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

FORM 10-Q

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

For the quarterly period ended September 29, 2018

or

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

For the transition period from ________________ to ________________

Commission file number: 001-37444

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

Delaware *(State or other jurisdiction of incorporation or organization)*	**20-8920744** *(I.R.S. Employer Identification No.)*
199 Fremont Street, 14th Floor **San Francisco, California** *(Address of principal executive offices)*	**94105** *(Zip Code)*

(415) 513-1000
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes ☑ No ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files).

Yes ☑ No ☐

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

Large accelerated filer	☑	Accelerated filer	☐
Non-accelerated filer	☐	Smaller reporting company	☐
		Emerging growth company	☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ☐ No ☑

As of October 24, 2018, there were 217,249,641 shares of the registrant's Class A common stock outstanding and 31,281,638 shares of the registrant's Class B common stock outstanding.

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NOTE ABOUT FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements, within the meaning of the Private Securities Litigation Reform Act of 1995, that involve risks and uncertainties. All statements contained in this Quarterly Report on Form 10-Q other than statements of historical fact, including statements regarding our future results of operations and financial position, our business strategy and plans, and our objectives for future operations, are forward-looking statements. The words "believe," "may," "will," "estimate," "continue," "anticipate," "intend," "expect," and similar expressions are intended to identify forward-looking statements. Forward-looking statements contained in this Quarterly Report on Form 10-Q include, but are not limited to, statements about:

- *continued investments in research and development, sales and marketing and international expansion and the impact of those investments;*
- *trends in our revenue, cost of revenue, gross margin, operating expenses, including personnel costs, research and development expense, sales and marketing expense and general and administrative expense;*
- *competitors and competition in our markets;*
- *our ability to anticipate and satisfy consumer preferences;*
- *our smartwatches and their market acceptance and future potential;*
- *our ability to develop and introduce new products and services, including recurring non-device revenue offerings, improve our existing products and services, or engage or expand our user base;*
- *the impact of tariffs or other restrictions placed on our products imported into the United States from China;*
- *potential insurance recoveries;*
- *our ability to accurately forecast consumer demand and adequately manage inventory;*
- *our ability to deliver an adequate supply of product to meet demand;*
- *our ability to maintain and promote our brand and expand brand awareness;*
- *our ability to detect, prevent, or fix defects;*
- *our reliance on third-party suppliers, contract manufacturers and logistics providers and our limited control over such parties;*
- *trends in our quarterly operating results and other operating metrics;*
- *legal proceedings and the impact of such proceedings;*
- *the impact of changes in tax law on our operating results;*
- *the impact of our adoption of accounting pronouncements;*
- *the effect of seasonality on our results of operations;*
- *our ability to attract and retain highly skilled employees;*
- *our expectations to derive the substantial majority of our revenue from sales of devices;*
- *our expectations with respect to shifts in advertising and marketing spend;*
- *the impact of our acquisitions in enhancing the features and functionality of our devices;*
- *the impact of foreign currency exchange rates;*
- *the sufficiency of our existing cash and cash equivalent balances and cash flow from operations to meet our working capital and capital expenditure needs for at least the next 12 months; and*
- *general market, political, economic and business conditions, including potential changes in tariffs .*

We caution you that the foregoing list does not contain all of the forward-looking statements made in this Quarterly Report on Form 10-Q.

You should not rely upon forward-looking statements as predictions of future events. We have based the forward-looking statements contained in this Quarterly Report on Form 10-Q primarily on our current expectations and projections about future events and trends that we believe may affect our business, financial condition, operating results, and prospects. The outcome of the events described in these forward-looking statements is subject to risks, uncertainties, and other factors described in the section titled "Risk Factors" and elsewhere in this Quarterly Report on Form 10-Q. Moreover, we operate in a very competitive and rapidly changing environment. New risks and uncertainties emerge from time to time, and it is not possible for us to predict all risks and uncertainties that could have an impact on the forward-looking statements contained in this Quarterly Report on Form 10-Q. We cannot assure you that the results, events, and circumstances reflected in the forward-looking statements will be achieved or occur, and actual results, events, or circumstances could differ materially from those described in the forward-looking statements.

The forward-looking statements made in this Quarterly Report on Form 10-Q relate only to events as of the date on which the statements are made. We undertake no obligation to update any forward-looking statements made in this Quarterly Report on Form 10-Q to reflect events or circumstances after the date of this Quarterly Report on Form 10-Q or to reflect new information or the occurrence of unanticipated events, except as required by law. We may not actually achieve the plans, intentions, or *expectations disclosed in our forward-looking statements and you should not place undue reliance on our forward-looking statements. Our forward-looking statements do not reflect the potential impact of any future acquisitions, mergers, dispositions, joint ventures, or investments we may make.*

PART I. FINANCIAL INFORMATION
Item 1. Condensed Consolidated Financial Statements

FITBIT, INC.
Condensed Consolidated Balance Sheets
(In thousands)
(unaudited)

	September 29, 2018	December 31, 2017
Assets		
Current assets:		
Cash and cash equivalents	$ 402,237	$ 341,966
Marketable securities	221,083	337,334
Accounts receivable, net	325,964	406,019
Inventories	195,112	123,895
Income tax receivable	8,962	77,882
Prepaid expenses and other current assets	45,541	97,269
Total current assets	1,198,899	1,384,365
Property and equipment, net	106,520	104,908
Goodwill	61,058	51,036
Intangible assets, net	25,680	22,356
Deferred tax assets	3,920	3,990
Other assets	10,003	15,420
Total assets	$ 1,406,080	$ 1,582,075
Liabilities and Stockholders’ Equity		
Current liabilities:		
Accounts payable	$ 232,991	$ 212,731
Accrued liabilities	386,384	452,137
Deferred revenue	27,350	35,504
Income taxes payable	6,580	928
Total current liabilities	653,305	701,300
Long-term deferred revenue	5,458	6,928
Other liabilities	52,596	49,884
Total liabilities	711,359	758,112
Commitments and contingencies (Note 6)		
Stockholders’ equity:		
Class A and Class B common stock	25	24
Additional paid-in capital	1,025,803	956,060
Accumulated other comprehensive income (loss)	3,333	(9)
Accumulated deficit	(334,440)	(132,112)
Total stockholders’ equity	694,721	823,963
Total liabilities and stockholders’ equity	$ 1,406,080	$ 1,582,075

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

FITBIT, INC.
Condensed Consolidated Statements of Operations
(In thousands, except per share amounts)
(unaudited)

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
Revenue	$ 393,575	$ 392,522	$ 940,784	$ 1,044,763
Cost of revenue	240,061	217,762	554,132	602,459
Gross profit	153,514	174,760	386,652	442,304
Operating expenses:				
Research and development	79,840	84,170	256,223	252,471
Sales and marketing	66,676	77,536	239,573	269,442
General and administrative	24,812	40,690	91,111	102,815
Total operating expenses	171,328	202,396	586,907	624,728
Operating loss	(17,814)	(27,636)	(200,255)	(182,424)
Interest income, net	2,072	1,162	5,599	2,451
Other income (expense), net	(5,141)	(702)	(2,366)	134
Loss before income taxes	(20,883)	(27,176)	(197,022)	(179,839)
Income tax expense (benefit)	(18,827)	86,227	4,179	51,883
Net loss	$ (2,056)	$ (113,403)	$ (201,201)	$ (231,722)
Net loss per share:				
Basic	$ (0.01)	$ (0.48)	$ (0.83)	$ (1.00)
Diluted	$ (0.01)	$ (0.48)	$ (0.83)	$ (1.00)
Shares used to compute net loss per share:				
Basic	245,838	234,242	242,746	230,918
Diluted	245,838	234,242	242,746	230,918

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

FITBIT, INC.
Condensed Consolidated Statements of Comprehensive Loss
(In thousands)
(unaudited)

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
Net loss	$ (2,056)	$ (113,403)	$ (201,201)	$ (231,722)
Other comprehensive income (loss):				
Cash flow hedges:				
Change in unrealized gain (loss) on cash flow hedges, net of tax benefit (expense) of $43, $192, $709 and $(7), respectively	868	(6,793)	6,780	(20,582)
Less: reclassification for realized net gains included in net loss, net of tax expense (benefit) of $(115), $-, $(244) and $7, respectively	(2,334)	6,617	(3,362)	8,264
Net change, net of tax	(1,466)	(176)	3,418	(12,318)
Change in foreign currency translation adjustment	—	—	—	314
Change in unrealized gain (loss) on available-for-sale investments, net of tax	120	48	(88)	133
Less reclassification for realized net gain (loss)	—	—	12	(12)
Net change, net of tax	120	48	(76)	121
Comprehensive loss	$ (3,402)	$ (113,531)	$ (197,859)	$ (243,605)

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

FITBIT, INC.
Condensed Consolidated Statements of Cash Flows
(In thousands)
(unaudited)

	Nine Months Ended	
	September 29, 2018	September 30, 2017
Cash Flows from Operating Activities		
Net loss	$ (201,201)	$ (231,722)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Provision for doubtful accounts	37	7,805
Provision for inventory obsolescence	9,019	13,395
Depreciation	35,388	28,338
Write-off of property and equipment	7,513	5,250
Amortization of intangible assets	5,866	4,134
Stock-based compensation	73,613	67,256
Deferred income taxes	(1,690)	132,815
Impairment of equity investment	6,000	—
Other	(693)	1,301
Changes in operating assets and liabilities, net of acquisition:		
Accounts receivable	80,227	208,899
Inventories	(80,064)	79,448
Prepaid expenses and other assets	123,356	(125,504)
Accounts payable	16,357	(122,160)
Accrued liabilities and other liabilities	(68,208)	(48,869)
Deferred revenue	(9,649)	(9,846)
Income taxes payable	5,653	(1,822)
Net cash provided by operating activities	1,524	8,718
Cash Flows from Investing Activities		
Purchase of property and equipment	(40,174)	(58,199)
Purchases of marketable securities	(284,986)	(494,540)
Sales of marketable securities	93,020	19,806
Maturities of marketable securities	309,323	500,576
Acquisition, net of cash acquired	(13,646)	(556)
Net cash provided by (used in) investing activities	63,537	(32,913)
Cash Flows from Financing Activities		
Repayment of debt	(747)	—
Proceeds from issuance of common stock	11,641	13,893
Taxes paid related to net share settlement of restricted stock units	(15,684)	(10,804)
Net cash (used in) provided by financing activities	(4,790)	3,089
Net increase (decrease) in cash and cash equivalents	60,271	(21,106)
Effect of exchange rate on cash and cash equivalents	—	467
Cash and cash equivalents at beginning of period	341,966	301,320
Cash and cash equivalents at end of period	$ 402,237	$ 280,681

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

FITBIT, INC.
Notes to Condensed Consolidated Financial Statements

1. Basis of Presentation and Summary of Significant Accounting Policies

The accompanying condensed consolidated financial statements of Fitbit, Inc. (the "Company") are unaudited. The condensed consolidated balance sheet at December 31, 2017 has been derived from the audited financial statements of the Company. The accompanying condensed financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America ("U.S. GAAP") for interim financial information, and in management's opinion, includes all adjustments, consisting of only normal recurring adjustments, necessary for the fair statement of the Company's financial position, its results of operations, and cash flows for the interim periods presented. The results of operations for the three and nine months ended September 29, 2018 are not necessarily indicative of the results to be expected for the full fiscal year or any other period.

The accompanying condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto contained in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2017, filed with the Securities and Exchange Commission ("SEC") on March 1, 2018.

The Company's fiscal year ends on December 31 of each year. The Company is on a 4-4-5 week quarterly calendar. There were 91 days in each of the three months ended September 29, 2018 and September 30, 2017 , and 272 and 273 days in the nine months ended September 29, 2018 and September 30, 2017 , respectively.

The condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All intercompany transactions and balances have been eliminated.

Use of Estimates

The preparation of condensed consolidated financial statements in accordance with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported and disclosed in the condensed consolidated financial statements and accompanying notes. The primary estimates and assumptions made by management are related to revenue recognition, reserves for sales returns and incentives, reserves for warranty, valuation of stock options, fair value of derivative assets and liabilities, allowance for doubtful accounts, inventory valuation, fair value of goodwill and acquired tangible and intangible assets and liabilities assumed during acquisitions, the number of reportable segments, the recoverability of intangible assets and their useful lives, contingencies, income taxes, impairment of equity investment, and unused advertising credits from a non-monetary transaction. Actual results could differ from those estimates, and such differences may be material to the condensed consolidated financial statements.

Significant Accounting Policies

There have been no significant changes in the Company's accounting policies from those disclosed in its Annual Report on Form 10-K, except for the policies described below in relation to the adoption of Accounting Standards Update ("ASU") 2014-09, *Revenue from Contracts with Customers (Topic 606)* , discussed below in the section titled " *Accounting Pronouncements Recently Adopted* ."

Revenue Recognition

The Company recognizes revenue upon transfer of control of promised goods or services to customers at transaction price, an amount that reflects the consideration the Company expects to receive in exchange for those goods or services. Transaction price is calculated selling price net of variable consideration which may include estimates for future returns and sales incentives related to current period product revenue.

Products and Services

The Company derives substantially all of its revenue from sales of its wearable devices, which includes both connected health and fitness devices and accessories and smartwatches. The Company also generates a small portion of revenue from its subscription-based services. The Company considers delivery of its products to have occurred once control has transferred and delivery of services to have occurred as control is transferred. The Company recognizes revenue, net of estimated sales returns, sales incentives, discounts, and sales tax.

Arrangements with Multiple Performance Obligations

The Company enters into contracts that have multiple performance obligations that include hardware, software, and services. The first performance obligation is the hardware and firmware essential to the functionality of the connected health and fitness device or smartwatch delivered at the time of sale. The second performance obligation is the software services included with the products, which are provided free of charge and enable users to sync, view, and access real-time data on the Company’s online dashboard and mobile apps. The third performance obligation is the embedded right included with the purchase of the device to receive, on a when-and-if-available basis, future unspecified firmware upgrades and features relating to the product’s essential firmware. In addition, the Company occasionally offers a fourth performance obligation in bundled arrangements that allows access to subscription-based services related to the Company’s Fitbit Coach offering.

The Company allocates revenue to all performance obligations based on their relative standalone selling prices (“SSP”). The Company’s process for determining its SSP considers multiple factors including consumer behaviors, the Company’s internal pricing model, and cost-plus margin and may vary depending upon the facts and circumstances related to each deliverable. SSP for the health and fitness devices and smartwatches reflect the Company’s best estimate of the selling prices if they were sold regularly on a stand-alone basis and comprise the majority of the arrangement consideration. SSP for upgrade rights currently ranges from $1.00 to $3.00 . SSP for the online dashboard and mobile apps is currently estimated at $0.99 . SSP for access to Fitbit Coach subscription-based services is based on the price charged when sold separately.

Amounts allocated to the delivered wearable devices are recognized at the time of delivery, provided the other conditions for revenue recognition have been met. Amounts allocated to the online dashboard and mobile apps and unspecified upgrade rights are deferred and recognized on a straight-line basis over the estimated usage period.

The Company offers its users the ability to purchase subscription-based services, through which the users receive incremental features, including access to a digital personal trainer, in-depth analytics regarding the user’s personal metrics, or video-based customized workouts. Amounts paid for subscriptions are deferred and recognized ratably over the service period, which is typically one year. Revenue from subscription-based services was less than 1% of revenue for all periods presented.

In addition, the Company offers subscription-based software and services to certain customers in the corporate wellness program, which includes a real-time dashboard, and the ability to create corporate challenges. SSP for the corporate wellness subscription is determined based on the Company’s internal pricing model for anticipated renewals for existing customers and pricing for new customers. Revenue allocated to the corporate wellness subscription is deferred and recognized on a straight-line basis over the estimated access period of one year, which is the typical service period. Revenue for corporate wellness software and services was less than 1% of revenue for all periods presented.

The Company applies a practical expedient to expense costs to obtain a contract with a customer as incurred when the amortization period would be one year or less. The Company applies a practical expedient to not consider the effect of a significant financing component as it expects that the period between transfer of control and payment from customer to be one year or less.

The Company accounts for shipping and handling fees billed to customers as revenue. Sales taxes and value added taxes (“VAT”) collected from customers which are remitted to governmental authorities are not included in revenue, and are reflected as a liability on the consolidated balance sheets.

Rights of Return, Stock Rotation Rights, and Price Protection

The Company offers limited rights of return, stock rotation rights, and price protection under various policies and programs with its retailer and distributor customers and end-users. Below is a summary of the general provisions of such policies and programs:

- Retailers and distributors are generally allowed to return products that were originally sold through to an end-user under provisions of their contracts, called “open-box” returns, and such returns may be made at any time after the original sale.
- All purchases through Fitbit.com are covered by a 45-day right of return.
- Certain distributors are allowed stock rotation rights which are limited rights of return of products purchased during a prior period, generally one quarter.
- Certain distributors and retailers are allowed return rights for defective products.
- Certain distributors are offered price protection that allows for the right to a partial credit for unsold inventory held by the distributor if the Company reduces the selling price of a product.

The Company estimates reserves for these policies and programs based on historical experience, and records the reserves as a reduction of revenue and an accrued liability. Through September 29, 2018 , actual returns have primarily been open-box returns. In addition, through September 29, 2018 , the Company has had limited price protection claims. On a quarterly basis, the amount of revenue that is reserved for future returns is calculated based on historical trends and data specific to each reporting period. The historical trends consider product life cycles, new product introductions, market acceptance of products, product sell-through, the type of customer, seasonality, and other factors. Return rates can fluctuate over time, but have been sufficiently predictable to allow the Company to estimate expected future product returns. The Company reviews the actual returns evidenced in prior quarters as a percent of related revenue to determine the historical rate of returns. The Company then applies the historical rate of returns to the current period revenue as a basis for estimating future returns. When necessary, the Company also provides a specific reserve for products in the distribution channel in excess of estimated requirements. This estimate can be affected by the amount of a particular product in the channel, the rate of sell-through, product plans, and other factors. The Company also considers whether there are circumstances which may result in anticipated returns higher than the historical return rate from direct customers and records an additional specific reserve as necessary. The estimates and assumptions used to reserve for rights of return, stock rotation rights, and price protection have been accurate in all material respects and have not materially changed in the past.

Sales Incentives

The Company offers sales incentives through various programs, consisting primarily of cooperative advertising and marketing development fund programs. The Company records advertising and marketing development fund programs with customers as a reduction to revenue unless it receives a distinct benefit in exchange for credits claimed by the customer and can reasonably estimate the fair value of the distinct benefit received, in which case the Company records it as a marketing expense. The Company recognizes a liability and reduces revenue for rebates or other incentives based on the estimated amount of rebates or credits that will be claimed by customers.

Refer to Note 10 for disaggregated revenue by geographic region, based on ship-to destinations.

Customer Bankruptcy

In September 2017, Wynit Distribution (“Wynit”) filed for bankruptcy protection under Chapter 11 of the United States Bankruptcy Code. Wynit was the Company’s largest customer, historically representing 11% of total revenue during the six months ended July 1, 2017 and 19% of total accounts receivables as of July 1, 2017. As of July 1, 2017, collectability of accounts receivables from Wynit was reasonably assured. In connection with Wynit’s bankruptcy filing, the Company believed that the collectability of the product shipments to Wynit during the third quarter of 2017 was not reasonably assured.

The Company ceased to recognize revenue from Wynit, which totaled $8.1 million during the third quarter of 2017. Additionally, the Company recorded a charge of $35.8 million during the third quarter ended September 30, 2017 comprised of cost of revenue of $5.5 million associated with shipments to Wynit in the third quarter of 2017 and bad debt expense of $30.3 million associated with all of Wynit’s outstanding accounts receivables. The Company maintains credit insurance that covers a portion of the exposure related to its customer receivables. The Company recorded an insurance receivable based on an analysis of its insurance policies, including their exclusions, an assessment of the nature of the claim, and information from its insurance carrier. As of September 30, 2017, the Company had recorded an insurance receivable of $26.8 million , included in prepaid expenses and other current assets, associated with the amount it had concluded was probable related to the claim. The $26.8 million insurance receivable allowed the Company to recover $22.7 million of bad debt expense and $4.1 million of cost of revenue, resulting in a net charge of $9.0 million in the consolidated statement of operations comprised of net bad debt expense of $7.6 million and net cost of revenue of $1.4 million . The Company received $21.4 million of the insurance receivable during the fourth quarter of 2017 and the remaining $5.4 million in January 2018.

During the nine months ended September 29, 2018 , the Company released $12.4 million in outstanding product return and rebate reserves related to Wynit, as it believed the possibility of future claims associated with these reserves was remote. This reserve release resulted in a $12.4 million increase in revenue during the nine months ended September 29, 2018 .

Non-Monetary Transaction

The Company entered into an agreement with a third party during 2016 to exchange inventory for advertising credits and cash, which was amended in October 2018 to extend the contractual period from four to six years. The Company recorded the transaction based on the estimated fair value of the products exchanged. For the year ended December 31, 2016, the Company recorded $15.0 million of revenue and $7.0 million of associated cost of goods sold upon exchange of the products for advertising credits of $13.0 million and cash of $2.0 million . The $13.0 million of unused advertising credits remaining as of December 31, 2016 were recorded in prepaid expenses and other current assets, and other assets. Such credits are expected to be used over the contractual period of six years, and will be expensed as advertising services are received. During the three months ended

September 29, 2018 and September 30, 2017 , negligible amounts of credits were utilized in each of these periods, and during the nine months ended September 29, 2018 and September 30, 2017 , $1.1 million and $0.3 million , respectively, of credits were utilized in each of these periods. The Company's prepaid and other assets related to unused advertising credits as of September 29, 2018 and December 31, 2017 were $11.1 million and $12.2 million , respectively.

Recent Accounting Pronouncements

Accounting Pronouncements Not Yet Adopted

In February 2016, the Financial Accounting Standards Board (the "FASB") issued ASU 2016-02, Leases (Topic 842) and subsequent amendments to the initial guidance; ASU 2017-13, ASU 2018-10 and ASU 2018-11 (collectively, Topic 842). Topic 842 requires lessees to recognize right-of-use assets and lease liabilities for operating leases, initially measured at the present value of the lease payments, on the balance sheet. Topic 842 will become effective for the Company on January 1, 2019, and requires adoption using a modified retrospective approach. The Company is continuing to make progress in evaluating the impact of this guidance on its consolidated financial statements, and preliminary assessments are subject to change. The Company's implementation team has made progress in its project plan, which includes evaluating contracts, developing policies, processes and information technology tools to report financial results, and implementing and evaluating the Company's internal controls over financial reporting that will be necessary under the new standard. Upon adoption, the Company expects to elect the transition package of practical expedients permitted within the new standard, which amount other things, allows the carryforward of the historical lease classification. The Company anticipates that the adoption will have a material impact on its consolidated balance sheets, as it will now include a right of use asset and a lease liability for the obligation to make lease payments related to substantially all operating lease arrangements; however, the Company does not expect the adoption to have a material impact on its consolidated statements of operations.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. ASU 2016-13 provides for a new impairment model which requires measurement and recognition of expected credit losses for most financial assets and certain other instruments, including but not limited to accounts receivable and available for sale debt securities. ASU 2016-13 will become effective for the Company on January 1, 2020 and early adoption is permitted. The Company is currently evaluating the impact of this guidance on its consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04, Intangibles-Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment. ASU 2017-04 simplifies the subsequent measurement of goodwill by eliminating the second step of the goodwill impairment test. The second step measures a goodwill impairment loss by comparing the implied fair value of a reporting unit's goodwill with the carrying amount of that goodwill. Under ASU 2017-04, a company will record an impairment charge based on the excess of a reporting unit's carrying amount over its fair value. ASU 2017-04 will be applied prospectively and is effective for annual or interim goodwill impairment tests in fiscal years beginning after December 15, 2019. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. The Company is currently evaluating the impact of this guidance on its consolidated financial statements.

In June 2018, the FASB issued ASU 2018-07, Compensation-Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting. ASU 2018-07 expands the scope of Topic 718 to include share-based payment transactions for acquiring goods and services from nonemployees. ASU 2018-07 will become effective for the Company on January 1, 2019 and early adoption is permitted. The Company is currently evaluating the impact of this guidance on its consolidated financial statements.

In August 2018, the FASB issued ASU 2018-13, Fair Value Measurement (Topic 820): Disclosure Framework-Changes to the Disclosure Requirements for Fair Value Measurement. ASU 2018-13 modifies the disclosure requirements on fair value measurements and will become effective for the Company on January 1, 2020 and early adoption is permitted. The Company is currently evaluating the impact of this guidance on its consolidated financial statements.

In August 2018, the FASB issued ASU 2018-15, Intangibles-Goodwill and Other-Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract. ASU 2018-15 clarifies the accounting for implementation costs in cloud computing arrangements and will become effective for the Company on January 1, 2020 and early adoption is permitted. The Company is currently evaluating the impact of this guidance on its consolidated financial statements.

Accounting Pronouncements Recently Adopted

In May 2014, the FASB, issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606), which affects any entity that either enters into contracts with customers to transfer goods and services or enters into contracts for the transfer of nonfinancial assets. The standard's core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services.

The Company adopted ASU 2014-09 effective January 1, 2018, utilizing the modified retrospective transition method. Prior periods were not retrospectively adjusted. Upon adoption, the Company recognized an immaterial cumulative effect of adopting this guidance as an adjustment to its opening accumulated deficit balance. The new standard may, in certain circumstances, impact the timing of when revenue is recognized for products shipped, and the timing and classification of certain sales incentives, which are expected to generally be recognized earlier than historical guidance. The Company believes the new guidance is materially consistent with its historical revenue recognition policy. In addition, ASU 2014-09 requires the presentation of sales returns reserve as a current liability. The Company's sales return reserve was $78.5 million as of September 29, 2018 , presented within "Accrued liabilities" and was $109.9 million as of December 31, 2017, presented within "Accounts receivable, net."

The impact to revenue, accounts receivable, deferred revenue, and accrued liabilities as a result of applying ASU 2014-09 for the three and nine months ended or as of September 29, 2018 was as follows (in thousands):

	Three Months Ended September 29, 2018			Nine Months Ended September 29, 2018		
	Under ASC 605	Impact	Under ASC 606	Under ASC 605	Impact	Under ASC 606
Revenue	$ 395,438	$ (1,863)	$ 393,575	$ 941,272	$ (488)	$ 940,784
Accounts receivable, net	247,447	78,517	325,964	247,447	78,517	325,964
Deferred revenue	33,102	(294)	32,808	33,102	(294)	32,808
Accrued liabilities	306,663	79,721	386,384	306,663	79,721	386,384
Accumulated deficit	(327,952)	(6,488)	(334,440)	(327,952)	(6,488)	(334,440)

The impact to other financial statement line items was immaterial. Adoption of the standard had no impact to net cash from or used in operating, investing, or financing activities in the Company's condensed consolidated statement of cash flows.

