cette attribution (le Plans U.S. et le Contrat d'Attribution) qui ont été communiqués en langue anglaise. Le participant accepte les termes en connaissance de cause.

Notifications

Tax Information. The PSUs are not intended to be French tax-qualified Awards.

Tax Reporting Information. If Participant retains Shares acquired under the Plans outside of France or maintains a foreign bank account, Participant is required to report such to the French tax authorities when filing Participant's annual tax return. Failure to comply could trigger significant penalties.

Germany

Notifications

Exchange Control Information. If Participant make cross-border payments in excess of €12,500 in connection with the sale of securities (including Shares acquired under the Plans) or the receipt of any dividends, Participant must file a report with the *Servicezentrum Außenwirtschaftsstatistik*, which is the competent federal office of the *Deutsche Bundesbank* (the German Central Bank) for such notifications in Germany. Participant is responsible for satisfying the reporting obligation and should be able to obtain a copy of the form used for this purpose from the German bank Participant uses to carry out the transfer.

In addition, in the unlikely event that Participant holds Shares exceeding 10% of the total capital of the Company, Participant must report Participant's holdings in the Company on an annual basis.

Hong Kong

Terms and Conditions

PSUs Payable Only in Shares. Notwithstanding any discretion in the Plans or anything to the contrary in the Award Agreement, the grant of PSUs does not provide any right for Participant to receive a cash payment, and the PSUs are payable in Shares only.

Securities Law Information. *Warning: The grant of PSUs under the terms of the Award Agreement and the Plans and the issuance of Shares at vesting of PSUs do not constitute a public offering of securities, and they are available only to Service Providers.*

Please be aware that the contents of the Award Agreement, including this Addendum, and the Plans have not been reviewed by any regulatory authority in Hong Kong. Participant is advised to exercise caution in relation to the right to acquire Shares at vesting of the PSUs, or otherwise, under the Plans. If Participant is in any doubt about any of the contents of the Award Agreement, including this Addendum, or the Plans, Participant should obtain independent professional advice.

Sale of Shares. By accepting the PSUs, Participant agrees that in the event that the PSUs vest and Shares are issued to Participant within six months of the Date of Grant, Participant agrees that Participant will not dispose of any Shares acquired prior to the six-month anniversary of the Date of Grant.

Hungary

There are no country-specific provisions.

India

Notifications

Exchange Control Information. Participant must repatriate to India the proceeds from the sale of Shares acquired at vesting and any dividends received in relation to the Shares within 90 days after receipt. Participant must obtain evidence of the repatriation of funds in the form of a foreign inward remittance certificate (the “FIRC”) from the bank where Participant deposited the foreign currency. Participant must retain the FIRC in Participant's records to present to the Reserve Bank of India or Participant's Employer in the event that proof of repatriation is requested.

Tax Reporting Information. Participant is required to declare his or her foreign bank accounts and any foreign financial assets (including Shares held outside India) in Participant's annual tax return. It is Participant's responsibility to comply with this reporting obligation and Participant should consult his or her personal advisor in this regard.

Indonesia

Notifications

Exchange Control Information. If Participant remits funds into Indonesia (*e.g*., proceeds from the sale of Shares), the Indonesian Bank through which the transaction is made will submit a report of the transaction to the Bank of Indonesia for statistical reporting purposes. For transactions of US$10,000 or more, a description of the transaction must be included in the report. Although the bank through which the transaction is made is required to make the report, Participant must complete a "Transfer Report Form." The Transfer Report Form should be provided to Participant by the bank through which the transaction is to be made.

Ireland

Notifications

Director Notification Obligation. If Participant is a director, shadow director or secretary of an Irish Parent or Subsidiary, Participant must notify the Irish Parent or Subsidiary in writing within five business days of receiving or disposing of an interest in the Company (*e.g*., PSUs, Shares, etc.), or within five business days of becoming aware of the event giving rise to the notification requirement or within five days of becoming a director or secretary if such an interest exists at the time. This notification requirement also applies with respect to the interests of a spouse or children under the age of 18 (whose interests will be attributed to the director, shadow director or secretary).

Isle of Man

There are no country-specific provisions.

