

EXTREME NETWORKS INC
Form PRE 14A
October 23, 2009
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

SCHEDULE 14A INFORMATION

Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934

Filed by the Registrant

Filed by a Party other than the Registrant

Check the appropriate box:

- Preliminary Proxy Statement
- Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))
- Definitive Proxy Statement
- Definitive Additional Materials
- Soliciting Material Pursuant to §240.14a-12

EXTREME NETWORKS, INC.

(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

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- No fee required.

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

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

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

 - 4) Proposed maximum aggregate value of transaction:

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- Fee paid previously with preliminary materials.

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 - 1) Amount Previously Paid:

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

 - 3) Filing Party:

 - 4) Date Filed:

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Extreme Networks, Inc.
3585 Monroe Street
Santa Clara, California 95051
(408) 579-2800

, 2009

Dear Stockholder:

You are cordially invited to attend our 2009 Annual Meeting of Stockholders to be held on Wednesday, December 23, 2009 at 2 p.m. Pacific Time at the Executive Briefing Center at our headquarters located at 3585 Monroe Street, Santa Clara, California 95051.

At this meeting, you are being requested to:

Elect three Class II members of the Board of Directors for a three-year term,

Ratify the appointment of our independent auditors for our fiscal year ending June 27, 2010,

Approve a voluntary program (the *Exchange Program*) that will permit eligible employees to exchange certain outstanding stock options that are underwater for a lesser number of shares of restricted stock units to be granted under the Extreme Networks 2005 Equity Incentive Plan (the *2005 Plan*), and with respect to stock options that are more substantially underwater, a cash payment,

Approve an amendment to the 2005 Plan to increase the shares of common stock reserved for issuance under the 2005 Plan by 5,300,000 shares from 23,000,000 shares to 28,300,000 shares, and

Transact such other business as may properly come before the meeting and any adjournment or postponement thereof.

Our Board of Directors recommends that you vote in favor of these proposals. Please refer to the Notice of Annual Meeting of Stockholders and Proxy Statement for further information on each of these proposals.

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It is important that you use this opportunity to take part in the affairs of Extreme Networks by voting on the business to come before this meeting. After reading the Proxy Statement, please promptly mark, sign, date and return the enclosed proxy card in the prepaid envelope to ensure that your shares will be represented. We also provide our stockholders the opportunity to receive stockholder communications electronically. If you elected for electronic delivery of the Proxy Statement and Annual Report on Form 10-K for fiscal year 2009, as amended, you will not be receiving a proxy card and must vote electronically. For more information, see *Electronic Delivery of Stockholder Communications* in the Proxy Statement. Our Annual Report on Form 10-K for the fiscal year ended June 28, 2009, as amended, is also enclosed.

If you have any further questions concerning the annual meeting or either of the proposals, please contact our proxy solicitor, MacKenzie Partners, Inc., toll free at (800) 322-2885 or our investor relations department at (408) 579-3030. We look forward to your attendance at the annual meeting.

Yours Very Truly,

Bob L. Corey

Acting President and Chief Executive Officer

Senior Vice President, Finance and

Chief Financial Officer

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NOTICE OF ANNUAL MEETING OF STOCKHOLDERS

December 23, 2009

TO THE STOCKHOLDERS:

Notice is hereby given that the Annual Meeting of Stockholders of Extreme Networks, Inc., a Delaware corporation, will be held on Wednesday, December 23, 2009 at 2 p.m. Pacific Time at the Executive Briefing Center at our headquarters located at 3585 Monroe Street, Santa Clara, California 95051, in order to:

1. Elect three Class II directors to hold office for a three-year term and until their successors are elected and qualified or until their earlier resignation or removal,
2. Ratify the appointment of Ernst & Young LLP, independent registered public accounting firm, as our independent auditors for the fiscal year ending June 27, 2010,
3. Approve a voluntary program (the *Exchange Program*) that will permit eligible employees to exchange certain outstanding stock options that are underwater for a lesser number of shares of restricted stock units to be granted under the Extreme Networks 2005 Equity Incentive Plan (the *2005 Plan*), and with respect to stock options that are more substantially underwater, a cash payment,
4. Approve an amendment to the 2005 Plan to increase the shares of common stock reserved for issuance under the 2005 Plan by 5,300,000 shares from 23,000,000 shares to 28,300,000 shares, and
5. Transact such other business as may properly come before the meeting and any adjournment or postponement thereof.

Stockholders of record at the close of business on _____, 2009 are entitled to notice of, and to vote at, this meeting and any adjournment or postponement thereof. For ten days prior to the meeting, a complete list of stockholders entitled to attend and vote at the meeting will be available for review by any stockholder during normal business hours at our headquarters located at 3585 Monroe Street, Santa Clara, California 95051.

