AGERE SYSTEMS INC
Form 10-K
December 12, 2005

As filed with the Securities and Exchange Commission on December 12, 2005

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended September 30, 2005

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

For the transition period from _____ to _____.

Commission File Number 001-16397

Agere Systems Inc.

(Exact name of registrant as specified in its charter)

Delaware	**22-3746606**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1110 American Parkway N.E. Allentown, Pennsylvania	**18109**
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code: **610-712-1000**

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	**Name of Each Exchange on Which Registered**
Common Stock, $.01 par value	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes [X] No [ ]

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act). Yes [ ] No [X]

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No [ ]

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [ ]

Indicate by check mark whether the registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2).
Yes [X] No [ ]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes [ ] No [X]

The aggregate market value of voting common equity held by non-affiliates of the registrant as of March 31, 2005 was approximately $2.5 billion, based on the reported last sale prices on the New York Stock Exchange of such equity on such date.

As of December 1, 2005, 179,962,331 shares of common stock were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Certain information required by Part III of this report is incorporated by reference from the registrant s proxy statement to be filed pursuant to Regulation 14A with respect to the registrant s 2006 annual meeting of stockholders.

Agere Systems Inc.
Form 10-K
For the Year Ended September 30, 2005

FORWARD-LOOKING STATEMENTS

Certain statements in this Form 10-K are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, and Section 21E of the Securities Exchange Act of 1934. The words estimate, plan, intend, expect, anticipate, believe and similar expressions are intended to identify forward-looking statements. These forward-looking statements are found at various places throughout this report and in the documents incorporated herein by reference. Agere disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Although we believe that our expectations are based on reasonable assumptions, we can give no assurance that our goals will be achieved. Important factors that could cause our actual results to differ from estimates or projections contained in the forward-looking statements are described in Item 1A.

PART I

Item 1. Business.

General

We are a leading provider of integrated circuit solutions for a variety of applications, including high-density storage, mobile wireless communications and enterprise and telecommunications networks. These solutions form the building blocks for a broad range of computing and communications applications. Some of our solutions include related software and reference designs. Our customers include manufacturers of hard disk drives, mobile phones, high-speed communications systems and personal computers.

Integrated circuits, or chips, are made using semiconductor wafers imprinted with a network of electronic components. They are designed to perform various functions such as processing electronic signals, controlling electronic system functions and processing and storing data. Reference designs are complete specifications for products that a customer can use to build an end product, including components, board layouts and software. By using one of our reference designs, a customer can reduce the amount of product design it must perform and the amount of time required to introduce a new product into the market.

We have operating segments that focus on four target markets: Storage, Mobility, Enterprise and Networking and Telecommunications. We have two reportable segments for financial reporting purposes, Consumer Enterprise and Telecommunications. The Consumer Enterprise segment includes the Storage, Mobility and Enterprise and Networking operating segments. Information about each of these groups is provided below. We also have an operations group that manages our manufacturing and supply chain activities.

In fiscal 2005 and fiscal 2004, 17% of our revenue was generated in the United States and 83% was generated outside the United States. See We conduct a significant amount of our sales activity and manufacturing efforts outside the United States, which subjects us to additional business risks and may adversely affect our results of operations due to increased costs in Item 1A. See Item 8 for financial information about our

reportable segments and geographic financial information.

In the fourth quarter of fiscal 2005, we ceased operations at our Orlando, Florida, manufacturing facility and sold substantially all of the semiconductor manufacturing equipment at the facility.

We have research and development and manufacturing sites in the United States, Australia, Canada, China, Germany, India, Ireland, Israel, Japan, Korea, Singapore, Spain, Taiwan, Thailand and the United Kingdom. As of September 30, 2005, we had approximately 6,200 employees worldwide, including approximately 500 employees who were expected to go off-roll as a result of the closure of our Orlando, Florida manufacturing facility. We were incorporated in Delaware in 2000 as part of the plan of Lucent Technologies Inc. to spin off its microelectronics business to its stockholders. Lucent completed our spin-off in June 2002.

On May 27, 2005, we reclassified our Class A common stock and Class B common stock into a new, single class of common stock and effected a 1-for-10 reverse stock split.

We maintain an Internet website at http://www.agere.com. We make available free of charge on our website our annual report on Form 10-K, our quarterly reports on Form 10-Q, our current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) of the Securities Exchange Act of 1934

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as soon as practicable after we electronically file such material with, or furnish it to, the Securities and Exchange Commission. Information on our website is not incorporated by reference into this report.

In March 2005, our Chief Executive Officer submitted to the New York Stock Exchange an annual certification stating that he was not aware of any violations of the New York Stock Exchange s corporate governance listing standards.