Israel

Terms and Conditions

Immediate Sale Restriction. Participant agrees that any Shares acquired at vesting of the PSUs will be immediately sold at vesting. If, however, the sale of the Shares is not permissible under the Company's insider trading policy, the Company retains the discretion to postpone the issuance of the Shares subject to Participant's vested PSUs until such time that the sale is again permissible and to then immediately sell the Shares subject to the PSUs. Participant further agrees that the Company is authorized to instruct its designated broker to assist with the mandatory sale of the Shares (on Participant's behalf pursuant to this authorization), and Participant expressly authorizes such broker to complete the sale of such Shares. Participant acknowledges that the Company's designated broker is under no obligation to arrange for the sale of the Shares at any particular price. Upon the sale of the Shares, the Company agrees to pay the cash proceeds from the sale, less any brokerage fees or commissions, to Participant, provided any liability for Tax-Related Items has been satisfied. Participant understands and agrees that the Company is not responsible for the amount of any loss Participant may incur and that the Company assumes no liability for any fluctuations in the Share price and/or US dollar exchange rate.

Italy

Terms and Conditions

Data Privacy Notification. This notification replaces Section 14 of the Award Agreement:

Participant understands that Participant's Employer, the Company and any Subsidiary or Affiliate may hold certain personal information about Participant, including, but not limited to, Participant's name, home address and telephone number, date of birth, social insurance or other identification number, salary, nationality, job title, any Shares or directorships held in the Company or any Subsidiary or Affiliate, details of all PSUs, or any other entitlement to Shares awarded, canceled, exercised, vested, unvested or outstanding in Participant's favor ("Data") and will process such data for the exclusive purpose of implementing, managing and administering the Plans and in compliance with applicable laws and regulations.

Participant also understands that providing the Company with Data is mandatory for compliance with local law and necessary for the performance of the Plans and that Participant's refusal to provide such Data would make it impossible for the Company to perform its contractual obligations and may affect Participant's ability to participate in the Plans. The Controller of personal data processing is Fortinet, Inc., with registered offices at 1090 Kifer Road, Sunnyvale, CA 94086, U.S.A., and, pursuant to Legislative Decree no. 196/2003, its Representative in Italy for privacy purposes is Fortinet Italy, S.r.L, with registered offices at Via del Casale Solaro, 119, 00143 Roma Italy.

Participant understands that Data will not be publicized, but it may be accessible by the Employer and its internal and external personnel in charge of processing of such Data and by the data processor (the "Processor"), if any. An updated list of Processors and other transferees of Data is available upon request from the Employer. Furthermore, Data may be transferred to banks, other financial institutions, or brokers involved in the management and administration of the Plans. Participant understands that Data may also be transferred to the independent registered public accounting firm engaged by the Company. Participant further understands that the Company and/or any Subsidiary or Affiliate will transfer Data among themselves as necessary for the purpose of implementing, administering and managing Participant's participation in the Plans, and that the Company and/or any Subsidiary or Affiliate may each further transfer Data to third parties assisting the Company in the implementation, administration, and management of the Plans, including any requisite transfer of Data to a broker or other third party with whom Participant may elect to deposit any Shares acquired at vesting of the PSUs. Such recipients may receive, possess, use, retain, and transfer Data in electronic or other form, for the purposes of implementing, administering, and managing Participant's participation in the Plans. Participant understands that these recipients may be acting as Controllers, Processors or persons in charge of processing, as the case may be, in accordance with local law and may be located in or outside the European Economic Area in countries such as in the United States that may not provide the same level of protection as intended under Italian data privacy laws. Should the Company exercise its discretion in suspending all necessary legal obligations connected with the management and administration of the Plans, it will delete Data as soon as it has completed all the necessary legal obligations connected with the management and administration of the Plans.

Participant understands that Data processing related to the purposes specified above shall take place under automated or non-automated conditions, anonymously when possible, that comply with the purposes for which Data is collected and with confidentiality and security provisions, as set forth by applicable laws and regulations, with specific reference to Legislative Decree no. 196/2003.

The processing activity, including communication, the transfer of Data abroad, including outside of the European Economic Area, as herein specified and pursuant to applicable laws and regulations, does not require Participant's consent thereto, as the processing is necessary to performance of contractual obligations related to implementation, administration, and management of the Plans. Participant understands that, pursuant to Section 7 of the Legislative Decree no. 196/2003, Participant have the right to, including but not limited to, access, delete, update, correct, or terminate, for legitimate reason, the Data processing. Participant should contact Participant's Employer in this regard.

Furthermore, Participant is aware that Data will not be used for direct-marketing purposes. In addition, Data provided can be reviewed and questions or complaints can be addressed by contacting Participant's local human resources representative.

