APPLIED MICRO CIRCUITS CORP (AMCC)

10-Q

Quarterly report pursuant to sections 13 or 15(d)
Filed on 11/09/2007
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2007

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: 000-23193

APPLIED MICRO CIRCUITS CORPORATION

(Exact name of registrant as specified in its charter)

Delaware **(State or other jurisdiction of incorporation or organization)**	**94-2586591** **(I.R.S. Employer Identification No.)**
215 Moffett Park Drive, **Sunnyvale, CA** **(Address of principal executive offices)**	**94089** **(Zip code)**

Registrant's telephone number, including area code: (408) 542-8600

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, as amended, 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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☑ Accelerated filer ☐ Non-accelerated filer ☐

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 31, 2007, 273,049,096 shares of the registrant's common stock were issued and outstanding.

APPLIED MICRO CIRCUITS CORPORATION

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

APPLIED MICRO CIRCUITS CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands, except par value)
(unaudited)

	September 30, 2007	March 31, 2007
ASSETS		
Current assets:		
Cash and cash equivalents	$ 48,818	$ 51,595
Short-term investments-available-for-sale	91,500	232,875
Accounts receivable, net	23,218	32,558
Inventories	40,481	31,286
Other current assets	11,830	14,438
Total current assets	215,847	362,752
Marketable securities	77,736	—
Property and equipment, net	25,655	27,150
Goodwill	335,624	335,857
Purchased intangibles, net	67,832	79,787
Other assets	17,152	10,966
Total assets	$ 739,846	$ 816,512
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 14,311	$ 26,893
Accrued payroll and related expenses	7,366	10,021
Other accrued liabilities	14,531	16,383
Deferred revenue	2,399	2,393
Total current liabilities	38,607	55,690
Stockholders' equity:		
Preferred stock, $0.01 par value:		
Authorized shares—2,000, none issued and outstanding	—	—
Common stock, $0.01 par value:		
Authorized shares—630,000 at September 30, 2007 and March 31, 2007 Issued and outstanding shares—272,873 at September 30, 2007 and 282,976 at March 31, 2007	2,729	2,830
Additional paid-in capital	5,923,857	5,954,223
Accumulated other comprehensive income (loss)	(4,419)	224
Accumulated deficit	(5,220,928)	(5,196,455)
Total stockholders' equity	701,239	760,822
Total liabilities and stockholders' equity	$ 739,846	$ 816,512

See Accompanying Notes to Condensed Consolidated Financial Statements

APPLIED MICRO CIRCUITS CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data)
(unaudited)

	Three Months Ended September 30,		Six Months Ended September 30,	
	2007	2006	2007	2006
Net revenues	$ 58,210	$ 76,364	$ 108,345	$ 146,043
Cost of revenues	30,328	35,536	56,826	67,064
Gross profit	27,882	40,828	51,519	78,979
Operating expenses:				
Research and development	24,480	24,853	49,962	47,692
Selling, general and administrative	15,850	16,162	31,913	32,612
Acquired in-process research and development	—	13,300	—	13,300
Amortization of purchased intangible assets	1,336	1,188	2,681	2,295
Restructuring charges	1,376	1,419	1,344	2,666
Option investigation	209	1,150	501	1,700
Total operating expenses	43,251	58,072	86,401	100,265
Operating loss	(15,369)	(17,244)	(34,882)	(21,286)
Interest income, net	2,128	3,254	5,176	6,595
Other income, net	4,778	175	4,806	199
Loss before income taxes	(8,463)	(13,815)	(24,900)	(14,492)
Income tax expense (benefit)	(410)	74	(427)	214
Net loss	$ (8,053)	$ (13,889)	$ (24,473)	$ (14,706)
Basic and diluted net loss per share:				
Net loss per share	$ (0.03)	$ (0.05)	$ (0.09)	$ (0.05)
Shares used in calculating basic and diluted net loss per share	275,132	281,762	278,394	286,470

See Accompanying Notes to Condensed Consolidated Financial Statements

APPLIED MICRO CIRCUITS CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)
(in thousands)

	Six Months Ended September 30,	
	2007	2006
Operating activities:		
Net loss	$ (24,473)	$ (14,706)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities		
Depreciation and amortization	3,227	4,678
Amortization of purchased intangibles	11,956	10,674
Acquired in-process research and development	—	13,300
Stock-based compensation expense:		
Stock options	5,268	5,153
Restricted stock units	649	36
Non-cash restructuring charges (benefit)	(32)	1,977
Net gain on sale of strategic equity investments	(4,649)	
Net gain on disposal of property	(64)	—
Changes in operating assets and liabilities:		
Accounts receivable	9,340	(9,199)
Inventories	(9,195)	(6,473)
Other assets	1,653	(350)
Accounts payable	(12,582)	3,994
Accrued payroll and other accrued liabilities	(4,474)	(5,141)
Deferred revenue	6	(415)
Net cash (used in) provided by operating activities	(23,370)	3,528
Investing activities:		
Proceeds from sales and maturities of investments	345,009	281,502
Purchases of investments	(286,191)	(217,982)
Purchase of strategic investments	(5,000)	—
Net proceeds from the sale of strategic equity investments	5,249	—
Purchase of property, equipment and other assets	(3,314)	(4,293)
Proceeds from sale of property, equipment and other assets	1,646	—
Net cash paid for acquisitions	—	(71,971)
Net cash provided by (used in) investing activities	57,399	(12,744)
Financing activities:		
Proceeds from issuance of common stock	3,286	243
Repurchase of company stock	(29,268)	(20,137)
Funding of structured stock repurchase agreements	(23,830)	—
Funds received from structured stock repurchase agreements including gains	13,237	17,379
Payments of long-term debt	—	(289)
Other	(231)	(169)
Net cash used in financing activities	(36,806)	(2,973)
Net decrease in cash and cash equivalents	(2,777)	(12,189)
Cash and cash equivalents at the beginning of the period	51,595	49,125
Cash and cash equivalents at the end of the period	$ 48,818	$ 36,936
Supplementary cash flow disclosure:		
Cash paid for:		
Interest	$ 9	$ —
Income taxes	$ 338	$ 357

See Accompanying Notes to Condensed Consolidated Financial Statements

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying unaudited interim condensed consolidated financial statements of Applied Micro Circuits Corporation ("AMCC" or the "Company") have been prepared in accordance with generally accepted accounting principles for interim financial information. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. The accompanying financial statements reflect all adjustments (consisting of normal recurring adjustments), which are, in the opinion of management, considered necessary for a fair presentation of the results for the interim periods presented. Interim results are not necessarily indicative of results for a full year. The Company has experienced significant quarterly fluctuations in net revenues and operating results and these fluctuations could continue.

The financial statements and related disclosures have been prepared with the presumption that users of the interim financial information have read or have access to the audited financial statements for the preceding fiscal year. Accordingly, these financial statements should be read in conjunction with the audited financial statements and the related notes thereto contained in the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission ("SEC") for the fiscal year ended March 31, 2007.

Certain amounts in the condensed consolidated financial statements have been reclassified to conform to the current period presentation.

Accounting changes:

Effective April 1, 2007, the Company adopted Financial Accounting Standards Board ("FASB") Interpretation No. 48 ("FIN 48"), "*Accounting for Uncertainty in Income Taxes—an Interpretation of FASB Statement No. 109*." See "Note 8: Income Taxes" for further discussion.

Use of Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of net revenue and expenses in the reporting period. The Company regularly evaluates estimates and assumptions related to inventory valuation, warranty liabilities and revenue reserves, which affects its cost of sales and gross margin; allowance for doubtful accounts, which affects its operating expenses; the valuation of purchased intangibles and goodwill, which affects its amortization and impairments of goodwill and other intangibles; the valuation of restructuring liabilities, which affects the amount and timing of restructuring charges; the valuation of deferred income taxes, which affects its income tax expense and benefit; and stock-based compensation, which affects its gross margin and operating expenses. The Company bases its estimates and assumptions on historical experience and on various other factors that it believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. The actual results experienced by the Company may differ materially and adversely from management's estimates. To the extent there are material differences between the estimates and the actual results, future results of operations will be affected.

Recent Accounting Pronouncements

In September 2006, the FASB issued Statement of Financial Accounting Standard ("SFAS") No. 157 ("SFAS 157"), *Fair Value Measurements*. SFAS 157 defines fair value, establishes a framework and gives guidance regarding the methods used for measuring fair value, and expands disclosures about fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is currently evaluating the impact of adopting SFAS 157 on its consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159 ("SFAS 159"), *The Fair Value Option for Financial Assets and Financial Liabilities* which permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. SFAS 159 is effective for financial statements issued for fiscal years beginning after November 15, 2007. The Company is currently evaluating the impact of adopting SFAS 159 on its consolidated financial statements.

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2. CERTAIN FINANCIAL STATEMENT INFORMATION

Accounts receivable (in thousands):

	September 30, 2007	March 31, 2007
Accounts receivable	$ 24,514	$ 34,116
Less: allowance for doubtful accounts	(1,296)	(1,558)
	$ 23,218	$ 32,558

Inventories (in thousands):

	September 30, 2007	March 31, 2007
Finished goods	$ 31,874	$ 16,691
Work in process	5,372	9,630
Raw materials	3,235	4,965
	$ 40,481	$ 31,286

Other current assets (in thousands):

	September 30, 2007	March 31, 2007
Deposits	$ 531	$ 1,247
Prepaid expenses	10,188	10,435
Interest receivable	606	1,104
Other	505	1,652
	$ 11,830	$ 14,438

Property and equipment (in thousands):

	Useful Life (in years)	September 30, 2007	March 31, 2007
Machinery and equipment	5-7	$ 39,844	$ 43,084
Leasehold improvements	1-15	7,611	10,156
Computers, office furniture and equipment	3-7	75,298	76,809
Buildings	31.5	2,756	2,756
Land	N/A	9,800	11,302
		135,309	144,107
Less: accumulated depreciation and amortization		(109,654)	(116,957)
		$ 25,655	$ 27,150

Goodwill:

Goodwill was as follows (in thousands):

	Goodwill
March 31, 2007	335,857
Canadian tax settlement	(233)
September 30, 2007	$ 335,624

During the quarter ended June 30, 2007, AMCC Canada (formerly Quake Technologies) received notification that its preacquisition Scientific Research and Experimental Development ("SRED") claim was settled by the Canadian tax authorities. As the settlement amount was $0.2 million in excess of the assessed value of the refund at the time of the acquisition, the Company has recorded the value of this incremental refund through a reduction to goodwill.

Purchased intangibles:

Purchased intangibles were as follows (in thousands):

	September 30, 2007			March 31, 2007		
	Gross	Accumulated Amortization and Impairments	Net	Gross	Accumulated Amortization and Impairments	Net
Developed technology	$ 425,000	$ (374,578)	$ 50,422	$ 425,000	$ (365,411)	$ 59,589
Backlog/customer relationships	6,330	(4,541)	1,789	6,330	(4,288)	2,042
Patents/core technology rights/tradename	62,305	(46,684)	15,621	62,305	(44,149)	18,156
	$ 493,635	$ (425,803)	$ 67,832	$ 493,635	$ (413,848)	$ 79,787

As of September 30, 2007, the estimated future amortization expense of purchased intangible assets to be charged to cost of sales and operating expenses was as follows (in thousands):

	Cost of Sales	Operating Expenses	Total
Fiscal year 2008	$ 9,187	$ 2,619	$ 11,806
Fiscal year 2009	17,823	5,239	23,062
Fiscal year 2010	12,097	4,018	16,115
Fiscal year 2011	10,500	4,018	14,518
Fiscal year 2012	875	852	1,727
Thereafter	—	604	604
Total	$ 50,482	$ 17,350	$ 67,832

Other assets (in thousands):

	September 30, 2007	March 31, 2007
Non-current portion of prepaid expenses	$ 3,902	$ 3,386
Strategic investments	10,000	5,000
Other	3,250	2,580
	$ 17,152	$ 10,966

Marketable securities:

The following is a summary of available-for-sale investments, at fair value (in thousands):

	September 30, 2007	March 31, 2007
U.S. Treasury securities and agency bonds	$ 18,580	$ 39,425
Corporate bonds	16,901	20,878
Mortgage-backed and asset-backed securities	55,269	60,820
Closed-end bond funds	57,660	85,252
Preferred stock and options	20,826	22,203
Marketable equity securities*	—	4,297
	$ 169,236	$ 232,875

	September 30, 2007	March 31, 2007
Reported as:		
Short-term investments available-for-sale	$ 91,500	$ 232,875
Marketable securities	77,736	—
	$ 169,236	$ 232,875

* Marketable equity securities represents the Company's equity investment in Mellanox Technologies, Ltd., an Israeli company listed on the Nasdaq Stock Market. This investment was sold during the three months ended September, 30, 2007.

The following is a summary of gross unrealized losses as of September 30, 2007 (in thousands):

	Less than 12 months of unrealized losses		12 months or more of unrealized losses		Total	
	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value*	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses
U.S. Treasury securities and agency Bonds	$ —	$ —	$ 5,297	$ 57	$ 5,297	$ 57
Corporate bonds	3,441	81	11,821	308	15,262	389
Mortgage-backed and asset-backed securities	6,218	36	37,337	993	43,555	1,029
Closed-end bond funds	30,533	1,401	23,281	2,125	53,814	3,526
Preferred stock and options	17,074	233	—	—	17,074	233
	$ 57,266	$ 1,751	$ 77,736	$ 3,483	$ 135,002	$ 5,234

* Classified as marketable securities.

As of September 30, 2007, the Company determined that approximately $77.7 million of its available-for-sale securities to be long-term marketable securities because the Company has the ability and the intent to hold these securities until a recovery of the amortized cost is achieved, which recovery may be at maturity. The fair value of each of these securities had been less than its amortized cost for 12 or more consecutive months, however, we have not recorded any write-down adjustment in connection with the unrealized loss as we believe the unrealized loss of approximately $3.5 million as of September 30, 2007 associated with each of these securities is not other-than-temporary.

Other accrued liabilities (in thousands):

	September 30, 2007	March 31, 2007
Executive deferred compensation	$ 4,503	$ 3,422
Employee related liabilities	2,289	2,732
Warranty	1,882	2,692
Professional fees	822	1,199
Restructuring liabilities	927	350
Current income taxes	447	1,212
Other taxes	1,021	918
Other	2,640	3,858
	$ 14,531	$ 16,383

Warranty reserves:

The Company generally provides a one-year warranty on production released integrated circuit ("IC") products and up to three years on board level products. Estimated expenses for warranty obligations are accrued as revenue is recognized. Reserve estimates are adjusted periodically to reflect actual experience and/or changes to contracted obligations entered into with our customers.

The following table summarizes the activity related to the warranty reserve activity (in thousands):

	Three Months Ended September 30,		Six Months Ended September 30,	
	2007	2006	2007	2006
Beginning accrual balance	$ 2,507	$ 4,066	$ 2,692	$ 4,066
Charged to (reductions in) costs and expenses	(571)	(404)	(363)	(245)
Payments	(54)	(145)	(447)	(304)
Ending accrual balance	$ 1,882	$ 3,517	$ 1,882	$ 3,517

During the three and six months ended September 30, 2007, the Company reduced its warranty accrual by $0.6 million for a specific exposure which is no longer deemed to be probable.

Interest income, net (in thousands):

	Three Months Ended September 30,		Six Months Ended September 30,	
	2007	2006	2007	2006
Interest income	$ 3,081	$ 3,898	$ 6,243	$ 7,899
Net realized loss on short-term investments	(947)	(644)	(1,058)	(1,304)
Interest expense	(6)	—	(9)	—
	$ 2,128	$ 3,254	$ 5,176	$ 6,595

Other income, net (in thousands):

	Three Months Ended September 30,		Six Months Ended September 30,	
	2007	2006	2007	2006
Net gains on disposals of property and equipment	$ 58	$ 25	$ 64	$ 20
Foreign currency loss	(13)	97	(51)	97
Gain on strategic investment	4,649	—	4,649	—
Other	84	53	144	82
	$ 4,778	$ 175	$ 4,806	$ 199

Net loss per share:

Basic net loss per share is calculated by dividing net loss by the weighted average number of common shares outstanding during the year. The reconciliation of shares used to calculate basic and diluted net loss per share consists of the following (in thousands, except per share data):

	Three Months Ended September 30,		Six Months Ended September 30,	
	2007	2006	2007	2006
Net loss	$ (8,053)	$ (13,889)	$ (24,473)	$ (14,706)
Shares used in basic and diluted net loss per share computation (denominator):				
Weighted average common shares outstanding	275,132	281,762	278,394	286,470
Less: Unvested common shares outstanding	—	—	—	—
Shares used in basic and diluted net loss per share computation	275,132	281,762	278,394	286,470
Basic and diluted net loss per share	$ (0.03)	$ (0.05)	$ (0.09)	$ (0.05)

Because the Company incurred losses for the three and six months ended September 30, 2007 and 2006, the effect of dilutive securities totaling 852,000 and 873,000 equivalent shares for the three and six months ended September 30, 2007, respectively, and 824,000 and 886,000 equivalent shares for the three and six months ended September 30, 2006, respectively, have been excluded from the net loss per share computations as their impact would be anti-dilutive.