Consumer Enterprise Segment

Storage

We sell integrated circuits for hard disk drives, which are used to store data in personal computers, corporate network servers and consumer electronics products such as digital video recorders, digital media players, mobile phones and game consoles.

Our TrueStore® family of storage electronics includes read channels, preamplifiers, motor controllers, disk controllers and firmware, as well as systems-on-a-chip. These are the critical chips required to read, write and protect data.

Read channels convert analog signals that are generated by reading the stored data on the hard disk into digital signals. Analog refers to a transmission technique employing a continuous signal that varies in amplitude, frequency or phase of the transmission. Digital refers to a method of transmitting, storing and processing data that uses distinct electronic or optical pulses to represent the binary digits 0 and 1. We also sell pre-amplifiers, or preamps, which are used to amplify the initial signal from the hard disk so the signal can be processed by the read channel. Together, these components are critical to determining the overall performance of a hard disk drive.

Our disk controllers are used to control signal processing and communications functions within the disk drive. We also sell motor controllers, which are used to control functions related to the spinning of the physical storage media.

A storage system-on-a-chip is an integrated circuit that combines the functionality of a read channel and a disk controller in a small, high-performance, low-power and cost-effective package. With these devices, manufacturers of hard disk drives get the performance and design flexibility needed to develop drives with outstanding storage capacity, speed, reliability and power savings.

Consumers are increasingly in need of more storage to manage their digital content whether it is MP3 files, home videos, digital photographs or downloaded video. As disk drives reach a capacity ceiling using current longitudinal recording techniques, design innovations are required in a disk drive s heads, media and electronics to deliver more storage. Perpendicular recording increases the amount of storage possible on a disk drive s platter. In fiscal 2005, we introduced our TrueStore CE family of integrated circuits targeting hard disk drives for portable consumer electronics. These integrated circuits support both horizontal and perpendicular recording, at a performance level that enables hard disk drives to store more data than competing solutions.

Mobility

We sell integrated circuits for use in mobile phones and other wireless data and voice communications products. We offer integrated wireless solutions that include:

Digital baseband processors for speech compression and encoding and transmission of voice and data;

Conversion signal processors to convert signals between frequencies used in digital signal processors and frequencies used for radio transmission; and

Software that controls the communication process.

Several different standards exist for mobile phones. The most prevalent standards are commonly referred to as second generation, or 2G , standards. Carriers are deploying advancements to their 2G networks that provide customers with higher data rates, thereby enabling services like Internet surfing and e-mail. Some carriers are also beginning to deploy networks based on third generation, or 3G , standards. These networks offer even higher data throughput, enabling revenue-generating applications, like streaming video, that require higher data rates than 2G networks can provide.

Our mobile phone products support a number of protocols, including General Packet Radio Service, or GPRS, which operates on the second generation Global System for Mobile Communications, or GSM, standard. GPRS provides enhanced data transmission capabilities for GSM mobile phones. We also provide integrated circuits for an extension of GPRS called EDGE. GPRS and EDGE are often referred to as 2.5G solutions because of the enhanced data rates they provide. We are sampling products that support the wideband Code Division Multiple Access, or W-CDMA, standard. W-CDMA is a third generation, or 3G , standard. In March 2005, we acquired Modem-Art Ltd., a privately-held developer of advanced processor technology for 3G mobile phone devices as part of our effort to develop 3G solutions. Because it is costly for a carrier to replace its network infrastructure to support 3G service, we expect that many carriers will choose to replace their infrastructure only in high usage areas, and to retain 2.5G infrastructure in lower use areas. To address this, we are developing a 3G solution which is designed to support both W-CDMA and EDGE and to enable consumers to experience 3G data rates in a 3G service area, while providing 2.5G data rates outside of 3G coverage.

In fiscal 2005, we introduced a new generation solution for mainstream EDGE feature phones and Smartphones. This is a dual-core, multi-processor solution that separates communications and applications processing to deliver improved handling of advanced multimedia tasks while ensuring that voice calling is continuously maintained. It delivers high-quality video and audio without requiring costly applications processors or multimedia companion chips. We have been sampling this solution and expect it will be available for volume production in late 2005.

Enterprise and Networking

The majority of our revenue from products used in enterprise and networking applications is derived from the sale of integrated circuits that are custom developed for our customers. These integrated circuits incorporate our intellectual property or combine our intellectual property with the intellectual property of our customers or other third parties to create a customized solution for these customers. For some customers, we design and manufacture the integrated circuit while the key intellectual property belongs solely to our customers.