In January 2016, the FASB issued ASU 2016-01, Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities, which updates certain aspects of recognition, measurement, presentation and disclosure of financial instruments. The Company has elected to measure equity investments that do not have readily determinable fair values at cost minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or a similar investment of the same issuer. The adoption of this standard did not have a material impact on the Company's consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230). ASU 2016-15 provides guidance intended to reduce diversity in practice in how certain transactions are classified in the statement of cash flows. ASU 2016-15 provides guidance in a number of situations including, among others, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims, distributions received from equity method investees, and classifying cash receipts and payments that have aspects of more than one class of cash flows. ASU 2016-15 became effective for the Company on January 1, 2018. The adoption of this standard did not have a material impact on the Company's consolidated financial statements.

In January 2017, the FASB issued ASU 2017-01, Business Combinations (Topic 805): Clarifying the Definition of a Business. The purpose of ASU 2017-01 is to change the definition of a business to assist entities with evaluating when a set of transferred assets and activities is a business. ASU 2017-01 became effective for the Company on January 1, 2018. The adoption of this standard did not have a material impact on the Company's consolidated financial statements.

In May 2017, the FASB issued ASU 2017-09, Compensation-Stock Compensation (Topic 718): Scope of Modification Accounting. ASU 2017-09 was issued to clarify and reduce both (i) diversity in practice and (ii) cost and complexity when applying the guidance in Topic 718 to a change to the terms and conditions of a share-based payment award. ASU 2017-09 became effective for the Company on January 1, 2018. The adoption of this standard did not have a material impact on the Company's consolidated financial statements.

In August 2017, the FASB issued ASU 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities. ASU 2017-12 amends the hedge accounting rules to simplify the application of hedge accounting standard and better portray the economic results of risk management activities in the financial statements. The standard expands the ability to hedge non-financial and financial risk components, reduces complexity in fair value hedges of interest rate risk, eliminates the requirement to separately measure and report hedge ineffectiveness, as well as eases certain hedge effectiveness assessment requirements. ASU 2017-12 becomes effective for the Company on January 1, 2019 with early adoption permitted. The Company early adopted this new standard in the first quarter of 2018. The adoption of this standard did not have a material impact on the Company's consolidated financial statements.

2. Fair Value Measurements

The carrying values of the Company's accounts receivable, accounts payable, and accrued liabilities approximated their fair values due to the short period of time to maturity or repayment.

The following tables set forth the Company's financial instruments that were measured at fair value on a recurring basis by level within the fair value hierarchy (in thousands):

	September 29, 2018			
	Level 1	Level 2	Level 3	Total
Assets:				
Money market funds	$ 218,567	$ —	$ —	$ 218,567
U.S. government agencies	—	82,734	—	82,734
Corporate debt securities	—	207,378	—	207,378
Derivative assets	—	4,681	—	4,681
Total	$ 218,567	$ 294,793	$ —	$ 513,360
Liabilities:				
Derivative liabilities	$ —	$ 86	$ —	$ 86
Stock warrant liability	—	—	412	412
Total	$ —	$ 86	$ 412	$ 498

	December 31, 2017			
	Level 1	Level 2	Level 3	Total
Assets:				
Money market funds	$ 193,066	$ —	$ —	$ 193,066
U.S. government agencies	—	79,624	—	79,624
Corporate debt securities	—	291,582	—	291,582
Total	$ 193,066	$ 371,206	$ —	$ 564,272
Liabilities:				
Derivative liabilities	$ —	$ 2,138	$ —	$ 2,138
Stock warrant liability	—	—	208	208
Total	$ —	$ 2,138	$ 208	$ 2,346

The fair value of the Company's Level 1 financial instruments is based on quoted market prices in active markets for identical instruments. The fair value of the Company's Level 2 financial instruments is based on observable inputs other than quoted prices in active markets for identical assets and liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data.

In addition, Level 2 assets and liabilities include derivative financial instruments associated with hedging activity, which are further discussed in Note 3. Derivative financial instruments are initially measured at fair value on the contract date and are subsequently remeasured to fair value at each reporting date using inputs such as spot rates, forward rates, and discount rates. There is not an active market for each hedge contract, but the inputs used to calculate the value of the instruments are tied to active markets.

There were no Level 3 assets as of September 29, 2018 and December 31, 2017. There were Level 3 liabilities as of September 29, 2018 and December 31, 2017. There have been no transfers between fair value measurement levels during the three and nine months ended September 29, 2018 and September 30, 2017 .

In December 2017, the Company acquired an equity ownership interest in a privately-held company in exchange for $6.0 million in cash. The Company does not have a controlling interest or the ability to exercise significant influence over the investee, and this investment does not have a readily determinable fair value. Upon adoption of ASU 2016-01 on January 1, 2018, the Company elected to measure equity investments that do not have readily determinable fair values at cost minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or a similar investment of the same issuer. Such changes in the basis of the equity investment are recognized in “Other income (expense), net” in the Company’s consolidated statement of operations. During the three months ended September 29, 2018, the Company identified events and circumstances that indicated that there was a decline in the fair value of this investment. As a result, the Company performed an assessment of the financial condition, financial forecast, near-term financing prospects, and other factors of the issuer, and concluded that this equity investment was fully impaired and recorded an impairment loss of $6.0 million . This equity investment was classified within “Other assets” on the Company’s consolidated balance sheets as of September 29, 2018 and December 31, 2017.

3. Financial Instruments

Cash, Cash Equivalents and Marketable Securities

The Company’s marketable securities are classified as available-for-sale as of the balance sheet date and are reported at fair value with unrealized gains and losses reported, net of tax, as a separate component of accumulated other comprehensive income (loss) in stockholders’ equity. Because the Company views marketable securities as available to support current operations as needed, it has classified all available-for-sale securities as current assets. Realized gains or losses and other-than-temporary impairments, if any, on available-for-sale securities are reported in other income (expense), net, as incurred.

Investments are reviewed periodically to identify potential other-than-temporary impairments. No impairment loss has been recorded on the securities included in the tables below because the Company believes that the decrease in fair value of these securities is temporary and expects to recover up to, or beyond, the initial cost of investment for these securities.

The following table sets forth cash, cash equivalents and marketable securities as of September 29, 2018 (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Cash and Cash Equivalents	Marketable Securities
Cash	$ 114,641	$ —	$ —	$ 114,641	$ 114,641	$ —
Money market funds	218,567	—	—	218,567	218,567	—
U.S. government agencies	82,837	1	(104)	82,734	13,649	69,085
Corporate debt securities	207,426	2	(50)	207,378	55,380	151,998
Total	$ 623,471	$ 3	$ (154)	$ 623,320	$ 402,237	$ 221,083

The following table sets forth cash, cash equivalents and marketable securities as of December 31, 2017 (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Cash and Cash Equivalents	Marketable Securities
Cash	$ 115,028	$ —	$ —	$ 115,028	$ 115,028	$ —
Money market funds	193,066	—	—	193,066	193,066	—
U.S. government agencies	79,722	1	(99)	79,624	6,595	73,029
Corporate debt securities	291,738	15	(171)	291,582	27,277	264,305
Total	$ 679,554	$ 16	$ (270)	$ 679,300	$ 341,966	$ 337,334

The gross unrealized gains or losses on marketable securities as of September 29, 2018 and December 31, 2017 were not material. There were no available-for-sale investments as of September 29, 2018 and December 31, 2017 that have been in a continuous unrealized loss position for greater than 12 months on a material basis.

The following table classifies marketable securities by contractual maturities (in thousands):

	September 29, 2018	December 31, 2017
Due in one year	$ 221,083	$ 319,112
Due in one to two years	—	18,222
Total	$ 221,083	$ 337,334

Derivative Financial Instruments

The Company operates in foreign countries, which exposes it to market risk associated with foreign currency exchange rate fluctuations between the U.S. dollar and various foreign currencies. In order to manage this risk, the Company may hedge a portion of its foreign currency exposures related to outstanding monetary assets and liabilities as well as forecasted revenues and expenses, using foreign currency exchange forward or option contracts. In general, the market risk related to these contracts is offset by corresponding gains and losses on the hedged transactions. The Company does not enter into derivative contracts for trading or speculative purposes.

Cash Flow Hedges

The Company has entered into foreign currency derivative contracts designated as cash flow hedges to hedge certain forecasted revenue and expense transactions denominated in currencies other than the U.S. dollar. The Company's cash flow hedges consist of forward contracts with maturities of 12 months or less.

The Company periodically assesses the effectiveness of its cash flow hedges. Effectiveness represents a derivative instrument's ability to generate offsetting changes in cash flows related to the hedged risk. The Company records the gains or losses, net of tax, related to its cash flow hedges as a component of accumulated other comprehensive income (loss) in stockholders' equity and subsequently reclassifies the gains or losses into revenue and operating expenses when the underlying hedged transactions are recognized. If the hedged transaction becomes probable of not occurring, the corresponding amounts in accumulated other comprehensive income (loss) would immediately be reclassified to other income (expense), net. Cash flows related to the Company's cash flow hedging program are recognized as cash flows from operating activities in its statements of cash flows. Prior to the adoption of ASU 2017-12, the Company recorded the gains or losses related to the ineffective portion of its cash flow hedges, if any, immediately in other income (expense), net. For the period ended September 30, 2017 , the ineffective portion of the Company's cash flow hedges were not material.

The Company had outstanding contracts with a total notional amount of $60.2 million in cash flow hedges for forecasted revenue as of September 29, 2018 , and no outstanding contracts that were designated in cash flow hedges for forecasted revenue as of December 31, 2017.

Balance Sheet Hedges

The Company enters into foreign exchange contracts to hedge certain monetary assets and liabilities that are denominated in currencies other than the functional currency of its subsidiaries. These foreign exchange contracts are carried at fair value, do not qualify for hedge accounting treatment, and are not designated as hedging instruments. Changes in the value of the foreign exchange contracts are recognized in other income (expense), net, and offset the foreign currency gain or loss on the underlying net monetary assets or liabilities.

The Company had outstanding balance sheet hedges with a total notional amount of $146.3 million and $141.2 million as of September 29, 2018 and December 31, 2017, respectively.

Fair Value of Foreign Currency Derivatives

The foreign currency derivative contracts that were not settled at the end of the period are recorded at fair value, on a gross basis, in the condensed consolidated balance sheets. The following table presents the fair value of the Company's foreign currency derivative contracts as of the periods presented (in thousands):

		September 29, 2018		December 31, 2017	
	Balance Sheet Location	Fair Value Derivative Assets	Fair Value Derivative Liabilities	Fair Value Derivative Assets	Fair Value Derivative Liabilities
Cash flow designated hedges	Prepaid expenses and other current assets	$ 3,882	$ —	$ —	$ —
Cash flow designated hedges	Accrued liabilities	—	—	—	—
Hedges not designated	Prepaid expenses and other current assets	799	—	—	—
Hedges not designated	Accrued liabilities	—	86	—	2,138
Total fair value of derivative instruments		$ 4,681	$ 86	$ —	$ 2,138

Financial Statement Effect of Foreign Currency Derivative Contracts

The following table presents the pre-tax impact of the Company's foreign currency derivative contracts on other comprehensive income ("OCI") and the condensed consolidated statements of operations for the periods presented (in thousands):

		Three Months Ended		Nine Months Ended	
	Income Statement Location	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
Foreign exchange cash flow hedges:					
Gain (loss) recognized in OCI – effective portion		$ 911	$ (6,603)	$ 7,489	$ (20,590)
Gain (loss) reclassified from OCI into income – effective portion	Revenue	2,449	(6,617)	3,606	(6,897)
Loss reclassified from OCI into income – effective portion	Operating expenses	—	—	—	(1,405)
Gain recognized in income – ineffective portion	Other income, net	—	—	—	21
Gain recognized in income – excluded time value portion	Other income, net	—	672	—	1,516
Foreign exchange balance sheet hedges:					
Gain (loss) recognized in income	Other income, net	1,035	(2,062)	3,335	(8,838)

As of September 29, 2018 , all net derivative gains related to the Company's cash flow hedges will be reclassified from OCI into revenue within the next 12 months.

Effect of Derivative Contracts on Condensed Consolidated Statements of Operations

The following table provides the location in the condensed consolidated statements of operations and amount of the recognized gains or losses to the Company's derivative instruments designated as hedging instruments (in thousands):

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
Total amounts presented in the condensed consolidated statement of operations in which the effects of cash flow hedges are recorded in revenue	$ 393,575	$ 392,522	$ 940,784	$ 1,044,763
Total amounts presented in the condensed consolidated statement of operations in which the effects of cash flow hedges are recorded in operating expenses	171,328	202,396	586,907	624,728
Gains (losses) on foreign exchange contracts designated as cash flow hedges reclassified from OCI into revenue	2,449	(6,617)	3,606	(6,897)
Losses on foreign exchange contracts designated as cash flow hedges reclassified from OCI into operating expenses	—	—	—	(1,405)

Offsetting of Foreign Currency Derivative Contracts

The Company presents its derivative assets and derivative liabilities at gross fair values in the condensed consolidated balance sheets. The Company generally enters into master netting arrangements, which mitigate credit risk by permitting net settlement of transactions with the same counterparty. The Company is not required to pledge, and is not entitled to receive, cash collateral related to these derivative instruments.

The following tables set forth the available offsetting of net derivative assets under the master netting arrangements as of September 29, 2018 and December 31, 2017 (in thousands):

	Gross Amounts Offset in the Condensed Consolidated Balance Sheets			Gross Amounts Not Offset in Condensed Consolidated Balance Sheets		
September 29, 2018	Gross Amounts Recognized	Gross Amounts Offset	Net Amounts Presented	Financial Instruments	Cash Collateral Received	Net Amount
Foreign exchange contracts assets	$ 4,681	$ —	$ 4,681	$ 86	$ —	$ 4,595
Foreign exchange contracts liabilities	86	—	86	86	—	—

	Gross Amounts Offset in the Condensed Consolidated Balance Sheets			Gross Amounts Not Offset in Condensed Consolidated Balance Sheets		
December 31, 2017	Gross Amounts Recognized	Gross Amounts Offset	Net Amounts Presented	Financial Instruments	Cash Collateral Received	Net Amount
Foreign exchange contracts assets	$ —	$ —	$ —	$ —	$ —	$ —
Foreign exchange contracts liabilities	2,138	—	2,138	—	—	2,138

4. Balance Sheet Components

Deferred Revenue

Deferred revenue consists of deferred shipments in transit for which control has not yet transferred, deferred software, or amounts allocated to mobile dashboard and on-line apps and unspecified upgrade rights, and deferred subscription-based services for which payments have been received by the customer prior to revenue recognition of these performance obligations. The deferred shipments performance obligation is anticipated to be recognized within the next quarter. The deferred software and deferred subscription-based services performance obligations are anticipated to be recognized over the useful life or service periods of twelve to seventeen months.

Changes in the total short-term and long-term deferred revenue balance were as follows (in thousands):

	Three Months Ended September 29, 2018	Nine Months Ended September 29, 2018
Beginning balances	$ 32,835	$ 42,432
Deferral of revenue	10,176	25,885
Recognition of deferred revenue	(10,203)	(35,509)
Ending balances	$ 32,808	$ 32,808

Revenue Returns Reserve

Revenue returns reserve activities were as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017 (1)	September 29, 2018	September 30, 2017 (1)
Beginning balances	$ 74,996	$ 51,520	$ 109,872	$ 98,851
Increases	43,383	56,445	106,385	146,356
Returns taken	(39,862)	(46,067)	(137,740)	(183,309)
Ending balances	$ 78,517	$ 61,898	$ 78,517	$ 61,898

(1) The Company corrected the amounts presented as “Increases” and “Returns taken” for the three and nine months ended September 30, 2017. The Company did not consider this correction to be material since it had no impact on the beginning and ending balances of the revenue returns reserve and did not have any impact on its condensed consolidated balance sheets and statements of operations.

Increases in the revenue returns reserve include provisions for open box returns and stock rotations.

Inventories

Inventories consisted of the following (in thousands):

	September 29, 2018	December 31, 2017
Components	$ 19,608	$ 3,825
Finished goods	175,504	120,070
Total inventories	$ 195,112	$ 123,895

Prepaid Expenses and Other Current Assets

Prepaid expenses and other current assets consisted of the following (in thousands):

	September 29, 2018	December 31, 2017
Prepaid expenses	$ 16,298	$ 24,204
Point-of-purchase displays, net	8,114	14,750
Derivative assets	4,681	—
Prepaid marketing	2,525	6,074
Insurance receivable	—	37,300
Other	13,923	14,941
Total prepaid expenses and other current assets	$ 45,541	$ 97,269

Property and Equipment, Net

Property and equipment, net, consisted of the following (in thousands):

	September 29, 2018	December 31, 2017
Tooling and manufacturing equipment	$ 69,889	$ 66,854
Furniture and office equipment	22,756	20,942
Purchased and internally-developed software	20,925	18,112
Leasehold improvements	66,053	58,431
Total property and equipment	179,623	164,339
Less: Accumulated depreciation and amortization	(73,103)	(59,431)
Property and equipment, net	$ 106,520	$ 104,908

Total depreciation and amortization expense related to property and equipment, net was $11.8 million and $9.1 million for the three months ended September 29, 2018 and September 30, 2017 , respectively, and $35.4 million and $28.3 million for the nine months ended September 29, 2018 and September 30, 2017 , respectively.

Goodwill and Intangible Assets

The changes in the carrying amount of goodwill were as follows (in thousands):

	Goodwill
Balance at December 31, 2017	$ 51,036
Goodwill acquired	10,022
Balance at September 29, 2018	$ 61,058

The increase in the carrying amount of goodwill during the nine months ended September 29, 2018 was attributable to an acquisition in February 2018 described in Note 11.

The carrying amounts of the intangible assets as of September 29, 2018 and December 31, 2017 were as follows (in thousands, except useful life):

	September 29, 2018			December 31, 2017		
	Gross	Accumulated Amortization	Net	Gross	Accumulated Amortization	Net
Developed technology	$ 35,988	$ (14,116)	$ 21,872	$ 30,588	$ (8,738)	$ 21,850
Customer relationships	3,790	(316)	3,474	—	—	—
Trademarks and other	1,278	(944)	334	1,278	(772)	506
Total intangible assets, net	$ 41,056	$ (15,376)	$ 25,680	$ 31,866	$ (9,510)	$ 22,356

The increase in the carrying amount of goodwill during the nine months ended September 29, 2018 was attributable to an acquisition in February 2018 described in Note 11. Total amortization expense related to intangible assets was $2.1 million and $1.4 million for the three months ended September 29, 2018 and September 30, 2017 , respectively, and $5.9 million and $4.1 million for the nine months ended September 29, 2018 and September 30, 2017 , respectively.

The estimated future amortization expense of acquired finite-lived intangible assets to be charged to cost of revenue and operating expenses after September 29, 2018 was as follows (in thousands):

	Cost of Revenue	Operating Expenses	Total
Remaining 2018	$ 1,854	$ 207	$ 2,061
2019	6,634	827	7,461
2020	5,854	643	6,497
2021	5,854	597	6,451
2022	1,180	597	1,777
Thereafter	—	1,433	1,433
Total finite-lived intangible assets, net	$ 21,376	$ 4,304	$ 25,680

Accrued Liabilities

Accrued liabilities consisted of the following (in thousands):

	September 29, 2018	December 31, 2017
Accrued sales incentives	$ 98,812	$ 111,592
Accrued revenue reserve from returns	78,517	—
Product warranty	47,855	87,882
Accrued manufacturing expense and freight	32,738	41,901
Employee-related liabilities	30,949	33,266
Accrued co-op advertising and marketing development funds	19,599	30,408
Accrued sales and marketing	15,325	44,401
Inventory received but not billed	15,218	10,526
Sales taxes and VAT payable	15,191	21,340
Accrued research and development	6,064	8,983
Accrued legal settlements and fees	4,979	36,693
Derivative liabilities	86	2,138
Other	21,051	23,007
Accrued liabilities	$ 386,384	$ 452,137

Product warranty reserve activities were as follows (in thousands) [(1)] :

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
Beginning balances	$ 50,468	$ 72,761	$ 87,882	$ 99,923
Charged to cost of revenue	9,245	26,825	(1,722)	44,167
Changes related to pre-existing warranties	(1,354)	5,669	(9,226)	8,142
Settlement of claims	(10,504)	(18,576)	(29,079)	(65,553)
Ending balances	$ 47,855	$ 86,679	$ 47,855	$ 86,679

(1) Does not include reserves established as a result of the recall of the Fitbit Force. See the section titled " — Fitbit Force Recall Reserve" in the Company's Annual Report on Form 10-K for additional information regarding such reserves.

Restructuring

In January 2017, the Company announced cost-efficiency measures to be implemented in 2017 that include realigning sales and marketing spend and improved optimization of research and development investments. In addition, the Company announced a reorganization, including a reduction in workforce. This reorganization impacted approximately 110 employees, or approximately 6% of the Company's global workforce. The Company recorded $6.4 million in total restructuring expenses, substantially all of which were severance and related costs, in the first quarter of 2017. The Company completed the reorganization in the fourth quarter of 2017.

Accumulated Other Comprehensive Income (Loss)

The components and activity of accumulated other comprehensive income ("AOCI"), net of tax, were as follows (in thousands):

	Unrealized Gains (Losses) on Cash Flow Hedges	Currency Translation Adjustments	Unrealized Gains (Losses) on Available-for-Sale Investments	Total
Balance at December 31, 2017	$ 66	$ —	$ (75)	$ (9)
Other comprehensive income (loss) before reclassifications	6,780	—	(88)	6,692
Amounts reclassified from AOCI	(3,362)	—	12	(3,350)
Other comprehensive income (loss)	3,418	—	(76)	3,342
Balance at September 29, 2018	$ 3,484	$ —	$ (151)	$ 3,333

5. Long-Term Debt

2015 Credit Agreement

In December 2015, the Company entered into a second amended and restated credit agreement (the "Senior Facility") with Silicon Valley Bank ("SVB"), as administrative agent, collateral agent, and lender, SunTrust Bank as syndication agent, SunTrust Robinson Humphrey, Inc. and several other lenders to replace the existing asset-based credit facility and cash flow facility. The Senior Facility allowed the Company to borrow up to $250.0 million , including up to $ 50.0 million for the issuance of letters of credit and up to $25.0 million for swing line loans, subject to certain financial covenants and ratios. The Company has the option to repay its borrowings under the Senior Facility without penalty prior to maturity. The Senior Facility requires the Company to comply with certain financial and non-financial covenants. The Senior Facility contains customary covenants that restrict the Company's ability to, among other things, incur additional indebtedness, sell certain assets, guarantee certain obligations of third parties, declare dividends or make certain distributions, and undergo a merger or consolidation or certain other transactions. Obligations under the Senior Facility are collateralized by substantially all of the Company's assets, excluding its intellectual property.

In May 2017, the Company entered into a first amendment to the Senior Facility (the “First Amendment”), pursuant to which the aggregate amount the Company can borrow under the Senior Facility was reduced from $250.0 million to $100.0 million , with up to $50.0 million available for the issuance of letters of credit and up to $25.0 million available for swing line loans. In addition, pursuant to the First Amendment, the applicable margin in respect of the interest rates under the Senior Facility was amended to be based on the Company’s level of liquidity (defined as the sum of the Company’s aggregate cash holdings and the amount available under its revolving commitments) and range from, with respect to Alternate Base Rate loans, 0.5% to 1.0% , and, with respect to LIBOR loans, 1.5% to 2.0% . Among other changes, the First Amendment also removed the fixed charge coverage ratio covenant and the consolidated leverage ratio covenant, and added a general liquidity covenant requiring the Company to maintain liquidity of at least $200.0 million in unrestricted cash, of which $100.0 million in cash or cash equivalents must be held in accounts subject to control agreements with, and maintained by, SVB or its affiliates.

The Company was in compliance with the financial covenants under the Senior Facility as of September 29, 2018 . As of September 29, 2018 , the Company had no outstanding borrowings under the Senior Facility and had outstanding letters of credit totaling $36.8 million , issued to cover various security deposits on its facility leases.

Letters of Credit

As of September 29, 2018 and December 31, 2017, the Company had outstanding letters of credit of $36.8 million and $36.9 million , respectively, in each period issued to cover the security deposit on the lease of its office headquarters in San Francisco, California, and other facility leases.

6. Commitments and Contingencies

Leases

The Company’s principal facility is located in San Francisco, California. The Company also leases office space in various locations with expiration dates between 2019 and 2024. The lease agreements often include leasehold improvement incentives, escalating lease payments, renewal provisions and other provisions which require the Company to pay taxes, insurance, maintenance costs or defined rent increases. All of Company’s leases are accounted for as operating leases. In June 2018, the Company notified the lessor of its intent to sublease a portion of one of its San Francisco offices. Under the terms of the lease, the lessor has the right to recapture this space. The lessor elected to exercise their recapture right effective August 1, 2018, which resulted in a reduction of approximately $81.4 million in the Company’s future lease obligations associated with this lease. Future minimum payments under the Company’s noncancelable lease agreements, reduced by the recaptured amount, was as follow (in thousands):

Remaining 2018	$	8,399
2019		33,550
2020		29,387
2021		27,130
2022		26,850
Thereafter		37,554
Total future minimum lease payments	$	162,870

Rent expense is recorded over the lease terms on a straight-line basis. Rent expense was $7.3 million and $10.4 million for the three months ended September 29, 2018 and September 30, 2017 , respectively, and $ 24.1 million and $29.6 million for the nine months ended September 29, 2018 and September 30, 2017 , respectively.

Purchase Commitments

The aggregate amount of open purchase orders as of September 29, 2018 was approximately $434.6 million , of which $185.0 million related to the Company’s migration to a third-party hosting provider. The Company cannot determine the aggregate amount of such purchase orders that represent contractual obligations because purchase orders may represent authorizations to purchase rather than binding agreements. The Company’s purchase orders are based on its current needs and are fulfilled by its suppliers, contract manufacturers, and logistics providers within short periods of time.

During the normal course of business, the Company and its contract manufacturers procure components based upon a forecasted production plan. If the Company cancels all or part of the orders, or materially reduces forecasted orders, it may be liable to its suppliers and contract manufacturers for the cost of the excess components purchased by its contract manufacturers. As of September 29, 2018 , $11.6 million was accrued for such liabilities to contract manufacturers.

Legal Proceedings

Jawbone. On May 27, 2015, Aliphcom, Inc. d/b/a Jawbone ("Jawbone"), filed a lawsuit in the Superior Court of California in the County of San Francisco against the Company and five of its employees who were formerly employed by Jawbone, alleging trade secret misappropriation and unfair and unlawful business practices against all defendants, and alleging breach of contract and breach of implied covenant of good faith and fair dealing against the employee defendants. The complaint sought unspecified damages, including punitive damages and injunctive relief. On June 23, 2016, Jawbone filed a Second Amended Complaint, adding a sixth employee defendant and related allegations.