Terms of Grant. By accepting the PSUs, Participant acknowledges that (1) Participant has received a copy of the Plans and the Award Agreement, including this Addendum; (2) Participant has reviewed those documents in their entirety and fully understands the contents thereof; and (3) Participant accepts all provisions of the Plans and the Award Agreement, including this Addendum. Participant further acknowledges that Participant has read and specifically and expressly approves, without limitation, the following sections of the Award Agreement: Section 6 - "Forfeiture upon Termination of Status as a Service Provider"; Section 8 - "Withholding of Taxes"; Section 10 - "No Guarantee of Continued Service"; Section 12 - "Nature of Grant"; Section 14 - "Data Privacy" as replaced by the above consent; Section 26 - "Governing Law and Venue"; and Section 27 - "Language."

Notifications

Exchange Control Information. Exchange control reporting is required if Participant transfers cash or Shares to or from Italy in excess of €10,000 or the equivalent amount in U.S. dollars. If the payment is made through an authorized broker resident in Italy, the broker will comply with the reporting obligation. In addition, Participant will have exchange control reporting obligations if Participant has any foreign investment (including Shares) held outside Italy in excess of €10,000. The reporting must be done on Participant's individual tax return.

Tax on Foreign Financial Assets. A tax on the value of financial assets held outside of Italy by individuals resident in Italy will be due. The taxable amount will be the fair market value of the financial assets (including Shares) assessed at the end of each calendar year.

Japan

Notifications

Exchange Control Information. If Participant maintains a foreign bank account outside of Japan with a value exceeding ¥50 million as of December 31, Participant is required to report such to the Japanese authorities by March 15th each year. Participant should consult with a personal tax advisor to ensure that he or she is properly complying with applicable reporting requirements in Japan.

Tax Reporting Information. Participant will be required to report details of any assets (including any Shares) held outside of Japan as of December 31 each year, to the extent such assets have a total net fair market value exceeding ¥50,000,000. Such report will be due by March 15 of the following year. Participant is advised to consult with his or her personal tax advisor as to whether the reporting obligation applies to Participant and whether Participant will be required to report details of any PSUs or Shares that Participant holds.

Korea

Notifications

Exchange Control Information. If Participant realizes US$500,000 or more from the sale of Shares or the receipt of dividends in a single transaction, Participant must repatriate the proceeds to Korea within 18 months of the receipt.

Malaysia

Notifications

Malaysian Insider Trading Notification. Participant should be aware of the Malaysian insider-trading rules, which may impact Participant's acquisition or disposal of Shares or rights to Shares under the Plans. Under the Malaysian insider-trading rules, Participant is prohibited from acquiring or selling Shares or rights to shares (*e.g*., PSUs granted under the Plans) when Participant possess information which is not generally available and which Participant know or should know will have a material effect on the price of Common Stock once such information is generally available.

Director Notification Obligation. If Participant is a director of a Malaysian Parent or Subsidiary, Participant is subject to certain notification requirements under the Malaysian Companies Act. Among these requirements is an obligation to notify the Company's Malaysian Parent or Subsidiary in writing when Participant receive or dispose of an interest (*e.g*., PSUs or Shares) in the Company or any related company. This notification must be made within 14 days of receiving or disposing of any interest in the Company or any related company.

Mexico

Terms and Conditions

No Entitlement or Claims for Compensation. These provisions supplement Section 11 of the Award Agreement:

Modification. By accepting the PSUs, Participant understands and agrees that any modification of the Plans or the Award Agreement or its termination shall not constitute a change or impairment of the terms and conditions of employment.

Policy Statement. The Award of PSUs the Company is making under the Plans is unilateral and discretionary and, therefore, the Company reserves the absolute right to amend it and discontinue it at any time without any liability.

The Company, with registered offices at 1090 Kifer Road, Sunnyvale, CA 94086, U.S.A., is solely responsible for the administration of the Plans and participation in the Plans and the acquisition of Shares does not, in any way, establish an employment relationship between Participant and the Company since Participant is participating in the Plans on a wholly commercial basis and the sole employer is Fortinet, Inc., located at Prol. Paseo de la Reforma 115 Int. 702, Col. Lomas de Santa Fe, Del. Alvaro Obregon, Mexico, D.F. C.P. 01219, nor does it establish any rights between Participant and the Employer.

Plan Document Acknowledgment. By accepting the Award of PSUs, Participant acknowledges that Participant has received copies of the Plans, has reviewed the Plans and the Award Agreement in their entirety and fully understands and accepts all provisions of the Plans and the Award Agreement.