BY ORDER OF THE BOARD OF DIRECTORS,

Diane C. Honda

Vice President,

General Counsel and Secretary

Santa Clara, California

, 2009

IMPORTANT: To assure your representation at the meeting, please complete, sign, date and return the enclosed proxy card in the enclosed envelope or follow the instructions on the enclosed proxy card to vote by telephone or via the Internet. If you attend the meeting, you may choose to vote in person even if you have previously sent in your proxy card.

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EXTREME NETWORKS, INC.

PROXY STATEMENT

INFORMATION CONCERNING SOLICITATION AND VOTING

General

Our Board of Directors is requesting that you permit your common stock to be represented at the Annual Meeting of Stockholders of Extreme Networks, to be held on Wednesday, December 23, 2009 (the **2009 Annual Meeting**), or any postponement or adjournment thereof, by the proxies named on the enclosed proxy card for the purposes set forth in the accompanying Notice of Annual Meeting of Stockholders. This Proxy Statement contains important information for you to consider when deciding how to vote on the matters brought before the meeting. Please read it carefully. Voting materials, which include the Proxy Statement, the Annual Report on Form 10-K for the fiscal year ended June 28, 2009, as amended, and the accompanying proxy card, will be first mailed on or about _____, 2009 to all stockholders entitled to vote at the annual meeting, and, on or about the same date, electronic versions of these documents will be sent via email to stockholders who have registered for electronic delivery.

In this Proxy Statement, Extreme Networks may also be referred to as we, our, or us.

Who May Vote

You may vote your shares of Extreme Networks common stock if our records show that you owned your shares on _____, 2009. At the close of business on that date, _____ shares of Extreme Networks common stock were outstanding and eligible to vote. You are entitled to one vote for each share you hold.

Voting Your Proxy

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All valid proxies received before the meeting will be exercised. All shares represented by a proxy will be voted, and where a proxy specifies a stockholder's choice with respect to any matter to be acted upon, the shares will be voted in accordance with that specification. If no choice is indicated on the proxy, the shares will be voted in favor of the proposal.

To assure that your vote is recorded promptly, please vote as soon as possible, even if you plan to attend the annual meeting in person. Instructions for voting by telephone, by using the Internet or by mail are on your proxy card. When you vote via the Internet or by phone, your vote is recorded immediately. We encourage our stockholders to vote using these methods whenever possible. If you attend the annual meeting, you may also submit your vote in person, and any previous votes that you submitted, whether by Internet, phone or mail, will be superseded by the vote that you cast at the annual meeting. A stockholder who has given a proxy may revoke it at any time before it is exercised by (i) filing with the Investor Relations department of Extreme Networks or MacKenzie Partners a written revocation or a duly executed proxy bearing a later date, or (ii) by voting in person at the annual meeting.

For those stockholders who are voting by Internet and received notification by mail, follow these steps:

1. Log on to *www.proxyvote.com*. To access an electronic ballot, enter the twelve-digit number contained in the proxy card or voting instruction form accompanying the Proxy Statement.
2. Complete the electronic ballot and submit your voting instructions.
3. Provide your email address if you want confirmation of your voting instructions.

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Or, for those stockholders who are voting by Internet and received notification by email, follow these steps:

1. Log on to *www.proxyvote.com*. To access an electronic ballot, enter the twelve-digit number contained in your email message and the personal identification number (PIN) you used when you enrolled for electronic delivery.
2. The ballot displayed contains Internet links to the applicable materials; read them carefully.
3. Complete the electronic ballot and submit your voting instructions.

For those stockholders who are voting by telephone, follow these steps:

1. Dial 1-800-690-6903 using a touch-tone telephone.
2. You will be prompted to enter the twelve-digit number contained in the proxy card or voting instruction form accompanying the Proxy Statement.
3. Follow the instructions the vote voice provides you to submit your voting instructions.

Whether you hold shares in your name or through a broker, bank or other nominee, you may vote without attending the meeting. You may vote by granting a proxy or, for shares held through a broker, bank or other nominee, by submitting voting instructions to that nominee. For shares held through a broker, bank or other nominee, follow the voting instructions set forth above. If you provide specific voting instructions, your shares will be voted as you have instructed. If you hold shares in your name and sign and return a proxy card without giving specific voting instructions, your shares will be voted as recommended by our Board of Directors. All shares represented by valid proxies received before the meeting will be voted.

Votes Needed to Hold the Meeting

The annual meeting will be held if a majority of the Extreme Networks outstanding shares of common stock entitled to vote, whether present in person or represented by proxy, is represented at the meeting. This is called a quorum. Your shares will be counted for purposes of determining if there is a quorum if you either are present and vote in person at the meeting, or have properly submitted a proxy card or voted by telephone or by using the Internet, even if you wish to abstain from voting on some or all matters introduced at the meeting. Votes for and against, abstentions and broker non-votes will each be counted as present for purposes of determining the presence of a quorum. A broker non-vote occurs when a nominee holding shares for a beneficial owner does not vote on a particular proposal because the nominee does not have discretionary power with respect to that item and has not received instructions from the beneficial owner.