3. RESTRUCTURING CHARGES

Over the last several years, the Company has undertaken significant restructuring activities under several plans in an effort to reduce operating costs. A combined summary of the restructuring activity as of September 30, 2007, is as follows (in thousands):

	Workforce Reduction	Facilities Consolidation and Operating Lease Commitments	Property and Equipment Impairments	Total
Liability, March 31, 2006	$ 5,830	$ 1,814	$ —	$ 7,644
Charged to expense	500	328	2,794	3,622
Cash payments	(5,287)	(504)	—	(5,791)
Noncash charges	—	—	(2,794)	(2,794)
Reductions to estimated liability	(693)	(1,638)	—	(2,331)
Liability, March 31, 2007	350	—	—	350
Charged to expense	1,376	—	—	1,376
Cash payments	(767)	—	—	(767)
Reductions to estimated liability	(32)	—	—	(32)
Liability, September 30, 2007	$ 927	$ —	$ —	$ 927

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The following table provides detailed activity related to the restructuring programs as of September 30, 2007 (in thousands):

	Workforce Reduction	Facilities Consolidation and Operating Lease Commitments	Property and Equipment Impairments	Total
April 2003 Restructuring Program				
Liability, March 31, 2006	$ —	$ 907	$ —	$ 907
Cash payments	—	(88)	—	(88)
Reductions to estimated liability	—	(819)	—	(819)
Liability, March 31, 2007	$ —	$ —	$ —	$ —
July 2005 Restructuring Program				
Liability, March 31, 2006	$ —	$ 907	$ —	$ 907
Cash payments	—	(88)	—	(88)
Reductions to estimated liability	—	(819)	—	(819)
Liability, March 31, 2007	$ —	$ —	$ —	$ —
March 2006 Restructuring Program				
Liability, March 31, 2006	$ 5,830	$ —	$ —	$ 5,830
Charged to expense	—	328	2,794	3,122
Cash payments	(4,917)	(328)	—	(5,245)
Non-cash charge	—	—	(2,794)	(2,794)
Reductions to estimated liability	(613)	—	—	(613)
Liability, March 31, 2007	300	—	—	300
Cash payments	(164)	—	—	(164)
Liability, September 30, 2007	$ 136	$ —	$ —	$ 136
June 2006 Restructuring Program				
Charged to expense	$ 500	$ —	$ —	$ 500
Cash payments	(370)	—	—	(370)
Reductions to estimated liability	(80)	—	—	(80)
Liability, March 31, 2007	50	—	—	50
Cash payments	(18)	—	—	(18)
Reductions to estimated liability	(32)	—	—	(32)
Liability, June 30, 2007	$ —	$ —	$ —	$ —
July 2007 Restructuring Program				
Charged to expense	$ 695	$ —	$ —	$ 695
Cash payments	(585)	—	—	(585)
Liability, September 30, 2007	$ 110	$ —	$ —	$ 110
September 2007 Restructuring Program				
Charged to expense	$ 681	$ —	$ —	$ 681
Cash payments	—	—	—	—
Liability, September 30, 2007	$ 681	$ —	$ —	$ 681

In April 2003, the Company announced a restructuring program. The April 2003 restructuring program consisted of a workforce reduction of 185 employees, consolidation of excess facilities and fixed asset disposals. The Company recognized a total of $23.8 million in restructuring costs related to this restructuring program. The restructuring costs consisted of approximately $5.7 million for employee severances, $7.2 million representing the discounted cash flow of lease payments on exited facilities, $3.4 million for the disposal of certain software licenses, and $7.5 million for the write-off of leasehold improvements and property and equipment. This restructuring charge was offset by a $2.6 million restructuring benefit in November 2003 related to the reoccupation of a portion of a building in San Diego and an adjustment for overestimated severance to be paid. During fiscal 2007, this restructuring accrual was reduced by $0.8 million to zero due to the planned reoccupation of this facility prior to September 2007.

In July 2005, the Company implemented another restructuring program. The July 2005 restructuring program was implemented to reduce job redundancies and reduce ongoing operating expenses. This restructuring program consisted of the elimination of approximately 40 employees, the disposal of idle fixed assets, and the consolidation of San Diego facilities. As a result of the July 2005 restructuring program, the Company recorded a charge of approximately $5.0 million, consisting of $1.4 million for employee severances, $2.6 million for property and equipment write-offs and $1.0 million representing expenses relating to the consolidation of facilities. During fiscal 2007, this restructuring accrual was reduced by $0.8 million to zero due to the planned reoccupation of this facility prior to September 2007.

In March 2006, the Company communicated and began implementation of a plan to exit its operations in France and India and reorganize part of its manufacturing operations. The restructuring program included the elimination of approximately 68 employees. The Company recorded a charge of approximately $7.6 million, consisting of $6.0 million for employee severances, $1.0 million for operating lease write-offs, and $0.6 million for asset impairments. During fiscal 2007, the Company recorded additional net charges of approximately $2.5 million, consisting of $0.2 million for excess lease liability, $0.1 million for operating lease commitments and $2.8 million for asset impairments, offset by $0.6 million in workforce reduction liability adjustments. During the six month period ended September 30, 2007, the Company paid down part of its remaining liability.

In June 2006, the Company implemented another restructuring program. The June 2006 restructuring program was implemented to reduce job redundancies. This restructuring program consisted of the elimination of approximately 20 employees. As a result of the June 2006 restructuring program, the Company recorded a net charge of approximately $0.5 million, consisting of employee severances. During the three months ended June 30, 2007, the Company paid all remaining liabilities related to this restructuring program and recorded a reversal of the remaining liability through restructuring expense.

In July 2007, the Company implemented another restructuring program. The July 2007 restructuring program was implemented to reduce job redundancies. This restructuring program consisted of the elimination of approximately 29 employees. As a result of the July 2007 restructuring program, the Company recorded a net charge of approximately $0.7 million, consisting of employee severances. During the three months ended September 30, 2007, the Company paid down part of its remaining liability.

In September 2007, the Company implemented another restructuring program. The September 2007 restructuring program was implemented to reduce job redundancies. This restructuring program consisted of the elimination of approximately 28 employees. As a result of the September 2007 restructuring program, the Company recorded a net charge of approximately $0.7 million, consisting of employee severances. During the three months ended September 30, 2007, the Company paid down part of its remaining liability.

4. COMPREHENSIVE LOSS

The components of comprehensive loss, net of tax, are as follows (in thousands):

	Three Months Ended September 30,		Six Months Ended September 30,	
	2007	2006	2007	2006
Net loss	$ (8,053)	$ (13,889)	$ (24,473)	$ (14,706)
Change in net unrealized gain (loss) on short-term investments	(4,102)	7,351	(4,221)	5,820
Foreign currency translation adjustment gain (loss)	(226)	25	(422)	(200)
Comprehensive loss	$ (12,381)	$ (6,513)	$ (29,116)	$ (9,086)

5. STOCKHOLDERS' EQUITY

Preferred Stock

The Company's Certificate of Incorporation allows for the issuance of up to 2.0 million shares of preferred stock in one or more series and permits the Company's Board of Directors ("Board") to fix the rights, preferences, privileges and restrictions thereof, including dividend rights, dividend rates, conversion rights, voting rights, terms of redemption, redemption prices, liquidation preferences, and the number of shares constituting any series so designated by the Board of Directors, without further vote or action by the stockholders.

Common Stock

At September 30, 2007 the Company had 630.0 million shares authorized for issuance and approximately 272.9 million shares issued and outstanding. At March 31, 2007, there were approximately 283.0 million shares issued and outstanding.

In March 2007, the Company's stockholders approved a proposal that allows the Board to implement a reverse stock split on the common stock using any one of three approved ratios: 1-for-2, 1-for-3 or 1-for-4. The Board has not yet implemented any reverse stock split and is not required to implement any of the approved splits. If the Board implements a 1-for-3 reverse stock split, the authorized number of shares of common stock will be reduced to 500 million shares. If the Board implements a 1-for-4 reverse stock split, the authorized number of shares of common stock will be reduced to 375 million shares. The Board's authority to implement any of the reverse stock splits approved in March 2007 expires on March 8, 2008.

Employee Stock Purchase Plan

The Company has in effect an employee stock purchase plan under which 19.2 million shares of common stock have been reserved for issuance. Under the terms of this plan, purchases are made semiannually and the purchase price of the common stock is equal to 85% of the fair market value of the common stock on the first or last day of the offering period, whichever is lower. During the six months ended September 30, 2007, Approximately 1.0 million shares were issued under this plan. There were no shares issued during the six months ended September 30, 2006. At September 30, 2007, approximately 11.0 million shares had been issued under this plan and approximately 8.2 million shares were available for future issuance.

Stock Repurchase Program

In August 2004, the Board authorized a stock repurchase program for the repurchase of up to $200.0 million of the Company's common stock. Under the program, the Company is authorized to make purchases in the open market or enter into structured repurchase agreements. During the six months ended September 30, 2007, 9.9 million shares were repurchased on the open market at a weighted average price of $2.95 per share. During the six months ended September 30, 2006, 6.2 million common shares were repurchased at a weighted average price of $3.23 per share. From the time the program was implemented through September 30, 2007, a total of 25.5 million shares were repurchased on the open market at a weighted average price of $2.99 per share. All repurchased shares were retired upon delivery. At September 30, 2007, $51.2 million remained available to repurchase shares under the stock repurchase program.

The Company also utilizes structured stock repurchase agreements to buy back shares which are prepaid written put options on the Company's common stock. The Company pays a fixed sum of cash upon execution of each agreement in exchange for the right to receive either a pre-determined amount of cash or stock depending on the closing market price of the Company's common stock on the expiration date of the agreement. Upon expiration of each agreement, if the closing market price of the Company's common stock is above the pre-determined price, the Company will have its investment returned with a premium. If the closing market price is at or below the pre-determined price, the Company will receive the number of shares specified at the agreement inception. Any cash received, including the premium, is treated as an increase to additional paid in capital on the balance sheet in accordance with the guidance issued in EITF 00-19, *Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock*.

During the six months ended September 30, 2007, the Company entered into structured stock repurchase agreements totaling $23.8 million. For those agreements that had been settled by September 30, 2007, the Company received 1.8 million shares of its common stock at an effective purchase price of $2.85 per share and $13.2 million in cash. At September 30, 2007, the Company had two outstanding structured stock repurchase agreements which settled with the receipt of $7.9 million in October 2007. During the six months ended September 30, 2006, the Company received $17.4 million in cash and 7.7 million shares of its common stock upon the settlement of structured stock repurchase agreements. From the inception of the Company's most recent stock repurchase program through September 30, 2007, the Company entered into structured stock repurchase agreements totaling $197.7 million. Upon settlement of these agreements through September 30, 2007, the Company received $128.7 million in cash and 24.7 million shares of its common stock at an effective purchase price of $2.52 per share.

The table below is a summary of the Company's repurchase program share activity for the six months ended September 30, 2007 and 2006 (in thousands, except per share data):

	Six Months Ended September 30,	
	2007	2006
Open market repurchases:		
Aggregate repurchase price	$ 29,268	$ 20,137
Repurchased shares	9,915	6,242
Average price per share	$ 2.95	$ 3.23
Structured stock repurchase agreements:		
Shares acquired in settlement	1,757	7,696
Average price per share*	$ 2.85	$ 3.25
Total shares acquired by repurchase or in settlement	11,672	13,938
Average price per share	$ 2.94	$ 3.24

* The average price per share of shares acquired in settlements of structured stock repurchase agreements during the six months ended September 30, 2007 and 2006 does not include gains on settlements in cash of $1.3 million and $1.5 million, respectively.

Stock Options

The Company has granted stock options to employees and non-employee directors under several plans. These option plans include two stockholder-approved plans (the 1992 Stock Option Plan and 1997 Directors' Stock Option Plan) and four plans not approved by stockholders (the 2000 Equity Incentive Plan, Cimaron Communications Corporation's 1998 Stock Incentive Plan assumed in the fiscal 1999 merger, and JNI Corporation's 1997 and 1999 Stock Option Plans assumed in the fiscal 2004 merger). Certain other outstanding options were assumed through the Company's various acquisitions.

In March 2007, the Company's stockholders approved a stock option exchange program to permit eligible employees to exchange outstanding stock options with exercise prices equal to or greater than $4.90 per share for a reduced number of restricted stock units to be granted under the 2000 Equity Incentive Plan. In May 2007, options for approximately 7.9 million shares of common stock with a weighted average exercise price of $8.50 were exchanged for approximately 1.8 million restricted stock units which vest semi-annually over a two year period. The exchange was considered a modification under SFAS123(R), and the incremental expense associated with the modification is considered the fair value of the modification, which was immaterial, was included in stock-based compensation expense for the three months ended June 30, 2007.

In March 2007, the Company's stockholders also approved the amendment and restatement of the 1992 Stock Option Plan (i) to expand the type of awards available under the plan, (ii) to rename the plan as the 1992 Equity Incentive Plan, (iii) to extend the plan's expiration date until January 10, 2017, (iv) to increase the share reserve under the plan by 9.0 million shares, (v) to serve as a successor plan to the 2000 Equity Incentive Plan, which will no longer be used for equity awards following completion of the stock option exchange described above, and (vi) to provide that any shares subject to stock awards under the 2000 Equity Incentive Plan that terminate or are forfeited or repurchased (other than options issued under the 2000 Equity Incentive Plan that were tendered in the stock option exchange) are added to the share reserve under the 1992 Equity Incentive Plan.

The Board has delegated administration of the Company's equity plans to the Compensation Committee, which generally determines eligibility, vesting schedules and other terms for awards granted under the plans. Options under the plans expire not more than ten years from the date of grant and are generally exercisable upon vesting. Vesting generally occurs over four years. In fiscal 2006, stock options covering 5.1 million shares were granted with a 2.5-year vesting schedule. New hire grants generally vest and become exercisable at the rate of 25% on the first anniversary of the date of grant and ratably on a monthly basis over a period of 36 months thereafter; subsequent option grants to existing employees generally vest and become exercisable ratably on a monthly basis over a period of 48 months measured from the date of grant.

In connection with its annual review of officer compensation in April 2006, the Compensation Committee granted to each of the Company's executive officers performance options that vest based on pre-determined Company goals. There are two types of performance options. The first type vests in 48 equal monthly installments beginning one month after the grant date; provided, however, if the Company achieved specific goals under its fiscal 2007 operating plan, the vesting of the option would have accelerated such that the option would have been fully exercisable at the end of two years instead of four years. The Company did not achieve these goals so the vesting on these options was not accelerated. The second type of

performance options becomes exercisable only if the Company achieves specific revenue and non-GAAP pre-tax profit targets in any fiscal quarter before fiscal 2010. During the three months ended June 30, 2007, the Company revised the amortization period from two years to three years.

In connection with its annual review of officer compensation in April 2007, the Compensation Committee granted to each of the Company's executive officers performance options that vest based on pre-determined Company goals. There are two types of performance options. The first type vests in 48 equal monthly installments beginning one month after the grant date; provided, however, if the Company achieves specific goals under its fiscal 2008 operating plan, the vesting of the option will accelerate such that the option will be fully exercisable at the end of two years instead of four years. The second type of performance options becomes exercisable only if the Company achieves certain rankings within a group of peer companies with respect to certain measures of performance by the end of fiscal 2008 as determined by the Compensation Committee.

At September 30, 2007 there were no shares of common stock subject to repurchase. Options are granted at prices at least equal to fair value of the Company's common stock on the date of grant.

Option activity under the Company's stock incentive plans in the six months ended September 30, 2007 is set forth below:

	Number of Shares (in thousands)	Weighted Average Exercise Price Per Share
Outstanding at the beginning of the period	40,612	$ 4.58
Granted	518	2.86
Exercised	(199)	1.49
Cancelled	(1,838)	4.91
Outstanding at the end of the period	39,093	$ 4.56
Vested at the end of the period	28,569	$ 5.08

At September 30, 2007, the weighted average remaining contractual term for options outstanding is 4.59 years and for options vested is 3.67 years.

The aggregate pretax intrinsic value of options exercised during the six months ended September 30, 2007 was $351,000. This intrinsic value represents the excess of the fair market value of the Company's common stock on the date of exercise over the exercise price of such options.

During the six months ended September 30, 2007 and 2006, the Company repurchased a total of 11.7 million and 13.9 million shares of its common stock at a weighted average effective price of $2.94 and $3.24, respectively.

The aggregate pretax intrinsic value, weighted average remaining contractual life, and weighted average per share exercise price of options outstanding and of options exercisable as of September 30, 2007 were as follows (in thousands, except exercise prices and years):

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Number of Shares	Weighted Average Exercise Price
$0.05 – $ 2.98	8,269	$ 2.48	5.38	5,314	$ 2.42
2.99 – 3.32	7,931	3.16	7.07	3,692	3.23
3.33 – 3.94	8,066	3.65	5.95	5,209	3.67
3.95 – 6.48	5,743	4.83	3.01	5,270	4.90
6.49 – 75.03	9,084	8.32	1.49	9,084	8.32
$0.05 – $75.03	39,093	$ 4.56	4.59	28,569	$ 5.08

As of September 30, 2007, the aggregate pre-tax intrinsic value of options outstanding and exercisable was $4.0 million and options outstanding was $6.0 million. The aggregate pretax intrinsic values in the preceding table were calculated based on the closing price of the Company's common stock of $3.16 on September 30, 2007.

Restricted Stock Units

The Company granted restricted stock units pursuant to its 2000 Equity Incentive Plan as part of its regular annual employee equity compensation review program as well as to new hires. In May 2007, the Company granted approximately 1.8 million restricted stock units in exchange for approximately 7.9 million options for shares of common stock in connection with the stock option exchange program approved by its stockholders in March 2007. Restricted stock units are share awards that upon vesting, will deliver to the holder, shares of the Company's common stock. Generally, restricted stock units vest ratably on a quarterly basis over four years from the date of grant. For employees hired after May 15, 2006, restricted stock units will vest on a quarterly basis over four years from the date of hire provided that no shares will vest during the first year, at the end of which the shares that would have vested during that year will vest and the remaining shares will vest over the remaining 12 quarters. Following the amendment and restatement of the 1992 Stock Option Plan as the 1992 Equity Incentive Plan and the completion of the stock option exchange program, the Company has discontinued making restricted stock unit awards from the 2000 Equity Incentive Plan. In the future, all restricted stock unit awards will be made from the 1992 Equity Incentive Plan.

Restricted stock unit activity for the six months ended September 30, 2007 is set forth below:

	Restricted Stock Units Outstanding Number of Shares (in thousands)
Balance at beginning of period	3,424
Awarded during the period	359
Vested during the period	(109)
Cancelled during the period	(134)
Balance at end of period	3,540

The weighted average grant-date fair value per share for the restricted stock units was $3.06, and the weighted average remaining contractual term for the restricted stock units outstanding as of September 30, 2007 was 1.3 years.

Based on the closing price of the Company's common stock of $3.16 on September 30, 2007, the total pretax intrinsic value of all outstanding restricted stock units on that date was $11.2 million.

6. STOCK-BASED COMPENSATION

SFAS 123(R) requires companies to estimate the fair value of stock-based compensation on the date of grant using an option-pricing model. The Company uses the Black-Scholes model to value stock-based compensation. The Black-Scholes model determines the fair value of share-based payment awards based on the stock price on the date of grant and is affected by assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to, the Company's expected stock price volatility over the term of the awards, and actual and projected employee stock option exercise behaviors. Option-pricing models were developed for use in estimating the value of traded options that have no vesting or hedging restrictions and are fully transferable. Although the fair value of stock options granted by the Company is determined in accordance with SFAS 123(R) and Staff Accounting Bulletin No. 107 ("SAB 107"), *Share-Based Payment*, using an option-pricing model, that value may not be indicative of the fair value observed in a willing buyer/ willing seller market transaction.