On June 10, 2015, Jawbone and BodyMedia, Inc., a wholly-owned subsidiary of Jawbone ("BodyMedia"), filed a lawsuit against the Company in the U.S. District Court for the Northern District of California, alleging that the Company infringes certain U.S. patents. The complaint sought unspecified compensatory damages and attorneys' fees from the Company and to permanently enjoin the Company from making, manufacturing, using, selling, importing, or offering the Company's products for sale. The lawsuit was stayed pending resolution the investigation in the U.S. International Trade Commission (the "ITC").

On July 7, 2015, Jawbone and BodyMedia filed a complaint with the ITC requesting an investigation into purported violations of the Tariff Act of 1930 by the Company and Flextronics International Ltd. and Flextronics Sales and Marketing (A-P) Ltd. The complaint makes the same patent infringement and trade secret misappropriation claims as the two earlier cases. The complaint seeks a limited exclusion order and a cease and desist order halting the importation and sale of the infringing products. The ITC instituted the investigation on August 17, 2015. As a result of motions, all of the patent infringement claims were dismissed from the case. A trial on the trade secrets allegations took place from May 9 to 17, 2016. On August 23, 2016, the administrative law judge concluded that the Company did not misappropriate any Jawbone trade secrets. On October 20, 2016, the ITC terminated the investigation in the ITC. Jawbone appealed the dismissal of the patent infringement claims to the Federal Circuit. Oral argument was scheduled for November 9, 2017.

On September 3, 2015, the Company filed a lawsuit against Jawbone in the U.S. District Court for the District of Delaware, alleging that Jawbone's activity trackers infringe certain U.S. patents. This case was transferred to the U.S. District Court for the Northern District of California. The trial was scheduled for July 13, 2020. On September 8, 2015, the Company filed a complaint for patent infringement against Jawbone in the U.S. District Court for the Northern District of California, asserting that Jawbone's activity trackers infringe certain U.S. patents. No trial date was set. On October 29, 2015, the Company filed a complaint for patent infringement against Jawbone in the U.S. District Court for the District of Delaware, asserting that Jawbone's activity trackers infringe certain U.S. patents. That case was also transferred to the U.S. District Court for the Northern District of California. No trial date was set.

On November 2, 2015, the Company filed a complaint with the ITC requesting an investigation into violations of the Tariff Act of 1930 by Jawbone and Body Media. The complaint asserted that Jawbone's products infringe certain U.S. patents. The complaint sought a limited exclusion order and a cease and desist order halting the importation and sale of infringing products. The ITC instituted the investigation on December 1, 2015. On December 23, 2016, the Company filed a motion to terminate the investigation, and the ITC terminated the investigation on February 1, 2017.

On December 8, 2017, the parties announced the global settlement of all of the outstanding civil litigation on confidential terms. Each of the pending cases has been dismissed with prejudice.

On August 12, 2016, the Company was notified by Jawbone that Jawbone had received a confidential subpoena from the U.S. Attorney's Office for the Northern District of California requesting certain of the Company's confidential business information that appeared to be related to Jawbone's allegations of trade secret misappropriation. On February 17, 2017, the Company received a subpoena for documents from the same office. On February 1, 2018, the Company received a second subpoena for documents. The Company is cooperating with the U.S. Attorney's Office. On June 14, 2018, the six former Jawbone employees who were named as individual defendants in the state trade secret case were charged in a federal indictment with being in possession of certain Jawbone trade secrets.

Sleep Tracking . On May 8, 2015, a purported class action lawsuit was filed against the Company in the U.S. District Court for the Northern District of California, alleging that the sleep tracking function available in certain trackers does not perform as advertised. Plaintiffs seek class certification, restitution, an award of unspecified compensatory and punitive damages, an award of reasonable costs and expenses, including attorneys' fees, and other further relief as the Court may deem just and proper. On January 31, 2017, plaintiffs filed a motion for class certification. Plaintiffs' motion for class certification was granted on November 20, 2017. On April 20, 2017, the Company filed a motion for summary judgment. The Company's motion for summary judgment was denied on December 8, 2017. During the three months ended June 30, 2018, the parties agreed to a settlement and on August 1, 2018, the plaintiffs filed a motion for preliminary approval of the class action settlement. On September 13, 2018, the court held a hearing and denied preliminary settlement approval without prejudice and ordered revised settlement papers be filed by October 26, 2018.

Heart Rate Tracking. On January 6, 2016 and February 16, 2016, two purported class action lawsuits were filed against the Company in the U.S. District Court for the Northern District of California, alleging that the PurePulse® heart rate tracking technology does not consistently and accurately record users' heart rates. Plaintiffs allege common law claims, as well as violations of various states' false advertising, unfair competition, and consumer protection statutes, and seek class certification, injunctive and declaratory relief, restitution, an award of unspecified compensatory damages, exemplary damages, punitive damages, and statutory penalties and damages, an award of reasonable costs and expenses, including attorneys' fees, and other further relief as the Court may deem just and proper. On April 15, 2016, the plaintiffs filed a Consolidated Master Class Action Complaint and, on May 19, 2016, filed an Amended Consolidated Master Class Action Complaint. On January 9, 2017, the Company filed a motion to compel arbitration. On October 11, 2017, the Court granted the motion to compel arbitration. Plaintiffs filed a motion for reconsideration, and that motion was denied on January 24, 2018.

On February 20, 2018, plaintiffs filed a Second Amended Consolidated Master Class Action Complaint ("SAC") on behalf of plaintiff Rob Dunn, the only plaintiff not ordered to arbitration, as a purported class action. The SAC alleges the same common law claims, as well as violations of false advertising, unfair competition, and consumer protection statutes of California and Arizona, and also seeks class certification, injunctive and declaratory relief, restitution, an award of unspecified compensatory damages, exemplary damages, punitive damages, and statutory penalties and damages, an award of reasonable costs and expenses, including attorneys' fees, and other further relief as the Court may deem just and proper. On March 13, 2018, the Company filed a motion to dismiss for failure to state a claim and separately moved to strike the class allegations. The Court dismissed the claims for revocation of acceptance, violation of California's Song-Beverly Consumer Warranty Act, and unjust enrichment, and allowed the remaining claims pending amendment to the complaint with further details. Plaintiff filed a Third Amended Complaint on June 19, 2018. The Court granted the motion to strike and ordered the plaintiff to amend to make clear that he is seeking to represent a class of opt-outs only, but that plaintiff would be free to amend in the event Fitbit's arbitration agreement was found to be unenforceable.

In response to an April 3, 2018 arbitration demand from Kate McLellan, one of the original plaintiffs who was compelled to arbitration, the Company attempted to resolve the individual claim with Ms. McLellan. At the May 31, 2018 hearing, the Court expressed concern that the Company was "picking off" McLellan and thereby undermining the arbitration option and the Court's prior order on arbitration, and ordered additional briefing. On July 24, 2018, the Court awarded the plaintiffs their attorneys' fees on the motion practice, but denied plaintiffs' request that the arbitration right should be waived as a sanction. The parties are moving forward in private arbitration with Ms. McLellan.

The Company believes that the plaintiffs' allegations are without merit, and intends to vigorously defend against the claims. Because the Company is in the early stages of this litigation matter, the Company is unable to estimate a reasonably possible loss or range of loss, if any, that may result from this matter.

Securities Litigation. On January 11, 2016, a putative securities class action was filed in the U.S. District Court for the Northern District of California naming as defendants the Company, certain of its officers and directors, and the underwriters of the Company's initial public offering (the "IPO"). On May 10, 2016, the Court appointed the Fitbit Investor Group (consisting of five individual investors) as lead plaintiff, and an Amended Complaint was filed on July 1, 2016. Plaintiffs allege violations of the Securities Act of 1933, as amended (the "Securities Act"), and the Securities Exchange Act of 1934, as amended, based on alleged materially false and misleading statements about the Company's products between October 27, 2014 and November 23, 2015. Plaintiffs seek to represent a class of persons who purchased or otherwise acquired the Company's securities (i) on the open market between June 18, 2015 and May 19, 2016; and/or (ii) pursuant to or traceable to the IPO. Plaintiffs seek class certification, an award of unspecified compensatory damages, an award of reasonable costs and expenses, including attorneys' fees, and other further relief as the Court may deem just and proper. On July 29, 2016, the Company filed a motion to dismiss. The court denied the motion on October 26, 2016. On April 26, 2017, the Company filed a motion for summary judgment, which is still pending.

On April 28, 2016, a putative class action lawsuit alleging violations of the Securities Act was filed in the Superior Court of California, County of San Mateo, naming as defendants the Company, certain of its officers and directors, the underwriters of the IPO, and a number of its investors. Plaintiffs allege that the IPO registration statement contained material misstatements about the Company's products. Plaintiffs seek to represent a class of persons who purchased the Company's common stock in and/or traceable to the IPO and/or the November 2015 follow-on public offering (the "Secondary Offering"). Plaintiffs seek class certification, an award of unspecified compensatory damages, an award of reasonable costs and expenses, including attorneys' fees, and other further relief as the Court may deem just and proper. On May 17, 2016, a similar class action lawsuit was filed in the Superior Court of California, County of San Francisco. The cases have now been consolidated in the County of San Francisco. On April 7, 2017, the Court granted a motion to dismiss the Section 11 claim based on the Secondary Offering and stayed the cases.

On January 8, 2018, the plaintiffs in the federal and class action cases filed their motion for preliminary approval of settlement of the putative federal and state class actions for $33.3 million , which the Company accrued for as of December 31, 2017. On January 19, 2018, the court entered an order preliminarily approving the proposed settlement, and on April 20, 2018, the court approved the final settlement. The federal and class action cases have been dismissed with prejudice.

On November 11, 2016, a derivative lawsuit was filed in the U.S. District Court for the Northern District of California derivatively on behalf of the Company naming as defendants certain of its officers and directors and as a nominal plaintiff the Company. The plaintiffs allege breach of fiduciary duty, unjust enrichment, section 14(a), and misappropriation based on the same set of alleged facts in the federal and state securities class action litigation. On February 2, 2017, a second derivative lawsuit was filed in the U.S. District Court for the District of Delaware on the same allegations and also including claims for abuse of control, gross mismanagement, and waste. On June 27, 2017, another derivative law suit was filed in the U.S. District Court for the Northern District of California on the same allegations. The Courts have ordered a stay in all three cases.

On June 1, 2017 and June 9, 2017, two additional derivative lawsuits were filed in the Delaware Court of Chancery. Plaintiffs allege breach of fiduciary duty and insider trading against certain defendants who sold shares in the IPO and/or the Secondary Offering. On August 3, 2017, another derivative lawsuit was filed in the Delaware Court of Chancery on the same allegations. There is temporary stay in all three cases. On March 15, 2018, the three derivative lawsuits were consolidated and a Second Amended Complaint was filed on the same allegations of the individual complaints, alleging the same claims, and seeking the same remedy. On April 26, 2017, the Company filed a motion to dismiss for failure to state a claim. The hearing on the motion was held on September 6, 2018.

On October 31, 2017, a seventh derivative lawsuit was filed in the Superior Court of California, Country of San Francisco, on the same allegations. The Company has not yet been served in that case.

On June 27, 2017, an individual investor lawsuit alleging violations of the Securities Act and state law claims for statutory fraud and unfair business practice was filed in the Superior Court of California, County of Alameda, naming as defendants the Company and certain of its officers. The allegations are based on the same set of alleged facts in the federal and state securities class action litigation. The individual case was resolved at a June 13, 2018 mediation.

The Company believes that the plaintiffs' allegations in the derivative actions and individual action are without merit, and intends to vigorously defend against the claims. Because the Company is in the early stages of these litigation matters, the Company is unable to estimate a reasonably possible loss or range of loss, if any, that may result from these matters.

Immersion. On July 10, 2017, Immersion Corporation filed a lawsuit against the Company in the U.S. District Court for the Northern District of California, alleging that certain Fitbit devices infringe on U.S. Patent Nos. 8,059,105, 8,351,299, and 8,638,301. On October 5, 2017, the Company filed a motion to dismiss on grounds the patents are not eligible subject matter for patents. On March 5, 2018, the Court granted in part and denied in part, granting as to the '301 patent, but denying as to the other two patents.

On July 10, 2017, Immersion Corporation also filed a lawsuit against the Company in the Shanghai Intellectual Property Court, alleging infringement of three Immersion Chinese patents. In addition to the Company, Immersion named Runtong, one of the Company's former distributors in China. On August 23, 2017, two additional defendants were added, Fitbit Shanghai and Rkylin, a current distributor in China. In December 2017, the Company filed petitions to invalidate the patents. The invalidation proceedings as to all three patents were instituted. Hearings on two of the patents were held on April 16, 2018 and April 26, 2018; the third was scheduled for May 30, 2018.

On July 8, 2018, the parties entered into a settlement agreement resolving the litigation globally. The cases have been dismissed with prejudice.

Other. The Company is and, from time to time, may in the future become, involved in other legal proceedings in the ordinary course of business. The Company currently believes that the outcome of any of these existing legal proceedings, including the aforementioned cases, either individually or in the aggregate, will not have a material impact on the operating results, financial condition or cash flows of the Company. With respect to existing legal proceedings, the Company has either determined that the existence of a material loss is not reasonably possible or that it is unable to estimate a reasonably possible loss or range of loss. The Company may incur substantial legal fees, which are expensed as incurred, in defending against these legal proceedings.

Indemnification

In the ordinary course of business, the Company enters into commercial agreements that may include indemnification provisions. Pursuant to such agreements, the Company may indemnify, hold harmless and defend an indemnified party for losses suffered or incurred by the indemnified party. Some of the provisions will limit losses to those arising from third-party actions. In some cases, the indemnification will continue after the termination of the agreement. The maximum potential amount of future payments the Company could be required to make under these provisions is not determinable. To date, the Company has not incurred material costs to defend lawsuits or settle claims related to these indemnification provisions. The Company has also entered into indemnification agreements with its directors and officers that may require the Company to indemnify its directors and officers against liabilities that may arise by reason of their status or service as directors or officers to the fullest extent permitted by Delaware corporate law. The Company also currently has directors' and officers' insurance.

7. Stockholders' Equity

Stock Option Exchange

On April 13, 2017, the Company filed its definitive proxy statement and submitted to stockholders a proposal for a stock option exchange program (the "Program"). The Program allowed the Company employees, including its executive officers other than its President, Chief Executive Officer, and Chairman, Chief Technology Officer, and Chief Financial Officer ("Eligible Employees"), to exchange out-of-the-money or "underwater" options to purchase shares of the Company's Class A common stock or Class B common stock currently held by such Eligible Employees for a lesser number of restricted stock units ("RSUs") that may be settled for shares of its Class A common stock, ("New RSUs"), under the Company's 2015 Equity Incentive Plan (the "2015 Plan"). Each New RSU represented an unfunded right to receive one share of the Company's Class A common stock on a date in the future, which generally is the date on which the New RSU will vest. Eligible Employees participating in the Program received one New RSU for every two "out-of-the-money" options that they exchanged. The New RSUs would generally vest over the remaining vesting period of the exchanged option (subject to a one -year minimum vesting period). None of the members of the Company's board of directors were eligible to participate in the Program. On May 25, 2017, the Company's stockholders approved the Program at the 2017 Annual Meeting of Stockholders. The Company subsequently commenced the Program by filing a tender offer statement on Schedule TO with the SEC on June 21, 2017. The Program expired on July 19, 2017. A total of 3.7 million "underwater" stock options were tendered by the Eligible Employees, representing approximately 85% of the stock options eligible for exchange. On July 20, 2017, the Company granted an aggregate of 1.8 million New RSUs under the 2015 Plan in exchange for the "underwater" stock options tendered. The completion of the Program resulted in total incremental unrecognized stock-based compensation expense of $8.5 million , to be recognized over the greater of one year or the remaining vesting service period of the tendered stock options.

Equity Incentive Plans

In May 2015, the Company's board of directors and stockholders adopted and approved the 2015 Plan. The 2015 Plan became effective on June 16, 2015 and serves as the successor to the Amended and Restated 2007 Stock Plan (the "2007 Plan"). The Company ceased granting awards under the 2007 Plan, and any outstanding stock options and RSUs granted under the 2007 Plan would remain subject to the terms of the 2007 Plan. As of September 29, 2018 , 18.3 million shares of Class A common stock were reserved and available for future issuance under the 2015 Plan.

Stock Options

Stock option activity under the equity incentive plans was as follows (in thousands, except per share amounts):

	Stock Options Outstanding		
	Number of Shares Subject to Stock Options	Weighted–Average Exercise Price	Aggregate Intrinsic Value [1]
Balance—December 31, 2017	21,386	$ 3.01	
Granted	—	—	
Exercised	(2,339)	2.33	
Forfeited or canceled	(582)	7.05	
Balance—September 29, 2018	18,465	2.97	$ 50,236
Stock options vested and expected to vest—September 29, 2018	18,455	2.97	50,219
Stock options exercisable—September 29, 2018	16,758	2.72	48,539

[1] The aggregate intrinsic values of stock options outstanding, exercisable, vested and expected to vest as of September 29, 2018 were calculated as the difference between the exercise price of the stock options and the fair value of the Class A common stock of $5.35 as of September 29, 2018 .

Restricted Stock Units

RSU activity under the equity incentive plans was as follows (in thousands, except per share amounts):

	RSUs Outstanding	Weighted-Average Grant Date Fair Value
Unvested balance—December 31, 2017	19,188	$ 9.13
Granted	13,709	5.11
Vested	(7,806)	8.42
Forfeited or canceled	(4,389)	8.07
Unvested balance—September 29, 2018	20,702	$ 6.96

On May 4, 2018, the Company issued 0.8 million shares of market-based awards that vest based upon the achievement of a specified stock price. Market conditions were factored into the grant date fair value using a Monte Carlo valuation model, which utilized multiple input variables to determine the probability of the Company achieving the specified stock price targets. Stock-based compensation expense related to these awards will be recognized over the requisite service period regardless of whether the market condition is satisfied, provided that the requisite service period has been completed.

Employee Stock Purchase Plan

In May 2015, the Company's board of directors adopted the 2015 Employee Stock Purchase Plan (the "2015 ESPP"), which became effective on June 17, 2015. A total of 3.8 million shares of Class A common stock were initially reserved for issuance under the 2015 ESPP. The 2015 ESPP allows eligible employees to purchase shares of the Company's Class A common stock through payroll deductions at a price per share equal to 85% of the lesser of the fair market value of the Company's Class A common stock (i) on the first trading day of the applicable offering period and (ii) the last trading day of each purchase period in the applicable offering period. Except for the initial offering period, the 2015 ESPP provides for 6-month offering periods beginning in May and November of each year.

Warrant

On July 10, 2017, the Company issued a warrant to purchase 0.5 million shares of Class A common stock. The warrant is exercisable based on service and performance-based conditions and has an exercise price of $5.23 per share and a contractual term of ten years. As of September 29, 2018 , 0.5 million warrants were outstanding.

Stock-Based Compensation Expense

Total stock-based compensation expense recognized was as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
Cost of revenue	$ 1,999	$ 1,379	$ 5,129	$ 2,889
Research and development	14,097	12,947	43,858	40,280
Sales and marketing	3,638	3,679	10,996	11,301
General and administrative	4,381	4,792	13,630	12,786
Total stock-based compensation expense	$ 24,115	$ 22,797	$ 73,613	$ 67,256

As of September 29, 2018 , the total unrecognized stock-based compensation expense related to unvested stock options and RSUs was $134.0 million , which the Company expects to recognize over an estimated weighted average period of 2.0 years.

8. Income Taxes

The Company is subject to income tax in the United States as well as other tax jurisdictions in which it conducts business. Earnings from non-U.S. activities are subject to local country income tax.

For the three and nine months ended September 29, 2018 , the Company recorded an expense (benefit) for income taxes of $(18.8) million and $4.2 million , respectively, for an effective tax rate of 90.2% and (2.1)% , respectively. The effective tax rate for the nine months ended September 29, 2018 , was different than the statutory federal tax rate primarily due to the impact of a full valuation allowance on the Company's U.S. deferred tax assets, the mix of income/losses between its foreign jurisdictions, and pretax losses in jurisdictions for which no tax benefit will be recognized. Included in this tax amount was a discrete tax benefit of $4.0 million in connection with a fixed assets depreciation tax method change filed with the 2017 income tax return.

On December 22, 2017, the U.S. Tax Cuts and Jobs Act of 2017 ("2017 Tax Act") was signed into law and includes several key tax provisions that affected the Company, including a reduction of the statutory corporate tax rate from 35% to 21% effective for tax years beginning after December 31, 2017, elimination of the carryback of net operating losses generated after December 31, 2017, and changes to how the United States imposes income tax on multinational corporations, among others.

In December 2017, Staff Accounting Bulletin No. 118 ("SAB 118") was issued to address U.S. GAAP application when a registrant does not have the necessary information available, prepared, or analyzed (including computations) in reasonable detail to complete the accounting for certain income tax effects by the 2017 Tax Act. For the nine months ended September 29, 2018 , no changes have been made to the provisional amounts previously recorded. The Company is still finalizing certain provisional amounts and will complete its analysis within the measurement period in accordance with SAB 118.

On July 24, 2018, the Ninth Circuit Court of Appeals issued an opinion in Altera Corp. v. Commissioner requiring related parties in an intercompany cost-sharing arrangement to share expenses related to share-based compensation. This opinion reversed the prior decision of the United States Tax Court. On August 7, 2018, the court withdrew the opinion issued on July 24, 2018 to allow time for a reconstituted panel of judges to confer. The Company will continue to monitor this case.

For the three and nine months ended September 30, 2017 , the Company recorded an expense for income taxes of $86.2 million and $51.9 million , respectively, for an effective tax rate of (317.3)% and (28.8)% , respectively. The effective tax rate for the nine months ended September 30, 2017 was different than the statutory federal tax rate primarily due to the impact of a valuation allowance recorded against U.S. deferred tax assets, and the mix of income between United States and foreign jurisdictions.

The Company accounts for deferred taxes under ASC Topic 740, "Income Taxes" ("ASC 740"), which involves weighing positive and negative evidence concerning the realizability of the Company's deferred tax assets in each jurisdiction. In evaluating its ability to realize the net deferred tax assets, the Company considered all available positive and negative evidence, including its past operating results and the forecast of future market growth, forecasted earnings, future taxable income, and prudent and feasible tax planning strategies. As of September 29, 2018 , the Company maintained a full valuation allowance against all its U.S. deferred tax assets. No valuation allowance has been recorded against the Company's foreign deferred tax assets. The Company will continue to assess the realizability of its deferred tax assets in each of the applicable jurisdictions going forward.

As of September 29, 2018 , the total amount of gross unrecognized tax benefits was $38.8 million , of which $25.9 million would affect the effective tax rate if recognized. The Company does not have any tax positions as of September 29, 2018 for which it is reasonably possible that the total amount of gross unrecognized tax benefits will increase or decrease within the following 12 months .

9. Net Loss per Share

The following table sets forth the computation of the Company's basic and diluted net loss per share (in thousands, except per share amounts):

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
Numerator:				
Net loss	$ (2,056)	$ (113,403)	$ (201,201)	$ (231,722)
Denominator:				
Weighted-average shares of common stock—basic for Class A and Class B	245,838	234,242	242,746	230,918
Effect of dilutive securities	—	—	—	—
Weighted-average shares of common stock—diluted for Class A and Class B	245,838	234,242	242,746	230,918
Net loss per share:				
Basic	$ (0.01)	$ (0.48)	$ (0.83)	$ (1.00)
Diluted	$ (0.01)	$ (0.48)	$ (0.83)	$ (1.00)

The following potentially dilutive common shares were excluded from the computation of diluted net loss per share for the periods presented because including them would have been anti-dilutive (in thousands):

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
Stock options to purchase common stock	11,982	14,768	12,150	18,874
RSUs	8,123	9,791	8,607	10,235
Warrant	230	411	230	137
Diluted impact of ESPP	191	73	177	125
Diluted common stock subject to vesting	—	100	—	113
Total	20,526	25,143	21,164	29,484

10. Significant Customer Information and Other Information

Retailer and Distributor Concentration

Retailers and distributors with revenue equal to or greater than 10% of total revenue for the three and nine months ended September 29, 2018 and September 30, 2017 were as follows:

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
D	13%	12%	*	*
C	12	17	10%	14%
G	10	*	*	*

* Represents less than 10%.

Retailers and distributors that accounted for equal to or greater than 10% of accounts receivable at September 29, 2018 and December 31, 2017 were as follows:

	September 29, 2018	December 31, 2017
G	13%	*
D	13	*
C	12	17%
B	*	13
E	*	11

* Represents less than 10%.

Geographic and Other Information

Revenue by geographic region, based on ship-to destinations, was as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
United States	$ 230,171	$ 244,204	$ 552,118	$ 613,825
Americas excluding United States	24,799	25,276	56,737	69,656
Europe, Middle East, and Africa	104,186	88,672	234,693	285,045
APAC	34,419	34,370	97,236	76,237
Total	$ 393,575	$ 392,522	$ 940,784	$ 1,044,763

As of September 29, 2018 and December 31, 2017, long-lived assets, which represent property and equipment, located outside the United States were $34.7 million and $30.0 million , respectively.

11. Acquisitions

2018 Acquisition

In February 2018, the Company completed a purchase of Twine Health, Inc., a privately-held company, which was accounted for as a business combination, for total purchase price consideration of $16.7 million , of which $5.4 million was allocated to developed technology intangible assets, $3.8 million to customer relationships intangible asset, $10.0 million to goodwill, $1.8 million to deferred tax liabilities, $0.2 million to deferred revenue, and $0.6 million to net assumed liabilities. The allocation of the purchase price consideration is provisional and the Company will complete its analysis within the measurement period pursuant to Topic 805, with any adjustments being recorded to goodwill. Approximately $2.6 million of the consideration payable to Twine Health, Inc. was held as partial security for certain indemnification obligations, and will be held back for payment until August 2019. The acquisition is expected to extend the Company's reach into healthcare and lay the foundation to expand its offerings to health plans, health systems and self-insured employers, while creating opportunities to increase subscription-based revenue. The amortization period of the acquired developed technology and customer relationships are approximately four and seven years, respectively. Goodwill is not deductible for tax purposes.

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

As discussed in the section titled "Note About Forward-Looking Statements," the following discussion and analysis contains forward-looking statements that involve risks and uncertainties, as well as assumptions that, if they never materialize or prove incorrect, could cause our results to differ materially from those expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified below, and those discussed in the section titled "Risk Factors" included under Part II, Item 1A below.

Overview

Our mission is to help people achieve positive health, wellness, and fitness outcomes by empowering them with intelligent insights, personalized guidance, and the motivation to reach their goals.

Fitbit is a technology company focused on delivering health solutions that impact health outcomes. The Fitbit platform combines wearable devices with software and services to give our users tools to help them reach their health and fitness goals, augmented by general purpose features that add further utility and drive user engagement. Our wearable devices, which include health and fitness trackers and smartwatches, enable our users to view data about their daily activity, exercise and sleep in real-time. Our software and services, which include an online dashboard and mobile app, provide our users with data analytics, motivational and social tools, and virtual coaching through customized fitness plans and interactive workouts. In addition, our software and services drive user engagement and can be leveraged to provide personalized insights. Together, our devices, services, and software have helped millions of users on their health and fitness journeys be more active, sleep better, eat smarter, and manage their weight. Fitbit appeals to a wide spectrum of consumers by addressing key health and fitness needs with advanced technology embedded in simple-to-use products and services.