Matters to Be Voted On at the Meeting

The following proposals will be presented for your consideration at the annual meeting in order to:

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1. Elect three Class II directors to hold office for a three-year term and until their successors are elected and qualified or until their earlier resignation or removal,
2. Ratify the appointment of Ernst & Young LLP, independent registered public accounting firm, as our independent auditors for the fiscal year ending June 27, 2010,
3. Approve a voluntary program (the *Exchange Program*) that will permit eligible employees to exchange certain outstanding stock options that are underwater for a lesser number of shares of restricted stock units to be granted under the Extreme Networks 2005 Equity Incentive Plan (the *2005 Plan*), and with respect to stock options that are more substantially underwater, a cash payment, and
4. Approve an amendment to the 2005 Plan to increase the shares of common stock reserved for issuance under the 2005 Plan by 5,300,000 shares from 23,000,000 shares to 28,300,000 shares.

You will also be asked to transact such other business as may properly come before the meeting.

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Cost of This Proxy Solicitation

We will pay the costs of the solicitation. We may request banks and brokers and other custodians, nominees and fiduciaries to solicit their customers who own our common stock and will reimburse them for reasonable out-of-pocket expenses. Our employees, directors, officers and others may solicit proxies on our behalf, personally or by telephone, without additional compensation. We are soliciting proxies electronically through the Internet from stockholders who previously registered to receive proxy materials electronically through the Internet. In addition, we have engaged MacKenzie Partners, Inc. of New York City to assist in the soliciting of proxies for a fee of approximately \$12,500 plus reasonable out-of-pocket expenses.

Attending the Meeting

Stockholders may attend our annual meeting in person. The annual meeting will be held at 2 p.m. Pacific Time on Wednesday, December 23, 2009 at the Executive Briefing Center at our headquarters located at 3585 Monroe Street, Santa Clara, California 95051.

You may vote shares held directly in your name in person at the meeting. If you choose to attend the meeting, please bring the enclosed proxy card or proof of identification for entrance to the meeting. If you want to vote shares that you hold in street name at the meeting, you must request a legal proxy from your broker, bank or other nominee that holds your shares.

Changing Your Vote

You may revoke your proxy and change your vote at any time before the final vote at the meeting. You may do this by signing a new proxy card with a later date, voting on a later date by telephone or by using the Internet (only your latest telephone or Internet proxy is counted), or by attending the meeting and voting in person. However, your attendance at the meeting will not automatically revoke your proxy; you must specifically revoke your proxy. See *Voting Your Proxy* above for further instructions.

Our Voting Recommendations

Our Board of Directors recommends that you vote:

FOR the election of three Class II directors to hold office for a three-year term and until their successors are elected and qualified or until their earlier resignation or removal,

FOR ratification of the appointment of Ernst & Young LLP, independent registered public accounting firm, as our independent auditors for the fiscal year ending June 27, 2010,

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FOR approving a voluntary program (the *Exchange Program*) that will permit eligible employees to exchange certain outstanding stock options that are underwater for a lesser number of shares of restricted stock units to be granted under the Extreme Networks 2005 Equity Incentive Plan (the *2005 Plan*), and with respect to stock options that are more substantially underwater, a cash payment, and

FOR an amendment to the 2005 Plan to increase the shares of common stock reserved for issuance under the 2005 Plan by 5,300,000 shares from 23,000,000 shares to 28,300,000 shares.

Voting Results

The preliminary voting results will be announced at the meeting. The final voting results will be published in our quarterly report on Form 10-Q for the second quarter of fiscal year 2010.

Electronic Delivery of Stockholder Communications

This year we are pleased to again offer our stockholders the opportunity to receive stockholder communications electronically. By signing up for electronic delivery, you can receive the Annual Report on

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Form 10-K, as amended, and the Proxy Statement via email notification as soon as these are available. You may also submit your stockholder votes online. This will help to reduce the number of paper documents in your personal files, eliminate duplicate mailings, conserve natural resources, and save on our printing and mailing costs. To sign up for electronic delivery, visit <http://investor.extremenetworks.com/> and enter information for all of your Extreme Networks stockholdings. Your enrollment will be effective until canceled. You may access the Notice of Annual Meeting of Stockholders, the Proxy Statement and the Annual Report on Form 10-K, as amended, on the Internet at <http://investor.extremenetworks.com/>. If you have questions about electronic delivery, please call our Investor Relations department at (408) 579-3030.

To reduce the expense of delivering duplicate voting materials to our stockholders who may have more than one Extreme Networks stock account, unless otherwise requested, pursuant to current householding rules, we will deliver only one set of voting materials, which includes the Proxy Statement, proxy card and Annual Report to Stockholders on Form 10-K, to stockholders who share the same address.