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The following table summarizes stock-based compensation expense related to stock options and restricted stock units under SFAS 123(R) for the three and six months ended September 30, 2007 and 2006, which is allocated as follows (in thousands):

	Three Months Ended September 30,		Six Months Ended September 30,	
	2007	2006	2007	2006
Stock-based compensation expense by type of awards				
Stock options	$ 2,929	$ 2,654	$ 5,268	$ 5,153
Restricted stock units	368	24	649	36
Total stock-based compensation expense	3,297	2,678	5,917	5,189
Stock-based compensation capitalized as part of inventory	48	—	192	—
Total stock-based compensation	3,345	$ 2,678	$ 6,109	$ 5,189

The fair value of the options granted during the three months ended September 30, 2007 and 2006 is estimated as of the grant date using the Black-Scholes option-pricing model assuming the weighted-average assumptions listed in the following table:

	Three Months Ended September 30,			
	Employee Stock Options		Employee Stock Purchase Plans	
	2007(1)	2006	2007(2)	2006
Expected life (years)	3.9	5.7	0.5	1.3
Risk-free interest rate	4.6%	4.8%	5.0%	2.9%
Volatility	49%	54%	55%	64%
Dividend yield	—%	—%	—%	—%
Weighted average fair value per share	$ 1.27	$ 2.04	$ 0.86	$ 1.50

(1) As of March 2007, option grants will have an expiration of 8 years instead of the previous expiration of 10 years with the exception of grants to non-employee directors, which will continue to be granted with a 10 year expiration.

(2) In January 2007, the Company reduced the offering period under its employee stock purchase plan from 24 months to 6 months.

The weighted average fair value per share of the restricted stock units awarded was $2.97 and $2.96 in the three and six months ended September 30, 2007, respectively, and was zero and $3.20 in the three and six months ended September 30, 2006, respectively. The weighted average fair value per share was calculated based on the fair market value of the Company's common stock on the respective grant dates.

Effective April 1, 2007, the Company revised its estimated forfeiture rate used in determining the amount of stock-based compensation from 5.73% to 6.10% as a result of an increasing rate of forfeitures in recent periods, which the Company believes is indicative of the rate it will experience during the remaining vesting period of currently outstanding unvested options.

The following table summarizes stock-based compensation expense as it relates to the Company's statement of operations (in thousands):

	Three Months Ended September 30,		Six Months Ended September 30,	
	2007	2006	2007	2006
Stock-based compensation included in expenses:				
Cost of revenues	$ 240	$ 158	$ 312	$ 291
Research and development	1,216	1,028	2,271	2,097
Selling, general and administrative	1,841	1,492	3,334	2,801
Total stock-based compensation expense	3,297	2,678	5,917	5,189
Stock-based compensation capitalized as part of inventory	48	—	192	—
Total stock-based compensation	$ 3,345	$ 2,678	$ 6,109	$ 5,189

The adoption of SFAS 123(R) will continue to have a significant adverse impact on the Company's reported results of operations, although it will have no impact on its overall financial position. The amount of unearned stock-based compensation currently estimated to be expensed from now through fiscal 2012 related to unvested share-based payment awards at September 30, 2007 is $20.0 million. The weighted-average period over which the unearned stock-based compensation is expected to be recognized is approximately 2.5 years. If there are any modifications or cancellations of the underlying unvested securities, the Company may be required to accelerate, increase or cancel any remaining unearned stock-based compensation expense. Future stock-based compensation expense and unearned stock-based compensation will increase to the extent that the Company grants additional equity awards or assumes unvested equity awards in connection with acquisitions.

7. CONTINGENCIES

Legal Proceedings

In October 2001, a shareholder derivative lawsuit was filed against JNI and certain of its former officers and directors in the Superior Court of the State of California in the County of San Diego, case no. GIC 775153. The complaint alleged that between October 16, 2000 and January 24, 2001, the defendants breached their fiduciary duty by failing to adequately oversee the activities of management and that JNI allegedly made false statements about its business and results causing its stock to trade at artificially inflated levels. The court sustained JNI's demurrers to each of the plaintiff's complaints and dismissed the complaint in June 2002. In June 2002, the court granted Sik-Lin Huang's motion to intervene. Huang filed a complaint in intervention in July 2002. In September 2002, JNI's board of directors appointed a special litigation committee to investigate the allegations. In February 2003, the special litigation committee issued a report of its investigation, which concluded that it was not in JNI's best interests to pursue the litigation. In November 2003, the court dismissed the complaint with prejudice. In January 2004, the plaintiff filed a notice of appeal. A motion to dismiss the appeal was filed by the defendants on the grounds that the plaintiff had lost standing because he no longer owned JNI shares. In October 2005, the court dismissed the appeal, finding the plaintiff had no standing to maintain the lawsuit. The California Supreme Court granted review of the Court of Appeal's decision in January 2006. In April 2006, plaintiff filed his opening brief. The Company filed its answer brief in May 2006. Plaintiff's reply brief was filed in August 2006. A hearing on this appeal has been set for December 4, 2007. A possible amount of loss cannot be reasonably estimated at this time.

In November 2001, a class action lawsuit was filed against JNI and the underwriters of its initial and secondary public offerings of common stock in the U.S. District Court for the Southern District of New York, case no. 01 Civ 10740 (SAS). The complaint alleges that defendants violated the Exchange Act in connection with JNI's public offerings. This lawsuit is among more than 300 class action lawsuits pending in this District Court that have come to be known as the "IPO laddering cases." In June 2003, a proposed partial global settlement, subsequently approved by JNI's board of directors, was announced between the issuer defendants and the plaintiffs that would guarantee at least $1 billion to investors who are class members from the insurers of the issuers. The proposed settlement, if approved by the District Court and by the issuers, would be funded by insurers of the issuers, and would not result in any payment by JNI or the Company. The District Court granted its preliminary approval of settlement subject to defendants' agreement to modify certain provisions of the settlement agreements regarding contractual indemnification. JNI accepted the District Court's proposed modifications. The District Court held a hearing for final approval of the settlement in April 2006. In December 2006, the U.S. Court of Appeals for the Second Circuit vacated the District Court's decision certifying as class actions the six lawsuits designated as "focus cases." Thereafter, on December 14, 2006, the Court ordered a stay of all proceedings in all of the lawsuits pending the outcome of plaintiffs' petition to the Second Circuit Court of Appeals for a rehearing en banc and resolution of the class certification issue. On April 6, 2007, the Second Circuit Court of Appeals denied plaintiffs' petition for a rehearing, but clarified that the plaintiffs may seek to certify a more limited class. Accordingly, the stay remains in place and the plaintiffs and issuers have stated that they are prepared to discuss how the settlement might be amended or renegotiated to comply with the decision of the Second Circuit Court of Appeals. If the settlement is not amended or renegotiated and then approved by the Court, the Company intends to defend the lawsuit vigorously. A possible amount of loss cannot be reasonably estimated at this time.

On or about November 20, 2002, Spirent Communications of Ottawa Limited ("Spirent") filed suit in the Ontario (Canada) Superior Court of Justice against Quake. Quake defended that lawsuit by way of a Statement of Defence and Counterclaim that was filed on or about December 20, 2002. In the lawsuit, Spirent's claim as submitted at trial was for the sum of $1.1 million, plus pre- and post-judgment interest, and legal costs. In its counterclaim, as submitted at trial, Quake claimed the amount of $122,000 against Spirent, the return of a $133,000 deposit paid by Quake to a third party, plus interest and legal costs. On June 28th, 2006, Quake received the Decision of the Ontario (Canada) Superior Court of Justice, providing that Spirent's action against Quake shall be dismissed, that Quake shall have judgment against Spirent on its counterclaim in the amount of $122,000, and that the deposit in the amount of $133,000 shall be returned to Quake together with interest. Subsequently, Quake received the Court's Decision As To Costs, providing that Spirent shall pay to Quake its

costs of the action in the amount of $312,000, payable within thirty days. Spirent's filed a Notice of Appeal on July 27, 2006, appealing the Decision to the Court of Appeal for Ontario. Payment of the monies owing by Spirent to Quake has been stayed pending disposition of the appeal. The appeal is scheduled to be heard by the Court of Appeal for Ontario on November 21, 2007. Quake does not expect that settlement negotiations will take place. In the event that Spirent is successful on its appeal, the upper limit on Quake's reasonably possible losses would be a total of approximately $1.8 million, plus its own legal fees of approximately $60,000. All amounts identified above are in Canadian Dollars.

Various current and former directors and officers of the Company have been named as defendants in two consolidated stockholder derivative actions filed in the United States District Court for the Northern District of California, captioned *In re Applied Micro Circuits Derivative Litigation* (N.D. Cal.) (The "Federal Action"); and four substantially similar consolidated stockholder derivative actions filed in the Superior Court of the State of California in the County of Santa Clara, captioned *In re Applied Micro Circuits Corporation Shareholder Derivative Litigation* (the "State Action"). Plaintiffs in the Federal and State Actions allege that the defendant directors and officers backdated stock option grants during the period from 1997 through 2005. Both actions assert claims for breach of fiduciary duty, gross mismanagement, waste of corporate assets, unjust enrichment, imposition of a constructive trust over the option contracts, and violations of Section 25402 of the California Corporations Code. The Federal Action also alleges that the defendants violated Section 14(a) of the Exchange Act and Rule 14a-9 promulgated thereunder, and Section 20(a) of the Exchange Act. Both actions seek to recover unspecified monetary damages against the individual defendants on behalf of the Company, restitution, rescission of the option contracts, disgorgement of profits and benefits, equitable relief and attorneys' fees and costs. The Company is named as a nominal defendant in both the Federal and State Actions; thus no recovery against the Company is currently sought.

The Company and the individual defendants have filed motions to dismiss in both the Federal and State Actions. Hearings on the motion to dismiss, or in the alternative stay, the State Action took place on March 2 and June 22, 2007. The Court in the State Action has taken the motion to dismiss, or in the alternative stay, under submission. The motions to dismiss in the Federal Action have been taken off calendar without prejudice to the Company and the individual defendants to re-file their motions. The Court in the Federal Action took the motions to dismiss off calendar while the parties engage in settlement discussions. The Company has also moved to stay discovery in the State Action, and the Company's motion was granted in part and denied in part. Discovery is currently stayed in the Federal Action. No trial date has been set in either Action.

On June 5, 2007, two former officers of the Company were named as defendants in another derivative action filed in the United States District Court for the Northern District of California, captioned *Segen v. Rickey, et al.*, No. C 07 2917 ("Section 16b Action"). The plaintiff in the Section 16b Action alleges that these two former officers violated Section 16b of the Securities Exchange Act of 1934 and Rule 16b-3 promulgated thereunder through the receipt of option grants and stock sales from 1999 through 2001 which plaintiff alleges constituted short-swing trading transactions. The Section 16b Action seeks disgorgement of profits and benefits from these individual defendants, and attorneys' fees and costs. The Company is named as a nominal defendant in the Section 16b Action, and thus no recovery against the Company is currently sought. The Company and the individual defendants have filed motions to dismiss. The hearing on those motions to dismiss is currently scheduled for November 27, 2007. Discovery is currently stayed in the Section 16b Action, and no trial date has been set.

Regulatory Proceedings

In June 2006, the Company received a request from the SEC to produce voluntarily certain documents concerning our historical stock option grant practices. The Company produced responsive documents and indicated its intent to cooperate fully with the SEC's investigation.

In June 2006, the Company announced in a press release that it had received a Grand Jury subpoena from the U.S. Attorney's Office for the Northern District of California relating to its historical stock option practices and that a parallel investigation had been initiated by the U.S. Attorney's Office for the Southern District of California. The U.S. Attorney's Office for the Northern District of California subsequently deferred the criminal investigation to the Southern District of California and withdrew its Grand Jury subpoena. In July 2006, the U.S. Attorney's Office for the Southern District of California served the Company with a Grand Jury subpoena substantially similar to the subpoena previously issued by the Northern District of California.

The Company has been cooperating with the SEC and Department of Justice in connection with their investigations, including through in-person and telephone meetings between Company representatives and the staff of the SEC and Department of Justice, and through the provision of information and documents.

8. INCOME TAXES

Effective April 1, 2007, the Company has adopted the provisions of FIN 48. There was no cumulative effect related to adopting FIN 48. However, the Company reclassified $0.8 million of its accrual under SFAS No. 5 to an unrecognized tax benefit under FIN 48 in order to comply with the requirements of FIN 48.

During the quarter ended September 30, 2007, the full accrual of $0.8 million for unrecognized tax benefits was released. Of that balance, $0.2 million was reclassified to income taxes payable and $0.6 million was a benefit to the income tax provision. The decrease was due to the completion and settlement of a foreign tax audit that resulted from the liquidation of one of its foreign subsidiaries.

The Company estimates that its accrual for unrecognized tax benefits will not materially change during the next twelve months.

At April 1, 2007, the Company had net deferred tax assets of $535.8 million. These deferred tax assets are primarily composed of federal and state tax net operating loss ("NOL") carryforwards and federal and state research and development ("R&D") credit carryforwards. Due to uncertainties surrounding the Company's ability to generate future taxable income to realize these assets, a full valuation has been established to offset its net deferred tax asset. Additionally, the future utilization of the Company's NOL and R&D credit carryforwards to offset future taxable income may be subject to a substantial annual limitation as a result of ownership changes that may have occurred previously or that could occur in the future. The Company has not yet determined whether such an ownership change has occurred; however, the Company plans to complete an analysis regarding the limitation of the net operating losses and research and development credits. When this analysis is completed, the Company plans to update its unrecognized tax benefits under FIN 48. Until the Company has determined whether such an ownership change has occurred, and until the amount of any limitation becomes known, no amounts are being presented as an uncertain tax position in accordance with FIN 48. Any carryforwards that will expire prior to utilization as a result of such limitations will be removed from deferred tax assets with a corresponding reduction of the valuation allowance. Due to the existence of the valuation allowance, future changes in the Company's unrecognized tax benefits, other than the $0.8 million previously mentioned, will not impact its effective tax rate.

The Company has not recognized any accrued interest or penalties related to unrecognized tax benefits through the quarter ended September 30, 2007 or during the years ended March 31, 2007 or 2006.

The Company is subject to taxation in the U.S. and various state and foreign jurisdictions. The Company currently has no years under examination by the Internal Revenue Service or any state jurisdiction. Effectively, all of the Company's historical tax years are subject to examination by the Internal Revenue Service and various state jurisdictions due to the generation of net operating loss and credit carryforwards. With few exceptions, the Company is no longer subject to foreign examinations by tax authorities for years before 2004.

9. ACQUISITION OF QUAKE TECHNOLOGIES, INC.

On August 25, 2006, the Company acquired Quake Technologies, Inc., a Delaware corporation (now known as "AMCC Canada"), for $81.2 million in cash including merger costs. Of the amount paid, $12.0 million was placed in escrow for at least one year in order to secure the indemnification obligations of Quake to the Company. In addition, the Company assumed unvested stock options covering 1.7 million shares of the Company's common stock that had a fair value of $3.5 million. The fair value of the unvested options was calculated using a Black-Scholes method and is being recorded as stock-based compensation over the requisite service period.

In connection with this transaction, the Company conducted valuations of the intangible assets acquired in order to allocate the purchase price in accordance with FASB Statement of Financial Accounting No. 141 ("SFAS 141"), *Business Combinations*. In accordance with SFAS 141, the Company has allocated the excess purchase price over the fair value of net tangible assets acquired to the identifiable intangible assets. The Company recorded a charge of $13.3 million for purchased in-process research and development ("IPR&D") expense. The amounts allocated to IPR&D were expensed upon acquisition as it was determined that the underlying projects had not reached technological feasibility and no alternative future uses existed. The purchase price in the transaction was allocated as follows (in thousands):

Net tangible assets	$	8,411
Purchased inventory fair market value		2,395
Existing technology		11,500
In-process research and development		13,300
Patents/trademarks		3,200
Customer relationships/backlog		2,800
Goodwill		39,597
	$	81,203

The total consideration issued in the acquisition was as follows (in thousands):

Cash	$	80,003
Merger costs		1,200
Total consideration paid	$	81,203

No supplemental pro forma information is presented for the acquisition due to the immaterial effect of the acquisition on the Company's results of operations.

During the quarter ended June 30, 2007, AMCC Canada received notification that its preacquisition SRED claim was settled by the Canadian tax authorities. As the settlement amount was $0.2 million in excess of the assessed value of the refund at the time of the acquisition, the Company has recorded the value of this incremental refund through a reduction to goodwill (not reflected in the table above.)

At the end of August 2007, the funds in escrow were released to the former shareholders of Quake.

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

Management's discussion and analysis of financial condition and results of operations ("MD&A") is provided as a supplement to the accompanying consolidated financial statements and footnotes to help provide an understanding of our financial condition, changes in our financial condition and results of our operations. The MD&A is organized as follows:

- *Caution concerning forward-looking statements.* This section discusses how forward-looking statements made by us in the MD&A and elsewhere in this report are based on management's present expectations about future events and are inherently susceptible to uncertainty and changes in circumstances.
- *Overview.* This section provides an introductory overview and context for the discussion and analysis that follows in the MD&A.
- *Critical accounting policies.* This section discusses those accounting policies that are both considered important to our financial condition and operating results and require significant judgment and estimates on the part of management in their application.
- *Results of operations.* This section provides an analysis of our results of operations for the three and six months ended September 30, 2007 and 2006. A brief description is provided of transactions and events that impact the comparability of the results being analyzed.
- *Financial condition and liquidity.* This section provides an analysis of our cash position and cash flows, as well as a discussion of our financing arrangements and financial commitments.

CAUTION CONCERNING FORWARD-LOOKING STATEMENTS

The MD&A should be read in conjunction with the consolidated financial statements and notes thereto included in this report. This discussion contains forward-looking statements. These forward-looking statements are made as of the date of this report. Any statement that refers to an expectation, projection or other characterization of future events or circumstances, including the underlying assumptions, is a forward-looking statement. We use certain words and their derivatives such as "anticipate", "believe", "plan", "expect", "estimate", "predict", "intend", "may", "will", "should", "could", "future", "potential", and similar expressions in many of the forward-looking statements. The forward-looking statements are based on our current expectations, estimates and projections about our industry, management's beliefs, and other assumptions made by us. These statements and the expectations, estimates, projections, beliefs and other assumptions on which they are based are subject to many risks and uncertainties and are inherently subject to change. We describe many of the risks and uncertainties that we face in Part II, Item 1A, "Risk Factors" in this report. We update our descriptions of the risks and uncertainties facing us in our periodic reports filed with the SEC in which we report our financial condition and results for the quarter and fiscal year-to-date. Our actual results and actual events could differ materially from those anticipated in any forward-looking statement. Readers should not place undue reliance on any forward-looking statement.

OVERVIEW

We are a leader in semiconductors and printed circuit board assemblies ("PCBAs") for the communications and storage markets. We design, develop, market and support high-performance ICs and storage components, which are essential for the processing, transporting and storing of information worldwide. In the communications market, we utilize a combination of design expertise coupled with system-level knowledge and multiple technologies to offer IC products and PCBAs, for wireline and wireless communications equipment such as wireless base stations, edge switches, routers, gateways, metro transport platforms and core switches and routers. In the storage market, we blend systems and software expertise with high-performance, high-bandwidth silicon integration to deliver high-performance, high capacity serial advanced technology attachment ("SATA") redundant array of integrated disks ("RAID") controllers for emerging storage applications such as disk-to-disk backup, near-line storage, network-attached storage, video, and high-performance computing. Our corporate headquarters are located in Sunnyvale, California. Sales and engineering offices are located throughout the world.