We generate substantially all of our revenue from sales of our wearable devices which includes both connected health and fitness devices and smartwatches. We sell our products in over 39,000 retail stores and in 86 countries, through our retailers' websites, through our online store at Fitbit.com, and as part of our corporate wellness offering.

We started shipping the following product during the third quarter of 2018:

- ***Fitbit Charge 3*** is the latest health and fitness tracker in our Charge family of devices. Fitbit Charge 3 offers a swim-proof design with a touchscreen display and an advanced health and fitness experience that includes features like goal-based exercise modes, female health tracking, automatic sleep insights and up to seven days of battery life. We began shipping Fitbit Charge 3 in September 2018.

The following are financial highlights for the three and nine months ended September 29, 2018 and September 30, 2017 (in thousands):

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
Revenue	$ 393,575	$ 392,522	$ 940,784	$ 1,044,763
Net loss	$ (2,056)	$ (113,403)	$ (201,201)	$ (231,722)
Adjusted EBITDA	$ 21,037	$ 5,853	$ (80,989)	$ (74,622)
Devices sold	3,539	3,624	8,372	9,952

See the section titled "Key Business Metrics" for additional information regarding devices sold and adjusted EBITDA, including a reconciliation of adjusted EBITDA to net loss.

Key Business Metrics

In addition to the measures presented in our condensed consolidated financial statements, we use the following key metrics to evaluate our business, measure our performance, develop financial forecasts, and make strategic decisions.

Devices Sold

Devices sold represents the number of wearable devices that are sold during a period, net of expected returns. Devices sold does not include sales of accessories. Growth rates between devices sold and revenue are not necessarily correlated because our revenue is affected by other variables, such as the types of products sold during the period, the introduction of new product offerings with differing U.S. manufacturer's suggested retail prices, or MSRPs, and sales of accessories and premium services.

Activations - Repeat and Re-Activated Users

We define an "Activation" as the first instance of a Fitbit device (excluding Aria, Aria 2, Flyer and other accessories) pairing to a user account during the three months prior to the date of measurement. A "Repeat User" is defined as a Fitbit user who activated a Fitbit device to his or her account during the measurement period and activated a different Fitbit device to his or her account during a prior period. A "Re-Activated User" is defined as Repeat User who has not synced his or her prior device and taken at least 100 steps for 90 days or more prior to the measurement period with such device. In the three and nine months ended September 29, 2018 , 42.3% and 38.8%, respectively, of Activations came from Repeat Users, with Re-Activated Users representing 49.2% and 49.8%, respectively, of those Repeat Users. In the three and nine months ended September 30, 2017 , 42.1% and 38.5%, respectively, of Activations came from Repeat Users, with Re-Activated Users representing 38.7% and 39.4%, respectively, of those Repeat Users. The number of Activations from Repeat Users and the number of Re-Activated Users for any period is measured promptly after the measurement period and is not updated.

We believe that the Activations metric is a potential indicator of repeat purchase behavior but not a guarantee of repeat purchase behavior. Actual repeat purchase behavior may depend on a number of factors, including but not limited to our ability to anticipate and satisfy consumer preferences.

Adjusted EBITDA

To supplement our condensed consolidated financial statements presented in accordance with generally accepted accounting principles in the United States, or U.S. GAAP, we monitor and consider adjusted EBITDA, which is a non-GAAP financial measure. This non-GAAP financial measure is not based on any standardized methodology prescribed by U.S. GAAP and is not necessarily comparable to similarly titled measures presented by other companies.

We define adjusted EBITDA as net loss adjusted to exclude stock-based compensation expense, depreciation, intangible assets amortization, litigation expense (credit) related to matters with Aliphcom, Inc. d/b/a Jawbone, or Jawbone, the impact of our restructuring in 2017, impairment of equity investment, interest income, net, and income tax benefit.

We use adjusted EBITDA to evaluate our operating performance and trends and make planning decisions. We believe that adjusted EBITDA helps identify underlying trends in our business that could otherwise be masked by the effect of the expenses and other items that we exclude in adjusted EBITDA. In particular, the exclusion of the effect of stock-based compensation expense and certain expenses in calculating adjusted EBITDA can provide a useful measure for period-to-period comparisons of our business. Accordingly, we believe that adjusted EBITDA provides useful information to investors and others in understanding and evaluating our operating results, enhancing the overall understanding of our past performance and future prospects, and allowing for greater transparency with respect to a key financial metric used by our management in its financial and operational decision-making.

Adjusted EBITDA is not prepared in accordance with U.S. GAAP, and should not be considered in isolation of, or as an alternative to, measures prepared in accordance with U.S. GAAP. There are a number of limitations related to the use of this non-GAAP financial measure rather than net loss, which is the nearest U.S. GAAP equivalent of adjusted EBITDA. For example, adjusted EBITDA excludes stock-based compensation expense, which has been, and will continue to be for the foreseeable future, a significant recurring expense for our business and an important part of our compensation strategy. Accordingly, adjusted EBITDA should be considered along with other operating and financial performance measures presented in accordance with U.S. GAAP.

The following table presents a reconciliation of net loss to adjusted EBITDA (in thousands):

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
Net loss	$ (2,056)	$ (113,403)	$ (201,201)	$ (231,722)
Stock-based compensation expense [(1)]	24,115	22,797	73,613	66,528
Litigation expense	—	874	765	2,293
Restructuring	—	—	—	6,375
Impairment of equity investment	6,000	—	6,000	—
Depreciation and intangible assets amortization	13,877	10,520	41,254	32,472
Interest income, net	(2,072)	(1,162)	(5,599)	(2,451)
Income tax expense (benefit)	(18,827)	86,227	4,179	51,883
Adjusted EBITDA	$ 21,037	$ 5,853	$ (80,989)	$ (74,622)

[(1)] A portion of stock-based compensation expense for the nine months ended September 30, 2017 was allocated to and included in "Restructuring," thus explaining the difference between the total in this table compared to the amount in the Stock-Based Compensation Expense table presented within Operating Results below.

Non-GAAP free cash flow

We define non-GAAP free cash flow as net cash provided by operating activities less purchase of property and equipment. We consider free cash flow to be a liquidity measure that provides useful information to management and investors about the amount of cash generated by the business that can possibly be used for investing in our business and strengthening our balance sheet, but it is not intended to represent the residual cash flow available for discretionary expenditures. Non-GAAP free cash flow is not prepared in accordance with U.S. GAAP, and should not be considered in isolation of, or as an alternative to, measures prepared in accordance with U.S. GAAP.

The following table presents a reconciliation of net cash provided by (used in) operating activities to non-GAAP free cash flow (in thousands):

	Nine Months Ended	
	September 29, 2018	September 30, 2017
Net cash provided by operating activities	$ 1,524	$ 8,718
Purchase of property and equipment	(40,174)	(58,199)
Non-GAAP free cash flow	$ (38,650)	$ (49,481)
Net cash provided by (used in) investing activities	$ 63,537	$ (32,913)
Net cash provided by (used in) financing activities	$ (4,790)	$ 3,089

Components of our Operating Results

Revenue

We generate substantially all of our revenue from the sale of our wearable devices, which includes both connected health and fitness devices and accessories and smartwatches. We also generate a small portion of our revenue from our subscription-based Fitbit Coach services and from our corporate wellness programs.

Cost of Revenue

Cost of revenue consists of product costs, including costs of contract manufacturers for production, shipping and handling costs, warranty replacement costs, packaging, fulfillment costs, manufacturing and tooling equipment depreciation, warehousing costs, write-downs of excess and obsolete inventory, amortization of developed technology intangible assets acquired, and certain allocated costs related to management, facilities, and personnel-related expenses and other expenses associated with supply chain logistics. Personnel-related expenses include salaries, bonuses, benefits, and stock-based compensation.

Operating Expenses

Operating expenses consist of research and development, sales and marketing, and general and administrative expenses.

Research and Development . Research and development expenses consist primarily of personnel-related expenses, consulting and contractor expenses, tooling and prototype materials, and allocated overhead costs.

Substantially all of our research and development expenses are related to developing new products and services and improving our existing products and services. To date, research and development expenses have been expensed as incurred, because the release of products and services for sale has been short and development costs qualifying for capitalization have been insignificant.

Sales and Marketing. Sales and marketing expenses represent a significant component of our operating expenses and consist primarily of advertising and marketing promotions of our products and services and personnel-related expenses, as well as sales incentives, trade show and event costs, sponsorship costs, consulting and contractor expenses, travel, point-of-purchase display expenses and related amortization, and allocated overhead costs.

General and Administrative . General and administrative expenses consist of personnel-related expenses for our finance, legal, human resources, and administrative personnel, as well as the costs of professional services, allocated overhead, information technology, bad debt expense, amortization of intangible assets acquired, and other administrative expenses.

Interest Income, Net

Interest income, net consists of interest expense associated with our debt financing arrangements, amortization of debt issuance costs, and interest income earned on our cash, cash equivalents, and marketable securities.

Other Income (Expense), Net

Other income, net consists of foreign currency gains and losses, and impairment loss from an equity investment.

Income Tax Expense (Benefit)

We are subject to income taxes in the United States and foreign jurisdictions in which we do business. These foreign jurisdictions have statutory tax rates different from those in the United States. Accordingly, our effective tax rates will vary depending on the relative proportion of foreign to U.S. income, the utilization of foreign tax credits, and changes in tax laws.

On July 24, 2018, the Ninth Circuit Court of Appeals issued an opinion in Altera Corp. v. Commissioner requiring related parties in an intercompany cost-sharing arrangement to share expenses related to share-based compensation. This opinion reversed the prior decision of the United States Tax Court. On August 7, 2018, the Court withdrew the opinion issued on July 24, 2018 to allow time for a reconstituted panel of judges to confer. We will continue to monitor the case.

On December 22, 2017, the U.S. Tax Cuts and Jobs Act of 2017, or the 2017 Tax Act, was signed into law and includes several key tax provisions that affected us, including a reduction of the statutory corporate tax rate from 35% to 21% effective for tax years beginning after December 31, 2017, elimination of certain deductions, and changes to how the United States imposes income tax on multinational corporations, among others. We are required to recognize the effect of tax law changes in the period of enactment, such as re-measuring our U.S. deferred tax assets and liabilities as well as re-assessing the net realizability of our deferred tax assets. In December 2017, the SEC staff issued Staff Accounting Bulletin No. 118, Income Tax Accounting Implications of the Tax Cuts and Jobs Act, or SAB 118, which allows us to record provisional amounts during a measurement period not to extend beyond one year of the enactment date. As we complete our analysis of the 2017 Tax Act, any subsequent adjustments to provisional amounts that we have recorded will be recorded in the period in which the adjustments are made.

Operating Results

The following tables set forth the components of our condensed consolidated statements of operations for each of the periods presented and as a percentage of our revenue for those periods. The period-to-period comparison of operating results is not necessarily indicative of results for future periods (in thousands).

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
Consolidated Statements of Operations Data:				
Revenue	$ 393,575	$ 392,522	$ 940,784	$ 1,044,763
Cost of revenue (1)	240,061	217,762	554,132	602,459
Gross profit	153,514	174,760	386,652	442,304
Operating expenses:				
Research and development (1)	79,840	84,170	256,223	252,471
Sales and marketing (1)	66,676	77,536	239,573	269,442
General and administrative (1)	24,812	40,690	91,111	102,815
Total operating expenses	171,328	202,396	586,907	624,728
Operating loss	(17,814)	(27,636)	(200,255)	(182,424)
Interest income, net	2,072	1,162	5,599	2,451
Other income (expense), net	(5,141)	(702)	(2,366)	134
Loss before income taxes	(20,883)	(27,176)	(197,022)	(179,839)
Income tax expense (benefit)	(18,827)	86,227	4,179	51,883
Net loss	$ (2,056)	$ (113,403)	$ (201,201)	$ (231,722)

(1) Includes stock-based compensation expense as follows (in thousands)

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
Stock-Based Compensation Expense:				
Cost of revenue	$ 1,999	$ 1,379	$ 5,129	$ 2,889
Research and development	14,097	12,947	43,858	40,280
Sales and marketing	3,638	3,679	10,996	11,301
General and administrative	4,381	4,792	13,630	12,786
Total stock-based compensation expense	$ 24,115	$ 22,797	$ 73,613	$ 67,256

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
	(as a percentage of revenue)			
Consolidated Statements of Operations Data:				
Revenue	100 %	100 %	100 %	100 %
Cost of revenue	61	55	59	58
Gross profit	39	45	41	42
Operating expenses:				
Research and development	20	21	27	24
Sales and marketing	17	20	25	26
General and administrative	6	10	10	10
Total operating expenses	43	51	62	60
Operating loss	(4)	(6)	(21)	(18)
Interest income, net	1	—	1	—
Other income (expense), net	(1)	—	—	—
Loss before income taxes	(4)	(6)	(20)	(18)
Income tax expense (benefit)	(5)	24	—	5
Net loss	1 %	(30)%	(20)%	(23)%

Revenue

	Three Months Ended		Change		Nine Months Ended		Change	
(dollars in thousands)	September 29, 2018	September 30, 2017	$	%	September 29, 2018	September 30, 2017	$	%
Revenue	$ 393,575	$ 392,522	$ 1,053	—%	$ 940,784	$ 1,044,763	$ (103,979)	(10)%

Revenue remained relatively flat during the three months ended September 29, 2018 compared to the same period in 2017. Consumers continued to migrate towards our higher-end smartwatches, offset in part by lower demand for our connected health and fitness devices. Revenue from our smartwatches increased to 49% of our revenue in the three months ended September 29, 2018 , compared to 9% of our revenue in the same period in 2017. Total number of devices sold declined by 2%, from 3.6 million in the three months ended September 30, 2017 to 3.5 million in the three months ended September 29, 2018 . The average selling prices of our devices increased by 3%, from $105 for the three months ended September 30, 2017 to $108 for the three months ended September 29, 2018 , primarily due to sales of our recently introduced smartwatches, partially offset by increased promotional activities for our legacy products. Revenue from new product introductions, or NPI, defined as new products shipped in the past 12 months, increased by 95% to $244.9 million, or 62% of revenue, in the three months ended September 29, 2018 , compared to the same period in the prior fiscal year. NPI revenue for the three months ended September 29, 2018 was primarily from Fitbit Versa, our new smartwatch, and Fitbit Charge 3, our latest tracker. Revenue from our direct channel, Fitbit.com, decreased by 34% to $22.1 million, or 6% of revenue, in the three months ended September 29, 2018 , compared to the same period in the prior fiscal year. The decrease in our direct channel revenue was primarily driven by two factors. We did not ship Fitbit Charge 3 in our direct channel during the three months ended September 29, 2018 in order to align with timing of availability at major retailers. In addition, direct channel revenue decreased in part due to a decline in discounted sales derived from customer claims. In response to customer complaints about out of warranty devices, we offer certain customers discounts on new products in lieu of providing replacements. These discounts are generally redeemed through our direct channel. The improved quality of our products has resulted in fewer customer complaints and, as a result, the issuance of fewer discount offers, therefore driving a decrease in direct channel revenue.

Revenue decreased $104.0 million , or 10% , from $1,044.8 million for the nine months ended September 30, 2017 to $940.8 million for the nine months ended September 29, 2018 . The decrease was driven by lower demand for our connected health and fitness devices as consumers continued their migration towards higher-end smartwatches. The decrease was offset in part by increased revenue from our smartwatches, which increased to 46% of our revenue in the nine months ended September 29, 2018 , compared to 4% of our revenue in the same period in 2017. Total number of devices sold declined by 16%, from 10.0 million in the nine months ended September 30, 2017 to 8.4 million in the nine months ended September 29, 2018 . The average selling prices of our devices increased by 8%, from $101 for the nine months ended September 30, 2017 to $108 for the nine months ended

September 29, 2018 , primarily due to our shift towards smartwatches. During the nine months ended September 29, 2018 , we also benefited from $12.4 million in revenue from the release of outstanding product return and rebate reserves related to Wynit Distribution, LLC, or Wynit, a distributor who filed for bankruptcy protection in September 2017, as we believe the possibility of future claims associated with these reserves is remote. NPI revenue decreased by 24% to $503.7 million, or 54% of revenue, in the nine months ended September 29, 2018 , compared to the same period in the prior fiscal year. NPI revenue for the nine months ended September 29, 2018 was primarily from Fitbit Versa and Fitbit Charge 3. Revenue from our direct channel decreased by 19% to $96.4 million, or 10% of revenue, in the nine months ended September 29, 2018 , compared to the same period in the prior fiscal year.

U.S. revenue, based on ship-to destinations, decreased $14.0 million, or 6%, from $244.2 million for the three months ended September 30, 2017 to $230.2 million for the three months ended September 29, 2018 . International revenue, based on ship-to destinations, increased $15.1 million, or 10%, from $148.3 million for the three months ended September 30, 2017 to $163.4 million for the three months ended September 29, 2018 , primarily due to an increase in revenue of 17% in the Europe, Middle East and Africa, or EMEA, region. Our Asia Pacific, or APAC, and Americas excluding the United States regions were relatively flat compared to the same period in the prior fiscal year.

U.S. revenue decreased $61.7 million, or 10%, from $613.8 million for the nine months ended September 30, 2017 to $552.1 million for the nine months ended September 29, 2018 . International revenue decreased $42.3 million, or 10%, from $430.9 million for the nine months ended September 30, 2017 to $388.7 million for the nine months ended September 29, 2018 , primarily due to decreases of 18% in the EMEA region, mainly due to a decline in the United Kingdom primarily due to the lag in its transition to smartwatches and thus was disproportionately exposed to the contraction in connected health and fitness devices, and 19% in the Americas excluding the United States region, offset in part by a 28% increase in the APAC region.

W e expect our revenue to decrease for the full year 2018 compared to the full year 2017 as declines in connected health and fitness device revenue exceed growth from our recent smartwatch introductions.

Cost of Revenue

	Three Months Ended		Change		Nine Months Ended		Change	
(dollars in thousands)	September 29, 2018	September 30, 2017	$	%	September 29, 2018	September 30, 2017	$	%
Cost of revenue	$ 240,061	$ 217,762	$ 22,299	10 %	$ 554,132	$ 602,459	$ (48,327)	(8)%
Gross profit	153,514	174,760	(21,246)	(12)%	386,652	442,304	(55,652)	(13)%
Gross margin	39%	45%			41%	42%		

Cost of revenue increased $22.3 million , or 10% , from $217.8 million for the three months ended September 30, 2017 to $240.1 million for the three months ended September 29, 2018 and decreased $48.3 million , or 8% , from $602.5 million for the nine months ended September 30, 2017 to $554.1 million for the nine months ended September 29, 2018 . The increase during the three months ended September 29, 2018, compared to the same period in 2017, was primarily due to significant product mix shift towards higher cost smartwatches, which increased from 9% of revenue in the three months ended September 30, 2017 to 49% of revenue in the three months ended September 29, 2018, partially offset by lower warranty costs and lower customer support contact rates due to improved quality of our products. The decrease during the nine months ended September 29, 2018, compared to the same period in 2017, was due to decline of 16% in the number of devices sold during the current period and lower warranty costs and lower customer support contact rates due to improved quality of our products, offset in part by product mix shift towards higher cost smartwatches, which increased from 4% of revenue in the nine months ended September 30, 2017 to 46% of revenue in the nine months ended September 29, 2018.

Gross margin decreased from 45% for the three months ended September 30, 2017 to 39% for the three months ended September 29, 2018 primarily due to our product mix shift towards smartwatches which have lower gross margins than our connected health and fitness devices and increased promotional activities associated with legacy products, offset in part by lower warranty costs and lower customer support contact rates due to improved quality of our products.

Gross margin decreased from 42% for the nine months ended September 30, 2017 to 41% for the nine months ended September 29, 2018 primarily due to our product mix shift towards smartwatches which have lower gross margins than our connected health and fitness devices, an increase in promotional activities associated with legacy products, higher production scrap costs due to yield loss at a contract manufacturer, and an increase in accelerated depreciation of manufacturing and tooling equipment, offset in part by lower warranty costs and lower customer support contact rates due to improved quality of our products, the utilization of previously reserved component materials, and the recognition of $12.4 million in revenue due to the release of outstanding product return and rebate reserves related to Wynit described above.

We expect our gross margin to trend lower in 2018 compared to 2017 primarily due to our product mix shift from connected health and fitness devices to smartwatches, offset in part by lower warranty costs.

Research and Development

	Three Months Ended		Change		Nine Months Ended		Change	
(dollars in thousands)	September 29, 2018	September 30, 2017	$	%	September 29, 2018	September 30, 2017	$	%
Research and development	$ 79,840	$ 84,170	$ (4,330)	(5)%	$ 256,223	$ 252,471	$ 3,752	1%

Research and development expenses decreased $4.3 million , or 5% , from $84.2 million for the three months ended September 30, 2017 to $79.8 million for the three months ended September 29, 2018 . The decrease was due to a $2.9 million decrease in consulting and contractor expenses, a $2.0 million decrease in tooling and prototype material costs, and a $2.1 million decrease in allocation of facilities and IT-related expense, offset in part by a $1.3 million increase in third party hosting costs and an increase in personnel-related expenses primarily from a 1% increase in headcount.

Research and development expenses increased $3.8 million , or 1% , from $252.5 million for the nine months ended September 30, 2017 to $256.2 million for the nine months ended September 29, 2018 . The increase was due to a $4.3 million increase in personnel-related expenses primarily from a 6% increase in headcount and a $2.6 million increase in third-party hosting costs, offset in part by a $4.2 million decrease in tooling and prototype material costs.

We expect our research and development expenses for the full year 2018 compared to the full year 2017 to remain relatively constant in absolute dollars and increase as a percentage of revenue.

Sales and Marketing

	Three Months Ended		Change		Nine Months Ended		Change	
(dollars in thousands)	September 29, 2018	September 30, 2017	$	%	September 29, 2018	September 30, 2017	$	%
Sales and marketing	$ 66,676	$ 77,536	$ (10,860)	(14)%	$ 239,573	$ 269,442	$ (29,869)	(11)%

Sales and marketing expenses for the three months ended September 29, 2018 decreased $10.9 million or 14% from $77.5 million for the three months ended September 30, 2017 to $66.7 million for the three months ended September 29, 2018 . During the three months ended September 29, 2018 , we experienced a decrease of $7.0 million in advertising and marketing costs as we aligned our marketing spend to support the launch of our new product offerings, a decrease of $3.4 million in customer support costs due to improved quality and reduced case volume of our products, a decrease of $1.0 million in point-of-purchase display costs due to a reduced number of new displays, offset in part by an increase of $1.4 million in personnel-related expenses due to a 6% increase in headcount.

Sales and marketing expenses decreased $29.9 million , or 11% , from $269.4 million for the nine months ended September 30, 2017 to $239.6 million for the nine months ended September 29, 2018 . The decline was primarily due to an $18.0 million decrease related to marketing activities accounted for as a reduction to revenue instead of sales and marketing expense, an $11.5 million decrease in customer support costs due to improved quality and reduced volume of our products, a $10.7 million decrease in point-of-purchase display costs due to a reduced number of new displays, offset in part by a $5.8 million increase in advertising and marketing costs to support our launch of Fitbit Versa and Fitbit Charge 3, and a $3.9 million increase in personnel-related expenses primarily due to a 6% increase in headcount.

We expect our sales and marketing expenses for the full year 2018 compared to the full year 2017 to decrease in absolute dollars and decrease as a percentage of revenue.

General and Administrative

(dollars in thousands)	Three Months Ended September 29, 2018	Three Months Ended September 30, 2017	Change $	Change %	Nine Months Ended September 29, 2018	Nine Months Ended September 30, 2017	Change $	Change %
General and administrative	$ 24,812	$ 40,690	$ (15,878)	(39)%	$ 91,111	$ 102,815	$ (11,704)	(11)%

General and administrative expenses for the three months ended September 29, 2018 decreased $15.9 million, or 39%, from $40.7 million for the three months ended September 30, 2017 to $24.8 million for the three months ended September 29, 2018. The decrease was primarily due to a $7.6 million decrease in bad debt expense resulting from Wynit's bankruptcy filing, a $4.0 million decrease in legal fees, a $2.2 million decrease in consulting and contractor expense and a decrease in allocated overhead costs, offset in part by an increase in personnel-related expenses primarily due to a 7% increase in headcount.

General and administrative expenses decreased $11.7 million , or 11% , from $102.8 million for the nine months ended September 30, 2017 to $91.1 million for the nine months ended September 29, 2018 . The decrease was primarily due to a $7.6 decrease in bad debt expense resulting from Wynit's bankruptcy filing, a $2.8 million decrease in consulting and contractor expense, a $1.4 million decrease in legal fees, a $1.2 million decrease in other taxes and a decrease in allocated overhead costs, offset in part by a $4.2 million increase in personnel-related expenses primarily due to a 8% increase in headcount.

We expect our general and administrative expenses for the full year 2018 compared to the full year 2017 to decrease in absolute dollars and remain relatively consistent as a percentage of revenue.

Interest and Other Income (Expense), Net

(dollars in thousands)	Three Months Ended September 29, 2018	Three Months Ended September 30, 2017	Change $	Change %	Nine Months Ended September 29, 2018	Nine Months Ended September 30, 2017	Change $	Change %
Interest income, net	$ 2,072	$ 1,162	$ 910	78%	$ 5,599	$ 2,451	$ 3,148	128 %
Other income (expense), net	(5,141)	(702)	(4,439)	632%	(2,366)	134	(2,500)	(1,866)%

Interest income, net increased $0.9 million , from $1.2 million for the three months ended September 30, 2017 to $2.1 million for the three months ended September 29, 2018 , primarily due to higher interest rates earned on cash, cash equivalents and marketable securities. Other income (expense), net decreased primarily due to an impairment loss of $6.0 million from an equity investment, offset in part by an increase in foreign currency gains.

Interest income, net increased $3.1 million , from $2.5 million for the nine months ended September 30, 2017 to $5.6 million for the nine months ended September 29, 2018 , primarily due to higher interest rates earned on cash, cash equivalents and marketable securities. Other income (expense), net decreased primarily due to an impairment loss of $6.0 million from an equity investment, offset in part by an increase in foreign currency gains.

