FARMER BROTHERS CO
Form DEF 14A
October 28, 2010

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

SCHEDULE 14A

(Rule 14a-101)

INFORMATION REQUIRED IN PROXY STATEMENT

SCHEDULE 14A INFORMATION

Proxy Statement Pursuant to Section 14(a) of the

Securities Exchange Act of 1934

(Amendment No.___)

Filed by the Registrant x Filed by a Party other than the Registrant ¨
Check the appropriate box:

¨ Preliminary Proxy Statement

¨ **Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**

x Definitive Proxy Statement

¨ Definitive Additional Materials

¨ Soliciting Material Pursuant to §240.14a-12

FARMER BROS. CO.

(Name of Registrant as Specified in its Charter)

(Name of Person(s) Filing Proxy Statement, if Other Than the Registrant)

Payment of Filing Fee (Check the appropriate box):

x No fee required.

¨ Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

(1) Title of each class of securities to which transaction applies:

(2) Aggregate number of securities to which transaction applies:

(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

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(1) Amount Previously Paid:

(2) Form, Schedule or Registration Statement No.:

(3) Filing Party:

(4) Date Filed:

FARMER BROS. CO.

20333 South Normandie Avenue

Torrance, California 90502

NOTICE OF ANNUAL MEETING OF STOCKHOLDERS

TO BE HELD ON DECEMBER 9, 2010

TO THE STOCKHOLDERS OF FARMER BROS. CO.:

NOTICE IS HEREBY GIVEN that the 2010 Annual Meeting of Stockholders (the Annual Meeting) of Farmer Bros. Co., a Delaware corporation (the Company or Farmer Bros.), will be held at the principal office of the Company located at 20333 South Normandie Avenue, Torrance, California 90502, on Thursday, December 9, 2010, at 10:00 a.m., Pacific Standard Time, for the following purposes:

1. To elect three Class I directors to the Board of Directors of the Company for a three-year term of office expiring at the 2013 Annual Meeting of Stockholders;

2. To ratify the selection of Ernst & Young LLP as the Company s independent registered public accounting firm for the fiscal year ending June 30, 2011; and

3. To transact such other business as may properly come before the Annual Meeting or any continuation, postponement or adjournment thereof.

The foregoing items of business are more fully described in the Proxy Statement accompanying this Notice of Annual Meeting of Stockholders.

The Board of Directors has fixed the close of business on October 15, 2010 as the record date for the determination of stockholders entitled to notice of, and to vote at, the Annual Meeting and at any continuation, postponement or adjournment thereof.

By Order of the Board of Directors

John M. Anglin

Secretary

Torrance, California

October 28, 2010

IMPORTANT NOTICE REGARDING THE AVAILABILITY OF PROXY MATERIALS

FOR THE STOCKHOLDER MEETING TO BE HELD ON DECEMBER 9, 2010

The accompanying Proxy Statement and the Company s 2010 Annual Report on

Form 10-K, as amended, are available at: *http://proxy.farmerbros.com.*

PLEASE SUBMIT A PROXY AS SOON AS POSSIBLE SO THAT YOUR SHARES CAN BE VOTED AT THE ANNUAL MEETING IN ACCORDANCE WITH YOUR INSTRUCTIONS. FOR SPECIFIC INSTRUCTIONS ON VOTING, PLEASE REFER TO THE INSTRUCTIONS ON THE PROXY CARD OR THE INFORMATION FORWARDED BY YOUR BROKER, BANK OR OTHER NOMINEE. ESOP PARTICIPANTS SHOULD FOLLOW THE INSTRUCTIONS PROVIDED BY THE ESOP TRUSTEE, GREATBANC TRUST COMPANY. EVEN IF YOU HAVE VOTED YOUR PROXY, YOU MAY STILL VOTE IN PERSON IF YOU ATTEND THE ANNUAL MEETING. PLEASE NOTE, HOWEVER, THAT IF YOUR SHARES ARE HELD OF RECORD BY A BROKER, BANK OR OTHER NOMINEE AND YOU WISH TO VOTE IN PERSON AT THE ANNUAL MEETING, YOU MUST OBTAIN A PROXY ISSUED IN YOUR NAME FROM SUCH BROKER, BANK OR OTHER NOMINEE.

YOUR VOTE IS VERY IMPORTANT. PLEASE SUBMIT YOUR PROXY EVEN IF YOU PLAN TO ATTEND THE ANNUAL MEETING.

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FARMER BROS. CO.

20333 South Normandie Avenue

Torrance, California 90502

PROXY STATEMENT

INFORMATION CONCERNING VOTING AND SOLICITATION

General

The enclosed proxy is solicited on behalf of the Board of Directors (the Board of Directors or the Board) of Farmer Bros. Co., a Delaware corporation (the Company or Farmer Bros.), for use at the 2010 Annual Meeting of Stockholders (the Annual Meeting) to be held on Thursday, December 9, 2010, at 10:00 a.m., Pacific Standard Time, or at any continuation, postponement or adjournment thereof, for the purposes discussed in this Proxy Statement and in the accompanying Notice of Annual Meeting of Stockholders, and any business properly brought before the Annual Meeting. Proxies are solicited to give all stockholders of record an opportunity to vote on matters properly presented at the Annual Meeting. The approximate date on which this Proxy Statement, the accompanying proxy card and Annual Report to Stockholders (which is not part of the Company s soliciting materials) are being mailed to the Company s stockholders is November 1, 2010. The Annual Meeting will be held at the principal office of the Company located at 20333 South Normandie Avenue, Torrance, California 90502. If you plan to attend the Annual Meeting in person, you can obtain directions to the Company s principal office at *http://proxy.farmerbros.com*.

Solicitation of Proxies

The Company will bear the entire cost of solicitation of proxies, including preparation, assembly and mailing of this Proxy Statement, the proxy and any additional information furnished to stockholders. Copies of solicitation materials will be furnished to banks, brokerage houses, fiduciaries and custodians holding shares of Farmer Bros. common stock (Common Stock) in their names that are beneficially owned by others to forward to those beneficial owners. The Company may reimburse persons representing beneficial owners for their costs of forwarding the solicitation materials to the beneficial owners. Original solicitation of proxies by mail may be supplemented by telephone, facsimile, electronic mail or personal solicitation by directors, officers or employees of the Company. No additional compensation will be paid to directors, officers or employees for such services. A list of stockholders entitled to vote at the Annual Meeting will be available for examination by any stockholder for any purpose germane to the Annual Meeting during ordinary business hours at the offices of the Company located at 20333 South Normandie Avenue, Torrance, California 90502 for the ten days prior to the Annual Meeting and also at the Annual Meeting.

What Am I Voting On?

You will be entitled to vote on the following proposals at the Annual Meeting:

- The election of three Class I directors to serve on our Board for a three-year term of office expiring at the 2013 Annual Meeting of Stockholders; and

The ratification of the selection of Ernst & Young LLP (EY) as our independent registered public accounting firm for the fiscal year ending June 30, 2011.

Who Can Vote?

You are entitled to vote if you are a stockholder of record of Common Stock as of the close of business on October 15, 2010. Your shares may be voted at the Annual Meeting only if you are present in person or represented by a valid proxy.

Shares Outstanding and Quorum

At the close of business on October 15, 2010, 16,156,861 shares of Common Stock were outstanding and entitled to vote at the Annual Meeting. The Company has no other class of securities outstanding. A majority of the outstanding shares of Common Stock, present in person or represented by proxy, will constitute a quorum at the Annual Meeting, which is required in order to hold the Annual Meeting and conduct business. Your shares are counted as present at the Annual Meeting if you: (i) are present in person at the Annual Meeting; or (ii) have properly submitted a proxy card by mail. If you submit your proxy but abstain from voting on one or more matters, your shares will be counted as present at the Annual Meeting for the purpose of determining a quorum. Your shares also will be counted as present at the Annual Meeting for the purpose of calculating the vote on the particular matter with respect to which you abstained from voting. If your shares are held in street name, your shares are counted as present for purposes of determining a quorum if your broker, bank or other nominee submits a proxy covering your shares. Your broker, bank or other nominee is entitled to submit a proxy covering your shares as to certain routine matters, even if you have not instructed your broker, bank or other nominee on how to vote on such matters.

Voting of Shares

Stockholders of record as of the close of business on October 15, 2010 are entitled to one vote for each share of Common Stock held on all matters to be voted upon at the Annual Meeting. There is no cumulative voting in the election of our directors. You may vote by attending the Annual Meeting and voting in person. You may also vote by completing and mailing the enclosed proxy card or the form forwarded by your bank, broker or other nominee. If your shares are held by a bank, broker or other nominee, please refer to the instructions they provide for voting your shares. Participants in the Farmer Bros. Co. Employee Stock Ownership Plan (the ESOP) should follow the instructions provided by the ESOP trustee, GreatBanc Trust Company. All shares entitled to vote and represented by properly executed proxies received before the polls are closed at the Annual Meeting, and not revoked or superseded, will be voted at the Annual Meeting in accordance with the instructions indicated on those proxies.

YOUR VOTE IS VERY IMPORTANT. PLEASE SUBMIT YOUR PROXY EVEN IF YOU PLAN TO ATTEND THE ANNUAL MEETING.

Voting Instructions by ESOP Participants

The ESOP owns approximately 17.5% of the outstanding Common Stock. Full time employees of Farmer Bros. and its subsidiaries participate in the ESOP. Each ESOP participant has the right to direct the ESOP trustee on how to vote the shares of Common Stock allocated to his or her account under the ESOP. Shares of Common Stock allocated to participant accounts for which properly executed voting instructions have been received by the ESOP trustee will be voted by the ESOP trustee in the manner directed or, in the absence of any direction, FOR each nominee named in Item 1 and FOR Item 2, and in accordance with the discretion of the ESOP trustee on such other matters as may properly come before the Annual Meeting, including any continuation, postponement or adjournment thereof, and any other matters incident to the conduct of the Annual Meeting. The ESOP trustee will vote all of the unallocated ESOP shares (i.e., shares of Common Stock held in the ESOP, but not allocated to any participant s account) and allocated shares for which no voting directions are timely received by the ESOP trustee in the same proportion as the voted allocated shares with respect to each item.

Counting of Votes

All votes will be tabulated by the inspector of election appointed for the Annual Meeting, who will separately tabulate affirmative and negative votes, abstentions and broker non-votes. Shares held by persons attending the Annual Meeting but not voting, shares represented by proxies that reflect abstentions as to one or more proposals and broker non-votes will be counted as present for purposes of determining a quorum. A broker non-vote occurs when a nominee holding shares for a beneficial owner has not received instructions from the beneficial owner and does not have discretionary authority to vote the shares. If you hold your shares in street name and do not provide voting instructions to your bank, broker or other nominee, your shares will be considered to be broker non-votes and will not be voted on any proposal on which your bank, broker or other nominee does not have discretionary authority to vote. Shares that constitute broker non-votes will be counted as present at the Annual Meeting for purposes of determining a quorum, but will not be considered entitled to vote on the proposal in question. Brokers generally have discretionary authority to vote on the ratification of the selection of EY as our independent registered public accounting firm.

Directors are elected by a plurality of the votes cast. This means that the three individuals nominated for election to the Board at the Annual Meeting who receive the largest number of properly cast FOR votes (among votes properly cast in person or by proxy) will be elected as directors. In director elections, stockholders may either vote FOR or withhold voting authority with respect to director nominees. Shares voting withhold are counted for purposes of determining a quorum. However, if you withhold authority to vote with respect to the election of some or all of the nominees, your shares will not be voted with respect to those nominees indicated. Therefore, withhold votes will not affect the outcome of the election of directors. Brokers do not have discretionary authority to vote on the election of directors. Broker non-votes and abstentions will have no effect on the election of directors.

The ratification of the selection of EY requires the affirmative vote of a majority of the shares present or represented by proxy at the Annual Meeting and entitled to vote on the matter. Abstentions will have the same effect as votes against the ratification. Because brokers have discretionary authority to vote on the ratification, we do not expect any broker non-votes in connection with the ratification.

If You Receive More Than One Proxy Card

If you receive more than one proxy card, it means you hold shares that are registered in more than one account. To ensure that all of your shares are voted, sign and return each proxy card.

Proxy Card and Revocation of Proxy

You may vote by completing and mailing the enclosed proxy card. If you sign the proxy card but do not specify how you want your shares to be voted, your shares will be voted by the proxy holders named in the enclosed proxy: (i) in favor of the election of all of the director nominees; and (ii) in favor of ratification of the selection of EY as the Company s independent registered public accounting firm for the fiscal year ending June 30, 2011. In their discretion, the proxy holders named in the enclosed proxy are authorized to vote on any other matters that may properly come before the Annual Meeting and at any continuation, postponement or adjournment thereof. The Board of Directors knows of no other items of business that will be presented for consideration at the Annual Meeting other than those described in this Proxy Statement. In addition, no stockholder proposal or nomination was received on a timely basis, so no such matters may be brought to a vote at the Annual Meeting.

If you vote by proxy, you may revoke that proxy at any time before it is voted at the Annual Meeting. Stockholders of record may revoke a proxy by sending to the Company s Secretary at the Company s principal office at 20333 South Normandie Avenue, Torrance, California 90502, a written notice of revocation or a duly executed proxy bearing a later date or by attending the Annual Meeting in person and voting in person. Attendance at the Annual Meeting will not, by itself, revoke a proxy.

If your shares are held in the name of a bank, broker or other nominee, you may change your vote by submitting new voting instructions to your bank, broker or other nominee. Please note that if your shares are held of record by a bank, broker or other nominee, and you decide to attend and vote at the Annual Meeting, your vote in person at the Annual Meeting will not be effective unless you present a legal proxy, issued in your name from the record holder, your bank, broker or other nominee.

Board Recommendations

The Board recommends that you vote your shares as follows:

- FOR the election of three Class I directors to serve on our Board for a three-year term of office expiring at the 2013 Annual Meeting of Stockholders; and

- FOR the ratification of the selection of Ernst & Young LLP as our independent registered public accounting firm for the fiscal year ending June 30, 2011.

ITEM 1

ELECTION OF DIRECTORS

General

Under the Company s Certificate of Incorporation and Amended and Restated Bylaws (the Bylaws), the Board of Directors is divided into three classes, each class consisting, as nearly as possible, of one-third of the total number of directors, with members of each class serving for a three-year term. Each year only one class of directors is subject to a stockholder vote. Class I presently consists of three directors whose term of office expires at the Annual Meeting and whose successors will be elected at the Annual Meeting to serve until the 2013 Annual Meeting of Stockholders. Class II consists of two directors, continuing in office until the 2011 Annual Meeting of Stockholders. Class III consists of two directors, continuing in office until the 2012 Annual Meeting of Stockholders.

The authorized number of directors is set forth in the Company s Certificate of Incorporation and shall consist of not less than five or more than seven members, the exact number of which shall be fixed from time to time by resolution of the Board. The authorized number of directors is currently seven. If the number of directors is changed, any increase or decrease will be apportioned among the classes so as to maintain the number of directors in each class as nearly equal as possible. Any vacancy on the Board of Directors that results from an increase in the number of directors may be filled by a majority of the Board of Directors then in office, provided that a quorum is present, and any other vacancy occurring on the Board of Directors may be filled by a majority of the Board of Directors then in office, even if less than a quorum, or by the sole remaining director. Any director of any class elected to fill a vacancy resulting from an increase in the number of directors of such class will hold office for a term that will coincide with the remaining term of that class. Any director elected to fill a vacancy not resulting from an increase in the number of directors will have the same remaining term as that of his or her predecessor.

Based on the recommendation of the Nominating Committee, the Board has nominated Roger M. Laverty III, Martin A. Lynch and James J. McGarry for re-election to the Board as Class I directors. If elected at the Annual Meeting, each would serve until the 2013 Annual Meeting of Stockholders and until his successor is elected and qualified, subject, however, to prior death, resignation, retirement, disqualification or removal from office. No nominations were made by stockholders.

All of the present directors were elected to their current terms by the stockholders. There are no family relationships among any current directors of the Company, or among any current directors and executive officers of the Company. Other than as disclosed in the tables below, none of the directors is a director of any other publicly-held company. None of our directors has been convicted in any criminal proceeding during the past ten years or is a party to any judicial or administrative proceeding during the past ten years that resulted in a judgment, decree or final order enjoining them from future violations of, or prohibiting activities subject to, federal or state securities laws or a finding of any violation of federal or state securities laws or commodities laws. Similarly, no bankruptcy petitions have been filed by or against any business or property of any of our directors or officers, nor has any bankruptcy petition been filed against a partnership or business association in which these persons were general partners, directors or executive officers.

Vote Required

Each share of Common Stock is entitled to one vote for each of the three director nominees and will be given the option of voting FOR or withholding authority to vote for each nominee. Cumulative voting is not permitted. It is the intention of the proxy holders named in the enclosed proxy to vote the proxies received by them for the election of the three nominees named below unless the proxies direct otherwise. If any nominee should become unavailable for election prior to the Annual Meeting, an event that currently is not anticipated by the Board, the proxies will be voted for the election of a substitute nominee or nominees proposed by the Board of Directors. Each nominee has agreed to serve if elected, and the Board of Directors has no reason to believe that any nominee will be unable to serve.

Directors are elected by a plurality of the votes cast. This means that the three individuals nominated for election to the Board at the Annual Meeting who receive the largest number of properly cast FOR votes (among votes properly cast in person or by proxy) will be elected as directors. In director elections, stockholders may either vote FOR or withhold voting authority with respect to director nominees. Shares voting withhold are counted for purposes of determining a quorum. However, if you withhold authority to vote with respect to the election of some or all of the nominees, your shares will not be voted with respect to those nominees indicated. Therefore, withhold votes will not affect the outcome of the election of directors. Brokers do not have discretionary authority to vote on the election of directors. Broker non-votes and abstentions will have no effect on the election of directors.

Nominees for Election as Directors

Set forth below is biographical information for each nominee for election as a Class I director at the Annual Meeting and a summary of the specific qualifications, attributes, skills and experiences which led our Board to conclude that the individual should be re-nominated to serve on the Board.

Name	Age	Director Since	Audit Committee	Compensation Committee	Nominating Committee
Roger M. Laverty III	63	2007			
Martin A. Lynch	73	2007	X		X
James J. McGarry	57	2007		X	X

Roger M. Laverty III joined Farmer Bros. in 2006, as the fifth chief executive to lead the Company since its founding in 1912. Under Mr. Laverty s leadership, the Company has positioned itself as one of the nation s largest direct-store delivery (DSD) businesses for coffee, tea and culinary products, including the acquisition of the DSD Coffee Business from Sara Lee in 2009, and the acquisition of Coffee Bean International, Inc. (CBI), one of the nation s leading roasters and wholesalers of specialty coffee, in 2007. Since joining Farmer Bros., Mr. Laverty has also focused on operational improvements through programs intended to enhance the efficiency and flexibility of the Company s manufacturing processes and supply chain, and initiatives intended to strengthen sales and branding. From 2003 to 2005, Mr. Laverty served as President and CEO of Diedrich Coffee, Inc., a diversified operator of coffee houses and franchises that was known for its expertise and traditions in specialty coffee. Earlier, Mr. Laverty served 20 years with retailer Smart & Final, Inc., an operator of non-membership grocery warehouse stores for food and foodservice supplies, playing key roles in the growth of its sales from $200 million to more than $1.4 billion. He served as President and CEO of Smart & Final from 1993 to 1998. Mr. Laverty received his undergraduate and law degrees from Stanford University. Mr. Laverty s knowledge regarding the Company s operations and the markets and industries in which we compete provides a critical link between management and the Board of Directors, enabling the Board to provide its oversight function with the benefit of management s perspective of the business.

Martin A. Lynch is currently the President of Claremorris Consulting, a privately-owned consulting company helping privately-held and publicly-held companies in the areas of strategic and financial projects, and has been serving in this capacity since 2002. From 2003 to 2005, Mr. Lynch served as the Executive Vice President and Chief Financial Officer of Diedrich Coffee, Inc. From 2001 to 2003, he served as a consultant to Smart & Final on strategic and financial projects. For twelve years, from 1989 to 2001, he served as Executive Vice President and Chief Financial Officer of Smart & Final. From 1984 to 1989, Mr. Lynch was Executive Vice President and Chief Financial Officer of San Francisco-based Duty Free Shoppers Group, Ltd. (retail). He served in a number of key positions with Los Angeles-based Tiger International (transportation and financial services) from 1970 to 1984 including the position of Senior Vice President, Chief Financial Officer from 1976 to 1984. Mr. Lynch s earlier experience includes merger and acquisition activities at Scot Lad Foods, Inc. (retail grocery) and service as audit manager for Price Waterhouse & Company (accounting) in Chicago. Mr. Lynch received his undergraduate degree from De Paul University and received his Certified Public Accountant designation in Illinois. Mr. Lynch s background and experience, particularly in the foodservice business, provide him with an understanding of our business, operations, financial results and prospects.

James J. McGarry has been a partner in the law firm of McGarry & Laufenberg, El Segundo, California, since 1995, and was a partner in other law firms bearing his name since 1984. A licensed attorney since 1980, his experience has been as a litigator and a mediator, specializing in business, tort and contract litigation. Mr. McGarry received his undergraduate degree from Loyola Marymount University and his law degree from Loyola Law School. Mr. McGarry s extensive legal and business experience provide him with an understanding of the Company s operations.

THE BOARD RECOMMENDS A VOTE FOR EACH OF THE THREE NAMED NOMINEES.

Directors Continuing in Office

Set forth below is biographical information for each director continuing in office and a summary of the specific qualifications, attributes, skills and experiences which led our Board to conclude that the individual should serve on the Board.

Name	Age	Director Since	Class	Term Expires	Audit Committee	Compensation Committee	Nominating Committee
Guenter W. Berger	73	1980	II	2011			
Jeanne Farmer Grossman	60	2009	III	2012		X	X
Thomas A. Maloof	58	2003	II	2011	X	Chair	X
John H. Merrell	66	2001	III	2012	Chair	X	X

Guenter W. Berger retired in December 2007 as Chief Executive Officer of Farmer Bros. after more than 47 years of service with the Company in various capacities. Mr. Berger served as Chief Executive Officer of the Company from 2005 to 2007, President from August 2005 through July 2006, and Interim President and Chief Executive Officer from January 2005 to August 2005. For more than 25 years, from 1980 to 2005, Mr. Berger served as Vice President of Torrance inventory, production, coffee roasting and distribution operations. Based on his longstanding tenure with the Company, Mr. Berger has a deep understanding of our operations and has acquired extensive knowledge of the foodservice industry and the production and distribution processes related to coffee, tea and culinary products.

Jeanne Farmer Grossman is a retired teacher and a homemaker. She is the sister of Carol Farmer Waite, a former director, and the late Roy E. Farmer, who served as Chairman of the Board from 2004 to 2005, Chief Executive Officer from 2003 to 2005, and President from 1993 to 2005, and the daughter of the late Roy F. Farmer, who served as Chairman of the Board from 1951 to 2004 and Chief Executive Officer from 1951 to 2003. Ms. Grossman received her undergraduate degree and teaching credentials from the University of California at Los Angeles.

Thomas A. Maloof served as Chief Financial Officer of Hospitality Marketing Concepts, LLC, Newport Beach, California, a provider of loyalty membership programs for the hospitality and leisure industries, from January 2001 to August 2005, and has been an independent consultant since 2005. Mr. Maloof served as President of Perinatal Practice Management, Inc., a national genetic testing provider, from 1998 to 2000. Mr. Maloof currently serves as a director for PC Mall, Inc. (Nasdaq: MALL), a direct marketing company, and The Ensign Group (Nasdaq: ENSG), an operator of skilled nursing facilities. Mr. Maloof s background and experience provide management, public company corporate governance and financial experience to the Board.

John H. Merrell is a retired partner of the regional accounting and consulting firm of Hutchinson and Bloodgood LLP, Glendale, California. He was an active Partner in the firm from 1978 to 2008. He served as Managing Partner of the firm from 1988 to 2002. Prior to 1978, Mr. Merrell spent six years with an international public accounting firm both in the audit and tax departments. Mr. Merrell has also served as the Corporate Controller and then Chief Financial Officer of a publicly-held company in the international insurance industry. Mr. Merrell received his undergraduate degree in Accounting from San Jose State University, and is a Certified Public Accountant. Mr. Merrell s background and experience provide valuable management and leadership skills, as well as an understanding of the operations and financial results and prospects of the Company. Based on his experience, the Board has determined that he is an Audit Committee financial expert.

ITEM 2

RATIFICATION OF SELECTION

OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

General

The Audit Committee of the Board of Directors has selected Ernst & Young LLP (EY) as the independent registered public accounting firm for the Company and its subsidiaries for the fiscal year ending June 30, 2011, and has further directed that management submit this selection for ratification by the stockholders at the Annual Meeting. EY served as the Company s independent registered public accounting firm in fiscal 2010. A representative of EY is expected to be present at the Annual Meeting and will have the opportunity to make a statement and respond to appropriate questions.

Stockholder ratification of the selection of EY as the Company s independent registered public accounting firm is not required by the Bylaws or otherwise. However, the Board is submitting the selection of EY to stockholders for ratification because the Company believes it is a matter of good corporate practice. If the Company s stockholders fail to ratify the selection, the Audit Committee will reconsider whether or not to retain EY but still may retain them. Even if the selection is ratified, the Audit Committee in its discretion may direct the appointment of a different independent registered public accounting firm at any time during the year if the Audit Committee determines that such a change would be in our best interests and that of our stockholders.

Vote Required

The affirmative vote of a majority of the shares present in person or represented by proxy at the Annual Meeting and entitled to vote is required to ratify the selection of EY.

THE BOARD RECOMMENDS A VOTE FOR RATIFICATION OF THE SELECTION OF ERNST & YOUNG LLP AS THE COMPANY S INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM.

SECURITY OWNERSHIP OF

CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

Security Ownership of Certain Beneficial Owners

The following table sets forth certain information regarding the beneficial ownership of Common Stock as of October 15, 2010, by all persons (including any group as that term is used in Section 13(d)(3) of the Securities Exchange Act of 1934, as amended (the Exchange Act)) known by the Company to be the beneficial owner of more than five percent (5%) of the Common Stock as of such date, except as noted in the footnotes below:

Name and Address of Beneficial Owner(1)	Amount and Nature of Beneficial Ownership(2)	Percent of Class(3)
Farmer Group	6,402,895 shares(4)	39.6%
Employee Stock Ownership Plan	2,834,060 shares(5)	17.5%
Franklin Mutual Advisers, LLC	2,040,293 shares(6)	12.6%

(1) The address for Franklin Mutual Advisers, LLC (Franklin) is 101 John F. Kennedy Parkway, Short Hills, New Jersey 07078. The address for all other beneficial owners is c/o Farmer Bros. Co., 20333 South Normandie Avenue, Torrance, California 90502.

(2) For purposes of this table, beneficial ownership is determined in accordance with Rule 13d-3 under the Exchange Act. A person is deemed to be the beneficial owner of a security if that person has the right to acquire beneficial ownership of such security within 60 days. Information in this table regarding beneficial owners of more than five percent (5%) of the Common Stock is based on information provided by them or obtained from filings under the Exchange Act. Unless otherwise indicated in the footnotes, each of the beneficial owners of more than five percent (5%) of the Common Stock has sole voting and/or investment power with respect to such shares.

(3) The Percent of Class reported in this column has been calculated based upon the number of shares of Common Stock outstanding as of October 15, 2010 and may differ from the Percent of Class reported in statements of beneficial ownership filed with the Securities and Exchange Commission (the SEC).

(4) For purposes of Section 13 of the Exchange Act, Carol Farmer Waite, Richard F. Farmer, Jeanne Farmer Grossman, Trust A created under the Roy E. Farmer Trust dated October 11, 1957 (Trust A) and Farmer Equities, LP, a California limited partnership (Farmer Equities), comprise a group (the Farmer Group). The Farmer Group is deemed to be the beneficial owner of all shares beneficially owned by its members with shared power to vote and dispose of such shares. Each member of the Farmer Group is the beneficial owner of the following shares (in accordance with the beneficial ownership regulations, in certain cases the same shares of Common Stock are shown as beneficially owned by more than one individual or entity):

Name of Beneficial Owner	Total Shares Beneficially Owned	Percent of Class	Shares Disclaimed	Sole Voting and Investment Power	Shared Voting and Investment Power
Carol Farmer Waite	6,320,938 shares	39.1%	14,474 shares	22,720 shares	6,312,692 shares
Richard F. Farmer	6,294,419 shares	39.0%	39,891 shares	21,820 shares	6,312,490 shares
Jeanne Farmer Grossman	4,133,125 shares	25.6%	6,030 shares	11,723 shares	4,127,432 shares
Trust A	1,463,640 shares	9.1%		1,463,640 shares	
Farmer Equities	2,617,530 shares	16.2%		2,617,530 shares	

(5) Includes 1,550,341 allocated shares and 1,283,719 shares as yet unallocated to plan participants as of October 15, 2010. The ESOP trustee votes the shares held by the ESOP that are allocated to participant accounts as directed by the participants or beneficiaries of the ESOP.

Under the terms of the ESOP, the ESOP trustee will vote all of the unallocated ESOP shares (i.e., shares of Common Stock held in the ESOP, but not allocated to any participant s account) and allocated shares for which no voting directions are timely received by the ESOP trustee in the same proportion as the voted allocated shares with respect to each item. The present members of the ESOP Administrative Committee are Roger M. Laverty III, Martin A. Lynch and John H. Merrell. Each member of the ESOP Administrative Committee disclaims beneficial ownership of the securities held by the ESOP except for those, if any, that have been allocated to the member as a participant in the ESOP.

(6) The amount shown was provided by Franklin pursuant to a Schedule 13F filed by Franklin Resources, Inc. with the SEC on August 10, 2010. Franklin is reported to have sole voting and investment power over 2,040,293 shares beneficially owned by one or more open-end investment companies or other managed accounts which, pursuant to investment management contracts, are managed by Franklin. Franklin reports that it has sole voting and dispositive power over all of these shares.

Security Ownership of Directors and Executive Officers

The following table sets forth certain information regarding the beneficial ownership of Common Stock as of October 15, 2010, by: (i) each director and nominee; (ii) the Company s Chief Executive Officer, (iii) all individuals serving as the Company s Chief Financial Officer or acting in a similar capacity during fiscal 2010; (iv) the Company s most highly compensated executive officers (other than the Chief Executive Officer and Chief Financial Officer) who were serving as executive officers at the end of fiscal 2010; (v) one additional individual for whom disclosure would have been provided but for the fact that she was not serving as an executive officer of the Company at the end of fiscal 2010 (collectively, the Named Executive Officers); and (vi) all directors and executive officers of the Company as a group.

Name of Beneficial Owner	Amount and Nature of Beneficial Ownership(1)(2)	Percent of Class
Non-Employee Directors and Nominees		
Guenter W. Berger	17,557(3)	*
Jeanne Farmer Grossman	4,133,125(4)	25.6%
Martin A. Lynch	4,873(5)	*
Thomas A. Maloof	7,873(6)	*
James J. McGarry	4,873(5)	*
John H. Merrell	6,373(7)	*
Named Executive Officers		
Roger M. Laverty III	105,540(8)	*
Jeffrey A. Wahba	3,000	*
Peter B. Knepper		
John E. Simmons	20,652(9)	*
Drew H. Webb	9,000(10)	*
Hortensia R. Gómez	9,041(11)	*
Heidi L. Modaro	(12)	
All directors and executive officers as a group (14 individuals)	4,326,780	26.8%

* Less than 1%

(1) For purposes of this table, beneficial ownership is determined in accordance with Rule 13d-3 under the Exchange Act. A person is deemed to be the beneficial owner of a security if that person has the right to acquire beneficial ownership of such security within 60 days. Information in this table is based on the Company s records and information provided by directors, nominees, executive officers and in public filings. Unless otherwise indicated in the footnotes and subject to community property laws where applicable, each of the directors, nominees and executive officers has sole voting and/or investment power with respect to such shares, including shares held in trust.

