

Experimental Materials

Note to reviewers: The experimental manipulations appear after the conditions highlighted in yellow. The post-experimental questionnaire begins on page 18.

Thank you in advance for participating in our research study. This research is administered by the Center for Audit Quality (CAQ). Your firm is a member in the CAQ and sponsor of this study because the firm leadership believes it is important.

We appreciate your time and we value your responses. This study will take about 30-40 minutes to complete and needs to be done in one sitting. If you can't spend 30-40 minutes now, please plan to complete the study at a better time.

Also, please do not discuss this study with your colleagues during or after the study as it could contaminate the results.

Click on the button below when you are ready to begin the study.

Page Break

Case Instructions and Background (please read carefully)

Assume you and your audit team are performing the year-end audit procedures for Limelight, Inc. (also referred to as the Company) for the year ended December 31, 2016. **Assume today's date is March 1, 2017 (about two months after year-end).**

Limelight is a large publicly-traded client, and it is the largest supplier of light sources used by chipmakers to create advanced semiconductor chips. Limelight's key figures for the current year are shown below:

- Total assets: \$777.4 million
- Revenues: \$456.7 million
- Net income before tax: \$50.3 million

Materiality is set at \$2.5 million (approximately 5% of pre-tax net income).

The audit is near completion, with the exception of the audit procedures related to the income tax provision. The income tax provision is a material account balance from both a quantitative and qualitative perspective because the valuation allowance for deferred tax assets is based on significant estimates involving judgment and uncertainty.

In conjunction with the tax specialist, your team has identified one potential issue that still needs to be evaluated. **Your task is to evaluate this issue including the reasonableness of the related assumptions and form a preliminary conclusion about the overall reasonableness of Limelight's income tax provision balance as of December 31, 2016.**

The following information is provided for your evaluation:

[Released Conditions]

- Background and financial information about Limelight, Inc. from their Q4 and annual earnings announcement (*unaudited*) which was *released and filed with the SEC approximately 16 days ago*.

[Drafted Conditions]

- Background and financial information about Limelight, Inc. from their Q4 and annual earnings announcement which they *anticipate releasing in March concurrent with the 10-K filing (in approximately 14 days)*.
- A summary memorandum for Limelight's income tax provision prepared by your audit firm's internal tax specialists.

The memorandum details the following potential issue and related assumptions:

- Valuation allowance – realizability of deferred tax assets (DTAs)
- Related assumptions: expectations of future profitability to recognize the DTAs, including (1) the anticipated pre-tax book income for 2017, and (2) the annual growth rate.

The Company did not adjust the existing cumulative valuation allowance for their deferred tax assets based on their tax-planning strategies and expectations of future taxable income, which are described in more detail in the memorandum from the tax specialist.

Your audit team verified the assumptions underlying the projection of future profitability as of June 30, 2016 (the valuation date) in conjunction with the goodwill impairment test. Your audit team determined the discount rate used by Limelight was reasonable and consistent with peer companies that demonstrate similar financial profiles as Limelight. Your audit team also verified that the assumptions underlying the projected financial information included within the goodwill impairment model were reasonable based on the information available as of the valuation date.

There are some new developments since these procedures as of June 30, 2016 that have potential implications for the assumptions underlying the projected future profitability of the Company that need to be considered in your evaluation, including the following: (1) lower than expected growth, sales, and earnings in the fourth quarter of 2016, and (2) unexpected industry and economic factors in the fourth quarter of 2016 thereby increasing the uncertainty of increased demand as projected as of June 30, 2016.

Therefore, you will be asked to evaluate the reasonableness of management's expectations about future taxable income for purposes of auditing the need for a valuation allowance, including assessing the characteristics affecting the viability of management's plan (e.g., economic outlook, industry outlook, operating history, financial condition, management's experience, products and services, competing assumptions and dependency of assumptions, etc.).

Your audit team considers the valuation allowance for deferred tax assets a significant accounting estimate. Per audit firm guidance, your audit team is required to discuss this significant accounting estimate with the audit committee. The discussion of this matter with the audit committee shall include the bases and procedures used by management in formulating the significant accounting estimates in connection with the valuation allowance, as well as your team's conclusions regarding the reasonableness of those estimates.

[Strong AC effectiveness Conditions]

The audit committee is composed of three individuals, who are all independent. Two of the members are CPAs with extensive experience in public accounting and qualify as financial experts as defined by the SEC, and the third member is financially literate. You have been very impressed with the audit committee's high level of diligence in representing shareholders' interest. They meet frequently and are actively involved in the resolution of key accounting and disclosure issues. The audit committee members are proactive, ask probing questions, and debate the appropriate accounting treatment regarding key transactions and issues.