Our systems-level knowledge and integrated circuit design methodologies allow us to turn our customers design concepts into a systems solution quickly and effectively. Our intellectual property gives our customers the flexibility to customize their products to meet their individual cost and performance objectives.

Networking Products

We sell custom-designed integrated circuits for use in storage area networks, Ethernet networks and wireless and wireline telecommunications applications. We are developing a family of standard products for high speed data networking applications. These products are intended to address enterprise and client applications for gigabit Ethernet, a high-speed data networking standard that operates at data rates of one billion bits, or one gigabit, per second. We are currently in production with five different products: our single and octal physical layer devices, our fully and lightly managed 48-port switches and our physical layer device controller.

Client Access Products

We sell integrated circuits and associated software for modem products, primarily to leading manufacturers of personal computers, modems and other electronic equipment. We also offer integrated circuits and software for use in packet telephony products that provide access to converged voice and data communications networks.

We sell high speed input/output products primarily to manufacturers of computers, peripheral equipment and communications equipment. Input/output refers to the transfer of data within and between computers; peripheral equipment, such as printers, scanners and digital cameras; and data networks. Our products support established connectivity and transmission standards known as Universal Serial Bus, or USB, and IEEE-1394.

We also sell integrated circuits for use in computer printing and imaging applications.

Other Products

We sell custom-designed integrated circuits for use in satellite digital radio receivers. Our integrated circuits process signals received from satellites and ground-based repeaters. In fiscal 2005, we introduced new media server chips that can be used in digital media servers and network-attached storage devices in homes and small businesses

to provide central data storage capabilities at a lower cost than a computer server. We also sell integrated circuits for use in other computing applications.

Telecommunications Segment

We offer solutions targeting wireless and wireline access and multiservice communications networks. Our products encompass integrated circuits, software and reference designs that facilitate the transmission and traffic management of voice, video and data signals within communications networks and are used primarily in the following types of equipment:

Wireline telecommunications equipment, including:

Network communications equipment, which facilitates the transmission and management of data and voice traffic within communications networks; and

Network access equipment, such as data communications equipment, which allows devices to connect with communications networks.

Wireless telecommunications equipment, such as a cellular base station, which transmits and receives data and voice communications through radio waves.

We sell integrated circuit solutions that include integrated circuits supporting SONET/SDH communication standards, broadband aggregation devices, network processing and traffic management devices and digital signal processing (DSP) devices, each of which is described below.

Wireline Telecommunications Equipment Solutions

We sell products designed for wired communications infrastructure. These products are used in high-speed transport networks and in the equipment used to access and interconnect these networks.

Multiservice Network Processing and Traffic Management Devices. Multiservice network processing and traffic management devices ensure that quality of service and service level agreement specifications are adhered to within wide area networks. Quality of service and service level agreements provide for reliable delivery of voice, video and data services to business and residential customers. These devices process data being sent over the network, providing for classification, traffic policing, queuing, scheduling and shaping of multiservice data.

Broadband Aggregation Devices. Broadband is a general term that refers to high-speed data transmission. Our broadband access integrated circuits, or mappers, support data transport between central offices and enterprise sites by aggregation and termination. Aggregation refers to the

combining of many low-speed, or tributary, data signals from enterprises into higher speed, or trunk, data signals for transmission to a central office. Termination refers to the separation of trunk data signals into lower-speed, tributary data signals.

Our products support data transport for T-carrier data transport in North America. T-carrier is a digital transmission service from a common carrier. We support similar services worldwide. These services are referred to as J-carrier in Japan and E-carrier in Europe. T-carrier services such as T1 and T3 lines are widely used to create point-to-point networks for use by enterprises. T1 and T3 lines refer to different levels of T-carrier service that transmit data at 1.544 megabits per second and 44.736 megabits per second, respectively. A megabit is a unit of measurement for data and is equal to approximately one million bits.

SONET/SDH Network Devices. Synchronous optical networks, which are typically referred to as SONET, and synchronous digital hierarchy standard networks, or SDH, carry data, voice and video traffic through a network by combining lines carrying traffic at slower speeds with lines carrying traffic at higher speeds. This process is known as multiplexing, and involves directing traffic from the individual lines into designated time slots in the higher speed lines, and those lines into still higher speed lines. The SONET/SDH equipment that handles the directing of traffic into slower speed and faster speed lines is the add-drop multiplexer. Add-drop multiplexers handle the addition and removal of traffic from a SONET/SDH communication transmission. We offer single-chip integrated circuit solutions, or framers, for add-drop multiplexing of data and voice traffic. In addition, our framers are used in high-speed routers within optical networks. A router is an interface, or link, between two networks.