(2) Includes (i) shares of restricted stock which have not yet vested as of October 15, 2010, awarded under the Farmer Bros. Co. 2007 Omnibus Plan (the Omnibus Plan) over which the individuals shown have voting power but no investment power, and (ii) shares which the individuals shown have the right to acquire upon the exercise of vested options as of October 15, 2010 or within 60 days thereafter as set forth in the table below. Such shares are deemed to be outstanding in calculating the percentage ownership of such individual (and the group), but are not deemed to be outstanding as to any other person.

Name	Vested Options (#)	Right to Acquire Under Vested Options Within 60 Days (#)	Restricted Stock (#)
Non-Employee Directors and Nominees			
Guenter W. Berger			3,542
Jeanne Farmer Grossman			2,173
Martin A. Lynch			3,542
Thomas A. Maloof			3,542
James J. McGarry			3,542
John H. Merrell			3,542
Named Executive Officers			
Roger M. Laverty III	40,001	37,609	24,372
Jeffrey A. Wahba			3,000
Peter B. Knepper			
John E. Simmons(a)	9,000		
Drew H. Webb(b)	9,000		
Hortensia R. Gómez	3,000	2,156	1,132
Heidi L. Modaro(c)			
Other Executive Officers			3,542

(a) Excludes 3,000 shares of restricted stock and 9,000 shares subject to unvested stock options previously granted to Mr. Simmons which were forfeited upon Mr. Simmons retirement from the Company on February 28, 2010.

(b) Excludes 6,458 shares of restricted stock and 31,542 shares subject to unvested stock options previously granted to Mr. Webb which were forfeited upon Mr. Webb s separation from the Company on September 17, 2010.

(c) Excludes 2,562 shares of restricted stock and 19,138 shares subject to unvested stock options previously granted to Ms. Modaro which were forfeited upon Ms. Modaro s separation from the Company on February 25, 2010.

(3) Includes 1,331 shares owned outright, 6,060 shares held in trust with voting and investment power shared by Mr. Berger and his wife, and 6,624 shares previously allocated to Mr. Berger under the ESOP which have been distributed to Mr. Berger and are now owned outright.

(4) Includes shares held in Farmer Equities and various family trusts of which Ms. Grossman (or a trust of which she is the sole trustee) is a general partner or the sole trustee, co-trustee, beneficiary and/or settlor. Ms. Grossman is the indirect beneficial owner of: (i) 9,550 shares of Common Stock as a successor trustee of a family trust for the benefit of her daughter over which she has sole voting and dispositive power; (ii) 2,617,530 shares of Common Stock as sole trustee of the Jeanne F. Grossman Trust, dated August 22, 1997, which is a general partner of Farmer Equities, and over which she has shared voting and dispositive power with trusts for the benefit of Carol Farmer Waite and Richard F. Farmer; and (iii) 1,509,902 shares of Common Stock as successor co-trustee of various family trusts, for the benefit of herself and family members, and over which she has shared voting and dispositive power with Carol Farmer Waite and/or Richard F. Farmer. Ms. Grossman disclaims beneficial ownership of 6,030 shares held in a trust for the

benefit of her nephew. Total beneficial ownership of the Farmer Group, which includes Ms. Grossman, is 6,402,895, as shown in the table above under the heading Security Ownership of Certain Beneficial Owners.

(5) Includes 1,331 shares owned outright.

(6) Includes 1,331 shares owned outright and 3,000 shares beneficially owned by Mr. Maloof through an IRA.

(7) Includes 1,331 shares owned outright and 1,500 shares held in a revocable living trust with voting and investment power shared by Mr. Merrell and his wife.

(8) Includes 1,000 shares held in a trust with voting and investment power shared by Mr. Laverty and his wife and 2,558 shares beneficially owned by Mr. Laverty through the ESOP, rounded to the nearest whole share.

(9) Includes 3,720 shares owned outright and 7,932 shares beneficially owned by Mr. Simmons through the ESOP, rounded to the nearest whole share.

(10) Excludes 1,471 shares allocated to Mr. Webb through the ESOP which were unvested and forfeited upon Mr. Webb s separation from the Company on September 17, 2010.

(11) Includes 129 shares held in a trust over which Ms. Gómez has sole voting and investment power and 2,624 shares beneficially owned by Ms. Gómez through the ESOP, rounded to the nearest whole share.

(12) Excludes 648 shares allocated to Ms. Modaro through the ESOP which were unvested and forfeited upon Ms. Modaro s separation from the Company on February 25, 2010.

CORPORATE GOVERNANCE

Board Independence

At least annually, the Board reviews the independence of each non-employee director and affirmatively determines whether each director qualifies as independent. The Board believes that stockholder interests are best served by having a number of objective, independent representatives on the Board. For this purpose, a director will be considered to be independent only if the Board affirmatively determines that the director has no relationship with the Company that would interfere with the exercise of independent judgment in carrying out the responsibilities of a director.

In making its independence determinations, the Board reviewed transactions and relationships between each director and nominee, or any member of his or her immediate family, and us or our subsidiaries based on information provided by the director or nominee, our records and publicly available information. The Board made the following independence determinations (the relationships and transactions reviewed by the Board in making such determinations are set forth in the footnotes below):

Director	Status
Guenter W. Berger	Not independent(1)
Jeanne Farmer Grossman	Independent(2)
Roger M. Laverty III	Not independent(3)
Martin A. Lynch	Independent(4)
Thomas A. Maloof	Independent(5)
James J. McGarry	Independent(6)
John H. Merrell	Independent(4)

(1) Mr. Berger is the Chairman and former Chief Executive Officer of the Company.

(2) Ms. Grossman is the sister of Carol Farmer Waite, a former director, and the sister of the late Roy E. Farmer and daughter of the late Roy F. Farmer, both of whom were executive officers of the Company more than three years ago. The Board considered these relationships and determined that such relationships do not interfere with Ms. Grossman s exercise of independent judgment in carrying out her responsibilities as a director.

(3) Mr. Laverty is the Company s President and Chief Executive Officer. Mr. Laverty s daughter is Producer Relationship Coordinator, a non-executive officer employee of CBI, a subsidiary of the Company. Her compensation is less than the threshold amount that would require disclosure as a related person transaction.

(4) The Board considered the membership of Messrs. Lynch and Merrell on the Company s ESOP Administrative Committee, and determined that such relationship does not interfere with their exercise of independent judgment in carrying out their responsibilities as directors.

(5) Mr. Maloof s son is a real estate salesperson employed by a real estate broker retained by the Company and may receive a commission in connection with the sale of real estate owned by the Company. Such commission, if any, is less than the threshold amount that would require disclosure as a related person transaction. The Board considered this relationship and transaction and determined that such relationship and transaction does not interfere with Mr. Maloof s exercise of independent judgment in carrying out his responsibilities as a director.

(6) Mr. McGarry is a partner in the law firm of McGarry & Laufenberg. During the last three fiscal years, McGarry & Laufenberg billed legal fees and costs to the Company and/or Liberty Mutual Insurance Company, the Company s insurance carrier, in connection with various matters relating to the Company. The foregoing amounts did not exceed the greater of 5% of McGarry & Laufenberg s gross revenues or

$200,000 during the applicable fiscal year. The Board considered these relationships and transactions and determined that such relationships and transactions do not interfere with Mr. McGarry s exercise of independent judgment in carrying out his responsibilities as a director.

Board Meetings and Attendance

The Board held five meetings during fiscal 2010, including four regularly scheduled and one special meeting. During fiscal 2010, each director attended at least 75% of the total number of meetings of the Board of Directors (held during the period for which he or she served as a director) and committees of the Board on which he or she served (during the periods that he or she served). Although it is customary for all Board members to attend, the Company has no formal policy in place with regard to Board members attendance at the Company s annual meeting of stockholders. All directors who were then serving were present at the 2009 Annual Meeting of Stockholders held on December 10, 2009 (the 2009 Annual Meeting).

The independent members of the Board met in executive session without management three times in fiscal 2010. Each independent director attended at least 75% of the total number of executive sessions (held during the period for which he or she served as a director) during fiscal 2010.

Charters; Code of Conduct and Ethics

The Board maintains charters for each of its standing committees, which include the Audit Committee, Compensation Committee and Nominating Committee. In addition, the Board has adopted a written Code of Conduct and Ethics for all employees, officers and directors. Current committee charters and the Code of Conduct and Ethics are available on the Company s website at *www.farmerbros.com*.

Board Committees

The Board maintains the following committees to assist it in discharging its oversight responsibilities:

Audit Committee

The Audit Committee is a standing committee of the Board established in accordance with Section 3(a)(58)(A) of the Exchange Act. The Audit Committee s principal purposes are to oversee the accounting and financial reporting processes of the Company and the audit of the Company s financial statements. The Committee s responsibilities include assisting the Board in overseeing: (i) the integrity of the Company s financial statements; (ii) the independent auditor s qualifications and independence; (iii) the performance of the Company s independent auditor; (iv) the Company s compliance with legal and regulatory requirements in connection with related person transactions; and (v) the Company s system of disclosure controls and system of internal financial, accounting and legal compliance controls. The Audit Committee is directly and solely responsible for the appointment, dismissal, compensation, retention and oversight of the work of any independent auditor engaged by the Company for the purpose of preparing or issuing an audit report or performing other audit, review or attest services for the Company. The independent auditor reports directly to the Audit Committee.

During fiscal 2010, the Audit Committee met seven times. John H. Merrell serves as Chairman, and Martin A. Lynch and Thomas A. Maloof currently serve as members of the Audit Committee. All members of the Audit Committee meet the Nasdaq composition requirements, including the requirements regarding financial literacy and financial sophistication, and the Board has determined that each member is independent under the Nasdaq listing standards and the rules of the SEC regarding audit committee membership. The Board has determined that at least one member of the Audit Committee is an audit committee financial expert as defined in Item 407(d) of Regulation S-K under the Exchange Act. That person is John H. Merrell, the Audit Committee Chairman.

Compensation Committee

Overview

The Compensation Committee is a standing committee of the Board. The Compensation Committee s principal purposes are to discharge the Board s responsibilities related to compensation of the Company s executive officers and administer the Company s incentive compensation plan for executive officers and the Company s equity compensation plan. The Compensation Committee also is responsible for evaluating and making recommendations to the Board regarding director compensation. In addition, the Compensation Committee is responsible for conducting an annual risk evaluation of the Company s compensation practices, policies and programs.

During fiscal 2010, the Compensation Committee met five times. Thomas A. Maloof serves as Chairman, and Jeanne Farmer Grossman, James J. McGarry and John H. Merrell currently serve as members of the Compensation Committee. The Board has determined that all Compensation Committee members are independent under the Nasdaq listing standards and the requirements of the SEC.

Executive Compensation

The processes and procedures of the Compensation Committee for considering and determining compensation for our executive officers are as follows:

Cash compensation for our executive officers is generally determined annually in the first quarter of the fiscal year, with any adjustments to base compensation retroactive to the beginning of the applicable fiscal year. Equity compensation is generally determined on the date of the regularly scheduled meeting of the Board of Directors in December of each year, with grants to executive officers hired or promoted since that grant date to receive an interim grant reviewed by the Board and approved by the Compensation Committee outside any blackout period under our insider trading policy.

In making determinations regarding executive officer compensation, the Compensation Committee considers competitive market data among several other factors such as Company performance, individual executive performance, tenure, the importance of the role at the Company and pay levels among the Company s executives, as well as input and recommendations of the Chief Executive Officer with respect to compensation for those executive officers reporting directly to him. The Compensation Committee has typically followed these recommendations. In the case of the Chief Executive Officer, the Compensation Committee may also solicit input from the other disinterested Board members.

In fiscal 2010, the Compensation Committee retained Mercer to update its study conducted in 2007 with respect to the Company s compensation levels and mix relative to market benchmarks. The updated study was based on a revised peer group and updated survey information reflecting the increase in size and scope of the Company s operations following the acquisition of the DSD coffee business from Sara Lee (the DSD Acquisition). Mercer reported directly to the Compensation Committee in connection with these services. Management interacted with the consultant to provide information or the perspective of management as requested by the consultant or Compensation Committee, and coordinated payment to the consultant out of the Board of Directors budget. During fiscal 2010, Mercer attended four of the five Compensation Committee meetings.

With respect to incentive compensation for our executive officers under the Farmer Bros. Co. 2005 Incentive Compensation Plan (the Incentive Plan), generally during the first quarter of each fiscal year, the Compensation Committee evaluates the executive officer s performance in light of the goals and objectives established for the prior year and determines the level of incentive compensation to be awarded to each executive officer. As part of the evaluation process, the Compensation Committee solicits comments from the Chief Executive Officer with respect to achievement of individual goals by those executive officers reporting to him. In the case of the Chief Executive Officer, the Compensation Committee may also solicit input from the other disinterested Board members. Additionally, the executive officers have an opportunity to provide input regarding their contributions to the Company s success and achievement of individual goals for the period being assessed. Incentive compensation for Named Executive Officers is approved by the Compensation Committee or, upon recommendation of the Compensation Committee, submitted to the disinterested members of the Board for approval. Following determination of incentive compensation awards for the prior fiscal year, the Compensation Committee establishes individual and corporate goals and objectives for each executive officer for the current fiscal year.

The Compensation Committee has the authority to make equity-based grants under the Omnibus Plan to eligible individuals for purposes of compensation, retention or promotion, and in connection with commencement of employment. Proposed equity awards to all executive officers are discussed and presented to the entire Board prior to award by the Compensation Committee.

The Compensation Committee has authority to delegate any of the functions described above to a subcommittee of its members. No delegation of this authority was made in fiscal 2010.

The Compensation Committee holds executive sessions (with no members of management present) at each of its regular meetings.

Director Compensation

In addition to considering and determining compensation for our executive officers, the Compensation Committee evaluates and makes recommendations to the Board regarding compensation for non-employee Board members. Any Board member who is also an employee of the Company does not receive separate compensation for service on the Board.

The processes and procedures of the Compensation Committee for considering and determining director compensation are as follows:

The Compensation Committee has authority to evaluate and make recommendations to the Board regarding director compensation. The Compensation Committee conducts this evaluation periodically by reviewing our director compensation practices against the practices of an appropriate peer group and market survey information. Based on this evaluation, the Compensation Committee may determine to make recommendations to the Board regarding possible changes. The Compensation Committee has the authority to delegate any of these functions to a subcommittee of its members. No delegation of this authority was made in fiscal 2010.

The Compensation Committee has the authority to retain consultants to advise on director compensation matters. In 2007, the Compensation Committee retained Mercer to evaluate the Company s director compensation levels relative to market benchmarks. No compensation consultants were engaged to provide advice regarding director compensation in 2008, 2009 or 2010. No executive officer has any role in determining or recommending the form or amount of director compensation.

The full Board serves as administrator under the Omnibus Plan with respect to equity awards made to non-employee directors.

Compensation Committee Interlocks and Insider Participation

During fiscal 2010, Thomas A. Maloof (Chair), Jeanne Farmer Grossman, James J. McGarry and John H. Merrell served as members of the Compensation Committee. No member of the Compensation Committee is an officer or former officer of the Company, was an employee of the Company during fiscal 2010, or has any relationship requiring disclosure by the Company as a related person transaction under SEC rules.

Compensation Committee Report

The Compensation Committee has reviewed and discussed the Compensation Discussion and Analysis with management and, based on the review and discussions, recommended to the Board that the Compensation Discussion and Analysis be included in this Proxy Statement and incorporated by reference in the Company s Annual Report on Form 10-K, as amended, for the fiscal year ended June 30, 2010.

Compensation Committee

of the Board of Directors

Thomas A. Maloof, Chairman

Jeanne Farmer Grossman

James J. McGarry

John H. Merrell

Nominating Committee

The Nominating Committee is a standing committee of the Board. The Nominating Committee s principal purposes are to identify persons qualified to become Board members and to recommend to the Board individuals to be selected as director nominees for the next annual meeting of stockholders or for appointment to vacancies on the Board.

During fiscal 2010, the Nominating Committee met once to nominate directors for election at the 2009 Annual Meeting. Jeanne Farmer Grossman, Martin A. Lynch, James J. McGarry, Thomas A. Maloof and John H. Merrell currently serve as members of the Nominating Committee. The Board has determined that all Nominating Committee members are independent under the Nasdaq listing standards.

Director Qualifications and Board Diversity

The Nominating Committee is responsible for determining Board of Director membership qualifications and selects, evaluates and recommends to the Board nominees to fill vacancies as they arise. The Nominating Committee maintains, with the approval of the Board, guidelines for selecting nominees to serve on the Board and considering stockholder recommendations for nominees. The Nominating Committee believes that its slate of nominees should include: the Chief Executive Officer of the Company; one or more nominees with upper management experience with the Company, in the coffee industry, in a complementary industry or who have desired professional expertise; three nominees who are independent and have the requisite accounting or financial qualifications to serve on the Audit Committee; and at least three nominees who are independent and have executive compensation experience to serve on the Compensation Committee. All nominees should contribute substantially to the Board s oversight responsibilities and reflect the needs of the Company s business. Additionally, the Nominating Committee believes that a member of the Farmer family, founding and substantial stockholders of the Company, or their representative should serve on the Board of Directors. The Nominating Committee believes that diversity has a place when choosing among candidates who otherwise meet the selection criteria, but the Company has not established a policy concerning diversity in Board composition. The Nominating Committee is responsible for evaluating and recommending to the Board the total size and composition of the Board. In connection with the annual nomination of directors, the Nominating Committee reviews with the Board the composition of the Board as a whole and recommends, if necessary, measures to be taken so that the Board reflects the appropriate balance of knowledge, experience, skills, background and diversity required for the Board as a whole. The background of each director and nominee is described above under Item 1 Election of Directors.

For purposes of identifying nominees for the Board of Directors, the Nominating Committee relies on professional and personal contacts of the Board and senior management. The Nominating Committee will consider recommendations for director nominees from Company stockholders. Biographical information and contact information for proposed nominees should be sent to Farmer Bros. Co., 20333 South Normandie Avenue, Torrance, California 90502, Attention: Secretary, subject to the notice provisions described below under the heading Other Matters Stockholder Proposals and Nominations. The Nominating Committee will evaluate candidates proposed by stockholders using the following criteria: Board needs (see discussion of slate of nominees above); relevant business experience; time availability; absence of conflicts of interest; and perceived ability to contribute to the Company s success.

Board Leadership Structure

Under our Bylaws, the Board of Directors, in its discretion, may choose a Chairman of the Board of Directors. If there is a Chairman of the Board of Directors, such person may exercise such powers as provided in the Bylaws or assigned by the Board of Directors. Since 2007, Guenter W. Berger has served as Chairman of the Board of Directors. As described above under Item 1 Election of Directors, Mr. Berger has served on our Board of Directors since 1980. He retired in 2007 as Chief Executive Officer after more than 47 years of service with our company in various capacities.

Notwithstanding the current separation of Chairman of the Board and Chief Executive Officer, our Chief Executive Officer is generally responsible for setting agenda items with input from the Board, and leading discussions during Board meetings. This structure allows for effective and efficient Board meetings and information flow on important matters affecting the Company. Other than Messrs. Laverty and Berger, all members of the Board are independent and all Board committees are comprised solely of independent directors. Due principally to the limited size of the Board and the long tenure of its members, the Board has not formally designated a lead independent director and believes that as a result thereof, executive sessions of the Board, which are attended solely by independent directors, result in an open and free flow of discussion of any and all matters that any director may believe relevant to the Company and/or its management.

Although the roles of Chairman and Chief Executive Officer are currently filled by different individuals, no single leadership model is right for all companies at all times, and the Company has no bylaw or policy in place that mandates this leadership structure. Accordingly, the Board of Directors periodically evaluates its leadership structure to ensure that it remains the optimal structure for the Company and its stockholders.

Board s Role in Risk Oversight

The Board of Directors recognizes that although risk management is primarily the responsibility of the Company s management team, the Board plays a critical role in the oversight of risk. The Board believes that an important part of its responsibilities is to assess the major risks which the Company faces and review the Company s options for monitoring and controlling these risks. The Board has delegated to the Audit Committee responsibility for oversight of risks associated with financial accounting and audits, internal control over financial reporting and the Company s major financial risk exposures, including risks relating to pension plan investments, commodity risk and hedging programs. The Compensation Committee oversees the risks relating to the Company s compensation policies and practices, as well as management development and leadership succession at the Company. At each regular meeting, or more frequently as needed, the Board of Directors considers reports from the Audit Committee and Compensation Committee which provide detail on risk management issues and management s response. The Board of Directors as a whole examines specific business risks in its periodic reviews of the individual business units and also on a company-wide basis as part of its regular reviews, including as part of the strategic planning process and annual budget review and approval. Outside of formal meetings, the Board and its committees have regular access to senior executives, including the Company s Chief Executive Officer and Chief Financial Officer. The Company believes that its leadership structure promotes effective Board oversight of risk management because the Board directly, and through its various committees, is regularly provided by management with the information necessary to appropriately monitor, evaluate and assess the Company s overall risk management, and all directors are actively involved in the risk oversight function.

Communication with the Board

The Company s annual meeting of stockholders provides an opportunity each year for stockholders to ask questions of or otherwise communicate directly with members of the Board on appropriate matters. In addition, stockholders may communicate in writing with any particular director, any committee of the Board, or the directors as a group, by sending such written communication to the Secretary of the Company at the Company s principal office, 20333 South Normandie Avenue, Torrance, California 90502. Copies of written communications received at such address will be collected and organized by the Secretary and provided to the Board or the relevant director unless such communications are considered, in the reasonable judgment of the Secretary, to be inappropriate for submission to the intended recipient(s). Examples of stockholder communications that would be considered inappropriate for submission to the Board include, without limitation, customer complaints, solicitations, communications that do not relate directly or indirectly to the Company s business, or communications that relate to improper or irrelevant topics. The Secretary or his designee may analyze and prepare a response to the information contained in communications received and may deliver a copy of the communication to other Company employees or agents who are responsible for analyzing or responding to complaints or requests. Communications concerning possible director nominees submitted by any of our stockholders will be forwarded to the members of the Nominating Committee.

COMPENSATION DISCUSSION AND ANALYSIS

This Compensation Discussion and Analysis describes our compensation philosophy, objectives and policies with respect to our Named Executive Officers which includes, for fiscal 2010, three current and four former executive officers as set forth in the table below:

Current Executive Officers Included Among Fiscal 2010 Named Executive Officers	Former Executive Officers Included Among Fiscal 2010 Named Executive Officers
Roger M. Laverty III President and Chief Executive Officer	Peter B. Knepper(2) Former Chief Financial Officer (Interim)
Jeffrey A. Wahba(1) Treasurer and Chief Financial Officer	John E. Simmons(3) Former Treasurer and Chief Financial Officer
Hortensia R. Gómez Vice President and Controller	Drew H. Webb(4) Former Executive Vice President of Sales and Marketing
	Heidi L. Modaro(5) Former Vice President Sales and Operations, Coffee & Tea

(1) Mr. Wahba joined the Company as Treasurer and Chief Financial Officer on June 1, 2010.

(2) Mr. Knepper is a member of Tatum, an executive services firm which provides full-time, part-time, and interim executives for organizations. Pursuant to an Interim Services Agreement between the Company and Tatum, Mr. Knepper served as a financial consultant to the Company from December 18, 2009 to February 8, 2010, at which time he was appointed Chief Financial Officer (Interim). Mr. Knepper served in this capacity through May 31, 2010, and thereafter provided consulting services to the Company through June 30, 2010. As a consultant, he did not participate in the Incentive Plan, Omnibus Plan or ESOP, or receive any other Company benefits.

(3) Mr. Simmons resigned as Treasurer and Chief Financial Officer on December 14, 2009 and retired from the Company on February 28, 2010.

(4) Mr. Webb separated from the Company on September 17, 2010.

(5) Ms. Modaro separated from the Company on February 25, 2010.

Primary Elements of Executive Compensation

The primary elements of the Company s executive compensation program and the purpose of each element are as follows:

Compensation Element	Description	Purpose

Base Salary	Fixed pay element determined annually in the first quarter of the fiscal year, with any adjustments to base pay retroactive to the beginning of the applicable fiscal year. May be subject to adjustment in the event of a promotion or job change.	Attract and retain top talent and compensate for day-to-day job responsibilities performed at an acceptable level.

Compensation

Element	Description	Purpose
Incentive Cash Bonus	Variable cash compensation based on the achievement of Company and individual annual performance objectives. May be subject to adjustment in the event of a promotion or job change.	Reward achievement of annual financial objectives as well as near term strategic objectives that will lead to the future success of the Company s business.
Long-Term Incentives	Variable equity-based compensation, typically consisting of a combination of stock options and restricted stock, however other forms of equity awards may be granted. May be subject to adjustment in the event of a promotion or job change.	Create a direct alignment with stockholder objectives, provide a focus on long-term value creation and potentially multi-year financial objectives, retain critical talent over extended timeframes, and enable key employees to share in value creation.
ESOP Allocation	Annual variable allocation of stock based on hours of service to the Company, subject to vesting after five years of service to the Company.	Enhance ownership interest and alignment with stockholders.
Welfare Benefits	General welfare benefits including medical, dental, life, disability and accident insurance, 401(k) plan and pension plan, as well as customary vacation, leave of absence and other similar policies.	Provide competitive welfare benefits generally consistent with those provided to all employees.
Perquisites	Fixed benefits consistent with practices among companies in our industry consisting of executive life insurance, use of a Company-owned automobile or automobile allowance, relocation assistance, and other similar personal benefits. May be subject to adjustment in the event of a promotion or job change.	Provide limited perquisites to facilitate the operation of the Company s business and assist the Company in recruiting and retaining key executives.

Executive Compensation Objectives

Our executive compensation program is based upon achieving the following objectives:

Balancing compensation elements and levels that attract, motivate and retain talented executives with forms of compensation that are performance-based and/or aligned with stock performance and stockholder interests;

Setting target total direct compensation (base salary, annual incentives and long-term incentives) for executive officers by reference to median compensation levels for comparable market reference points; and

Appropriately adjusting total direct compensation to reflect the performance of the executive officer over time (as reflected in his or her goals under the Incentive Plan), as well as the Company s annual performance (as reflected in the financial performance goals established under the Incentive Plan), and the Company s long-term performance (as reflected by stock appreciation for equity-based awards granted under the Omnibus Plan).

Consistent with new SEC disclosure requirements, the Compensation Committee assessed the Company s compensation programs and concluded that the Company s compensation policies and practices do not create risks that are reasonably likely to have a material adverse effect on the Company. This risk assessment process included a review of program policies and practices, the balance of potential risk to potential reward, and the support of the programs and their risks to Company strategy. Although we reviewed all compensation programs, we focused on the programs with the ability of a participant to directly affect payout and the controls on participant action and payout. The Company generally uses a combination of base salary, performance-based compensation, and retirement plans throughout the Company. In most cases, the compensation policies and practices are centrally designed and administered, and are substantially identical at each business unit. Route sales personnel are paid primarily on a sales commission basis, but all of our executive officers are paid under the programs and plans for non-sales employees. Certain departments have different or supplemental compensation programs tailored to their specific operations and goals. Based on the foregoing, the Compensation Committee determined that the Company s compensation programs are designed to reward actions and outcomes that are consistent with sound operation of our Company and are aligned with the creation of long-term stockholder value. To further align the interests of our executive officers with our stockholders, we have in place a clawback policy that requires the Board to consider recapturing past bonuses and other incentive and equity compensation awarded to executive officers if it is subsequently determined that the amounts of such compensation were determined based on financial results that are later restated. We also maintain stock ownership guidelines which require our executive officers to own and hold certain minimum levels of our Common Stock.

Oversight of the Executive Compensation Program

Compensation Committee

Under its charter, pursuant to the powers delegated by the Board, the Compensation Committee has the sole authority to determine and approve compensation for our Chief Executive Officer and each of our other executive officers, subject to Board review prior to approval in the case of equity compensation awards. In exercising this authority, the Compensation Committee evaluates the performance of the Chief Executive Officer within the context of the overall performance of the Company. The information considered includes a summary of the Company s performance compared to annual measures, a listing of accomplishments in addition to the areas covered by these measures, and a listing and analysis of challenges or issues encountered during the year. The Compensation Committee also reviews and discusses the Chief Executive Officer s assessment of the performance of our other executive officers. The Compensation Committee is comprised solely of independent directors and reports to the Board of Directors.

Compensation Committee Consultants

The Compensation Committee has the authority to retain the services of outside consultants to assist it in performing its responsibilities. During fiscal 2010, the Compensation Committee retained Mercer, a wholly-owned subsidiary of Marsh & McLennan Companies, Inc. (MMC), to assist the Compensation Committee with its responsibilities related to the Company s executive compensation programs. Mercer s fees for executive compensation consulting to the Compensation Committee in fiscal 2010 were $94,000.

Executive compensation consulting services provided by Mercer to the Compensation Committee during fiscal 2010 included analysis and advice related to the following:

- Executive compensation trends;
- Peer companies for competitive pay comparisons;
- Compensation levels and mix for the Company s executives;
- Design of short- and long-term incentives; and
- Incentive Plan financial goals.

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During fiscal 2010, management retained Mercer and certain MMC affiliates to provide other services unrelated to executive compensation. The aggregate fees paid for these other services were $809,220, which generally consisted of non-executive benchmarking and compensation analysis and advisory services for the Company and its subsidiary, CBI, implementation and monthly subscription fees for compensation management software, and fees paid by insurance carriers to Mercer Health and Benefits and Marsh Risk and Insurance Services. While neither the Compensation Committee nor the Board has historically approved such other services, because of the policies and procedures Mercer and the Compensation Committee have in place, the Compensation Committee believes that the advice it receives from the individual executive compensation consultant is objective and not influenced by Mercer s or its affiliates relationships with the Company. These policies and procedures include:

- The consultant receives no incentive or other compensation based on the fees charged to the Company for other services provided by Mercer or any of its affiliates;
- The consultant is not responsible for selling other Mercer or affiliate services to the Company;
- Mercer s professional standards prohibit the individual consultant from considering any other relationships Mercer or any of its affiliates may have with the Company in rendering his or her advice and recommendations;
- The Compensation Committee has the sole authority to retain and terminate the executive compensation consultant;
- The consultant has direct access to the Compensation Committee without management intervention;
- The Compensation Committee evaluates the quality and objectivity of the services provided by the consultant each year and determines whether to continue to retain the consultant; and
- The protocols for the engagement (described below) limit how the consultant may interact with management.

While it is necessary for the consultant to interact with management to gather information, the Compensation Committee has adopted protocols governing if and when the consultant s advice and recommendations can be shared with management. These protocols are included in the consultant s engagement letter. This approach protects the Compensation Committee s ability to receive objective advice from the consultant so that the Compensation Committee may make independent decisions about executive pay at the Company.

Management s Role in Establishing Compensation

There are no material differences in how the compensation policies or decisions are determined with respect to the Named Executive Officers, except that the compensation of the Named Executive Officers other than the Chief Executive Officer is determined by the Compensation Committee taking into account the input and recommendations of the Chief Executive Officer with respect to compensation for those executive officers reporting to him. In the case of the Chief Executive Officer, the Compensation Committee may also solicit input from other disinterested Board members. No executive officer has any role in approving his or her own compensation, and the Chief Executive Officer is not present during the portion of the meeting at which the Compensation Committee considers his compensation. The Chief Executive Officer routinely attends the meetings of the Compensation Committee. Other members of the Company s management may attend Compensation Committee meetings for the purpose of making presentations at the invitation of the Compensation Committee.

Peer Group Market Information

The Compensation Committee compares the pay levels and programs for the Company s executive officers to compensation information from a relevant peer group as well as information from published survey sources. The Compensation Committee uses this comparative data as a reference in its review and determination of executive compensation.