How To Obtain A Separate Set of Voting Materials

If you share an address with another stockholder and have received only one set of voting materials, you may write or call us to request a separate copy of these materials at no cost to you. For future annual meetings, you may request separate voting materials, or request that we send only one set of voting materials to you if you are receiving multiple copies, by calling our proxy solicitor, MacKenzie Partners, Inc., toll free at (800) 322-2885 or our Investor Relations department at: (408) 579-3030. You may also write us at: Extreme Networks, Inc., 3585 Monroe Street, Santa Clara, CA 95051, Attn: Investor Relations.

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PROPOSAL ONE:

ELECTION OF DIRECTORS

We have a classified Board of Directors consisting of two Class I directors, three Class II directors and two Class III directors. The current term of the Class II directors will expire on the date of the upcoming 2009 annual meeting.

At the recommendation of the Board of Directors Nominating and Corporate Governance Committee, the Board of Directors nominees for election at the 2009 Annual Meeting as Class II directors are John H. Kispert, Edward B. Meyercord, III and Harry Silverglide. Messrs. Kispert, Meyercord and Silverglide are each current members our Board of Directors.

Please see below for information concerning each nominee. If elected, Messrs. Kispert, Meyercord and Silverglide will serve as directors until the annual meeting of stockholders in 2012 and until their successors are elected and qualified or until their earlier resignation or removal.

If any of Messrs. Kispert, Meyercord or Silverglide decline to serve or become unavailable for any reason, or if a vacancy otherwise occurs before the election, although management knows of no reason that this will occur, the proxies may be voted for a substitute nominee as the Nominating and Corporate Governance Committee or the Board of Directors may designate.

Vote Required and Board of Directors Recommendation

The persons receiving the highest number of votes represented by outstanding shares of common stock present or represented by proxy and entitled to vote at the annual meeting of stockholders will be elected. Votes for and against, abstentions and broker non-votes will be counted as present in determining if a quorum is present; however, abstentions and broker non-votes will have no effect on the outcome of the election.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE FOR THE NOMINEES NAMED ABOVE.

Class II Directors Serving a Term Expiring, and Nominated for Re-Election, at the 2009 Annual Meeting

John H. Kispert. Mr. Kispert has served as one of our directors since May 2009. In February 2009, Mr. Kispert was hired to serve as President and Chief Executive Officer of Spansion, Inc., a publicly-traded manufacturer of flash memory products, to oversee that company's reorganization of its business. Beginning in 1995 and continuing through February 2009, Mr. Kispert held various executive management positions at KLA-Tencor Corporation, including President and Chief Operation Officer, Executive Vice President and Chief Financial Officer and Vice President, Finance and Accounting. Previously, Mr. Kispert served in a number of positions with the IBM Corporation. Mr. Kispert received his bachelor's degree in Political Science from Grinnell College and his MBA from the University of California, Los Angeles.

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Edward B. Meyercord, III has served as one of our directors since October 2009. Mr. Meyercord is currently the President and Managing Partner of Council Rock Advisors LLC, a private company that provides advisory, capital raising and management consulting services. From December 2006 until January 2009, Mr. Meyercord served as Chief Executive Officer, President and a member of the board of directors of Cavalier Telephone & TV, a privately held voice and data services provider based in Richmond, Virginia. From January 2004, until its sale to Cavalier Telephone & TV in December 2006, Mr. Meyercord served as Chief Executive Officer, President and a member of the board of directors of Talk America, Inc., a publicly traded company that provided phone and internet services to consumers and small businesses. He served as President and a director of Talk America from 2001 until 2003 and as its Chief Financial Officer and Chief Operating Officer from 2000 until 2001. Mr. Meyercord joined Talk America in September of 1996 as the Executive Vice President,

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Marketing and Corporate Development. Prior to joining Talk America, Mr. Meyercord was a Vice President in the Global Telecommunications Corporate Finance Group at Salomon Brothers, Inc., based in New York. Prior to Salomon Brothers, Mr. Meyercord worked in the corporate finance department at PaineWebber Incorporated. Mr. Meyercord received his bachelor's degree in Economics from Trinity College in Hartford, CT and his MBA from New York University.

Harry Silverglide. Mr. Silverglide has served as one of our directors since June 2004. From January 1997 to July 2002, Mr. Silverglide served as our Vice President of Sales. From May 1995 to January 1997, he served as Vice President of Western Region Sales for Bay Networks. From July 1994 to May 1995, he served as Vice President of Sales for Centillion Networks, a provider of LAN switching products which was acquired by Bay Networks in 1995.