In addition, by accepting the Award Agreement, Participant further acknowledges that Participant has read and specifically and expressly approved the terms and conditions in the Award Agreement, in which the following is clearly described and established: (i) participation in the Plans does not constitute an acquired right; (ii) the Plans and participation in the Plans are offered by the Company on a wholly discretionary basis; (iii) participation in the Plans is voluntary; and (iv) the Company and any Parent or Subsidiary are not responsible for any decrease in the value of the Shares underlying the PSUs.

Finally, Participant hereby declares that Participant does not reserve any action or right to bring any claim against the Company for any compensation or damages as a result of Participant's participation in the Plans and therefore grants a full and broad release to the Employer, the Company and any Parent or Subsidiary with respect to any claim that may arise under the Plans.

Spanish Translation

Sin derecho a compensación o reclamaciones por compensación. *Estas disposiciones complementan el Contrato:*

Modificación. *Al aceptar las Unidades de Acciones Restringidas, el Participante entiende y acuerda que cualquier modificación al Plan o al Contrato o su terminación no constituirá un cambio o perjuicio a los términos y condiciones de empleo.*

Declaración de Política. *El Otorgamiento de Unidades de Acciones Restringidas que la Compañía está haciendo de conformidad con el Plan es unilateral y discrecional y, por lo tanto, la Compañía se reserva el derecho absoluto de modificar y discontinuar el mismo en cualquier momento, sin responsabilidad alguna.*

La Compañía, con oficinas registradas ubicadas en 1090 Kifer Road, Sunnyvale, CA 94086, , EE.UU. es únicamente responsable de la administración del Plan y la participación en el Plan y la adquisición de Acciones no establece, de forma alguna, una relación de trabajo entre el Participante y la Compañía, ya que el Participante participa en el Plan de una forma totalmente comercial y el único patrón es *Fortinet, Inc., Prol. Paseo de la Reforma 115 Int. 702, Col. Lomas de Santa Fe, Del. Alvaro Obregon, Mexico, D.F. C.P. 01219, y tampoco establece ningún derecho entre el Participante y el Patrón.*

Reconocimiento del Documento del Plan. *Al aceptar el Otorgamiento de las Unidades de Acciones Restringidas, el Participante reconoce que el Participante ha recibido copias del Plan, ha revisado el Plan y el Contrato en su totalidad y entiende y acepta completamente todas las disposiciones contenidas en el Plan y en el Contrato.*

Adicionalmente, al aceptar el Contrato, el Participante reconoce que el Participante ha leído y específica y expresamente ha aprobado los términos y condiciones del Contrato, en el que claramente se ha descrito y establecido que: (i) la participación en el Plan no constituye un derecho adquirido; (ii) el Plan y la participación en el Plan es ofrecida por la Compañía de forma enteramente discrecional; (iii) la participación en el Plan es voluntaria; y (iv) la Compañía, así como su Sociedad Controlante, Subsidiaria no son responsables por cualquier disminución en el valor de las Acciones subyacentes a las Unidades de Acciones Restringidas.

Finalmente, el Participante en este acto declara que el Participante no se reserva ninguna acción o derecho para interponer cualquier demanda o reclamación en contra de la Compañía por compensación, daño o perjuicio alguno como resultado de su participación en el Plan y, por lo tanto, otorga el más amplio finiquito al Patrón, la Compañía, así como su Sociedad Controlante, Subsidiaria con respecto a cualquier demanda o reclamación que pudiera surgir en virtud del Plan.

Netherlands

Notifications

Securities Law Information. Participant should be aware of Dutch insider-trading rules, which may impact the sale of Shares acquired at vesting of the PSUs. In particular, Participant may be prohibited from effectuating certain transactions involving Shares during the period in which Participant possess “inside information” regarding the Company.

By accepting the PSUs, Participant acknowledges having read and understood the Securities Law Information and further acknowledges that it is Participant's responsibility to comply with the following Dutch insider trading rules:

Under Article 5:56 of the Dutch Financial Supervision Act, anyone who has “inside information” related to the Company is prohibited from effectuating a transaction in securities in or from the Netherlands. “Inside information” is knowledge of a detail concerning the issuer to which the securities relate that is not public and which, if published, would reasonably be expected to affect the stock price, regardless of the development of the price. The insider could be any Service Provider in the Netherlands who has inside information as described herein.

New Zealand

There are no country-specific provisions.

Nigeria

There are no country-specific provisions.

Norway

There are no country-specific provisions.

Panama

Notifications

Securities Law Information. The PSUs and any Shares which may be issued to Participant upon vesting and settlement of the PSUs are not subject to registration under Panamanian Law as they are not intended for the public, but solely for Participant's benefit.