Income Tax Expense (Benefit)

(dollars in thousands)	Three Months Ended September 29, 2018	Three Months Ended September 30, 2017	Change $	Change %	Nine Months Ended September 29, 2018	Nine Months Ended September 30, 2017	Change $	Change %
Income tax expense (benefit)	$ (18,827)	$ 86,227	$ (105,054)	(122)%	$ 4,179	$ 51,883	$ (47,704)	(92)%
Effective tax rate	90.2%	(317.3)%			(2.1)%	(28.8)%		

Income tax benefit increased $105.1 million , from an expense of $86.2 million for the three months ended September 30, 2017 to a benefit of $(18.8) million for the three months ended September 29, 2018 . Our effective tax rate was 90.2% and (317.3)% for the three months ended September 29, 2018 and September 30, 2017 , respectively. The increase in our effective tax rate for the three months ended September 29, 2018 was primarily due to the impact of a full valuation allowance on our U.S. deferred tax assets, and the mix of income/losses between our United States and foreign jurisdictions. Included in this tax amount was a discrete tax benefit of $4.0 million in connection with a fixed assets depreciation tax method change filed with our 2017 income tax return.

Income tax expense decreased $47.7 million , from an expense of $51.9 million for the nine months ended September 30, 2017 to an expense of $4.2 million for the nine months ended September 29, 2018 . Our effective tax rate was (2.1)% and (28.8)% for the nine months ended September 29, 2018 and September 30, 2017 , respectively. The increase in our effective tax rate for the nine months ended September 29, 2018 was primarily due to the impact of a full valuation allowance on our U.S. deferred tax assets, and the mix of income/losses between our United States and foreign jurisdictions. Included in this tax amount was a discrete tax benefit of $4.0 million in connection with a fixed assets depreciation tax method change filed with our 2017 income tax return.

Liquidity and Capital Resources

Our operations have been financed primarily through cash flow from operating activities, the net proceeds from the sale of our equity securities, and letters of credit under our credit facilities. As of September 29, 2018 , we had cash and cash equivalents of $402.2 million and marketable securities of $221.1 million , approximately 86% of which is held in the United States.

Of our total cash, cash equivalents, and marketable securities, $85.0 million is held by our foreign subsidiaries. Our intent is to indefinitely reinvest our earnings from foreign operations and based on our current plans we do not anticipate that we will require funds generated from foreign operations to fund our domestic operations. In the event funds from foreign operations are needed to fund operations in the United States in the future, we may be required to accrue and pay additional taxes on repatriated funds at that time.

We believe our existing cash, cash equivalent, and marketable securities balances, and cash flow from operations, will be sufficient to meet our working capital and capital expenditure needs for at least the next 12 months. Our future capital requirements may vary materially from those currently planned and will depend on many factors, including our levels of revenue, the timing and extent of spending on research and development efforts and other business initiatives, the expansion of sales and marketing activities, the timing of new product introductions, market acceptance of our products, acquisitions, and overall economic conditions. To the extent that current and anticipated future sources of liquidity are insufficient to fund our future business activities and requirements, we may be required to seek additional equity or debt financing. The sale of additional equity would result in additional dilution to our stockholders. The incurrence of debt financing would result in debt service obligations and the instruments governing such debt could provide for operating and financing covenants that would restrict our operations.

Credit Facility

In December 2015, we entered into a second amended and restated credit agreement, or the Senior Facility, with Silicon Valley Bank, or SVB, as administrative agent, collateral agent, and lender, SunTrust Bank as syndication agent, SunTrust Robinson Humphrey, Inc. and several other lenders to replace the then existing asset-based credit facility and cash flow facility. The Senior Facility allowed us to borrow up to $250.0 million, including up to $50.0 million for the issuance of letters of credit and up to $25.0 million for swing line loans, subject to certain financial covenants and ratios. We have the option to repay our borrowings under the Senior Facility without penalty prior to maturity. The Senior Facility requires us to comply with certain financial and non-financial covenants. The Senior Facility contains customary covenants that restrict our ability to, among other things, incur additional indebtedness, sell certain assets, guarantee certain obligations of third parties, declare dividends or make certain distributions, and undergo a merger or consolidation or certain other transactions. Obligations under the Senior Facility are collateralized by substantially all of our assets, excluding our intellectual property.

In May 2017, we entered into a first amendment to the Senior Facility, or the First Amendment, pursuant to which the aggregate amount we can borrow under the Senior Facility was reduced from $250.0 million to $100.0 million, with up to $50.0 million available for the issuance of letters of credit and up to $25.0 million available for swing line loans. In addition, pursuant to the First Amendment, the applicable margin in respect of the interest rates under the Senior Facility was amended to be based on our level of liquidity (defined as the sum of our aggregate cash holdings and the amount available under our revolving commitments) and range from, with respect to Alternate Base Rate loans, 0.5% to 1.0%, and, with respect to LIBOR loans, 1.5% to 2.0%. Among other changes, the First Amendment also removed the fixed charge coverage ratio covenant and the consolidated leverage ratio covenant, and added a general liquidity covenant requiring us to maintain liquidity of at least $200.0 million in unrestricted cash, of which $100.0 million in cash or cash equivalents must be held in accounts subject to control agreements with, and maintained by, SVB or its affiliates.

We were in compliance with the financial covenants under the Senior Facility, as amended, as of September 29, 2018 . As of September 29, 2018 , we had no outstanding borrowings under the Senior Facility, as amended, and had outstanding letters of credit of $36.8 million issued to cover various security deposits on our facility leases.

Cash Flows

The following table summarizes our cash flows for the periods indicated (in thousands):

	Nine Months Ended	
	September 29, 2018	September 30, 2017
Net cash provided by (used in):		
Operating activities	$ 1,524	$ 8,718
Investing activities	63,537	(32,913)
Financing activities	(4,790)	3,089
Net change in cash and cash equivalents	$ 60,271	$ (21,106)

Cash Flows from Operating Activities

Net cash provided from operating activities of $1.5 million for the nine months ended September 29, 2018 was primarily due to a decrease in net change in operating assets and liabilities of $67.7 million, which consisted of a decrease in prepaid expenses and other assets primarily due to the receipt of a $72 million income tax refund, a decrease in account receivables due to the decline in sales offset in part by the shift in presentation of sales returns reserve from within accounts receivable to within accrued liabilities upon adoption of ASU 2014-09 on January 1, 2018, and an increase in accounts payables, offset in part by an increase in inventory primarily related to Fitbit Charge 3 and Fitbit Versa, and a decrease in accrued liabilities as a result of lower operating activity during the current period.

The net change in operating assets and liabilities was also impacted by non-cash adjustments of $135.1 million, primarily resulting from stock-based compensation expense of $73.6 million, depreciation and amortization expense of $41.3 million, provision for inventory obsolescence of $9.0 million, write-off of property and equipment of $7.5 million and impairment loss from an equity investment of $6.0 million, partially offset by a net loss of $201.2 million . Our days sales outstanding in accounts receivable, calculated as the number of days represented by the accounts receivable balance as of period end, decreased from 76 days as of December 31, 2017 to 72 days as of September 29, 2018 due to higher collections during the three months ended September 29, 2018 compared to the fourth quarter of 2017.

Cash Flows from Investing Activities

Net cash provided from investing activities for the nine months ended September 29, 2018 of $63.5 million was primarily due to maturities and sales of marketable securities of $402.3 million, partially offset by purchases of marketable securities of $285.0 million, purchases of property and equipment of $40.2 million and the cash portion of an acquisition of $13.6 million, net of cash acquired.

Cash Flows from Financing Activities

Net cash provided from financing activities for the nine months ended September 29, 2018 was primarily due to $11.6 million in proceeds from exercise of stock options and stock purchases made through our 2015 Employee Stock Purchase Plan, offset by $15.7 million in net cash used for payment of taxes on common stock issued under our employee equity incentive plans.

Contractual Obligations and Other Commitments

Future minimum payments under our operating leases as of the date of this filing was $162.9 million .

The aggregate amount of open purchase orders as of September 29, 2018 was approximately $434.6 million , of which $185.0 million related to our migration to a third-party hosting provider. We cannot determine the aggregate amount of such purchase orders that represent contractual obligations because purchase orders may represent authorizations to purchase rather than binding agreements.

During the normal course of business, we and our contract manufacturers procure components based upon a forecasted production plan. If we cancel all or part of the orders, or materially reduce forecasted orders, in certain circumstances we may be liable to our suppliers and contract manufacturers for the cost of the excess components purchased by our contract manufactures. As of September 29, 2018 , $11.6 million was accrued for such liabilities to contract manufacturers.

We have recorded a liability for uncertain tax positions of $26.4 million as of September 29, 2018 .

Off-Balance Sheet Arrangements

As of September 29, 2018 , we did not have any off-balance sheet arrangements or holdings in variable interest entities.

Critical Accounting Polices and Estimates

Our management's discussion and analysis of our financial condition and results of operations is based on our condensed consolidated financial statements, which have been prepared in accordance with U.S. GAAP. The preparation of these condensed consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, as well as the reported revenue generated and expenses incurred during the reporting periods. Our estimates are based on our historical experience and on various other factors that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

There have been no material changes to our critical accounting policies and estimates from those disclosed in our Annual Report on Form 10-K for the fiscal year ended December 31, 2017 filed with the SEC on March 1, 2018, except for policies related to revenue recognition discussed in Note 1 of the notes to our condensed consolidated financial statements.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

We are exposed to market risks in the ordinary course of our business. These risks primarily include interest rate and foreign currency risks as follows:

Interest Rate Risk

Our exposure to changes in interest rates relates primarily to our investment portfolio. As of September 29, 2018 , we had cash and cash equivalents of $402.2 million and marketable securities of $221.1 million , which consisted primarily of bank deposits, money market funds, U.S. government and agency securities, commercial paper, and corporate notes and bonds. The primary objectives of our investment activities are to preserve principal and provide liquidity without significantly increasing risk. Our investment policy specifies credit quality standards for our investments and limits the amount of credit exposure to any single issue, issuer, or type of investment.

To date, we have not been exposed, nor do we anticipate being exposed, to material risks due to changes in interest rates. A hypothetical 10% change in interest rates during any of the periods presented would not have had a material impact on our condensed consolidated financial statements.

Foreign Currency Risk

To date, all of our inventory purchases have been denominated in U.S. dollars. Our international sales are primarily denominated in foreign currencies and any unfavorable movement in the exchange rate between U.S. dollars and the currencies in which we conduct sales in foreign countries could have an adverse impact on our revenue. A portion of our operating expenses are incurred outside the United States and are denominated in foreign currencies, which are also subject to fluctuations due to changes in foreign currency exchange rates. In addition, our suppliers incur many costs, including labor costs, in other currencies. To the extent that exchange rates move unfavorably for our suppliers, they may seek to pass these additional costs on to us, which could have a material impact on our gross margins. Our operating results and cash flows are, therefore, subject to fluctuations due to changes in foreign currency exchange rates.

To partially mitigate the impact of changes in currency exchange rates on net cash flows from our foreign currency denominated revenue and expenses, we enter into foreign currency exchange forward and option contracts. We also hedge certain monetary assets and liabilities denominated in foreign currencies, which reduces but does not eliminate our exposure to currency fluctuations between the date a transaction is recorded and the date that cash is collected or paid. In general, the market risks of these contracts are offset by corresponding gains and losses on the transactions being hedged.

We had outstanding contracts with a total notional amount of $60.2 million in cash flow hedges for forecasted revenue transactions as of September 29, 2018 . We had outstanding balance sheet hedges with a total notional amount of $146.3 million as of September 29, 2018 . We assessed our exposure to movements in currency exchange rates by performing a sensitivity analysis of adverse changes in exchange rates and the corresponding impact to our results of operations. A hypothetical change of 10% in exchange rates would not have materially affected our operating results.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures . Our management has evaluated, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, the effectiveness of our disclosure controls and procedures (as defined in Rules 13-a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, or the Exchange Act) as of September 29, 2018 . Our disclosure controls and procedures are designed to provide reasonable assurance that the information required to file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure.

Based on this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that as of September 29, 2018 , our disclosure controls and procedures were not effective as a result of the material weakness in our internal control over financial reporting, previously reported in Item 9A of our Annual Report on Form 10-K for the fiscal year ended December 31, 2017, which has not yet been fully remediated.

Notwithstanding the material weakness, management, including our Chief Executive Officer and Chief Financial Officer, believes the condensed consolidated financial statements included in this Quarterly Report on Form 10-Q fairly represent in all material respects our financial condition, results of operations and cash flows at and for the periods presented in accordance with U.S. GAAP.

Remediation Plans. As disclosed in Item 9A of our Annual Report on Form 10-K for the fiscal year ended December 31, 2017, management determined that we did not maintain effective controls over the accuracy of the inputs in the sales order entry process. Specifically, we did not sufficiently execute controls over the review of data inputs in the sales order entry process to ensure accuracy of the price, quantity, and related customer data. This control deficiency did not result in a misstatement for the year ended December 31, 2017; however, this control deficiency could result in a misstatement of revenue that would result in a material misstatement to the annual or interim consolidated financial statements that would not be prevented or detected. Accordingly, our management has determined that this control deficiency constitutes a material weakness that had not been remediated as of September 29, 2018 .

We have identified and begun implementing changes to our internal control over financial reporting to remediate the control deficiencies that led to the material weakness. We have made progress toward remediating the material weakness by:

- redesigning controls over the inputs of the sales order entry process, including the design of systematic checks and new reports to review inputs,
- adding additional resources, and
- enhancing existing order entry controls and procedures, including implementation of more robust review procedures for accuracy of sales orders.

The material weakness will not be considered remediated until the applicable measures have been implemented for a sufficient period of time and management has concluded, through testing, that the enhanced control is operating effectively.

Inherent Limitations on Effectiveness of Controls. Our management, including the Chief Executive Officer and Chief Financial Officer, recognizes that our disclosure controls or our internal control over financial reporting cannot prevent or detect all possible instances of errors and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. The design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs.

Changes in Internal Control over Financial Reporting. There were no changes in our internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f)) during the period covered by this Quarterly Report on Form 10-Q that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II

Item 1. Legal Proceedings

For a discussion of legal proceedings, see Note 6, “Commitments and Contingencies,” in the notes to our condensed consolidated financial statements.

Further, we are and, from time to time, we may become, involved in legal proceedings or be subject to claims arising in the ordinary course of our business. We are not presently a party to any other legal proceedings that in the opinion of our management, if determined adversely to us, would individually or taken together have a material adverse effect on our business, operating results, financial condition, or cash flows.

Item 1A. Risk Factors

An investment in our Class A common stock involves a high degree of risk. You should carefully consider the risks and uncertainties described below, together with all of the other information in this Quarterly Report on Form 10-Q, including the section titled “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and our condensed consolidated financial statements and related notes, before making a decision to invest in our Class A common stock. Our business, operating results, financial condition, or prospects could be materially and adversely affected by any of these risks and uncertainties. If any of these risks actually occurs, the trading price of our Class A common stock could decline and you might lose all or part of your investment. Our business, operating results, financial performance, or prospects could also be harmed by risks and uncertainties not currently known to us or that we currently do not believe are material.

Risks Related to Our Business

We operate in a highly competitive market. If we do not compete effectively, our prospects, operating results, and financial condition could be adversely affected.

The wearable device market is highly competitive, with companies offering a variety of products and services. Wearables can be broadly defined as connected health and fitness trackers, fitness watches, smartwatches and devices beyond the wrist. We expect competition in our market to intensify in the future as new and existing competitors introduce new or enhanced products and services that are potentially more competitive than our products and services. In terms of units sold, we have primarily operated in the connected health and fitness tracker segment of the wearables device market, and more recently in the smartwatch category. The wearable device market has a multitude of participants, including specialized consumer electronics companies, such as Garmin, and traditional watch companies such as Fossil.

In addition, many large, broad-based consumer electronics companies either compete in our market or adjacent markets or have announced plans to do so, including Apple, Google, LG and Samsung. For example, Apple sells the Apple Watch, which is a smartwatch with broad-based functionalities, including some health and fitness tracking capabilities, and Apple has sold a significant volume of its smartwatches since introduction. Moreover, smartwatches with health and fitness functionalities may displace the market for traditional tracker devices. For example, Apple’s recently introduced Apple Watch includes ECG functionality and fall detection capability. We also face competition from manufacturers of lower-cost devices, such as Xiaomi and its Mi Band devices. In addition, we compete with a wide range of stand-alone health and fitness-related mobile apps that can be purchased or downloaded through mobile app stores.

We believe many of our competitors and potential competitors have significant advantages, including longer operating histories, ability to leverage their sales efforts and marketing expenditures across a broader portfolio of products and services, larger and broader customer bases, more established relationships with a larger number of suppliers, contract manufacturers, and channel partners, greater brand recognition, ability to leverage app stores which they may operate, experience manufacturing particular wearable devices, such as smartwatches, and greater financial, research and development, marketing, distribution, and other resources than we do.

Some of our competitors may aggressively discount their products and services in order to gain market share, which could result in pricing pressures, reduced profit margins, lost market share, or a failure to grow market share for us. In addition, new products may have lower selling prices or higher costs than legacy products, which could negatively impact our gross margins and operating results. Our competitors and potential competitors may also be able to develop products or services that are equal or superior to ours, achieve greater market acceptance of their products and services, and increase sales by utilizing different distribution channels than we do.

Furthermore, current or potential competitors may be acquired by third parties with greater available resources. As a result of such acquisitions, our current or potential competitors might be able to adapt more quickly to new technologies and consumer needs, devote greater resources to the promotion or sale of their products and services, initiate or withstand substantial price competition, take advantage of acquisition or other opportunities more readily or develop and expand their products and services more quickly than we do. If we are not able to compete effectively against our current or potential competitors, our prospects, operating results, and financial condition could be adversely affected.

If we are unable to anticipate and satisfy consumer preferences in a timely manner, our business may be adversely affected.

Our success depends on our ability to anticipate and satisfy consumer preferences in a timely manner. All of our products and services are subject to changing consumer preferences that cannot be predicted with certainty. In terms of units sold, we have primarily operated in the connected health and fitness tracker segment of the wearables device market. However, consumer preference has increasingly shifted to the smartwatch segment of the wearables device market. Although we are building out our smartwatch offerings, consumers may ultimately decide not to purchase our products and services as their preferences could shift rapidly to different types of wearable devices or away from these types of products and services altogether. In addition, adoption of our products may vary by geographic region. Our future success depends in part on our ability to anticipate and respond to shifts in consumer preferences. If we do not anticipate such shifts in a timely manner, our reputation and business may be adversely affected.

Our newer products and services that have additional features or new product designs, such as Fitbit Ionic and Fitbit Versa, may also have higher prices than many of our earlier products and the products of some of our competitors, which may not appeal to consumers or only appeal to a smaller subset of consumers. It is also possible that competitors could introduce new products and services that negatively impact consumer preference for our wearable devices, which could result in decreased sales of our products and services and a loss in market share.

In addition, although we intend to build out our recurring non-device revenue offerings, such as with a premium experience that offers a variety of features, insights and programs, it is possible that consumers or enterprise customers may not be receptive to these new services or that revenue from these offerings may continue to be immaterial. For example, in the first quarter of 2018, we acquired Twine Health, Inc., or Twine Health, a health coaching platform and in the third quarter of 2018, we introduced Fitbit Care, a connected health platform for health plans and employers, and revenue from these offerings is an immaterial portion of our overall revenue.

Accordingly, if we fail to anticipate and satisfy consumer preferences in a timely manner, or if it is perceived that our future products and services will not satisfy consumer preferences, our business may be adversely affected.

If we are unable to successfully develop, timely introduce, and effectively manage the introduction of new products and services or enhance existing products and services, our business may be adversely affected.

We must continually develop and introduce new products and services and improve and enhance our existing products and services to maintain or increase our sales. We believe that our future growth depends on continuing to engage and expand our user base by introducing new form factors, software services and other offerings. For example, in the first quarter of 2018, we started shipping Fitbit Versa, our second smartwatch; in the second quarter of 2018, we started shipping Fitbit Ace, our activity tracker designed for kids ages 8 and older; and in the third quarter of 2018, we started shipping Fitbit Charge 3, our newest activity tracker. In addition, in the first quarter of 2018, we acquired Twine Health, and in the third quarter of 2018, we introduced Fitbit Care. The success of new or enhanced products and services may depend on a number of factors including, anticipating and effectively addressing consumer preferences and demand, timely and successful research and development, the success of our sales and marketing efforts, effective forecasting and management of product demand, purchase commitments, and inventory levels, effective management of manufacturing and supply costs, and the quality of or defects in our products.

The development of our products and services is complex and costly, and we typically have several products and services in development at the same time. Given the complexity, we occasionally have experienced, and could experience in the future, delays in completing the development and introduction of new and enhanced products and services, product costs that are higher than planned, or lower than expected manufacturing yields of new and enhanced products, which may adversely affect our revenue and gross margins.

If revenues decline, we may be forced to reduce costs and may not be able to compete effectively. Unanticipated problems in developing products and services could also divert substantial research and development resources, which may impair our ability to develop new products and services and enhancements of existing products and services, and could substantially increase our costs. Problems in the design or quality of our products or services may also have an adverse effect on our brand, business, financial condition, and operating results.

We must also successfully manage introductions of new or enhanced products. Introductions of new or enhanced products could adversely impact the sales of our existing products to retailers and consumers. For instance, retailers often purchase less of our existing products in advance of new product launches. Furthermore, we may experience greater returns from retailers or users of existing products, or retailers may be granted stock rotation rights and price protection. Moreover, consumers may decide to purchase new or enhanced products instead of existing products. We may face challenges managing the inventory of existing products, which could lead to excess inventory and discounting of our existing products. In addition, new products may have lower selling prices or higher costs than legacy products, which could negatively impact our gross margins and operating results. We have also historically incurred higher levels of sales and marketing expenses accompanying each product introduction. Accordingly, if we fail to effectively manage introductions of new or enhanced products, our operating results could be harmed.

Our operating results could be materially harmed if we are unable to accurately forecast consumer demand for our products and services and adequately manage our inventory.

If we fail to accurately forecast consumer demand, we may experience excess inventory levels or a shortage of products available for sale. Our ability to accurately forecast demand for our products and services could be affected by many factors, including an increase or decrease in consumer demand for our products and services or for the products and services of our competitors, product and service introductions by us and our competitors, channel inventory levels, sales promotions by us or our competitors, unanticipated changes in general market conditions, and the weakening of economic conditions or consumer confidence in future economic conditions. To ensure adequate inventory supply, we must forecast inventory needs and expenses and place orders sufficiently in advance with our suppliers and contract manufacturers based on our estimates of future demand for particular products. We have previously faced and may continue to face challenges acquiring adequate and timely supplies of our products to satisfy demand, particularly in connection with new product introductions, which we believe may negatively affect our revenue. For example, during the three months ended June 30, 2018, we were impacted by supply constraints associated with Fitbit Versa, which limited our ability to fully satisfy all of the current demand for this product. As we continue to introduce new products, we may face challenges managing the inventory of existing products. No assurance can be given that we will not incur additional charges in future periods related to our inventory management or that we will not underestimate or overestimate forecasted sales in a future period.

Inventory levels in excess of consumer demand may result in inventory write-downs or write-offs and the sale of inventory at discounted prices, which have caused and may continue to cause our gross margin to decline and could impair the strength of our brand. For example, during the fourth quarter of 2016, as a result of reduced demand, we recorded write-downs for excess and obsolete inventory, accelerated depreciation of manufacturing and tooling equipment, and recorded a liability to our contract manufacturers for unutilized manufacturing capacity and components. In addition, we offered, and recorded reserves for, additional rebates and promotions during the fourth quarter of 2016 to retailers and distributors. During 2017, we recorded additional write-downs for excess and obsolete inventory, accelerated depreciation of manufacturing and tooling equipment due to continued reduced demand, price protection on certain products, and rebates. Reserves and write-downs for rebates, promotions, excess inventory, tooling and manufacturing capacity are recorded based on our forecast of future demand. Actual future demand could be less than our forecast which may result in additional reserves and write-downs in the future or actual demand could be stronger than forecast which may result in a reduction to previously recorded reserves and write-downs in the future and increase the volatility of our operating results.

Conversely, if we underestimate consumer demand for our products, we may in future periods be unable to meet customer, retailer or distributor demand for our products. We may also be required to incur higher costs to secure the necessary production capacity and components if we underestimate demand and our business and operating results could be adversely affected, including damage to our brand and customer relationships.

Our quarterly operating results or other operating metrics may fluctuate significantly, which could cause the trading price of our Class A common stock to decline.

Our quarterly operating results and other operating metrics have fluctuated in the past and may continue to fluctuate from quarter to quarter. We expect that this trend will continue as a result of a number of factors, many of which are outside of our control and may be difficult to predict, including:

- the level of demand for our wearable devices and our ability to maintain or increase the size and engagement of our community of users;
- the timing and success of new product and service introductions by us and the transition from legacy products;
- the timing and success of new product and service introductions by our competitors or any other change in the competitive landscape of our market;
- the mix of products sold in a quarter;
- the continued market acceptance of, and the growth of the market for, wearable devices, and evolution of this market into smartwatches and other form factors;
- pricing pressure as a result of competition or otherwise;
- delays or disruptions in our supply, manufacturing, or distribution chain;
- errors in our forecasting of the demand for our products, which could lead to lower revenue or increased costs, or both;
- seasonal buying patterns of consumers;
- increases in levels of channel inventory resulting from sales to our retailers and distributors in anticipation of future demand;
- increases in and timing of sales and marketing and other operating expenses that we may incur to grow and expand our operations and to remain competitive;
- impact of sales and marketing efforts and promotions by competitors, which are difficult to predict;
- insolvency, credit, or other difficulties faced by our distributors and retailers, affecting their ability to purchase or pay for our products;
- insolvency, credit, or other difficulties confronting our suppliers, contract manufacturers, or logistics providers leading to disruptions in our supply or distribution chain;
- levels of product returns, stock rotation, and price protection rights;
- levels of warranty claims or estimated costs of warranty claims;
- adverse litigation judgments, settlements, or other litigation-related costs;
- changes in the legislative or regulatory environment, such as with respect to privacy, information security, health and wellness devices, consumer product safety, advertising, and taxes;
- product recalls, regulatory proceedings, or other adverse publicity about our products;
- fluctuations in foreign exchange rates;
- costs related to the acquisition of businesses, talent, technologies, or intellectual property, including potentially significant amortization costs and possible write-downs; and
- general economic conditions in either domestic or international markets, including potential changes in tariffs.

Any one of the factors above or the cumulative effect of some of the factors above may result in significant fluctuations in our operating results.

The variability and unpredictability of our quarterly operating results or other operating metrics could result in our failure to meet our expectations, those of any analysts that publish financial coverage of us, or investors with respect to revenue or other operating results for a particular period. If we fail to meet or exceed such expectations for these or any other reasons, the market price of our Class A common stock could fall substantially, and we could face costly lawsuits, including securities class action suits.

We may not be able to achieve revenue growth or profitability in the future.

Our historical revenue growth should not be considered indicative of our future performance. Our revenue has declined in recent periods, and we expect our revenue growth to be slower than in the past or to decline in future periods due to a number of factors which may include slowing demand for our products and services, increasing competition, a decrease in the growth of our overall market, our failure, for any reason, to capitalize on growth opportunities, or the maturation of our business.