Wireless Telecommunications Equipment

Wireless Infrastructure Devices. We sell integrated circuit solutions used in wireless infrastructure products, which are primarily cellular base stations and cellular base transceiver stations. Our solutions include digital signal processors for speech compression and encoding and transmission of voice and data and networking products that

connect cellular equipment to the wired communications network. Some of these products are standard offerings that are sold to multiple customers and some are customized for a particular customer. The customized offerings may combine our intellectual property with intellectual property from our customer. Many of the multiservice networking devices used in wireline communications infrastructure, including network processors and asynchronous transfer mode, or ATM, traffic management devices, are also used in wireless infrastructure.

In fiscal 2005, we introduced a new telecommunications product platform, TrueAdvantage , to serve as a building block for intelligent converged access networks and services. The TrueAdvantage family includes hardware and software development tools, application software and reference designs that are intended to help telecommunications equipment makers reduce product development costs, increase their products revenue-generating capabilities and accelerate time-to-market. We also announced new TrueAdvantage wireless access solutions that can simultaneously support current and future wireless systems over a single network.

Customers, Sales And Distribution

Customers

We have a globally diverse base of customers, consisting primarily of manufacturers of computer and communications equipment. In fiscal 2005, we sold our products directly to approximately 260 end customers and indirectly, through distributors, to approximately 339 end customers. For some end customers, we deliver the product to, and are paid by, a third party associated with the customer, such as their contract manufacturer. Our top 20 end customers in fiscal 2005, based on revenue, accounted for approximately 80% of our revenue and our top 10 end customers in fiscal 2005, based on revenue, accounted for approximately 67% of our revenue. These amounts include both product revenue and revenue from the licensing of intellectual property. Our top ten end customers in fiscal 2005 were:

Apple Computer, Inc.	NEC Corporation
Cisco Systems, Inc.	Nokia Corporation
Hitachi Global Storage Technologies	Samsung Electronics Co., Ltd.
Lucent Technologies Inc.	Seagate Technology, Inc.
Maxtor Corp.	Toshiba Corporation

In fiscal 2005, our sales to Maxtor represented 15% of our total revenue, our sales to Seagate represented 15% of our total revenue and our sales to Samsung represented 14% of our total revenue. No other customer accounted for 10% or more of our total revenue in fiscal 2005.

Sales and Distribution

We have a worldwide sales organization with approximately 300 employees as of September 30, 2005, located in seven U.S. sales offices and 16 sales offices outside the U.S. We sell our products globally primarily through our direct sales force. To complement our direct sales force, we also sell our products through distributors, which sales in fiscal 2005 represented approximately six percent of our revenue.

We aim to have our customers incorporate our products into the end products they design and develop. Typically, manufacturers of computer and communications equipment conduct a competitive process to select suppliers for the parts that they will include in their end products. Our sales, marketing and technical personnel work with customers to demonstrate our products ability to satisfy any specific requirements. We call winning the competitive process a design win. A design win is important because it allows us to establish a long-term relationship with the customer, at least through the life cycle of the product. We generally do not, however, enter into written agreements with our customers after achieving a design win. A customer could terminate its relationship with us or discontinue developing the product. Most of our revenue originates from sales that are the result of design wins.

After we achieve a design win and negotiate the terms of the sale, we deliver our products to our end customers in a number of ways. Our end customers typically have us ship our products to their facilities directly. In some instances, however, our customer may use a contract manufacturer to manufacture and assemble its end product. When our product is being incorporated into an end product being manufactured by a contract manufacturer, we often ship our product directly to the contract manufacturer and receive payment from that contract manufacturer. To determine our sales to particular customers, however, we recognize this type of transaction as a sale to, and revenue from, the end customer. Sometimes a customer for whom we have achieved a design win will have us sell

that product to a distributor or trading company from whom the customer then buys our product. We recognize these transactions as indirect sales.

Manufacturing

We had three facilities located in two countries devoted to manufacturing integrated circuits as of September 30, 2005. These sites utilized approximately 687,000 square feet of space dedicated to manufacturing. As of September 30, 2005, we had joint venture wafer fabrication operations in Singapore, while our assembly and test operations were in Singapore and Thailand. Prior to September 30, 2005, we also conducted wafer fabrication operations in Orlando, Florida. As of September 30, 2005, we had approximately 3,100 employees in manufacturing and other functions involved in delivering products to customers. Included in this amount are approximately 500 people who were expected to go off-roll as a result of the closure of the Orlando facility.

Because of the high cost of implementing new manufacturing processes, we have decided to use foundry partners, rather than internal manufacturing capabilities, to produce integrated circuits using newer processes. Our primary foundry partners are Chartered Semiconductor Manufacturing, Ltd. and Taiwan Semiconductor Manufacturing Corporation. We believe that our internal assembly and test operations provide us with a competitive advantage and intend to continue operating those facilities.