Compensation decisions for fiscal 2007 through fiscal 2009 were based in part on Mercer s study conducted in 2007. That study was based on published survey data for similarly sized companies as well as the following seventeen-company peer group, which was developed based on industry, annual revenue and business characteristics that were similar to those of the Company at the time of the study:

Bridgford Foods Corporation	Green Mountain Coffee, Inc.
Calavo Growers, Inc.	J & J Snack Foods Corp.
Cal-Maine Foods, Inc.	Monterey Gourmet Foods, Inc.
Caribou Coffee Company, Inc.	Overhill Farms, Inc.
Coffee Holding Co., Inc.	Peet s Coffee & Tea, Inc.
Cuisine Solutions, Inc.	Reddy Ice Holdings, Inc.
Diamond Foods, Inc.	John B. Sanfilippo & Son, Inc.
Diedrich Coffee, Inc.	Vita Food Products, Inc.
Golden Enterprises, Inc.	

In August 2009, the members of the peer group were adjusted in light of the Company s increased size and operations following the DSD Acquisition. Mercer selected the following fourteen-company peer group (the 2009 Peer Group) using a similar screening process to that used for the 2007 peer group, including the consideration of industry, annual revenue and business characteristics:

B&G Foods, Inc.	Imperial Sugar Company
Calavo Growers, Inc.	J & J Snack Foods Corp.
Cal-Maine Foods, Inc.	Lance, Inc.
Caribou Coffee Company, Inc.	Overhill Farms, Inc.
Diamond Foods, Inc.	Peet s Coffee & Tea, Inc.
Green Mountain Coffee Roasters, Inc.	Reddy Ice Holdings, Inc.
Hansen Natural Corporation	John B. Sanfilippo & Son, Inc.

The 2009 Peer Group is considered appropriate by the Compensation Committee because it represents a meaningful sample of comparable companies in terms of industry, annual revenue and business characteristics following the DSD Acquisition. Mercer combined data from the above peer companies with data from published survey sources to establish the market reference information. The survey data is derived from manufacturing companies with comparable revenue size.

The Compensation Committee used data based on the 2009 Peer Group and the published surveys as a reference point in evaluating fiscal 2010 executive officer compensation. The Compensation Committee s approach also considers competitive compensation practices and other relevant factors in setting pay rather than establishing compensation at very specific benchmark percentiles.

Base Salary

Consistent with the compensation philosophy and objectives described above, and based in part on the benchmarking comparisons provided by Mercer in their 2009 study, the Compensation Committee set fiscal 2010 base salaries for the Named Executive Officers as follows:

Name	Fiscal 2010 Annual Base Salary	Fiscal 2009 Annual Base Salary	Fiscal 2010 Annual Base Salary Percentage Change
Roger M. Laverty III	$ 425,000	$ 390,000	9%
Jeffrey A. Wahba	$ 305,000		
Peter B. Knepper(1)			
John E. Simmons(2)	$ 299,000	$ 299,000	0%
Drew H. Webb	$ 314,000	$ 314,000	0%
Hortensia R. Gómez(3)	$ 180,000	$ 162,000	10%
Heidi L. Modaro(2)	$ 250,000		

(1) Mr. Knepper served as a financial consultant to the Company from December 18, 2009 to February 8, 2010, at which time he was appointed Chief Financial Officer (Interim). Mr. Knepper served in this capacity through May 31, 2010, and thereafter provided consulting services to the Company through June 30, 2010. The Company paid Tatum $55,000 per month for services provided by Mr. Knepper, plus a 5% administrative fee. Total fees and expenses paid to Mr. Knepper and Tatum under this arrangement during fiscal 2010 were $239,750 and $135,625, respectively.

(2) Actual base salaries for Mr. Simmons and Ms. Modaro were prorated through their respective separation dates.

(3) Ms. Gómez s base salary increased effective March 17, 2009 in connection with her promotion to Vice President and Controller.

The fiscal 2010 annual base salaries shown in the table above were at or below the median base salary of the 2009 Peer Group for comparable positions.

Incentive Cash Bonus

Under the Incentive Plan, at the beginning of each fiscal year, the Compensation Committee, as administrator, determines who will participate in the Incentive Plan, establishes a target bonus for each participant, and establishes both Company financial performance criteria and individual participant goals for the ensuing year. The Compensation Committee also determines the weighting to be assigned to the Company s financial performance criteria and the individual goals as a whole, which may differ among the executive officers. A threshold level for the Company s financial performance may also be established which, if not met, may preclude the award of bonuses.

After the end of the fiscal year and promptly upon availability of the Company s audited financial statements, the Compensation Committee will determine the Company s level of achievement of its financial performance criteria. At such time, the Compensation Committee will also determine for each executive officer the percentage of achievement of assigned individual goals. The level of achievement will be multiplied by the assigned weighting to determine the weighted achievement percentage for each of the executive officer s assigned individual goals. The weighted achievement percentages for the Company s financial performance criteria and each individual assigned goal will be added up, and multiplied by the executive officer s target bonus percentage. The resulting percentage will be multiplied by the executive officer s base salary. The result will be the amount of the executive officer s preliminary bonus award. The preliminary bonus award is subject to adjustment, upward or downward, by the Compensation Committee in its discretion. The Compensation

Committee also has the discretion to alter the financial performance criteria and individual goals during the year and to decline to award any bonus should the Compensation Committee determine such actions to be warranted by a change in circumstances. Accordingly, no bonus is earned unless and until an award is actually made by the Compensation Committee after year-end.

It is the Compensation Committee s intent to achieve median target cash compensation (comprised of base salary and target annual cash incentive award) positioning over time, however the Compensation Committee may take other factors into consideration in establishing pay levels, including the amount of the increase in target cash compensation over the prior year, the performance of the executive, the performance of the Company, and the pay levels among the senior executive team. The Compensation Committee believes that the target levels of corporate and individual performance in any given year should not be easily achievable, and typically would not be achieved all of the time.

In 2009, the Compensation Committee established fiscal 2010 target bonus amounts for our executive officers equal to a percentage of their annual base salary. Individual target amounts were determined by the Compensation Committee based on the 2009 Peer Group median for comparable positions, as well as expected total compensation, job responsibilities, expected job performance, and, in the case of certain executive officers, the terms of their employment agreements with the Company. When combined with fiscal 2010 base salaries, the target awards resulted in total cash compensation between the 25th percentile and median of the 2009 Peer Group for comparable positions, with the exception of Mr. Laverty, whose total cash compensation for fiscal 2010 remained below the 25th percentile of the 2009 Peer Group for his position. Each executive officer s target bonus was also weighted between corporate and individual performance as set forth in the table below. Fiscal 2010 bonus information for the Named Executive Officers is as follows:

Name	Fiscal 2010 Target Bonus	Fiscal 2010 Target Bonus as Percentage of Fiscal 2010 Base Salary	Corporate Performance Goals (Weight)	Individual Performance Goals (Weight)	Fiscal 2010 Actual Bonus Award
Roger M. Laverty III	$ 318,750	75%	70%	30%	$ 0
Jeffrey A. Wahba(1)					
Peter B. Knepper (2)					
John E. Simmons(3)	$ 164,450	55%			$ 0
Drew H. Webb	$ 172,700	55%	65%	35%	$ 0
Hortensia R. Gómez	$ 45,000	25%	40%	60%	$ 0
Heidi L. Modaro(4)	$ 112,500	45%	30%	70%	$ 75,004

(1) Mr. Wahba joined the Company in June 2010, and therefore did not participate in the Incentive Plan for fiscal 2010.

(2) As a consultant, Mr. Knepper did not participate in the Incentive Plan.

(3) Although the Compensation Committee initially assigned a target bonus to Mr. Simmons, the Compensation Committee did not assign Company and individual goals to Mr. Simmons and determined that he would not participate in the Incentive Plan for fiscal 2010 due to his resignation as Treasurer and Chief Financial Officer on December 14, 2009.

(4) Pursuant to the terms of her Employment Agreement with the Company, Ms. Modaro was entitled to receive a bonus equal to her target award prorated through her effective separation date, February 25, 2010.

With the exception of Ms. Modaro, for fiscal 2010, actual bonus awards were based on the Company s financial performance and the level achievement of individual goals assigned by the Compensation Committee to each executive officer. The Company s financial performance was gauged by the level of operating cash flow (weighted at 70%) and net sales (weighted at 30%) as determined from the Company s audited financial statements. For this purpose, operating cash flow is defined as income from operations, after bonus accruals and excluding non-recurring items such as income from the sale of capital assets, plus depreciation and ESOP compensation expense. Subject to the Compensation Committee s discretion under the Incentive Plan, threshold operating cash flow of $22.35 million had to be achieved in fiscal 2010 to earn any bonus payout under the Incentive Plan. Assuming this threshold is achieved, a multiplier ranging from 0.0x to 1.5x would be assigned depending upon the level of achievement of operating cash flow and net sales, as follows:

Performance Measure	**Weighting**	**Below Threshold (0.0x)**	**Threshold (0.5x)**	**Target (1.0x)**	**Maximum (1.5x)**
Operating Cash Flow	70%	< $22.35 million	$22.35 million	$29.80 million	$37.25 million
Net Sales	30%	< $463 million	$463 million	$502 million	$515 million

The Compensation Committee also assigned individual weighted goals for fiscal 2010 to each of the executive officers, which are generally subjective and qualitative.

Because the Company did not achieve threshold operating cash flow of $22.35 million, no bonuses were awarded to the Named Executive Officers in fiscal 2010, with the exception of Ms. Modaro who was entitled to receive a prorated bonus under the terms of her Employment Agreement with the Company as described above.

Long-Term Incentives

At the 2007 Annual Meeting of Stockholders, the stockholders of the Company approved the Omnibus Plan. The Omnibus Plan provides for the grant or issuance of long-term incentive awards including stock options, stock appreciation rights, restricted stock, restricted stock units, dividend equivalents, performance-based awards, stock payments, cash-based awards or other incentives payable in cash or shares of stock, or any combination thereof. Each award is set forth in a separate agreement with the person receiving the award and indicates the type, terms and conditions of the award. The total number of shares available for issuance under the Omnibus Plan is 1,000,000, and no individual may be granted awards representing more than 250,000 shares in any calendar year, in each case, subject to adjustment as provided in the Omnibus Plan.

The Omnibus Plan is administered by the Compensation Committee. Subject to the terms and conditions of the Omnibus Plan, the Compensation Committee has the authority to select the persons to whom awards are to be made, to determine the number of shares to be subject thereto and the terms and conditions thereof, and to make all other determinations and to take all other actions necessary or advisable for the administration of the Omnibus Plan. Grants to executive officers are subject to Board review prior to approval. The Compensation Committee is also authorized to adopt, establish or revise rules relating to administration of the Omnibus Plan. The full Board administers the Omnibus Plan with respect to awards to non-employee directors.

Awards under the Omnibus Plan may be granted to individuals who are then Company officers or employees or are officers or employees of any of the Company s subsidiaries. Such awards, other than performance-based awards, may also be granted to the Company s directors and consultants. Only employees may be granted incentive stock options.

Based on Mercer s recommendations, the Company generally expects to make annual long-term incentive awards under the Omnibus Plan to our executive officers. Since adoption of the Omnibus Plan, grants to executive officers have consisted of stock options and restricted stock, with the number of shares underlying the stock options and shares of restricted stock determined based on the closing price of the Common Stock on the date of grant. Stock options are rights to purchase Common Stock at a pre-determined price (the closing price of the Common Stock on the date of grant), after the stock options have vested. Stock options are designed to create incentives for executives by providing them with an opportunity to share, along with stockholders, in the long-term performance of the Common Stock. The stock options have a seven-year term and generally vest ratably over three to five years. The Compensation Committee believes a seven-year option term provides a reasonable time frame within which the executive s contributions to corporate performance can align with stock appreciation. In addition, as compared with a ten-year option term typical at other companies, a seven-year option term allows the Company to more effectively manage the number of unexercised options that are outstanding. Restricted stock are shares that are subject to certain forfeiture restrictions. Restricted stock is designed as a retention device and to directly align the interests of the recipient and the Company s stockholders. The restricted stock is expected generally to vest at the end of three to five years.

In making long-term incentive awards, the general intent is to have a majority of the award be performance based and a minority of the award be retention based. In the case of awards made to our executive officers during fiscal 2010, generally two-thirds of the value of each award consisted of stock options and one-third of the value of each award consisted of restricted stock. The Compensation Committee considers options to be an appropriate performance based vehicle given that the stock options have no value unless the stock increases above the price on the date of grant.

In light of Mercer s conclusions in fiscal 2010 that long-term incentives for the Company s executive officers are significantly below the 25th percentile of the 2009 Peer Group for comparable positions, on December 10, 2009, the Compensation Committee made the following grants of non-qualified stock options and restricted stock under the Omnibus Plan:

Name	Fiscal 2010 Stock Option Grant (# of Shares of Common Stock Issuable Upon Exercise)	Fiscal 2010 Restricted Stock Grant (# of Shares)
Roger M. Laverty III	72,828	11,172
Drew H. Webb(1)	22,542	3,458
Hortensia R. Gómez	3,468	532
Heidi L. Modaro(2)	12,138	1,862

(1) Unvested and forfeited upon Mr. Webb s separation from the Company on September 17, 2010.

(2) Unvested and forfeited upon Ms. Modaro s separation from the Company on February 25, 2010.

The stock options shown above have an exercise price per share of $18.41, which was the closing price of the Common Stock as reported on Nasdaq on the date of grant. The stock options have a seven-year term expiring on December 10, 2016 and vest in one-third increments on each anniversary of the date of grant. The shares of restricted stock vest on December 10, 2012. The Compensation Committee did not grant any equity to Mr. Simmons in fiscal 2010 due to his resignation as an executive officer of the Company in December 2009. As a consultant, Mr. Knepper did not participate in the Omnibus Plan.

On June 1, 2010, the Compensation Committee granted stock options exercisable for 22,000 shares of Common Stock and 3,000 shares of restricted stock to Mr. Wahba in connection with his initial hire. The stock options have an exercise price equal to $16.78 per share, which was the closing price of the Common Stock as reported on Nasdaq on the date of grant. The stock options have a seven-year term expiring on June 1, 2017 and vest in one-third increments on each anniversary of the date of grant. The shares of restricted stock vest on June 1, 2013.

ESOP Allocation

In 2000, the Company adopted the ESOP. ESOP assets are allocated in accordance with a formula based on participant compensation. In order to participate in the ESOP, a participant must complete at least one thousand hours of service to the Company within twelve consecutive months. A participant s interest in the ESOP becomes one hundred percent vested after five years of service to the Company. Benefits are distributed from the ESOP at such time as a participant retires, dies or terminates service with the Company in accordance with the terms and conditions of the ESOP. Benefits may be distributed in cash or in shares of Common Stock. No participant contributions are allowed to be made to the ESOP.

Company contributions to the ESOP may be in the form of Common Stock or cash. Alternatively, the ESOP can borrow money from the Company or an outside lender and use the proceeds to purchase Common Stock. Shares acquired with loan proceeds are held in a suspense account and are released from the suspense account as the loan is repaid. The loan is repaid from the Company s annual contribution to the ESOP. The shares of Common Stock that are released are then allocated to participants accounts in the same manner as if they had been contributed to the ESOP by the Company. The allocation of ESOP assets is determined by a formula based on participant compensation during the calendar year. The ESOP is intended to satisfy applicable requirements of the Internal Revenue Code of 1986, as amended (the Code), and the Employee Retirement and Income Security Act of 1974. As of October 15, 2010, the ESOP owned of record 2,834,060 shares of Common Stock, including 1,550,341 allocated shares and 1,283,719 shares as yet unallocated to plan participants. An unaffiliated bank is trustee of the ESOP. The present members of the ESOP Administrative Committee are Roger M. Laverty III, Martin A. Lynch and John H. Merrell.

Our executive officers participate in the ESOP in the same manner as all other participants. In calendar 2010, the Company s Named Executive Officers received the following ESOP allocations based on compensation earned during calendar 2009:

Name	2010 ESOP Allocation (# of Shares)
Roger M. Laverty III	684
Jeffrey A. Wahba	(1)
Peter B. Knepper	(2)
John E. Simmons	785
Drew H. Webb	664(3)
Hortensia R. Gómez	610
Heidi L. Modaro	648(4)

(1) Mr. Wahba joined the Company in June 2010, and therefore did not receive an ESOP allocation.

(2) As a consultant, Mr. Knepper did not participate in the ESOP.

(3) Unvested and forfeited upon Mr. Webb s separation from the Company on September 17, 2010.

(4) Unvested and forfeited upon Ms. Modaro s separation from the Company on February 25, 2010.

Welfare Benefits

The welfare benefits received by employee executive officers are the same as received by other employees, including medical, dental, life, disability and accident insurance. The Company also offers a supplemental disability plan to higher income staff members, including our executive officers, which allows them to buy an additional amount of disability coverage at their own expense. Employee executive officers are eligible on the same basis as other employees for participation in a pension plan, a 401(k) plan and the ESOP. The Company does not contribute or match any participant contributions under the 401(k) plan. The value of the employee executive officer s 401(k) plan balances depends solely on the performance of investment alternatives selected by the employee executive officer from among the alternatives offered to all participants. All investment options in the 401(k) plan are market-based, meaning there are no above-market or guaranteed rates of return. Upon retirement, employee executive officers receive benefits, such as a pension and retiree life and medical insurance benefits, under the same terms as other retirees.

Perquisites

Perquisites are limited at the Company; however we believe that offering our executive officers certain perquisites facilitates the operation of our business, allows our executive officers to better focus their time,

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attention and capabilities on our business, and assists the Company in recruiting and retaining key executives. We also believe that the perquisites offered to our executive officers are generally consistent with practices among companies in our relevant industry.

The perquisites available only to employee executive officers are: (i) in the case of certain employee executive officers, benefits under an executive life insurance plan; (ii) in the case of certain employee executive officers, use of a Company-owned automobile; and (iii) in the case of one former employee executive officer, tuition reimbursement benefits, coaching and payment of disability premiums. Term life insurance premiums paid by the Company under the Company s executive life insurance plan are shown in the Summary Compensation Table below under the heading All Other Compensation. During fiscal 2010, we provided Messrs. Laverty and Webb and Ms. Modaro with automobiles owned by the Company and paid the associated maintenance and operating costs. The aggregate incremental cost associated with personal use of these automobiles is shown in the Summary Compensation Table below under the heading All Other Compensation. In fiscal 2010, the Company gave Ms. Modaro the Company-owned automobile that she was using valued at $11,600. This amount is also shown in the Summary Compensation Table below under the heading All Other Compensation. Additionally, during fiscal 2010, the Audit Committee approved a relocation payment to Mr. Webb of $250,000, less $32,500 in rent and travel expenses previously paid by the Company during fiscal 2010, and a temporary housing allowance of $3,500 per month ($42,000 total), as shown in the Summary Compensation Table below under the heading All Other Compensation.

It is the Company s intention to continually assess business needs and evolving practices to ensure that perquisite offerings are competitive and reasonable.

Change in Control and Termination Arrangements

Change in Control Severance Agreements; Employment Agreements

The Company has entered into agreements with each of its current Named Executive Officers (other than Ms. Gómez who elected not to enter into such agreement) pursuant to which they will be entitled to receive severance benefits upon the occurrence of certain enumerated events in connection with a change in control or threatened change in control. The events that trigger payment are generally those related to (i) termination of employment other than for cause, disability or death, or (ii) resignation for good reason. The payments and benefit levels under these agreements do not influence and were not influenced by other elements of compensation. These agreements were adopted, and are continued, to help: (i) assure the executives full attention and dedication to the Company, free from distractions caused by personal uncertainties and risks related to a pending or threatened change in control; (ii) assure the executives objectivity for stockholders interests; (iii) assure the executives of fair treatment in case of involuntary termination following a change in control or in connection with a threatened change in control; and (iv) attract and retain key talent during uncertain times. The agreements are structured so that payments and benefits are provided only if there is both a change in control or threatened change in control and a termination of employment, either by us (other than for Cause, Disability or death), or by the participant for Good Reason (as each is defined in the agreement). This is sometimes referred to as a double-trigger because the intent of the agreement is to provide appropriate severance benefits in the event of a termination following a change in control, rather than to provide a change in control bonus. A more detailed description of the severance benefits to which our current Named Executive Officers are entitled in connection with a change in control or threatened change in control is set forth below under the heading Executive Compensation Change in Control and Termination Arrangements.

The change in control agreements with Mr. Simmons, Ms. Modaro and Mr. Webb automatically expired in connection with their retirement or separation, as applicable, from the Company. The Company did not enter into a change in control agreement with Mr. Knepper since he was a consultant. In connection with his employment by the Company, the Company and Mr. Wahba entered into a change in control agreement effective February 25, 2010.

Pursuant to the terms of their Employment Agreements, Mr. Laverty, Mr. Wahba, Mr. Webb and Ms. Modaro are entitled to receive certain benefits upon their termination without cause or resignation with good reason. The Company believes such benefits were necessary to attract and retain these executive officers with demonstrated leadership abilities and to secure the services of these executive officers at agreed upon terms. A more detailed description of the benefits to which these officers are entitled in connection with their termination, including the benefits paid to Ms. Modaro and Mr. Webb in connection with their separation from the Company, is set forth below under the heading Executive Compensation Change in Control and Termination Arrangements.

Equity Awards

Under the terms of the stock option and restricted stock awards, in the event of death or disability a prorata portion (determined based on the actual number of service days during the vesting period divided by the total number of days during the vesting period) of any unvested stock options and restricted stock will be deemed to have vested immediately prior to the date of death or disability and, in the case of the restricted stock, will no longer be subject to forfeiture. Additionally, under the Omnibus Plan, the plan administrator has discretionary authority regarding accelerated vesting upon termination other than by reason of death or disability, or in connection with a change in control.

Compensation Policies and Practices

Stock Ownership Guidelines

The Board has adopted Stock Ownership Guidelines to further align the interests of the Company s executive officers and non-employee directors with the interests of the Company s stockholders. Under these guidelines, executive officers are expected to own and hold a number of shares of Common Stock based on the following guidelines:

Officer	**Value of Shares Owned**
Chief Executive Officer	$450,000
Other Executive Officers	$100,000 - $250,000, as determined by the Board in its discretion

Non-employee directors are expected to own and hold during their service as a Board member a number of shares of Common Stock with a value equal to at least three (3) times the amount of the non-employee director annual stock-based award, as the same may be adjusted from time to time, under the Omnibus Plan.

Stock that counts toward satisfaction of these guidelines includes: (i) shares of Common Stock owned outright by the officer or non-employee director and his or her immediate family members who share the same household, whether held individually or jointly; (ii) restricted stock or restricted stock units (whether or not the restrictions have lapsed); (iii) ESOP shares; and (iv) shares of Common Stock held in trust for the benefit of the officer or non-employee director or his or her family.

Until the applicable guideline is achieved, each officer and non-employee director is required to retain all profit shares, which are those shares remaining after payment of taxes on earned equity awards under the Omnibus Plan, such as shares granted pursuant to the exercise of vested options and restricted stock that has vested. Officers and non-employee directors are expected to continuously own sufficient shares to meet these guidelines once attained.

The guidelines may be waived at the discretion of the Board if compliance would create severe hardship or prevent an officer or non-employee director from complying with a court order. It is expected that these instances will be rare.

Insider Trading Policy

Our insider trading policy prohibits all employees, officers, directors, consultants and other associates of the Company and certain of their family members from, among other things, purchasing or selling any type of security, whether the issuer of that security is the Company or any other company, while aware of material, non-public information relating to the issuer of the security or from providing such material, non-public information to any person who may trade while aware of such information. The insider trading policy also prohibits employees from engaging in short sales with respect to our securities, purchasing or pledging Company stock on margin and entering into derivative or similar transactions (i.e., puts, calls, options, forward contracts, collars, swaps or exchange agreements) with respect to our securities. We also have procedures that require trades by certain insiders, including our directors and executive officers, to be pre-cleared by appropriate Company personnel. Additionally, such insiders are prohibited from conducting transactions involving the purchase or sale of the Company s securities from 12:01 a.m. New York City time on the 15th calendar day before the end of each of the Company s four fiscal quarters (including fiscal year end) through 11:59 p.m. New York City time on the second business day following the date of the public release containing the Company s quarterly (including annual) results of operations.

Policy on Executive Compensation in Restatement Situations

In the event of a material restatement of the financial results of the Company, the Board of Directors, or the appropriate committee thereof, will review all bonuses and other incentive and equity compensation awarded to the Company s executive officers on the basis of having met or exceeded performance targets for performance periods that occurred during the restatement period. If such bonuses and other incentive and equity compensation would have been lower had they been calculated based on such restated results, the Board of Directors, or the appropriate committee thereof, will, to the extent permitted by governing law and as appropriate under the circumstances, seek to recover for the benefit of the Company all or a portion of such bonuses and incentive and equity compensation awarded to executive officers whose fraud or misconduct caused or partially caused such restatement, as determined by the Board of Directors, or the appropriate committee thereof.

Equity Award Grants

Our current and historical practice is to grant long-term incentive awards to our executive officers on the date of the regularly scheduled meeting of the Board of Directors in December of each year, with grants to executive officers hired or promoted since that grant date to receive an interim grant reviewed by the Board and approved by the Compensation Committee outside any blackout period under our insider trading policy described above.

Taxes and Accounting Standards

Tax Deductibility Under Section 162(m) of the Internal Revenue Code

Section 162(m) of the Code places a $1 million limit on the amount of compensation the Company may deduct for tax purposes in any year with respect to each of the Named Executive Officers, except that performance-based compensation that meets applicable requirements is excluded from the $1 million limit. The Company s executive compensation program is designed to maximize the deductibility of compensation. However, when warranted due to competitive or other factors, the Compensation Committee may decide in certain circumstances to exceed the deductibility limit under Section 162(m) or to otherwise pay non-deductible compensation. There were no such circumstances in fiscal 2010.

Section 409A of the Internal Revenue Code

Section 409A of the Code requires programs that allow executives to defer a portion of their current income to meet certain requirements regarding risk of forfeiture and election and distribution timing (among other considerations). With respect to our compensation and benefit plans that are subject to Section 409A of the Code, in accordance with Section 409A of the Code and regulatory guidance issued by the Internal Revenue Service, we are currently operating such plans in compliance with Section 409A of the Code based upon our good faith, reasonable interpretation of the statute and the Internal Revenue Service s regulatory guidance.

Accounting Standards

Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 718 requires us to recognize an expense for the fair value of equity-based compensation awards. Grants of stock options and restricted stock, under our Omnibus Plan are accounted for under FASB ASC Topic 718. The Compensation Committee considers the accounting implications of significant compensation decisions, especially in connection with decisions that relate to our equity award program. As accounting standards change, the Company may revise certain programs to appropriately align accounting expenses of our equity awards with our overall executive compensation philosophy and objectives.

EXECUTIVE OFFICERS

The following table sets forth the executive officers of the Company as of the date hereof. All executive officers are elected annually by the Board of Directors and serve at the pleasure of the Board. No executive officer has any family relationship with any director or any other executive officer.

Name	Age	Title	Executive Officer Since
Roger M. Laverty III	63	President and Chief Executive Officer	2006
Jeffrey A. Wahba	54	Treasurer and Chief Financial Officer	2010
Mark A. Harding	50	Senior Vice President of Operations	2010
Hortensia R. Gómez	53	Vice President and Controller	2009
John M. Anglin	63	Secretary	2003

Roger M. Laverty III joined Farmer Bros. in 2006, as the fifth chief executive to lead the Company since its founding in 1912. Under Mr. Laverty s leadership, the Company has positioned itself as one of the nation s largest direct-store delivery (DSD) businesses for coffee, tea and culinary products, including the acquisition of the DSD Coffee Business from Sara Lee in 2009, and the acquisition of CBI, one of the nation s leading roasters and wholesalers of specialty coffee, in 2007. Since joining Farmer Bros., Mr. Laverty has also focused on operational improvements through programs intended to enhance the efficiency and flexibility of the Company s manufacturing processes and supply chain, and initiatives intended to strengthen sales and branding. From 2003 to 2005, Mr. Laverty served as President and CEO of Diedrich Coffee, Inc., a diversified operator of coffee houses and franchises that was known for its expertise and traditions in specialty coffee. Earlier, Mr. Laverty served 20 years with retailer Smart & Final, Inc., an operator of non-membership grocery warehouse stores for food and foodservice supplies, playing key roles in the growth of its sales from $200 million to more than $1.4 billion. He served as President and CEO of Smart & Final from 1993 to 1998. Mr. Laverty received his undergraduate and law degrees from Stanford University.

Jeffrey A. Wahba was appointed to the position of Treasurer and Chief Financial Officer in June 2010. Prior to joining Farmer Bros., Mr. Wahba served as Chief Financial Officer of Nero AG, a digital-media software provider based in Glendale, California and Karlsbad, Germany. Earlier, Mr. Wahba served as Chief Financial Officer of HireRight, Inc., a global leader in employment background screening solutions, based in Irvine, California, which he helped lead through its initial public offering in 2007. From 1986 to 2006, he served as Chief Financial Officer of the Henry Group of Companies, an international manufacturer of building products and a distributor of premium wines. He also served as Chief Financial Officer of Vault Corp., a software security firm, and as international controller of Max Factor and Co., a cosmetics manufacturer. Mr. Wahba graduated from Stanford University with a B.S. and M.S. in Industrial Engineering and Engineering Management and earned an M.B.A. degree from the University of Southern California.

Mark A. Harding joined the Company in March 2008 as Vice President of Operations, responsible for warehousing, transportation, manufacturing, fleet operations, purchasing and Brewmatic manufacturing. He was promoted to Senior Vice President of Operations in March 2010, responsible for route sales, branch operations, warehousing, transportation, manufacturing, fleet operations, purchasing, the National Equipment Service Organization, and Brewmatic refurbishment centers. Prior to joining the Company, Mr. Harding was Vice President of Operations of Intercontinental Art, Inc., a producer and importer of home decor, from March 2002 to March 2008, where his responsibilities included warehousing, transportation, quality control, domestic manufacturing and China manufacturing. Mr. Harding attended the University of Phoenix, where he received a B.A. in Business Administration.

Hortensia R. Gómez joined the Company in 2005 as Controller after serving as Chief Financial Officer at Barco Uniforms Inc., a professional apparel company, from 1992 to 2005. Ms. Gómez has more than 28 years of experience in management, accounting and finance positions. Ms. Gómez graduated from the University of California at Los Angeles.

John M. Anglin has served as Secretary of Farmer Bros. since 2003. He served as a member of the Company s Board of Directors from 1985 until 2003. In addition to his role at Farmer Bros., Mr. Anglin is a partner in the Pasadena-based law firm of Anglin, Flewelling, Rasmussen, Campbell & Trytten LLP (AFRCT), where his practice is concentrated in the corporate and real estate areas. Prior to this, Mr. Anglin was a partner of Walker Wright Tyler & Ward, LLP, Los Angeles, California from 1978 to 2002 (managing partner from 1994 to 2000). Mr. Anglin received his undergraduate and law degrees from the University of Southern California. AFRCT provided legal services to the Company in fiscal 2010 as discussed below under the heading Certain Relationships and Related Person Transactions. We expect to continue to engage AFRCT to perform legal services in fiscal 2011.

EXECUTIVE COMPENSATION

Summary Compensation Table

The following table sets forth summary information concerning compensation awarded to, earned by, or paid to each of our Named Executive Officers for all services rendered in all capacities to the Company and its subsidiaries in the last three fiscal years. For a complete understanding of the table, please read the footnotes and narrative disclosures that follow the table.