The following tables present a summary of our results of operations for the three and six months ended September 30, 2007 and 2006 (dollars in thousands):

	Three Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Increase (Decrease)	% Change
Net revenues	$ 58,210	100.0%	$ 76,364	100.0%	$ (18,154)	(23.8)%
Cost of revenues	30,328	52.1	35,536	46.5	(5,208)	(14.7)
Gross profit	27,882	47.9	40,828	53.5	(12,946)	(31.7)
Total operating expenses	43,251	74.3	58,072	76.1	(14,821)	(25.5)
Operating loss	(15,369)	(26.4)	(17,244)	(22.6)	1,875	10.9
Interest and other income, net	6,906	11.9	3,429	4.5	3,477	101.4
Loss before income taxes	(8,463)	(14.5)	(13,815)	(18.1)	5,352	38.7
Income tax expense (benefit)	(410)	(0.7)	74	0.1	(484)	(654.1)
Net loss	$ (8,053)	(13.8)%	$ (13,889)	(18.2)%	$ 5,836	42.0

	Six Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Increase (Decrease)	% Change
Net revenues	$ 108,345	100.0%	$ 146,043	100.0%	$ (37,698)	(25.8)%
Cost of revenues	56,826	52.4	67,064	45.9	(10,238)	(15.3)
Gross profit	51,519	47.6	78,979	54.1	(27,460)	(34.8)
Total operating expenses	86,401	79.8	100,265	68.7	(13,864)	(13.8)
Operating loss	(34,882)	(32.2)	(21,286)	(14.6)	(13,596)	(63.9)
Interest and other income, net	9,982	9.2	6,794	4.7	3,188	46.9
Loss before income taxes	(24,900)	(23.0)	(14,492)	(9.9)	(10,408)	(71.8)
Income tax expense (benefit)	(427)	(0.4)	214	0.2	(641)	(299.5)
Net loss	$ (24,473)	(22.6)%	$ (14,706)	(10.1)%	$ (9,767)	(66.4)

Net Revenue. We generate revenues primarily through sales of our IC products, embedded processors and PCBAs to original equipment manufacturers ("OEMs"), such as Alcatel-Lucent, Ciena, Cisco, Brocade, Fujitsu, Hitachi, Huawei, Juniper, Ericsson, NEC, Nortel, Nokia Siemens Networks, and Tellabs, who in turn supply their equipment principally to communications service providers. In the storage market we generate revenues primarily through sales of our SATA RAID controllers to our distribution channel partners who in turn sell to enterprises, small and mid-size businesses, value added resellers ("VARs"), systems integrators and retail consumers.

The demand for our products has been affected in the past, and may continue to be affected in the future, by various factors, including, but not limited to, the following:

- the timing, rescheduling or cancellation of significant customer orders and our ability, as well as the ability of our customers, to manage inventory corrections;
- the qualification, availability and pricing of competing products and technologies and the resulting effects on sales and pricing of our products.
- our ability to specify, develop or acquire, complete, introduce, and market new products and technologies in a cost effective and timely manner;
- the rate at which our present and future customers and end-users adopt our products and technologies in our target markets;
- general economic and market conditions in the semiconductor industry and communications markets; and
- combinations of companies in our customer base, resulting in the combined company choosing our competitor's IC standardization other than our supported product platforms.

For these and other reasons, our net revenue and results of operations for the first three and six months ended September 30, 2007 and prior periods may not necessarily be indicative of future net revenue and results of operations.

Based on direct shipments, net revenues to customers that exceeded 10% of total net revenues in the three and six months ended September 30, 2007 and 2006 were as follows:

	Three Months Ended September 30,		Six Months Ended September 30,	
	2007	2006	2007	2006
Avnet Inc.	23%	26%	23%	26%
Hon Hai Precision Industry Co, Ltd.	10%	*	*	*

* Less than 10% of total net revenues for period indicated.

We expect that our largest customers will continue to account for a substantial portion of our net revenues for the foreseeable future.

Net revenues by geographic region were as follows (dollars in thousands):

	Three Months Ended September 30,			
	2007		2006	
	Amount	% of Net Revenue	Amount	% of Net Revenue
United States of America	$ 20,378	35.0%	$ 32,869	43.0%
Other North America	4,454	7.7	6,160	8.1
Europe and Israel	12,459	21.4	13,436	17.6
Asia	20,680	35.5	23,596	30.9
Other	239	0.4	303	0.4
	$ 58,210	100.0%	$ 76,364	100.0%

	Six Months Ended September 30,			
	2007		2006	
	Amount	% of Net Revenue	Amount	% of Net Revenue
United States of America	$ 38,941	35.9%	$ 59,826	41.0%
Other North America	8,593	7.9	16,348	11.2
Europe and Israel	22,696	20.9	25,351	17.4
Asia	37,654	34.8	43,677	29.8
Other	461	0.5	841	0.6
	$ 108,345	100.0%	$ 146,043	100.0%

All of our revenue to date has been denominated in U.S. dollars.

Net Loss. Our net loss has been affected in the past, and may continue to be affected in the future, by various factors, including, but not limited to, the following:

- stock-based compensation expense;
- amortization of purchased intangibles;
- acquired in-process research and development ("IPR&D");
- litigation settlement costs;
- restructuring charges;
- goodwill impairment charges;
- combinations of companies within our customer base;
- purchased intangible asset impairment charges; and
- income tax expenses (benefits).

Since the start of fiscal 2006, we have invested a total of $240.1 million in the research and development of new products, including higher-speed, lower-power and lower-cost products, products that combine the functions of multiple existing products into single highly integrated products, and other products to complete our portfolio of communications and storage products. These products, and our customers' products for which they are intended, are highly complex. Due to this complexity, it often takes several years to complete the development and qualification of these products before they enter into volume production. Accordingly, we have not yet generated significant revenues from some of the products developed during this time period. In addition, downturns in the telecommunications market can severely impact our customers' business and usually results in significantly less demand for our products than was expected when the development work commenced and, as a result of restructuring activities, we discontinued development of several products that were in process and slowed down development of others as we realized that demand for these products would not materialize as originally anticipated.

CRITICAL ACCOUNTING POLICIES

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of net revenue and expenses in the reporting period. We regularly evaluate our estimates and assumptions related to inventory valuation and warranty liabilities, which affects our cost of sales and gross margin; the valuation of purchased intangibles and goodwill, which affects our impairments of goodwill and amortization and impairments of other intangibles; the valuation of restructuring liabilities, which affects the amount and timing of restructuring charges; and the valuation of deferred income taxes, which affects our income tax expense and benefit. We also have other key accounting policies, such as our policies for stock-based compensation, revenue recognition, including the deferral of a portion of revenues on sales to distributors, and allowance for bad debts. The methods, estimates and judgments we use in applying these most critical accounting policies have a significant impact on the results we report in our financial statements. We base our estimates and assumptions on historical experience and on various other factors that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. The actual results experienced by us may differ materially and adversely from management's estimates. To the extent there are material differences between our estimates and the actual results, our future results of operations will be affected.

We believe the following critical accounting policies require us to make significant judgments and estimates in the preparation of our consolidated financial statements.

Inventory Valuation and Warranty Liabilities

Our policy is to value inventories at the lower of cost or market on a part-by-part basis. This policy requires us to make estimates regarding the market value of our inventories, including an assessment of excess or obsolete inventories. We determine excess and obsolete inventories based on an estimate of the future demand for our products within a specified time horizon, generally 12 months. The estimates we use for future demand are also used for near-term capacity planning and inventory purchasing and are consistent with our revenue forecasts. If our demand forecast is greater than our actual demand we may be required to take additional excess inventory charges, which would decrease gross margin and net operating results. For example, as of September 30, 2007, reducing our future demand estimate to six months could increase our current reserve balance by approximately $10.9 million or increasing our future demand forecast to 18 months could reduce our exposure by approximately $0.1 million below the current estimate.

Our products typically carry a one to three year warranty. We establish reserves for estimated product warranty costs at the time revenue is recognized. Although we engage in extensive product quality programs and processes, our warranty obligation is affected by product failure rates, use of materials and service delivery costs incurred in correcting any product failure and changes to master purchase agreements with our larger customers. Should actual product failure rates, use of materials or service delivery costs differ from our estimates, additional warranty reserves could be required, which could reduce our gross margin. Additional change to negotiated master purchase agreements could result in increased warranty reserves and unfavorably impact present and future gross margins.

Goodwill and Intangible Asset Valuation

The purchase method of accounting for acquisitions requires extensive use of accounting estimates and judgments to allocate the purchase price to the fair value of the net tangible and intangible assets acquired, including IPR&D. Goodwill and intangible assets deemed to have indefinite lives are not amortized, but are subject to annual impairment tests. The amounts and useful lives assigned to other intangible assets impact future amortization, and the amount assigned to IPR&D is expensed immediately. Determining the fair values and useful lives of intangible assets requires the use of estimates and the exercise of judgment. While there are a number of different generally accepted valuation methods to estimate the value of intangible assets acquired, we primarily use the discounted cash flow method and the market comparison approach. These

methods require significant management judgment to forecast the future operating results used in the analysis. In addition, other significant estimates are required such as residual growth rates and discount factors. The estimates we use to value and amortize intangible assets are consistent with the plans and estimates that we use to manage our business and are based on available historical information and industry estimates and averages. These judgments can significantly affect our net operating results.

We are required to assess goodwill impairment annually using the methodology prescribed by Statement of Financial Accounting Standards No. 142 ("SFAS 142"), *Goodwill and Other Intangible Assets*. SFAS 142 requires that goodwill be tested for impairment at the reporting unit level on at least an annual basis and between annual tests in certain circumstances. Application of the goodwill impairment test requires judgment, including the identification of reporting units, assigning assets and liabilities to reporting units, assigning goodwill to reporting units and determining the fair value of each reporting unit. In fiscal 2007 and 2006, in accordance with SFAS 142, we determined that there were three reporting units to be tested. The goodwill impairment test compares the implied fair value of the reporting unit with the carrying value of the reporting unit. The implied fair value of goodwill is determined in the same manner as in a business combination. Determining the fair value of the implied goodwill is judgmental in nature and often involves the use of significant estimates and assumptions. These estimates and assumptions could have a significant impact on whether or not an impairment charge is recognized and also the magnitude of any such charge. Estimates of fair value are primarily determined using discounted cash flows and market comparisons. These approaches use significant estimates and assumptions, including projection and timing of future cash flows, discount rates reflecting the risk inherent in future cash flows, perpetual growth rates, determination of appropriate market comparables, and determination of whether a premium or discount should be applied to comparables. It is possible that the plans and estimates used to value these assets may be incorrect. If our actual results, or the plans and estimates used in future impairment analyses, are lower than the original estimates used to assess the recoverability of these assets, we could incur additional impairment charges.

For fiscal 2007, the discounted cash flows for each reporting unit were based on discrete ten-year financial forecasts developed by management for planning purposes. Cash flows beyond the discrete forecasts were estimated using terminal value calculations. The sales compound annual growth rates ranged from 13% to 20% for the reporting units during the discrete forecast period and the future cash flows were discounted to present value using a discount rate of 16% and terminal growth rates of 4%. We did not recognize any goodwill impairment as a result of performing this annual test. A variance in the discount rate or the estimated revenue growth rate could have had a significant impact on the estimated fair value of the reporting unit and consequently the amount of identified goodwill impairment. For example, a 2% – 3% increase in the discount rate would have resulted in an indication of possible impairment that would have led us to further quantify the impairment and potentially record a charge to write-down these assets in fiscal 2007.

Restructuring Charges

Over the last several years we have undertaken significant restructuring initiatives, which have required us to develop formalized plans for exiting certain business activities and reducing spending levels. We have had to record estimated expenses for employee severance, long-term asset write downs, lease cancellations, facilities consolidation costs, and other restructuring costs. Given the significance, and the timing of the execution, of such activities, this process is complex and involves periodic reassessments of estimates made at the time the original decisions were made. In calculating the charges for our excess facilities, we have to estimate the timing of exiting certain facilities. Our assumptions for exiting and/or reoccupying certain facilities may be incorrect, which could result in the need to record additional costs or reduce estimated amounts previously charged to restructuring expense. For example, in fiscal 2007, when we decided to reoccupy a previously restructured facility, we eliminated the liability which reduced our restructuring expense. Our policies require us to periodically evaluate, at least semiannually, the adequacy of the remaining liabilities under our restructuring initiatives. During the six months ended September 30, 2007, we recorded restructuring charges of $1.4 million associated with our restructuring actions. In fiscal 2007, we recorded net restructuring charges of $1.3 million associated with our restructuring actions. For a full description of our restructuring activities, refer to our discussion of restructuring charges in the Results of Operations section.

Valuation of Deferred Income Taxes

We record valuation allowances to reduce our deferred tax assets to an amount that we believe is more likely than not to be realized. We consider estimated future taxable income and ongoing prudent and feasible tax planning strategies, including reversals of deferred tax liabilities, in assessing the need for a valuation allowance. If we were to determine that we will not realize all or part of our deferred tax assets in the future, we would make an adjustment to the carrying value of the deferred tax asset, which would be reflected as income tax expense. Conversely, if we were to determine that we will realize a deferred tax asset, which currently has a valuation allowance, we would reverse the valuation allowance which would be reflected as an income tax benefit or as an adjustment to stockholders' equity, for tax assets related to stock options, or goodwill, for tax assets related to acquired businesses.

Stock-Based Compensation Expense

Effective April 1, 2006 we adopted revised Statement of Financial Accounting Standards No. 123 ("SFAS 123(R)"), *Share-Based Payment*, SFAS 123(R) requires all share-based payments, including grants of stock options, restricted stock units and employee stock purchase rights, to be recognized in our financial statements based on their respective grant date fair values. Under this standard, the fair value of each employee stock option and employee stock purchase right is estimated on the date of grant using an option pricing model that meets certain requirements. We currently use the Black-Scholes option pricing model to estimate the fair value of our share-based payments. The Black-Scholes model meets the requirements of SFAS 123(R) but the fair values generated by the model may not be indicative of the actual fair values of our stock-based awards as it does not consider certain factors important to stock-based awards, such as continued employment, periodic vesting requirements and limited transferability. The determination of the fair value of share-based payment awards utilizing the Black-Scholes model is affected by our stock price and a number of assumptions, including expected volatility, expected life, risk-free interest rate and expected dividends. We estimate the expected volatility of our stock options at grant date by equally weighting the historical volatility and the implied volatility of our stock over specific periods of time as the expected volatility assumption required in the Black-Scholes model. The expected life of the stock options is based on historical and other data including life of the option and vesting period. The risk-free interest rate assumption is the implied yield currently available on zero-coupon government issues with a remaining term equal to the expected term. The dividend yield assumption is based on our history and expectation of dividend payouts. The fair value of our restricted stock units are based on the fair market value of our common stock on the date of grant. Stock-based compensation expense recognized in our financial statements in fiscal 2007 and thereafter was based on awards that are ultimately expected to vest. The amount of stock-based compensation expense in fiscal 2007 and thereafter was reduced for estimated forfeitures based on historical experience. Forfeitures are required to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ significantly from those estimated. We evaluate the assumptions used to value stock-based awards on a quarterly basis. If factors change and we employ different assumptions, stock-based compensation expense may differ significantly from what we have recorded in the past. If there are any modifications or cancellations of the underlying unvested securities, we may be required to accelerate, increase or cancel any remaining unearned stock-based compensation expense. We currently estimate when and if performance-based options will be earned. If the awards are not considered probable of achievement, no amount of stock-based compensation is recognized. If we considered the award to be probable, expense is recorded over the estimated service period. To the extent that our assumptions are incorrect, the amount of stock-based compensation recorded will be increased or decreased. To the extent that we grant additional equity securities to employees or we assume unvested securities in connection with any acquisitions, our stock-based compensation expense will be increased by the additional unearned compensation resulting from those additional grants or acquisitions.

Revenue Recognition

We recognize revenue in accordance with SEC Staff Accounting Bulletin No. 104, *Revenue Recognition*. These pronouncements require that four basic criteria be met before revenue can be recognized: 1) there is evidence that an arrangement exists; 2) delivery has occurred; 3) the fee is fixed or determinable; and 4) collectibility is reasonably assured. We recognize revenue upon determination that all criteria for revenue recognition have been met. In addition, we do not recognize revenue until all customers' acceptance criteria have been met. The criteria are usually met at the time of product shipment, except for shipments to distributors with rights of return. The portion of revenue from shipments to distributors subject to rights of return is deferred until the agreed upon percentage of return or cancellation privileges lapse. Revenue from shipments to distributors without return rights is recognized upon shipment. In addition, we record reductions to revenue for estimated allowances such as returns not pursuant to contractual rights, competitive pricing programs and rebates. These estimates are based on our experience with product returns and the contractual terms of the competitive pricing and rebate programs. Shipping terms are generally FCA (Free Carrier) shipping point. If actual returns or pricing adjustments exceed our estimates, we would record additional reductions to revenue.

Allowance for Bad Debts

We maintain an allowance for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. Our allowance for doubtful accounts is based on our assessment of the collectibility of specific customer accounts, the aging of accounts receivable, our history of bad debts, and the general condition of the industry. If a major customer's credit worthiness deteriorates, or our customers' actual defaults exceed our historical experience, our estimates could change and impact our reported results.

RESULTS OF OPERATIONS

Comparison of the Three and Six Months Ended September 30, 2007 to the Three and Six Months Ended September 30, 2006

Net Revenues. Net revenues for the three and six months ended September 30, 2007 was $58.2 million and $108.3 million respectively, representing a decrease of 23.8% and 25.8% from net revenues of $76.4 million and $146.0 million for the three and six months ended September 30, 2006. We classify our revenues into three categories based on markets that the underlying products serve. The categories are Integrated Communication Products ("ICP"), which consists of communications and embedded products, Storage and Other. We use this information to analyze our performance and success in these markets. See the following tables (dollars in thousands):

	Three Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Decrease	% Change
ICP	$ 45,344	77.9%	$ 63,012	82.5%	$ (17,668)	(28.0)%
Storage	12,229	21.0	12,323	16.1	(94)	(0.8)
Other	637	1.1	1,029	1.4	(392)	(38.1)
	$ 58,210	100.0%	$ 76,364	100.0%	$ (18,154)	(23.8)

	Six Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Increase (Decrease)	% Change
ICP	$ 81,788	75.5%	$ 119,005	81.5%	$ (37,217)	(31.3)%
Storage	25,473	23.5	24,553	16.8	920	3.7
Other	1,084	1.0	2,485	1.7	(1,401)	(56.4)
	$ 108,345	100.0%	$ 146,043	100.0%	$ (37,698)	(25.8)

The net revenue decrease for the three and six months ended September 30, 2007 was primarily due to downward inventory corrections at our customers, product transitions and overall softness in demand. The decline was primarily in net revenues of our ICP products.