[Moderate AC effectiveness Conditions]

The audit committee is composed of three individuals, who are all independent. Only one of the members qualifies as a financial expert as defined by the SEC as he is viewed as a supervisory financial expert. The other two members are financially literate. None of the members have direct accounting or financial reporting experience. Your experience with the audit committee is that they meet infrequently and are somewhat involved in the resolution of key accounting and disclosure issues. The audit committee members are reactive; they follow discussions of the issues during meetings but they do not ask too many questions regarding the issues.

The remainder of this case contains the Q4 and annual earnings announcement and the tax specialist memorandum, followed by a questionnaire. You will be able to access the documents throughout the study.

Please click the next arrow to advance to the Q4 and annual earnings announcement release.

Page Break

[Note to reviewers: The next four pages include the earnings announcement release for the Released Conditions, followed by four pages for the earnings announcement release for the Drafted Conditions]

LIMELIGHT

FOR IMMEDIATE RELEASE

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LIMELIGHT, INC. REPORTS FOURTH QUARTER AND 2016 OPERATING RESULTS

San Jose, CA, February 13, 2017 – Limelight, Inc., the world’s leading supplier of light sources used by chipmakers to create advanced semiconductor chips, today announced operating results for the fourth quarter and year ended December 31, 2016.

For the fourth quarter of 2016:

- Net income totaled \$3,984,000, equal to \$0.13 per share (diluted), compared to net income of \$21,437,000 equal to \$0.67 per share (diluted) in the fourth quarter of 2015 and net income of \$5,331,000, equal to \$0.18 per share (diluted) in the third quarter of 2016.
- Revenue totaled \$100,448,000 compared to revenue of \$139,922,000 in the fourth quarter of 2016, and revenue of \$110,619,000 in the third quarter of 2016.

For the year ended December 31, 2016:

- Net income totaled \$36,540,000, equal to \$1.22 per share (diluted), compared to net income of \$88,362,000, equal to \$2.50 per share (diluted) for the year ended December 31, 2015.
- Revenue total \$459,010,000 compared to revenue of \$521,696,000 in the prior year.

Commenting on the fourth quarter Patrick Francis, Limelight’s chief executive officer, said, “Limelight employees executed well in a very difficult business environment. Our operating results were below our fourth quarter expectations. We extended our argon fluoride (ArF) immersion market leadership, and made continued progress towards the development and commercialization of our extreme ultraviolet (EUV) light source technology.”

In the fourth quarter of 2016, the company shipped 19 light sources, including 15 XLs, resulting in an average selling price of approximately \$1.9 million. Installed Base Products (IBP) revenue totaled \$63.2 million. During the quarter the company installed 15 light sources at chipmaker locations. The company reported gross profit on product sales of \$44.7 million, yielding a 44.5 percent gross margin. Fourth quarter 2016 cost of revenue included additional field inventory changes of approximately \$2.3 million in response to lower chipmaker utilization. Excluding the additional field inventory charge, non-GAAP gross margin would have been 46.8 percent. Operating expenses of

\$40.4 million included \$1.9 million of costs associated with the November 2016 reduction in workforce and a \$1.9 million additional allowance for doubtful accounts receivable related to certain customer's deteriorating financial condition. Operating income totaled \$4.4 million and the fourth quarter effective tax rate was approximately 5% primarily due to the passage of the federal research and development tax credit in October 2016, which was effective retroactively to January 1, 2016.

Sales bookings to key customers were up from 2015. Deep ultraviolet (DUV) bookings for the fourth quarter of 2016 totaled \$83.7 million, resulting in a book-to-bill ratio of 0.83. All of the light source systems bookings in the fourth quarter were XL. The company ended the quarter with a DUV backlog of approximately \$33.7 million, with ArF immersion light sources comprising approximately 84 percent of the value of systems in backlog.

The full year revenue for 2016, at \$459 million was down 12 percent from 2015. The decrease is largely attributable to a continued market-wide decline in lithography light source demand, as the product is at the end of its life-cycle. However, this decline is partially offset by the successful launch of our new product, the XL Series, and a 10 percent annual growth in IBP revenue. Through increased operational efficiency and XL platform reliability improvements, the company achieved a gross margin of 47.3 percent on product sales in 2016.