Peru

Notifications

Securities Law Information. The offer of the PSUs is considered a private offering in Peru; therefore, it is not subject to registration in Peru.

Philippines

Terms and Conditions

PSUs Payable Only in Cash. Notwithstanding Section 2 of the Award Agreement, each PSU represents the right to receive the cash equivalent of the Fair Market Value of a Share on the date it vests. For the avoidance of doubt, Participant shall not be entitled to receive any Shares pursuant to any vested PSUs.

Poland

Notifications

Exchange Control Information. Polish residents holding foreign securities (including Shares) and maintaining accounts abroad must report information to the National Bank of Poland on transactions and balances of the securities and cash deposited in such accounts if the value of such securities and cash (when combined with all other assets held abroad) exceeds PLN 7,000,000. If required, the reports must be filed on a quarterly basis on special forms available on the website of the National Bank of Poland. Further, any transfer of funds in excess of a specified threshold (currently €15,000) must be effected through a bank account in Poland. Participant should maintain evidence of such foreign exchange transactions for five years, in case of a request for their production by the National Bank of Poland.

Portugal

Terms and Conditions

Language Consent. Participant hereby expressly declares that he or she has full knowledge of the English language and has read, understood and fully accepted and agreed with the terms and conditions established in the Plans and the Award Agreement.

Conhecimento da Lingua. O Participante pelo presente declara expressamente que tem pleno conhecimento da língua inglesa e que leu, compreendeu e livremente aceitou e concordou com os termos e condições estabelecidas no Plano e no Acordo de Atribuição

Notifications

Exchange Control Information. If Participant does not hold the Shares acquired at vesting with a Portuguese financial intermediary, Participant may need to file a report with the Portuguese Central Bank. If the Shares are held by a Portuguese financial intermediary, it will file the report for Participant.

Puerto Rico

There are no country-specific provisions.

Qatar

There are no country-specific provisions.

Romania

Notifications

Exchange Control Information. If Participant deposits the proceeds from the sale of Shares issued to him or her at vesting and settlement of the Shares in a bank account in Romania, Participant may be required to provide the Romanian bank with appropriate documentation explaining the source of the funds.

Participant should consult his or her personal advisor to determine whether Participant will be required to submit such documentation to the Romanian bank.

Russia

Terms and Conditions

U.S. Transaction. The Plans, the Award Agreement, including this Addendum, and all other materials Participant may receive regarding Participant's participation in the Plans or the grant of PSUs do not constitute advertising or an offering of securities in Russia. The issuance of Shares acquired at vesting has not and will not be registered in Russia; therefore, such Shares may not be offered or placed in public circulation in Russia. In no event will Shares acquired at vesting be delivered to Participant in Russia; all Shares will be maintained on Participant's behalf in the United States. Participant is not permitted to sell Shares acquired at vesting directly to a Russian legal entity or resident.

Depending on the development of local regulatory requirements, the Company reserves the right to settle PSUs in cash and/or to pay any proceeds related to the PSUs to Participant through local payroll.

Data Privacy. This notification supplements Section 14 of the Award Agreement:

Participant understands and agrees that he or she must complete and return a Consent to Processing of Personal Data (the "Consent") form to the Company. Further, Participant understands and agrees that if Participant does not complete and return a Consent form to the Company, the Company will not be able to grant PSUs to Participant or other awards or administer or maintain such awards. Therefore, Participant understands that refusing to complete a Consent form or withdrawing his or her consent may affect Participant's ability to participate in the Plans.

Notifications

Exchange Control Information. Participant must repatriate the proceeds from the sale of Shares and any dividends received in relation to the Shares to Russia within a reasonably short period after receipt. The sale proceeds and any dividends received must be initially credited to Participant through a foreign currency account opened in Participant's name at an authorized bank in Russia. After the funds are initially received in Russia, they may be further remitted to a foreign bank subject to the following limitations: (i) the foreign account may be opened only for individuals; (ii) the foreign account may not be used for business activities; and (iii) the Russian tax authorities must be given notice about the opening/closing of each foreign account within one month of the account opening/closing. Participant is strongly advised to contact his or her personal advisor before PSUs vest and Shares are sold as significant penalties may apply in the case of non-compliance with exchange control requirements and because such exchange control requirements may change.