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PROPOSAL TWO:

RATIFICATION OF APPOINTMENT OF INDEPENDENT AUDITORS

FOR THE FISCAL YEAR ENDING JUNE 27, 2010

The Board of Directors has appointed Ernst & Young LLP, independent registered public accounting firm, to serve as independent auditors to audit our financial statements for the fiscal year ending June 27, 2010. Ernst & Young LLP has acted in this capacity since its appointment in fiscal year 1997. A representative of Ernst & Young LLP is expected to be present at the annual meeting, will have an opportunity to make a statement if desired and will be available to respond to appropriate questions.

Vote Required and Board of Directors Recommendation

Stockholder ratification of the selection of Ernst & Young LLP as our independent registered public accounting firm is not required by our bylaws or otherwise. The Board of Directors, however, is submitting the selection of Ernst & Young LLP to the stockholders for ratification as a matter of good corporate practice. If the stockholders fail to ratify the selection, the Audit Committee and the Board of Directors will reconsider whether or not to retain that firm. Even if the selection is ratified, the Audit Committee and the Board of Directors in their discretion may direct the appointment of different independent auditors at any time during the year if they determine that such a change would be in the best interests of us and our stockholders.

Approval of this proposal requires the affirmative vote of a majority of the shares present or represented by proxy and entitled to vote at the annual meeting of stockholders, at which a quorum representing a majority of all outstanding shares of our common stock is present and voting, either in person or by proxy. Abstentions and broker non-votes will each be counted as present for purposes of determining the presence of a quorum but will not have any effect on the outcome of the vote on this proposal.

THE BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS A VOTE FOR THE PROPOSAL TO RATIFY ERNST & YOUNG LLP AS EXTREME NETWORKS INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM FOR THE FISCAL YEAR ENDING JUNE 27, 2010.

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PROPOSAL NO. THREE

APPROVAL OF THE EXCHANGE PROGRAM

On July 28, 2009, our Board of Directors authorized, subject to stockholder approval, a voluntary program (the *Exchange Program*) that will permit eligible employees to exchange certain outstanding stock options (*Eligible Options*) that are underwater for a lesser number of shares of restricted stock units to be granted under our 2005 Plan and to exchange certain other stock options that are more substantially underwater for a cash payment. We believe that the Exchange Program is in the best interests of our stockholders because the program will help us to retain and motivate our most talented employees while reducing the total number of outstanding stock options held by our employees.

Summary of the Exchange Program

The following is a summary of the material terms of the Exchange Program, which are described in more detail below:

The Exchange Program would be open to all of our United States employees, except for the members of our Board of Directors and our executive officers (as defined by SEC rules) (*Eligible Employees*).

Eligible Options must have been issued at least 12 months prior to the date of the commencement of the Exchange Program.

Eligible Options must have a per share exercise price above the *Exchange Price Floor*. We expect to set the Exchange Price Floor at a reasonable premium above the per share trading price of our common stock on the NASDAQ Global Select Market directly prior to the commencement of the Exchange Program, provided that the Exchange Price Floor will not be less than the highest per share closing price of our common stock during the 52 weeks prior to the commencement of the Exchange Program. For illustrative purposes only, we have used \$3.06, the per share closing price of our common stock on September 22, 2009, to provide information regarding Eligible Options and the impact of the program. This was the highest per share closing price of our common stock during the 52 weeks prior to September 27, 2009, the last day of our first fiscal quarter.

The Exchange Program would not be a one-for-one exchange. Rather, Eligible Employees who participate in the program would exchange their existing options for a lesser number of restricted stock units. (Restricted stock units are rights to receive shares of common stock on specified future dates when those rights have vested following a required period of employment.) Our objective in determining the exchange ratios under the Exchange Program (which we expect to range from 3-to-1 to 5-to-1) is to provide for grants of replacement restricted stock units that will have a value approximately equal to the value of the stock options surrendered.

None of the restricted stock units would be vested on the date of grant. They will be subject to vesting schedules ranging from a minimum of two years to a maximum of three years.

Eligible Options with an exercise price equal to or greater than \$7.00 will be exchanged for a cash payment. The amount of the per share cash payment will be the same regardless of the exercise price of the option and will be calculated in a manner intended to create minimal additional compensation expense.

Shares subject to Eligible Options surrendered under the Exchange Program in excess of the number required for the restricted stock units to be granted under the program will not be returned to the Equity Plan or otherwise be made available for the future grant.

The intent of the Exchange Program is that it will not result in us incurring significant additional compensation expenses in connection with the Exchange Program.

If approved by our stockholders, the exchange program would replace our normally-scheduled employee annual focal grant program for Eligible Employees for our fiscal year ending June 27, 2010. We believe

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that the Exchange Program will allow us to more effectively retain Eligible Employees without incurring the additional equity dilution and stock-based compensation expense associated with making an annual focal grant to them this year.