SUMMARY COMPENSATION TABLE

A	B	C	D	E	F	G	H	I	J
Name and Principal Position	**Fiscal Year**	**Salary ($)**	**Bonus ($)**	**Stock Awards ($)**	**Option Awards ($)**	**Non-Equity Incentive Plan Compensation ($)**	**Change in Pension Value ($)**	**All Other Compensation ($)**	**Total ($)**
Roger M. Laverty III(1)	2010	424,077		205,677	447,164	0	37,445	27,675	1,142,038
President and CEO	2009	389,654	234,000	143,616	267,200		27,445	32,969	1,094,884
	2008	350,038		149,820	244,800	175,000	22,229	33,419	975,306
Jeffrey A. Wahba(2)	2010	47,939		50,340	124,080				222,359
Treasurer and CFO									
Peter B. Knepper(3)	2010	239,750							239,750
Former CFO (Interim)									
John E. Simmons(4)	2010	207,618					109,027	124,821	441,466
Former Treasurer and CFO	2009	298,103	135,000	32,640	60,120		163,796	44,712	734,371
	2008	287,375		34,050	55,080	100,000	31,983	41,390	549,878
Drew H. Webb(5)	2010	314,001		63,662	138,408			305,720	821,791
Former Executive VP Sales and Marketing	2009	313,909	140,000	32,640	60,120		7,582	67,792	622,043
	2008	143,613	58,000	33,165	55,080			23,703	313,561
Hortensia R. Gómez(6)	2010	180,073		9,794	21,294		29,263	11,269	251,693
Vice President and Controller	2009	166,465	40,000	6,528	20,040		17,045	16,265	266,343
Heidi L. Modaro(7)	2010	173,076		34,279	74,527	75,004	14,740	536,128	907,754
Former Vice President Sales and Operations, Coffee & Tea	2009	76,923	30,000	15,449	46,760		3,991	51,300	224,423

(1) Mr. Laverty was promoted to Chief Executive Officer on December 6, 2007. The amounts shown in the table for fiscal 2008 reflect Mr. Laverty s compensation in all capacities for the full fiscal year. The amount reported in column I for fiscal 2010 includes life insurance premiums, dividends paid on restricted stock awards and an ESOP allocation ($10,324). The total value of all perquisites and other personal benefits did not exceed $10,000 in fiscal 2010 and has been excluded from the table.

(2) Mr. Wahba joined the Company as Treasurer and Chief Financial Officer on June 1, 2010. Mr. Wahba received no perquisites or other personal benefits in fiscal 2010.

(3) Mr. Knepper is a member of Tatum. Pursuant to an Interim Services Agreement between the Company and Tatum, Mr. Knepper served as a financial consultant to the Company from December 18, 2009 to February 8, 2010, at which time he was appointed Chief Financial Officer (Interim). Mr. Knepper served in this capacity through May 31, 2010, and thereafter provided consulting services to the Company through June 30, 2010. As a consultant, he did not participate in the Incentive Plan, Omnibus Plan or ESOP, or receive any other Company benefits. In addition to Mr. Knepper s compensation shown in the table above, Tatum received $135,625 associated with Mr. Knepper s services to the Company.

(4) Mr. Simmons resigned as Treasurer and Chief Financial Officer on December 14, 2009 and retired from the Company on February 28, 2010. The amount reported in column C for fiscal 2010 reflects Mr. Simmons prorated annual base salary through his retirement date. The amount reported in column I for fiscal 2010

includes life insurance premiums, dividends paid on restricted stock awards, an ESOP allocation ($11,841), and sick days paid over the maximum accumulation amount and accrued vacation ($106,234). The total value of all perquisites and other personal benefits did not exceed $10,000 in fiscal 2010 and has been excluded from the table.

(5) Mr. Webb became Executive Vice President of Sales and Marketing on February 25, 2010, prior to which time he served as Executive Vice President and Chief Operating Officer. Mr. Webb separated from the Company on September 17, 2010. The amounts shown in the table for fiscal 2010 reflect Mr. Webb s compensation in all capacities for the full fiscal year. The amount reported in column C for fiscal 2008 includes $48,229 in consulting fees and expenses paid to Mr. Webb from January 3, 2008 to March 3, 2008, when he was hired as Executive Vice President and Chief Operating Officer of the Company. The amount reported in column I for fiscal 2010 includes dividends paid on restricted stock awards, an ESOP allocation ($10,022), and perquisites and other personal benefits in the amount of $295,698, consisting of personal use of a Company-owned automobile calculated based on the aggregate incremental cost to the Company and relocation assistance ($292,000). The cost for personal use of a Company-owned automobile is calculated by allocating the costs of operating the car between personal and business use. The cost of operating the car is allocated to personal use on the basis of miles driven for personal use to total miles driven. Mr. Webb s accumulated ESOP allocation was unvested and forfeited upon Mr. Webb s separation from the Company.

(6) Ms. Gómez was promoted to Vice President and Controller on March 17, 2009. Prior to her promotion, Ms. Gómez was Controller of the Company. The amounts shown in the table for fiscal 2009 reflect Ms. Gómez s compensation in all capacities for the full fiscal year. The amount reported in column I for fiscal 2010 includes life insurance premiums, dividends paid on restricted stock awards and an ESOP allocation. The total value of all perquisites and other personal benefits did not exceed $10,000 in fiscal 2010 and has been excluded from the table.

(7) Ms. Modaro separated from the Company on February 25, 2010. The amount reported in column C for fiscal 2010 reflects Ms. Modaro s prorated annual base salary through her separation date. The amount reported in column C for fiscal 2009 represents Ms. Modaro s prorated annual base salary from March 1, 2009 through June 30, 2009. The amount reported in column G for fiscal 2010 reflects a prorated bonus paid to Ms. Modaro based on her target award for fiscal 2010 pursuant to the terms of her Employment Agreement. The amount reported in column I for fiscal 2010 includes (a) amounts paid in connection with Ms. Modaro s separation pursuant to the terms of her Employment Agreement, consisting of outplacement services ($10,000), severance payments made in fiscal 2010 ($76,923), severance payments to be made in fiscal 2011 ($174,037), and other amounts relating to her separation ($235,000); (b) accrued vacation ($14,718); (c) an ESOP allocation; (d) dividends paid on restricted stock awards; (e) short- and long-term disability premiums in lieu of healthcare benefits; and (f) perquisites and other personal benefits in the amount of $12,876, consisting of personal use of a Company-owned automobile calculated based on the aggregate incremental cost to the Company and transfer of title to such automobile to Ms. Modaro. The cost for personal use of a Company-owned automobile is calculated by allocating the costs of operating the car between personal and business use. The cost of operating the car is allocated to personal use on the basis of miles driven for personal use to total miles driven. Ms. Modaro s ESOP allocation was unvested and forfeited upon Ms. Modaro s separation from the Company.

Salary (Column C)

The amounts reported in column C represent base salaries earned by each of the Named Executive Officers for the fiscal year indicated.

Bonus (Column D)

The amounts reported in column D for fiscal 2009 reflect non-recurring bonuses paid to the Company s executive officers. In light of the then pending DSD Acquisition, the Compensation Committee determined not to establish bonus targets under the Incentive Plan for fiscal 2009 during the first quarter of fiscal 2009. Instead, upon completion of the DSD Acquisition, the Compensation Committee determined that it was advisable to award discretionary bonuses to the Company s executive officers outside the Incentive Plan for fiscal 2009 in recognition of their efforts in the successful consummation of the DSD Acquisition and related integration efforts, and their respective contributions to the Company s fiscal 2009 organic growth after taking into account certain non-recurring expenses associated with the DSD Acquisition and the relocation of the Company s specialty coffee operations to a new facility in Portland, Oregon. In addition to the foregoing executive officer bonuses, Ms. Modaro also received a discretionary bonus of $30,000 for fiscal 2009 in lieu of any bonus under the Incentive Plan.

Ms. Gómez was not a participant in the Incentive Plan for fiscal 2009. In light of her promotion and contributions to the success of the Company during fiscal 2009, the Compensation Committee awarded her a discretionary bonus for fiscal 2009 of $40,000.

The amount reported in column D for fiscal 2008 for Mr. Webb represents a non-recurring bonus paid to Mr. Webb reflecting his contribution to the Company from March 3, 2008, the date he joined the Company, through the end of fiscal 2008. Mr. Webb did not participate in the Incentive Plan in fiscal 2008.

All non-equity incentive plan compensation paid to the Named Executive Officers under the Incentive Plan is shown in column G.

Stock Awards (Column E)

The amounts reported in column E represent the aggregate grant date fair value computed in accordance with FASB ASC Topic 718. The amounts previously reported have been restated in accordance with new SEC rules relating to executive compensation. A discussion of the assumptions used in calculating the amounts in this column may be found in Note 11 to our audited consolidated financial statements for the fiscal year ended June 30, 2010 included in our Annual Report on Form 10-K, as amended, filed with the SEC on September 14, 2010, except that, as required by applicable SEC rules, we did not reduce the amounts in this column for any forfeitures relating to service-based (time-based) vesting conditions.

Option Awards (Column F)

The amounts reported in column F represent the aggregate grant date fair value computed in accordance with FASB ASC Topic 718. The amounts previously reported have been restated in accordance with new SEC rules relating to executive compensation. A discussion of the assumptions used in calculating the amounts in this column may be found in Note 11 to our audited consolidated financial statements for the fiscal year ended June 30, 2010 included in our Annual Report on Form 10-K, as amended, filed with the SEC on September 14, 2010, except that, as required by applicable SEC rules, we did not reduce the amounts in this column for any forfeitures relating to service-based (time-based) vesting conditions.

Non-Equity Incentive Plan Compensation (Column G)

The amounts reported in column G represent the aggregate dollar value for each of the Named Executive Officers of the annual performance bonus under the Incentive Plan for the fiscal years indicated. Annual bonuses under the Incentive Plan were approved by the Compensation Committee and paid to the Named Executive Officers in the first quarter of the subsequent fiscal year consistent with past practice.

As described above under Compensation Discussion and Analysis, because the Company did not achieve threshold operating cash flow of $22.35 million for fiscal 2010, no bonuses were awarded to the Company s current Named Executive Officers in fiscal 2010, with the exception of Ms. Modaro who received a prorated bonus based on her target award under the terms of her Employment Agreement with the Company.
Mr. Wahba

joined the Company in June 2010, and therefore did not participate in the Incentive Plan for fiscal 2010. As a consultant, Mr. Knepper did not participate in the Incentive Plan.

Change in Pension Value (Column H)

The amounts representing the change in pension value reported in column H were generated by the combination of increases in the accrued pension benefit and change in conversion of that benefit to a present value. Accrued pension benefits for each of the Named Executive Officers were calculated based on the final average pay times years of service as of the end of the fiscal year. Except in the case of Mr. Simmons who began receiving benefits upon his retirement in fiscal 2010, accrued benefits as of the end of each fiscal year increased over accrued benefits as of the end of the prior fiscal year because an additional year of service was included and because the averages of the most recent five years of pay were greater than the averages as of one year earlier. The conversion to a present value produced a further increase because normal retirement age, the assumed commencement of benefits, was one year closer. The present value conversion can also cause an increase or decrease in value due to changes in actuarial assumptions. The discount rate used to calculate present values decreased from 6.25% as of the end of fiscal 2009 to 5.60% as of the end of fiscal 2010, producing an increase in the present value. The discount rate used to calculate present values decreased from 6.80% as of the end of fiscal 2008 to 6.25% as of the end of fiscal 2009, producing an increase in the present value. The discount rate used to calculate present values increased from 6.00% as of the end of fiscal 2007 to 6.80% as of the end of fiscal 2008, producing a decrease in the present value. No other actuarial assumptions changed between the end of fiscal 2007 and the end of fiscal 2010.

All Other Compensation (Column I)

The amounts reported in column I represent the aggregate dollar amount for each Named Executive Officer for perquisites and other personal benefits; term life insurance premiums paid by the Company under the Company s executive life insurance plan; allocations under the ESOP; payment for sick time accrued above the maximum accumulation amount and accrued vacation; and certain other compensation described in the footnotes to the Summary Compensation Table above.

Total Compensation (Column J)

The amounts reported in column J are the sum of columns C through I for each of the Named Executive Officers. All compensation amounts reported in column J include amounts paid and amounts deferred.

Grants of Plan-Based Awards

The following table sets forth summary information regarding all grants of plan-based awards made to our Named Executive Officers for fiscal 2010.

GRANTS OF PLAN-BASED AWARDS

Name	Grant Date	Approval Date(1)	Estimated Future Payouts Under Non-Equity Incentive Plan Awards(2) Threshold ($)	Target ($)	Maximum ($)	All Other Stock Awards: Number of Shares of Stock or Units (#)(3)	All Other Option Awards: Number of Securities Underlying Options (#)(4)	Exercise or Base Price of Option Awards ($/Sh)(5)	Grant Date Fair Value of Stock and Option Awards ($)(6)
Roger M. Laverty III									
Annual Cash Incentive Bonus				318,750					
Time Based	12/10/09	12/10/09				11,172	72,828	18.41	652,840
Jeffrey A. Wahba									
Annual Cash Incentive Bonus									
Time Based	6/1/10	5/27/10				3,000	22,000	16.78	174,420
Peter B. Knepper									
Annual Cash Incentive Bonus									
Time Based									
John E. Simmons(7)									
Annual Cash Incentive Bonus				164,450					
Time Based									
Drew H. Webb									
Annual Cash Incentive Bonus				172,700					
Time Based	12/10/09	12/10/09				3,458	22,542	18.41	202,070
Hortensia R. Gómez									
Annual Cash Incentive Bonus				40,000					
Time Based	12/10/09	12/10/09				532	3,468	18.41	31,088
Heidi L. Modaro									
Annual Cash Incentive Bonus				112,500					
Time Based	12/10/09	12/10/09				1,862	12,138	18.41	108,807

(1) Reflects the date on which the grants were approved by the Compensation Committee.

(2) Represents annual cash incentive opportunities based on fiscal 2010 performance under the Incentive Plan. There are no thresholds or maximums under the Incentive Plan. The targets are set each fiscal year by the Compensation Committee. The bonus amounts are based on the Company s financial performance and satisfaction of individual participant goals. The Compensation Committee has discretion to increase, decrease or entirely eliminate the bonus amount derived from the Incentive Plan s formula. The maximum amount that can be awarded under the Incentive Plan is within the discretion of the Compensation Committee.

(3)

Restricted stock for the Named Executive Officers cliff vests on the third anniversary of the date of grant, subject to the acceleration provisions contained in the Omnibus Plan. The restricted stock shown in the table granted to Ms. Modaro and Mr. Webb was unvested and forfeited upon their respective separation from the Company. The Compensation Committee did not grant any equity to Mr. Simmons in fiscal 2010 due to his resignation as an executive officer of the Company in December 2009. As a consultant, Mr. Knepper did not participate in the Omnibus Plan.

(4) Stock options vest in one-third (1/3) increments on each anniversary of the date of grant, subject to the acceleration provisions contained in the Omnibus Plan. The stock options shown in the table granted to Ms. Modaro and Mr. Webb were unvested and forfeited upon their respective separation from the Company. The Compensation Committee did not grant any equity to Mr. Simmons in fiscal 2010 due to his resignation as an executive officer of the Company in December 2009. As a consultant, Mr. Knepper did not participate in the Omnibus Plan.

(5) Exercise price of stock option awards is equal to the closing market price on the date of grant.

(6) Reflects the grant date fair value of restricted stock and stock option awards computed in accordance with FASB ASC Topic 718. A discussion of the assumptions used in calculating the amounts in this column may be found in Note 11 to our audited consolidated financial statements for the fiscal year ended June 30, 2010 included in our Annual Report on Form 10-K, as amended, filed with the SEC on September 14, 2010, except that, as required by applicable SEC rules, we did not reduce the amounts in these columns for any forfeitures relating to service-based (time-based) vesting conditions.

(7) Although the Compensation Committee initially assigned a target bonus to Mr. Simmons, the Compensation Committee did not assign Company and individual goals to Mr. Simmons and determined that he would not participate in the Incentive Plan for fiscal 2010 due to his resignation as Treasurer and Chief Financial Officer on December 14, 2009.

Outstanding Equity Awards at Fiscal Year-End

The following table sets forth summary information regarding the outstanding equity awards at June 30, 2010 granted to each of our Named Executive Officers.

OUTSTANDING EQUITY AWARDS AT FISCAL YEAR-END

	Option Awards					Stock Awards			
Name	**Number of Securities Underlying Unexercised Options (#) Exercisable**	**Number of Securities Underlying Unexercised Options (#) Unexercisable(1)**	**Equity Incentive Plan Awards: Number of Securities Underlying Unexercised Unearned Options (#)**	**Option Exercise Price ($)**	**Option Expiration Date**	**Number of Shares or Units of Stock That Have Not Vested (#) (2)**	**Market Value of Shares or Units of Stock That Have Not Vested ($) (3)**	**Equity Incentive Plan Awards: Number of Unearned Shares, Units or Other Rights That Have Not Vested (#)**	**Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested ($)**
Roger M. Laverty III		72,828		18.41	12/10/16	11,172	168,585		
	13,333	26,667		21.76	12/11/15	6,600	99,594		
	26,667	13,333		22.70	2/20/15	6,600	99,594		
Jeffrey A. Wahba		22,000		16.78	6/1/17	3,000	45,270		
Peter B. Knepper									
John E. Simmons(4)	3,000			21.76	12/11/15				
	6,000			22.70	2/20/15				
Drew H. Webb(5)		22,542		18.41	12/10/16	3,458	52,181		
	3,000	6,000		21.76	12/11/15	1,500	22,635		
	6,000	3,000		22.11	3/3/15	1,500	22,635		
Hortensia R. Gómez		3,468		18.41	12/10/16	532	8,028		
	1,000	2,000		21.76	12/11/15	300	4,527		
	2,000	1,000		22.70	2/20/15	300	4,527		
Heidi L. Modaro(6)									

(1) Stock options vest in one-third (1/3) increments on each anniversary of the date of grant, subject to the acceleration provisions contained in the Omnibus Plan.

(2) Restricted stock for the Named Executive Officers cliff vests on the third anniversary of the date of grant, subject to the acceleration provisions contained in the Omnibus Plan.

(3) The market value was calculated by multiplying the closing price of our Common Stock on June 30, 2010 ($15.09) by the number of shares of unvested restricted stock.

(4) Excludes 3,000 shares of restricted stock and 9,000 shares subject to unvested stock options previously granted to Mr. Simmons which were forfeited upon Mr. Simmons retirement from the Company on February 28, 2010.

(5) Includes 6,458 shares of restricted stock and 31,542 shares subject to unvested stock options which were forfeited upon Mr. Webb s separation from the Company on September 17, 2010.

(6) Excludes 2,562 shares of restricted stock and 19,138 shares subject to unvested stock options previously granted to Ms. Modaro which were forfeited upon Ms. Modaro s separation from the Company on February 25, 2010.

Option Exercises and Stock Vested

No stock options were exercised by our Named Executive Officers and no shares of restricted stock held by our Named Executive Officers vested in fiscal 2010.

Employment Agreements and Arrangements

Laverty Employment Agreement

The Company has entered into an Employment Agreement, as amended, with Roger M. Laverty III (the Laverty Employment Agreement). The Laverty Employment Agreement provides that Mr. Laverty will serve as Chief Executive Officer and President of the Company, with the powers, general duties and responsibilities typically vested in a chief executive officer. Mr. Laverty s annual base salary is subject to annual review and may be adjusted upward or downward by the Company from time to time but may not be reduced below $320,000 per annum. Mr. Laverty is entitled to participate in the Incentive Plan (or any successor plan), with the amount of any target award thereunder to be set by the Compensation Committee. Mr. Laverty is entitled to use of a Company car or an equivalent car allowance, paid vacation of twenty-five (25) days per year, group health insurance, life insurance, business travel insurance, qualified retirement plan, 401(k) plan, employee stock ownership plan, cell phone, Company credit card, and business expense reimbursement. Mr. Laverty is entitled to participate in the Omnibus Plan in accordance with the provisions thereof. Mr. Laverty s employment may be terminated by the Company at any time with or without Cause (as defined in the Laverty Employment Agreement). Mr. Laverty s employment also will terminate upon his resignation, with or without Good Reason (as defined in the Laverty Employment Agreement), death or permanent incapacity. Upon certain events of termination, Mr. Laverty is entitled to the benefits described below under the heading Change in Control and Termination Arrangements.

Wahba Employment Agreement

On February 25, 2010, the Company entered into an Employment Agreement with Jeffrey A. Wahba (the Wahba Employment Agreement). The Wahba Employment Agreement provides that Mr. Wahba will serve as Treasurer and Chief Financial Officer of the Company, with oversight responsibility for all financial (including treasury functions), accounting and compliance functions of the Company. Mr. Wahba s initial annual base salary is $305,000. Mr. Wahba is entitled to participate in the Incentive Plan (or any successor plan), with the amount of any target award thereunder to be equal to 55% of his base salary. Mr. Wahba is entitled to all benefits and perquisites provided by the Company to its senior executives, including paid vacation, group health insurance, business travel insurance, retirement plan, 401(k) plan, employee stock ownership plan, cell phone, Company credit card, and business expense reimbursement. An automobile benefit may also be provided. Mr. Wahba is entitled to participate in the Omnibus Plan in accordance with the provisions thereof. Mr. Wahba s employment may be terminated by the Company at any time with or without Cause (as defined in the Wahba Employment Agreement). Mr. Wahba s employment also will terminate upon his resignation, with or without Good Reason (as defined in the Wahba Employment Agreement), death or permanent incapacity. Upon certain events of termination, Mr. Wahba is entitled to the benefits described below under the heading Change in Control and Termination Arrangements.

Webb Employment Agreement

The Company entered into an Employment Agreement, as amended, with Drew H. Webb (the Webb Employment Agreement). The Webb Employment Agreement provided that Mr. Webb would serve as Executive Vice President of Sales and Marketing of the Company, with oversight responsibility for the Company s sales, marketing, strategic planning and corporate development. On September 17, 2010, Mr. Webb separated from the Company. As a result, Mr. Webb may be entitled to certain severance payments and benefits described below under the heading Change in Control and Termination Arrangements.

Modaro Employment Agreement

The Company entered into an Employment Agreement with Heidi L. Modaro (the Modaro Employment Agreement). The Modaro Employment Agreement provided that Ms. Modaro would serve as Vice President Sales and Operations, Coffee & Tea of the Company, with oversight responsibility for the Company s direct store delivery sales and operations. On February 25, 2010, Ms. Modaro separated from the Company. As a result, Ms. Modaro has received and will continue to receive certain severance payments and benefits described below under the heading Change in Control and Termination Arrangements.

Pension Benefits

The following table provides information as of the end of fiscal 2010 with respect to the Farmer Bros. Plan, a defined benefit plan for the majority of the Company s employees who are not covered under a collective bargaining agreement, for each of the Named Executive Officers. For a complete understanding of the table, please read the narrative disclosures that follow the table.

PENSION BENEFITS

Name	Plan Name	Number of Years Credited Service (#)	Present Value of Accumulated Benefit ($)	Payments During Last Fiscal Year ($)
Roger M. Laverty III	Farmer Bros. Plan	2.92	87,119	
Jeffrey A. Wahba	Farmer Bros. Plan			
Peter B. Knepper	Farmer Bros. Plan			
John E. Simmons	Farmer Bros. Plan	27.92	995,713	22,518
Drew H. Webb	Farmer Bros. Plan			
Hortensia R. Gómez	Farmer Bros. Plan	3.42	55,791	
Heidi L. Modaro	Farmer Bros. Plan			

Annuity benefits payable monthly under the Farmer Bros. Plan are calculated as 1.50% of average compensation multiplied by the number of years of credited service, but not less than $60 per month for the first 20 years of credited service plus $80 per month for each year of credited service in excess of 20 years. For this formula, average compensation is defined as the monthly average of total pay received for the 60 consecutive months out of the 120 latest months before the retirement date which gives the highest average. The formula above produces the amount payable as a monthly annuity for the life of the Named Executive Officer beginning as early as age 62. Benefits can begin as early as age 55 upon retirement, but are subject to a 4% per year reduction for the number of years before age 62 when benefits began. Benefits under a predecessor plan are included in the figures shown in the table above for Mr. Simmons. Maximum annual combined benefits under both plans generally cannot exceed the lesser of $195,000 or the average of the employee s highest three years of compensation.

While a present value is shown in the table, benefits are not available as a lump sum and must be taken in the form of an annuity. Present values were calculated using the same actuarial assumptions applied in the calculation of pension liabilities reported in Note 8 to our audited consolidated financial statements for the fiscal year ended June 30, 2010 included in our Annual Report on Form 10-K, as amended, filed with the SEC on September 14, 2010.

Mr. Webb opted not to participate in the Farmer Bros. Plan. Ms. Modaro did not complete the required five years of service prior to separation from the Company on February 25, 2010 and, therefore, forfeited the unvested present value of her accumulated pension benefit in the amount of $18,731.

Change in Control and Termination Arrangements

Change in Control Agreements

The Company has entered into a Change in Control Severance Agreement (Severance Agreement) with each of its current Named Executive Officers (other than Ms. Gómez who elected not to enter into such agreement) which provides certain severance benefits to such persons in the event of a Change in Control (as generally defined below). Each Severance Agreement expires at the close of business on December 31, 2010, subject to automatic one year extensions unless the Company or such executive officer notified the other no later than September 30, 2010 that the term would not be extended. Neither the Company nor any executive officer notified the other that the term would not be extended, so the term of each Severance Agreement has been extended to December 31, 2011, subject to possible further extensions. Notwithstanding the foregoing, if prior to a Change in Control, an executive officer ceases to be an employee of the Company, his or her Severance Agreement will be deemed to have expired. The Severance Agreements with Mr. Simmons, Ms. Modaro and Mr. Webb automatically expired in connection with their retirement or separation, as applicable, from the Company. The Company did not enter into a Severance Agreement with Mr. Knepper since he was a consultant.

Under each of the Severance Agreements, a Change in Control generally will be deemed to have occurred at any of the following times: (i) upon the acquisition by any person, entity or group of beneficial ownership of 50% or more of either the then outstanding Common Stock or the combined voting power of the Company s then outstanding securities entitled to vote generally in the election of directors; (ii) at the time individuals making up the Incumbent Board (as defined in the Severance Agreements) cease for any reason to constitute at least a majority of the Board; or (iii) the approval of the stockholders of the Company of a reorganization, merger, consolidation, complete liquidation, or dissolution of the Company, the sale or disposition of all or substantially all of the assets of the Company or any similar corporate transaction (other than any transaction with respect to which persons who were the stockholders of the Company immediately prior to such transaction continue to represent at least 50% of the outstanding Common Stock of the Company or such surviving entity or parent or affiliate thereof immediately after such transaction). In the event of certain termination events in connection with a Change in Control or Threatened Change in Control (as defined in the Severance Agreements), the current Named Executive Officers will be entitled to certain payments and benefits shown in the tables below.

Each Severance Agreement provides that while such executive officer is receiving compensation and benefits thereunder, such executive officer will not in any manner attempt to induce or assist others to attempt to induce any officer, employee, customer or client of the Company to terminate its association with the Company, nor do anything directly or indirectly to interfere with the relationship between the Company and any such persons or concerns. In the event such executive officer breaches this provision, all compensation and benefits under the Severance Agreement will immediately cease.

Employment Agreements

Under the Employment Agreements with Mr. Laverty and Mr. Wahba, upon termination for any reason, the Company will pay such officer his accrued base salary and accrued but unused vacation. In addition, if such termination occurs at the election of the Company without Cause (as defined in the Employment Agreements) or by such officer s resignation with Good Reason (as defined in the Employment Agreements), such officer will be entitled to certain payments and benefits shown in the tables below. Receipt of any severance amounts under any Employment Agreement is conditioned upon execution of a general release of claims against the Company. Notwithstanding the foregoing, if the officer becomes eligible for severance benefits under the Severance Agreement described above, the benefits provided under that agreement will be in lieu of, and not in addition to, the severance benefits under his Employment Agreement.

Equity Awards

Under the terms of the stock option and restricted stock awards, in the event of death or disability a prorata portion (determined based on the actual number of service days during the vesting period divided by the total number of days during the vesting period) of any unvested stock options and restricted stock will be deemed to have vested immediately prior to the date of death or disability and, in the case of the restricted stock, will no longer be subject to forfeiture. Additionally, under the Omnibus Plan, the plan administrator has discretionary authority regarding accelerated vesting upon termination other than by reason of death or disability, or in connection with a change in control.

Potential Payments Upon Termination or Change in Control

The following tables describe potential payments and benefits upon termination, including resignation, severance, retirement or a constructive termination, or a change in control, including under the agreements described above, to which our current Named Executive Officers would be entitled. The estimated amount of compensation payable to each such Named Executive Officer in each situation is listed in the tables below assuming that the termination and/or change in control of the Company occurred at June 30, 2010. The actual amount of payments and benefits can only be determined at the time of such a termination or change in control and therefore the actual amounts will vary from the estimated amounts in the tables below. Descriptions of how such payments and benefits are determined under the circumstances, material conditions and obligations applicable to the receipt of payments or benefits and other material factors regarding such agreements, as well as other material assumptions that we have made in calculating the estimated compensation, follow these tables.

The tables and discussion below do not reflect (i) payments that would be provided to each Named Executive Officer under the Farmer Bros. Plan following termination of employment on the last business day of the fiscal year end; and (ii) the value of retiree medical and life insurance benefits, if any, that would be provided to each Named Executive Officer following such termination of employment, because, in each case, these benefits are generally available to all regular Company employees similarly situated in age, years of service and date of hire and do not discriminate in favor of executive officers.

The tables exclude Mr. Simmons who retired from the Company on February 28, 2010, Mr. Webb who separated from the Company on September 17, 2010, and Ms. Modaro who separated from the Company on February 25, 2010. Pursuant to the terms of the Modaro Employment Agreement, Ms. Modaro will continue to receive her base salary for a period of one (1) year from the effective termination date, such payment to be made in installments in accordance with the Company s standard payroll practices. In addition, Ms. Modaro received $75,004 representing the prorated amount of her target award under the Incentive Plan for fiscal 2010. As further required under the Modaro Employment Agreement, the Company paid Ms. Modaro a $200,000 retention bonus and $35,000 representing a prorated bonus payment for fiscal 2009, and paid a third party $10,000 for executive outplacement services. In exchange for the foregoing payments, Ms. Modaro provided the Company a general release of claims as required under the Modaro Employment Agreement. Under certain circumstances, Mr. Webb may be entitled to salary and benefit continuation and certain other severance payments and benefits as provided in the Webb Employment Agreement.