Corporate Outlook

Commenting on the economic outlook, Francis stated, "We are optimistic about our 2017 and future prospects. The current business environment is changing, characterized by increased turnover and competition in the market, but we also anticipate increasing demand in the market. Looking at the first quarter of 2017, demand for new light sources and installed base products has increased compared to the fourth quarter of 2016. While visibility into 2017 is extremely limited, we expect ArF technology buys to comprise a more significant fraction of total market demand, which plays well to our competitive strength and should have a beneficial effect on our share beginning in the second quarter of 2017. We have taken action to reduce Limelight's cost structure and we will continue to focus on maintaining operating costs in-line with business conditions. We will continue to introduce new higher performance models to remain strongly positioned in this rapidly growing industry."

Based on information available at this time, Limelight is currently providing the following guidance for the first quarter of 2017, and anticipates:

- Revenue to increase approximately 20%, plus or minus 5% compared to the revenue reported for the fourth quarter of 2016
- Gross margin to be approximately 45%, plus or minus 3%, depending on revenue levels
- R&D expenses to be approximately \$18.5 million to \$19 million
- SG&A expense to be approximately \$11.5 million to \$12 million
- We currently estimate that Net Other Income and Expense will be at breakeven for the first quarter, excluding net effects of foreign currency exchange gains or losses.

Limelight's management will hold a conference call at 2:00 pm (PST) today, February 10, 2017 to discuss fourth quarter and 2016 operating results and first quarter 2017 guidance.

Limelight, Inc.
Consolidated Statement of Income
(In thousands, except per share data)

	Three Months Ended Dec. 31 2016 (UNAUDITED)	2015 (UNAUDITED)	Twelve Months Ended Dec 31 2016 (UNAUDITED)	2015 (AUDITED)
Revenues	\$99,967	\$139,296	\$456,729	\$517,980
Revenues – related party	<u>481</u>	<u>626</u>	<u>2,281</u>	<u>3,716</u>
Total revenues	100,448	139,922	459,010	521,696
COST OF REVENUES	<u>55,749</u>	<u>72,596</u>	<u>241,881</u>	<u>260,280</u>
GROSS PROFIT	44,699	67,326	217,129	261,416
OPERATING EXPENSES:				
Research and development	25,192	21,082	96,464	81,842
Sales and marketing	5,673	6,568	24,039	26,163
General and administrative	<u>9,454</u>	<u>10,476</u>	<u>36,544</u>	<u>38,949</u>
Total operating expense	<u>40,319</u>	<u>38,126</u>	<u>157,047</u>	<u>146,954</u>
OPERATING INCOME	4,380	29,200	60,082	114,462
OTHER INCOME (EXPENSE):				
Foreign currency exchange gain (loss)	(214)	69	(6,642)	2,025
Write-down of investment	(206)		(5,309)	
Interest and other income	1,123	3,824	8,845	20,074
Interest and other expense	<u>(1,769)</u>	<u>(1,902)</u>	<u>(6,712)</u>	<u>(6,709)</u>
Total other income (expenses) – net	(1,066)	1,991	(9,818)	15,390
INCOME BEFORE INCOME TAX PROVISION AND MINORITY INTEREST	3,314	31,191	50,264	129,852
INCOME TAX PROVISION MINORITY INTEREST	154	10,314	16,587	44,413
	<u>824</u>	<u>560</u>	<u>2,863</u>	<u>2,923</u>
NET INCOME	\$3,984	\$21,437	\$36,540	\$88,362
EARNINGS PER SHARE				
Basic earnings per share	\$0.13	\$0.71	\$1.22	\$2.64
Weighted average common shares outstanding – basic	29,569	30,404	29,924	33,522
Diluted earnings per share	\$0.13	\$0.67	\$1.22	\$2.50
Weighted average common shares outstanding – diluted	29,645	33,623	29,992	36,784

Limelight, Inc.
Consolidated Balance Sheet
(In thousands)