The following table illustrates revenue from our focus and nonfocus areas (dollars in thousands):

	Three Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Decrease	% Change
Focus	$ 53,333	91.6%	$ 66,066	86.5%	$ (12,733)	(19.3)%
Nonfocus	4,877	8.4	10,298	13.5	(5,421)	(52.6)
	$ 58,210	100.0%	$ 76,364	100.0%	$ (18,154)	(23.8)

	Six Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Decrease	% Change
Focus	$ 98,991	91.4%	$ 123,462	84.5%	$ (24,471)	(19.8)%
Nonfocus	9,354	8.6	22,581	15.5	(13,227)	(58.6)
	$ 108,345	100.0%	$ 146,043	100.0%	$ (37,698)	(25.8)

As a result of our efforts to reduce ongoing operating expenses, we have refocused our product development efforts on higher growth opportunities ("focus" products) and away from certain legacy products ("nonfocus" products). Product areas we have focused on are products that process, transport and store information. Our process technology products focus on utilizing our sixth generation of network processor cores and our Power Architecture portfolio to meet the needs of the converged internet protocol ("IP")/Ethernet network while the transport technology products focus on Metro Ethernet, Triple Play access technologies and error correction solutions. The storage technology products address the needs of mass storage based on high-performance sequential input/output ("I/O"). The nonfocus product areas are our legacy switching products, application-specific integrated circuits ("ASICs"), Fibre Channel HBAs, storage area network ("SAN") ICs, pointer processors, and legacy framers. We expect the revenues from our nonfocus products to continue to decline in the future.

Gross Profit. The following table presents net revenues, cost of revenues and gross profit for the three and six months ended September 30, 2007 and 2006 (dollars in thousands):

	Three Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Decrease	% Change
Net revenues	$ 58,210	100.0%	$ 76,364	100.0%	$ (18,154)	(23.8)%
Cost of revenues	30,328	52.1	35,536	46.5	(5,208)	(14.7)
Gross profit	$ 27,882	47.9%	$ 40,828	53.5%	$ (12,946)	(31.7)

	Six Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Decrease	% Change
Net revenues	$ 108,345	100.0%	$ 146,043	100.0%	$ (37,698)	(25.8)%
Cost of revenues	56,826	52.4	67,064	45.9	(10,238)	(15.3)
Gross profit	$ 51,519	47.6%	$ 78,979	54.1%	$ (27,460)	(34.8)

The gross profit percentage for the three and six months ended September 30, 2007 declined to 47.9% and 47.6%, compared to 53.5% and 54.1% for the three and six months ended September 30, 2006, respectively. The decrease in gross profit percentage for the three and six months ended September 30, 2007 was primarily attributable to the decline in net revenues, unfavorable product mix and supply constraints on our transport and storage product lines that prevented us from shipping higher margin products, offset by favorable cost improvements. In addition, the gross profit for the three months ended September 30, 2007 included the reversal of $0.6 million of warranty reserves no longer required. We expect gross margins to improve marginally for the three months ending December 31, 2007.

The amortization of purchased intangible assets included in cost of revenues during the three and six months ended September 30, 2007 was $4.6 million and $9.3 million compared to $4.0 million and $7.7 million for the three and six months ended September 30, 2006. Based on the amount of capitalized purchased intangibles on the balance sheet as of September 30, 2007, we expect amortization expense for purchased intangibles charged to cost of revenues to be $18.5 million in fiscal 2008, $17.8 million in fiscal 2009 and $23.5 million for fiscal periods thereafter. Future acquisitions of businesses may result in substantial additional charges, which would impact the gross margin in future periods.

Research and Development and Selling, General and Administrative Expenses. The following table presents research and development and selling, general and administrative expenses for the three and six months ended September 30, 2007 and 2006 (dollars in thousands):

	Three Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Decrease	% Change
Research and development	$ 24,480	42.1%	$ 24,853	32.5%	$ (373)	(1.5)%
Selling, general and administrative	15,850	27.2	16,162	21.2	(312)	(1.9)

	Six Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Increase (Decrease)	% Change
Research and development	$ 49,962	46.1%	$ 47,692	32.7%	$ 2,270	4.8%
Selling, general and administrative	31,913	29.5	32,612	22.3	(699)	(2.1)

Research and Development. Research and development ("R&D") expenses consist primarily of salaries and related costs (including stock-based compensation) of employees engaged in research, design and development activities, costs related to engineering design tools, subcontracting costs and facilities expenses. The decrease in R&D expenses of 1.5% for the three months ended September 30, 2007, compared to the three months ended September 30, 2006, was primarily due to a $0.7 million reversal of a liability related to an arrangement to license tools due to renegotiated terms and a decrease of $0.6 million in other expenses, offset by an increase of $0.5 million in personnel expenses related to the acquisition of Quake and $0.4 million in foundry costs. The increase in R&D expenses of 4.8% for the six months ended September 30, 2007, compared to the six months ended September 30, 2006, was due to an increase of $1.6 million in personnel expenses related primarily to the acquisition of Quake, $1.1 million in foundry costs, $0.9 million for contractors and a decrease of $0.5 million in credits from order settlements offset by a $0.7 million reversal of a liability related to an arrangement to license tools and a decrease of $1.0 million in miscellaneous R&D expenses. We believe that a continued commitment to R&D is vital to our goal of maintaining a leadership position with innovative ICP and storage products. Currently, R&D expenses are focused on the development of ICP and storage products and we expect to continue this focus. We expect our R&D expenses to decrease in dollars as we take measures to reduce our overall operating expenses. These reductions will be offset by our continued investment in our product road map. Future acquisitions of businesses may result in substantial additional on-going costs.

Selling, General and Administrative. Selling, general and administrative ("SG&A") expenses consist primarily of personnel-related expenses, professional and legal fees, corporate branding and facilities expenses. The decrease in SG&A expenses of 1.9% for the three months ended September 30, 2007 compared to the three months ended September 30, 2006, was primarily due to a decrease of $1.0 million in personnel expenses, offset by an increase of $0.4 million in product interface software costs for demonstration products to specific requirements of potential customers and $0.3 million in stock-based compensation expense. The decrease in SG&A expenses of 2.1% for the six months ended September 30, 2007 compared to the six months ended September 30, 2006, was primarily due to a decrease of $0.7 million in personnel expenses. We expect our SG&A expenses to decrease in dollars as we take measures to reduce our overall operating expenses. Future acquisitions of businesses may result in substantial additional on-going costs.

Stock-Based Compensation. The following table presents stock-based compensation expense for the three and six months ended September 30, 2007 and 2006, which was included in the tables above (dollars in thousands):

	Three Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Increase	% Change
Costs of revenues	$ 240	0.4%	$ 158	0.2%	$ 82	51.9%
Research and development	1,216	2.1	1,028	1.3	188	18.3
Selling, general and administrative	1,841	3.2	1,492	2.0	349	23.4
	$ 3,297	5.7%	$ 2,678	3.5%	$ 619	23.1

	Six Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Increase	% Change
Costs of revenues	$ 312	0.3%	$ 291	0.2%	$ 21	7.2%
Research and development	2,271	2.1	2,097	1.4	174	8.3
Selling, general and administrative	3,334	3.1	2,801	1.9	533	19.0
	$ 5,917	5.5%	$ 5,189	3.6%	$ 728	14.0

On April 1, 2006 we adopted SFAS 123(R). The adoption of SFAS 123(R) will continue to have a significant adverse impact on our reported results of operations, although it will have no impact on our overall liquidity. The increase in stock-based compensation expense for the three and six months ended September 30, 2007 compared to the three and six months ended September 30, 2006 is primarily due to option grants. The amount of unearned stock-based compensation currently estimated to be expensed from now through fiscal 2012 related to unvested share-based payment awards at September 30, 2007 is $20.0 million. This expense relates to equity instruments already issued and will not be affected by our future stock price. The weighted-average period over which the unearned stock-based compensation is expected to be recognized is approximately 2.5 years. If there are any modifications or cancellations of the underlying unvested securities, we may be required to accelerate, increase or cancel any remaining unearned stock-based compensation expense. Future stock-based compensation expense will increase to the extent that we grant additional equity awards. We anticipate we will continue to grant additional employee stock options and restricted stock units in fiscal 2008 and thereafter. The value of these grants cannot be predicted at this time because it will depend on the number of share-based payments granted and the then current fair values.

Restructuring Charges. The following table presents restructuring charges for the three and six months ended September 30, 2007 and 2006 (dollars in thousands):

	Three Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Decrease	% Change
Restructuring charges	$ 1,376	2.4%	$ 1,419	1.9%	$ (43)	(3.0)%

	Six Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Decrease	% Change
Restructuring charges	$ 1,344	1.2%	$ 2,666	1.8%	$ (1,322)	(49.6)%

In March 2006, we communicated and began implementation of a plan to exit our operations in France and India and reorganize part of our manufacturing operations. The restructuring program included the elimination of approximately 68 employees. In fiscal 2006, we recorded a charge of approximately $7.6 million, consisting of $6.0 million for employee severance, $1.0 million for operating lease write-offs, and $0.6 million for asset impairments. During the three months ended September 30, 2006, we recorded an additional charge of approximately $0.7 million consisting of $0.1 million for operating lease write-offs, $0.1 million for operating lease commitments and $0.5 million for asset impairments. During the three months ended September 30, 2007, we paid down part of its remaining liability.

In June 2006, we implemented another restructuring program. The June 2006 restructuring program was implemented to reduce job redundancies. This restructuring program consisted of the elimination of approximately 20 employees. As a result of the June 2006 restructuring, we recorded a net charge of approximately $0.5 million, consisting of employee severances. During the first quarter of fiscal 2008, we paid all remaining liabilities related to this restructuring program and recorded a reversal of the remaining liability through restructuring expense.

In July 2007, we implemented another restructuring program. The July 2007 restructuring program was implemented to reduce job redundancies. This restructuring program consisted of the elimination of approximately 29 employees. As a result of the July 2007 restructuring program, we recorded a net charge of approximately $0.7 million, consisting of employee severances. During the three months ended September 30, 2007, we paid down part of our remaining liability.

In September 2007, we implemented another restructuring program. The September 2007 restructuring program was implemented to reduce job redundancies. This restructuring program consisted of approximately 28 employees. As a result of the September 2007 restructuring program, we recorded a net charge of approximately $0.7 million, consisting of employee severances. During the three months ended September 30, 2007, we paid down part of our remaining liability.

Option investigation and related expenses. The following table presents option investigation and related expenses for the three and six months ended September 30, 2007 and 2006 (dollars in thousands):

	Three Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Decrease	% Change
Option investigation	$ 209	0.4%	$ 1,150	1.5%	$ (941)	(81.8)%

	Six Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Increase (Decrease)	% Change
Option investigation	$ 501	0.5%	$ 1,700	1.2%	$ (1,199)	(70.5)%

During the three months ended June 30, 2006, we initiated a review of our historical stock option granting policies. We incurred professional and legal fees as a result of our self-initiated review. Though we have concluded our investigation during the three months ended March 31, 2007, we continue to incur expenses for the related ongoing legal and regulatory proceedings as a result of the option investigation.

Interest and Other Income. The following table presents interest and other income for the three and six months ended September 30, 2007 and 2006 (dollars in thousands):

	Three Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Increase (Decrease)	% Change
Interest income, net	$ 2,128	3.7%	$ 3,254	4.3%	$ (1,126)	(34.6)%
Other income, net	4,778	8.2	175	0.2	4,603	2,630.3

	Six Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Increase (Decrease)	% Change
Interest income, net	$ 5,176	4.8%	$ 6,595	4.5%	$ (1,419)	(21.5)%
Other income, net	4,806	4.4	199	0.1	4,607	2,315.1

Interest Income, net. Interest income, net of management fees, reflects interest earned on cash and cash equivalents and short-term investment balances as well as realized gains and losses from the sale of short-term investments, less interest expense. The decrease for the three and six months ended September 30, 2007 is primarily due to the impact of lower cash and short-term investment balances.

Other Income, net. The increase in other income, net for the three and six months ended September 30, 2007 is primarily due to the impact of $4.6 million of realized gain recorded from the sale of a strategic investment.

Income Taxes. The following table presents our income tax expense (benefit) for the three and six months ended September 30, 2007 and 2006 (dollars in thousands):

	Three Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Decrease	% Change
Income tax expense (benefit)	$ (410)	(0.7)%	$ 74	0.1%	$ (484)	(654.1)%

	Six Months Ended September 30,					
	2007		2006			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Decrease	% Change
Income tax expense (benefit)	$ (427)	(0.4)%	$ 214	0.1%	$ (641)	(299.5)%

The federal statutory income tax rate was 35% for the three months ended September 30, 2007 and 2006. The decrease in the income tax expense recorded for the three and six months ended September 30, 2007, is primarily due a reduction of $0.6 million in our income tax liability from the final settlement of an uncertain tax position in Israel. This is offset by the income tax expense relating to estimated foreign taxes and alternative minimum taxes.

FINANCIAL CONDITION AND LIQUIDITY

As of September 30, 2007, our principal source of liquidity consisted of $218.1 million in cash, cash equivalents and investments. Working capital as of September 30, 2007 was $177.2 million. Total cash, cash equivalents, and investments decreased by $66.4 million during the six months ended September 30, 2007 primarily as a result of cash paid for stock buybacks and structured stock repurchase agreements, cash paid for strategic investments and cash used to fund our operations, offset by realized gains from the sale of a strategic equity investment and other property. At September 30, 2007, we had contractual obligations not included on our balance sheet totaling $44.4 million, primarily related to facility leases, engineering design software tool licenses and inventory purchase commitments.

For the six months ended September 30, 2007, we used $23.4 million of cash in our operations compared to generating $3.5 million for the six months ended September 30, 2006. Our net loss of $24.5 million for the six months ended September 30, 2007 included $21.1 million of non-cash charges such as $3.2 million of depreciation, $12.0 million of amortization of purchased intangibles, and $5.9 million of stock-based compensation charges recorded in accordance with SFAS 123(R). The remaining change in operating cash flows for the six months ended September 30, 2007 primarily reflected increases in our inventories due to purchases of ICP inventory to meet estimated future demand and deferred revenue and decreases in accounts receivable, other assets, accounts payable and accrued payroll and other accrued liabilities. The decrease in our accounts receivable balance is attributable primarily to decreased revenues. Our overall days sales outstanding decreased to 36 days for the three months ended September 30, 2007, compared to 42 days for the three months ended March 31, 2007.

We generated $3.5 million of cash from our operations during the six months ended September 30, 2006. Our net loss of $14.7 million included $35.9 million of non-cash charges such as $4.7 million of depreciation, $10.7 million of amortization of purchased intangibles, $5.2 million of stock-based compensation charges recorded in accordance with SFAS 123(R), $13.3 million in in-process research and development charge related to the acquisition of Quake and $2.0 million in non-cash restructuring charges. The remaining change in operating cash flows primarily reflected increases in our accounts receivable, inventories, other assets, accounts payable and decreases in accrued payroll and other accrued liabilities, and deferred revenue. The increase in our accounts receivable balance is attributable primarily to the timing and collection of our receivables. The days sales outstanding was 44 days for the three months ended September 30, 2006. The increase in our inventory balance was attributable primarily to serve our longer term inventory commitments.

For the six months ended September 30, 2007, we generated $57.4 million of cash in investing activities compared to expending $12.7 million during the six months ended September 30, 2006. During the six months ended September 30, 2007, we generated net proceeds of $58.8 million from investment activities, $5.2 million in proceeds from the sale of a strategic investment, $1.6 million in proceeds from the sale of property, offset by $3.3 million for the purchase of property, equipment and other assets and $5.0 million in strategic investments.

The use of $12.7 million of cash from investing activities during the six months ended September 30, 2006 primarily reflects net proceeds of $63.5 million from the sales and maturities of short-term investments offset by $4.3 million in purchases of property, equipment and other assets and $72.0 million in net cash paid for the acquisition of Quake.

For the six months ended September 30, 2007, we used $36.8 million of cash in financing activities compared to $3.0 million for the six months ended September 30, 2006. The major financing use of cash for the six months ended September 30, 2007 was open market repurchase of our common stock and the funding of our structured stock repurchase agreements for $53.1 million offset by the sales of common stock through employee stock options of $3.3 million and proceeds of $13.2 million from the settlement of structured stock repurchase agreements.

The use of $3.0 million of cash for financing activities for the six months ended September 30, 2006 primarily reflects the net funding of our stock repurchase program of $2.8 million offset by the issuance of common stock through the exercise of employee stock options for $0.2 million.

In August 2004, our board of directors authorized a stock repurchase program for the repurchase of up to $200.0 million of our common stock. Under the program, we are authorized to make purchases in the open market or enter into structured agreements. During the six months ended September 30, 2007, 9.9 million shares were repurchased on the open market at a weighted average price of $2.95 per share. During the six months ended September 30, 2006, 6.2 million common shares were repurchased at a weighted average price of $3.23 per share. From the time the program was first implemented through September 30, 2007, a total of 25.5 million shares were repurchased on the open market at a weighted average price of $2.99 per share. All repurchased shares were retired upon delivery to us. At September 30, 2007, $51.2 million remained available to repurchase shares under the authorized program. We expect repurchases to continue under our stock repurchase program.

We also utilize structured stock repurchase agreements to buy back shares which are prepaid written put options on our common stock. We pay a fixed sum of cash upon execution of each agreement in exchange for the right to receive either a pre-determined amount of cash or stock depending on the closing market price of our common stock on the expiration date of the agreement. Upon expiration of each agreement, if the closing market price of our common stock is above the pre-determined price, we will have our investment returned with a premium. If the closing market price is at or below the pre-determined price, we will receive the number of shares specified at the agreement inception. Any cash received, including the premium, is treated as an increase to additional paid in capital on the balance sheet in accordance with the guidance issued in the Emerging Issues Task Force No. ("EITF") 00-19, *Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock*.

During the six months ended September 30, 2007, we entered into structured stock repurchase agreements totaling $23.8 million. For those agreements that had settled by September 30, 2007, we received 1.8 million shares of our common stock at an effective purchase price of $2.85 per share and $13.2 million in cash. At September 30, 2007, we had two outstanding structured stock repurchase agreements which settled with the receipt of $7.9 million in October 2007. During the six months ended September 30, 2006, we received $17.4 million in cash and 7.7 million shares of our common stock upon settlement of structured stock repurchase agreements. From the inception of our most recent stock repurchase program through September 30, 2007, we entered into structured stock repurchase agreements totaling $197.7 million. Upon settlement of these agreements through September 30, 2007, we received $128.7 million in cash and 24.7 million shares of our common stock at an effective purchase price of $2.52 per share.