We have a joint venture, called Silicon Manufacturing Partners, with Chartered Semiconductor Manufacturing Ltd., that operates a 54,000 square foot integrated circuit manufacturing facility in Singapore. We are entitled to 51% of the managed wafer capacity of the facility. The joint venture agreement may be terminated by either party upon two years written notice, but may not be terminated prior to February 2008. The agreement may also be terminated for material breach, bankruptcy or insolvency of either party.

Competition

We sell products designed for communications, consumer electronics and computer equipment manufacturers. Our customers products are sold in market segments that are intensely competitive and characterized by:

- Rapid technological change;

Evolving standards;

Short product life cycles; and

Price erosion.

There are many competitors for our products. We expect the intensity of competition in the market segments we serve to continue to increase in the future as existing competitors enhance and expand their product offerings and as our customers attempt to limit the number of suppliers from which they buy. Increased competition may result in price reductions, reduced revenues and loss of market share. We cannot assure you that we will be able to compete successfully against existing or future competitors. Some of our customers and companies with which we have strategic relationships also are, or may be in the future, competitors of ours.

Our primary competitors are listed in the table below.

Storage	Mobility	Enterprise and Networking	Telecommunications
Infineon Technologies AG	Broadcom Corp.	Broadcom Corp.	Applied Micro Circuits Corp.
Marvell Technology Group Ltd.	Koninklijke Philips Electronics N.V.	Conexant Systems	Infineon Technologies AG
STMicroelectronics N.V.	Freescale Semiconductor, Inc.	International Business Machines	Intel Corp.
Texas Instruments Incorporated	QUALCOMM Inc.	LSI Logic Corp.	Freescale Semiconductor, Inc.
	Skyworks Solutions, Inc.	Marvell Technology Group Ltd.	PMC-Sierra, Inc.
	STMicroelectronics N.V.	Texas Instruments Incorporated	STMicroelectronics N.V.
	Telefonaktiebolaget LM Ericsson		Vitesse Semiconductor Corporation
	Texas Instruments Incorporated		Wintegra, Inc.

Our competitive position varies depending on the market and product areas within these markets. For example, we are number one or two, based on revenue, in many of our product areas, including read channels and systems-on-a-chip for hard disks used in consumer electronics products, integrated circuits for notebook computer modems, digital signal processors for wireless infrastructure, SONET/SDH integrated circuits and wired communications integrated circuits. However, our competitive position is not as strong in the gigabit Ethernet product area, which is a new area for us. While improving our position in many of the product areas where our position is less well-established is an objective of ours, we cannot assure you that we will be able to accomplish this goal. Further, because we expect to face increasing competitive pressures from both current and future competitors in the product areas we serve, we may not be able to maintain our position in the product areas in which we are currently a leader.

We believe competition in our industry is based on the following factors:

Performance and reliability;

Price;

Compatibility of products with other products and communications standards used in communications networks;

Product size;

Ability to offer integrated solutions;

Time to market;

Breadth of product line;

Customer support;

Logistics and planning systems; and

Quality of manufacturing processes.

While we believe we are competitive on the basis of all the factors listed above, we believe some of our competitors compete more favorably on the basis of price and on delivering products to market more quickly. However, we feel we are particularly strong in offering integrated solutions, our broad product lines, our customer support and our logistics and planning systems.

Research and development

As of September 30, 2005, our product development team consisted of approximately 2,000 employees. Our research and development expenditures were $462 million, $496 million and $467 million for fiscal 2005, 2004 and 2003, respectively. We anticipate that we will continue to make significant research and development expenditures to maintain our competitive position with a continuing flow of innovative products and technology.

Patents, Trademarks And Other Intellectual Property

We own or have rights to a number of patents, trademarks, copyrights, trade secrets and other intellectual property directly related to and important to our business. We have approximately 5,875 U.S. patents and patent applications and their corresponding foreign patents and patent applications. These patents include patents related to the following technologies:

Integrated circuit and optoelectronic manufacturing processes;

Modems, digital signal processors, wireless communications, network processors and communication protocols; and

Optoelectronic products including lasers, optical modulators, optical receivers and optical amplifiers.

The patents described above include patents of all ages ranging from pending applications, which will have a duration of 20 years from their filing dates, through patents soon to expire.

We indemnify our customers for some of the costs and damages of patent infringement in circumstances where our product is the primary factor creating the customer s infringement exposure. We generally exclude coverage where infringement arises out of the combination of our products with products of others.