ROGER M. LAVERTY III	**Death**	**Disability**	**Retirement**	**Change in Control and Involuntarily Terminated or Resignation for Good Reason within 24 Months of Change in Control**	**Threatened Change in Control and Involuntarily Terminated or Resignation for Good Reason**	**Termination Without Cause or Resignation With Good Reason**
Base Salary Continuation	$	$	$	$ 850,000	$ 850,000	$ 425,000
Bonus Payments	$ 318,750	$ 318,750	$	$ 318,750	$ 318,750	$ 318,750
Value of Accelerated Stock Options	$	$	$	$	$	$
Value of Accelerated Restricted Stock	$ 130,724	$ 130,724	$	$	$	$
Qualified and Non-Qualified Plans	$	$	$	$ 162,100	$ 162,100	$
ESOP	$ 38,600	$ 38,600	$	$ 61,312	$ 61,312	$
Health and Dental Insurance	$	$ 18,401	$	$ 36,802	$ 36,802	$ 18,401
Outplacement Services	$	$	$	$ 25,000	$ 25,000	$
Life Insurance Proceeds	$ 725,000	$	$	$	$	$
Total Pre-Tax Benefit	$ 1,213,074	$ 506,475	$	$ 1,453,964	$ 1,453,964	$ 762,151

JEFFREY A. WAHBA	**Death**	**Disability**	**Retirement**	**Change in Control and Involuntarily Terminated or Resignation for Good Reason within 24 Months of Change in Control**	**Threatened Change in Control and Involuntarily Terminated or Resignation for Good Reason**	**Termination Without Cause or Resignation With Good Reason**
Base Salary Continuation	$	$	$	$ 610,000	$ 610,000	$ 305,000
Bonus Payments	$ 167,750	$ 167,750	$	$ 167,750	$ 167,750	$ 167,750
Value of Accelerated Stock Options	$	$	$	$	$	$
Value of Accelerated Restricted Stock	$ 1,199	$ 1,199	$	$	$	$
Qualified and Non-Qualified Plans	$	$	$	$	$	$
ESOP	$	$	$ 226.4	$ —	$226.4	
Certificate of deposit	—	42.5	—	42.5		
Commercial paper	—	22.4	—	22.4		
Corporate debt securities	—	535.6	—	535.6		
Foreign government debt securities	—	5.0	—	5.0		

Government-sponsored enterprise obligations	254.9	16.1	—	271.0
Money market funds (1)	1,145.2	—	—	1,145.2
Mutual funds (2)	1.0	2.0	—	3.0
Publicly-traded equity securities	2.9	—	—	2.9
U.S. government securities	275.9	218.6	—	494.5
Total available-for-sale securities	1,679.9	1,068.6	—	2,748.5
Trading securities in mutual funds (3)	12.6	—	—	12.6
Derivative assets:				
Foreign exchange contracts	—	3.5	—	3.5
Total assets measured at fair value	$ 1,692.5	$ 1,072.1	$ —	$ 2,764.6
Liabilities measured at fair value:				
Derivative liabilities:				
Foreign exchange contracts	$ —	$ 0.1	$ —	$ 0.1
Total liabilities measured at fair value	$ —	$ 0.1	$ —	$ 0.1
Total assets measured at fair value, reported as:				
Cash equivalents	$ 1,048.7	$ 177.2	$ —	$ 1,225.9
Restricted investments	103.6	2.0	—	105.6
Short-term investments	224.4	217.1	—	441.5
Long-term investments	315.8	672.3	—	988.1
Prepaid expenses and other current assets	—	3.5	—	3.5
Total assets measured at fair value	$ 1,692.5	$ 1,072.1	$ —	$ 2,764.6
Total liabilities measured at fair value, reported as:				
Other accrued liabilities	$ —	$ 0.1	$ —	$ 0.1
Total liabilities measured at fair value	$ —	$ 0.1	$ —	$ 0.1

(1) Balance includes $102.6 million of restricted investments measured at fair market value, related to the Company's D&O trust and acquisition-related escrows.
(2) Balance relates to the restricted investments measured at fair market value of the Company's India Gratuity Trust.
(3) Balance relates to investments measured at fair value related to the Company's non-qualified deferred compensation plan assets.

The Company's Level 2 available-for-sale fixed income securities are priced using quoted market prices for similar instruments or non-binding market prices that are corroborated by observable market data. The Company uses inputs such as actual trade data, benchmark yields, broker/dealer quotes, or alternative pricing sources with reasonable levels of price transparency which

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Juniper Networks, Inc.
Notes to Condensed Consolidated Financial Statements (Continued)
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are obtained from quoted market prices, independent pricing vendors, or other sources, to determine the ultimate fair value of these assets. The Company's policy is to recognize asset or liability transfers among Level 1, Level 2, and Level 3 as of the actual date of the events or change in circumstances that caused the transfer. During the three months ended March 31, 2013 and March 31, 2012, the Company had no transfers between levels of the fair value hierarchy of its assets or liabilities measured at fair value.

Assets and Liabilities Measured at Fair Value on a Nonrecurring Basis

Certain of the Company's assets, including intangible assets, goodwill, and privately-held investments, are measured at fair value on a nonrecurring basis if impairment is indicated. As of March 31, 2013 and December 31, 2012, the Company had no assets or liabilities measured at fair value on a nonrecurring basis.

Assets and Liabilities Not Measured at Fair Value

The carrying amounts of the Company's accounts receivable, financing receivables, accounts payable, and other accrued liabilities approximate fair value due to their short maturities. The fair value of the Company’s long-term debt is disclosed in Note 10, Long-Term Debt and Financing, and was determined using quoted market prices (Level 1).

Note 6. Derivative Instruments

The Company uses derivatives to partially offset its market exposure to fluctuations in certain foreign currencies and does not enter into derivatives for speculative or trading purposes.

The notional amount of Company's foreign currency derivatives are summarized as follows (in millions):

	As of	
	March 31, 2013	December 31, 2012
Cash flow hedges	$67.6	$85.8
Non-designated derivatives	114.4	112.8
Total	$182.0	$198.6

Cash Flow Hedges

The Company can use foreign currency forward or option contracts to hedge certain forecasted foreign currency transactions relating to cost of services and operating expenses. The derivatives are intended to hedge the U.S. Dollar equivalent of the Company's planned cost of services and operating expenses denominated in foreign currencies. These derivatives are designated as cash flow hedges. Execution of these cash flow hedge derivatives typically occurs every month with maturities of one year or less. The effective portion of the derivative's gain or loss is initially reported as a component of accumulated other comprehensive (loss) income, and upon occurrence of the forecasted transaction, is subsequently reclassified into the cost of services or operating expense line item to which the hedged transaction relates. The Company records any ineffectiveness of the hedging instruments in other expense, net in its Condensed Consolidated Statements of Operations. Cash flows from such hedges are classified as operating activities. All amounts within other comprehensive income are expected to be reclassified into earnings within the next 12 months.

As of March 31, 2013 and December 31, 2012, the total fair value of the Company’s derivative assets recorded in other current assets on the Condensed Consolidated Balance Sheets was $1.6 million and $3.5 million, respectively. As of March 31, 2013 and December 31, 2012, the total fair value of the Company’s derivative liabilities recorded in other accrued liabilities on the Condensed Consolidated Balance Sheets was $1.1 million and $0.1 million, respectively.

During the three months ended March 31, 2013 and March 31, 2012, the Company recognized a loss of $2.1 million and a gain of $6.0 million, respectively, in accumulated other comprehensive (loss) income for the effective portion of its derivative instruments and reclassified a gain of $1.4 million and a loss of $3.5 million, respectively, from other comprehensive income to operating expense in the Condensed Consolidated Statements of Operations.

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The ineffective portion of the Company's derivative instruments recognized in its Condensed Consolidated Statements of Operations was not material during the three months ended March 31, 2013 and March 31, 2012.

Non-Designated Derivatives

The Company also uses foreign currency forward contracts to mitigate variability in gains and losses generated from the remeasurement of certain monetary assets and liabilities denominated in foreign currencies. These derivatives do not qualify for special hedge accounting treatment. These derivatives are carried at fair value with changes recorded in other expense, net in the Condensed Consolidated Statements of Operations. Changes in the fair value of these derivatives are largely offset by re-measurement of the underlying assets and liabilities. Cash flows from such derivatives are classified as operating activities. The derivatives have maturities within two months.

The Company recognized a net loss of $0.7 million and $0.1 million, during the three months ended March 31, 2013 and March 31, 2012, respectively, on non-designated derivative instruments within other expense, net, in its Condensed Consolidated Statements of Operations.

Offsetting of Derivatives

The Company presents its derivative assets and derivative liabilities on a gross basis in the Condensed Consolidated Balance Sheets. However, under master netting agreements with certain counterparties of foreign exchange contracts, subject to applicable requirements, the Company is allowed to net settle transactions on the same date in the same currency, with a single net amount payable by one party to the other. As of March 31, 2013 and December 31, 2012, the potential effect of rights of setoff associated with derivative instruments would be an offset to both assets and liabilities of $0.2 million and $0.1 million, respectively. The resulting net derivative assets and derivative liabilities of the potential offset impact are $1.4 million and $0.9 million as of March 31, 2013, respectively. The resulting net derivative assets are $3.4 million and not material for derivative liabilities as of December 31, 2012. The Company is not required to pledge nor is it entitled to receive cash collateral related to these derivative transactions.

Note 7. Goodwill and Purchased Intangible Assets

Goodwill
The following table presents the goodwill activity allocated to the Company's reportable segments during the three months ended March 31, 2013 (in millions):

	PSD	SSD	Total
Balance as of December 31, 2012	$1,866.3	$2,191.5	$4,057.8
Reclassifications	(179.0)	179.0	—
Balance as of March 31, 2013	$1,687.3	$2,370.5	$4,057.8

Goodwill associated with security products previously reported under PSD has been reclassified to SSD in connection with the Company's product realignment of all security products within SSD from PSD. See Note 13, Segments, for further discussion of the Company's product realignment. Goodwill was reclassified based on the relative fair value allocation of the reporting units affected. There were no impairments to goodwill during the three months ended March 31, 2013 and March 31, 2012.

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Notes to Condensed Consolidated Financial Statements (Continued)
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Purchased Intangible Assets

The Company's purchased intangible assets were as follows (in millions):

	Gross	Accumulated Amortization	Impairments and Other Charges	Net
As of March 31, 2013				
Intangible assets with finite lives:				
Technologies and patents	$564.0	$(431.7)	$(30.5)	$101.8
Customer contracts, support agreements, and related relationships	74.3	(60.1)	(2.2)	12.0
Other	18.8	(18.8)	—	—
Total intangible assets with finite lives	657.1	(510.6)	(32.7)	113.8
IPR&D with indefinite lives	17.4	—	—	17.4
Total purchased intangible assets	$674.5	$(510.6)	$(32.7)	$131.2
As of December 31, 2012				
Intangible assets with finite lives:				
Technologies and patents	$554.1	$(425.0)	$(30.5)	$98.6
Customer contracts, support agreements, and related relationships	74.3	(59.2)	(2.2)	12.9
Other	18.8	(18.8)	—	—
Total intangible assets with finite lives	647.2	(503.0)	(32.7)	111.5
IPR&D with indefinite lives	17.4	—	—	17.4
Total purchased intangible assets	$664.6	$(503.0)	$(32.7)	$128.9

The purchased intangible assets balance as of March 31, 2013, includes intangible assets acquired through the acquisition completed during the first quarter of 2013. Refer to Note 3, Business Combinations, for further details.

Amortization of purchased intangible assets included in operating expenses and cost of product revenues totaled $7.5 million and $7.3 million for the three months ended March 31, 2013 and March 31, 2012, respectively. There were no impairment charges with respect to the purchased intangible assets during the three months ended March 31, 2013 and March 31, 2012.

As of March 31, 2013, the estimated future amortization expense of purchased intangible assets with finite lives is as follows (in millions):

Years Ending December 31,	Amount
Remainder of 2013	$22.9
2014	30.4
2015	26.8
2016	14.2
2017	10.5
Thereafter	9.0
Total	$113.8

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Juniper Networks, Inc.
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Note 8. Other Financial Information

Inventories, Net

The Company purchases and holds inventory to provide adequate component supplies over the life of the underlying products. The majority of the Company's inventory is production components. Inventories, net are reported within prepaid expenses and other current assets on the Condensed Consolidated Balance Sheets and consisted of the following (in millions):

	As of March 31, 2013	December 31, 2012
Inventories, net:		
Production materials	$50.1	$54.6
Finished goods	4.0	4.1
Total inventories, net	$54.1	$58.7

Warranties

The Company accrues for warranty costs as part of its cost of sales based on associated material costs, labor costs for customer support, and overhead at the time revenue is recognized. This provision is reported as accrued warranty within current liabilities on the Condensed Consolidated Balance Sheets. Changes in the Company's warranty reserve during the three months ended March 31, 2013 were as follows (in millions):

Balance as of December 31, 2012	$29.7
Provisions made during the period, net	7.3
Change in estimate	(0.3)
Actual costs incurred during the period	(7.3)
Balance as of March 31, 2013	$29.4

Deferred Revenue

Details of the Company's deferred revenue, as reported on the Condensed Consolidated Balance Sheets, were as follows (in millions):

	As of March 31, 2013	December 31, 2012
Deferred product revenue:		
Undelivered product commitments and other product deferrals	$250.5	$256.9
Distributor inventory and other sell-through items	122.7	138.4
Deferred gross product revenue	373.2	395.3
Deferred cost of product revenue	(86.4)	(99.4)
Deferred product revenue, net	286.8	295.9
Deferred service revenue	693.9	627.5
Total	$980.7	$923.4
Reported as:		
Current	$774.7	$693.5
Long-term	206.0	229.9
Total	$980.7	$923.4

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Juniper Networks, Inc.
Notes to Condensed Consolidated Financial Statements (Continued)
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Deferred product revenue represents unrecognized revenue related to shipments to distributors that have not sold through to end-users, undelivered product commitments, and other shipments that have not met all revenue recognition criteria. Deferred product revenue is recorded net of the related costs of product revenue. Deferred service revenue represents customer payments made in advance for services, which include technical support, hardware and software maintenance, professional services, and training.

Other Expense, Net

Other expense, net consisted of the following (in millions):

	Three Months Ended March 31,	
	2013	2012
Interest income	$2.1	$2.8
Interest expense	(14.3)	(14.2)
Other	2.1	(13.0)
Other expense, net	$(10.1)	$(24.4)

Interest income primarily includes interest earned on the Company’s cash, cash equivalents, and investments. Interest expense primarily includes interest net of capitalized interest expense from long-term debt and customer financing arrangements. Other typically consists of investment and foreign exchange gains and losses and other non-operational income and expense items. During the three months ended March 31, 2013, Other was primarily comprised of a $1.6 million gain related to a privately-held investment. During the three months ended March 31, 2012, Other was primarily comprised of an other-than-temporary impairment charge of $14.0 million, related to a privately-held equity investment.

Note 9. Restructuring Charges

Restructuring charges are based on the Company's restructuring plans that were committed to by management. These restructuring charges are recorded within cost of revenues or restructuring charges in the Condensed Consolidated Statements of Operations, as applicable. Any changes in the estimates of executing the approved plans are reflected in the Company's results of operations. Restructuring liabilities are reported within other accrued liabilities and other long-term liabilities on the Condensed Consolidated Balance Sheets.

During 2012, the Company initiated a restructuring plan (the "2012 Restructuring Plan") to bring its cost structure more in line with its long-term financial and strategic model. The 2012 Restructuring Plan consists of workforce reductions, facility consolidations or closures, and supply chain and procurement efficiencies. During the three months ended March 31, 2013, the Company continued to implement restructuring activities under the 2012 Restructuring Plan and recorded $7.8 million in charges for workforce reductions, facility consolidations or closures, and contract terminations. Under the 2012 Restructuring Plan, total costs incurred through March 31, 2013, was $101.1 million of which $53.6 million was recorded within cost of revenues and $47.5 million was recorded within restructuring charges in the Condensed Consolidated Statements of Operations. The Company expects to incur charges related to this plan through the end of fiscal 2013.

During 2011, the Company implemented a restructuring plan (the "2011 Restructuring Plan") in an effort to better align its business operations with the current market and macroeconomic conditions. The 2011 Restructuring Plan consisted of certain workforce reductions, facility closures and to a lesser extent, contract terminations. The Company recorded the majority of the restructuring charges associated with this plan during the years ended 2012 and 2011 and recorded severance-related adjustments of $0.1 million during the three months ended March 31, 2013. As of March 31, 2013, the remaining restructuring liability under this plan relates to facility charges, which are expected to be completed by March 2018.

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The following table presents restructuring charges included in cost of revenues and restructuring charges in the Condensed Consolidated Statements of Operations under the Company's restructuring plans (in millions):

	Three Months Ended March 31,	
	2013	2012
Severance	$4.4	$3.0
Facilities	2.6	(0.2)
Contract terminations and other	0.7	(0.8)
Total	$7.7	$2.0

The following table provides a summary of changes in the restructuring liability related to the Company's plans during the three months ended March 31, 2013 (in millions):

	December 31, 2012	Charges	Cash Payments	Non-cash Settlements and Other	March 31, 2013
Severance	$10.6	$4.4	$(8.2)	$(0.1)	$6.7
Facilities	5.2	2.6	(1.8)	(0.2)	5.8
Contract terminations and other	2.4	0.7	(2.1)	0.5	1.5
Total	$18.2	$7.7	$(12.1)	$0.2	$14.0

In connection with the restructuring plans discussed above, the Company expects to record aggregate future charges of approximately $14.0 million through the remainder of 2013, consisting of approximately $1.0 million and $13.0 million related to workforce reductions and facility closures, respectively.

Note 10. Long-Term Debt and Financing

Long-Term Debt

The following table summarizes the Company's long-term debt (in millions, except percentages):

	As of March 31, 2013	
	Amount	Effective Interest Rates
Senior notes:		
3.10% fixed-rate notes, due 2016 ("2016 Notes")	$300.0	3.12%
4.60% fixed-rate notes, due 2021 ("2021 Notes")	300.0	4.63%
5.95% fixed-rate notes, due 2041 ("2041 Notes")	400.0	6.01%
Total senior notes	1,000.0	
Unaccreted discount	(0.8)	
Total	$999.2	

The effective interest rates for the 2016 Notes, 2021 Notes, and 2041 Notes (collectively the “Notes”) include the interest on the Notes, accretion of the discount, and amortization of issuance costs. As of March 31, 2013 and December 31, 2012, the estimated fair value of the Notes included in long-term debt in the Condensed Consolidated Balance Sheets was approximately $1,074.3 million and $1,090.7 million, respectively, based on quoted market prices (Level 1). As of March 31, 2013, the Company was in compliance with all of its debt covenants.

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Customer Financing Arrangements

The Company has customer financing arrangements to factor its accounts receivable to a third-party financing provider for certain customers that require longer payment terms than those typically provided by the Company. The program does not and is not intended to affect the timing of revenue recognition because the Company only recognizes revenue upon sell-through. Under the financing arrangements, proceeds from the financing provider are due to the Company 30 days from the sale of the receivable. In these transactions with the financing provider, the Company surrendered control over the transferred assets. The factored accounts receivable were isolated from the Company and put beyond the reach of creditors, even in the event of bankruptcy. The Company does not maintain effective control over the transferred assets through obligations or rights to redeem, transfer, or repurchase the receivables after they have been transferred.

Pursuant to the financing arrangements for the sale of receivables, the Company sold net receivables of $181.0 million and $120.6 million during the three months ended March 31, 2013 and March 31, 2012, respectively. The Company received cash proceeds from the financing provider of $162.7 million and $178.5 million during the three months ended March 31, 2013 and March 31, 2012, respectively. As of March 31, 2013 and December 31, 2012, the amounts owed by the financing provider were $159.2 million and $147.6 million, respectively, and were recorded in accounts receivable on the Company’s Condensed Consolidated Balance Sheets.

The portion of the receivable financed that has not been recognized as revenue is accounted for as a financing arrangement and is included in other accrued liabilities and other long-term liabilities in the Condensed Consolidated Balance Sheets. As of March 31, 2013 and December 31, 2012, the estimated cash received from the financing provider not recognized as revenue from distributors was $28.5 million and $30.7 million, respectively.

Note 11. Equity

Stock Repurchase Activities

The Company currently has authority granted by the Board of Directors (the "Board") to repurchase up to $1.0 billion of its common stock under its stock repurchase program. As of March 31, 2013, there is $438.3 million of authorized funds remaining under the Company's stock repurchase program. In addition to repurchases under the Company’s stock repurchase program, the Company can also repurchase common stock from its employees in connection with net issuance of shares to satisfy minimum tax withholding obligations for the vesting of certain stock awards.

The Company repurchased and retired approximately 6.2 million shares of its common stock at an average price of $20.99 per share for an aggregate purchase price of $129.9 million during the three months ended March 31, 2013, under its stock repurchase program. The Company repurchased and retired approximately 2.4 million shares of its common stock at an average price of $21.75 per share for an aggregate purchase price of $51.6 million during the three months ended March 31, 2012 under its stock repurchase program. Repurchases associated to net issuances were not significant during the three months ended March 31, 2013 and March 31, 2012.

All shares of common stock repurchased under the Company's stock repurchase program and from its employees in connection with net issuance have been retired. Future share repurchases under the Company’s stock repurchase program will be subject to a review of the circumstances in place at that time and will be made from time to time in private transactions or open market purchases as permitted by securities laws and other legal requirements. This program may be discontinued at any time. See Note 17, Subsequent Events, for discussion of the Company's stock repurchase activity subsequent to March 31, 2013.

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Accumulated Other Comprehensive (Loss) Income, Net of Tax

The components of accumulated other comprehensive (loss) income, net of related taxes, during the three months ended March 31, 2013 were as follows (in millions):

	Unrealized Gains (Losses) on Available-for-Sale Securities[1]	Unrealized Gains (Losses) on Cash Flow Hedges[2]	Foreign Currency Translation Adjustments	Total
Balance as of December 31, 2012	$2.1	$3.0	$(0.4)	$4.7
Other comprehensive loss before reclassifications	(0.2)	(2.1)	(5.8)	(8.1)
Amount reclassified from accumulated other comprehensive (loss) income	(0.4)	(1.4)	—	(1.8)
Other comprehensive loss[3]	(0.6)	(3.5)	(5.8)	(9.9)
Balance as of March 31, 2013	$1.5	$(0.5)	$(6.2)	$(5.2)

(1) The reclassifications out of accumulated comprehensive income during the three months ended March 31, 2013 for realized gains on available-for-sale securities of $0.4 million are included in other expense, net in the Condensed Consolidated Statements of Operations.

(2) The reclassifications out of accumulated comprehensive income during the three months ended March 31, 2013 for realized gains on cash flow hedges are included within cost of revenues of $0.2 million, research and development of $0.4 million, sales and marketing of $0.5 million, and general and administrative of $0.3 million for which the hedged transactions relate in the Condensed Consolidated Statements of Operations.

(3) Taxes related to each component of other comprehensive loss were not material for the three months ended March 31, 2013 and March 31, 2012.

Note 12. Employee Benefit Plans

Share-Based Compensation Plans

The Company’s share-based compensation plans include the 2006 Equity Incentive Plan (the “2006 Plan”), the 2000 Nonstatutory Stock Option Plan (the “2000 Plan”), the Amended and Restated 1996 Stock Plan (the “1996 Plan”), various equity incentive plans assumed through acquisitions, and the 2008 Employee Stock Purchase Plan (the "2008 Purchase Plan"). Under these plans, the Company has granted (or in the case of acquired plans assumed) stock options, restricted stock units ("RSUs"), restricted stock awards ("RSAs"), and performance share awards ("PSAs").

The 2006 Plan was adopted and approved by the Company’s stockholders in May 2006. To date, the Company's stockholders have approved a share reserve of 149.5 million shares of common stock plus the addition of any shares subject to options under the 2000 Plan and the 1996 Plan that were outstanding as of May 18, 2006, and that subsequently expire unexercised, up to a maximum of an additional 75.0 million shares. As of March 31, 2013, the 2006 Plan had 52.5 million shares subject to currently outstanding equity awards and 43.8 million shares available for future issuance.

The 2008 Purchase Plan was adopted in May 2008. To date, the Company's stockholders have approved a share reserve of 19.0 million shares of the Company's common stock for issuance under this plan. The 2008 Purchase Plan permits eligible employees to acquire shares of the Company’s common stock at a 15% discount to the offering price (as determined in the 2008 Purchase Plan) through periodic payroll deductions of up to 10% of base compensation, subject to individual purchase limits of 6,000 shares in any twelve-month period or $25,000 worth of stock, determined at the fair market value of the shares at the time the stock purchase option is granted, in one calendar year. As of March 31, 2013, approximately 11.4 million shares have been issued and 7.6 million shares remain available for future issuance under the 2008 Purchase Plan.

In connection with certain past acquisitions, the Company assumed stock options, RSU, and RSA awards under the assumed stock plans of the acquired companies and exchanged the assumed awards for Juniper Networks' stock options, RSUs, and RSAs, respectively. No new stock options, RSUs, and RSAs can be granted under these plans. As of March 31, 2013, stock options, RSUs and RSAs representing approximately 6.6 million shares of common stock were outstanding under all awards assumed through the Company's acquisitions.

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Juniper Networks, Inc.
Notes to Condensed Consolidated Financial Statements (Continued)
(Unaudited)

Stock Option Activities

The following table summarizes the Company's stock option activity and related information as of and for the three months ended March 31, 2013 (in millions, except for per share amounts and years):

	Outstanding Options				
	Number of Shares		Weighted Average Exercise Price per Share	Weighted Average Remaining Contractual Term (In Years)	Aggregate Intrinsic Value
Balance as of December 31, 2012	34.1		$24.13		
Options granted	—		—		
Options canceled	(0.4	)	31.35		
Options exercised	(2.3	)	16.17		
Options expired	(1.4	)	27.73		
Balance as of March 31, 2013	30.0		$24.46	3.1	$35.8
As of March 31, 2013:					
Vested and expected-to-vest options	29.2		$24.50	3.0	$32.5
Exercisable options	24.5		$24.33	2.4	$18.8

Aggregate intrinsic value represents the difference between the Company's closing stock price on the last trading day of the period, which was $18.54 per share as of March 31, 2013, and the exercise price multiplied by the number of related options. The pre-tax intrinsic value of options exercised, representing the difference between the fair market value of the Company's common stock on the date of the exercise and the exercise price of each option, was $11.9 million for the three months ended March 31, 2013.

Restricted Stock Unit, Restricted Stock Award, and Performance Share Award Activities

The following table summarizes the Company's RSU, RSA, and PSA activity and related information as of and for the three months ended March 31, 2013 (in millions, except per share amounts and years):

	Outstanding RSUs, RSAs, and PSAs				
	Number of Shares		Weighted Average Grant-Date Fair Value per Share	Weighted Average Remaining Contractual Term (In Years)	Aggregate Intrinsic Value
Balance as of December 31, 2012	26.8		$27.76		
RSUs granted	7.7		20.41		
PSAs granted (*)	2.0		21.36		
RSUs vested	(3.8	)	28.80		
PSAs vested	(1.0	)	28.26		
RSAs vested	(0.2	)	19.59		
RSUs canceled	(0.7	)	24.20		
PSAs canceled	(1.8	)	29.05		

Balance as of March 31, 2013	29.0	$25.28	1.7	$538.4
As of March 31, 2013:				
Vested and expected-to-vest RSUs, RSAs, and PSAs	24.9	$23.95	1.6	$461.3

(*) The number of shares subject to PSAs granted represents the aggregate maximum number of shares that may be issued pursuant to the award over its full term. The aggregate number of shares subject to these PSAs that would be issued if performance goals determined by the Compensation Committee are achieved at target is 1.0 million shares. Depending on achievement of such performance goals, the range of shares that could be issued under these awards is 0 to 2.0 million shares.

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Employee Stock Purchase Plan ("ESPP")

The Company's 2008 Purchase Plan is implemented in a series of offering periods, each six months in duration, or a shorter period as determined by the Board. Employees purchased approximately 1.9 million and 1.7 million shares of common stock through the 2008 Purchase Plan at an average per share price of $15.05 and $17.79 for the three months ended March 31, 2013 and March 31, 2012, respectively.

Share-Based Compensation Expense

The weighted-average assumptions used and the resulting estimates of fair value for stock options and ESPP were as follows:

	Three Months Ended March 31,	
	2013	2012
Stock Options:		
Volatility	—	46%
Risk-free interest rate	—	0.8%
Expected life (years)	—	4.2
Dividend yield	—	—
Weighted-average fair value per share	—	$8.51
ESPP:		
Volatility	36%	51%
Risk-free interest rate	0.1%	0.1%
Expected life (years)	0.5	0.5
Dividend yield	—	—
Weighted-average fair value per share	$5.63	$6.38

Share-based compensation expense associated with stock options, ESPP, RSUs, RSAs, and PSAs was recorded in the following cost and expense categories in the Company's Condensed Consolidated Statements of Operations (in millions):

	Three Months Ended March 31,	
	2013	2012
Cost of revenues - Product	$0.9	$1.0
Cost of revenues - Service	4.6	5.3
Research and development	23.6	25.8
Sales and marketing	14.5	21.9
General and administrative	6.3	11.0
Total	$49.9	$65.0

The following table summarizes share-based compensation expense by award type (in millions):

	Three Months Ended March 31,	
	2013	2012
Stock options	$9.5	$17.7
RSUs and PSAs	33.7	41.8
RSAs	3.3	—

ESPP	3.4	5.5
Total	$49.9	$65.0

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Juniper Networks, Inc.
Notes to Condensed Consolidated Financial Statements (Continued)
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The following table presents unrecognized compensation cost, adjusted for estimated forfeitures, recognized over a weighted-average period related to unvested stock options, RSUs, PSAs, and RSAs as of March 31, 2013 (in millions, except years):

	Unrecognized Compensation Cost	Weighted Average Period (In Years)
Stock options	$59.0	2.3
RSUs and PSAs	342.7	2.2
RSAs	$65.2	3.2

Note 13. Segments

The Company’s chief operating decision maker (“CODM”) allocates resources and assesses performance based on financial information of the Company’s divisions. In the first quarter of 2013, the Company consolidated operational oversight and management of all security products within the SSD segment. As a result of this change, security products previously reported in the PSD segment (including the Branch SRX, Branch Firewall, and J Series product families) are now reported in the SSD segment. The Company reclassified the segment data for the prior period to conform to the current period's presentation.

The Company’s PSD segment primarily offers scalable routing and switching products that are used in service provider, enterprise, and public sector networks to control and direct network traffic from data centers, core, edge, aggregation, campus, Wide Area Networks ("WANs"), and customer premise equipment level. The Company's PSD segment consists of routing and switching products and services. Routing products and services include the ACX, E, M, MX, PTX, and T Series. Switching products and services primarily consist of the EX Series and wireless local area network solutions, as well as QFabric™.

The Company's SSD segment offers solutions that meet a broad array of our customers’ priorities, from protecting the users, applications and data on the network to providing network services across a distributed infrastructure. The SSD segment primarily consists of security, software, management, virtualization, routing products and services. Security includes SRX, firewall, vGW Virtual Gateways, virtual private network systems and appliances, secure socket layer virtual private network appliances, intrusion detection and prevention appliances, wide area network optimization platforms, Junos Pulse, and J Series. Software and services for the mobile and wireline network edge include traffic flow monitoring, mobile business services, dynamic application and subscriber awareness, next generation network addressing, as well as the MobileNext architecture for mobile networks. Management and virtualization products include Junosphere, Junos SDK, JunosV App Engine and the network management platform, Junos Space.

The CODM does not allocate to the Company's business segments certain operating expenses managed separately at the corporate level. Direct costs and operating expenses, such as standard cost of goods sold, research and development, and product marketing expenses, are generally applied to each segment. Indirect costs, such as manufacturing overhead and other cost of revenues, are allocated based on factors including headcount, usage, and revenue. Segment contribution margin provides supplemental data on operational performance and is comprised of these direct costs and operating expenses, as well as these indirect costs. Corporate unallocated expenses include: sales, marketing, general and administrative costs, share-based compensation, amortization of purchased intangible assets, restructuring and other charges, gains or losses on equity investments, other expense, net, income taxes, and certain other charges. Segment contribution margin excludes these corporate unallocated expenses.

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The following table summarizes financial information for each segment used by the CODM (in millions):

	Three Months Ended March 31,	
	2013	2012
Net revenues:		
PSD	$809.2	$765.7
SSD	250.0	266.8
Total net revenues	$1,059.2	$1,032.5
Segment contribution margin:		
PSD	$330.1	$276.3
SSD	102.0	110.3
Total segment contribution margin	$432.1	$386.6
Corporate unallocated expenses[1]	$(266.1)	$(263.1)
Amortization of purchased intangible assets[2]	(7.5)	(7.3)
Share-based compensation expense	(49.9)	(65.0)
Share-based payroll tax expense	(3.5)	(0.3)
Restructuring charges[3]	(7.7)	(2.0)
Acquisition and litigation charges	(10.4)	(1.2)
Total operating income	87.0	47.7
Other expense, net	(10.1)	(24.4)
Income before income taxes	$76.9	$23.3

(1) Amount includes unallocated costs for global functions such as sales, marketing, and general and administrative.
(2) Amount includes amortization expense of purchased intangible assets reported in operating expenses and in cost of revenues.
(3) Amount includes restructuring charges reported in operating expenses and in cost of revenues.