From 2014 to 2016, our annual revenue grew rapidly from $745.4 million to $2.2 billion. However, in recent quarters, our revenue growth has declined, and our historical growth should not be considered as indicative of our future performance. Although our annual revenue in 2016 was up 17% compared to 2015, our annual revenue in 2017 declined 26% compared to 2016, and our revenue in the nine months ended September 29, 2018 declined 10% compared to the nine months ended September 30, 2017 . In future periods, we could again experience a decline in revenue, or revenue could grow more slowly than we expect, which could have a material negative effect on our future operating results.

Because we have only a limited history operating our business at its current scale, it is difficult to evaluate our current business and future prospects, including our ability to plan for and model future growth. Our limited operating experience at this scale, combined with the rapidly evolving nature of the market in which we sell our products and services, substantial uncertainty concerning how these markets may develop, and other economic factors beyond our control, reduces our ability to accurately forecast quarterly or annual revenue. As such, any predictions about our future revenue and expenses may not be as accurate as they would be if we had a longer operating history or operated in a more developed and predictable market. Failure to manage our future growth effectively could have an adverse effect on our business, which, in turn, could have an adverse impact on our operating results and financial condition.

In addition, we have not consistently achieved profitability on a quarterly or annual basis. For example, we recorded a net loss of $201.2 million in the nine months ended September 29, 2018 and a net loss of $277.2 million in 2017. Lower levels of revenue and higher levels of operating expenses may result in limited profitability or losses in the future.

If we fail to manage our operating expenses effectively, our financial performance may be negatively impacted.

Our success also depends on our ability to manage our operating expenses effectively. Our employee headcount and the scope and complexity of our business have increased significantly during recent years and we had 1,736 employees as of September 29, 2018. We have incurred significant net losses of $201.2 million in the nine months ended September 29, 2018 and $277.2 million and $102.8 million in 2017 and 2016, respectively.

In addition, we are also investing in areas we believe will grow revenue and our operating expenses might increase as a result of these investments. The development of our products and services is complex and costly, and we typically have several products and services in development at the same time. Our research and development efforts may require us to incur substantial expenses to support the development of our next generation devices and other new products and services. Our research and development expenses were $ 79.8 million and $84.2 million, for the three months ended September 29, 2018 and September 30, 2017, respectively, and $256.2 million and $252.5 million for the nine months ended September 29, 2018 and September 30, 2017, respectively.

We could also be required to continue to expand our sales and marketing, product development, and distribution functions, to upgrade our management information systems and other processes and technology, and to obtain more space for our expanding workforce. This expansion could increase the strain on our resources, and we could experience serious operating difficulties, including difficulties in hiring, training, and managing an increasing number of employees.

If our continued investments do not result in future revenue as expected, we may incur greater than expected losses and our liquidity position may be materially adversely affected.

Conversely, in the future, we may again need to strategically realign our resources, adjust our product line and/or enact price reductions in order to stimulate demand, implement additional restructuring and workforce reductions or downsize our facilities for our reduced workforce. Any such actions may result in the recording of special charges including inventory-related write-offs, workforce reductions, or other restructuring costs. Additionally, our estimates with respect to the useful life or ultimate recoverability of our assets, including purchased intangible assets and tooling, could also change and result in impairment charges.

If we are unable to operate efficiently and manage our costs, we may continue to incur significant losses in the future and may not be able to achieve or maintain profitability.

Because some of the key components in our products come from a limited number or single source of supply, we are susceptible to supply shortages, long lead times for components, and supply changes, any of which could disrupt our supply chain.

Some of the key components used to manufacture our products come from a limited or single source of supply. Our contract manufacturers generally purchase these components on our behalf, subject to certain approved supplier lists. We are subject to the risk of shortages and long lead times in the supply of these components and the risk that our suppliers discontinue or modify components used in our products. In addition, the lead times associated with certain components are lengthy and preclude rapid changes in quantities and delivery schedules. We have in the past experienced and may in the future experience component shortages, and the predictability of the availability of these components may be limited. While component shortages have historically been immaterial, they could be material in the future. In the event of a component shortage or supply interruption from suppliers of these components, we may not be able to develop suitable alternate sources in a timely manner. In addition, some of our suppliers, contract manufacturers, and logistics providers may have more established relationships with our competitors, and as a result of such relationships, such suppliers may choose to limit or terminate their relationship with us. Developing suitable alternate sources of supply for these components may be time-consuming, difficult, and costly and we may not be able to source these components on terms that are acceptable to us, or at all, which may adversely affect our ability to meet our requirements or to fill our orders in a timely or cost-effective manner. Any interruption or delay in the supply of any of these parts or components, or the inability to obtain these parts or components from alternate sources at acceptable prices and within a reasonable amount of time, would harm our ability to meet our scheduled product deliveries to our customers and users. This could harm our relationships with our channel partners and users and could cause delays in shipment of our products and adversely affect our operating results. In addition, increased component costs could result in lower gross margins. 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 products and services to our customers and users, which could adversely impact our revenue, gross margins, and operating results.

Our future success depends on the continuing efforts of our key employees, including our founders, James Park and Eric N. Friedman, and on our ability to attract and retain highly skilled personnel and senior management.

Our future success depends, in part, on our ability to continue to attract and retain highly skilled personnel. In particular, we are highly dependent on the contributions of our co-founders, James Park and Eric N. Friedman, as well as other members of our management team. The loss of any key personnel could make it more difficult to manage our operations and research and development activities, reduce our employee retention and revenue, and impair our ability to compete. Although we have generally entered into employment offer letters with our key personnel, these agreements have no specific duration and provide for at-will employment, which means they may terminate their employment relationship with us at any time.

Competition for highly skilled personnel is often intense, especially in the San Francisco Bay area where we are located, and we may incur significant costs to attract them. We may not be successful in attracting, integrating, or retaining qualified personnel to fulfill our current or future needs. We have, from time to time, experienced, and we expect to continue to experience, difficulty in hiring and retaining highly skilled employees with appropriate qualifications. Job candidates and existing employees often consider the value of the equity awards they receive in connection with their employment, and the significant decline in the price of our Class A common stock since our initial public offering may adversely affect our ability to attract or retain highly skilled employees. Fluctuations in the price of our Class A common stock may also make it more difficult or costly to use equity awards to motivate, incentivize and retain our employees. Furthermore, there can be no assurances that the number of shares reserved for issuance under our equity incentive plans will be sufficient to grant equity awards adequate to recruit new employees and to compensate existing employees. Additionally, changes in immigration laws may make it harder to attract and retain highly skilled employees. If we fail to attract new personnel or fail to retain and motivate our current personnel, our business and future growth prospects could be severely harmed.

We spend significant amounts on advertising and other marketing campaigns to acquire new users, which may not be successful or cost effective.

We spend significant amounts on advertising and other marketing campaigns, such as television, cinema, print advertising, and social media, as well as promotional activities, to acquire new users and we expect to continue to spend significant amounts marketing our products and services to acquire new users and increase awareness of our products and services. In 2017 and the nine months ended September 29, 2018 , advertising expenses, excluding co-op advertising and rebates which are recorded as contra-revenue, were $226.3 million and $105.2 million, respectively, representing approximately 14% and 11% of our revenue, respectively. Co-op advertising costs were $45.0 million and $48.6 million for 2017 and the nine months ended September 29, 2018 , respectively. A significant portion of our advertising and marketing spend is typically incurred in the fourth quarter as part of our holiday promotions, as well as when new products are released. While we seek to structure our advertising campaigns in the manner that we believe is most likely to encourage people to buy our products and services, we may fail to identify advertising opportunities that satisfy our anticipated return on advertising spend as we scale our investments in marketing, accurately predict user acquisition, or fully understand or estimate the conditions and behaviors that drive user behavior. Particularly during the holiday season, there is significant competition for holiday spending; if competitors or other products offer more compelling promotions or products, we may not realize our expected sales or recover our advertising and promotional spend. If new products do not meet customer expectations, we may not recover our advertising and promotional spend for new product introductions. If for any reason any of our advertising campaigns prove less successful than anticipated in attracting new users, we may not be able to recover our advertising spend, and our rate of user acquisition may fail to meet market expectations, either of which could have an adverse effect on our business. There can be no assurance that our advertising and other marketing efforts will result in increased sales of our products and services.

Our current and future products and services may experience quality problems from time to time that can result in adverse publicity, product recalls, litigation, regulatory proceedings, and warranty claims resulting in significant direct or indirect costs, decreased revenue and operating margin, and harm to our brand.

We sell complex products and services that could contain design and manufacturing defects in their materials, hardware, and firmware. These defects could include defective materials or components, or "bugs," that can unexpectedly interfere with the products' intended operations or cause injuries to users or property. Although we extensively and rigorously test new and enhanced products and services before their release, there can be no assurance we will be able to detect, prevent, or fix all defects. For example, our products may fail to provide accurate measurements and data to all users under all circumstances, or there may be reports or claims of inaccurate measurements under certain circumstances.

Failure to detect, prevent, or fix defects, or an increase in defects could result in a variety of consequences including a greater number of returns of products than expected from users and retailers, increases in warranty costs, regulatory proceedings, product recalls, and litigation, which could harm our revenue and operating results. For example, in 2016, we experienced an increase in actual and estimated warranty claims of $108.5 million as compared to 2015, which caused a 4% decline in gross margin in 2016 as compared to 2015. We generally provide a 45-day right of return for purchases through Fitbit.com and a 12-month limited warranty on all of our products, though warranty duration and scope may vary by jurisdiction in compliance with applicable local law. The occurrence of real or perceived quality problems or material defects in our current and future products could expose us to warranty claims in excess of our current reserves. Moreover, we may offer stock rotation rights and price protection to our distributors. If we experience greater returns from retailers or users, or greater warranty claims, in excess of our reserves, our business, revenue, gross margin, and operating results could be harmed. In addition, any negative publicity or lawsuits filed against us related to the perceived quality and safety of our products could also affect our brand and decrease demand for our products and services, adversely affecting our operating results and financial condition.

We rely on a limited number of suppliers, contract manufacturers, and logistics providers, and each of our products is manufactured by a single contract manufacturer.

We rely on a limited number of suppliers, contract manufacturers, and logistics providers. In particular, we use contract manufacturers located in Asia, and each of our products is manufactured by a single contract manufacturer. Our reliance on a sole contract manufacturer for each of our products increases the risk that in the event of an interruption from any one of these contract manufacturers, including, without limitation, due to a natural catastrophe, labor dispute or increased tariffs on goods produced in certain countries, we may not be able to develop an alternate source without incurring material additional costs and substantial delays. Accordingly, an interruption from any key supplier, contract manufacturer, or logistics provider could adversely impact our revenue, gross margins, and operating results.

If we experience a significant increase in demand, or if we need to replace an existing supplier, contract manufacturer, or logistics provider or move our contract manufacturing to a different country, we may be unable to supplement or replace such supply, contract manufacturing, or logistics capacity on terms that are acceptable to us, which may adversely impact our ability to deliver our products to customers in a timely manner. For example, for certain of our products, it may take a significant amount of time to onboard a contract manufacturer that has the capability and resources to build the product to our specifications in sufficient volume. Identifying suitable suppliers, contract manufacturers, and logistics providers is an extensive process that requires us to become satisfied with their quality control, technical capabilities, responsiveness and service, financial stability, regulatory compliance, and labor and other ethical practices. In addition, our contract manufacturers often make significant investments to build capacity based upon our forecasted production. If we experience a significant decrease in demand as compared to our forecast, our contract manufacturers may seek to renegotiate the terms of their commitments or choose to limit or terminate their relationship with us. Accordingly, a loss of any key supplier, contract manufacturer, or logistics provider could adversely impact our revenue, gross margins, and operating results.

We have limited control over our suppliers, contract manufacturers, and logistics providers, which subjects us to significant risks, including the potential inability to obtain or produce quality products on a timely basis or in sufficient quantity.

We have limited control over our suppliers, contract manufacturers, and logistics providers, including aspects of their specific manufacturing processes and their labor, environmental, or other practices, which subjects us to significant risks, including the following:

- inability to satisfy demand for our products;
- reduced control over delivery timing and product reliability;
- reduced ability to oversee the manufacturing process and components used in our products;
- reduced ability to monitor compliance with our product manufacturing specifications;
- price increases;
- insolvency, credit problems, or other financial difficulties confronting our suppliers, contract manufacturers, or logistic providers;
- difficulties in establishing additional or alternative contract manufacturing relationships if we experience difficulties with our existing suppliers, contract manufacturers or logistic providers;
- shortages of materials or components;
- misappropriation of our intellectual property;
- suppliers, contract manufacturers, and logistics providers may choose to limit or terminate their relationship with us;
- exposure to natural catastrophes, political unrest, terrorism, labor disputes, and economic instability resulting in the disruption of trade from foreign countries in which our products are manufactured;
- changes in local economic conditions in countries where our suppliers, contract manufacturers, or logistics providers are located;
- the imposition of new laws and regulations, including those relating to labor conditions, quality and safety standards, imports, duties, taxes, and other charges on imports, as well as trade restrictions and restrictions on currency exchange or the transfer of funds and tariffs; and
- insufficient warranties and indemnities on components supplied to our contract manufacturers.

If there are defects in the manufacture of our products, we may face negative publicity, government investigations, and litigation, and we may not be fully compensated by our contract manufacturers for any financial or other liability that we suffer as a result.

We are, and may in the future, be subject to claims and lawsuits alleging that our products fail to provide accurate measurements and data to our users.

Our products and services are used to track and display various information about users' activities, such as daily steps taken, calories burned, distance traveled, floors climbed, active minutes, sleep duration and quality, and heart rate and GPS-based information such as speed, distance, and exercise routes. We anticipate new features and functionality in the future, as well. From time to time, there have been reports and claims made against us alleging that our products do not provide accurate measurements and data to users, including claims asserting that certain features of our products do not operate as advertised. Such reports and claims have resulted in negative publicity, and, in some cases, have required us to expend time and resources to defend litigation. For example, in the first quarter of 2016, class action lawsuits were filed against us based upon claims that the PurePulse heart rate tracking technology in the Fitbit Charge HR, Fitbit Surge, and Fitbit Blaze do not consistently and accurately record users' heart rates. If our products fail to provide accurate measurements and data to users, or if there are reports or claims of inaccurate measurements, claims of false advertisement, or claims of inaccuracy regarding the overall health benefits of our products and services in the future, we may become the subject of negative publicity, litigation, including class action litigation, regulatory proceedings, and warranty claims, and our brand, operating results, and business could be harmed.

Our operating margins have declined and may continue to decline as a result of decreased revenues, increasing product costs and operating expenses.

Our business is subject to significant pressure on pricing and costs caused by many factors, including intense competition, new product introductions, the cost of components used in our products, labor costs, constrained sourcing capacity, inflationary pressure, pressure from users to reduce the prices we charge for our products and services, warranty claims, and changes in consumer demand. Costs for the components used in the manufacture of our products are affected by, among other things, energy prices, consumer demand, fluctuations in commodity prices and currency, tariffs, and other factors that are generally unpredictable and beyond our control. Any change to pricing and costs could have an adverse effect on, among other things, our average selling price, the cost of our products, gross margins, operating results, financial condition, and cash flows. Moreover, if we are unable to offset any decreases in our average selling price by increasing our sales volumes or by adjusting our product mix, or if our sales volume declines and we are not able to reduce our costs, our operating results and financial condition may be harmed.

A substantial portion of our expenses are personnel related and include salaries, stock-based compensation and benefits, which are not seasonal in nature. Accordingly, in the event of revenue shortfalls, we are generally unable to mitigate a negative impact on operating margins in the short term. To the extent such revenue shortfalls recur in future periods, our operating results would be harmed.

Our success depends on our ability to maintain our brand. If events occur that damage our brand, our business and financial results may be harmed.

Our success depends on our ability to maintain the value of the “Fitbit” brand. The “Fitbit” name is integral to our business as well as to the implementation of our strategies for expanding our business. Maintaining, promoting, and positioning our brand will depend largely on the success of our marketing and merchandising efforts, our ability to provide consistent, high quality products and services, and our ability to successfully secure, maintain, and defend our rights to use the “Fitbit” mark and other trademarks important to our brand. Our brand could be harmed if we fail to achieve these objectives or if our public image or brand were to be tarnished by negative publicity. For example, there has been media coverage of some of the users of our products reporting skin irritation, as well as personal injury lawsuits filed against us relating to the Fitbit Zip, Fitbit One, Fitbit Flex, Fitbit Charge, Fitbit Charge HR, and Fitbit Surge products. We also believe that our reputation and brand may be harmed if we fail to maintain a consistently high level of customer service. In addition, we believe the popularity of the “Fitbit” brand makes it a target for counterfeiting or imitation, with third parties attempting to sell counterfeit products that attempt to replicate our products.

In addition, our products may be diverted from our authorized retailers, distributors, and other business partners and sold on the “gray market.” Gray market products result in shadow inventory that is not visible to us, thus making it difficult to forecast demand accurately. Also, when gray market products enter the market, we and our channel partners compete with often heavily discounted gray market products, which adversely affects demand for our products and negatively impacts our margins. In addition, our inability to control gray market activities could result in user satisfaction issues, which may have a negative impact on our brand. When products are purchased outside our authorized retailers and distributors, there is a risk that our customers are buying substandard products, including products that may have been designed by us for destruction, altered, mishandled, or damaged, or used products represented as new.

Any occurrence of counterfeiting, imitation, or confusion with our brand could adversely affect our reputation, place negative pricing pressure on our products, reduce sales of our products, and impair the value of our brand. Additionally, counterfeit and unauthorized grey market sales may result in secondary warranty replacement and service costs. Maintaining, protecting, and enhancing our brand may require us to make substantial investments, and these investments may not be successful. If we fail to successfully maintain, promote, and position our brand and protect our reputation or if we incur significant expenses in this effort, our business, financial condition and operating results may be adversely affected.

If significant tariffs or other restrictions are placed on our goods imported into the United States from China or any related counter-measures are taken by China, our revenue, gross margin, and results of operations may be materially harmed.

If significant tariffs or other restrictions are placed on goods imported into the United States from China or any related counter-measures are taken by China, our revenue and results of operations may be materially harmed. The Trump Administration has signaled that it may alter trade terms between China and the United States, including by limiting trade with China and/or imposing tariffs on imports from China. Between July and September 2018, the U.S. Trade Representative imposed additional duties, ranging from 10% to 25% on a variety of goods imported from China that will potentially be subjected to a 10% tariff until 2019, when the tariffs will increase to 25%. While these tariffs do not currently apply to our products, if additional tariffs that cover our products are imposed, the cost of our products may increase. In addition, any such additional tariffs may also make our products more expensive for consumers, which may reduce consumer demand. We may need to offset the financial impact by, among other things, moving our product manufacturing to other locations, modifying other business practices or raising prices. If we are not successful in offsetting the impact of any such tariffs, our revenue, gross margins, and operating results may be adversely affected.

Any insolvency, credit problems, or other financial difficulties impacting our retailers and distributors could expose us to financial risk.

Some of our retailers and distributors have experienced and may continue to experience financial difficulties. Insolvency, credit challenges, or other financial difficulties may impact our retailers and distributors and could expose us to significant financial risk. In addition, if the credit capacity of any retailer or distributor declines due to deterioration in their financial condition or increases in their outstanding payable balance to us, we may be subject to additional financial risk. Financial difficulties of our retailers and distributors could impede their effectiveness and also expose us to risks if they are unable to pay for the products they purchase from us. For example, Wynit Distribution, LLC, or Wynit, historically our largest customer, filed for bankruptcy protection in September 2017, which caused us to incur $7.6 million in net bad debt expenses and $1.4 million in net cost of revenues in 2017. Credit and financial difficulties of our retailers and distributors may also lead to a reduction in sales, price reductions, increased returns of our products, and adverse effects on our brand and operating results. We maintain credit insurance for the majority of our customer balances, perform ongoing credit evaluations of our customers, and maintain allowances for potential credit losses on customers' accounts when deemed necessary. Credit and financial difficulties may lead to an increase in our credit insurance premiums and make it more difficult or impossible to obtain sufficient coverage, which could increase our exposure and result in increased bad debt expense or additional write-offs. We also may not have sufficient insurance coverage to cover losses resulting from the credit and financial difficulties of our retailers and distributors. Any reduction in sales by our current retailers or distributors, loss of large retailers or distributors, or decrease in revenue from our retailers or distributors could adversely affect our revenue, operating results, and financial condition.

We depend on retailers and distributors to sell and market our products, and our failure to maintain and further develop our sales channels could harm our business.

We primarily sell our products through retailers and distributors and depend on these third-parties to sell and market our products to consumers. Any changes to our current mix of retailers and distributors could adversely affect our gross margin and could negatively affect both our brand image and our reputation. Our sales depend, in part, on retailers adequately displaying our products, including providing attractive space and point of purchase displays in their stores, and training their sales personnel to sell our products. Our retailers also often offer products and services of our competitors in their stores. If our retailers and distributors are not successful in selling our products or overestimate demand for our products or promote competing products and services more effectively than our products and services, our revenue would decrease and our gross margins could decline due to increased product returns or price protection claims. In addition, our success in expanding and entering into new markets internationally will depend on our ability to establish relationships with new retailers and distributors. We also sell and will need to continue to expand our sales through online retailers, such as Amazon.com, and through our direct channel, Fitbit.com, as consumers increasingly make purchases online. If we do not maintain our relationship with existing retailers and distributors or develop relationships with new retailers and distributors our ability to sell our products and services could be adversely affected and our business may be harmed.

In 2017 and the nine months ended September 29, 2018 , our five largest retailers and distributors accounted for approximately 43% and 39%, respectively, of our revenue. Of these retailers and distributors, Amazon.com accounted for approximately 13% of our revenue for 2017 and D&H Distribution Company, Amazon.com and Kohl's Department Stores, Inc. accounted for approximately 13%, 12% and 10%, respectively, of our revenue for the nine months ended September 29, 2018 . No other retailers or distributors accounted for 10% or more of our revenue during these periods. Accordingly, the loss of a small number of our large retailers and distributors, or the reduction in business with one or more of these retailers and distributors, could have a significant adverse impact on our operating results. For example, Wynit, historically our largest customer at the time, filed for bankruptcy protection in September 2017. While we have agreements with these large retailers and distributors, these agreements do not require them to purchase any meaningful amount of our products.

Consolidation of retailers or concentration of retail market share among a few retailers may increase and concentrate our credit risk and impair our ability to sell products.

The electronics retail and sporting goods markets in some countries, including the United States, our largest market, are dominated by a few large retailers with many stores. These retailers have in the past increased their market share and may continue to do so in the future by expanding through acquisitions and construction of additional stores. This can further concentrate our credit risk to a relatively small number of retailers, and, if any of these retailers were to experience credit or liquidity issues, it would increase the risk that our receivables from these customers may not be paid. In addition, increasing market share concentration among one or a few retailers in a particular country or region increases the risk that if any one of them substantially reduces their purchases of our wearable devices, we may be unable to find a sufficient number of other retail outlets for our products to sustain the same level of sales. These situations also may result in pricing pressure to us. Any reduction in sales by our retailers would adversely affect our revenue, operating results, and financial condition.

Our business is affected by seasonality and if our sales fall below our forecasts, our overall financial conditions and operating results could be adversely affected.

Our revenue and operating results are affected by general seasonal spending trends associated with holidays. For example, our fourth quarter has typically been our strongest quarter in terms of revenue and operating income, reflecting our historical strength in sales during the holiday season. We generated approximately 35%, 26% and 38% of our full year revenue during the fourth quarters of 2017, 2016 and 2015, respectively. Accordingly, any shortfall in expected fourth quarter revenue would adversely affect our annual operating results, as was the case in the fourth quarter of 2016. In addition, although we expect to achieve cash flow breakeven in 2018, we expect to incur net cash outflows in the second and third quarters of 2018, and positive cash flow in the fourth quarter of 2018. Any shortfall in revenue, particularly in the fourth quarter of 2018, would negatively affect our ability to achieve cash flow breakeven in 2018, and may adversely affect our liquidity. We may also experience excess inventory levels or a shortage of products available for sale if we fail to accurately forecast consumer demand for the holiday season.

Furthermore, our growth rate in recent years may obscure the extent to which seasonality trends have affected our business and may continue to affect our business. Accordingly, yearly or quarterly comparisons of our operating results may not be useful and our results in any particular period will not necessarily be indicative of the results to be expected for any future period. Seasonality in our business can also be significantly impacted by introductions of new or enhanced products and services, including the costs associated with such introductions.

We collect, store, process, and use personal information and other customer data, which subjects us to governmental regulation and other legal obligations related to privacy, information security, and data protection, and any security breaches or our actual or perceived failure to comply with such legal obligations could harm our business.

We collect, store, process, and use personal information and other user data, and we rely on third parties that are not directly under our control to do so. Our users' exercise and activity-related data and other personal information may include, among other information, names, addresses, phone numbers, email addresses, payment account information, height, weight, and information such as heart rates, sleeping patterns, GPS-based location, and activity patterns.

Due to the volume of the personal information and data we manage and the nature of our products, the security features of our platform and information systems are critical. If our security measures, some of which we manage using third-party solutions, are breached or fail, unauthorized persons may be able to obtain access to or acquire our users' data. Furthermore, if third-party service providers that host user data on our behalf experience security breaches or violate applicable laws, agreements, or our policies, such events may also put our users' information at risk and could in turn have an adverse effect on our business. Additionally, if we or any third-party, including third-party applications, with which our users choose to share their Fitbit data were to experience a breach of systems compromising our users' personal data, our brand and reputation could be adversely affected, use of our products and services could decrease, and we could be exposed to a risk of loss, litigation, and regulatory proceedings.

Depending on the nature of the information compromised, in the event of a data breach or other unauthorized access to or acquisition of our user data, we may also have obligations to notify users about the incident and we may need to provide some form of remedy, such as a subscription to a credit monitoring service, for the individuals affected by the incident. A growing number of legislative and regulatory bodies have adopted consumer notification requirements in the event of unauthorized access to or acquisition of certain types of personal data. Such breach notification laws continue to evolve and may be inconsistent from one jurisdiction to another. Complying with these obligations could cause us to incur substantial costs and could increase negative publicity surrounding any incident that compromises user data. Our users may also inadvertently disclose or lose control of their passwords, creating the perception that our systems are not secure against third-party access. While we maintain insurance coverage that, subject to policy terms and conditions and a significant self-insured retention, is designed to address certain aspects of cyber risks, such insurance coverage may be insufficient to cover all losses or all types of claims that may arise in the event we experience a security breach. In addition, any such security breaches may result in negative publicity, adversely affect our brand, decrease demand for our products and services, and adversely affect our operating results and financial condition.

Our failure to comply with U.S. and foreign laws related to privacy, data security, and data protection, such as the European Union's new General Data Protection Regulation, which has broad scope, raised standards, and substantial penalties, and requires an adequate legal mechanism for the transfer of personal data outside of Europe, could adversely affect our financial condition, operating results, and our brand.