We protect our products and processes by asserting our intellectual property rights where appropriate and prudent. We also obtain licenses to patents, copyrights and other intellectual property rights used in connection with our business when practicable and appropriate.

Government Regulation

Many of our customers end products that include our products are subject to extensive telecommunications-based regulation by the United States and foreign laws and international treaties. We must design and manufacture our products to ensure that our customers are able to satisfy a variety of regulatory requirements and protocols established to, among other things, avoid interference among users of radio frequencies and to permit interconnection of equipment.

Each country has different regulations and a different regulatory process. In order for our customers products to be used in some jurisdictions, regulatory approval and, in some cases, specific country compliance testing may be required. The delays inherent in this regulatory approval process may force our customers to reschedule, postpone or cancel the incorporation of our products into their products, which may result in significant reductions in our sales. The failure to comply with current or future regulations or changes in the interpretation of existing regulations in a particular country could result in the suspension or cessation of sales in that country by us or our customers. It also may require us to incur substantial costs to modify our products to aid our customers in complying with the regulations of that country. Changes in our regulatory environment that generally result from our expansion into new areas or changes in current regulations could increase the cost of manufacturing our products because we must continually modify our products to respond to these changes.

In addition, domestic and international authorities continue to regulate the allocation and auction of the radio frequency spectrum. These regulations have a direct impact on us because many of our customers licensed products can be marketed only if permitted by suitable frequency allocations, auctions and regulations. The implementation of these regulations may delay our end-users in deploying their systems, which could, in turn, lead to delays in orders of our products by our customers and end users.

Employees

As of September 30, 2005, we had approximately 6,200 full-time employees, including approximately 500 employees who were expected to go off-roll as a result of the closure of our Orlando manufacturing facility in September 2005. As of September 30, 2005, we had approximately 450 U.S. union-represented employees covered by collective bargaining agreements. Three hundred and seventy of these employees had been assigned to our Orlando manufacturing facility and were expected to go off-roll as a result of the closure of that facility.

On May 27, 2003, we entered into a collective bargaining agreement with local unions 1522, 1560, 1898 and 2000 of the International Brotherhood of Electrical Workers. This agreement, which covers our U.S. union-represented employees, will be effective until May 31, 2006, unless the parties reach a mutual agreement to amend the terms.

We believe that we generally have good relationships with our employees and the unions that represent them.

Backlog

Our backlog, which represents the aggregate of the sales price of orders received from customers for delivery within six months, but not yet recognized as revenue, was approximately $311 million and $447 million on September 30, 2005 and September 30, 2004, respectively. The majority of these orders are fulfilled within three months. All orders, however, are subject to possible rescheduling by customers. Our customers often change their orders two or three times between initial order and delivery. Our customers frequent changes usually relate to quantities or delivery dates, but sometimes relate to the specifications of the products we are shipping. Although we believe that the orders included in the backlog are firm, generally orders may be cancelled by the customer without penalty. We also may elect to permit cancellation of orders without penalty where we believe it is in our interest to do so. For these reasons, we believe that our backlog at any given date may not be a reliable indicator of future revenues.

Environmental, Health And Safety Matters

We are subject to a wide range of laws and regulations relating to protection of the environment and employee health and safety. Our manufacturing facilities have undergone regular internal audits relating to environmental, health and safety requirements. Most of those facilities also are regularly audited and certified by an independent and accredited third party registrar, such as Lloyd s Register Quality Assurance, as conforming to the internationally recognized ISO 14001 standard relating to environmental management. In addition, our non-U.S. manufacturing facilities conform to BS 8800, the British standard for occupational health and safety management systems. Based upon these reviews, we believe that our manufacturing facilities are in substantial compliance with all applicable environmental, health and safety requirements.

Item 1A. Risk Factors

Set forth below are some of the risks and uncertainties that, if they were to occur, could materially adversely affect our business or that could cause our actual results to differ materially from the results contemplated by the forward-looking statements contained in this report and other public statements we make.

Because our sales are concentrated on a limited number of key customers, our revenue may materially decline if one or more of our key customers do not continue to purchase our existing and new products in significant quantities.

Our customer base is highly concentrated. Our top 10 end customers accounted for approximately 67% of our revenue in fiscal 2005. If any one of our key customers were to decide to purchase significantly less from us or to terminate its relationship with us, our revenue may materially decline. Because we have a long product design and development cycle for most of our products, we may be unable to replace these customers quickly or at all. We could lose our key customers or significant sales to our key customers because of factors beyond our control, such as a significant disruption in our customers businesses generally or in a specific product line.

If we fail to keep pace with technological advances in our industry or if we pursue technologies that do not become commercially accepted, customers may not buy our products and our results of operations may be adversely affected.