Singapore

Notifications

Securities Law Information. The PSUs are being granted in reliance on Section 273(1)(f) of the Securities and Futures Act (Chapter 289, 2006 Ed.) (“SFA”), under which it is exempt from the prospectus and registration requirements under the SFA. The Plans have not been lodged or registered as a prospectus with the Monetary Authority of Singapore. Participant hereby acknowledge that the PSUs are subject to Section 257 of the SFA and that Participant will not be able to sell, or offer for sale, Shares acquired upon vesting of the PSUs, unless such sale or offer is made pursuant to the exemptions under Part XIII Division (1) Subdivision (4) (other than Section 280) of the SFA.

Director Notification Obligation. Directors of a Singaporean Parent or Subsidiary are subject to certain notification requirements under the Singapore Companies Act. Directors must notify the Singapore Parent or Subsidiary in writing of an interest (*e.g.*, unvested PSUs, Shares, etc.) in the Company or any Parent or Subsidiary within two (2) business days of (i) its acquisition or disposal, (ii) any change in previously disclosed interest (*e.g.*, when Shares acquired at vesting are sold), or (iii) becoming a director.

Insider Trading Notification. Participant should be aware of the Singaporean insider-trading rules, which may impact Participant's acquisition or disposal of Shares or rights to Shares under the Plans. Under the Singaporean insider-trading rules, Participant is prohibited from acquiring or selling Shares or rights to Shares (*e.g.*, an Award under the Plans) when he or she is in possession of information which is not generally available and which Participants knows or should know will have a material effect on the price of Shares once such information is generally available.

Slovenia

There are no country-specific provisions.

South Africa

Terms and Conditions

Withholding Taxes. This provision supplements Section 8 of the Award Agreement:

By accepting the PSUs, Participant agrees to immediately notify the Employer of the amount of any gain realized upon vesting of the PSUs. If Participant fails to advise the Employer of the gain realized at vesting, Participant may be liable for a fine. Participant will be responsible for paying any difference between the actual tax liability and the amount withheld.

Notifications

Exchange Control Information. Participant is solely responsible for complying with applicable South African exchange control regulations. Since the exchange control regulations change frequently and without notice, Participant should consult Participant's legal advisor prior to the acquisition or sale of Shares acquired under the Plans to ensure compliance with current regulations. As noted, it is Participant's responsibility to comply with South African exchange control laws, and neither the Company nor any Parent or Subsidiary will be liable for any fines or penalties resulting from Participant's failure to comply with applicable laws.

Spain

Terms and Conditions

Nature of Grant. This provision supplements Section 12 of the Award Agreement:

By accepting the PSUs, Participant consents to participation in the Plans and acknowledges that Participant has received a copy of the Plans.

Participant understands that the Company has unilaterally, gratuitously, and in its sole discretion decided to grant PSUs under the Plans to individuals who may be Service Providers throughout the world. The decision is a limited decision that is entered into upon the express assumption and condition that any grant will not bind the Company or any Parent or Subsidiary, other than to the extent set forth in this Award Agreement. Consequently, Participant understands that the PSUs are granted on the assumption and condition that the PSUs and any Shares acquired at vesting of the PSUs are not part of any employment or service contract (either with the Company or any Parent or Subsidiary), and shall not be considered a mandatory benefit, salary for any purposes (including severance compensation), or any other right whatsoever. In addition, Participant understands that this grant would not be made but for the assumptions and conditions referred to above; thus, Participant acknowledges and freely accepts that, should any or all of the assumptions be mistaken or should any of the conditions not be met for any reason, then any grant of or right to the PSUs shall be null and void.

Further, except as otherwise provided in the Plans and the Award Agreement, Participant understands that he or she will not be entitled to continue vesting in any PSUs once Participant's status as a Service Provider terminates. This will be the case, for example, even in the event of a termination of Participant's status of a Service Provider by reason of, but not limited to, resignation, retirement, disciplinary dismissal adjudged to be with cause, disciplinary dismissal adjusted or recognized to be without cause, individual or collective dismissal or objective grounds, whether adjudged or recognized to be without cause, material modification of the terms of employment under Article 41 of the Workers' Statute, relocation under Article 40 of the Workers' Statute, Article 50 of the Workers' Statute, unilateral withdrawal by the Employer and under Article 10.3 of the Royal Decree 1382/1985. Participant acknowledges that Participant has read and specifically accepts the vesting and termination conditions in the Award Agreement.

Notifications

Securities Law Information. The PSUs do not qualify under Spanish Law as securities. No “offer to the public,” as defined under Spanish Law, has taken place or will take place in the Spanish territory. Neither the Plans nor the Award Agreement have been registered with the *Comisión Nacronal del Mercado de Valores* and do not constitute a public offering prospectus.