Reasons for the Exchange Program

Our business has experienced the effects of the severe economic downturn in the United States and other parts of the world. We believe that the credit market crisis, global recession and other challenges affecting global economic conditions were the primary drivers of our financial performance during our fiscal year ended June 28, 2009 resulting in a 7.3% decrease in net revenue and a 66.4% decrease in net income from fiscal year 2008. In addition, our net revenue declined substantially in our first fiscal quarter ended September 27, 2009 from the first fiscal quarter ended September 28, 2008. Significant uncertainty around current economic conditions persists, particularly the effect these conditions will have on the purchasing decisions of our customers. In the context of these economic and market realities and their effect on our business and stock price, it is challenging to deliver meaningful incentives to retain, compensate and motivate our employees.

We have granted stock options periodically to a substantial portion of our employees. Each stock option award specifies the exercise price that the employee must pay to purchase shares of common stock when the option is exercised. The exercise price per share is set at the closing market price of a share of our common stock on the date the option is granted, generally the second trading day following the public announcement of quarterly financial results. Employees receive value from their options only by exercising their rights under the options to purchase shares of common stock and subsequently selling the purchased shares at a price that exceeds their exercise price. However, the options have no value to employees when the price of a share of our common stock is below the exercise price. In this situation, the options are commonly referred to as "underwater." At this time, a substantial percentage of the stock options held by our employees are underwater. On September 25, 2009 (the last business day of our first fiscal quarter), when the closing price of our common stock on the NASDAQ Global Select Market was \$2.88, options to purchase approximately 14.6 million shares held by our employees were underwater, representing approximately 85% of all outstanding options held by employees. The exercise prices of these underwater options ranged from \$2.95 to \$44.31 per share.

In addition to the issues with our equity compensation, we are also limited in our ability to increase cash compensation to motivate and retain employees. Any increase in cash compensation would reduce our cash flow from operations, which could adversely affect our business and operating results. Therefore, we have determined that, in general, base salaries for employees will not be increased as part of our regular focal review process for our current fiscal year. Further, to manage our business in the current economic environment, we have taken and plan to continue to take a variety of steps which will impact the morale of and benefits to our employees including suspending the employer matching contributions for our 401(k) plan, reducing training offerings, reducing our contingent work force, scheduling shutdown weeks, reducing travel and other discretionary spending, and restricting hiring activities.

In the context of these challenges to employee motivation and morale and these pronounced limitations on the benefits that we can provide to employees, we believe that to enhance long-term stockholder value we need to maintain competitive employee compensation and incentive programs that will assist us in motivating and retaining our employees. As of September 27, 2009 (the last day of our first fiscal quarter) and assuming an Exercise Price Floor of \$3.06, there were 403 Eligible Employees who held underwater Eligible Options to purchase approximately 8.4 million shares. These underwater options will not be sufficiently effective as performance and retention incentives. We believe the Exchange Program will offer a meaningful retention incentive for these Eligible Employees to remain with us.

The Exchange Program will also serve to reduce our current stock option overhang. Since many of the Eligible Options have been out of the money for an extended period of time, employees have had little or no incentive to exercise them. Coupled with periodic grants of options to new and continuing employees, the

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number of shares subject to outstanding options has steadily increased as a percentage of our total shares of common stock outstanding, creating a significant stock option overhang. Under the Exchange Program, participating employees will receive significantly fewer restricted stock units than the number of shares subject to the options they surrender. As a result, the number of shares of stock subject to outstanding employee equity awards will be reduced, thus reducing the current stock option overhang. Assuming that all Eligible Options are exchanged in the Exchange Program and a Exchange Price Floor of \$3.06, our stock option overhang as of September 27, 2009 (the last day of our first fiscal quarter) would decrease by 7.1 million shares.

Alternatives Considered

As part of our consideration of the Exchange Program, we considered the following alternatives:

Increasing cash compensation. To replace the underwater stock options, we considered whether we could increase base and target cash incentive compensation of our employees. However, increases in cash compensation would reduce our cash flow from operations, which could adversely affect our business and operating results. In addition, this alternative would not reduce our stock option overhang and would not necessarily best align the interests of our employees with those of our stockholders.

Grant additional equity awards. We also considered special grants of additional stock options at current market prices or restricted stock units. However, we do not have sufficient shares available for grant under our stock option plan to provide meaningful incentives to motivate and retain employees (see *Proposal Number Four; Amendment to the 2005 Equity Incentive Plan*, below) In addition, additional grants would increase our stock option overhang and further dilute the interests of our stockholders.

Exchange options for cash. We also considered implementing a program to exchange significantly underwater options solely for cash payments. However, such a program would increase our compensation expenses and reduce our cash flow from operations, which could adversely affect our business and operating results. In addition, we generally do not believe that such a program would have significant long-term retention value. However, for options with an exercise price equal to or greater than \$7.00, where we have determined that offering restricted stock units would provide minimal retentive value because the number of restricted stock units offered in exchange for tendered Eligible Options would not be a compelling benefit to employees, we will provide for a cash payment in exchange for surrendered options.