The demand for our products can change quickly and in ways we may not anticipate because our industry is generally characterized by:

rapid, and sometimes disruptive, technological developments;

evolving industry standards;

changes in customer requirements;

limited ability to accurately forecast future customer orders;

frequent new product introductions and enhancements; and

short product life cycles with declining prices over the life cycle of the product.

If we fail to make sufficient investments in research and development programs in order to develop new and enhanced products and solutions, or if we focus on technologies that do not become widely adopted, new technologies could render our current and planned products obsolete, resulting in the need to change the focus of our research and development and product strategies and disrupting our business significantly.

The integrated circuit industry is intensely competitive, and our failure to compete effectively could result in reduced revenue.

The market for integrated circuits is intensely competitive and subject to rapid and disruptive technological change. We expect the intensity of competition to continue to increase as existing competitors enhance and expand their product offerings and as new participants enter the market. Increased competition may result in price reductions, reduced gross margins and loss of market share. We may not be able to compete successfully against existing or future competitors, which may result in reduced revenue.

The size and number of our competitors vary across our product areas, as do the resources we have allocated to the segments we target. Therefore, many of our competitors have greater financial, personnel, production capacity and other resources than we have in a particular market segment or overall. Competitors with greater financial resources may be able to offer lower prices, additional products or services or other incentives that we cannot match or offer. These competitors may be in a stronger position to respond quickly to new technologies and may be able to undertake more extensive marketing campaigns. They also may adopt more aggressive pricing policies and make more attractive offers to potential customers, employees and strategic partners. These competitors may also make strategic acquisitions or establish cooperative relationships among themselves or with third parties to increase their ability to gain market share.

Further, some of our competitors are currently selling commercial quantities of products that we are sampling to our customers, that are still in the initial stages of development or that we may develop in the future. By being able to offer these products in commercial quantities before we do, our competitors can establish significant market share, acquire design wins in customer equipment programs and create a market position that we may be unable to overcome once we have completed development and testing of our product.

Our revenue and operating results may fluctuate because we derive most of our revenue from semiconductor devices and the integrated circuits industry is highly cyclical, and because of other characteristics of our business, and these fluctuations may cause our stock price to fall.

We expect to derive most of our revenue from the sale of integrated circuits. Because the integrated circuits industry is highly cyclical, we may experience declines in our revenue that are primarily related to industry conditions and not our products. This industry has experienced significant downturns, often in connection with, or in anticipation of, excess manufacturing capacity worldwide, maturing product cycles and declines in general economic conditions.

We focus primarily on winning competitive selection processes to develop products for use in our customers equipment. These selection processes can be lengthy. After winning a product design for a customer, that customer may not begin volume production of their equipment for a period of up to two years, if at all. Due to this lengthy design and development cycle, we may experience delays from the time we begin incurring expenses until the time we generate revenue from our products. We have no assurances that our customers will ultimately market and sell their equipment or that such efforts by our customers will be successful. Thus, we may never generate any revenue from our products after incurring significant design and development expenditures.

If we are not selected by a customer to provide a product, we may experience significantly lower revenue later, as compared to prior periods with more revenue from earlier design wins. In addition, sales of our products for specific customer projects often begin and end abruptly, so revenue may increase rapidly and later decrease just as quickly. The relative timing of the beginning and end of our sales and design processes can make our revenues less predictable.

Fluctuations in our revenue or operating results could cause our stock price to decline, even if our results meet expectations. Further, stock prices in our industry have recently been highly volatile for reasons that sometimes are unrelated to the performance of the companies in the industry. These broad fluctuations could adversely affect our stock price.

If we do not achieve adequate manufacturing utilization, yields or volumes or sufficient product reliability, our gross margins will be reduced.

Because the manufacturing costs at our owned and joint venture manufacturing facilities are relatively fixed, efficient utilization of manufacturing facilities and manufacturing yields are critical to our results of operations. If we do not experience adequate utilization of our manufacturing facilities, our results of operations may be adversely affected. In addition, from time to time, we may have to pay to reserve capacity at third-party manufacturers. If this is the case and we overestimate demand for our products, we may have to pay for capacity that we do not use, and our results of operations may be adversely affected.

The manufacture of our products involves highly complex and precise processes, requiring production in highly controlled and clean environments. Changes in our manufacturing processes or those of our suppliers or contractors, or the inadvertent use of defective or contaminated materials, could significantly reduce our manufacturing yields and product reliability. Lower than expected manufacturing yields could adversely affect our results of operations and delay product shipments.

Because we are subject to order and shipment uncertainties, any significant cancellations or deferrals could cause our revenue to decline or fluctuate.