Exchange Control Information. Participant must declare the acquisition of Shares to the *Spanish Dirección General de Comercio e Inversiones* (the “DGCI”), the Bureau for Commerce and Investments, which is a department of the Ministry of Economy and Competitiveness. Participant must also declare ownership of any Shares by filing a Form D-6 with the Directorate of Foreign Transactions each January while the Shares are owned. In addition, the sale of Shares must also be declared on Form D-6 filed with the DGCI in January, unless the sale proceeds exceed the applicable threshold (currently €1,502,530), in which case, the filing is due within one month after the sale.

When receiving foreign currency payments derived from the ownership of Shares exceeding €50,000 (*e.g.*, dividends or sale proceeds), Participant must inform the financial institution receiving the payment of the basis upon which such payment is made. Participant will need to provide the institution with the following information: (i) Participant's name, address, and fiscal identification number; (ii) the name and corporate domicile of the Company; (iii) the amount of the payment; (iv) the currency used; (v) the country of origin; (vi) the reasons for the payment; and (vii) any further information that may be required.

In addition, Participant may be required to declare electronically to the Bank of Spain any foreign accounts (including brokerage accounts held abroad), any foreign instruments (including any Shares acquired under the Plans) and any transactions with non-Spanish residents (including any payments of Shares made to Participant by the Company) depending on the value of such accounts and instruments and the amount of the transactions during the relevant year as of December 31 of the relevant year.

Tax Reporting Information. If Participant holds rights or assets (*e.g.*, Shares or cash held in a bank or brokerage account) outside of Spain with a value in excess of €50,000 per type of right or asset (*e.g.*, Shares, cash, etc.) as of December 31 each year, Participant is required to report certain information regarding such rights and assets on tax form 720. After such rights and/or assets are initially reported, the reporting obligation will apply for subsequent years only if the value of any previously-reported rights or assets increases by more than €20,000. The reporting must be completed by the March 31 each year.

Sweden

There are no country-specific provisions.

Switzerland

Notifications

Securities Law Information. The offering of PSUs is considered a private offering in Switzerland and is, therefore, not subject to registration in Switzerland.

Taiwan

Notifications

Exchange Control Information. Participant may acquire and remit foreign currency (including proceeds from the sale of Shares or the receipt of dividends) up to US$5,000,000 per year without justification.

If the transaction amount is TWD500,000 or more in a single transaction, Participant must submit a Foreign Exchange Transaction Form. If the transaction amount is US$500,000 or more in a single transaction, Participant must also provide supporting documentation to the satisfaction of the remitting bank.

Thailand

Notifications

Exchange Control Information. If the proceeds from the sale of Shares or the receipt of dividends are equal to or greater than US$50,000 in a single transaction, Participant must repatriate the proceeds to Thailand immediately upon receipt and to convert the funds to Thai Baht or deposit the proceeds in a foreign currency deposit account maintained by a bank in Thailand within 360 days of remitting the proceeds to Thailand. In addition, Participant must specifically report the inward remittance to the Bank of Thailand on a Foreign Exchange Transaction Form.

If Participant does not comply with this obligation, Participant may be subject to penalties assessed by the Bank of Thailand. Because exchange control regulations change frequently and without notice, Participant should consult a legal advisor before selling Shares to ensure compliance with current regulations. It is Participant's responsibility to comply with exchange control laws in Thailand, and neither the Company nor any Parent or Subsidiary will be liable for any fines or penalties resulting from Participant's failure to comply with applicable laws.

Tunisia

Terms and Conditions

Settlement of PSUs and Sale of Shares. Due to local regulatory requirements, upon the vesting of the PSUs, Participant agrees to the immediate sale of any Shares to be issued to him or her upon vesting and settlement of the PSUs. Participant further agrees that the Company is authorized to instruct its designated broker to assist with the mandatory sale of such Shares (on Participant's behalf pursuant to this authorization) and Participant expressly authorizes the Company's designated broker to complete the sale of such Shares. Participant acknowledges that the Company's designated broker is under no obligation to arrange for the sale of the Shares at any particular price. Upon the sale of the Shares, the Company agrees to pay Participant the cash proceeds from the sale of the Shares, less any brokerage fees or commissions and subject to any obligation to satisfy Tax-Related Items. Participant acknowledges that he or she are not aware of any material nonpublic information with respect to the Company or any securities of the Company as of the date of the Award Agreement.