Exchange options for options with lower exercise prices. We also considered implementing a program to exchange significantly underwater options for options having an exercise price equal to the market price of our common stock on the date of the exchange. We believe, however, that implementing a restricted stock unit-for-option exchange program would result in the issuance of fewer shares subject to the replacement awards and, thus, a greater decrease in our stock option overhang.

Description of the Exchange Program

General. We have not commenced the Exchange Program and will not do so unless our stockholders approve this proposal. Our Board of Directors, upon recommendation by the Compensation Committee, authorized the Exchange Program on July 28, 2009. If this proposal is approved, and our Board of Directors or the Compensation Committee determines to implement the Exchange Program, the option exchange would commence within 12 months of the date of the Annual Meeting. Our Board of Directors may elect not to move forward with or to modify the terms of the Exchange Program if they determine that such actions would be in the best interests of the stockholders.

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Under the proposed Exchange Program, Eligible Employees will be offered the opportunity to participate in the Exchange Program pursuant to a written offer that will be distributed to all Eligible Employees. The Eligible Employees will be given at least 20 business days in which to accept the offer of the new restricted stock units in exchange for the surrender of their eligible options. The surrendered options will be cancelled on the first

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business day following this election period. The new restricted stock units will be granted under the 2005 Plan on the date of cancellation of the surrendered options. Where cash payments are made in exchange for surrendered options, such payments also will be made on, or shortly thereafter, the date of the cancellation of the surrendered options.

Prior to commencement of the Exchange Program, we will file the offer to exchange with the Securities and Exchange Commission (the *SEC*) as part of a tender offer statement on Schedule TO. Eligible Employees, as well as stockholders and members of the public, will be able to review the offer to exchange and other related documents filed by us with the SEC free of charge on the SEC's website at www.sec.gov.

Eligible Employees. If implemented, the Exchange Program will be open to all of our active United States employees who hold options with a per share exercise price greater than or equal to the Exchange Price Floor. International employees, members of our Board of Directors and executive officers will not be eligible to participate in the Exchange Program. Our other vice presidents who are not executive officers (as defined by SEC rules) will be eligible to participate in the Exchange Program. The Exchange Program will not be available to any former employees. If an option holder is no longer an active employee with us for any reason, including layoff, termination, voluntary resignation, death or disability, on the date that the Exchange Program is commenced, that option holder cannot participate in the Exchange Program. In addition, if an option holder is no longer an active employee with us for any reason on the date that the new Restricted Stock Unit grant is made following the completion of the offer, even if the option holder had elected to participate and had tendered his or her options for exchange, such option holder's tender will automatically be deemed withdrawn and he or she will not participate in the Exchange Program. An option holder will retain his or her outstanding options in accordance with their original terms and conditions and may exercise them during a limited period of time following termination of employment in accordance with their terms and to the extent that they are vested. A vote by an employee in favor of this proposal at the Annual Meeting does not constitute an election to participate in the Exchange Program.

Election to Participate. Participation in the Exchange Program will be entirely voluntary on part of the Eligible Employees. The Eligible Employees will have an election period of at least 20 business days from the commencement of the Exchange Program in which to determine whether they wish to participate.

Eligible Options. Only stock options with an exercise price above the Exchange Price Floor will be eligible for exchange. In addition, only stock options that were granted at least 12 months prior to the commencement of the Exchange Program will be eligible for exchange under the Exchange Program. As of September 25, 2009 (the last business day of our first fiscal quarter) when the closing price of our common stock was \$2.88, approximately 85% of all of our currently outstanding options were underwater and approximately 49% of our currently outstanding stock options would be eligible for exchange in the Exchange Program, assuming an Exchange Price Floor of \$3.06.

Exchange Ratio. Our objective in determining the Exchange Ratios applicable under Exchange Program is to provide for the grant of replacement restricted stock units that will have a value approximately equal to the value of the stock options surrendered. In order to determine appropriate Exchange Ratios, we estimated the fair value of the Eligible Options using the Black-Scholes option valuation model. The Black-Scholes model is a common method used for estimating the fair value of a stock option which we use for calculating stock expenses under FAS 123(R). For purposes of estimating the fair value of an Eligible Option under the Black-Scholes model, the following factors were used:

- (a) the option's exercise price;
- (b) an assumed value of \$2.88 per share of our common stock, the closing price of our common stock on September 25, 2009 (the last business day of our first fiscal quarter);

- (c) a weighted average expected volatility of our common stock price of 56.07%;

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- (d) the remaining expected life of the stock option;
- (e) a weighted average risk-free interest rate of 1.85%; and
- (f) no expected dividends.

These factors were used for the purpose of determining Exchange Ratios. The actual incremental compensation expense resulting from the Exchange Program will be calculated after the Exchange Program is completed.