Depreciation expense allocated to the PSD segment was $34.4 million and $26.9 million in the three months ended March 31, 2013 and March 31, 2012, respectively. Depreciation expense allocated to the SSD segment was $9.7 million and $9.2 million in the three months ended March 31, 2013 and March 31, 2012, respectively.

The Company attributes revenues to geographic region based on the customer's ship-to location. The following table presents net revenues by geographic region (in millions):

	Three Months Ended March 31,	
	2013	2012
Americas:		
United States	$547.0	$468.4
Other	45.1	62.9
Total Americas	592.1	531.3
Europe, Middle East, and Africa	290.6	307.1
Asia Pacific	176.5	194.1
Total	$1,059.2	$1,032.5

During the three months ended March 31, 2013, AT&T and Verizon Communications, Inc. ("Verizon") accounted for 10.2% and 10.1% of net revenues, respectively. During the three months ended March 31, 2012, Verizon accounted for 12.2% of net revenues.

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The Company tracks assets by physical location. The majority of the Company's assets, excluding cash and cash equivalents and investments, as of March 31, 2013 and December 31, 2012, were attributable to U.S. operations. As of March 31, 2013 and December 31, 2012, gross property and equipment held in the U.S., as a percentage of total property and equipment, was approximately 83% for both periods. Although management reviews asset information on a corporate level and allocates depreciation expense by segment, the CODM does not review asset information on a segment basis.

Note 14. Income Taxes

The Company recorded a tax benefit of $14.1 million and a tax provision of $7.0 million, or effective tax rates of (18.3)% and 30.1% for the three months ended March 31, 2013 and March 31, 2012, respectively.

The effective tax rate for the three months ended March 31, 2013, reflects the Company's recognition of total tax benefits of approximately $43.0 million related to a tax settlement with the Internal Revenue Service ("IRS") and the reinstatement of the U.S. federal research and development ("R&D") tax credit on January 2, 2013.

In March 2013, the Company finalized a closing agreement with the IRS covering specific matters related to the audit of the Company's federal income tax returns for these tax years from 2004 through 2006. As a result of the settlement, the Company recognized a net tax benefit of $27.8 million, which included interest expense of $3.0 million. The Company is no longer subject to an audit of its U.S. federal income taxes through tax year 2006.

On January 2, 2013, the American Taxpayer Relief Act of 2012 retroactively reinstated the U.S. federal R&D tax credit from January 1, 2012 to December 31, 2013. As a result, for the three months ended March 31, 2013, the Company recognized a tax benefit of $15.2 million related to fiscal 2012 R&D credits.

The effective tax rate for the three months ended March 31, 2012, differs from the federal statutory rate of 35% primarily due to the benefit of earnings in foreign jurisdictions, which are subject to lower tax rates, partially offset by an increase in the Company's valuation allowance attributable to investment losses currently disallowed for income tax purposes. The effective rate for the period does not reflect the benefit of the federal R&D credit which had expired on December 31, 2011.

As a result of the IRS tax settlement, the amount of gross unrecognized tax benefits was reduced by approximately $29.1 million. The total amount of gross unrecognized tax benefits was $111.2 million as of March 31, 2013, of which $98.2 million, if recognized, would affect the effective tax rate.

The Company engages in continuous discussions and negotiations with tax authorities regarding tax matters in various jurisdictions. There is a greater than remote likelihood that the balance of the gross unrecognized tax benefits will decrease by approximately $11.1 million within the next twelve months due to lapses of applicable statutes of limitation and the completion of tax review cycles in various tax jurisdictions.

The Company is currently under examination by the IRS for the 2007 through 2009 tax years. The Company is also subject to separate ongoing examinations by the India tax authorities for the 2004 tax year, 2004 through 2008 tax years and the 2009 through 2010 tax years. The Company is not aware of any other examinations by tax authorities in any other major jurisdictions in which it files income tax returns as of March 31, 2013.

In 2008, the Company received a proposed adjustment from the India tax authorities related to the 2004 tax year. In 2009, the India tax authorities commenced a separate investigation of our 2004 through 2008 tax returns and are disputing the Company's determination of taxable income due to the cost basis of certain fixed assets. The Company accrued $4.6 million in penalties and interest in 2009 related to this matter. The Company understands that in accordance with the administrative and judicial process in India, the Company may be required to make payments that are substantially higher than the amount accrued in order to ultimately settle this issue. The Company strongly believes that any assessment it may receive in excess of the amount accrued would be inconsistent with applicable India tax laws and intends to defend this position vigorously.

The Company is pursuing all available administrative procedures relative to these matters. The Company believes that it has adequately provided for any reasonably foreseeable outcomes related to these proposed adjustments and the ultimate resolution of these matters is unlikely to have a material effect on its consolidated financial condition or results of operations; however

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Notes to Condensed Consolidated Financial Statements (Continued)
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there is still a possibility that an adverse outcome of these matters could have a material effect on its consolidated financial condition and results of operations. For more information, see Note 16, Commitments and Contingencies, under the heading "IRS Notices of Proposed Adjustments."

Note 15. Net Income per Share

The Company computed basic and diluted net income per share as follows (in millions, except per share amounts):

	Three Months Ended March 31,	
	2013	2012
Numerator:		
Net income	$91.0	$16.3
Denominator:		
Weighted-average shares used to compute basic net income per share	504.7	527.2
Dilutive effect of employee stock awards	8.0	6.5
Weighted-average shares used to compute diluted net income per share	512.7	533.7
Net income per share:		
Basic	$0.18	$0.03
Diluted	$0.18	$0.03

Basic net income per share is computed using net income available to common stockholders and the weighted-average number of common shares outstanding for the period. Diluted net income per share is computed using net income available to common stockholders and the weighted-average number of common shares outstanding plus potentially dilutive common shares outstanding during the period. Dilutive potential common shares consist of common shares issuable upon exercise of stock options, ESPP issuances, and vesting of RSUs, RSAs, and PSAs.

The Company excludes both outstanding stock options with exercise prices that are greater than the average market price and RSUs and RSAs with grant date fair market value that are greater than the average market price from the calculation of diluted net income per share because their effect would be anti-dilutive. The Company includes the common shares underlying PSAs in the calculation of diluted net income per share when they become contingently issuable and excludes such shares when they are not contingently issuable. Potentially dilutive common shares of approximately 24.7 million and 30.6 million shares were outstanding but were not included in the computation of diluted earnings per share for the three months ended March 31, 2013 and March 31, 2012, respectively.

Note 16. Commitments and Contingencies

Commitments

Operating Leases

The Company leases its facilities and certain equipment under non-cancelable operating leases that expire at various dates through November 30, 2022. Certain leases require the Company to pay variable costs such as taxes, maintenance, and insurance and include renewal options and escalation clauses. Future minimum payments under the non-cancelable operating leases totaled $252.8 million as of March 31, 2013. Rent expense was $13.7 million and $15.7 million for the three months ended March 31, 2013 and March 31, 2012, respectively.

Purchase Commitments

In order to reduce manufacturing lead times and ensure adequate component supply, the Company enters into agreements with contract manufacturers and certain suppliers to procure inventory based on the Company's requirements. A significant portion of the Company's purchase commitments arising from these agreements consists of firm and non-cancelable commitments. These purchase commitments totaled $459.1 million as of March 31, 2013. The Company establishes a liability in connection

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with these purchase commitments related to carrying charges, quantities in excess of our demand forecasts, or obsolete materials charges for materials purchased by contract manufacturers to meet the Company’s forecast or customer orders. As of March 31, 2013, the Company accrued $24.0 million based on its estimate of such charges.

Long-Term Debt and Interest Payment on Long-Term Debt

As of March 31, 2013, the Company held long-term debt consisting of senior notes with a carrying value of $999.2 million. Of these Notes, $300.0 million will mature in 2016 and bears interest at a fixed rate of 3.10%, $300.0 million will mature in 2021 and bears interest at a fixed rate of 4.60%, and $400.0 million will mature in 2041 and bears interest at a fixed rate of 5.95%. Interest on the Notes is payable semiannually. See Note 10, Long-Term Debt and Financing, for further discussion of the Company's long-term debt.

Other Contractual Obligations

As of March 31, 2013, other contractual obligations primarily consisted of $94.4 million in indemnity-related and service related escrows, required by certain asset purchases and acquisitions completed in 2005, 2010, 2011, and 2012, campus build-out obligations of $47.5 million, and other miscellaneous commitments of $14.7 million.

Tax Liabilities

As of March 31, 2013, the Company had $87.1 million included in long-term incomes taxes payable in the Condensed Consolidated Balance Sheets for unrecognized tax positions. At this time, the Company is unable to make a reasonably reliable estimate of the timing of payments related to this amount due to uncertainties in the timing of tax audit outcomes.

Guarantees

The Company enters into agreements with customers that contain indemnification provisions relating to potential situations where claims could be alleged that the Company’s products infringe the intellectual property rights of a third-party. The Company also has financial guarantees consisting of guarantees of product and service performance, guarantees related to third-party customer-financing arrangements, customs and duties guarantees, and standby letters of credit for certain lease facilities. As of March 31, 2013 and December 31, 2012, the Company had $11.7 million and $12.6 million, respectively, in bank guarantees and standby letters of credit related to these financial guarantees.

Legal Proceedings

The Company is involved in disputes, litigation, and other legal actions, including, but not limited to, the matters described below. The Company is aggressively defending its current litigation matters, and while there can be no assurances and the outcome of these matters is currently not determinable, the Company currently believes that there are no existing claims or proceedings that are likely to have a material adverse effect on its financial position. There are many uncertainties associated with any litigation and these actions or other third-party claims against the Company may cause the Company to incur costly litigation and/or substantial settlement charges. In addition, the resolution of any intellectual property litigation may require the Company to make royalty payments, which could adversely affect gross margins in future periods. If any of those events were to occur, the Company's business, financial condition, results of operations, and cash flows could be adversely affected. The actual liability in any such matters may be materially different from the Company's estimates, if any, which could result in the need to adjust the liability and record additional expenses. Unless otherwise noted below, during the period presented, we have not:

recorded any accrual for loss contingencies associated with such legal proceedings; determined that an unfavorable outcome is probable or reasonably possible; or determined that the amount or range of any possible loss is reasonably estimable.

2011 Federal Securities Class Action

On August 15, 2011, a purported securities class action lawsuit, captioned City of Royal Oak Retirement System v. Juniper Networks, Inc., et al., Case No. 11-cv-04003-LHK, was filed in the United States District Court for the Northern District of California naming the Company and certain of its officers and directors as defendants. The complaint alleges that the defendants made false and misleading statements regarding the Company's business and prospects. Plaintiffs seek an

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unspecified amount of monetary damages on behalf of the purported class. On January 9, 2012 the Court appointed City of Omaha Police and Fire Retirement System and City of Bristol Pension Fund as lead plaintiffs. Lead plaintiffs allege that defendants made false and misleading statements about the Company's business and future prospects, and failed to adequately disclose the impact of certain changes in accounting rules. Lead plaintiffs purport to assert claims for violations of Sections 10 (b), 20(a) and 20A of the Securities Exchange Act of 1934 and SEC Rule 10b-5 on behalf of those who purchased or otherwise acquired Juniper Networks' common stock between July 20, 2010 and July 26, 2011, inclusive. On March 14, 2012, Defendants filed motions to dismiss lead plaintiffs' amended complaint. On July 23, 2012, the Court issued an order dismissing the action and giving lead plaintiffs leave to file an amended complaint. Lead plaintiffs filed their second amended complaint on August 20, 2012. Defendants filed a motion to dismiss the second amended complaint on September 17, 2012, and lead plaintiffs filed their opposition on October 22, 2012. Defendants filed their reply brief on November 8, 2012. A hearing on the motion to dismiss is scheduled for May 16, 2013.

2011 California State Derivative Lawsuits

Between August 22 and September 9, 2011, four purported shareholder derivative actions were filed in the Superior Court of the State of California, County of Santa Clara, naming certain of the Company's officers and directors as defendants. The Company is named only as a nominal defendant in the actions. The actions were consolidated as In re Juniper Networks, Inc. Shareholder Litigation, Case No. 1-11-CV-207701 (Lead Case), by order dated September 12, 2011. The complaints are generally based upon the disclosures and alleged omissions challenged in the securities class action. The complaints purport to assert claims against the defendants for breach of fiduciary duties, unjust enrichment, abuse of control, gross mismanagement, and waste of corporate assets. The complaints seek, among other relief, damages in an unspecified amount, restitution, and attorneys' fees and costs. On March 8, 2012, the Company filed a motion to stay the action until resolution of the federal securities class action discussed above, and also filed a demurrer seeking to dismiss the action for the reason that plaintiffs lack standing. The plaintiffs filed oppositions to both motions on April 5, 2012. Defendants filed reply briefs on May 7, 2012. At a hearing on July 27, 2012, the Court ordered that the actions be stayed until such time as the federal court issues an order denying a motion to dismiss in the securities class action, City of Omaha Police and Fire Retirement System v. Juniper Networks, Inc. et al., Case No. CV-11-4003-LHK. The Court deferred deciding the demurrer pending the stay.

2011 Federal Derivative Lawsuit

On September 27, 2011 and December 28, 2011, two purported shareholder derivative actions, captioned Ratinova v. Johnson, et al., Case No. 11-cv-04792 and Lisa E. Coppola, ERA v. Johnson, et al., Case No. 11-cv-06667, respectively, were filed in the United States District Court for the Northern District of California naming certain of the Company's officers and directors as defendants. The Company is named only as a nominal defendant in the action. Like the state derivative actions, the federal derivative lawsuits are generally based upon the disclosures and alleged omissions challenged in the securities class action. The complaints purport to assert claims against the defendants for breach of fiduciary duties and unjust enrichment. The complaints seek, among other relief, damages in an unspecified amount, restitution, and attorneys' fees and costs. By order dated January 30, 2012, the Court consolidated the actions as In re Juniper Networks, Inc. Shareholder Derivative Litigation, Master File No. 11-cv-04792-LHK. On February 3, 2012, the parties filed a stipulation in which the parties requested that the Court stay the action until such time as the Court entered an order denying a motion to dismiss in the related federal securities class action described above. On February 6, 2012, the Court granted the parties' stipulation.

IRS Notices of Proposed Adjustments

The Company is currently under examination by the IRS for the 2007 through 2009 tax years.

In March 2013, the Company executed a closing agreement with the Appeals Division of the IRS related to its intercompany R&D cost sharing arrangement for the license of intangibles acquired in 2004, 2005 and 2006. The Company reached a final resolution with the IRS on all proposed adjustments for all tax years through 2006, which resulted in a settlement of approximately $20.9 million, including interest.

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Note 17. Subsequent Events

Stock Repurchases

Subsequent to March 31, 2013, through the filing of this Report, the Company repurchased 5.0 million shares of its common stock, for $80.0 million at an average purchase price of $16.16 per share, under its stock repurchase program. All of the 5.0 million shares were settled prior to the filing of this Report. Under its stock repurchase program, the Company has $358.3 million authorized funds remaining as of the filing date. Purchases under the Company's stock repurchase program are subject to a review of the circumstances in place at the time and will be made from time to time as permitted by securities laws and other legal requirements. This program may be discontinued at any time.

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

This Quarterly Report on Form 10-Q (“Report”), including “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” contains forward-looking statements regarding future events and the future results of Juniper Networks, Inc. (“we,” “us,” or the “Company”) that are based on our current expectations, estimates, forecasts, and projections about our business, our results of operations, the industry in which we operate and the beliefs and assumptions of our management. Words such as “expects,” “anticipates,” “targets,” “goals,” “projects,” “would,” “c “intends,” “plans,” “believes,” “seeks,” “estimates,” variations of such words, and similar expressions are intended to identify such forward-looking statements. Forward-looking statements by their nature address matters that are, to different degrees, uncertain, and these forward-looking statements are only predictions and are subject to risks, uncertainties, and assumptions that are difficult to predict. Therefore, actual results may differ materially and adversely from those expressed in any forward-looking statements. Factors that might cause or contribute to such differences include, but are not limited to, those discussed in this Report under the section entitled “Risk Factors” in Item 1A of Part II and elsewhere, and in other reports we file with the U.S. Securities and Exchange Commission ("SEC"), specifically our most recent Annual Report on Form 10-K. While forward-looking statements are based on reasonable expectations of our management at the time that they are made, you should not rely on them. We undertake no obligation to revise or update publicly any forward-looking statements for any reason.

The following discussion is based upon our unaudited Condensed Consolidated Financial Statements included in Part 1, Item I, of this Report, which have been prepared in accordance with U.S. generally accepted accounting principles (“U.S. GAAP”). In the course of operating our business, we routinely make decisions as to the timing of the payment of invoices, the collection of receivables, the manufacturing and shipment of products, the fulfillment of orders, the purchase of supplies, and the building of inventory and spare parts, among other matters. Each of these decisions has some impact on the financial results for any given period. In making these decisions, we consider various factors, including contractual obligations, customer satisfaction, competition, internal and external financial targets and expectations, and financial planning objectives.

To aid in understanding our operating results for the periods covered by this Report, we have provided an executive overview and summary of our business and market environment along with a financial results overview. These sections should be read in conjunction with the more detailed discussion and analysis of our consolidated financial condition and results of operations in this Item 2, our “Risk Factors” section included in Item 1A of Part II, and our unaudited Condensed Consolidated Financial Statements and Notes included in Item 1 of Part I of this Report, as well as our audited Consolidated Financial Statements and Notes included in Item 8 of Part II of our Annual Report on Form 10-K for the fiscal year ended December 31, 2012.

Business and Market Environment

At Juniper Networks, we design, develop, and sell products and services that together provide our customers with a high performance network infrastructure built on simplicity, security, openness, and scale. We serve the high-performance networking requirements of global service providers, enterprises, governments, and research and public sector organizations that view the network as critical to their success. Our core competencies in hardware systems, silicon design, network architecture and our open cross-network software platform are helping customers achieve superior performance, greater choice and flexibility, while reducing overall total cost of ownership.

We do business in three geographic regions: Americas, Europe, Middle East and Africa (“EMEA”), and Asia Pacific (“APAC”). Our organizational structure is focused on two business segments: Platform Systems Division ("PSD") and Software Solutions Division ("SSD"). Our PSD segment primarily offers scalable routing and switching products that are used in service provider, enterprise, and public sector networks to control and direct network traffic between data centers, core, edge, aggregation, campus, Wide Area Networks ("WANs"), and consumer and business devices. Our

SSD segment offers solutions focused on network security and network services applications for both service providers and enterprise customers. Both segments offer worldwide services, including technical support and professional services, as well as educational and training programs to our customers. In the first quarter of 2013, we consolidated operational oversight and management of all security products within the SSD segment. As a result of this product realignment, security products previously reported in the PSD segment (including the Branch SRX, Branch Firewall, and J Series product families) are now reported in the SSD segment. We reclassified the segment data for the prior period to conform to the current period's presentation. We believe this change will provide investors with increased financial reporting transparency and will enable better insight into the market and performance trends driving our business.

During the first quarter of 2013, we saw moderate growth in some of our primary markets. We continued to experience an uncertain global macroeconomic environment in which our customers exercised care and conservatism in their investment prioritization and project deployments. We expect that our customers will continue to remain cautious with their capital spending in the near term. We also saw higher product gross margins compared to the same period in 2012, partially due to our

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cost reduction efforts. We believe our product gross margins may decline in the future due to competitive pricing pressure, offset by additional operational improvements and cost efficiencies. Nevertheless, we are focused on executing our strategy to address the market trends of mobile Internet and cloud computing and we continue to see positive long-term fundamentals for high-performance networking.

In the first quarter of 2013, we saw increased momentum with our recent product offerings, including new customer adoption of our QFabric solutions, T4000 Core Routers, and PTX Series Packet Transport switches. Additionally, we experienced new customer wins contributing to the growth in our ACX Series and MX Series. In security, we introduced next-generation products for protecting data center environments, fortified by the Junos Spotlight Secure, a global attacker intelligence service. We also launched new security line cards for the SRX Series to enhance performance and reliability for LTE mobile network operators. We announced an intent to expand our technology partnership with RSA to collaborate on threat intelligence and secure mobile access to help customers detect and prevent advanced threats and enable mobile productivity securely. Further, we completed a business combination that enhances our data center security portfolio.

In the first quarter of 2013, we articulated a clear vision for the industry as well as a pathway for our customers to embrace Software Defined Networking ("SDN") in their networks, helping them make their networks more agile and lower their operating expenses. Additionally, we announced the PTX3000, the world's smallest Converged Supercore to address the scale and flexibility challenges facing service providers as they converge the optical and packet layers of their networks to optimize their business.

We remain focused on improved operational execution, continued innovation, and prudent capital allocation. We continue to believe that the underlying trends driving network investment around the cloud and mobility are intact and remain strong. We continue to align our cost structure with our focused priorities to achieve cost reduction savings of $150.0 million, primarily in operating expenses, and to a lesser extent, in both product and service cost of revenues for the full year 2013, in comparison to our 2012 full year levels.

Financial Results and Key Performance Metrics Overview

The following table provides an overview of our key financial metrics (in millions, except per share amounts, percentages, days sales outstanding ("DSO"), and book-to-bill):

	Three Months Ended March 31,			
	2013	2012	$ Change	% Change
Net revenues	$1,059.2	$1,032.5	$26.7	3 %
Gross Margin	$670.8	$634.1	$36.7	6 %
Percentage of net revenues	63.3 %	61.4 %		
Operating income	$87.0	$47.7	$39.3	82 %
Percentage of net revenues	8.2 %	4.6 %		
Net income	$91.0	$16.3	$74.7	458 %
Percentage of net revenues	8.6 %	1.6 %		
Net income per share:				
Basic	$0.18	$0.03	$0.15	500 %
Diluted	$0.18	$0.03	$0.15	500 %
Operating cash flows	$(8.9)	$102.3	$(111.2)	(109)%
DSO	45	39	6	15 %
Book-to-bill	<1	<1		

Stock repurchase plan activity	$129.9	$51.6	$78.3	152	%

	March 31, 2013	December 31, 2012	$ Change	% Change	
Deferred revenue	$980.7	$923.4	$57.3	6	%

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- Net Revenues: During the three months ended March 31, 2013, we experienced net revenue growth in the Americas, offset by declines in EMEA and APAC compared to the same period in 2012. The year-over-year increase in our net revenues during the three months ended March 31, 2013, was primarily due to an increase in service provider revenue from strong contract renewals and an increase from the sales of our edge routing products and switching products, partially offset by a decline in our high-end security products.

- Gross Margin: Our gross margin as a percentage of revenues increased for the three months ended March 31, 2013, compared to the same period in 2012, due to cost reductions in excess of normal pricing pressures.

- Operating Income: Our operating income increased as a percentage of net revenues during the three months ended March 31, 2013, compared to the same period in 2012, primarily due to the growth in net revenue and gross margin, as we continue to invest in our innovative portfolio, bring new products to market, and optimize our cost structure. The increase was partially offset by litigation charges of $10.3 million for commercial litigation and restructuring charges of $7.7 million recorded during the three months ended March 31, 2013.

- Operating Cash Flows: Operating cash flows decreased during the three months ended March 31, 2013, compared to the same period in 2012, primarily due to timing of receipts from our customers, timing of payments to our supply chain, and an increase in annual payments for incentive compensation.

- DSO: DSO is calculated as the ratio of ending accounts receivable, net of allowances, divided by average daily net sales for the preceding 90 days. DSO for the quarter ended March 31, 2013 increased by 6 days, or 15% compared to the quarter ended March 31, 2012. The increase in DSO was primarily due to a significant volume of shipments at the end of the period which increased our outstanding receivables compared to the same period in 2012.

- Book-to-bill: Book-to-bill represents the ratio of product orders booked divided by product revenues during the respective period. Book-to-bill was less than one for the three months ended March 31, 2013 and March 31, 2012 which is a typical pattern in the first quarter.

- Stock Repurchase Plan Activity: Under our stock repurchase program, we repurchased approximately 6.2 million shares of our common stock in the open market at an average price of $20.99 per share for an aggregate purchase price of $129.9 million during the three months ended March 31, 2013.

- Deferred Revenue: Total deferred revenue increased by $57.3 million to $980.7 million as of March 31, 2013, compared to $923.4 million as of December 31, 2012, primarily due to an increase in deferred service revenue driven by service contract renewals, slightly offset by a decrease in deferred product revenue.

Critical Accounting Policies and Estimates

The preparation of financial statements and related disclosures in conformity with U.S. GAAP requires us to make judgments, assumptions, and estimates that affect the amounts reported in the condensed consolidated financial statements and the accompanying notes. On an ongoing basis, we evaluate our estimates and assumptions. These estimates and assumptions are based on current facts, historical experience, and various other factors that we believe are reasonable under the circumstances to determine reported amounts of assets, liabilities, revenue and expenses that are not readily apparent from other sources.

An accounting policy is considered to be critical if the nature of the estimates or assumptions is material due to the levels of subjectivity and judgment necessary to account for highly uncertain matters or the susceptibility of such matters to change, and the effect of the estimates and assumptions on financial condition or operating performance is material. The accounting policies we believe to reflect our more significant estimates, judgments, and assumptions and are most critical to understanding and evaluating our reported financial results are as follows:

- Inventory Valuation and Contract Manufacturer Liabilities;
- Goodwill and Other Long-Lived Assets;
- Warranty Reserves;
- Revenue Recognition;
- Share-Based Compensation;
- Income Taxes and
- Loss Contingencies.

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During the three months ended March 31, 2013, there were no significant changes to our critical accounting policies and estimates as compared to the critical accounting policies and estimates disclosed in Management's Discussion and Analysis of Financial Condition and Results of Operations contained in Part II, Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2012.

Recent Accounting Pronouncements

See Note 2, Summary of Significant Accounting Policies, in the Notes to Condensed Consolidated Financial Statements in Item 1 of Part I of this Report, for a full description of recent accounting pronouncements, including the actual and expected dates of adoption and estimated effects on our consolidated results of operations and financial condition, which is incorporated herein by reference.

Results of Operations

The following table presents product and service net revenues (in millions, except percentages):

	Three Months Ended March 31,			
	2013	2012	$ Change	% Change
Product	$781.8	$771.9	$9.9	1 %
Percentage of net revenues	73.8 %	74.8 %		
Service	277.4	260.6	16.8	6 %
Percentage of net revenues	26.2 %	25.2 %		
Total net revenues	$1,059.2	$1,032.5	$26.7	3 %

The increase in product revenues during the three months ended March 31, 2013, compared to the same period in 2012, was primarily due to an increase in sales of our routing and switching products, specifically MX and PTX, partially offset by a decrease in sales of security products.

The increase in service revenues during the three months ended March 31, 2013, compared to the same period in 2012, was primarily driven by strong contract renewals from our install base.

Net Revenues by Market and Customer

The following table presents net revenues by market (in millions, except percentages):

	Three Months Ended March 31,			
	2013	2012	$ Change	% Change
Service provider	$712.9	$685.6	$27.3	4 %
Percentage of net revenues	67.3 %	66.4 %		
Enterprise	346.3	346.9	(0.6)	— %
Percentage of net revenues	32.7 %	33.6 %		
Total net revenues	$1,059.2	$1,032.5	$26.7	3 %

We sell our high-performance network products and service offerings from both our PSD and SSD segments to two primary markets: service provider and enterprise. Determination of which market a particular revenue transaction relates to is based primarily upon the customer's industrial classification code, but may also include subjective factors such as the intended use of the product. The service provider market generally includes wireline, wireless, and cable operators, as well as major Internet content and application providers, including those that provide social networking and search engine services. The enterprise market generally comprises businesses; federal, state, and local governments; and research and education institutions.

Net revenues from sales to the service provider market increased during the three months ended March 31, 2013, compared to the same period in 2012, primarily due to increased demand for routing products and growth with large carriers, cable, and content providers in the Americas, partially offset by a decrease in sales with certain large carriers in Eastern Europe, Japan, and Australia.

Net revenues generated from the enterprise market decreased during the three months ended March 31, 2013, compared to the same period in 2012, reflecting a steep decline in federal demand in the Americas.

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During the three months ended March 31, 2013, AT&T and Verizon Communications, Inc. ("Verizon") accounted for 10.2% and 10.1% of net revenues, respectively. During the three months ended March 31, 2012, Verizon accounted for 12.2% of net revenues.

Net Revenues by Geographic Region

The following table presents net revenues by geographic region (in millions, except percentages):

	Three Months Ended March 31,			
	2013	2012	$ Change	% Change
Americas:				
United States	$547.0	$468.4	$78.6	17 %
Other	45.1	62.9	(17.8)	(28)%
Total Americas	592.1	531.3	60.8	11 %
Percentage of net revenues	55.9 %	51.5 %		
EMEA	290.6	307.1	(16.5)	(5)%
Percentage of net revenues	27.4 %	29.7 %		
APAC	176.5	194.1	(17.6)	(9)%
Percentage of net revenues	16.7 %	18.8 %		
Total net revenues	$1,059.2	$1,032.5	$26.7	3 %

Net revenues in the Americas increased during the three months ended March 31, 2013, compared to the same period in 2012, primarily due to an increase in sales to certain large carriers, content providers, and cable providers in the United States, partially offset by a decline in the enterprise market, particularly with federal customers.

Net revenues in EMEA decreased for the three months ended March 31, 2013, compared to the same period in 2012, primarily due to a decrease in sales to certain service provider customers, offset by a slight increase in enterprise customers. For the three months ended March 31, 2013, compared to the same period in 2012, the decrease was primarily in Eastern Europe, partially offset by increased sales in Central Europe and the Middle East.

Net revenues in APAC decreased during the three months ended March 31, 2013, compared to the same period in 2012, primarily due to a decline in sales with certain large service providers in Japan and Australia, partially offset by increases in sales with regional service providers.

Gross Margins

The following table presents gross margins (in millions, except percentages):

	Three Months Ended March 31,			
	2013	2012	$ Change	% Change
Product gross margin	$503.6	$491.3	$12.3	3 %
Percentage of product revenues	64.4 %	63.6 %		
Service gross margin	167.2	142.8	24.4	17 %
Percentage of service revenues	60.3 %	54.8 %		
Total gross margin	$670.8	$634.1	$36.7	6 %
Percentage of net revenues	63.3 %	61.4 %		

Product gross margin percentage increased during the three months ended March 31, 2013, compared to the same period in 2012, primarily due to cost reduction initiatives in excess of normal pricing pressures and a shift in geographical mix.

Service gross margin percentage increased during the three months ended March 31, 2013, compared to the same period in 2012, primarily due to higher service revenue, as well as a reduction in costs and greater efficiency in the delivery of services.

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Operating Expenses

The following table presents operating expenses (in millions, except percentages):

	Three Months Ended March 31,			
	2013	2012	$ Change	% Change
Research and development	$262.2	$269.6	$(7.4)	(3)%
Percentage of net revenues	24.7%	26.1%		
Sales and marketing	255.2	257.7	(2.5)	(1)%
Percentage of net revenues	24.1%	25.0%		
General and administrative	47.8	54.7	(6.9)	(13)%
Percentage of net revenues	4.5%	5.3%		
Amortization of purchased intangible assets	1.2	1.2	—	—%
Percentage of net revenues	0.1%	0.1%		
Restructuring charges	7.0	2.0	5.0	250%
Percentage of net revenues	0.7%	0.2%		
Acquisition and litigation charges	10.4	1.2	9.2	767%
Percentage of net revenues	1.0%	0.1%		
Total operating expenses	$583.8	$586.4	$(2.6)	—%
Percentage of net revenues	55.1%	56.8%		

Our operating expenses have historically been driven by personnel-related costs, including wages, commissions, bonuses, vacation, benefits, share-based compensation, and travel, and we expect this trend to continue. Facility and information technology (“IT”) departmental costs are allocated to other departments based on usage and headcount.