We are or may become subject to a variety of laws and regulations in the United States and abroad regarding privacy, data protection, and data security. These laws and regulations are continuously evolving and developing. The scope and interpretation of the laws that are or may be applicable to us are often uncertain and may be conflicting, particularly with respect to foreign laws.

In particular, there are numerous U.S. federal, state, and local laws and regulations and foreign laws and regulations regarding privacy and the collection, sharing, use, processing, disclosure, and protection of personal data. Such laws and regulations often have changes in scope, may be subject to differing interpretations, and may be inconsistent among different jurisdictions. For example, the General Data Protection Regulation, or GDPR, became effective in May 2018. The GDPR includes operational requirements for companies that receive or process personal data of residents of the European Union that are more stringent than those currently in place in the European Union, and that will include significant penalties for non-compliance, including fines of up to €20 million or 4% of total worldwide revenue. Additionally, in June 2018, California passed the California Consumer Privacy Act, or CCPA, provides new data privacy rights for consumers and new operational requirements for companies, effective in 2020. Fines for noncompliance may be up to $7,500 per violation. The costs of compliance with, and other burdens imposed by, the GDPR and CCPA may limit the use and adoption of our products and services and could have an adverse impact on our business.

Additionally, we rely on various legal mechanisms for transferring certain personal data outside of the European Economic Area, or EEA, including the EU-US Privacy Shield Framework, or Privacy Shield, and EU Standard Contractual Clauses, or SCCs. In November 2016, the US Department of Commerce approved our Privacy Shield self-certification, which is available on the Department's Privacy Shield website. Both Privacy Shield and the SCCs are the subject of ongoing legal challenges in European courts. If we fail or are perceived to fail to meet the Privacy Shield principles or our obligations under the SCCs, or if any of these legal mechanisms for transferring data from the EEA are invalidated by European courts or otherwise become defunct, EU data protection authorities or the Federal Trade Commission could bring enforcement actions seeking to prohibit or suspend our data transfers or alleging unfair or deceptive practices. In such cases, we could be required to make potentially expensive changes to our information technology infrastructure and business operations, and we could face legal liability, fines, negative publicity, and resulting loss of business.

Certain privacy laws and regulations also apply to the collection of personal information from children, including the Children's Online Privacy Protection Act, or COPPA, and GDPR. In the first quarter of 2018, we introduced Fitbit Ace, our first activity tracker designed for kids ages 8 and up and Fitbit family accounts. If these products no not comply with any applicable laws or regulations, we could be subject to claims, legal liabilities, penalties, fines, and negative publicity, which could harm our operating results.

We strive to comply with all applicable laws, policies, legal obligations, and industry codes of conduct relating to privacy, data security, and data protection. However, given that the scope, interpretation, and application of these laws and regulations are often uncertain and may be conflicting, it is possible that these obligations may be interpreted and applied in a manner that is inconsistent from one jurisdiction to another and may conflict with other rules or our practices. Any failure or perceived failure by us or third-party service-providers to comply with our privacy or security policies or privacy-related legal obligations, or the failure or perceived failure by third-party apps with which our users choose to share their Fitbit data to comply with their privacy policies or privacy-related legal obligations as they relate to the Fitbit data shared with them, or any compromise of security that results in the unauthorized release or transfer of personal data, may result in governmental enforcement actions, litigation, or negative publicity, and could have an adverse effect on our brand and operating results.

Certain health-related laws and regulations such as the Health Insurance Portability and Accountability Act of 1996, or HIPAA, and the Health Information Technology for Economic and Clinical Health Act, or HITECH, may have an impact on our business. For example, in September 2015 we announced that we intend to offer HIPAA compliant capabilities to certain customers of our corporate wellness offerings who are "covered entities" under HIPAA, which may include our execution of Business Associate Agreements with such covered entities. In addition, changes in applicable laws and regulations may result in the user data we collect being deemed protected health information, or PHI, under HIPAA and HITECH. Furthermore, because we accept payment via credit cards, we are subject to payment card association operating rules and certification requirements, including the Payment Card Industry Data Security Standard, or PCI DSS. If we are unable to comply with the applicable privacy and security requirements under HIPAA, HITECH, or PCI DSS, or we fail to comply with Business Associate Agreements that we enter into with covered entities, we could be subject to claims, legal liabilities, penalties, fines, and negative publicity, which could harm our operating results.

Governments are continuing to focus on privacy and data security and it is possible that new privacy or data security laws will be passed or existing laws will be amended in a way that is material to our business. Any significant change to applicable laws, regulations, or industry practices regarding our users' data could require us to modify our services and features, possibly in a material manner, and may limit our ability to develop new products, services, and features. Although we have made efforts to design our policies, procedures, and systems to comply with the current requirements of applicable state, federal, and foreign laws, changes to applicable laws and regulations in this area could subject us to additional regulation and oversight, any of which could significantly increase our operating costs.

Cybersecurity risks could adversely affect our business and disrupt our operations.

The threats to network and data security are increasingly diverse and sophisticated. Despite our efforts and processes to prevent breaches, our devices, as well as our servers, computer systems, and those of third parties that we use in our operations are vulnerable to cybersecurity risks, including cyber-attacks such as viruses and worms, phishing attacks, denial-of-service attacks, physical or electronic break-ins, employee theft or misuse, and similar disruptions from unauthorized tampering with our servers and computer systems or those of third parties that we use in our operations, which could lead to interruptions, delays, loss of critical data, unauthorized access to user data, and loss of consumer confidence. In addition, we may be the target of email scams that attempt to acquire personal information or company assets. Despite our efforts to create security barriers to such threats, we may not be able to entirely mitigate these risks. Any cyber-attack that attempts to obtain our or our users' data and assets, disrupt our service, or otherwise access our systems, or those of third parties we use, if successful, could adversely affect our business, operating results, and financial condition, be expensive to remedy, and damage our reputation. In addition, any such breaches may result in negative publicity, adversely affect our brand, decrease demand for our products and services, and adversely affect our operating results and financial condition.

Any material disruption of our information technology systems, or those of third-party partners and data center providers could materially damage user and business partner relationships, and subject us to significant reputational, financial, legal, and operational consequences.

We depend on our information technology systems, as well as those of third parties, to develop new products and services, operate our website, host and manage our services, store data, process transactions, respond to user inquiries, and manage inventory and our supply chain. Any material disruption or slowdown of our systems or those of third parties whom we depend upon, including a disruption or slowdown caused by our failure to successfully manage significant increases in user volume or successfully upgrade our or their systems, system failures, or other causes, could cause outages or delays in our services, which could harm our brand and adversely affect our operating results. In addition, such disruption could cause information, including data related to orders, to be lost or delayed which could---especially if the disruption or slowdown occurred during the holiday season---result in delays in the delivery of products to stores and users or lost sales, which could reduce demand for our merchandise, harm our brand and reputation, and cause our revenue to decline. Problems with our third-party data center service providers, the telecommunications network providers with whom they contract, or with the systems by which telecommunications providers allocate capacity among their users could adversely affect the experience of our users. Our third-party data center service providers could decide to close their facilities or cease providing us services without adequate notice. Any changes in third-party service levels at our data centers or any errors, defects, disruptions, or other performance problems with our platform could harm our brand and may damage the data of our users. If changes in technology cause our information systems, or those of third parties whom we depend upon, to become obsolete, or if our or their information systems are inadequate to handle our growth, we could lose users and our business and operating results could be adversely affected.

Our failure or inability to protect our intellectual property rights, or claims by others that we are infringing upon or unlawfully using their intellectual property could diminish the value of our brand and weaken our competitive position, and adversely affect our business, financial condition, operating results, and prospects.

We currently rely on a combination of patent, copyright, trademark, trade secret, and unfair competition laws, as well as confidentiality agreements and procedures and licensing arrangements, to establish and protect our intellectual property rights. We have devoted substantial resources to the development of our proprietary technologies and related processes. In order to protect our proprietary technologies and processes, we rely in part on trade secret laws and confidentiality agreements with our employees, licensees, independent contractors, commercial partners, and other advisors. These agreements may not effectively prevent disclosure of confidential information and may not provide an adequate remedy in the event of unauthorized disclosure of confidential information. We cannot be certain that the steps taken by us to protect our intellectual property rights will be adequate to prevent infringement of such rights by others, including imitation of our products and misappropriation of our brand. Additionally, the process of obtaining patent or trademark protection is expensive and time-consuming, and we may not be able to file, apply for or prosecute all necessary or desirable patent applications or trademark applications at a reasonable cost or in a timely manner. We have obtained and applied for U.S. and foreign trademark registrations for the "Fitbit" brand and a variety of our product names, and will continue to evaluate the registration of additional trademarks as appropriate. However, we cannot guarantee that any of our pending trademark or patent applications will be approved by the applicable governmental authorities. Moreover, intellectual property protection may be unavailable or limited in some foreign countries where laws or law enforcement practices may not protect our intellectual property rights as fully as in the United States, and it may be more difficult for us to successfully challenge the use of our intellectual property rights by other parties in these countries. Costly and time-consuming litigation could be necessary to enforce and determine the scope of our proprietary rights, and our failure or inability to obtain or maintain trade secret protection or otherwise protect our proprietary rights could adversely affect our business.

We are and may in the future be subject to patent infringement and trademark claims and lawsuits in various jurisdictions, and we cannot be certain that our products or activities do not violate the patents, trademarks, or other intellectual property rights of third-party claimants. Companies in the technology industry and other patent, copyright, and trademark holders seeking to profit from royalties in connection with grants of licenses own large numbers of patents, copyrights, trademarks, domain names, and trade secrets and frequently commence litigation based on allegations of infringement, misappropriation, or other violations of intellectual property or other rights. Companies and individuals may also be subject to criminal prosecution for trade secret theft under 18 U.S.C. section 1832. As we face increasing competition, the intellectual property rights claims against us and asserted by us have grown and will likely continue to grow. For example, we had been involved in litigation with Jawbone and under a related federal criminal investigation concerning alleged theft of Jawbone's trade secrets, which is described in Note 6, "Commitments and Contingencies" in the notes to our consolidated financial statements. In addition, on June 14, 2018, the six former Jawbone employees who were named as individual defendants in the state trade secret case were charged in a federal indictment with being in possession of certain Jawbone trade secrets.

We intend to vigorously defend and prosecute these litigation matters and, based on our review, we believe we have valid defenses and claims with respect to each of these matters. However, litigation is inherently uncertain, and any judgment or injunctive relief entered against us or any adverse settlement could materially and adversely impact our business, financial condition, operating results, and prospects. In addition, litigation can involve significant management time and attention and can be expensive, regardless of outcome. During the course of these litigation matters, there may be announcements of the results of hearings and motions, and other interim developments related to the litigation matters. If securities analysts or investors regard these announcements as negative, the market price of our Class A common stock may decline.

Further, from time to time, we have received and may continue to receive letters from third parties alleging that we are infringing upon their intellectual property rights. Successful infringement claims against us could result in significant monetary liability, prevent us from selling some of our products and services, or require us to change our branding. In addition, resolution of claims may require us to redesign our products, license rights from third parties at a significant expense, or cease using those rights altogether. We have also in the past and may in the future bring claims against third parties for infringing our intellectual property rights. Costs of supporting such litigation and disputes may be considerable, and there can be no assurances that a favorable outcome will be obtained. Patent infringement, trademark infringement, trade secret misappropriation, and other intellectual property claims and proceedings brought against us or brought by us, whether successful or not, could require significant attention of our management and resources and have in the past and could further result in substantial costs, harm to our brand, and have an adverse effect on our business.

We are regularly subject to general litigation, regulatory disputes, and government inquiries.

We are regularly subject to claims, lawsuits, including potential class actions, government investigations, and other proceedings involving competition and antitrust, intellectual property, privacy, consumer protection, accessibility claims, securities, tax, labor and employment, commercial disputes, and other matters. The number and significance of these disputes and inquiries have increased as our company has grown larger, our business has expanded in scope and geographic reach, and our products and services have increased in complexity.

The outcome and impact of such claims, lawsuits, government investigations, and proceedings cannot be predicted with certainty. Regardless of the outcome, such investigations and proceedings can have an adverse impact on us because of legal costs, diversion of management resources, and other factors. Determining reserves for our pending litigation is a complex, fact-intensive process that is subject to judgment calls. It is possible that a resolution of one or more such proceedings could require us to make substantial payments to satisfy judgments, fines, or penalties or to settle claims or proceedings, any of which could harm our business. These proceedings could also result in reputational harm, criminal sanctions, or orders preventing us from offering certain products, or services, or requiring a change in our business practices in costly ways, or requiring development of non-infringing or otherwise altered products or technologies. Any of these consequences could harm our business.

We may experience difficulties managing our cloud infrastructure migration.

We recently announced our move to the Google Cloud Platform. Cloud infrastructure migrations are complex, time-consuming, and can involve substantial expenditures. Our cloud service is critical to accurately maintain data, books and records, or otherwise operate our business; any such implementation involves risks inherent in the conversion to a new system, including loss of information and potential disruption to our normal operations. We may discover deficiencies in our design or implementation or maintenance of the new cloud system that could adversely affect our ability to accurately maintain data, books and records, or otherwise operate our business.

The market for wearable devices is still evolving and if it does not continue to grow, grows more slowly than we expect, or fails to grow as large as we expect, our business and operating results would be harmed.

The market for wearable devices, which includes both connected health and fitness trackers and smartwatches, is still evolving and it is uncertain whether wearable devices will sustain high levels of demand and wide market acceptance. Our success will depend to a substantial extent on the willingness of people to widely adopt these products and services. In part, adoption of our products and services will depend on the increasing prevalence of wearable devices driven by the introduction of new form factors, related software services and other offerings. However, it is not certain whether consumers will respond to these new form factors, and if our offerings fail to satisfy consumer preferences, our business may be adversely affected.

Furthermore, some individuals may be reluctant or unwilling to use wearable devices because they have concerns regarding the risks associated with data privacy and security. If the wider public does not perceive the benefits of our wearable devices or chooses not to adopt them as a result of concerns regarding privacy or data security or for other reasons, then the market for these products and services may not further develop, it may develop more slowly than we expect, or it may not achieve the growth potential we expect it to, any of which would adversely affect our operating results. The development and growth of this market may not be sustained.

Our activation metric is only an indicator of potential repeat behavior. Therefore, you should not rely on the activation metric as a guarantee of repeat purchasing behavior.

Our activation metric tracks the first instance of a Fitbit device (excluding Aria, Aria 2, Flyer and other accessories) pairing to a user account during the three months ending on the date of measurement, as well as Fitbit users who previously activated another Fitbit device to his or her account.

The activation metric is only an indicator of potential repeat behavior. Actual repeat purchase behavior may depend on a number of factors, including but not limited to our ability to anticipate and satisfy consumer preferences. Therefore, you should not rely on our activation metric as a guarantee of repeat purchase behavior.

See the sections titled, “Management’s Discussion and Analysis of Financial Condition and Results of Operations-Key Business Metrics-Activations” in this Periodic Report on Form 10-Q for additional information.

Our business and products are subject to a variety of additional U.S. and foreign laws and regulations that are central to our business; our failure to comply with these laws and regulations could harm our business or our operating results.

We are or may become subject to a variety of laws and regulations in the United States and abroad that involve matters central to our business, including laws and regulations regarding consumer protection, advertising, privacy, intellectual property, manufacturing, anti-bribery and anti-corruption, and economic or other trade prohibitions or sanctions.

The manufacturing, labeling, distribution, importation, marketing, and sale of our products are subject to extensive regulation by various U.S. state and federal and foreign agencies, including the U.S. Consumer Product Safety Commission, or CPSC, FTC, FDA, Federal Communications Commission, and state attorneys general, as well as by various other federal, state, provincial, local, and international regulatory authorities in the countries in which our products and services are manufactured, distributed marketed or sold. If we fail to comply with any of these regulations, we could become subject to enforcement actions or the imposition of significant monetary fines, other penalties, or claims, which could harm our operating results or our ability to conduct our business.

The global nature of our business operations also create various domestic and foreign regulatory challenges and subject us to laws and regulations such as the U.S. Foreign Corrupt Practices Act, or FCPA, the U.K. Bribery Act, and similar anti-bribery and anti-corruption laws in other jurisdictions, and our products are also subject to U.S. export controls, including the U.S. Department of Commerce's Export Administration Regulations and various economic and trade sanctions regulations established by the Treasury Department's Office of Foreign Assets Controls. If we become liable under these laws or regulations, we may be forced to implement new measures to reduce our exposure to this liability. This may require us to expend substantial resources or to discontinue certain products or services, which would negatively affect our business, financial condition, and operating results. In addition, the increased attention focused upon liability issues as a result of lawsuits, regulatory proceedings, and legislative proposals could harm our brand or otherwise impact the growth of our business. Any costs incurred as a result of compliance or other liabilities under these laws or regulations could harm our business and operating results.

Our international operations subject us to additional costs and risks, and our continued expansion internationally may not be successful.

We have entered into many international markets in a relatively short time and may enter into additional markets in the future. Outside of the United States, we currently have operations in Australia and a number of countries in Asia and Europe. There are significant costs and risks inherent in conducting business in international markets, including:

- establishing and maintaining effective controls at foreign locations and the associated increased costs;
- adapting our technologies, products, and services to non-U.S. consumers' preferences and customs;
- variations in margins by geography;
- increased competition from local providers of similar products;
- longer sales or collection cycles in some countries;
- compliance with foreign laws and regulations;
- compliance with the laws of numerous taxing jurisdictions where we conduct business, potential double taxation of our international earnings, and potentially adverse tax consequences due to U.S. and foreign tax laws as they relate to our international operations;
- compliance with anti-bribery laws, such as the FCPA and the U.K. Bribery Act, by us, our employees, and our business partners;
- complexity and other risks associated with current and future foreign legal requirements, including legal requirements related to consumer protection, consumer product safety, and data privacy frameworks, such as the GDPR, and any applicable privacy and data protection laws in foreign jurisdictions where we currently conduct business or intend to conduct business in the future;
- currency exchange rate fluctuations and related effects on our operating results;
- economic and political instability in some countries, particularly those in China where we have expanded;
- the uncertainty of protection for intellectual property rights in some countries and practical difficulties of enforcing rights abroad;
- tariffs and customs duties and the classification of our products by applicable governmental bodies; and
- other costs of doing business internationally.

Our products are manufactured overseas and imported into the United States, the European Union, and other countries and may be subject to duties, tariffs and anti-dumping penalties imposed by applicable customs authorities. Those duties and tariffs are based on the classification of each of our products and is routinely subject to review by the applicable customs authorities. We are unable to predict whether those authorities will agree with our classifications and if those authorities do not agree with our classifications additional duties, tariffs or other trade restrictions may be imposed on the importation of our products. Such actions could result in increases in the cost of our products generally and might adversely affect our sales and profitability.

These factors and other factors could harm our international operations and, consequently, materially impact our business, operating results, and financial condition. Further, we may incur significant operating expenses as a result of our international expansion, and it may not be successful. We have limited experience with regulatory environments and market practices internationally, and we may not be able to penetrate or successfully operate in new markets. We may also encounter difficulty expanding into new international markets because of limited brand recognition in certain parts of the world, leading to delayed acceptance of our products and services by users in these new international markets. If we are unable to continue to expand internationally and manage the complexity of our global operations successfully, our financial condition and operating results could be adversely affected.

To date, we have derived substantially all of our revenue from sales of our wearable devices, and sales of our subscription-based premium services have historically accounted for less than 1% of our revenue.

To date, substantially all of our revenue has been derived from sales of our wearable devices, and we expect to continue to derive the substantial majority of our revenue from sales of these devices for the foreseeable future. In 2016 and 2017, we derived less than 1% of our revenue from sales of our subscription-based premium services. However, in the future we plan to increase sales of subscriptions to these services. For example, in October 2017, we launched Fitbit Coach, our premium guidance and coaching paid offering, and we intend to further build out our recurring non-device revenue offerings, such as with a premium experience that offers additional features, insights and programs. If consumer reception is unfavorable or we are unable to successfully sell and market our premium services, we may be deprived of a potentially significant source of revenue in the future. In addition, sales of our premium services may lead to additional sales of our wearable devices and user engagement with our platform. As a result, our future growth and financial performance may depend, in part, on our ability to sell more subscriptions to our premium services.

An economic downturn or economic uncertainty may adversely affect consumer discretionary spending and demand for our products and services.

Our products and services may be considered discretionary items for consumers. Factors affecting the level of consumer spending for such discretionary items include general economic conditions, and other factors, such as consumer confidence in future economic conditions, fears of recession, the availability and cost of consumer credit, levels of unemployment, and tax rates. As global economic conditions continue to be volatile or economic uncertainty remains, including economic conditions resulting from recent volatility in European markets, trends in consumer discretionary spending also remain unpredictable and subject to reductions. Unfavorable economic conditions may lead consumers to delay or reduce purchases of our products and services and consumer demand for our products and services may not grow as we expect. Our sensitivity to economic cycles and any related fluctuation in consumer demand for our products and services may have an adverse effect on our operating results and financial condition.

Our financial performance is subject to risks associated with changes in the value of the U.S. dollar versus local currencies.

Our primary exposure to movements in foreign currency exchange rates relates to non-U.S. dollar denominated sales and operating expenses worldwide. Weakening of foreign currencies relative to the U.S. dollar adversely affects the U.S. dollar value of our foreign currency-denominated sales and earnings, and generally leads us to raise international pricing, potentially reducing demand for our products. In some circumstances, for competitive or other reasons, we may decide not to raise local prices to fully offset the strengthening of the U.S. dollar, or at all, which would adversely affect the U.S. dollar value of our foreign currency denominated sales and earnings. Conversely, a strengthening of foreign currencies relative to the U.S. dollar, while generally beneficial to our foreign currency-denominated sales and earnings, could cause us to reduce international pricing, incur losses on our foreign currency derivative instruments, and incur increased operating expenses, thereby limiting any benefit. Additionally, strengthening of foreign currencies may also increase our cost of product components denominated in those currencies, thus adversely affecting gross margins.

We use derivative instruments, such as foreign currency forward contracts, to hedge certain exposures to fluctuations in foreign currency exchange rates. The use of such hedging activities may not offset any, or more than a portion, of the adverse financial effects of unfavorable movements in foreign exchange rates over the limited time the hedges are in place. In addition, our counterparties may be unable to meet the terms of the agreements. We seek to mitigate this risk by limiting counterparties to major financial institutions and by spreading the risk across several major financial institutions.

Changes in our tax rates or exposure to additional tax liabilities could adversely affect our earnings and financial condition.

We are subject to income taxes in the United States and foreign jurisdictions in which we do business. These foreign jurisdictions have statutory tax rates different from those in the United States. Accordingly, our provision for income taxes is subject to volatility and could be adversely affected by earnings being lower than anticipated in countries where we have lower statutory rates and higher than anticipated in countries where we have higher statutory rates, by changes in foreign currency exchange rates, or by changes in the relevant tax, accounting, and other laws, regulations, principles, and interpretations, or by changes in the valuation of our deferred tax assets and liabilities. As we operate in numerous taxing jurisdictions, the application of tax laws can be subject to diverging and sometimes conflicting interpretations by tax authorities of these jurisdictions.

Uncertainties in the interpretation and application of the 2017 Tax Cuts and Jobs Act could materially affect our tax obligations and effective tax rate.

On December 22, 2017, the U.S. Tax Cuts and Jobs Act of 2017, or the 2017 Tax Act, was signed into law and includes several key tax provisions that affected us, including a reduction of the statutory corporate tax rate from 35% to 21% effective for tax years beginning after December 31, 2017, elimination of certain deductions, and changes to how the United States imposes income tax on multinational corporations, among others. The 2017 Tax Act requires complex computations to be performed that were not previously required in U.S. tax law, and preparation and analysis of information not previously required or regularly produced which will require significant judgment in interpreting accounting guidance for such items that is currently uncertain. We have provided our best estimate of the impact of the 2017 Tax Act in our year-end income tax provision in accordance with our understanding of the 2017 Tax Act. However, the interpretation of issued or future guidance on how provisions of the 2017 Tax Act will be applied or otherwise administered by the U.S. Treasury Department, the Internal Revenue Services, and other standard-setting bodies could be different from our interpretation. As additional regulatory guidance is issued by the applicable taxing authorities, as accounting treatment is clarified, as we perform additional analysis on the application of the law, and as we refine estimates in calculating the effect, our final analysis, which will be recorded in the period completed, may be different from our current provisional amounts, which could materially affect our tax obligations and effective tax rate. In addition, foreign governments may enact tax laws in response to the 2017 Tax Act that could result in further changes to global taxation that may affect our financial position and results of operations in the future.

If we are unable to protect our domain names, our brand, business, and operating results could be adversely affected.

We have registered domain names for websites, or URLs, that we use in our business, such as Fitbit.com. If we are unable to maintain our rights in these domain names, our competitors or other third parties could capitalize on our brand recognition by using these domain names for their own benefit. In addition, although we own the “Fitbit” domain name under various global top level domains such as .com and .net, as well as under various country-specific domains, we might not be able to, or may choose not to, acquire or maintain other country-specific versions of the “Fitbit” domain name or other potentially similar URLs. The regulation of domain names in the United States and elsewhere is generally conducted by Internet regulatory bodies and is subject to change. If we lose the ability to use a domain name in a particular country, we may be forced to either incur significant additional expenses to market our solutions within that country, including the development of a new brand and the creation of new promotional materials, or elect not to sell our solutions in that country. Either result could substantially harm our business and operating results. Regulatory bodies could establish additional top-level domains, appoint additional domain name registrars, or modify the requirements for holding domain names. As a result, we may not be able to acquire or maintain the domain names that utilize the name “Fitbit” in all of the countries in which we currently conduct or intend to conduct business. Further, the relationship between regulations governing domain names and laws protecting trademarks and similar proprietary rights varies among jurisdictions and is unclear in some jurisdictions. Domain names similar to ours have already been registered in the United States and elsewhere, and we may be unable to prevent third parties from acquiring and using domain names that infringe, are similar to, or otherwise decrease the value of, our brand or our trademarks. Protecting and enforcing our rights in our domain names and determining the rights of others may require litigation, which could result in substantial costs, divert management attention, and not be decided favorably to us.

Our use of “open source” software could negatively affect our ability to sell our products and subject us to possible litigation.

A portion of the technologies we use incorporates “open source” software, and we may incorporate open source software in the future. From time to time, companies that incorporate open source software into their products have faced claims challenging the ownership of open source software or compliance with open source license terms. Therefore, we could be subject to suits by parties claiming ownership of what we believe to be open source software or noncompliance with open source licensing terms. Some open source licenses may subject us to certain unfavorable conditions, including requirements that we offer our products and services that incorporate the open source software for no cost or that we make publicly available all or part of the source code for modifications or derivative works. Additionally, if a third-party software provider has incorporated open source software into software that we license or obtain from such provider, we could be required to disclose or provide at no cost all or part of our source code that incorporates such licensed software. If a copyright holder that distributes open source software that we use or license or other third party were to allege that we had not complied with the conditions of the applicable license, we could be required to incur significant legal expenses defending against such allegations and may be required to release portions of our proprietary source code, subject to significant damages, re-engineer our products and services, enjoined from the sale of our products and services that contained the open source software if re-engineering our products or services cannot be accomplished on a timely basis, or take other remedial action that may divert resources away from our development efforts. Any of the foregoing could disrupt the distribution and sale of our products and services and harm our business.