	December 31, 2016 (UNAUDITED)	December 31, 2015 (AUDITED)
CURRENT ASSETS:		
Cash and cash equivalents	\$252,391	\$305,707
Short-term investments	30,900	22,355
Accounts receivables – net	64,296	91,875
Accounts receivables – related party	818	1,112
Inventories	194,746	129,757
Deferred and prepaid income taxes	46,886	42,147
Prepaid expenses and other assets	<u>9,344</u>	<u>8,930</u>
Total current assets	599,381	601,883
PROPERTY AND EQUIPMENT – NET	114,390	116,725
LONG TERM INVESTMENTS	9,456	29,443
DEFERRED INCOME TAXES	29,168	19,272
GOODWILL	8,833	8,833
INTANGIBLE ASSETS – NET	9,898	12,951
OTHER ASSETS	<u>6,318</u>	<u>5,045</u>
TOTAL ASSETS	\$777,444	\$794,152
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	\$15,003	\$23,980
Accounts payable – related party	4,108	4,428
Accrued warranty	23,565	24,350
Accrued payroll and benefits	12,682	24,406
Accrued patents, royalties and other fees	3,795	3,303
Convertible subordinated notes	140,722	
Income taxes payable	1,085	13,468
Deferred revenue	15,344	4,974
Accrued and other current liabilities	<u>8,278</u>	<u>4,569</u>
Total current liabilities	224,582	103,478
CONVERTIBLE SUBORDINATED NOTES		140,722
INCOME TAXES PAYABLE	18,447	17,755
DEFERRED REVENUE		5,562
OTHER LIABILITIES	<u>11,791</u>	<u>17,401</u>
Total Liabilities	254,820	284,918
MINORITY INTEREST	4,848	5,711
STOCKHOLDERS' EQUITY		
Preferred Stock		
Common Stock	42	42
Additional paid-in capital	586,539	579,711
Treasury Stock	(473,580)	(450,704)
Accumulated other comprehensive income (loss)	(6,025)	214
Retained earnings	<u>410,800</u>	<u>374,260</u>
Total stockholders' equity	<u>517,776</u>	<u>503,523</u>
TOTAL LIABILITIES AND EQUITY	\$777,444	\$794,152

LIMELIGHT, INC. REPORTS FOURTH QUARTER AND 2016 OPERATING RESULTS

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- Net income totaled \$3,984,000, equal to \$0.13 per share (diluted), compared to net income of \$21,437,000 equal to \$0.67 per share (diluted) in the fourth quarter of 2015 and net income of \$5,331,000, equal to \$0.18 per share (diluted) in the third quarter of 2016.
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Limelight's management will hold a conference call at 2:00 pm (PST) on March XX, 2017 to discuss fourth quarter and 2016 operating results and first quarter 2017 guidance.

TO BE RELEASED ON MARCH XX, 2017 (DATE OF 10-K FILING)

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(In thousands, except per share data)

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Please click the next arrow to advance to the tax specialist memorandum. You will be able to return to the earnings release throughout the study.

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MEMORANDUM

TO: AUDIT PARTNER on Limelight, Inc.
FROM: TAX SPECIALIST (at your accounting firm)
SUBJECT: **Limelight, Inc.** 12/31/2016 INCOME TAX PROVISION
DATE: MARCH 1, 2017

We have completed our review of Limelight's 2016 income tax provision. Based on our procedures and reviews, we have identified one potential issue that warrants further evaluation prior to concluding that the income tax accounts and anticipated financial statement presentation and disclosures are free of material misstatements. We discuss the remaining potential issues herein.

Deferred taxes – Realizability

Limelight provided its documentation to support its analysis of the need for a valuation allowance. Their analysis of future taxable income includes (1) determination of the deferred tax liabilities (DTLs) and deferred tax assets (DTAs) that will reverse, (2) evaluating expectations of future profitability, and (3) evaluating potential tax-planning strategies.

We have considered the available evidence, both positive and negative, to determine whether it is more-likely-than-not that some portion, or all, of the DTAs will not be realized. With the exception of the fiscal year ending in 2013, in which the company experienced significant losses due to restructuring (a nonrecurring event), Limelight has a history of profitability and expects that trend to continue. Limelight has concluded that the future realization of the majority of their DTAs is more-likely-than-not to occur. Therefore, Limelight has established a valuation allowance only for those DTAs for which they are unable to project reversal prior to expiration. The cumulative valuation allowance is \$1.8 million at 12/31/16, which relates to capital loss carryforwards.

Limelight utilizes historical financial information, current year financial information and projected financial information to analyze the realizability of the federal domestic DTAs. The Company concludes that the future reversals of DTLs and projections of future taxable income provided sufficient positive evidence to support the conclusion that the DTAs were more likely than not realizable. In their analysis of the future realization of DTAs, Limelight indicates that they project pre-tax book income of \$64.9 million for 2017 and an annual growth rate of 8% for each of the years 2018-2021. They note that while they experienced a 61% decrease in pre-tax income from \$129.9 million in 2015 to \$50.3 million in 2016, 2016 includes significant, non-operating income and expense items that they do not anticipate to occur in the future (approximately \$5.3 million), for a total net expense of \$9.8 million. In addition, they expect an annual growth rate of 8% for 2017 resulting from increased demand for new and existing products (i.e., the XL series and the IBPs) which partially offsets the decrease in market demand for lithography light sources experienced during 2015 which has now stabilized. They project that increased sales combined with cost cutting measures will allow them to arrive at a pre-tax book income of \$64.9 million in the coming year. We note that Limelight's assumptions about future profitability are consistent with those utilized by the company for internal planning purposes.