The table below is a summary of our repurchase program share activity for the six months ended September 30, 2007 and 2006 (in thousands, except per share data):

	Six Months Ended September 30,	
	2007	2006
Open market repurchases:		
Aggregate repurchase price	$ 29,268	$ 20,137
Repurchased shares	9,915	6,242
Average price per share	$ 2.95	$ 3.23
Structured stock repurchase agreements:		
Shares acquired in settlement	1,757	7,696
Average price per share*	$ 2.85	$ 3.25
Total shares acquired by repurchase or in settlement	11,672	13,938
Average price per share	$ 2.94	$ 3.24

* The average price per share of shares acquired in settlements of structured stock repurchase agreements during the six months ended September 30, 2007 and 2006 does not include gains on settlements in cash of $1.3 million and $1.5 million, respectively.

The following table summarizes our contractual operating leases and other purchase commitments as of September 30, 2007 (in thousands):

	Operating Leases	Other Purchase Commitments	Total
Fiscal Years Ending March 31,			
2008	$ 15,222	$ 19,781	$ 35,003
2009	6,210	—	6,210
2010	2,240	—	2,240
2011	984	—	984
2012 and thereafter	—	—	—
Total minimum payments	$ 24,656	$ 19,781	$ 44,437

We did not have any off-balance sheet arrangements as of September 30, 2007 or March 31, 2007.

We believe that our available cash, cash equivalents and short-term investments will be sufficient to meet our capital requirements and fund our operations for at least the next 12 months, although we could elect or could be required to raise additional capital during such period. There can be no assurance that such additional debt or equity financing will be available on commercially reasonable terms or at all.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk is the potential loss arising from adverse changes in market rates and prices, such as foreign currency exchange rates, interest rates and a decline in the stock market. We are exposed to market risks related to changes in interest rates and foreign currency exchange rates.

We maintain an investment portfolio of various holdings, types and maturities. These securities are classified as available-for-sale and, consequently, are recorded on our consolidated balance sheets at fair value with unrealized gains or losses reported as a separate component of accumulated other comprehensive income or loss. We have established guidelines relative to diversification and maturities that attempt to maintain safety and liquidity. These guidelines are periodically reviewed and modified to take advantage of interest rate trends. We invest our excess cash in debt instruments of the U.S. Treasury, corporate bonds, mortgage-backed and asset backed securities and closed-end bond funds, with credit ratings as specified in our investment policy. We also have invested in preferred stocks, which pay quarterly fixed rate dividends. We generally do not utilize derivatives to hedge against increases in interest rates which decrease market values, except for investments managed by one investment manager who utilizes U.S. Treasury bond futures options ("futures options") as a protection against the impact of increases in interest rates on the fair value of preferred stocks managed by that investment manager.

We are exposed to market risk as it relates to changes in the market value of our investments. At September 30, 2007, our investment portfolio included fixed-income securities classified as available-for-sale investments and marketable securities with an aggregate fair market value of $169.2 million and a cost basis of $173.8 million. These securities are subject to interest rate risk, as well as credit risk, and will decline in value if interest rates increase or an issuer's credit rating or financial condition is decreased. The following table presents the hypothetical changes in fair value of our short-term investments held at September 30, 2007 (in thousands):

	Valuation of Securities Given an Interest Rate Decrease of X Basis Points ("BPS")			Fair Value as of September 30, 2007	Valuation of Securities Given an Interest Rate Increase of X Basis Points ("BPS")		
	(150 BPS)	(100 BPS)	(50 BPS)		50 BPS	100 BPS	150 BPS
Available-for-sale investments	$ 181,149	$ 177,037	$ 173,109	$ 169,236	$ 165,587	$ 162,433	$ 159,251

The modeling technique used measures the change in fair market value arising from selected potential changes in interest rates. Market changes reflect immediate hypothetical parallel shifts in the yield curve of plus or minus 50 basis points, 100 basis points, and 150 basis points.

We invest in equity instruments of private companies for business and strategic purposes. These investments are valued based on our historical cost, less any recognized impairments. The estimated fair values are not necessarily representative of the amounts that we could realize in a current transaction.

We generally conduct business, including sales to foreign customers, in U.S. dollars, and as a result, we have limited foreign currency exchange rate risk. However, we have entered into forward currency exchange contracts to hedge our overseas monthly operating expenses when deemed appropriate. Gains and losses on foreign currency forward contracts that are designated and effective as hedges of anticipated transactions, for which a firm commitment has been attained, are deferred and included in the basis of the transaction in the same period that the underlying transaction is settled. Gains and losses on any instruments not meeting the above criteria are recognized in income or expenses in the consolidated statement of operations in the current period. The effect of an immediate 10 percent change in foreign exchange rates would not have a material impact on our financial condition or results of operations.

ITEM 4. CONTROLS AND PROCEDURES

Our chief executive officer and chief financial officer performed an evaluation of our disclosure controls and procedures (as defined in Rule 13a-15(e) of the Exchange Act) as of September 30, 2007. Based on that evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures were effective and sufficient to ensure that the information required to be disclosed in the reports that we file under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms.

Changes in Internal Control Over Financial Reporting

There was no change in our internal controls over financial reporting that occurred during the most recent quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The information set forth under Note 7 of Notes to Consolidated Financial Statements, included in Part I, Item 1 of this report, is incorporated herein by reference.

ITEM 1A. RISK FACTORS

Before deciding to invest in us or to maintain or increase your investment, you should carefully consider the risks described below, in addition to the other information contained in this report and in our other filings with the SEC. We update our descriptions of the risks and uncertainties facing us in our periodic reports filed with the SEC. The risks and uncertainties described below and in our other filings are not the only ones facing us. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also affect our business. If any of these known or unknown risks or uncertainties actually occurs, our business, financial condition and results of operations could be seriously harmed. In that event, the market price for our common stock could decline and you may lose your investment. The risks and uncertainties set forth below with an asterisk ("") next to the title contain changes to the description of the risks and uncertainties associated with our business as previously disclosed in Item 1A to our Annual Report on Form 10-K for the fiscal year ended March 31, 2007.*

Our business strategy may contemplate the acquisition of other companies, products and technologies. Merger and acquisition activities involve numerous risks and we may not be able to address these risks successfully without substantial expense, delay or other operational or financial problems. *

Acquiring products, technologies or businesses from third parties is part of our business strategy. The risks involved with merger and acquisition activities include:

- potential dilution to our stockholders;
- use of a significant portion of our cash reserves;
- diversion of management's attention;
- failure to retain or integrate key personnel;
- difficulty in completing an acquired company's in-process research or development projects;
- amortization of acquired intangible assets and deferred compensation;
- customer dissatisfaction or performance problems with an acquired company's products or services;
- costs associated with acquisitions or mergers;
- difficulties associated with the integration of acquired companies, products or technologies;
- difficulties competing in markets that are unfamiliar to us;
- ability of the acquired companies to meet their financial projections; and
- assumption of unknown liabilities, or other unanticipated events or circumstances.

Any of these risks could materially harm our business, financial condition and results of operations.

As with past acquisitions, future acquisitions could adversely affect operating results. In particular, acquisitions may materially and adversely affect our results of operations because they may require large one-time charges or could result in increased debt or contingent liabilities, adverse tax consequences, substantial additional depreciation or deferred compensation charges. Our past purchase acquisitions required us to capitalize significant amounts of goodwill and purchased intangible assets. As a result of the slowdown in our industry and reduction of our market capitalization, we have been required to record significant impairment charges against these assets as noted in our financial statements. At September 30, 2007, we had $403.5 million of goodwill and purchased intangible assets. We cannot assure you that we will not be required to take additional significant charges as a result of an impairment to the carrying value of these assets, due to further declines in market conditions.

Our operating results may fluctuate because of a number of factors, many of which are beyond our control. *

If our operating results are below the expectations of public market analysts or investors, then the market price of our common stock could decline. Some of the factors that affect our quarterly and annual results, but which are difficult to control or predict are:

- communications, information technology and semiconductor industry conditions;
- fluctuations in the timing and amount of customer requests for product shipments;
- the reduction, rescheduling or cancellation of orders by customers, including as a result of slowing demand for our products or our customers' products or over-ordering of our products or our customers' products;
- changes in the mix of products that our customers buy;
- the gain or loss of one or more key customers or their key customers, or significant changes in the financial condition of one or more of our key customers or their key customers;
- our ability to introduce, certify and deliver new products and technologies on a timely basis;
- the announcement or introduction of products and technologies by our competitors;
- competitive pressures on selling prices;
- the ability of our customers to obtain components from their other suppliers;
- market acceptance of our products and our customers' products;
- fluctuations in manufacturing output, yields or other problems or delays in the fabrication, assembly, testing or delivery of our products or our customers' products;
- increases in the costs of products or discontinuance of products by suppliers;
- the availability of external foundry capacity, contract manufacturing services, purchased parts and raw materials including packaging substrates;
- problems or delays that we and our foundries may face in shifting the design and manufacture of our future generations of IC products to smaller geometry process technologies and in achieving higher levels of design and device integration;
- the amounts and timing of costs associated with warranties and product returns;
- the amounts and timing of investments in research and development;
- the amounts and timing of the costs associated with payroll taxes related to stock option exercises or settlement of restricted stock units;
- costs associated with acquisitions and the integration of acquired companies, products and technologies;
- the impact of potential one-time charges related to purchased intangibles;
- our ability to successfully integrate acquired companies, products and technologies;
- the impact on interest income of a significant use of our cash for an acquisition, stock repurchase or other purpose;
- the effects of changes in interest rates or credit worthiness on the value and yield of our short-term investment portfolio;
- costs associated with compliance with applicable environmental, other governmental or industry regulations including costs to redesign products to comply with those regulations or lost revenue due to failure to comply in a timely manner;
- the effects of changes in accounting standards;
- costs associated with litigation, including without limitation, attorney fees, litigation judgments or settlements, relating to the use or ownership of intellectual property or our internal option review or other claims arising out of our operations;
- our ability to identify, hire and retain senior management and other key personnel;
- the effects of war, acts of terrorism or global threats, such as disruptions in general economic activity and changes in logistics and security arrangements; and
- general economic conditions.

Our business, financial condition and operating results would be harmed if we do not achieve anticipated revenues.

We can have revenue shortfalls for a variety of reasons, including:

- the reduction, rescheduling or cancellation of customer orders;
- declines in the average selling prices of our products;
- delays when our customers are transitioning from old products to new products;
- a decrease in demand for our products or our customers' products;
- a decline in the financial condition or liquidity of our customers or their customers;
- delays in the availability of our products or our customers' products;
- the failure of our products to be qualified in our customers' systems or certified by our customers;
- excess inventory of our products at our customers resulting in a reduction in their order patterns as they work through the excess inventory of our products;
- fabrication, test, product yield, or assembly constraints for our products that adversely affect our ability to meet our production obligations;
- the failure of one of our subcontract manufacturers to perform its obligations to us;
- our failure to successfully integrate acquired companies, products and technologies; and
- shortages of raw materials or production capacity constraints that lead our suppliers to allocate available supplies or capacity to other customers, which may disrupt our ability to meet our production obligations.

Our business is characterized by short-term orders and shipment schedules. Customer orders typically can be cancelled or rescheduled without significant penalty to the customer. Because we do not have substantial non-cancellable backlog, we typically plan our production and inventory levels based on internal forecasts of customer demand, which is highly unpredictable and can fluctuate substantially. Customer orders for our products typically have non-standard lead times, which make it difficult for us to predict revenues and plan inventory levels and production schedules. If we are unable to plan inventory levels and production schedules effectively, our business, financial condition and operating results could be materially harmed.

From time to time, in response to anticipated long lead times to obtain inventory and materials from our outside contract manufacturers, suppliers and foundries, we may order materials in advance of anticipated customer demand. This advance ordering has in the past and may in the future result in excess inventory levels or unanticipated inventory write-downs if expected orders fail to materialize, or other factors render our products less marketable. If we are forced to hold excess inventory or we incur unanticipated inventory write-downs, our financial condition and operating results could be materially harmed.

Our expense levels are relatively fixed and are based on our expectations of future revenues. We have limited ability to reduce expenses quickly in response to any revenue shortfalls. Changes to production volumes and impact of overhead absorption may result in a decline in our financial condition or liquidity.

Our business substantially depends upon the continued growth of the technology sector and the Internet.

The technology equipment industry is cyclical and has experienced significant and extended downturns in the past. A substantial portion of our business and revenue depends on the continued growth of the technology sector and the Internet. We sell our communications IC products primarily to communications equipment manufacturers that in turn sell their equipment to customers that depend on the growth of the Internet. OEMs and other customers that buy our storage products are similarly dependent on continued Internet growth and information technology spending. If there is an economic slowdown or reduction in capital spending, our business, operating results, and financial condition may be materially harmed.

The loss of one or more key customers, the diminished demand for our products from a key customer, or the failure to obtain certifications from a key customer or its distribution channel could significantly reduce our revenues and profits. *

A relatively small number of customers have accounted for a significant portion of our revenues in any particular period. We have no long-term volume purchase commitments from our key customers. One or more of our key customers may discontinue operations as a result of consolidation, liquidation or otherwise. Reductions, delays and cancellation of orders from our key customers or the loss of one or more key customers could significantly reduce our revenues and profits. We cannot assure you that our current customers will continue to place orders with us, that orders by existing customers will continue at current or historical levels or that we will be able to obtain orders from new customers.

Our ability to maintain or increase sales to key customers and attract significant new customers is subject to a variety of factors, including:

- customers may stop incorporating our products into their own products with limited notice to us and may suffer little or no penalty;
- customers or prospective customers may not incorporate our products in their future product designs;
- design wins with customers or prospective customers may not result in sales to such customers;
- the introduction of new products by customers may be later or less successful in the market than planned;
- we may successfully design a product to customer specifications but the customer may not be successful in the market;
- sales of customer product lines incorporating our products may rapidly decline or the product lines may be phased out;
- our agreements with customers typically are non-exclusive and do not require them to purchase a minimum amount of our products;
- many of our customers have pre-existing relationships with current or potential competitors that may cause them to switch from our products to competing products;
- some of our OEM customers may develop products internally that would replace our products;
- we may not be able to successfully develop relationships with additional network equipment vendors;
- our relationships with some of our larger customers may deter other potential customers (who compete with these customers) from buying our products;
- the impact of terminating certain sales representatives or sales personnel as a result of a Company workforce reduction or otherwise; and
- the continued viability of our customers and prospective customers.

The occurrence of any one of the factors above could have a material adverse effect on our business, financial condition and results of operations.

In addition, before we can sell our storage products to an OEM, either directly or through the OEM's distribution channel, that OEM must certify our products. The certification process can take up to 12 months. This process requires the commitment of OEM personnel and test equipment, and we compete with other suppliers for these resources. Any delays in obtaining these certifications or any failure to obtain these certifications would adversely affect our ability to sell our storage products.

There is no guarantee that design wins will become actual orders and sales.

A "design win" occurs when a customer or prospective customer notifies us that our product has been selected to be integrated with the customer's product. There can be delays of several months or more between the design win and when a customer initiates actual orders of our product. Following a design win, we will commit significant resources to the integration of our product into the customer's product before receiving the initial order. Receipt of an initial order from a customer, however, is dependent on a number of factors, including the success of the customer's product, and cannot be guaranteed. The design win may never result in an actual order or sale.

Any significant order cancellations or order deferrals could cause unplanned inventory growth resulting in excess inventory which may adversely affect our operating results. *

Our customers may increase orders during periods of product shortages or cancel orders if their inventories are too high. Major inventory corrections by our customers are not uncommon and can last for significant periods of time and affect demand for our product. Customers may also cancel or delay orders in anticipation of new products or for other reasons. Cancellations or deferrals could cause us to hold excess inventory, which could reduce our profit margins by reducing sales prices, incurring inventory write-downs or writing off additional obsolete product.

Inventory fluctuations could affect our results of operations and restrict our ability to fund our operations. Inventory management remains an area of focus as we balance the need to maintain strategic inventory levels to ensure competitive lead times against the risk of inventory obsolescence because of changing technology and customer requirements.

We generally recognize revenue upon shipment of products to a customer. If a customer refuses to accept shipped products or does not pay for these products, we could miss future revenue projections or incur significant charges against our income, which could materially and adversely affect our operating results.

Our customers' products typically have lengthy design cycles. A customer may decide to cancel or change its product plans, which could cause us to lose anticipated sales. *

After we have developed and delivered a product to a customer, the customer will usually test and evaluate our product prior to designing its own equipment to incorporate our product. Our customers may need more than six months to test, evaluate and adopt our product and an additional nine months or more to begin volume production of equipment that incorporates our product. Due to this lengthy design cycle, we may experience significant delays from the time we increase our operating expenses and make investments in inventory until the time that we generate revenue from these products. It is possible that we may never generate any revenue from these products after incurring such expenditures. Even if a customer selects our product to incorporate into its equipment, we cannot assure you that the customer will ultimately market and sell its equipment or that such efforts by our customer will be successful. The delays inherent in this lengthy design cycle increase the risk that a customer will decide to cancel or change its product plans. Such a cancellation or change in plans by a customer could cause us to lose sales that we had anticipated.

While our customers' design cycles are typically long, some of our product life cycles tend to be short as a result of the rapidly changing technology environment in which we operate. As a result, the resources devoted to product sales and marketing may not generate material revenue for us, and from time to time, we may need to write off excess and obsolete inventory. If we incur significant marketing expenses and investments in inventory in the future that we are not able to recover, and we are not able to mitigate those expenses, our operating results could be adversely affected. In addition, if we sell our products at reduced prices in anticipation of cost reductions but still hold higher cost products in inventory, our operating results would be harmed.

An important part of our strategy is to continue our focus on the markets for communications and storage equipment. If we are unable to further expand our share of these markets, our revenues may not grow and could decline. *

Our markets frequently undergo transitions in which products rapidly incorporate new features and performance standards on an industry-wide basis. If our products are unable to support the new features or performance levels required by OEMs in these markets, or if our products fail to be certified by OEMs, we would lose business from an existing or potential customer and may not have the opportunity to compete for new design wins or certification until the next product transition occurs. If we fail to develop products with required features or performance standards, or if we experience a delay as short as a few months in certifying or bringing a new product to market, or if our customers fail to achieve market acceptance of their products, our revenues could be significantly reduced for a substantial period.

We expect a significant portion of our revenues to continue to be derived from sales of products based on current, widely accepted transmission standards. If the communications market evolves to new standards, we may not be able to successfully design and manufacture new products that address the needs of our customers or gain substantial market acceptance.

Customers for our products generally have substantial technological capabilities and financial resources. Some customers have traditionally used these resources to internally develop their own products. The future prospects for our products in these markets are dependent upon our customers' acceptance of our products as an alternative to their internally developed products. Future prospects also are dependent upon acceptance of third-party sourcing for products as an alternative to in-house development. Network equipment vendors may in the future continue to use internally developed components. They also may decide to develop or acquire components, technologies or products that are similar to, or that may be substituted for, our products.