We may engage in merger and acquisition activities, which could require significant management attention, disrupt our business, dilute stockholder value, and adversely affect our operating results.

As part of our business strategy, we may make investments in other companies, products, or technologies. For example, in 2016, we acquired assets from Coin, Inc., Pebble Industries, Inc., and Vector Watch S.R.L and in 2018 we acquired Twine Health. We may not be able to find suitable acquisition candidates and we may not be able to complete acquisitions on favorable terms, if at all. If we do complete acquisitions, we may not ultimately strengthen our competitive position or achieve our goals, and any acquisitions we complete could be viewed negatively by users or investors. In addition, if we fail to successfully integrate such acquisitions, or the technologies associated with such acquisitions, into our company, the revenue and operating results of the combined company could be adversely affected.

Acquisitions may disrupt our ongoing operations, divert management from their primary responsibilities, subject us to additional liabilities, increase our expenses, and adversely impact our business, financial condition, operating results, and cash flows. We may not successfully evaluate or utilize the acquired technology and accurately forecast the financial impact of an acquisition transaction, including accounting charges. We would have to pay cash, incur debt, or issue equity securities to pay for any such acquisition, each of which may affect our financial condition or the value of our capital stock and could result in dilution to our stockholders. If we incur more debt it would result in increased fixed obligations and could also subject us to covenants or other restrictions that would impede our ability to manage our operations. Additionally, we may receive indications of interest from other parties interested in acquiring some or all of our business. The time required to evaluate such indications of interest could require significant attention from management, disrupt the ordinary functioning of our business, and adversely affect our operating results.

There have been reports that some users of certain of our devices have experienced skin irritations, which could result in additional negative publicity or otherwise harm our business. In addition, some of our users have filed personal injury lawsuits against us relating to certain of our devices, which could divert management's attention from our operations and result in substantial legal fees and other costs.

Due to the nature of some of our wearable devices, some users have had in the past and may in the future experience skin irritations or other biocompatibility issues not uncommon with jewelry or other wearable products that stay in contact with skin for extended periods of time. There have been reports of some users of certain of our devices experiencing skin irritations. This negative publicity could harm sales of our products and also adversely affect our relationships with retailers that sell our products, including causing them to be reluctant to continue to sell our products. In addition, in the past, some of our users have filed personal injury lawsuits against us arising out of such claims relating to certain of our devices. While we do not believe that these lawsuits are material, due to the inherent uncertainties of litigation, we cannot accurately predict the ultimate outcome of any proceedings arising from such claims, and these actions or other third-party claims against us may result in the diversion of our management's time and attention from other aspects of our business and may cause us to incur substantial litigation or settlement costs. If large numbers of users experience these problems, we could be subject to enforcement actions or the imposition of significant monetary fines, other penalties, or proceedings by the CPSC or other U.S. or foreign regulatory agencies and face additional personal injury or class action litigation, any of which could have a material adverse impact on our business, financial condition, and operating results.

We may be subject to CPSC recalls, regulatory proceedings and litigation in various jurisdictions, including multi-jurisdiction federal and state class action and personal injury claims, which may require significant management attention and disrupt our business operations, and adversely affect our financial condition, operating results, and our brand.

We face product liability, product safety and product compliance risks relating to the marketing, sale, use, and performance of our products. The products we sell must be designed and manufactured to be safe for their intended purposes. Certain of our products must comply with certain federal and state laws and regulations. For example, all of our products are subject to the Consumer Product Safety Act and the Consumer Product Safety Improvement Act, which empower the CPSC. The CPSC is empowered to take action against hazards presented by consumer products, up to and including product recalls. We are required to report certain incidents related to the safety and compliance of our products to the CPSC, and failure to do so could result in a civil penalty.

Our products may, from time to time, be subject to recall for product safety and compliance reasons. For example, in March 2014, we recalled one of our products, the Fitbit Force, after some of our users experienced allergic reactions to adhesives in the wristband. These reactions included skin irritation, rashes, and blistering. The recall had a negative impact on our operating results, primarily in our fourth quarter of 2013, the first quarter of 2014, and the fourth quarter of 2015. We have provided and are continuing to provide full refunds to consumers who return the Fitbit Force. If returns of the Fitbit Force or other costs related to the recall are higher than anticipated, we will be required to increase our reserves related to the recall which would negatively impact our operating results in the future.

The recall was conducted in conjunction with the CPSC, which monitored recall effectiveness and compliance. In addition to the financial impacts discussed elsewhere in this Annual Report on Form 10-K, this recall required us to collect a significant amount of information for the CPSC, which takes significant time and internal and external resources.

A large number of lawsuits, including multi-jurisdiction complex federal and state class action and personal injury claims, were filed against us relating to the Fitbit Force. These litigation matters required significant attention of our management and resources and disrupted the ordinary course of our business operations. We have settled all of the class action lawsuits and related individual personal injury claims. In the fourth quarter of 2015, we received proceeds from the insurance policies that apply to these claims and related legal fees, and we recorded an accrual for liabilities arising under these claims that was immaterial and falls within the amount of the insurance proceeds received.

In addition, the CPSC previously conducted an investigation into several of our products. Although the CPSC did not find a substantial product hazard, there can be no assurances that investigations will not be conducted or that product hazards or other defects will not be found in the future with respect to our products. The Fitbit Force product recall, regulatory proceedings, and litigation have had and may continue to have, and any future recalls, regulatory proceedings, and litigation could have an adverse impact on our financial condition, operating results, and brand. Furthermore, because of the global nature of our product sales, in the event we experience defects with respect to products sold outside the United States, we could become subject to recalls, regulatory proceedings, and litigation by foreign governmental agencies and private litigants, which could significantly increase the costs of managing any product issues. Any ongoing and future regulatory proceedings or litigation, regardless of their merits, could further divert management's attention from our operations and result in substantial legal fees and other costs.

Our Aria scales are subject to FDA and corresponding regulations, and sales of this product or future regulated products could be adversely affected if we fail to comply with the applicable requirements.

Medical devices, including our Aria scales, are regulated by the FDA and corresponding state regulatory agencies, and we may have future features or products that are regulated as medical devices by the FDA. The medical device industry in the United States is regulated by governmental authorities, principally the FDA and corresponding state regulatory agencies. Before we can market or sell a new regulated product or make a significant modification to an existing medical device in the United States, we must comply with FDA Quality Management System regulations, and must obtain regulatory clearance or approval from the FDA, unless an exemption from pre-market review applies. In addition, certain future software functionality, whether standalone or embedded in existing or future devices, may be regulated as a medical device and require pre-market review and approval by the FDA. The process of obtaining regulatory clearances or approvals to market a medical device can be costly and time consuming, and we may not be able to obtain these clearances or approvals on a timely basis, or at all, for future products. Any delay in, or failure to receive or maintain, clearance or approval for any medical device products under development could prevent us from generating revenue from these products. Medical devices are also subject to numerous ongoing compliance requirements under the regulations of the FDA and corresponding state regulatory agencies, which can be costly and time consuming. For example, under FDA regulations medical device manufacturers are required to, among other things, (i) establish a quality management system to help ensure that their products consistently meet applicable requirements and specifications, (ii) establish and maintain procedures for receiving, reviewing, and evaluating complaints, (iii) establish and maintain a corrective and preventive action procedure, (iv) report certain device-related adverse events and product problems to the FDA, and (v) report to the FDA the removal or correction of a distributed product. If we experience any product problems requiring reporting to the FDA or if we otherwise fail to comply with applicable FDA regulations or the regulations of corresponding state regulatory agencies, with respect to our Aria scales or future regulated products, we could jeopardize our ability to sell our products and could be subject to enforcement actions such as fines, civil penalties, injunctions, recalls of products, delays in the introduction of products into the market, and refusal of the FDA or other regulators to grant future clearances or approvals, which could harm our reputation, business, operating results, and financial condition.

If we fail to maintain an effective system of disclosure controls and internal control over financial reporting, our ability to produce timely and accurate financial statements or comply with applicable regulations could be impaired.

We are subject to the reporting requirements of the Exchange Act, the Sarbanes-Oxley Act of 2002, or the Sarbanes-Oxley Act, and the rules and regulations of the applicable listing standards of the New York Stock Exchange. We expect that the requirements of these rules and regulations will continue to increase our legal, accounting, and financial compliance costs, make some activities more difficult, time-consuming, and costly, and place strain on our personnel, systems, and resources.

The Sarbanes-Oxley Act requires, among other things, that we maintain effective disclosure controls and procedures and internal control over financial reporting. We are also required to make a formal assessment and provide an annual management report on the effectiveness of our internal control over financial reporting, which must be attested to by our independent registered public accounting firm. In order to maintain the effectiveness of our disclosure controls and procedures and internal control over financial reporting, we have expended, and anticipate that we will continue to expend, resources, including accounting-related costs and management oversight.

As disclosed in Item 4 of this Quarterly Report on Form 10-Q, we did not maintain effective controls over the accuracy of invoicing gross revenue. This represented a material weakness that did not result in the identification of any adjustments to our annual or interim consolidated financial statements. A material weakness is defined as a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis. As a result of the material weakness identified, our management concluded that our internal control over financial reporting was not effective as of December 31, 2017. Management has identified and implemented changes to our internal control over financial reporting to remediate the control deficiencies that led to this material weakness. However, we cannot assure you that remediation efforts will be effective, and the enhanced controls and procedures could require increased management time and attention and resources.

Additional current controls and any new controls that we develop may become inadequate because of changes in conditions in our business. Further, additional weaknesses in our disclosure controls and internal control over financial reporting may be discovered in the future. Any failure to maintain or develop effective controls or any difficulties encountered in their implementation or improvement could harm our operating results or cause us to fail to meet our reporting obligations and may result in a restatement of our financial statements for prior periods. Any failure to maintain effective internal control over financial reporting also could adversely affect the results of periodic management evaluations and annual independent registered public accounting firm attestation reports regarding the effectiveness of our internal control over financial reporting. Ineffective disclosure controls and procedures and internal control over financial reporting could also cause investors to lose confidence in our reported financial and other information, which would likely have a negative effect on the trading price of our Class A common stock. In addition, if we are unable to continue to meet these requirements, we may not be able to remain listed on the New York Stock Exchange.

Our business is subject to the risk of political events, war, terrorism, other business interruptions, earthquakes, fire, power outages, floods, and other catastrophic events.

War, terrorism, geopolitical uncertainties, trade restrictions, public health issues, natural disasters and other business interruptions have caused and may cause damage or disruption to the economy and commerce on a global, regional or country-specific basis, which could have a material adverse effect on our business, our customers, and companies with which we do business. For example, the Trump Administration recently signaled that it may alter trade terms between China and the United States, including limiting trade with China and/or imposing tariffs on imports from China. Political uncertainty surrounding these trade terms could have a negative effect on consumer confidence and spending, which could adversely affect our business.

Our business is also vulnerable to damage or interruption from earthquakes, fires, floods, power losses, telecommunications failures, human errors, break-ins, and similar events. The third-party systems and operations and contract manufacturers we rely on, such as the data centers we lease, are subject to similar risks. For example, a significant natural disaster, such as an earthquake, fire, or flood, could have an adverse effect on our business, operating results, and financial condition, and our insurance coverage may be insufficient to compensate us for losses that may occur. Our corporate offices and one of our data center facilities are located in California, a state that frequently experiences earthquakes. In addition, the facilities at which our contract manufacturers manufacture our products are located in parts of Asia that frequently endure typhoons and earthquakes. Acts of terrorism, which may be targeted at metropolitan areas that have higher population density than rural areas, could also cause disruptions in our or our suppliers', contract manufacturers', and logistics providers' businesses or the economy as a whole. We may not have sufficient protection or recovery plans in some circumstances, such as natural disasters affecting California or other locations where we have data centers or store significant inventory of our products. As we rely heavily on our data center facilities, computer and communications systems, and the Internet to conduct our business and provide high-quality customer service, these disruptions could negatively impact our ability to run our business and either directly or indirectly disrupt suppliers' businesses, which could have an adverse effect on our business, operating results, and financial condition.

If our estimates or judgments relating to our critical accounting policies prove to be incorrect, our operating results could be adversely affected.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, as provided in "Management's Discussion and Analysis of Financial Condition and Results of Operations" in this Annual Report on Form 10-K. The results of these estimates form the basis for making judgments about the carrying values of assets, liabilities, and equity, and the amount of revenue and expenses that are not readily apparent from other sources. Significant assumptions and estimates used in preparing our consolidated financial statements include those related to revenue recognition, inventories, product warranty reserves, business combinations, accounting for income taxes, and stock-based compensation expense. Our operating results may be adversely affected if our assumptions change or if actual circumstances differ from those in our assumptions, which could cause our operating results to fall below the expectations of securities analysts and investors, resulting in a decline in the price of our Class A common stock.

Our revolving credit facility provides our lenders with first-priority liens against substantially all of our assets, excluding our intellectual property, and contains financial covenants and other restrictions on our actions, which could limit our operational flexibility and otherwise adversely affect our financial condition.

In December 2015, we amended and restated our existing revolving credit facility and revolving credit and guarantee agreement into one senior credit facility. We further amended this agreement in May 2017. Our credit agreement restricts our ability to, among other things:

- use our accounts receivable, inventory, trademarks, and most of our other assets as security in other borrowings or transactions;
- incur additional indebtedness;
- sell certain assets;
- guarantee certain obligations of third parties;
- declare dividends or make certain distributions; and
- undergo a merger or consolidation or other transactions.

Our credit agreement requires us to maintain a minimum liquidity reserve. Our ability to comply with these and other covenants is dependent upon a number of factors, some of which are beyond our control.

Our failure to comply with the covenants or payment requirements, or the occurrence of other events specified in our credit agreement, could result in an event of default under the credit agreement, which would give our lenders the right to terminate their commitments to provide additional loans under the credit agreement and to declare all borrowings outstanding, together with accrued and unpaid interest and fees, to be immediately due and payable. In addition, we have granted our lenders first-priority liens against all of our assets, excluding our intellectual property, as collateral. Failure to comply with the covenants or other restrictions in the credit agreement could result in a default. If the debt under our credit agreement was to be accelerated, we may not have sufficient cash on hand or be able to sell sufficient collateral to repay it, which would have an immediate adverse effect on our business and operating results. This could potentially cause us to cease operations and result in a complete loss of your investment in our Class A common stock.

We are exposed to fluctuations in the market values of our investments.

Credit ratings and pricing of our investments can be negatively affected by liquidity, credit deterioration, financial results, economic risk, political risk, sovereign risk, changes in interest rates, or other factors. As a result, the value and liquidity of our cash, cash equivalents, and marketable securities may fluctuate substantially. Therefore, although we have not realized any significant losses on our cash, cash equivalents, and marketable securities, future fluctuations in their value could result in a significant realized loss, which could materially adversely affect our financial condition and operating results.

Regulations related to conflict minerals may cause us to incur additional expenses and could limit the supply and increase the costs of certain metals used in the manufacturing of our products.

We are subject to requirements under the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, which will require us to conduct due diligence on and disclose whether or not our products contain conflict minerals. The implementation of these requirements could adversely affect the sourcing, availability, and pricing of the materials used in the manufacture of components used in our products. In addition, we will incur additional costs to comply with the disclosure requirements, including costs related to conducting diligence procedures to determine the sources of minerals that may be used or necessary to the production of our products and, if applicable, potential changes to products, processes, or sources of supply as a consequence of such due diligence activities. It is also possible that we may face reputational harm if we determine that certain of our products contain minerals not determined to be conflict free or if we are unable to alter our products, processes, or sources of supply to avoid such materials.

Risks Related to Ownership of Our Class A Common Stock

The market price of our Class A common stock has been and will likely continue to be volatile, and you could lose all or part of your investment.

The market price of our Class A common stock has been, and will likely continue to be, volatile. Since shares of our Class A common stock were sold in our IPO in June 2015 at a price of $20.00 per share, our stock price has ranged from $4.51 to $51.90 through September 29, 2018 . In addition, the trading prices of the securities of technology companies in general have been highly volatile.

The market price of our Class A common stock may continue to fluctuate significantly in response to numerous factors, many of which are beyond our control, including:

- overall performance of the equity markets;
- actual or anticipated fluctuations in our revenue and other operating results;
- changes in the financial projections we may provide to the public or our failure to meet these projections;
- failure of securities analysts to initiate or maintain coverage of us, changes in financial estimates by any securities analysts who follow our company, or our failure to meet these estimates or the expectations of investors;
- recruitment or departure of key personnel;
- the economy as a whole and market conditions in our industry;
- negative publicity related to problems in our manufacturing or the real or perceived quality of our products, as well as the failure to timely launch new products that gain market acceptance;
- rumors and market speculation involving us or other companies in our industry;
- announcements by us or our competitors of significant technical innovations, acquisitions, strategic partnerships, joint ventures, or capital commitments;
- new laws or regulations or new interpretations of existing laws or regulations applicable to our business;
- lawsuits threatened or filed against us;
- other events or factors, including those resulting from war, incidents of terrorism, or responses to these events; and
- sales of shares of our Class A common stock by us or our stockholders.

In addition, the stock markets have experienced extreme price and volume fluctuations that have affected and continue to affect the market prices of equity securities of many companies. Stock prices of many companies have fluctuated in a manner unrelated or disproportionate to the operating performance of those companies. We are currently subject to securities litigation, which is described in Note 6, “Commitments and Contingencies” in the notes to our consolidated financial statements. This or any future securities litigation could subject us to substantial costs, divert resources and the attention of management from our business, and adversely affect our business.

Sales of substantial amounts of our Class A common stock in the public markets, or the perception that they might occur, could cause the market price of our Class A common stock to decline.

Sales of a substantial number of shares of our Class A common stock into the public market, particularly sales by our directors, executive officers, and principal stockholders, or the perception that these sales might occur, could cause the market price of our Class A common stock to decline.

As of September 29, 2018 , there were 247.6 million shares of Class A and Class B common stock outstanding. All shares of our common stock are available for sale in the public market, subject in certain cases to volume limitations under Rule 144 under the Securities Act of 1933, as amended, or the Securities Act, various vesting agreements, as well as our insider trading policy.

In addition, as of September 29, 2018 , we had stock options outstanding that, if fully exercised, would result in the issuance of 1.5 million shares of Class A common stock and 17.0 million shares of Class B common stock (which shares of Class B common stock generally convert to Class A common stock upon their sale or transfer). We also had restricted stock units, or RSUs, outstanding as of September 29, 2018 that may be settled for 20.7 million shares of Class A common stock and 0.1 million shares of Class B common stock. As of September 29, 2018 , all of the shares issuable upon the exercise of stock options or settlement of RSUs and the shares reserved for future issuance under our equity incentive plans, are registered for public resale under the Securities Act. Accordingly, these shares may be freely sold in the public market upon issuance subject to applicable vesting requirements.

In addition, certain holders of our capital stock have rights, subject to some conditions, to require us to file registration statements for the public resale of their shares or to include such shares in registration statements that we may file for us or other stockholders.

The dual class structure of our common stock has the effect of concentrating voting control with our founders and certain other holders of our Class B common stock, including our directors, executive officers, and significant stockholders. This will limit or preclude your ability to influence corporate matters, including the election of directors, amendments of our organizational documents, and any merger, consolidation, sale of all or substantially all of our assets, or other major corporate transaction requiring stockholder approval.

Our Class B common stock has ten votes per share and our Class A common stock has one vote per share. As of September 29, 2018 , our directors, executive officers, and holders of more than 5% of our common stock, and their respective affiliates, held a substantial majority of the voting power of our capital stock. Because of the ten-to-one voting ratio between our Class B and Class A common stock, our co-founders, who currently serve as our chief executive officer and chief technology officer, control a majority of the combined voting power of our common stock and therefore are able to control all matters submitted to our stockholders for approval until the earlier of June 17, 2027 or the date the holders of a majority of our Class B common stock choose to convert their shares. This concentrated control will limit or preclude your ability to influence corporate matters for the foreseeable future, including the election of directors, amendments of our organizational documents, and any merger, consolidation, sale of all or substantially all of our assets, or other major corporate transaction requiring stockholder approval. In addition, this may prevent or discourage unsolicited acquisition proposals or offers for our capital stock that you may feel are in your best interest as one of our stockholders.

Transfers by holders of Class B common stock will generally result in those shares converting to Class A common stock, subject to limited exceptions, such as certain transfers effected for estate planning purposes. The conversion of Class B common stock to Class A common stock will have the effect, over time, of increasing the relative voting power of those holders of Class B common stock who retain their shares in the long term.

If securities or industry analysts do not publish research, or publish inaccurate or unfavorable research, about our business, the price of our Class A common stock and trading volume could decline.

The trading market for our Class A common stock depends in part on the research and reports that securities or industry analysts publish about us or our business. We do not have any control over these analysts. If industry analysts cease coverage of us, the trading price for our common stock would be negatively affected. If one or more of the analysts who cover us downgrade our Class A common stock or publish inaccurate or unfavorable research about our business, our common stock price would likely decline. If one or more of these analysts' cease coverage of us or fail to publish reports on us regularly, demand for our Class A common stock could decrease, which might cause our Class A common stock price and trading volume to decline.

We do not intend to pay dividends for the foreseeable future.

We have never declared or paid any cash dividends on our common stock and do not intend to pay any cash dividends in the foreseeable future. We anticipate that we will retain all of our future earnings for use in the development of our business and for general corporate purposes. Any determination to pay dividends in the future will be at the discretion of our board of directors. Accordingly, investors must rely on sales of their common stock after price appreciation, which may never occur, as the only way to realize any future gains on their investments. In addition, our credit facility contains restrictions on our ability to pay dividends.

Provisions in our charter documents and under Delaware law could make an acquisition of our company more difficult, limit attempts by our stockholders to replace or remove our current management, limit our stockholders' ability to obtain a favorable judicial forum for disputes with us or our directors, officers, or employees, and limit the market price of our common stock.

Provisions in our restated certificate of incorporation and restated bylaws may have the effect of delaying or preventing a change of control or changes in our management. Our restated certificate of incorporation and restated bylaws include provisions that:

- provide that our board of directors will be classified into three classes of directors with staggered three-year terms at such time as the outstanding shares of our Class B common stock represent less than a majority of the combined voting power of our common stock;
- permit the board of directors to establish the number of directors and fill any vacancies and newly created directorships;
- require super-majority voting to amend some provisions in our restated certificate of incorporation and restated bylaws;
- authorize the issuance of "blank check" preferred stock that our board of directors could use to implement a stockholder rights plan;
- provide that only the chairman of our board of directors, our chief executive officer, or a majority of our board of directors will be authorized to call a special meeting of stockholders;
- provide for a dual class common stock structure in which holders of our Class B common stock have the ability to control the outcome of matters requiring stockholder approval, even if they own significantly less than a majority of the outstanding shares of our Class A and Class B common stock, including the election of directors and significant corporate transactions, such as a merger or other sale of our company or its assets;
- prohibit stockholder action by written consent, which requires all stockholder actions to be taken at a meeting of our stockholders;
- provide that the board of directors is expressly authorized to make, alter, or repeal our bylaws; and
- establish advance notice requirements for nominations for election to our board of directors or for proposing matters that can be acted upon by stockholders at annual stockholder meetings.

In addition, our restated certificate of incorporation provides that the Court of Chancery of the State of Delaware will be the exclusive forum for: any derivative action or proceeding brought on our behalf; any action asserting a breach of fiduciary duty; any action asserting a claim against us arising pursuant to the Delaware General Corporation Law, our restated certificate of incorporation, or our restated bylaws; or any action asserting a claim against us that is governed by the internal affairs doctrine. This choice of forum provision may limit a stockholder's ability to bring a claim in a judicial forum that it finds favorable for disputes with us or any of our directors, officers, or other employees, which may discourage lawsuits with respect to such claims. Alternatively, if a court were to find the choice of forum provision contained in our restated certificate of incorporation to be inapplicable or unenforceable in an action, we may incur additional costs associated with resolving such action in other jurisdictions, which could harm our business, operating results, and financial condition.

Moreover, Section 203 of the Delaware General Corporation Law may discourage, delay, or prevent a change in control of our company. Section 203 imposes certain restrictions on mergers, business combinations, and other transactions between us and holders of 15% or more of our common stock.

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

(a) Sales of Unregistered Securitie s

None.

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Item 6. Exhibit Index

Exhibit Number	Exhibit Description	Incorporated by Reference				Filed Herewith
		Form	File No.	Exhibit	Filing Date	
31.1	Rule 13a-14(a) / 15d-14(a) Certification of Chief Executive Officer.					X
31.2	Rule 13a-14(a) / 15d-14(a) Certification of Chief Financial Officer.					X
32.1#	Section 1350 Certifications of Chief Executive Officer and Chief Financial Officer.					X
101.INS	XBRL Instance Document.					X
101.SCH	XBRL Taxonomy Extension Schema Document.					X
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.					X
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.					X
101.LAB	XBRL Taxonomy Extension Labels Linkbase Document.					X
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.					X

These certifications are deemed not filed for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section, nor shall they be deemed incorporated by reference into any filing under the Securities Act or the Exchange Act.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Quarterly Report on Form 10-Q to be signed on its behalf by the undersigned, thereunto duly authorized.

		FITBIT, INC.
Date:	November 2, 2018	/s/ Ronald W. Kisling
		Ronald W. Kisling
		Chief Financial Officer *(Principal Financial and Accounting Officer)*

EXHIBIT 31.1

CERTIFICATION OF CHIEF EXECUTIVE OFFICER PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, James Park, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Fitbit, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 2, 2018

/s/ James Park

James Park
President, Chief Executive Officer, and Chairman
(Principal Executive Officer)

EXHIBIT 31.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Ronald W. Kisling, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Fitbit, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 2, 2018

/s/ Ronald W. Kisling

Ronald W. Kisling
Chief Financial Officer
(Principal Financial and Accounting Officer)

EXHIBIT 32.1

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

I, James Park, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge, the Quarterly Report on Form 10-Q of Fitbit, Inc. for the fiscal quarter ended September 29, 2018 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and that information contained in such Quarterly Report on Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of Fitbit, Inc.

Date: November 2, 2018	By:	/s/ James Park
		James Park
		President, Chief Executive Officer, and Chairman *(Principal Executive Officer)*

I, Ronald W. Kisling, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge, the Quarterly Report on Form 10-Q of Fitbit, Inc. for the fiscal quarter ended September 29, 2018 fully complies with the requirements of Section 13(a) or 15(d) of the Exchange Act and that information contained in such Quarterly Report on Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of Fitbit, Inc.

Date: November 2, 2018	By:	/s/ Ronald W. Kisling
		Ronald W. Kisling
		Chief Financial Officer *(Principal Financial and Accounting Officer)*