Based on the projections provided by the company, all DTAs associated with the federal net operating loss (NOL) carryforwards of \$247.1 million would be utilized by 2020. The anticipated pre-tax book income for 2017 of \$64.9 million represents a 29.1% increase over the current year. While we acknowledge that the company is undertaking efforts to improve profitability and that 2016 was a down year, the achievability of this projection should be considered. Additionally, we note that projected NOL utilization is also contingent on an 8% annual growth rate in anticipated pre-tax book income for future years 2018 to 2021. Both of these assumptions include significant uncertainty, and variations in the assumptions could lead to a wide range of possible outcomes as it relates to adjustments to the valuation allowance.

Because we are not in a position to assess the reasonableness of the assumptions used in this estimate, we have provided you with a sensitivity analysis of the incremental valuation allowance that would be required under varying assumptions for (1) the anticipated pre-tax book income for 2017, and (2) the anticipated annual growth rate. We present the amount of valuation allowance expense that would be necessary for varying growth rate assumptions ranging from 3-8%, and for varying anticipated 2017 pre-tax book income amounts including (a) the 2016 pre-tax book income of \$50.3 million, (b) the 2016 pre-tax book income adjusted for a one-time (non-recurring) expense of \$55.6 million, and (c) management's estimate of \$64.9 million. We hope this analysis is helpful in your determination about the reasonableness of management's estimate.

Adjustments to valuation allowance with varying assumptions for the annual growth rate (8%) and for the anticipated pre-tax book income for 2017

Assumptions for Annual Growth Rate	Assumptions for anticipated pre-tax book income for 2017		
	\$64.9 million (Limelight's estimate)	\$55.6 million (2016 pre-tax income adjusted*)	\$50.3 million (2016 pre-tax income)
8%	0	0	0
7%	0	0	1,635,227
6%	0	0	4,766,186
5%	0	0	7,816,809
4%	0	321,909	10,788,822
3%	0	3,522,800	13,683,925

Notes:

Limelight projects pre-tax book income of \$64.9 million for 2017 and an annual growth rate of 8% for each of the years 2018-2021.

* \$55.6 million represents the actual 2016 pre-tax income of \$50.3 million adjusted by \$5.3 million for a one-time expense for the write-down of investments that occurred in 2016.

Supplemental Information (Optional)

Please note: Additional information about Limelight and its current operating environment can be obtained below in each of the links. The information in the links includes representations from Limelight's management that relates to characteristics affecting the viability of management's projections. Please click on any links to obtain the supplemental details at your discretion (i.e., reading this supplemental information is not required).

Volatile economic year	Stable customer base
Growing consumer demand	Market uncertainty for existing products
2016 operating results below expectations	Extensive experience of company management

[Note to reviewers: What follows is the information that is included in the links above.]

Volatile Economic Year

2016 was a very volatile economic year. In January 2017, Gartner Dataquest forecasted that 2016 worldwide semiconductor capital equipment spending would decrease 30.6% from 2015 levels and that 2017 worldwide semiconductor capital equipment spending is on pace to decline 34.1% from 2016 levels. In response to these rapidly changing business conditions, we took several actions to reduce our cost structure, including executing a reduction in our workforce and reducing operating expenses. During a year of declining demand, we were able to considerably strengthen our DUV product portfolio and overall product reliability, and quality continued to increase. Our installed base products business grew and we believe we are in a leadership position with our core products.

2016 Operating Results Below Expectations

Although we and many of the companies in our industry initially expected 2016 to be another growth year, activity levels decreased as the year progressed and the semiconductor industry entered a slowdown. As a result of the downturn in the global economy and the semiconductor industry in 2015, there were negative impacts to our financial results in 2016 beyond those described above related to our revenues. They include the following which we recorded in our consolidated financial statements during the year ended December 31, 2016:

- A \$5.3 million impairment of an auction rate security with a face value of \$5.6 million in our investment portfolio that we purchased in October 2015. Based on the type and magnitude of this impairment, we were required to record this as an other-than-temporary loss in our consolidated statement of income in 2016.
- Foreign currency losses which totaled \$6.6 million and were associated with the significant fluctuations of the foreign exchange rates in the countries in which our subsidiaries are located and do business.

- Bad debt expense of \$1.9 million as a result of certain of our customers experiencing financial difficulties associated with the downturn in the semiconductor industry and global economy.
- Write downs of the value of our inventory of \$5.9 million in response to the decreasing demand for our products and increased risk of parts on hand in excess of our demand plan.