If our network equipment vendor customers fail to accept our products as an alternative, if they develop or acquire the technology to develop such components internally rather than purchase our products, or if we are otherwise unable to develop or maintain strong relationships with them, our business, financial condition and results of operations would be materially and adversely affected.

Our industry and markets are subject to consolidation, which may result in stronger competitors, fewer customers and reduced demand.

There has been industry consolidation among communications IC companies, network equipment companies and telecommunications companies in the past. We expect this consolidation to continue as companies attempt to strengthen or hold their positions in evolving markets. Consolidation may result in stronger competitors, fewer customers and reduced demand, which in turn could have a material adverse effect on our business, operating results, and financial condition.

Our operating results are subject to fluctuations because we rely heavily on international sales.

International sales account for a significant part of our revenues and may account for an increasing portion of our future revenues. The revenues we derive from international sales may be subject to certain risks, including:

- foreign currency exchange fluctuations;
- changes in regulatory requirements;
- tariffs and other barriers;
- timing and availability of export licenses;
- political and economic instability;
- difficulties in accounts receivable collections;
- difficulties in staffing and managing foreign operations;
- difficulties in managing distributors;
- difficulties in obtaining governmental approvals for communications and other products;
- reduced or uncertain protection for intellectual property rights in some countries;
- longer payment cycles to collect accounts receivable in some countries;
- the burden of complying with a wide variety of complex foreign laws and treaties; and
- potentially adverse tax consequences.

We are subject to risks associated with the imposition of legislation and regulations relating to the import or export of high technology products. We cannot predict whether quotas, duties, taxes or other charges or restrictions upon the importation or exportation of our products will be implemented by the United States or other countries.

Because sales of our products have been denominated to date primarily in United States dollars, increases in the value of the United States dollar could increase the price of our products so that they become relatively more expensive to customers in the local currency of a particular country, leading to a reduction in sales and profitability in that country. Future international activity may result in increased foreign currency denominated sales. Gains and losses on the conversion to United States dollars of accounts receivable, accounts payable and other monetary assets and liabilities arising from international operations may contribute to fluctuations in our results of operations.

Some of our customer purchase orders and agreements are governed by foreign laws, which may differ significantly from laws in the United States. As a result, our ability to enforce our rights under such agreements may be limited compared with our ability to enforce our rights under agreements governed by laws in the United States.

Our cash and cash equivalents and portfolio of short-term investments and long-term marketable securities are exposed to certain market risks. *

We maintain an investment portfolio of various holdings, types of instruments and maturities. These securities are recorded on our consolidated balance sheets at fair value with unrealized gains or losses reported as a separate component of accumulated other comprehensive income (loss), net of tax. Our investment portfolio is exposed to market risks related to changes in interest rates and credit ratings of the issuers, as well as to the risks of default by the issuers. Substantially all of these securities are subject to interest rate and credit rating risk and will decline in value if interest rates increase or one of the issuers' credit ratings is reduced. Increases in interest rates or decreases in the credit worthiness of one or more of the issuers in our investment portfolio could have a material adverse impact on our financial condition or results of operations. As of September 30, 2007, we determined $77.7 million of our available-for-sale securities are long-term. These securities have fair values that have been less than their amortized cost for 12 or more consecutive months. If the fair value of any of these securities does not recover to at least the amortized cost of such security or we are unable to hold these securities until they recover, we may be required to record as expense the decline in the value of these securities. At September 30, 2007, the continuous unrealized losses on these securities over the 12 months preceding September 30, 2007 was approximately $3.5 million.

Our restructuring activities could result in management distractions, operational disruptions and other difficulties. *

Over the past several years, we have initiated several restructuring activities in an effort to reduce operating costs, including a new restructuring initiatives announced in July and September 2007. Employees whose positions were eliminated in connection with these restructuring plans may seek future employment with our customers or competitors. Although all employees are required to sign a confidentiality agreement with us at the time of hire, we cannot assure you that the confidential nature of our proprietary information will be maintained in the course of such future employment. Any additional restructuring efforts could divert the attention of our management away from our operations, harm our reputation and increase our expenses. We cannot assure you that we will not undertake additional restructuring activities, that any of our restructuring efforts will be successful, or that we will be able to realize the cost savings and other anticipated benefits from our previous or future restructuring plans. In addition, if we continue to reduce our workforce, it may adversely impact our ability to respond rapidly to any new growth opportunities.

Our markets are subject to rapid technological change, so our success depends heavily on our ability to develop and introduce new products. *

The markets for our products are characterized by:

- rapidly changing technologies;
- evolving and competing industry standards;
- changing customer needs;
- frequent new product introductions and enhancements;
- increased integration with other functions;
- long design and sales cycles;
- short product life cycles; and
- intense competition.

To develop new products for the communications, storage or other technology markets, we must develop, gain access to and use leading technologies in a cost-effective and timely manner and continue to develop technical and design expertise. We must have our products designed into our customers' future products and maintain close working relationships with key customers in order to develop new products that meet customers' changing needs. We must respond to changing industry standards, trends towards increased integration and other technological changes on a timely and cost-effective basis. Our pursuit of technological advances may require substantial time and expense and may ultimately prove unsuccessful. If we are not successful in adopting such advances, we may be unable to timely bring to market new products and our revenues will suffer.

Many of our products are based on industry standards that are continually evolving. Our ability to compete in the future will depend on our ability to identify and ensure compliance with these evolving industry standards. The emergence of new industry standards could render our products incompatible with products developed by major systems manufacturers. As a result, we could be required to invest significant time and effort and to incur significant expense to redesign our products to ensure compliance with relevant standards. If our products are not in compliance with prevailing industry standards or requirements, we could miss opportunities to achieve crucial design wins which in turn could have a material adverse effect on our business, operating and financial results.

The markets in which we compete are highly competitive, and we expect competition to increase in these markets in the future. *

The markets in which we compete are highly competitive, and we expect that domestic and international competition will increase in these markets, due in part to deregulation, rapid technological advances, price erosion, changing customer preferences and evolving industry standards. Increased competition could result in significant price competition, reduced revenues, lower profit margins or loss of market share. Our ability to compete successfully in our markets depends on a number of factors, including:

- our ability to partner with OEM and channel partners who are successful in the market;
- success in designing and subcontracting the manufacture of new products that implement new technologies;
- product quality, interoperability, reliability, performance and certification;
- customer support;
- time-to-market;

- price;
- production efficiency;
- design wins;
- expansion of production of our products for particular systems manufacturers;
- end-user acceptance of the systems manufacturers' products;
- market acceptance of competitors' products; and
- general economic conditions.

Our competitors may offer enhancements to existing products, or offer new products based on new technologies, industry standards or customer requirements, that are available to customers on a more timely basis than comparable products from us or that have the potential to replace or provide lower cost alternatives to our products. The introduction of enhancements or new products by our competitors could render our existing and future products obsolete or unmarketable. We expect that certain of our competitors and other semiconductor companies may seek to develop and introduce products that integrate the functions performed by our IC products on a single chip, thus eliminating the need for our products. Each of these factors could have a material adverse effect on our business, financial condition and results of operations.

In the communications IC markets, we compete primarily against companies such as LSI, Broadcom, Intel, Mindspeed, PMC-Sierra and Vitesse. In the storage market, we primarily compete against companies such as Adaptec, Areca, Hewlett-Packard, LSI, and Promise. Our embedded processor products compete against products from Freescale Semiconductor, IBM and Intel. Many of these companies have substantially greater financial, marketing and distribution resources than we have. Certain of our customers or potential customers have internal IC design or manufacturing capabilities with which we compete. We may also face competition from new entrants to our target markets, including larger technology companies that may develop or acquire differentiating technology and then apply their resources to our detriment. Any failure by us to compete successfully in these target markets, would have a material adverse effect on our business, financial condition and results of operations.

The storage market continues to mature and become commoditized. To the extent that commoditization leads to significant pricing declines, whether initiated by us or by a competitor, we will be required to increase our product volumes and reduce our costs of goods sold to avoid resulting pressure on our profit margin for these products, and we cannot assure you that we will be successful in responding to these competitive pricing pressures.

We do not have an internal wafer fabrication capability, which could result in unanticipated liability and reduced revenues.

During fiscal 2003, we closed our internal wafer fabrication facility and no longer have the ability to manufacture products internally. As a result, we are subject to substantial risks, including:

- if we have not effectively stored certain products manufactured in our internal facility before its closure, we may incur liability to those customers to whom we have committed to deliver such products; and
- we may be unable to repair or replace such products.

Our dependence on third-party manufacturing and supply relationships increases the risk that we will not have an adequate supply of products to meet demand or that our cost of materials will be higher than expected.

We depend upon third parties to manufacture, assemble or package certain of our products. As a result, we are subject to risks associated with these third parties, including:

- reduced control over delivery schedules and quality;
- inadequate manufacturing yields and excessive costs;
- difficulties selecting and integrating new subcontractors;
- potential lack of adequate capacity during periods of excess demand;
- limited warranties on products supplied to us;
- potential increases in prices;
- potential instability in countries where third-party manufacturers are located; and
- potential misappropriation of our intellectual property.

Our outside foundries generally manufacture our products on a purchase order basis, and we have very few long-term supply arrangements with these suppliers. We have less control over delivery schedules, manufacturing yields and costs than competitors with their own fabrication facilities. A manufacturing disruption experienced by one or more of our outside foundries or a disruption of our relationship with an outside foundry, including discontinuance of our products by that foundry, would negatively impact the production of certain of our products for a substantial period of time.

Our IC products are generally only qualified for production at a single foundry. These suppliers can allocate, and in the past have allocated, capacity to the production of other companies' products while reducing deliveries to us on short notice. There is also the potential that they may discontinue manufacturing our products or go out of business. Because establishing relationships, designing or redesigning ICs, and ramping production with new outside foundries may take over a year, there is no readily available alternative source of supply for these products.

Difficulties associated with adapting our technology and product design to the proprietary process technology and design rules of outside foundries can lead to reduced yields of our IC products. The process technology of an outside foundry is typically proprietary to the manufacturer. Since low yields may result from either design or process technology failures, yield problems may not be effectively determined or resolved until an actual product exists that can be analyzed and tested to identify process sensitivities relating to the design rules that are used. As a result, yield problems may not be identified until well into the production process, and resolution of yield problems may require cooperation between us and our manufacturer. This risk could be compounded by the offshore location of certain of our manufacturers, increasing the effort and time required to identify, communicate and resolve manufacturing yield problems. Manufacturing defects that we do not discover during the manufacturing or testing process may lead to costly product recalls. These risks may lead to increased costs or delayed product delivery, which would harm our profitability and customer relationships.

If the foundries or subcontractors we use to manufacture our products discontinue the manufacturing processes needed to meet our demands, or fail to upgrade their technologies needed to manufacture our products, we may be unable to deliver products to our customers, which could materially adversely affect our operating results. The transition to the next generation of manufacturing technologies at one or more of our outside foundries could be unsuccessful or delayed.

Our requirements typically represent a very small portion of the total production of the third-party foundries. As a result, we are subject to the risk that a producer will cease production of an older or lower-volume process that it uses to produce our parts. We cannot assure you that our external foundries will continue to devote resources to the production of our products or continue to advance the process design technologies on which the manufacturing of our products are based. Each of these events could increase our costs and materially impact our ability to deliver our products on time.

Some companies that supply our customers are similarly dependent on a limited number of suppliers to produce their products. These other companies' products may be designed into the same networking equipment into which our products are designed. Our order levels could be reduced materially if these companies are unable to access sufficient production capacity to produce in volumes demanded by our customers because our customers may be forced to slow down or halt production on the equipment into which our products are designed.

Our operating results depend on manufacturing output and yields of our ICs and printed circuit board assemblies, which may not meet expectations.

The yields on wafers we have manufactured decline whenever a substantial percentage of wafers must be rejected or a significant number of die on each wafer are nonfunctional. Such declines can be caused by many factors, including minute levels of contaminants in the manufacturing environment, design issues, defects in masks used to print circuits on a wafer, and difficulties in the fabrication process. Design iterations and process changes by our suppliers can cause a risk of defects. Many of these problems are difficult to diagnose, are time consuming and expensive to remedy, and can result in shipment delays.

We estimate yields per wafer and final packaged parts in order to estimate the value of inventory. If yields are materially different than projected, work-in-process inventory may need to be revalued. We may have to take inventory write-downs as a result of decreases in manufacturing yields. We may suffer periodic yield problems in connection with new or existing products or in connection with the commencement of production at a new manufacturing facility.

We may experience difficulties in transitioning to smaller geometry process technologies or in achieving higher levels of design integration and that may result in reduced manufacturing yields, delays in product deliveries and increased expenses.

As smaller line width geometry processes become more prevalent, we expect to integrate greater levels of functionality into our IC products and to transition our IC products to increasingly smaller geometries. This transition will require us to redesign certain products and will require us and our foundries to migrate to new manufacturing processes for our products.

We may not be able to achieve higher levels of design integration or deliver new integrated products on a timely basis. We periodically evaluate the benefits, on a product-by-product basis, of migrating to smaller geometry process technologies to reduce our costs and increase performance, and we have designed IC products to be manufactured at as little as .09 micron geometry processes. We have experienced some difficulties in shifting to smaller geometry process technologies and new manufacturing processes. These difficulties resulted in reduced manufacturing yields, delays in product deliveries and increased expenses. We may face similar difficulties, delays and expenses as we continue to transition our IC products to smaller geometry processes. We are dependent on our relationships with our foundries to transition to smaller geometry processes successfully. We cannot assure you that our foundries will be able to effectively manage the transition or that we will be able to maintain our relationships with our foundries. If we or our foundries experience significant delays in this transition or fail to implement this transition, our business, financial condition and results of operations could be materially and adversely affected.

We must develop or otherwise gain access to improved IC process technologies.

Our future success will depend upon our ability to improve existing IC process technologies or acquire new IC process technologies. In the future, we may be required to transition one or more of our IC products to process technologies with smaller geometries, other materials or higher speeds in order to reduce costs or improve product performance. We may not be able to improve our process technologies or otherwise gain access to new process technologies in a timely or affordable manner. Products based on these technologies may not achieve market acceptance.

The complexity of our products may lead to errors, defects and bugs, which could negatively impact our reputation with customers and result in liability.

Products as complex as ours may contain errors, defects and bugs when first introduced or as new versions are released. Our products have in the past experienced such errors, defects and bugs. Delivery of products with production defects or reliability, quality or compatibility problems could significantly delay or hinder market acceptance of the products or result in a costly recall and could damage our reputation and adversely affect our ability to retain existing customers and to attract new customers. Errors, defects or bugs could cause problems with device functionality, resulting in interruptions, delays or cessation of sales to our customers.

We may also be required to make significant expenditures of capital and resources to resolve such problems. We cannot assure you that problems will not be found in new products after commencement of commercial production, despite testing by us, our suppliers or our customers. Any problem could result in:

- additional development costs;
- loss of, or delays in, market acceptance;
- diversion of technical and other resources from our other development efforts;
- claims by our customers or others against us; and
- loss of credibility with our current and prospective customers.

Any such event could have a material adverse effect on our business, financial condition and results of operations.

If our internal controls over financial reporting are not considered effective, our business and stock price could be adversely affected.

Section 404 of the Sarbanes-Oxley Act of 2002 requires us to evaluate the effectiveness of our internal controls over financial reporting as of the end of each fiscal year, and to include a management report assessing the effectiveness of our internal controls over financial reporting in our annual report on Form 10-K for that fiscal year. Section 404 also requires our independent registered public accounting firm to attest to, and report on, management's assessment of our internal controls over financial reporting.

Our management, including our chief executive officer and chief financial officer, does not expect that our internal controls over financial reporting will prevent all 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. Further, 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. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud involving a company have been, or will be, detected. The design of any system of controls is based in part on certain assumptions about the likelihood of future events, and we cannot assure you that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

Our management has concluded, and our independent registered public accounting firm has attested, that our internal control over financial reporting was effective as of March 31, 2007. In connection with the investigation of our historical stock option grant practices, we did identify material weaknesses in our internal control over financial reporting that existed in fiscal years prior to fiscal 2005. We cannot assure you that we or our independent registered public accounting firm will not identify a material weakness in our internal controls in the future. A material weakness in our internal controls over financial reporting would require management and our independent registered public accounting firm to evaluate our internal controls as ineffective. If our internal controls over financial reporting are not considered effective, we may experience another restatement and/or a loss of public confidence, which could have an adverse effect on our business and on the market price of our common stock.

If we are unable to transition our accounting function smoothly, our ability to report our financial results accurately or on a timely basis may be adversely affected.

We are in the process of completing the transition of most of our accounting functions from San Diego to Sunnyvale. We also have open employment positions in the accounting department that will remain in San Diego. If we are unable to complete the transition to the new team in an effective manner, it could adversely impact our ability to report our financial results accurately and/or in a timely manner. The inability to transition to the new accounting team in an effective manner could also have an adverse impact on our internal control environment. This could cause us to have material weaknesses in our internal controls over our financial reporting and consequently could cause our management or our independent registered public accounting firm to determine our internal controls are ineffective. If this were to occur, it could have an adverse impact on our business and could cause us to lose public confidence and may jeopardize the continued listing of our common stock, which could have an adverse impact on the market price of our common stock.

Our future success depends in part on the continued service of our key senior management, design engineering, sales, marketing, and manufacturing personnel and our ability to identify, hire and retain additional, qualified personnel.

Our future success depends to a significant extent upon the continued service of our senior management personnel. The loss of key senior executives could have a material adverse effect on our business. There is intense competition for qualified personnel in the semiconductor industry, in particular design, product and test engineers, and we may not be able to continue to attract and retain engineers or other qualified personnel necessary for the development of our business, or to replace engineers or other qualified personnel who may leave our employment in the future. There may be significant costs associated with recruiting, hiring and retention of personnel. Periods of contraction in our business may inhibit our ability to attract and retain our personnel. Loss of the services of, or failure to recruit, key design engineers or other technical and management personnel could be significantly detrimental to our product development or other aspects of our business.

To manage operations effectively, we will be required to continue to improve our operational, financial and management systems and to successfully hire, train, motivate, and manage our employees. The integration of future acquisitions would require significant additional management, technical and administrative resources. We cannot assure you that we would be able to manage our expanded operations effectively.

Our ability to supply a sufficient number of products to meet demand could be severely hampered by a shortage of water, electricity or other supplies, or by natural disasters or other catastrophes.

The manufacture of our products requires significant amounts of water. Previous droughts have resulted in restrictions being placed on water use by manufacturers. In the event of a future drought, reductions in water use may be mandated generally and our external foundries' ability to manufacture our products could be impaired.