Research and development expense decreased during the three months ended March 31, 2013, compared to the same period in 2012, primarily due to a decrease in personnel-related expenses attributable to lower R&D headcount and share-based compensation expense, as well as a decrease in outside services. The decrease was partially offset by an increase in depreciation expense related to capital expenditures from 2012.

Sales and marketing expense decreased marginally during the three months ended March 31, 2013, compared to the same period in 2012, primarily due to a decrease in personnel-related expenses attributable to lower share-based compensation expense, partially offset by an increase in salaries and fringe resulting from higher sales and marketing headcount as well as an increase in consulting services.

General and administrative expense decreased during the three months ended March 31, 2013, compared to the same period in 2012, primarily due to a decrease in personnel-related expenses related to lower share-based compensation expense.

Restructuring charges increased during the three months ended March 31, 2013, compared to the same period in 2012, due to our 2012 Restructuring Plan. During the three months ended March 31, 2013, we recorded $7.0 million in charges for workforce reductions, facility consolidations or closures, and contract terminations related to our restructuring plans. In connection with our restructuring plans, we expect to record aggregate future charges of approximately $14.0 million through 2013, consisting of approximately $1.0 million and $13.0 million related to the workforce reductions and facility closures and other charges, respectively.

Acquisition and litigation charges increased during the three months ended March 31, 2013, compared to the same period in 2012, primarily due to a litigation charge of $10.3 million for commercial litigation.

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Share-Based Compensation

Share-based compensation expense associated with stock options, employee stock purchases, restricted stock units ("RSUs"), restricted stock awards ("RSAs") and performance share awards ("PSAs") was recorded in the following cost and expense categories (in millions, except percentages):

	Three Months Ended March 31,			
	2013	2012	$ Change	% Change
Cost of revenues - Product	$0.9	$1.0	$(0.1)	(10)%
Cost of revenues - Service	4.6	5.3	(0.7)	(13)%
Research and development	23.6	25.8	(2.2)	(9)%
Sales and marketing	14.5	21.9	(7.4)	(34)%
General and administrative	6.3	11.0	(4.7)	(43)%
Total	$49.9	$65.0	$(15.1)	(23)%

Share-based compensation expense decreased during the three months ended March 31, 2013, compared to the same period in 2012, primarily due to a decrease in actual shares vested and a decline in grant date fair values due to lower stock prices.

Effect of Foreign Currency

For the three months ended March 31, 2013 and March 31, 2012, foreign currency fluctuations were not material.

Other Expense, Net and Income Tax (Benefit) Provision

The following table presents other expense, net and income tax (benefit) provision (in millions, except percentages):

	Three Months Ended March 31,			
	2013	2012	$ Change	% Change
Interest income	$2.1	$2.8	$(0.7)	(25)%
Interest expense	(14.3)	(14.2)	(0.1)	1%
Other	2.1	(13.0)	15.1	(116)%
Total other expense, net	$(10.1)	$(24.4)	$14.3	(59)%
Percentage of net revenues	(1.0)%	(2.4)%		
Income tax (benefit) provision	$(14.1)	$7.0	$(21.1)	(301)%
Effective tax rate	(18.3)%	30.1%		

Interest income primarily includes interest income from our cash, cash equivalents, and investments. Interest expense primarily includes interest, net of capitalized interest expense from our long-term debt and customer financing arrangements. Other typically consists of investment and foreign exchange gains and losses and other non-operational income and expense items. During the three months ended March 31, 2013, Other was primarily comprised of a $1.6 million gain related to a privately-held investment. During the three months ended March 31, 2012, Other was primarily comprised of an other-than-temporary impairment charge of $14.0 million, related to a privately-held equity investment.

The effective tax rate for the three months ended March 31, 2013, reflects our recognition of total tax benefits of approximately $43.0 million related to a tax settlement with the Internal Revenue Service (“IRS”) and to the reinstatement of the U.S. federal research and development (“R&D”) tax credit on January 2, 2013.

The effective tax rate for the three months ended March 31, 2012, differs from the federal statutory rate of 35% primarily due to the benefit of earnings in foreign jurisdictions, which are subject to lower tax rates, partially offset by an increase in the Company's valuation allowance attributable to investment losses currently disallowed for income tax purposes. The effective rate for the period does not reflect the benefit of the federal R&D credit which had expired on December 31, 2011.

For further explanation of our income tax (benefit) provision, see Note 14, Income Taxes, in Notes to Condensed Consolidated Financial Statements in Item 1 of Part I of this Report.

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Segment Information

For a description of the products and services for each segment, see Note 13, Segments, in Notes to Condensed Consolidated Financial Statements in Item I of Part I of this Report.

Platform Systems Division Segment
(in millions, except percentages)

	Three Months Ended March 31, 2013	2012	$ Change	% Change
PSD product revenues:				
Routing	$488.1	$457.6	$30.5	7 %
Switching	131.5	123.5	8.0	6 %
Total PSD product revenues	619.6	581.1	38.5	7 %
PSD service revenues	189.6	184.6	5.0	3 %
Total PSD revenues	$809.2	$765.7	$43.5	6 %
PSD contribution margin (*)	$330.1	$276.3	$53.8	19 %
Percentage of PSD revenues	40.8 %	36.1 %		

(*) A reconciliation of total segment operating income to income before taxes can be found in Note 13, Segments, in Notes to Condensed Consolidated Financial Statements in Item I of this Report.

During the three months ended March 31, 2013, PSD product revenues increased, compared to the same period in 2012, primarily due to growth in sales of our routing and switching products, specifically MX and PTX.

During the three months ended March 31, 2013, PSD service revenues increased, compared to the same period in 2012, primarily due to strong contract renewals of support services.

PSD contribution margin as a percent of PSD revenues increased during the three months ended March 31, 2013, compared to the same period in 2012, due to a combination of revenue growth, an expansion of gross margin, and a reduction in operating expenses.

Software Solutions Division Segment
(in millions, except percentages)

	Three Months Ended March 31, 2013	2012	$ Change	% Change
SSD product revenues:				
Security	$136.7	$168.2	$(31.5)	(19)%
Routing	25.5	22.6	2.9	13 %
Total SSD product revenues	162.2	190.8	(28.6)	(15)%
SSD service revenues	87.8	76.0	11.8	16 %
Total SSD revenues	$250.0	$266.8	$(16.8)	(6)%
SSD contribution margin (*)	$102.0	$110.3	$(8.3)	(8)%
Percentage of SSD revenues	40.8 %	41.3 %		

(*) A reconciliation of total segment operating income to income before taxes can be found in Note 13, Segments, in Notes to Condensed Consolidated Financial Statement in Item I of this Report.

During the three months ended March 31, 2013, SSD product revenues decreased, compared to the same period in 2012, primarily due to a decline in sales of our high-end SRX products and our firewall products.

During the three months ended March 31, 2013, SSD service revenues increased, compared to the same period in 2012, due to contract renewals of support services.

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SSD contribution margin as a percentage of SSD revenues decreased during the three months ended March 31, 2013, compared to the same period in 2012, due to lower revenue and a decrease in gross margin, partially offset by a reduction in operating expenses.

Liquidity and Capital Resources

Historically, we have funded our business primarily through our operating activities and the issuance of our common stock, and more recently, the issuance of our long-term debt. The following table presents our capital resources (in millions, except percentages):

	As of March 31, 2013	December 31, 2012	$ Change	% Change
Working capital	$2,116.3	$2,178.7	$(62.4)	(3)%
Cash and cash equivalents	$2,043.7	$2,407.8	$(364.1)	(15)%
Short-term investments	613.1	441.5	171.6	39%
Long-term investments	1,015.2	988.1	27.1	3%
Total cash, cash equivalents, and investments	3,672.0	3,837.4	(165.4)	(4)%
Long-term debt	999.2	999.2	—	—%
Net cash, cash equivalents, and investments	$2,672.8	$2,838.2	$(165.4)	(6)%

The significant components of our working capital are cash and cash equivalents, short-term investments, and accounts receivable, reduced by accounts payable, accrued liabilities, and short-term deferred revenue. Working capital decreased by $62.4 million during the three months ended March 31, 2013, primarily due to a decrease in cash and cash equivalents partially offset by increases in short-term investments and accounts receivable.

Summary of Cash Flows

During the three months ended March 31, 2013, cash and cash equivalents decreased by $364.1 million. The decrease was the result of cash used in our operating, investing, and financing activities of $8.9 million, $285.1 million, and $70.1 million, respectively.

Operating Activities

Net cash used in operations for the three months ended March 31, 2013, was $8.9 million, compared to net cash provided by operations of $102.3 million for the same period in 2012. The net cash outflows for the three months ended March 31, 2013, were attributable to an increase in accounts receivable of $94.3 million due to a significant volume of shipments at the end of the quarter, $59.6 million prepaid in connection with consolidating our contract manufacturers from three to two, and to a lesser extent, annual payments for incentive compensation.

Investing Activities

For the three months ended March 31, 2013, net cash used in investing activities was $285.1 million, compared to $93.3 million for the three months ended March 31, 2012. The increase in net cash used in investing activities was primarily due to purchases of available-for sale investments partially offset by proceeds from the sale of available-for-sale investments.

Financing Activities

Net cash used in financing activities was $70.1 million for the three months ended March 31, 2013, compared to $6.3 million for the same period in 2012. The increase in net cash used in financing activities was primarily due to purchases and retirement of our common stock partially offset by an increase in proceeds from employee stock option exercises.

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Stock Repurchase Activities

We currently have authority granted by the Board of Directors (the "Board") to repurchase up to $1.0 billion of our common stock under our stock repurchase program. As of March 31, 2013, there is $438.3 million of authorized funds remaining under our stock repurchase program.

During the three months ended March 31, 2013, we repurchased and retired approximately 6.2 million shares of our common stock under our stock repurchase program at an average price of $20.99 per share for an aggregate purchase price of $129.9 million.

Restructuring

As of March 31, 2013, our restructuring liability was approximately $14.0 million of which approximately $8.2 million related to severance and contract termination charges, which are expected to be substantially paid during the third quarter of fiscal 2013. The remaining $5.8 million related to facility closures are expected to be paid through March 2018.

Deferred Revenue

The following table summarizes our deferred product and service revenues (in millions):

	As of March 31, 2013	December 31, 2012
Deferred product revenue:		
Undelivered product commitments and other product deferrals	$250.5	$256.9
Distributor inventory and other sell-through items	122.7	138.4
Deferred gross product revenue	373.2	395.3
Deferred cost of product revenue	(86.4)	(99.4)
Deferred product revenue, net	286.8	295.9
Deferred service revenue	693.9	627.5
Total	$980.7	$923.4

As of March 31, 2013, net deferred product revenue decreased by $9.1 million compared to December 31, 2012, primarily due to releases of product revenue. As of March 31, 2013, the increase in deferred service revenue of $66.4 million compared to December 31, 2012, was driven by service contract renewals.

Off-Balance Sheet Arrangements

As of March 31, 2013, we did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. It is not our business practice to enter into off-balance sheet arrangements. However, in the normal course of business, we enter into contracts consisting of guarantees of product and service performance, guarantees related to third-party customer-financing arrangements, customs and duties guarantees, and standby letters of credit for certain lease facilities. See Note 16, Commitments and Contingencies, in Notes to the Condensed Consolidated Financial Statements in Item 1 of Part I of this Report for additional information regarding our guarantees.

Contractual Obligations

As of March 31, 2013, our principle commitments consist of obligations under operating leases, purchase commitments, debt, and other contractual obligations. There have been no significant changes to these obligations during the three months ended March 31, 2013 compared to the contractual obligations disclosed in Management's Discussion and Analysis of Financial Condition and Results of Operations, set forth in Part II, Item 7, of our Annual Report on Form 10-K for the fiscal year ended December 31, 2012.

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Guarantees

We have entered into agreements with customers that contain indemnification provisions relating to potential situations where claims could be alleged that our products infringe the intellectual property rights of a third-party. We also have financial guarantees consisting of guarantees of product and service performance, guarantees related to third-party customer-financing arrangements, customs and duties guarantees, and standby letters of credit for certain lease facilities. As of March 31, 2013 and December 31, 2012, we had $11.7 million and $12.6 million, respectively, in bank guarantees and standby letters of credit related to these financial guarantees.

Liquidity and Capital Resource Requirements

Liquidity and capital resources may be impacted by our operating activities as well as acquisitions and investments in strategic relationships that we have made or we may make in the future. Additionally, if we were to repurchase additional shares of our common stock under our stock repurchase program, our liquidity may be impacted. As of March 31, 2013, 60% of our cash and investment balances were held outside of the U.S., which may be subject to U.S. taxes if repatriated.

In August 2010, we filed a $1.5 billion shelf registration with the SEC. In March 2011, we issued notes in the amount of $1.0 billion under the shelf registration statement. Therefore, while we have no current plans to do so, we may issue up to $500 million in additional securities under the shelf registration statement. The shelf registration is intended to give us flexibility to take advantage of financing opportunities as needed or deemed desirable in light of market conditions. Any additional offerings of securities under the shelf registration statement will be made pursuant to a prospectus.

We have been focused on managing our annual equity usage as a percentage of the common stock outstanding to align with peer group competitive levels and have made changes in recent years to reduce the number of shares underlying the equity awards we grant. For fiscal year 2013, we intend to target the number of shares underlying equity awards granted on an annual basis at 2.75% or less of our common stock outstanding. Based upon shares underlying our grants to date of options, RSUs, RSAs, and PSAs (counting only the on-target measure of such PSAs), we believe we are on track with respect to this goal for 2013.

Based on past performance and current expectations, we believe that our existing cash and cash equivalents, short-term, and long-term investments (which includes the proceeds from the issuance of our long-term debt), together with cash generated from operations as well as cash generated from the exercise of stock options and purchases under our employee stock purchase plan will be sufficient to fund our operations and anticipated growth for at least the next twelve months. We believe our working capital is sufficient to meet our liquidity requirements for capital expenditures, commitments, and other liquidity requirements associated with our existing operations during the same period. However, our future liquidity and capital requirements may vary materially from those now planned depending on many factors, including:

- level and mix of our product, sales, and gross profit margins;

- our business, product, capital expenditures and R&D plans;

- repurchases of our common stock;

- incurrence and repayment of debt and related interest obligations;

- litigation expenses, settlements, and judgments, or similar items related to resolution of tax audits;

- volume price discounts and customer rebates;
- accounts receivable levels that we maintain;
- acquisitions and/or funding of other businesses, assets, products, or technologies;
- changes in our compensation policies;
- capital improvements for new and existing facilities;
- technological advances;

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- our competitors' responses to our products and/or pricing;
- our relationships with suppliers, partners, and customers;
- possible future investments in raw material and finished goods inventories;
- expenses related to future restructuring plans, if any;
- tax expense associated with share-based awards;
- issuance of share-based awards and the related payment in cash for withholding taxes in the current year and possibly during future years;
- level of exercises of stock options and stock purchases under our equity incentive plans; and
- general economic conditions and specific conditions in our industry and markets, including the effects of disruptions in global credit and financial markets, international conflicts, and related uncertainties.

Factors That May Affect Future Results

A description of the risk factors associated with our business is included under “Risk Factors” in Item 1A of Part II of this Report.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Our exposures to market risk have not changed materially since December 31, 2012. For quantitative and qualitative disclosures about market risk, see Item 7A Quantitative and Qualitative Disclosures About Market Risk, in our Annual Report on Form 10-K for the year ended December 31, 2012.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Attached, as exhibits to this report are certifications of our principal executive officer and principal financial officer, which are required in accordance with Rule 13a-14 of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). This “Controls and Procedures” section includes information concerning the controls and related evaluations referred to in the certifications and it should be read in conjunction with the certifications for a more complete understanding of the topics presented.

We carried out an evaluation, under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act. Based upon that evaluation, our principal executive officer and principal financial officer concluded that, as of the end of the period covered in this report, our disclosure controls and procedures were effective to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in Securities and Exchange Commission rules and forms and is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Controls

There were no changes in our internal control over financial reporting that occurred during the first quarter of 2013 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Inherent Limitations on Effectiveness of Controls

Our management, including the Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"), does not expect that our disclosure controls or our internal control over financial reporting will prevent or detect all error and all fraud. A control

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

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PART II — OTHER INFORMATION

Item 1. Legal Proceedings

The information set forth under the “Legal Proceedings” section in Note 16, Commitments and Contingencies, in Notes to Condensed Consolidated Financial Statements in Item 1 of Part I of this Report, is incorporated herein by reference.

Item 1A. Risk Factors

Factors That May Affect Future Results

Investments in our securities involve significant risks. The market price of our stock has historically reflected a higher multiple of earnings than many other companies. Accordingly, even small changes in investor expectations for our future growth and earnings, whether as a result of actual or rumored financial or operating results, changes in the mix of the products and services sold, acquisitions, industry changes, or other factors, could trigger, and have triggered in the past, significant fluctuations in the market price of our common stock. Investors in our securities should carefully consider all of the relevant factors disclosed by us, including, but not limited to, the following factors, that could affect our business, operating results and stock price.

Our quarterly results are unpredictable and subject to substantial fluctuations, and, as a result, we may fail to meet the expectations of securities analysts and investors, which could adversely affect the trading price of our common stock.

Our revenues and operating results may vary significantly from quarter-to-quarter due to a number of factors, many of which are outside of our control and any of which may cause our stock price to fluctuate.

The factors that may cause our quarterly results to vary quarter by quarter and be unpredictable include, but are not limited to: limited visibility into customer spending plans, changes in the mix of products and services sold, changes in geographies in which our products and services are sold, changing market and economic conditions, current and potential customer consolidation, competition, customer concentration, long sales and implementation cycles, regional economic and political conditions, and seasonality. For example, we, and many companies in our industry, experience adverse seasonal fluctuations in customer spending, particularly in the first and third quarters. Market trends, competitive pressures, commoditization of products, seasonal rebates, increased component or shipping costs, regulatory impacts and other factors may result in reductions in revenue or pressure on gross margins of certain segments in a given period, which may necessitate adjustments to our operations.

As a result of these factors, as well as other variables affecting our operating results, we believe that quarter-to-quarter comparisons of operating results are not necessarily a good indication of what our future performance will be. It is likely that in some future quarters, our operating results may be below our guidance, our long-term financial model or the expectations of securities analysts or investors, in which case the price of our common stock may decline. Such a decline could occur, and has occurred in the past, even when we have met our publicly stated revenues and/or earnings guidance.

Fluctuating economic conditions make it difficult to predict revenues for a particular period and a shortfall in revenues or increase in costs of production may harm our operating results.

Our revenues and gross margin depend significantly on general economic conditions and the demand for products in the markets in which we compete. Economic weakness, customer financial difficulties, and constrained spending on network expansion and enterprise infrastructure have in the past resulted in, and may in the future result in, decreased revenues and earnings. Such factors could make it difficult to accurately forecast sales and operating results and could negatively affect our ability to provide accurate forecasts to our contract manufacturers and manage our contract manufacturer relationships and other expenses. In addition, economic uncertainty concerns over the sovereign debt situation in certain countries in the European Union, as well as continued turmoil in the geopolitical environment in many parts of the world, have, and may continue to, put pressure on global economic conditions, which has led, and could continue to lead, to reduced demand for our products, to delays or reductions in network expansions or infrastructure projects, and/or higher costs of production. Economic weakness may also lead to longer collection cycles for payments due from our customers, an increase in customer bad debt, restructuring initiatives and associated expenses, and impairment of investments. Furthermore, continued weakness and the sovereign debt situation in certain countries in the European Union, may adversely impact the ability of our customers to adequately fund their expected capital expenditures, which could lead to delays or cancellations of planned purchases of our products or services. In addition, our operating expenses are largely based on anticipated revenue trends and a high percentage of our expenses is, and will continue to be, fixed in the short and medium term.

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Uncertainty about future economic conditions also makes it difficult to forecast operating results and to make decisions about future investments. Future or continued economic weakness, failure of our customers and markets to recover from such weakness, customer financial difficulties, increases in costs of production, and reductions in spending on network maintenance and expansion could have a material adverse effect on demand for our products and consequently on our business, financial condition, and results of operations.

A limited number of our customers comprise a significant portion of our revenues and there is an ongoing trend toward consolidation in the industry in which our customers and partners operate. Any decrease in revenues from our customers or partners could have an adverse effect on our net revenues and operating results.

A substantial majority of our net revenues depend on sales to a limited number of customers and distribution partners. For example, AT&T and Verizon accounted for greater than 10% of our net revenues during the first quarter of 2013. Changes in the business requirements, vendor selection, financial prospects, capital resources, and expenditures, or purchasing behavior (including product mix purchased) of our key customers could significantly decrease sales to such customers or could lead to delays or cancellations of planned purchases of our products or services, which increases the risk of quarterly fluctuations in our revenues and operating results. Any of these factors could adversely affect our business, financial condition, and results of operations.

In addition, in recent years, there has been movement towards consolidation in the telecommunications industry (for example, the acquisitions of Global Crossing by Level 3 Communications and Qwest Communications by CenturyLink and Softbank's proposed purchase of a controlling interest in Sprint Nextel) and that consolidation trend has continued. If our customers or partners are parties to consolidation transactions they may delay, suspend or indefinitely reduce or cancel their purchases of our products or other unforeseen consequences could harm our business, financial condition, and results of operations.

The long sales and implementation cycles for our products, as well as our expectation that some customers will sporadically place large orders with short lead times, may cause our revenues and operating results to vary significantly from quarter-to-quarter.

A customer's decision to purchase certain of our products, particularly new products, involves a significant commitment of its resources and a lengthy evaluation and product qualification process. As a result, the sales cycle may be lengthy. In particular, customers making critical decisions regarding the design and implementation of large network deployments may engage in very lengthy procurement processes that may delay or impact expected future orders. Throughout the sales cycle, we may spend considerable time educating and providing information to prospective customers regarding the use and benefits of our products. Even after making the decision to purchase, customers may deploy our products slowly and deliberately. Timing of deployment can vary widely and depends on the skill set of the customer, the size of the network deployment, the complexity of the customer's network environment, and the degree of hardware and operating system configuration necessary to deploy the products. Customers with large networks usually expand their networks in large increments on a periodic basis. Accordingly, we may receive purchase orders for significant dollar amounts on an irregular basis. These long cycles, as well as our expectation that customers will tend to sporadically place large orders with short lead times, both of which may be exacerbated by the impact of continued global economic weakness, may cause revenues and operating results to vary significantly and unexpectedly from quarter-to-quarter.

We face intense competition that could reduce our revenues and adversely affect our business and financial results.

Competition is intense in the markets that we address. The PSD market has historically been dominated by Cisco, with competition coming from other companies such as Alcatel-Lucent, Brocade, Extreme Networks, Hewlett Packard Company, and Huawei. In the SSD market, we face intense competition from a broader group of companies such as

Check Point, Cisco, F5 Networks, Palo Alto Networks, and Fortinet. Further, a number of other small public and private companies have products or have announced plans for new products to address the same challenges and markets that our products address.

In addition, actual or speculated consolidation among competitors, or the acquisition of our partners and/or resellers by competitors, can increase the competitive pressures faced by us as customers may delay spending decisions or not purchase our products at all. In this regard, Oracle acquired Acme Packet, Inc. in 2013 and Cisco acquired Meraki Networks, Inc. in 2013. A number of our competitors have substantially greater resources and can offer a wider range of products and services for the overall network equipment market than we do. If we are unable to compete successfully against existing and future competitors on the basis of product offerings or price, we could experience a loss in market share and revenues and/or be required to reduce prices, which could reduce our gross margins, and which could materially and adversely affect our business, financial condition, and results of operations.

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We expect our gross margins to vary over time, and the level of product gross margins achieved by us in recent years may not be sustainable.

We expect our product gross margins to vary from quarter-to-quarter, and the gross margins we have achieved in recent years may not be sustainable and may be adversely affected in the future by numerous factors, including customer, product and geographic mix shifts, increased price competition in one or more of the markets in which we compete, increases in material or labor costs, increases in inventory carrying costs, excess product component or obsolescence charges from our contract manufacturers, increased costs due to changes in component pricing or charges incurred due to component holding periods if we do not accurately forecast product demand, warranty related issues, or our introduction of new products or entry into new markets with different pricing and cost structures. For example, in the third quarter of fiscal 2012, our margins declined as a result of an inventory charge resulting from inventory we held in excess of forecasted demand. Failure to sustain or improve our gross margins reduces our profitability and may have a material adverse effect on our business and stock price.

If we receive product orders late in a quarter, we may be unable to recognize revenue for these orders in the same period, which could adversely affect our quarterly revenues.

Generally, our PSD products are not stocked by distributors or resellers due to their cost and complexity and configurations required by our customers, and we generally build such products as orders are received. In recent years, the volume of orders received late in any given fiscal quarter has generally continued to increase but remains unpredictable. If orders for certain products are received late in any quarter, we may not be able to build, ship, and recognize revenue for these orders in the same period, which could adversely affect our ability to meet our expected revenues for such quarter. Additionally, we determine our operating expenses largely on the basis of anticipated revenues and a high percentage of our expenses are fixed in the short and medium term. As a result, a failure or delay in generating or recognizing revenue could cause significant variations in our operating results and operating margin from quarter-to-quarter.

We are dependent on sole source and limited source suppliers for several key components, which makes us susceptible to shortages or price fluctuations in our supply chain, and we may face increased challenges in supply chain management in the future.

During periods of high demand for electronic products, component shortages are possible, and the predictability of the availability of such components may be limited. Any future growth in our business, IT spending and the economy in general is likely to create greater pressures on us and our suppliers to accurately forecast overall component demand and to establish optimal component inventories. If shortages or delays persist, the price of these components may increase, or the components may not be available at all. We may not be able to secure enough components at reasonable prices or of acceptable quality to build new products in a timely manner, and our revenues and gross margins could suffer until other sources can be developed. For example, from time to time, we have experienced component shortages that resulted in delays of product shipments. We currently purchase numerous key components, including ASICs, from single or limited sources. The development of alternate sources for those components is time-consuming, difficult, and costly. In addition, the lead times associated with certain components are lengthy and preclude rapid changes in quantities and delivery schedules. Also, long-term supply and maintenance obligations to customers increase the duration for which specific components are required, which may further increase the risk of component shortages or the cost of carrying inventory. In the event of a component shortage or supply interruption from these suppliers, we may not be able to develop alternate or second sources in a timely manner. If we are unable to buy these components in quantities sufficient to meet our requirements on a timely basis, we will not be able to deliver product to our customers, which would seriously affect present and future sales, which would, in turn, adversely affect our business, financial condition, and results of operations.

In addition, the development, licensing, or acquisition of new products in the future may increase the complexity of supply chain management. Failure to effectively manage the supply of key components and products would adversely affect our business.

We rely on value-added and other resellers, as well as distribution partners, to sell our products, and disruptions to, or our failure to effectively develop and manage, our distribution channel and the processes and procedures that support it could adversely affect our ability to generate revenues from the sale of our products.

Our future success is highly dependent upon establishing and maintaining successful relationships with a variety of value-added and other reseller and distribution partners, including our worldwide strategic partners such as Ericsson, IBM, and NSN. The majority of our revenues are derived through value-added resellers and distributors, most of which also sell our competitors' products, and some of which sell their own products that compete with our products. Our revenues depend in part on the performance of these partners. The loss of or reduction in sales to our value-added resellers or distributors could materially reduce our revenues. For example, in 2006, one of our largest resellers, Lucent, was acquired by Alcatel, a competitor of ours. As a result of the merger, Lucent became a competitor, their resale of our products declined, and we ultimately terminated our reseller agreement with Lucent. Our competitors may in some cases be effective in leveraging their market share positions or in providing incentives to current or potential resellers and distributors to favor their products or to prevent or reduce sales of our products. If we fail to develop and maintain relationships with our partners, fail to develop new relationships with value-added resellers and distributors in new markets, or expand the number of distributors and resellers in existing markets, fail to manage, train or motivate existing value-added resellers and distributors effectively, or if these partners are not successful in their sales efforts, sales of our products may decrease, and our business, financial condition, and results of operations would suffer.

In addition, we recognize a portion of our revenues based on a sell-through model using information provided by our distributors. If those distributors provide us with inaccurate or untimely information, the amount or timing of our revenues could be adversely impacted.

Further, in order to develop and expand our distribution channel, we must continue to offer attractive channel programs to potential partners and scale and improve our processes and procedures that support the channel. As a result, our programs, processes and procedures may become increasingly complex and inherently difficult to manage. We have previously entered into OEM agreements with partners pursuant to which they rebrand and resell our products as part of their product portfolios. These types of relationships are complex and require additional processes and procedures that may be challenging and costly to implement, maintain and manage. Our failure to successfully manage and develop our distribution channel and the programs, processes and procedures that support it could adversely affect our ability to generate revenues from the sale of our products.

Our ability to process orders and ship products in a timely manner is dependent in part on our business systems and performance of the systems and processes of third parties such as our contract manufacturers, suppliers, or other partners, as well as the interfaces between our systems and the systems of such third parties. If our systems, the systems and processes of those third parties, or the interfaces between them experience delays or fail, our business processes and our ability to build and ship products could be impacted, and our financial results could be harmed.

Some of our business processes depend upon our information technology ("IT") systems, the systems, and processes of third parties and on the interfaces of our systems with the systems of third parties. For example, our order entry system feeds information into the systems of our contract manufacturers, which enables them to build and ship our products. If those systems fail or are interrupted, our processes may function at a diminished level or not at all. This could negatively impact our ability to ship products or otherwise operate our business, and our financial results could be harmed. For example, although it did not adversely affect our shipments, an earthquake in late December of 2006 disrupted our communications with China, where a significant part of our manufacturing occurs.

We also rely upon the performance of the systems and processes of our contract manufacturers to build and ship our products. If those systems and processes experience interruption or delay, our ability to build and ship our products in a timely manner may be harmed. For example, as we have expanded our contract manufacturing base to China, we have experienced instances where our contract manufacturer was not able to ship products in the time periods expected by us. If we are not able to ship our products or if product shipments are delayed, our ability to recognize revenue in a timely manner for those products would be affected and our financial results could be harmed.

Telecommunications companies and our other large customers generally require more onerous terms and conditions in our contracts with them. As we seek to sell more products to such customers, we may be required to agree to terms and conditions that could have an adverse effect on our business or ability to recognize revenues.

Telecommunications service provider companies, which comprise a significant portion of our customer base, and other large companies, because of their size, generally have greater purchasing power and, accordingly, have requested and received more favorable terms from others, which often translate into more onerous terms and conditions from us. Recently, France Telecom-Orange and Deutsche Telekom AG have formed a company for the purpose of purchasing products from, and negotiating more favorable contractual terms with, suppliers. As we seek to sell more products to this class of customer, we may be required to agree to such terms and conditions, which may include terms that affect the timing of our ability to recognize revenue and have an adverse effect on our business, financial condition, and results of operations. Consolidation among such large customers can further increase their buying power and ability to require onerous terms.

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In addition, telecommunications service providers have purchased products from other vendors who promised but failed to deliver certain functionality and/or had products that caused problems or outages in the networks of these customers. As a result, these customers may request additional features from us and require substantial penalties for failure to deliver such features or may require substantial penalties for any network outages that may be caused by our products. These additional requests and penalties, if we are required to agree to them, may require us to defer revenue recognition from such sales, which may negatively affect our business, financial condition, and results of operations.

System security risks, data protection breaches, and cyber-attacks could compromise our proprietary information, disrupt our internal operations and harm public perception of our security products, which could cause our business and reputation to suffer and adversely affect our stock price.

In the ordinary course of business, we store sensitive data, including intellectual property, our proprietary business information and that of our customers, suppliers and business partners on our networks. The secure maintenance of this information is critical to our operations and business strategy. Increasingly, companies, including Juniper Networks, are subject to a wide variety of attacks on their networks on an ongoing basis. Despite our security measures, Juniper Networks' information technology and infrastructure may be vulnerable to penetration or attacks by computer programmers and hackers, or breached due to employee error, malfeasance or other disruptions. Any such breach could compromise our networks, creating system disruptions or slowdowns and exploiting security vulnerabilities of our products, and the information stored on our networks could be accessed, publicly disclosed, lost or stolen, which could subject us to liability to our customers, suppliers, business partners and others, and cause us reputational and financial harm. In addition, sophisticated hardware and operating system software and applications that we produce or procure from third parties may contain defects in design or manufacture, including "bugs" and other problems that could unexpectedly interfere with the operation of our networks.