Market Uncertainty for Existing Products

Future technologies such as EUV, nano-imprint lithography, and certain maskless lithography techniques may render our lithography light source products obsolete. We must manage product transitions, as introduction of new products could adversely affect our sales of existing products. We may not be able to develop and introduce new products or enhancements to our existing products and processes in a timely or cost effective manner that satisfies customer needs or achieves market acceptance. Failure to develop and introduce these new products and enhancements could materially adversely affect our operating results, financial condition and cash flows.

Growing Consumer Demand

In recent years, the semiconductor industry has experienced significant growth. The volume of chips produced has increased every year, driven by demand for more consumer electronic devices that contain chips. The complexity of chips has increased dramatically, due to growing consumer demand for more sophisticated electronic devices. Additionally, there is rapidly growing consumer demand for this increased functionality to be available virtually everywhere, through wireless connectivity. These advances in functionality have been achieved without the devices increasing in size or price because chipmakers have been able, over the years, to make each generation of chips with smaller features and finer circuitry than the previous generation.

As a result of the cyclicity of the semiconductor industry, the semiconductor capital equipment industry historically has experienced periodic ups and downs. The cyclical nature of the semiconductor and the semiconductor capital equipment industries affects our ability to accurately predict future revenue and therefore our ability to manage our future expense levels. When cyclical fluctuations result in lower than expected revenue levels, operating results may be adversely affected and cost reduction actions may be necessary in order for us to remain competitive and financially sound.

Extensive Experience of Company Management

Patrick J. Francis, one of our co-founders, has served as our chairman and chief executive officer since our inception in 1994, and served as president from 1994 until May 2008. He currently serves on the board of directors of KLA-Tencor Corporation and of the UC San Diego Foundation. Prior to starting the company, he had extensive experience in the semi-conductor industry. Mr. Francis received a bachelor's degree in physics, a bachelor's degree in literature, and a doctorate in applied physics from the University of California, San Diego.

Robert M. White has served as president and chief operating officer since September 2013. Prior to joining us, Mr. White was Group Vice President and Senior Advisor to the President at Applied Materials Inc., the world's largest provider of semiconductor equipment and services. From 1992 until 2013, Mr. White held several high-level management positions at Applied Materials, where he was responsible for overseeing global operations. Mr. White received a master's degree in business administration from Stanford University and a bachelor's degree in industrial studies from San Diego State University.

Stable Customer Base

We sell our photolithography light source products to each of the three lithography tool manufacturers, ASML, Canon and Nikon, who then integrate our light sources into their DUV photolithography tools. We strive to maintain and strengthen our relationships with our lithography tool manufacturer customers by developing and providing compelling light source solutions in advance of their need.

Sales to ASML, Nikon and Samsung accounted for 22%, 20% and 10%, respectively, of total revenue in 2015 and approximately 59% of total accounts receivable at December 31, 2016. We expect that sales of our light source and other related products to these three customers will continue to account for a substantial portion of our revenue in the foreseeable future. We believe there is limited credit risk exposure for us with these companies who continue to demonstrate sound credit worthiness.

Please answer the following questions about the case. You may refer back to the case when answering questions #1 - 3 below. Click on the following links to return to the previous materials.

[Instructions and background](#)

[Earnings announcement draft](#)

[Tax specialist memorandum](#)

1. Based on your evaluation, how likely is it that Limelight's income tax provision balance as of December 31, 2016 is reasonable?

Not at all likely												Extremely likely
0	1	2	3	4	5	6	7	8	9	10		
<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

2. How likely is it that you would recommend an initial adjustment to the income tax provision as of December 31, 2016?

Not at all likely												Extremely likely
0	1	2	3	4	5	6	7	8	9	10		
<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

3. Please indicate an approximate amount you would recommend as an initial adjustment to the income tax provision as of December 31, 2016, if any.

\$ in Millions

0	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
---	---	---	---	---	---	---	---	---	---	----	----	----	----	----	----

Page Break

4. Please explain all factors impacting your assessments provided on the previous page related to the reasonableness of Limelight's income tax provision balance as of December 31, 2016.

Page Break

5. For each of the following factors (a. through i.), please assess the extent to which the available evidence supports Limelight's position about the reasonableness of the income tax provision as December 31, 2016.

	Does not at all support		Neutral								Supports a great extent		N/A
	0	1	2	3	4	5	6	7	8	9	10		
a. The economic outlook	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
b. The industry outlook	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
c. Limelight's operating history	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
d. Limelight's customer base	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
e. Limelight's financial condition	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
f. Management's experience	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
g. The stability of Limelight's products	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
h. The sensitivity analysis of assumptions related to the significant estimates	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
i. The dependency of assumptions on the outcome of the firecasted results related to the significant estimates	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

Feel free to explain any of your assessments here (optional):

Page Break

6. Please rank order the importance of the following factors in your evaluation of the reasonableness of Limelight's income tax provision balance as of December 31, 2016. (You do not have to rank all items, but please rank the top 5 factors at a minimum. Enter the ranking number with 1 being the most important).