Several of our facilities, including our principal executive offices, are located in California. In 2001, California experienced prolonged energy alerts and blackouts caused by disruption in energy supplies. As a consequence, California continues to experience substantially increased costs of electricity and natural gas. We are unsure whether these alerts and blackouts will reoccur or how severe they may become in the future. Many of our customers and suppliers are also headquartered or have substantial operations in California. If we or any of our major customers or suppliers located in California, experience a sustained disruption in energy supplies, our results of operations could be materially and adversely affected.

A portion of our test and assembly facilities are located in our San Diego, California location and a significant portion of our manufacturing operations are located in Asia. These areas are subject to natural disasters such as earthquakes or floods. We do not have earthquake or business interruption insurance for these facilities, because adequate coverage is not offered at economically justifiable rates. A significant natural disaster or other catastrophic event could have a material adverse impact on our business, financial condition and operating results.

The effects of war, acts of terrorism or global threats, including, but not limited to, the outbreak of epidemic disease, could have a material adverse effect on our business, operating results and financial condition. The continued threat of terrorism and heightened security and military action in response to this threat, or any future acts of terrorism, may cause further disruptions to local and global economies and create further uncertainties. To the extent that such disruptions or uncertainties result in delays or cancellations of customer orders, or the manufacture or shipment of our products, our business, operating results and financial condition could be materially and adversely affected.

We have been named as a party to several derivative action lawsuits arising from our internal option review, and we may be named in additional litigation, all of which could require significant management time and attention and result in significant legal expenses and may result in an unfavorable outcome which could have a material adverse effect on our business, financial condition, results of operations and cash flows.

We are subject to a number of lawsuits purportedly on behalf of Applied Micro Circuits Corporation against certain of our current and former executive officers and board members, and we may become the subject of additional private or government actions. The expense of defending such litigation may be significant. The amount of time to resolve these lawsuits is unpredictable and defending ourselves may divert management's attention from the day-to-day operations of our business, which could adversely affect our business, results of operations and cash flows. In addition, an unfavorable outcome in such litigation could have a material adverse effect on our business, results of operations and cash flows.

As a result of our option review and restatement, we are subject to investigations by the SEC and Department of Justice ("DOJ"), which may not be resolved favorably and have required, and may continue to require, a significant amount of management time and attention and accounting and legal resources, which could adversely affect our business, results of operations and cash flows.

The SEC and the DOJ are currently conducting investigations relating to our historical stock option grant practices. We have been responding to, and continue to respond to, inquiries from the SEC and DOJ. The period of time necessary to resolve the SEC and DOJ investigations is uncertain, and these matters could require significant management and financial resources which could otherwise be devoted to the operation of our business. If we are subject to an adverse finding resulting from the SEC and DOJ investigations, we could be required to pay damages or penalties or have other remedies imposed upon us. The restatement of our financial statements, the ongoing SEC and DOJ investigations and any negative outcome that may occur from these investigations could impact our relationships with customers and our ability to generate revenue. In addition, considerable legal and accounting expenses related to these matters have been incurred to date and significant expenditures may continue to be incurred in the future. The SEC and DOJ investigations, and any negative outcome that may result from such investigation, could adversely affect our business, results of operations, financial position and cash flows.

The process of restating our financial statements, making the associated disclosures, and complying with SEC requirements was subject to uncertainty and evolving requirements. *

We worked with our independent registered public accounting firm and the SEC to make our filings comply with all related requirements. The issues surrounding the historical stock option grant practices are complex and the regulatory guidelines or requirements continue to evolve. There can be no assurance that we will not be required to further amend our filings with the SEC. In addition to the cost and time to amend financial reports, such an amendment may have a material adverse effect on our investors' confidence and our common stock price.

If we do not maintain compliance with Nasdaq listing requirements, our common stock could be delisted, which could have a material adverse effect on the trading price of our common stock and cause some investors to lose interest in our company.

As a result of our option investigation, we were delinquent in filing certain of our periodic reports with the SEC, and consequently we were not in compliance with Nasdaq's Marketplace Rules. As a result, we underwent a review and hearing process with Nasdaq to determine our listing status. Once we filed the delinquent periodic reports with the SEC, Nasdaq permitted our securities to remain listed on the Nasdaq Global Select Market, but our securities could be delisted in the future if we do not maintain compliance with applicable listing requirements. Being delisted could affect our access to the capital markets and our ability to raise capital through alternative financing sources on terms acceptable to us or at all and could cause our investors, suppliers, customers and employees to lose confidence in us.

We could incur substantial fines or litigation costs associated with our storage, use and disposal of hazardous materials. *

We are subject to a variety of federal, state and local governmental regulations related to the use, storage, discharge and disposal of toxic, volatile or otherwise hazardous chemicals that were used in our manufacturing process. Any failure to comply with present or future regulations could result in the imposition of fines, the suspension of production or a cessation of operations. These regulations could require us to acquire costly equipment or incur other significant expenses to comply with environmental regulations or clean up prior discharges. Since 1993, we have been named as a potentially responsible party ("PRP") along with a large number of other companies that used Omega Chemical Corporation in Whittier, California to handle and dispose of certain hazardous waste material. We are a member of a large group of PRPs that has agreed to fund certain on-going remediation efforts at the Omega Chemical site. To date, our payment obligations with respect to these funding efforts have not been material, and we believe that our future obligations to fund these efforts will not have a material adverse effect on our business, financial condition or operating results. In 2003, we closed our wafer fabrication facility in San Diego, and the property was returned to the landlord. In operating the facility at this site, we stored and used hazardous materials. Although we believe that we have been and currently are in material compliance with applicable environmental laws and regulations, we cannot assure you that we are or will be in material compliance with these laws or regulations or that our future obligations to fund any remediation efforts, including those at the Omega Chemical site, will not have a material adverse effect on our business.

Environmental laws and regulations could cause a disruption in our business and operations.

We are subject to various state, federal and international laws and regulations governing the environment, including those restricting the presence of certain substances in electronic products and making manufacturers of those products financially responsible for the collection, treatment, recycling and disposal of certain products. Such laws and regulations have been passed in several jurisdictions in which we operate, including various European Union ("EU") member countries. For example, the European Union has enacted the Restriction of the Use of Certain Hazardous Substances in Electrical and Electronic Equipment ("RoHS") and the Waste Electrical and Electronic Equipment ("WEEE") directives. RoHS prohibits the use of lead and other substances, in semiconductors and other products put on the market after July 1, 2006. The WEEE directive obligates parties that place electrical and electronic equipment on the market in the EU to put a clearly identifiable mark on the equipment, register with and report to EU member countries regarding distribution of the equipment, and provide a mechanism to take back and properly dispose of the equipment. There can be no assurance that similar programs will not be implemented in other jurisdictions resulting in additional costs, possible delays in delivering products, and even the discontinuance of existing and planned future product replacements if cost were to become prohibitive.

Any acquisitions we make could disrupt our business and harm our results of operation and financial condition. *

In August 2006, we acquired Quake Technologies, Inc. (now know as "AMCC Canada"), and we may make additional investments in or acquire other companies, products or technologies. These acquisitions involve numerous risks, including:

- problems combining or integrating the purchased operations, technologies or products;
- unanticipated costs;
- diversion of management's attention from our core business;
- adverse effects on existing business relationships with suppliers and customers;
- risks associated with entering markets in which we have no or limited prior experience; and
- potential loss of key employees, particularly those of the acquired organizations.

In addition, in the event of any such investments or acquisitions, we could

- issue stock that would dilute our current stockholders' percentage ownership;
- incur debt;
- assume liabilities;
- incur amortization or impairment expenses related to goodwill and other intangible assets; or
- incur large and immediate write-offs.

We cannot assure you that we will be able to successfully integrate any businesses, products, technologies or personnel that we might acquire. For example, with the acquisition of AMCC Canada, we acquired the technology necessary to introduce 10 Gigabit Ethernet physical layer chips and advance our efforts in the enterprise part of the market. 10 Gigabit Ethernet is an emerging technology, and we cannot assure you that this technology will be successful. In addition, several of our competitors have introduced similar products in the last quarter. If our customers do not purchase our new power amplifier modules, our development and integration efforts will have been unsuccessful, and our business may suffer.

Our subsidiary has been named as a defendant in litigation that could result in substantial costs and divert management's attention and resources.

JNI Corporation, which we acquired in October 2003, has a number of pending lawsuits relating to alleged securities law violations and alleged breaches of fiduciary duty. We believe that the claims pending against JNI are without merit, and we have engaged in a vigorous defense against such claims. If we are not successful in our defense against such claims, we could be forced to make significant payments to the plaintiffs and their lawyers, and such payments could have a material adverse effect on our business, financial condition and results of operations if not covered by our insurance carriers. Even if such claims are not successful, the litigation could result in substantial costs including, but not limited to, attorney and expert fees, and divert management's attention and resources, which could have an adverse effect on our business. Although insurers have paid defense costs to date, we cannot assure you that insurers will continue to pay such costs, judgments or other expenses associated with the lawsuit.

We may not be able to protect our intellectual property adequately. *

We rely in part on patents to protect our intellectual property. We cannot assure you that our pending patent applications or any future applications will be approved, or that any issued patents will adequately protect the intellectual property in our products, will provide us with competitive advantages or will not be challenged by third parties, or that if challenged, any such patent will be found to be valid or enforceable. Others may independently develop similar products or processes, duplicate our products or processes or design around any patents that may be issued to us.

To protect our intellectual property, we also rely on the combination of mask work protection under the Federal Semiconductor Chip Protection Act of 1984, trademarks, copyrights, trade secret laws, employee and third-party nondisclosure agreements, and licensing arrangements. Despite these efforts, we cannot assure you that others will not independently develop substantially equivalent intellectual property or otherwise gain access to our trade secrets or intellectual property, or disclose such intellectual property or trade secrets, or that we can meaningfully protect our intellectual property. A failure by us to meaningfully protect our intellectual property could have a material adverse effect on our business, financial condition and operating results.

We generally enter into confidentiality agreements with our employees, consultants and strategic partners. We also try to control access to and distribution of our technologies, documentation and other proprietary information. Despite these efforts, parties may attempt to copy, disclose, obtain or use our products, services or technology without our authorization. Also, former employees may seek employment with our business partners, customers or competitors and we cannot assure you that the confidential nature of our proprietary information will be maintained in the course of such future employment. Additionally, former employees or third parties could attempt to penetrate our network to misappropriate our proprietary information or interrupt our business. Because the techniques used by computer hackers to access or sabotage networks change frequently and generally are not recognized until launched against a target, we may be unable to anticipate these techniques. As a result, our technologies and processes may be misappropriated, particularly in foreign countries where laws may not protect our proprietary rights as fully as in the United States.

We could be harmed by litigation involving patents, proprietary rights or other claims.

Litigation may be necessary to enforce our intellectual property rights, to determine the validity and scope of the proprietary rights of others or to defend against claims of infringement or misappropriation. The semiconductor industry is characterized by substantial litigation regarding patent and other intellectual property rights. Such litigation could result in substantial costs and diversion of resources, including the attention of our management and technical personnel, and could have a material adverse effect on our business, financial condition and results of operations. We may be accused of infringing on the intellectual property rights of third parties. We have certain indemnification obligations to customers with respect to the infringement of third-party intellectual property rights by our products. We cannot assure you that infringement claims by third parties or claims for indemnification by customers or end users resulting from infringement claims will not be asserted in the future, or that such assertions will not harm our business.

Any litigation relating to the intellectual property rights of third parties would at a minimum be costly and could divert the efforts and attention of our management and technical personnel. In the event of any adverse ruling in any such litigation, we could be required to pay substantial damages, cease the manufacturing, use and sale of infringing products, discontinue the use of certain processes or obtain a license under the intellectual property rights of the third party claiming infringement. A license might not be available on reasonable terms or at all.

From time to time, we may be involved in litigation relating to other claims arising out of our operations in the normal course of business. We cannot assure you that the ultimate outcome of any such matters will not have a material, adverse effect on our business, financial condition or operating results.

Our stock price is volatile.

The market price of our common stock has fluctuated significantly. In the future, the market price of our common stock could be subject to significant fluctuations due to general economic and market conditions and in response to quarter-to-quarter variations in:

- our anticipated or actual operating results;
- announcements or introductions of new products by us or our competitors;
- anticipated or actual operating results of our customers, peers or competitors;
- technological innovations or setbacks by us or our competitors;
- conditions in the semiconductor, communications or information technology markets;
- the commencement or outcome of litigation or governmental investigations;
- changes in ratings and estimates of our performance by securities analysts;
- announcements of merger or acquisition transactions;
- management changes;
- our inclusion in certain stock indices; and
- other events or factors.

The stock market in recent years has experienced extreme price and volume fluctuations that have affected the market prices of many high technology companies, particularly semiconductor companies. In some instances, these fluctuations appear to have been unrelated or disproportionate to the operating performance of the affected companies. Any such fluctuation could harm the market price of our common stock.

The anti-takeover provisions of our certificate of incorporation and of the Delaware general corporation law may delay, defer or prevent a change of control.

Our board of directors has the authority to issue up to 2,000,000 shares of preferred stock and to determine the price, rights, preferences and privileges and restrictions, including voting rights, of those shares without any further vote or action by our stockholders. The rights of the holders of common stock will be subject to, and may be harmed by, the rights of the holders of any shares of preferred stock that may be issued in the future. The issuance of preferred stock may delay, defer or prevent a change in control, as the terms of the preferred stock that might be issued could potentially prohibit our consummation of any merger, reorganization, sale of substantially all of our assets, liquidation or other extraordinary corporate transaction without the approval of the holders of the outstanding shares of preferred stock. The issuance of preferred stock could have a dilutive effect on our stockholders.

If we issue additional shares of stock in the future, it may have a dilutive effect on our stockholders.

We have a significant number of authorized and unissued shares of our common stock available. These shares will provide us with the flexibility to issue our common stock for proper corporate purposes, which may include making acquisitions through the use of stock, adopting additional equity incentive plans and raising equity capital. Any issuance of our common stock may result in immediate dilution of our stockholders.

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

Below is a summary of stock repurchases for the three months ended September 30, 2007 (in thousands, except average price per share).

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Amount that May Yet Be Purchased Under the Plans or Programs
July 1 – July 31, 2007	—	$ —	—	$ 71,329
August 1 – August 31, 2007	7,000	2.88	7,000	51,199
September 1– September 30, 2007 (1)	—		—	51,199
Total shares repurchased	7,000	$ 2.88	7,000	$ 51,199

(1) At September 30, 2007, we had two structured stock repurchase agreements outstanding.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

We held our annual meeting of stockholders on August 21, 2007. Of the 280.4 million shares of our common stock that could be voted at the annual meeting, 251.4 million shares, or 90% were represented at the meeting in person or by proxy, which constituted a quorum. Voting results were as follows:

Election of the following persons to our Board of Directors to hold office until the next annual meeting of stockholders:

	For	Withheld
Cesar Cesaratto	239,275,449	12,083,709
Donald Colvin	243,129,854	8,229,304
Kambiz Hooshmand	244,046,128	7,313,030
Niel Ransom	241,214,264	10,144,894
Fred Shlapak	243,129,558	8,229,600
Arthur B. Stabenow	217,928,814	33,430,344
Julie H. Sullivan	243,128,719	8,230,439

Ratification of the appointment of Ernst & Young LLP as our independent registered public accounting firm for the period ending March 31, 2008:

For	Against	Abstain
246,886,992	4,344,165	128,001

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

3.1(1)	Amended and Restated Certificate of Incorporation of the Company.
3.2(2)	Amended and Restated Bylaws of the Company.
4.1(3)	Specimen Stock Certificate.
10.1(4)	Executive Severance Benefit Plan adopted September 19, 2007.
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended.
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended.
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(1) Incorporated by reference to Exhibit 3.2 filed with the Company's Registration Statement (No. 333-37609) filed October 10, 1997, and as amended by Exhibit 3.3 filed with the Company's Registration Statement (No. 333-45660) filed September 12, 2000.

(2) Incorporated by reference to identically numbered exhibit filed with the Company's Quarterly Report on Form 10-Q for the quarter ended December 31, 2001.

(3) Incorporated by reference to identically numbered exhibit filed with the Company's Registration Statement (No. 333-37609) filed October 10, 1997, or with any amendments thereto, which registration statement became effective November 24, 1997.

(4) Incorporated by reference to Exhibit 99.1 filed with the Company's Current Report on Form 8-K filed September 24, 2007.

SIGNATURES

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

Date: November 9, 2007

Applied Micro Circuits Corporation

By: /s/ Robert G. Gargus

Robert G. Gargus
Senior Vice President and Chief Financial Officer
(Duly Authorized Signatory and Principal
Financial and Accounting Officer)

Exhibit Index

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Exhibit 31.1

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

I, Kambiz Hooshmand, President and Chief Executive Officer, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Applied Micro Circuits Corporation;

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 that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

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

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

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

/s/ Kambiz Hooshmand

Kambiz Hooshmand
President and Chief Executive Officer

Date: November 9, 2007

Exhibit 31.2

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

I, Robert G. Gargus, Senior Vice President and Chief Financial Officer, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Applied Micro Circuits Corporation;

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 that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

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

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

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

/s/ Robert G. Gargus

Robert G. Gargus,
Senior Vice President and Chief Financial Officer

Dated: November 9, 2007

Exhibit 32.1

CERTIFICATION

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C.§ 1350, as adopted), Kambiz Hooshmand, Chief Executive Officer of Applied Micro Circuits Corporation (the "Company"), hereby certifies that, to the best of his knowledge:

1. This Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2007 (the "Report") fully complies with the requirements of section 13(a) or section 15(d) of the Securities Exchange Act of 1934, as amended (the "Exchange Act").

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission ("SEC") or its staff upon request.

This certification accompanies the Report to which it relates, is not deemed filed with the SEC and is not to be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Exchange Act (whether made before or after the date of the Report), irrespective of any general incorporation language contained in such filing.

/s/ Kambiz Hooshmand

Kambiz Hooshmand
President and Chief Executive Officer

Dated: November 9, 2007

Exhibit 32.2

CERTIFICATION

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C.§ 1350, as adopted), Robert G. Gargus, Chief Financial Officer of Applied Micro Circuits Corporation (the "Company"), hereby certifies that, to the best of his knowledge:

1. This Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2007 (the "Report") fully complies with the requirements of section 13(a) or section 15(d) of the Securities Exchange Act of 1934, as amended (the "Exchange Act").

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission ("SEC") or its staff upon request.

This certification accompanies the Report to which it relates, is not deemed filed with the SEC and is not to be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Exchange Act (whether made before or after the date of the Report), irrespective of any general incorporation language contained in such filing.

/s/ Robert G. Gargus

Robert G. Gargus,
Senior Vice President and Chief Financial Officer

Dated: November 9, 2007