If an actual or perceived breach of network security occurs in our network or in the network of a customer of our security products, regardless of whether the breach is attributable to our products, the market perception of the effectiveness of our products could be harmed. Because the techniques used by computer programmers and hackers, many of whom are highly sophisticated and well-funded, to access or sabotage networks change frequently and generally are not recognized until after they are used, we may be unable to anticipate or immediately detect these techniques. This could impede our sales, manufacturing, distribution or other critical functions. In addition, the economic costs to us to eliminate or alleviate cyber or other security problems, bugs, viruses, worms, malicious software systems and security vulnerabilities could be significant and may be difficult to anticipate or measure because the damage may differ based on the identity and motive of the programmer or hacker, which are often difficult to identify.

Regulation of the telecommunications industry could harm our operating results and future prospects.

The traditional telecommunications industry is highly regulated, and our business and financial condition could be adversely affected by changes in regulations relating to the Internet telecommunications industry. Currently, there are few laws or regulations that apply directly to access to or commerce on IP networks, but future regulations could include sales taxes on products sold via the Internet and Internet service provider access charges. We could be adversely affected by regulation of IP networks and commerce in any country where we market equipment and services to service or content providers. Regulations governing the range of services and business models that can be offered by service providers or content providers could adversely affect those customers' needs for products designed to enable a wide range of such services or business models. For instance, the U.S. Federal Communications Commission has issued regulations governing aspects of fixed broadband networks and wireless networks; these regulations might impact service provider and content provider business models and as such, providers' needs for Internet telecommunications equipment and services. Also, many jurisdictions are evaluating or implementing regulations relating to cyber security, supply chain integrity, privacy and data protection, any of which can affect the market and requirements for networking and security equipment.

In addition, environmental regulations relevant to electronic equipment manufacturing or operations may impact our business and financial condition adversely. For instance, the European Union and China have adopted WEEE and ROHS regulations, which require producers of electrical and electronic equipment to assume responsibility for collecting, treating, recycling and disposing of products when they have reached the end of their useful life, as well as REACH regulations, which regulate handling of certain chemical substances that may be used in our products. In addition, some governments have regulations prohibiting government entities from purchasing security products that do not meet specified indigenous certification criteria, even though those criteria may be in conflict with accepted international standards. These regulations are in effect or under consideration in several jurisdictions where we do business.

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The adoption and implementation of such regulations could reduce demand for our products, increase the cost of building and selling our products, result in product inventory write-offs, impact our ability to ship products into affected areas and recognize revenue in a timely manner and require us to spend significant time and expense to comply, and we could face fines and civil or criminal sanctions or claims if we were to violate or become liable under such regulations. Any of these impacts could have a material adverse effect on our business, financial condition, and results of operations.

Governmental regulations affecting the import or export of products or affecting products containing encryption capabilities could negatively affect our revenues.

Certain of our products contain or use encryption technology. The United States and various foreign governments have imposed controls, export license requirements, and restrictions on the import or export, among other things, encryption technology. In addition, from time to time, governmental agencies have proposed additional regulation of encryption technology, such as requiring certification, notifications, review of source code, or the escrow and governmental recovery of private encryption keys. For example, Russia and China recently have implemented new requirements relating to products containing encryption and India has imposed special warranty and other obligations associated with technology deemed critical. Governmental regulation of encryption or IP networking technology and regulation of imports or exports, or our failure to obtain required import or export approval for our products, could harm our international and domestic sales and adversely affect our revenues. In addition, failure to comply with such regulations could result in harm to our reputation, penalties, costs, and restrictions on import or export privileges or adversely affect sales to government agencies or government-funded projects.

If we do not successfully anticipate technological shifts, market needs and opportunities, and develop products and product enhancements that meet those technological shifts, needs and opportunities, or if those products are not made available in a timely manner or do not gain market acceptance, we may not be able to compete effectively and our ability to generate revenues will suffer.

We cannot guarantee that we will be able to anticipate future technological shifts, market needs and opportunities or be able to develop new products or product enhancements to meet such technological shifts, needs or opportunities in a timely manner or at all. For example, the move from traditional network infrastructures towards software defined networks ("SDN") has been receiving considerable attention. In our view, it will take several years to see the full impact of SDN, and we believe the successful products and solutions in this market will combine hardware and software elements together. If we fail to anticipate market requirements or fail to develop and introduce new products or product enhancements to meet those needs in a timely manner, it could cause us to lose customers, and such failure could substantially decrease or delay market acceptance and sales of our present and future products, which would significantly harm our business, financial condition, and results of operations. Even if we are able to anticipate, develop, and commercially introduce new products and enhancements, there can be no assurance that new products or enhancements will achieve widespread market acceptance.

In addition, as a result of our acquisitions of Altor and Trapeze in 2010, we have been offering a virtualization security product and a WLAN product. Also, in 2012, we announced new products, including the smaller version of our QFabric solutions, the latest QFX3000-M QFabric System, T4000 Core Routers, PTX Series Packet Transport switches, MX2020 and MX2010 3D Universal Edge Routers and JunosV App Engine. If these or other new products do not gain market acceptance at a sufficient rate of growth, our ability to meet future financial targets may be adversely affected. In addition, if we fail to achieve market acceptance at a sufficient rate of growth, our ability to meet future financial targets and aspirations may be adversely affected. Finally, if we fail to deliver new or announced products to the market in a timely manner, it could adversely affect the market acceptance of those products and harm our competitive position and our business and financial results.

Our ability to develop, market, and sell products could be harmed if we are unable to retain or hire key personnel.

Our future success depends upon our ability to recruit and retain the services of executive, engineering, sales and marketing, and support personnel. The supply of highly qualified individuals, in particular engineers in very specialized technical areas, or sales people specializing in the service provider and enterprise markets, is limited and competition for such individuals is intense. None of our officers or key employees is bound by an employment agreement for any specific term. The loss of the services of any of our key employees, the inability to attract or retain personnel in the future or delays in hiring required personnel, particularly engineers and sales people, and the complexity and time involved in replacing or training new employees, could delay the development and introduction of new products, and negatively impact our ability to market, sell, or support our products.

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Changes in effective tax rates or adverse outcomes resulting from examination of our income or other tax returns could adversely affect our results.

Our future effective tax rates could be subject to volatility or adversely affected by: earnings being lower than anticipated in countries where we have lower statutory rates and higher than anticipated earnings in countries where we have higher statutory rates; changes in the valuation of our deferred tax assets and liabilities; expiration of, or lapses in, the R&D tax credit laws applicable to us; transfer pricing adjustments related to certain acquisitions, including the license of acquired intangibles under our intercompany R&D cost sharing arrangement; costs related to intercompany restructuring; tax effects of share-based compensation; or changes in tax laws, regulations, accounting principles, or interpretations thereof. In addition, we are subject to the continuous examination of our income tax returns by the Internal Revenue Service ("IRS") and other tax authorities. 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 business, financial condition, and results of operations.

If we fail to accurately predict our manufacturing requirements, we could incur additional costs or experience manufacturing delays, which would harm our business.

We provide demand forecasts to our contract manufacturers and the manufacturers order components and plan capacity based on these forecasts. If we overestimate our requirements, our contract manufacturers may assess charges, or we may have liabilities for excess inventory, each of which could negatively affect our gross margins. For example, in the third quarter of fiscal 2012, our gross margins were reduced as a result of an inventory charge resulting from inventory we held in excess of forecasted demand. Conversely, because lead times for required materials and components vary significantly and depend on factors such as the specific supplier, contract terms, and the demand for each component at a given time, and because our contract manufacturers are third-party manufacturers for numerous other companies, if we underestimate our requirements, as we did in the third quarter of 2010 with respect to certain components, our contract manufacturers may have inadequate time, materials, and/or components required to produce our products, which could increase costs or could delay or interrupt manufacturing of our products and result in delays in shipments and deferral or loss of revenues.

We are dependent on contract manufacturers with whom we do not have long-term supply contracts, and changes to those relationships, expected or unexpected, may result in delays or disruptions that could cause us to lose revenues and damage our customer relationships.

We depend on independent contract manufacturers (each of which is a third-party manufacturer for numerous companies) to manufacture our products. Although we have contracts with our contract manufacturers, these contracts do not require them to manufacture our products on a long-term basis in any specific quantity or at any specific price. In addition, it is time-consuming and costly to qualify and implement additional contract manufacturer relationships. Therefore, if we fail to effectively manage our contract manufacturer relationships, which includes failing to provide accurate forecasts of our requirements, or if one or more of them experiences delays, disruptions, or quality control problems in our manufacturing operations, or if we had to change or add additional contract manufacturers or contract manufacturing sites, our ability to ship products to our customers could be delayed. Also, the addition of manufacturing locations or contract manufacturers would increase the complexity of our supply chain management. Moreover, an increasing portion of our manufacturing is performed in China and other countries and is therefore subject to risks associated with doing business in other countries. In addition, in late 2012, we confirmed that we were reducing the number of our contract manufacturers. As a result, we will be transitioning the work of one manufacturer to two of our other existing manufacturers during 2013. If we do not manage that transition effectively, we could experience delays or quality issues. Each of these factors could adversely affect our business, financial condition and results of operations.

Upgrades to key internal systems and processes, and problems with the design or implementation of these systems and processes could interfere with, and therefore harm, our business and operations.

We previously initiated a multi-year project to upgrade certain key internal systems and processes, including our company-wide human resources management system, our customer relationship management ("CRM") system and enterprise resource planning ("ERP") system. In the first quarter of 2010, we implemented a major upgrade of our CRM system. In 2012 and continuing into 2013, we expect to implement major changes to our ERP system. We have invested, and will continue to invest, significant capital and human resources in the design and implementation of these systems and processes. Any disruptions or delays in the design and implementation of the new systems or processes, particularly any disruptions or delays that impact our operations, could adversely affect our ability to process customer orders, ship products, provide service and support to our customers, bill and track our customers, fulfill contractual obligations, record and transfer information in a timely and accurate manner, file SEC reports in a timely manner, or otherwise run our business. Even if we do not encounter these adverse effects, the design and implementation of these new systems and processes may be much more costly than we anticipated. If we are unable to successfully design and implement these new systems and processes as planned, or if the implementation of these systems and processes is more costly than anticipated, our business, financial condition, and results of operations could be negatively impacted.

We are a party to lawsuits, proceedings, and other disputes, which are costly to defend and, if determined adversely to us, could require us to pay damages or prevent us from taking certain actions, any or all of which could harm our business, financial condition, and results of operations.

We, and certain of our current and former officers and current and former members of our Board of Directors, are subject to various lawsuits. We have been served with lawsuits related to employment matters, commercial transactions and patent infringement as well as securities laws. A description of the securities lawsuits can be found in Note 16, Commitments and Contingencies, in Notes to Consolidated Financial Statements of this Report, under the heading “Legal Proceedings.” There can be no assurance that these or any actions that have been or may in the future be brought against us, our officers, and our directors will be resolved favorably or that tentative settlements will become final. Regardless of whether they are resolved, these lawsuits are, and any future lawsuits or threatened legal proceedings to which we, our officers, or our directors may become a party will likely be, expensive and time-consuming to defend, settle, and/or resolve. Legal proceedings, threatened legal proceedings or investigations, regardless of their ultimate outcome, could harm our reputation. Costs of defense, as well as any losses resulting from these claims or settlement of these claims, could significantly increase our expenses and could harm our business, financial condition, and results of operations.

We are a party to litigation and claims regarding intellectual property rights, resolution of which may be time-consuming and expensive, as well as require a significant amount of resources to prosecute, defend, or make our products non-infringing.

Our industry is characterized by the existence of a large number of patents and frequent claims and related litigation regarding patent and other intellectual property rights. We expect that infringement claims may increase as the number of products and competitors in our market increases and overlaps occur. Third parties have asserted and may in the future assert claims or initiate litigation related to patent, copyright, trademark, and other intellectual property rights to technologies and related standards that are relevant to our products. The asserted claims and/or initiated litigation may include claims against us or our manufacturers, suppliers, partners, or customers, alleging that our products or services infringe proprietary rights. Regardless of the merit of these claims, they have been and can be time-consuming, result in costly litigation, and may require us to develop non-infringing technologies or enter into license agreements. Furthermore, because of the potential for high awards of damages or injunctive relief that are not necessarily predictable, even arguably unmeritorious claims may be settled for significant amounts of money. If any infringement or other intellectual property claim made against us by any third-party is successful, if we are required to settle litigation for significant amounts of money, or if we fail to develop non-infringing technology or license required proprietary rights on commercially reasonable terms and conditions, our business, financial condition, and results of operations could be materially and adversely affected.

We may face difficulties enforcing our proprietary rights.

We generally rely on a combination of patents, copyrights, trademarks, and trade secret laws and restrictions on disclosure of confidential and proprietary information, to establish and maintain proprietary rights in our technology and products. Although we have been issued numerous patents and other patent applications are currently now pending, there can be no assurance that any of these patents or other proprietary rights will not be challenged, invalidated, infringed or circumvented or that our rights will, in fact, provide competitive advantages to us or protect our technology, either of which could result in costly product redesign efforts, discontinuance of certain product offerings and other competitive harm. Furthermore, the laws of some foreign countries may not protect our proprietary rights to the same extent as do the laws of the United States. The outcome of any actions taken in these foreign countries may be different than if such actions were determined under the laws of the United States. Although we are not dependent on any individual patents or group of patents for particular segments of the business for which we compete, if we are unable to protect our proprietary rights in a market, we may find ourselves at a competitive disadvantage to others who need not incur the substantial expense, time, and effort required to create innovative products that have enabled our success.

Our success depends upon our ability to effectively plan and manage our resources and restructure our business through rapidly fluctuating economic and market conditions.

Our ability to successfully offer our products and services in a rapidly evolving market requires an effective planning, forecasting, and management process to enable us to effectively scale and adjust our business in response to fluctuating market opportunities and conditions.

In periods of market expansion, we have increased investment in our business by, for example, increasing headcount and increasing our investment in R&D, sales and marketing, and other parts of our business.
Conversely, in the third quarter of 2012, to align our cost structure with long-term strategic plans as part of our productivity and efficiency initiatives, we restructured our business, rebalanced our workforce, and reduced our real estate portfolio. Many of our expenses, such as real estate expenses, are fixed costs that cannot be rapidly or easily adjusted in response to fluctuations in our business or numbers of employees. Moreover, rapid changes in the size of our workforce could adversely affect our ability to develop and deliver products and services as planned or impair our ability to realize our current or future business objectives. Our ability to achieve the anticipated cost savings and other benefits from our restructuring initiatives within the expected time frame is subject to many estimates and assumptions. These estimates and assumptions are subject to significant economic, competitive and other uncertainties, some of which are beyond our control. If these estimates and assumptions are incorrect, if we are unsuccessful at implementing changes, or if other unforeseen events occur, our business and results of operations could be adversely affected.

Our financial condition and results of operations could suffer if there is an additional impairment of goodwill or other intangible assets with indefinite lives.

We are required to test annually and review on an interim basis, our goodwill and intangible assets with indefinite lives, including the goodwill associated with acquisitions, to determine if impairment has occurred. As of March 31, 2013, our goodwill was $4,057.8 million and our intangible assets were $131.2 million. If goodwill or intangible assets are deemed impaired, an impairment loss equal to the amount by which the carrying amount exceeds the fair value of the assets would be recognized. This would result in incremental expenses for that quarter, which would reduce any earnings or increase any loss for the period in which the impairment was determined to have occurred. For example, such impairment could occur if the market value of our common stock falls below certain levels for a sustained period, or if the portions of our business related to companies we have acquired fail to grow at expected rates or decline. In the second quarter of 2006, our impairment evaluation resulted in a reduction of $1,280.0 million to the carrying value of goodwill on our Condensed Consolidated Balance Sheets, primarily due to the decline in our market capitalization that occurred over a period of approximately nine months prior to the impairment review and, to a lesser extent, a decrease in forecasted future cash flows. In the third quarter of 2012, our impairment evaluation resulted in a reduction of $5.4 million to the carrying value of certain purchased intangibles on our Condensed Consolidated Balance Sheets, primarily due to the decline in discounted cash flow projections. In recent years, economic weakness contributed to extreme price and volume fluctuations in global stock markets that reduced the market price of many technology company stocks, including ours. Future declines in our stock price, as well as declines in our level of revenues or gross margins, increase the risk that goodwill and intangible assets may become impaired in future periods. We cannot accurately predict the amount and timing of any impairment of assets. However, any such impairment would have an adverse effect on our results of operations.

We are subject to risks arising from our international operations, which may adversely affect our business, financial condition, and results of operations.

We derive a majority of our revenues from our international operations, and we plan to continue expanding our business in international markets in the future. We conduct significant sales and customer support operations directly and indirectly through our distributors and VARs in countries throughout the world and depend on the operations of our contract manufacturers and suppliers that are located outside of the United States. In addition, a portion of our R&D and our general and administrative operations are conducted outside the United States. In some countries, we may experience reduced intellectual property protection.

As a result of our international operations, we are affected by economic, regulatory, social, and political conditions in foreign countries, including the following:

- changes in general IT spending,
- the imposition of government controls, inclusive of critical infrastructure protection,

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- changes or limitations in trade protection laws or other regulatory requirements, which may affect our ability to import or export our products from various countries,

- the impact of the following on service provider and government spending patterns: political considerations, unfavorable changes in tax treaties or laws, natural disasters, epidemic disease, labor unrest, earnings expatriation restrictions, misappropriation of intellectual property, military actions, acts of terrorism, political and social unrest and difficulties in staffing and managing international operations. Any or all of these factors could have a material adverse impact on our business, financial condition, and results of operations.

Moreover, local laws and customs in many countries differ significantly from those in the United States. In many foreign countries, particularly in those with developing economies, it is common for others to engage in business practices that are prohibited by our internal policies and procedures or United States regulations applicable to us. There can be no assurance that our employees, contractors, channel partners, and agents will not take actions in violation of our policies and procedures, which are designed to ensure compliance with U.S. and foreign laws and policies. Violations of laws or key control policies by our employees, contractors, channel partners, or agents could result in financial reporting problems, fines, penalties, or prohibition on the importation or exportation of our products, and could have a material adverse effect on our business, financial condition and results of operations.

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

Because a majority of our business is conducted outside the United States, we face exposure to adverse movements in non-U.S. currency exchange rates. These exposures may change over time as business practices evolve and could have a material adverse impact on our financial condition and results of operations.

The majority of our revenues and expenses are transacted in U.S. Dollars. We also have some transactions that are denominated in foreign currencies, primarily the British Pound, Euro, Indian Rupee, and Japanese Yen related to our sales and service operations outside of the United States. An increase in the value of the U.S. Dollar could increase the real cost to our customers of our products in those markets outside the United States in which we sell in U.S. Dollars, and a weakened U.S. Dollar could increase the cost of local operating expenses and procurement of raw materials to the extent we must purchase components in foreign currencies.

Currently, we hedge only those currency exposures associated with certain assets and liabilities denominated in nonfunctional currencies and periodically hedge anticipated foreign currency cash flows. The hedging activities undertaken by us are intended to offset the impact of currency fluctuations on certain nonfunctional currency assets and liabilities. However, such attempts to offset the impact of currency fluctuations are costly and no amount of hedging can be effective against all circumstances, including long-term declines in the value of the U.S. Dollar. If our attempts to hedge against these risks are not successful, or if long-term declines in the value of the U.S. Dollar persist, our financial condition and results of operations could be adversely impacted.

Integration of acquisitions could disrupt our business and harm our financial condition and stock price and may dilute the ownership of our stockholders.

We have made, and may continue to make, acquisitions in order to enhance our business. For example, in 2012, we acquired Contrail Systems Inc. ("Contrail") and Mykonos, and in 2010 we acquired Altor, Trapeze, SMobile, and Ankeena. Acquisitions involve numerous risks, including problems combining the purchased operations, technologies or products, unanticipated costs, diversion of management's attention from our core businesses, adverse effects on existing business relationships with suppliers and customers, risks associated with entering markets in which we have no or limited prior experience, and potential loss of key employees. There can be no assurance that we will be able to integrate successfully any businesses, products, technologies, or personnel that we might acquire. The integration of businesses that we may acquire is likely to be a complex, time-consuming, and expensive process and we may not realize the anticipated revenues or other benefits associated with our acquisitions if we fail to successfully manage and operate the acquired business. If we fail in any acquisition integration efforts and are unable to efficiently operate as a combined organization utilizing common information and communication systems, operating procedures, financial controls, and human resources practices, our business, financial condition, and results of operations may be adversely affected.

Acquisitions may also require us to issue common stock or assume equity awards that dilute the ownership of our current stockholders, use a substantial portion of our cash resources, assume liabilities, record goodwill and amortizable intangible assets that will be subject to impairment testing on a regular basis and potential periodic impairment charges, incur amortization expenses related to certain intangible assets, and incur large and immediate write-offs and restructuring and other related expenses, all of which could harm our financial condition and results of operations.

If we fail to adequately evolve our financial and managerial control and reporting systems and processes, our ability to manage and grow our business will be negatively affected.

Our ability to successfully offer our products and implement our business plan in a rapidly evolving market depends upon an effective planning and management process. We will need to continue to improve our financial and managerial control and our reporting systems and procedures in order to manage our business effectively in the future. If we fail to continue to implement improved systems and processes, our ability to manage our business, financial condition, and results of operations may be negatively affected.

Our products are highly technical and if they contain undetected errors or malware or do not meet customer quality expectations, our business could be adversely affected, and we may be subject to lawsuits or be required to pay damages in connection with any alleged or actual failure of our products and services.

Our products are highly technical and complex, are critical to the operation of many networks, and, in the case of our security products, provide and monitor network security and may protect valuable information. Our products have contained and may contain one or more undetected errors, defects, malware, or security vulnerabilities. Some errors in our products may only be discovered after a product has been installed and used by end-customers. Any errors, defects, malware or security vulnerabilities discovered in our products after commercial release could result in monetary penalties, loss of revenues or delay in revenue recognition, loss of customers, loss of future business and reputation, penalties, and increased service and warranty cost, any of which could adversely affect our business, financial condition, and results of operations. In addition, in the event an error, defect, malware, or vulnerability is attributable to a component supplied by a third-party vendor, we may not be able to recover from the vendor all of the costs of remediation that we may incur. In addition, we could face claims for product liability, tort, or breach of warranty. Defending a lawsuit, regardless of its merit, is costly and may divert management's attention. If our business liability insurance coverage is inadequate, or future coverage is unavailable on acceptable terms or at all, our financial condition and results of operations could be harmed. Moreover, if our products fail to satisfy our customers' quality expectations for whatever reason, the perception of and the demand for our products could be adversely affected.

If our products do not interoperate with our customers' networks, installations will be delayed or cancelled and could harm our business.

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

Our products incorporate and rely upon licensed third-party technology, and if licenses of third-party technology do not continue to be available to us or become very expensive, our revenues and ability to develop and introduce new products could be adversely affected.

We integrate licensed third-party technology into certain of our products. From time to time, we may be required to license additional technology from third-parties to develop new products or product enhancements. Third-party licenses may not be available or continue to be available to us on commercially reasonable terms. The failure to comply with the terms of any license, including free open source software, may result in our inability to continue to use such license. Our inability to maintain or re-license any third-party licenses required in our products or our inability to obtain third-party licenses necessary to develop new products and product enhancements, could require us, if possible, to develop substitute technology or obtain substitute technology of lower quality or performance standards or at a greater cost, any of which could delay or prevent product shipment and harm our business, financial condition, and results of operations.

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We sell our products to customers that use those products to build networks and IP infrastructure, and if the demand for network and IP systems does not continue to grow, then our business, financial condition, and results of operations could be adversely affected.

A substantial portion of our business and revenues depends on the growth of secure IP infrastructure and on the deployment of our products by customers that depend on the continued growth of IP services. As a result of changes in the economy capital spending or the building of network capacity in excess of demand, all of which have in the past particularly affected telecommunications service providers, spending on IP infrastructure can vary, which could have a material adverse effect on our business, financial condition, and results of operations. In addition, a number of our existing customers are evaluating the build-out of their next generation networks. During the decision-making period when the customers are determining the design of those networks and the selection of the equipment they will use in those networks, such customers may greatly reduce or suspend their spending on secure IP infrastructure. Such delays in purchases can make it more difficult to predict revenues from such customers can cause fluctuations in the level of spending by these customers and, even where our products are ultimately selected, can have a material adverse effect on our business, financial condition, and results of operations.

We are required to evaluate the effectiveness of our internal control over financial reporting, and any adverse results from such evaluation may adversely affect investor perception, our stock price and cause us to incur additional expense.

Section 404 of the Sarbanes-Oxley Act of 2002 requires our management to report on, and our independent auditors to attest to, the effectiveness of our internal control over financial reporting. We have an ongoing program to perform the system and process evaluation and testing necessary to comply with these requirements. We have and will continue to incur significant expenses and devote management resources to Section 404 compliance on an ongoing basis. In the event that our Chief Executive Officer, Chief Financial Officer, or independent registered public accounting firm determine in the future that, our internal controls over financial reporting are not effective as defined under Section 404, investor perceptions may be adversely affected if our financial statements are not reliable and could cause a decline in the market price of our stock and otherwise negatively affect our liquidity and financial condition.

The investment of our cash balance and our investments in government and corporate debt securities are subject to risks, which may cause losses and affect the liquidity of these investments.

At March 31, 2013, we had $2,043.7 million in cash and cash equivalents and $1,628.3 million in short- and long-term investments. We have invested these amounts primarily in asset-backed securities, certificate of deposit, commercial paper, corporate debt securities, foreign government debt securities, government- sponsored enterprise obligations, money market funds, mutual funds, publicly-traded equity securities and U.S. government securities. Certain of these investments are subject to general credit, liquidity, market, and interest rate risks, which may be exacerbated by U.S. sub-prime mortgage defaults that have affected various sectors of the financial markets and caused credit and liquidity issues at many financial institutions. Our future investment income may fall short of expectations due to changes in interest rates or if the decline in fair value of our publicly traded debt or equity investments is judged to be other-than-temporary. These market risks associated with our investment portfolio may have a negative adverse effect on our liquidity, financial condition, and results of operations.

We may be unable to generate the cash flow to service our debt obligations, including the Senior Notes.

In March 2011, we issued senior unsecured notes for an aggregate principle amount of $1.0 billion (see discussion in Note 10, Long-Term Debt and Financing, in the Notes to Condensed Consolidated Financial Statements of this Report). We may not be able to generate sufficient cash flow to enable us to service our indebtedness, including the notes, or to make anticipated capital expenditures. Our ability to pay our expenses and satisfy our debt obligations, refinance our debt obligations and fund planned capital expenditures will depend on our future performance, which will be affected by general economic, financial, competitive, legislative, regulatory and other factors beyond our control. Based upon current levels of operations, we believe cash flow from operations and available cash will be adequate for the foreseeable future to meet our anticipated requirements for working capital, capital expenditures and scheduled payments of principal and interest on our indebtedness, including the senior notes. However, if we are unable to generate sufficient cash flow from operations or to borrow sufficient funds in the future to service our debt, we may be required to sell assets, reduce capital expenditures, refinance all or a portion of our existing debt (including the senior notes) or obtain additional financing. There is no assurance that we will be able to refinance our debt, sell assets or borrow more money on terms acceptable to us, or at all.

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The indenture that governs the senior notes also contains various covenants that limit our ability and the ability of our subsidiaries to, among other things:

- incur liens;
- incur sale and leaseback transactions; and
- consolidate or merge with or into, or sell substantially all of our assets to, another person

As a result of these covenants, we are limited in the manner in which we can conduct our business, and we may be unable to engage in favorable business activities or finance future operations or capital needs. Accordingly, these restrictions may limit our ability to successfully operate our business. A failure to comply with these restrictions could lead to an event of default, which could result in an acceleration of the indebtedness. Our future operating results may not be sufficient to enable compliance with these covenants to remedy any such default. In addition, in the event of an acceleration, we may not have or be able to obtain sufficient funds to make any accelerated payments, including those under the senior notes.

Uninsured losses could harm our operating results.

We self-insure against many business risks and expenses, such as intellectual property litigation and our medical benefit programs, where we believe we can adequately self-insure against the anticipated exposure and risk or where insurance is either not deemed cost-effective or is not available. We also maintain a program of insurance coverage for various types of property, casualty, and other risks. We place our insurance coverage with various carriers in numerous jurisdictions. The types and amounts of insurance that we obtain vary from time to time and from location to location, depending on availability, cost, and our decisions with respect to risk retention. The policies are subject to deductibles, policy limits, and exclusions that result in our retention of a level of risk on a self-insurance basis. Losses not covered by insurance could be substantial and unpredictable and could adversely affect our financial condition and results of operations.

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

There were no unregistered sales of equity securities during the period covered by this Report.

Purchases of Equity Securities by the Issuer and Affiliated Purchasers

The following table provides a summary of stock repurchases during the three months ended March 31, 2013 (in millions, except per share amounts):

Period	Total Number of Shares Purchased (1)	Average Price Paid per Share (1)	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (2)	Maximum Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (2)
January 1 - January 31, 2013	—	$—	—	$568.2
February 1 - February 28, 2013	3.7	$22.19	3.6	$488.3
March 1 - March 31, 2013	2.6	$19.32	2.6	$438.3
Total	6.3	$21.01	6.2	

(1) Amounts include repurchases under our stock repurchase program and repurchases of our common stock for our employees in connection with net issuances of shares to satisfy minimum tax withholding obligations for the vesting of certain stock awards. The amount of shares of common stock repurchased from our employees in connection with net issuances was not significant during the three months ended March 31, 2013.

(2) Shares were repurchased under our stock repurchase program approved by the Board, which authorized us to purchase an aggregate of up to $1.0 billion of our common stock. Future share repurchases under this program will be subject to a review of the circumstances in place at that time and will be made from time to time in private transactions or open market purchases as permitted by securities laws and other legal requirements. This program may be discontinued at any time. As of March 31, 2013, our stock repurchase program had $438.3 million remaining authorized funds available for future stock repurchases.

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Item 6. Exhibits

Exhibit Number	Description of Document
12.1	Computation of Ratio of Earnings to Fixed Charges*
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934*
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934*
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350*
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350*
101	The following materials from Juniper Network Inc.'s Quarterly Report on Form 10-Q for the quarter ended March 31, 2013, formatted in XBRL (Extensible Business Reporting Language): (i) the Condensed Consolidated Statements of Operations (ii) the Condensed Consolidated Statements of Comprehensive Income, (iii) the Condensed Consolidated Balance Sheets, and (iv) the Condensed Consolidated Statements of Cash Flows, and (v) Notes to Condensed Consolidated Financial Statements*
101.INS	XBRL Instance Document*
101.SCH	XBRL Taxonomy Extension Schema Document*
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document*
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document*
101.LAB	XBRL Taxonomy Extension Label Linkbase Document*
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document*

*Filed herewith.

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SIGNATURES

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

Juniper Networks, Inc.

May 8, 2013	By: /s/ Robyn M. Denholm Robyn M. Denholm Executive Vice President and Chief Financial Officer (Duly Authorized Officer and Principal Financial Officer)
May 8, 2013	By: /s/ Terrance F. Spidell Terrance F. Spidell Vice President, Corporate Controller (Duly Authorized Officer and Principal Accounting Officer)

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Exhibit Index

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101.INS	XBRL Instance Document*
101.SCH	XBRL Taxonomy Extension Schema Document*
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document*
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document*
101.LAB	XBRL Taxonomy Extension Label Linkbase Document*
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document*

*Filed herewith.