- a. Economic outlook
- b. Industry outlook
- c. Limelight's operating history
- d. Limelight's customer base
- e. Limelight's financial condition
- f. Management's experience
- g. The stability of Limelight's products
- h. The sensitivity of assumptions related to the significant estimates
- i. The dependency of assumptions on the outcome of the forecasted results related to the significant estimates

Page Break

Please answer the following additional questions about the case.

7a. How likely is it that Limelight's management will achieve their anticipated pre-tax book income of \$64.9 million for 2017?

Not at all likely										Extremely likely
0	1	2	3	4	5	6	7	8	9	10
<input type="radio"/>										

7b. How likely is it that Limelight's management will achieve their estimated annual growth rate of 8% for the next four years?

Not at all likely										Extremely likely
0	1	2	3	4	5	6	7	8	9	10
<input type="radio"/>										

Page Break

8. Please evaluate the following goal: To "build a justifiable case that Limelight's tax provision balance is reasonable and appropriate as of December 31, 2016 considering the current circumstances."

	Strongly disagree				Strongly agree
	1	2	3	4	5
1. I thought this was a good goal to shoot for.	<input type="radio"/>				
2. I was strongly committed to pursuing this goal.	<input type="radio"/>				
3. It was hard to take this goal seriously.	<input type="radio"/>				
4. Quite frankly, I didn't care if I achieved this goal or not.	<input type="radio"/>				
5. It wouldn't have taken much to make me abandon this goal.	<input type="radio"/>				

Page Break

9. Which best describes the timing of Limelight's Q4 and annual earnings announcement for the year ended December 31, 2016?

- a. It has already been released and filed with the SEC.
- b. It has been drafted, but not yet released and filed with the SEC.
- c. I don't know.

10. Which date were you asked to assume it was when reading the case?

- a. January 1, 2017
- b. February 1, 2017
- c. March 1, 2017
- d. April 1, 2017
- e. I don't know

Page Break

[Drafted Conditions]

11. Do you think other auditors (at your level) would have assessed the reasonableness of the income tax provision differently if Limelight's Q4 and annual earnings announcement for the year ended December 31, 2016 *had already been released and filed with the SEC prior to the completion of your audit* including your evaluation of the income tax provision?

- a. Yes
- b. No

[Released Conditions]

11. Do you think other auditors (at your level) would have assessed the reasonableness of the income tax provision differently if Limelight's Q4 and annual earnings announcement for the year ended December 31, 2016 *would not have been released and filed with the SEC until after the completion of your audit* including your evaluation of the income tax provision?

- a. Yes
- b. No

Please explain how you think their assessments might be impacted.

Page Break

12. To what extent do you feel that Limelight's audit committee will advocate your position with these accounting issues?

Not at all									To a great extent	
1	2	3	4	5	6	7	8	9	10	11
<input type="radio"/>										

13. Please rate the strength of Limelight's audit committee effectiveness at resolving accounting issues.

Very weak		Moderate							Very strong	
1	2	3	4	5	6	7	8	9	10	11
<input type="radio"/>										

14. Please rank order in importance the following factors as it relates to your answer for the previous question (where 1 = most important and 5= least important).

	1	2	3	4	5
a. Independence of members	<input type="radio"/>				
b. Financial expertise	<input type="radio"/>				
c. Frequency of meetings	<input type="radio"/>				
d. Active involvement in the resolution of key accounting and disclosure issues	<input type="radio"/>				
e. Level of professional skepticism exercised	<input type="radio"/>				

Page Break

15. To what extent do you think other auditors (at your level) would feel pressure to accept Limelight's accounting treatment in this situation?

Very low pressure				Average pressure				Very high pressure
1	2	3	4	5	6	7		
<input type="radio"/>								

Page Break

16. Based on the information in this case, how would assess the strength of Limelight management's internal controls as it relates to "tone at the top" in their control environment?

Very weak					Moderate					Very strong
1	2	3	4	5	6	7	8	9	10	11
<input type="radio"/>										

Page Break

17. What percent of your public company audit engagements in the past year have released annual earnings prior to your audit report date?