We grouped Eligible Options within three exercise price ranges that also represent a range of associated Black-Scholes values. We then determined an exchange ratio for each grouping of Eligible Options based on the relationship of the Black-Scholes value estimate for the most valuable option within the group to an assumed fair market value of one share of our common stock to be made subject to a restricted stock right issued in the Exchange Program. The following table provides, for each of the three option exercise price ranges, the number of shares subject to Eligible Options an employee must surrender in order to receive one restricted stock unit in the Exchange Program:

Table of Example Exchange Ratios

Exercise Price					
Range of	Total Shares	Weighted Avg.	Weighted Avg.	Exchange Ratio:	Total Restricted
Eligible Options	Underlying	Remaining Life of	Exercise Price of	Stock Option Shares per	Stock Units
	Eligible Options	Eligible Options	Eligible	Restricted Stock Right	(assuming 100%
			Options		participation)
\$3.06 to \$3.49	248,367	6.90	\$ 3.31	3.0 to 1	82,789
\$3.50 to \$3.99	1,039,930	6.18	\$ 3.59	4.0 to 1	259,983
\$4.00 to \$7.00	4,886,420	6.57	\$ 4.48	5.0 to 1	977,284

The total number of restricted stock units a participating Eligible Employee will receive with respect to a surrendered Eligible Option will be determined by dividing the number of shares subject to the surrendered option by the applicable exchange ratio and rounding up to the nearest whole share.

Vesting of New Restricted Stock Units. New restricted stock units granted in the Exchange Program will not be vested on their date of grant regardless of whether the surrendered option was fully vested. Instead, with respect to the Eligible Options that are fully vested at the time of the exchange, the new restricted stock units will vest 50% on the first anniversary of the grant date and the remainder on the second anniversary. For any grants that are surrendered where the Eligible Options are unvested or partially unvested, the new restricted stock units granted in exchange will vest in equal installments over a three year period (33 1/3% on each anniversary date). The vesting schedules of the replacement restricted stock units are intended to support our goals of retaining our employees, incenting them to participate in the exchange, and reducing our stock option overhang.

New restricted stock units will only vest if the award holder remains an employee with us on the applicable vesting date. Any portion of the new restricted stock units that are not vested at termination of employment will be forfeited. As described above, the new restricted stock units will be completely unvested on the date of grant, regardless of whether the surrendered options were partially or completely vested.

Term and Conditions of New Restricted Stock Units. The terms and conditions of the new restricted stock units will be governed by the terms and conditions of the 2005 Plan and the restricted stock unit agreement entered into thereunder.

Cash Payments. In certain instances where we have determined that offering restricted stock units would provide minimal retentive value and/or would not provide a meaningful benefit to holders of Eligible Options, we will provide for a cash payment in exchange for surrendered options. This will be limited to the 2,224,153

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shares underlying Eligible Options where the exercise price of the Eligible Option is equal to or greater than \$7.00, as of September 27, 2009 (the last day of our first fiscal quarter). The amount of the per share cash payment will be the same regardless of the exercise price of the option. This amount will be determined, using the Black-Scholes valuation model, in a manner intended to create minimal additional compensation expense. Based on \$2.88, the closing price of our common stock on September 25, 2009 (the last business day of our first fiscal quarter) and Eligible Options with an exercise price of \$7.00 outstanding as of September 27, 2009 (the last day of our first fiscal quarter), the per share payment would be approximately \$0.10 per share, and the total payment to all Eligible Employees would be approximately \$222,000, assuming all Eligible Options are tendered. We will deduct any applicable taxes due prior to making the payments. To ensure that the payments satisfy securities laws requiring prompt payment following the completion of the Exchange Program, we have determined that such payments cannot be subject to vesting or other delayed payment schedules. Accordingly, any cash payments that we provide in exchange for surrendered options will not be subject to any vesting schedule and will be made on or shortly after the date that replacement restricted stock units are granted. Shares underlying Eligible Options tendered in exchange for a cash payment in the Exchange Program will not be returned to the Equity Plan or otherwise be made available for the future grant of equity awards.

Potential Modification to Terms to Comply with Government Requirements. The terms of the Exchange Program will be described in a tender offer document that will be filed with the SEC. Although we do not anticipate that the SEC would require us to modify the terms materially, it is possible that we will need to alter the terms of the Exchange Program to comply with potential SEC comments. The Compensation Committee will retain the discretion to make any such necessary or desirable changes to the terms of the Exchange Program for purposes of complying with comments from the SEC or optimizing the United States tax consequences.

Key Data:

Assuming an Exercise Price Floor of \$3.06 and based on options outstanding data as September 27, 2009 (the last day of our first fiscal quarter), the following table summarizes information regarding our outstanding equity awards and shares available for future awards before and after the proposed Exchange Program (assuming 100% participation). The actual number of eligible options, RSUs to be issued, exchange ratios and overhang changes will depend on our stock price and trailing 52-week high directly before the commencement of the Exchange Program.