We generally sell products pursuant to purchase orders that customers may cancel or defer on short notice without incurring a significant penalty. Cancellations or deferrals could cause us to hold excess inventory, which could adversely affect our results of operations. If a customer cancels or defers product shipments, we may incur unanticipated reductions or delays in our revenue. If a customer refuses to accept shipped products or does not pay for these products in a timely manner, we could incur significant charges against our income, which could materially and adversely affect our results of operations.

A joint venture and third parties manufacture all of our wafers for us. If these suppliers are unable to fill our orders on a timely and reliable basis, our revenue may be adversely affected.

The integrated circuit manufacturing industry has a history of developing new manufacturing processes. We believe that the costs associated with implementing new processes, including acquiring the necessary equipment and building appropriate facilities, are increasing with each generation of manufacturing processes. We have not wanted to make the significant financial investments necessary for new processes and in the last few years we have relied on contract manufacturers to fabricate products using processes that we did not have internally or at our joint

venture manufacturer. We recently discontinued operations at our last wholly-owned wafer fabrication facility and now rely on our joint venture and third-party manufacturers to fabricate all of our wafers. To the extent we rely on joint ventures and third-party manufacturing relationships, we face the following risks:

- that they may not be able to develop manufacturing methods appropriate for our products;
- that manufacturing costs will be higher than planned;
- that reliability of our products will decline;
- that they may be unwilling to devote adequate capacity to produce our products;
- that they may not be able to maintain continuing relationships with our suppliers; and
- that we may have reduced control over delivery schedules and costs of our products.

If any of these risks were to be realized, we could experience an interruption in supply or an increase in costs, which could adversely affect our results of operations.

In the event of an increase in demand, failure to increase our manufacturing volumes or obtain capabilities from third parties may result in our not being able to meet customer demand for our products, which could hurt our relationships with our customers and result in our recording lower revenues than would be the case if we had greater manufacturing capacity.

Because many of our current and planned products are highly complex, they may contain defects or errors that are detected only after deployment in commercial applications, and if this occurs, it could harm our reputation and result in reduced revenues or increased expenses.

Our products are highly complex and may contain undetected defects, errors or failures. These products can only be fully tested when deployed in commercial applications and other equipment. Consequently, our customers may discover errors after the products have been deployed. The occurrence of any defects, errors or failures could result in:

- cancellation of orders;
- product returns, repairs or replacements;
- diversion of our resources;
- legal actions by our customers or our customers end-users;
- increased insurance costs; and
- other losses to us or to our customers or end-users.

Any of these occurrences could also result in the loss of or delay in market acceptance of our products and loss of sales, which would harm our business and adversely affect our results of operations. We have from time

to time experienced defects in our products and expect to experience defects in the future. Because the trend in our industry is moving toward

even more complex products in the future, this risk will intensify over time and may result in increased expenses.

We are expanding, and may seek in the future to expand, into new areas, and if we are not successful, our results of operations may be adversely affected.

We are currently developing products in new areas, including wireless communications infrastructure, high-speed networking and consumer electronics. We may seek to expand into additional areas in the future. We may expand through internal development efforts, through acquisitions of companies or technologies, or a combination of these methods.

Our efforts may not result in sales that are sufficient for us to recoup our investment, and we may experience higher costs than we anticipated. For example, we may not be able to manufacture our products at a competitive cost, may need to rely on new suppliers or may find that the development efforts are more costly or time consuming than we had anticipated. Our products may support protocols that are not widely adopted. Where we choose to develop capabilities by acquiring another company, we may not be able to integrate the other company successfully into our operations, which may mean that we have difficulty retaining employees from the acquired company or integrating its technology into our products. We may have difficulties entering markets where competitors have strong market positions.

We have recently upgraded our enterprise financial management system, and it is possible that we may have a defect in the design of the system that may result in the generation of incorrect financial information, an adverse impact on the processing of customer orders or some other adverse impact on our business.

We recently upgraded the enterprise-wide computer system that we use to control activities such as the processing of customer orders and accounts, the generation of financial data used in the preparation of financial statements and the handling of employee expense and payroll information. The system is extremely complex because of the wide range of processes that it integrates. Because of the complex nature of the system, it is possible that we will have a flaw in our design of the upgrade that has an adverse impact on our business. While we tested the system before implementing the upgrade, we cannot assure you that our testing would uncover every defect in the design or implementation of the upgrade that might be made. If such a defect did exist in the system after the upgrade, it could have a significant impact on how we conduct our business and we may not be able to mitigate that impact through other actions.

A widespread outbreak of an illness or other health issue could negative