- a. 0%
 - b. 1 - 20%
 - c. 21 - 40%
 - d. 41 - 60%
 - e. 61 - 80%
 - f. 81 - 100%
-

18. In these audit engagements where the public company released annual earnings prior to the audit report date, assuming that the financial information in the annual earnings announcement is labeled “unaudited,” please indicate the following:

a. In these audits, approximately what percentage of the total audit hours are remaining, on average?
(slide the bar or a click on a percent)



b. In these audits, how likely is it that conclusions about significant accounting estimates might not yet be finalized?

Not at all											To a great extent
1	2	3	4	5	6	7	8	9	10	11	
<input type="radio"/>											

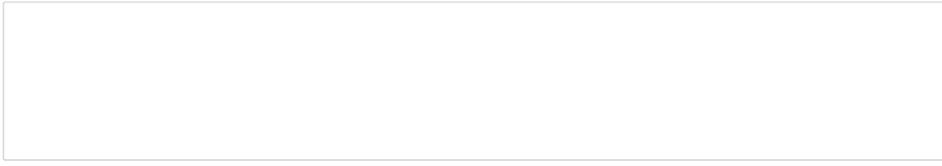
c. In these audits, how likely is it that the engagement quality review partner has completed his/her review?

Not at all											To a great extent
1	2	3	4	5	6	7	8	9	10	11	
<input type="radio"/>											

d. In these audits, how important is support from the audit committee when a potential audit adjustment arises after the annual earnings have been released?

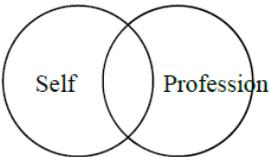
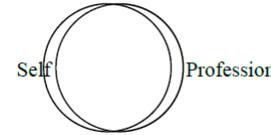
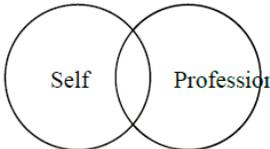
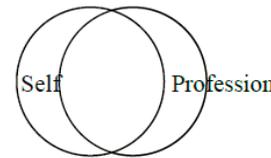
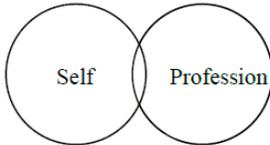
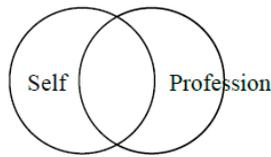
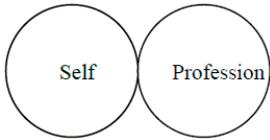
Not at all											To a great extent
1	2	3	4	5	6	7	8	9	10	11	
<input type="radio"/>											

e. In general, what is your view about the practice of audit clients releasing earnings prior to the completion of the audit (i.e., the audit report date)?



Page Break

19. Select the picture below that best describes how your personal attributes, qualities, and values align or overlap with the attributes, qualities, and values of the accounting profession.



Page Break

20. Please indicate your level of agreement with the following statements:

	Strongly disagree				Strongly agree
	1	2	3	4	5
a. When someone criticizes my profession, it feels like a personal insult.	<input type="radio"/>				
b. When I talk about my profession, I usually say "We" rather than "They."	<input type="radio"/>				
c. I am very interested in what others think about my profession.	<input type="radio"/>				
d. My profession's successes are my successes.	<input type="radio"/>				
e. When someone praises my profession, it feels like a personal compliment.	<input type="radio"/>				

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21. Please think about your largest audit client and then indicate your agreement with the following statements:

	Strongly disagree				Strongly agree
	1	2	3	4	5
a. When someone praises my client, it feels like a personal compliment.	<input type="radio"/>				
b. When I talk about my client, I usually say "We" rather than "They."	<input type="radio"/>				
c. My client's successes are my successes.	<input type="radio"/>				
d. When someone criticizes my client, it feels like a personal insult.	<input type="radio"/>				

Page Break

Please answer the following questions about yourself.

22. What is your current position in the firm?

a. Audit manager

b. Audit senior-
manager

c. Audit partner

d. Audit director

e. Other (explain) **23. How many years of experience do you have in public-company auditing?****24. In what industry(ies) are most of your audit clients?****25. Please indicate the extent of your experience auditing in the following areas:**

	A small extent										A great extent	
	1	2	3	4	5	6	7	8	9	10	11	
a. Auditing income tax provisions	<input type="radio"/>											
b. Auditing the valuation allowance for deferred tax assets	<input type="radio"/>											

26. Approximately, what percentage of your total time (i.e., billable time) was spent working on audit client engagements during the past 12 months?**27. Relative to a normal work week, how busy have you been over the past two days?**

Below average										Above average	
1	2	3	4	5	6	7	8	9	10	11	
<input type="radio"/>											

28. What is your gender?

Female

Male

I prefer to not disclose my gender

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