Notifications

Exchange Control Information. All proceeds from the sale of Shares as described above must be repatriated to Tunisia. Participant should consult his or her personal advisor before taking action with respect to remittance of proceeds into Tunisia. Participant is responsible for ensuring compliance with all exchange control laws in Tunisia. In addition, if Participant holds assets abroad in excess of 500 Tunisian Dinars, Participant must report the assets to the Central Bank of Tunisia.

Turkey

Notifications

Securities Law Information. Under Turkish law, the Participant is not permitted to sell Shares acquired under the Plans in Turkey. The Shares are currently traded on the Nasdaq Global Select Market, which is located outside of Turkey, under the ticker symbol “FTNT” and the Shares may be sold through this exchange.

Exchange Control Information. Participant likely will be required to engage a Turkish financial intermediary to assist with the sale of Shares acquired under the Plans and may also need to engage a Turkish financial intermediary with respect to the acquisition of such Shares, although this is less certain. As Participant is solely responsible for complying with the financial intermediary requirements and their application to participation in the Plans is uncertain, Participant should consult his or her personal legal advisor prior to the vesting of the PSUs or any sale of Shares to ensure compliance.

United Arab Emirates

Notifications

Securities Law Information. Participation in the Plans is being offered only to selected Service Providers and is in the nature of providing equity incentives to Service Providers in the United Arab Emirates. The Plans and the Award Agreement are intended for distribution only to such Service Providers and must not be delivered to, or relied on by, any other person. Prospective purchasers of the securities offered should conduct their own due diligence on the securities. If Participant does not understand the contents of the Plans and the Award Agreement, Participant should consult an authorized financial adviser. The Emirates Securities and Commodities Authority has no responsibility for reviewing or verifying any documents in connection with the Plans. Neither the Ministry of Economy nor the Dubai Department of Economic Development have approved the Plans or the Award Agreement nor taken steps to verify the information set out therein, and have no responsibility for such documents.

United Kingdom

Terms and Conditions

PSUs Payable Only in Shares. Notwithstanding any discretion in the Plans or anything to the contrary in the Award Agreement, the grant of PSUs does not provide any right for Participant to receive a cash payment, and the PSUs are payable in Shares only.

Withholding Taxes. This provision supplements Section 8 of the Award Agreement:

If payment or withholding of the income tax due is not made within ninety (90) days of the event giving rise to the income tax, or such other period specified in Section 222(1)(c) of the U.K. Income Tax (Earnings and Pensions) Act 2003 (the “Due Date”), the amount of any uncollected income tax shall constitute a loan owed by Participant to the Employer, effective on the Due Date. Participant agrees that the loan will bear interest at the then-current Official Rate of Her Majesty's Revenue & Customs (“HMRC”), it will be immediately due and repayable, and the Company or the Employer may recover it at any time thereafter by any of the means referred to in Section 8 of the Award Agreement.

Notwithstanding the foregoing, if Participant is a director or executive officer of the Company (within the meaning of Section 13(k) of the U.S. Securities and Exchange Act of 1934, as amended), Participant shall not be eligible for a loan from the Company to cover the income tax. In the event that Participant is a director or executive officer and income tax not collected from or paid by Participant by the Due Date, the amount of any uncollected income tax will constitute a benefit to Participant on which additional income tax and national insurance contributions (“NICs”) may be payable. Participant acknowledges that Participant ultimately will be responsible for reporting and paying any income tax due on this additional benefit directly to HMRC under the self-assessment regime and for reimbursing the Company or the Employer (as applicable) for the value of any employee NICs due on this additional benefit, which the Company and/or the Employer may recover from Participant at any time thereafter by any of the means referred to in Section 8 of the Award Agreement.

Joint Election for Transfer of the Employer's Secondary Class 1 NICs Liability to the Participant. As a condition of vesting in the PSUs, Participant agrees to accept any liability for secondary Class 1 NICs, which may be payable by the Company or the Employer in connection with the PSUs (“Employer NICs”). Without limitation to the foregoing, Participant agrees to enter into an election between Participant and the Company or the Employer (the “Election”), in the form approved for such Election by HMRC, and any other consents or elections required to accomplish the transfer of the Employer NICs to Participant, prior to vesting of the PSUs. Participant further agrees to enter into such other joint elections as may be required between Participant and any successor to the Company and/or the Employer. If Participant does not enter into the Election prior to the vesting of the PSUs, Participant shall, without any liability to the Company or any Parent or Subsidiary, not be entitled to vest in the PSUs.

Participant further agrees that the Company and/or the Employer may collect the Employer NICs by any of the means set forth in Section 8 of the Award Agreement, as supplemented above.