CIRRUS LOGIC INC
Form 10-Q/A
April 18, 2007

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

FORM 10-Q/A

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

For the quarterly period ended June 24, 2006

o **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 0-17795

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

DELAWARE	**77-0024818**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
2901 Via Fortuna Austin, Texas	**78746**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code:
(512) 851-4000

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 o NO þ

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o Accelerated filer þ Non-accelerated filer o

Indicate by check mark whether the registrant is a shell Company (as defined in Rule 12b-2 of the Exchange Act). YES o NO þ

The number of shares of the registrant s common stock, $0.001 par value, outstanding as of March 31, 2007 was 88,163,467.

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EXPLANATORY NOTE

Cirrus Logic, Inc. (Cirrus, We, Us, Our, or the Company) is filing this Amendment No.1 (Form 10-Q/A quarterly report on Form 10-Q for the three months ended June 24, 2006 (the Original Filing) as filed with the Securities and Exchange Commission (the Commission) on July 31, 2006 to restate our:

Consolidated balance sheets for the three months ended June 24, 2006 and March 25, 2006;

Consolidated statements of operations and cash flows for the three months ended June 24, 2006 and June 25, 2005; and

Related disclosures.

These items are being restated to reflect the recognition of $32.3 million in additional share-based compensation expense resulting from the investigation of past stock grants to non-employee directors, executive officers and employees as described below in this Explanatory Note. Within stockholder s equity, additional paid in capital increased by $32.3 million and accumulated deficit increased by $32.3 million. The restatement had no net effect on the consolidated statement of cash flows. A detailed discussion of the financial effects of these matters is also included in Item 2 Management s Discussion and Analysis of Financial Condition and Results of Operations Restatement of Consolidated Financial Statements and Note 1A, Restatement of Consolidated Financial Statements, of the Notes to Consolidated Financial Statements.

We are making the restatement in accordance with generally accepted accounting principles to record the following:

Non-cash share-based compensation expense for grants recorded with incorrect measurement dates;

certain share-based compensation expenses related to the extension of the post-service exercise or vesting period for stock options of terminated employees; and

Related tax effects for these items.

Concurrent with this filing, we have also separately amended our annual report on Form 10-K for the fiscal year ended March 25, 2006. This Form 10-Q/A should be read in conjunction with that Form 10-K/A as well as the periodic filings made with the Commission subsequent to the date of the Original Filing, including any amendments to those filings, as well as any Current Reports filed on Form 8-K subsequent to the date of the Original Filing. Other previously filed annual reports on Form 10-K and quarterly reports on Form 10-Q affected by the restatements have not been amended and should not be relied upon. Further, all reports of our registered public accounting firm, all earnings press releases, and all similar communications for the restated periods should not be relied upon. All information in this Form 10-Q/A is as of June 24, 2006 and does not reflect events occurring after the date of the Original Filing, other than the restatement and updating of certain disclosures affected by events related to the results of the investigation of the company s historical stock option grants. For the convenience of the reader, this Form 10-Q/A sets forth the Original Filing in its entirety, as amended and modified to reflect the restatement. The following items have been amended principally as a result of, and to reflect, the restatement, and no other information in the Original Filing is amended hereby as a result of the restatement:

Part I Item 1: Financial Statements and Supplementary Data;

Part I Item 2: Management s Discussion and Analysis of Financial Condition and Results of Operations;

Part I Item 4: Controls and Procedures;

Part II Item 1A: Risk Factors;

In accordance with applicable Commission rules, this Form 10-Q/A also includes updated certifications from our Acting President and Chief Executive Officer (CEO) and Chief Financial Officer (CFO) as Exhibits 31.1, 31.2, 32.1 and 32.2.

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Review of Consolidated Financial Statements Based on Review of Stock Option Practices

Background Investigation

Our decision to restate our Consolidated Financial Statements was based on the results of a voluntary internal review and independent investigation into past stock option granting practices. In October 2006, we announced that an internal review of past practices related to grants of stock options had revealed information that raised potential questions about the dates used to account for certain stock option grants. We also announced that, at the recommendation of the Audit Committee of the Company s Board of Directors (the Board), the Board appointed an independent director to serve as a Special Committee to conduct an investigation into our historic stock option granting practices.

The Special Committee retained independent legal counsel to assist in the investigation. During the eight-month investigation, the Special Committee and its independent counsel, assisted by independent forensic accountants, reviewed the facts and circumstances surrounding annual stock option grants made to executive officers, employees and non-employee directors, searched relevant physical and electronic documents and interviewed current directors, officers and employees. This review included an examination of all stock option grants from January 1, 1997 to December 31, 2006, encompassing approximately 42.3 million stock options granted to employees and non-employee directors on 148 different grant dates. The Special Committee s legal and accounting advisors identified, preserved, collected, and reviewed over 104 gigabytes of electronic information, including approximately 1.6 million pages of electronic and hard copy files, and conducted 25 interviews of current and former employees and members of the Board.

In March 2007, we announced that the Special Committee had reported its principal findings to the Board relating to the above investigation. Based on the report of the Special Committee and on management s preliminary conclusions and recommendations, the Board concluded that incorrect measurement dates were used for financial accounting purposes for certain stock options granted between January 1, 1997 and December 31, 2005. We disclosed the fact that the anticipated non-cash charges required to correct the discrepancy would be material and that we expected to restate our financial statements for the fiscal years 2001 through 2006 and for the first quarter of fiscal year 2007. Accordingly, we announced that based on the findings of the Special Committee, and the recommendations of management and the Audit Committee, the Board had concluded that the financial statements, related notes and selected financial data and all financial press releases and similar communications issued by us and the related reports of the Company s independent registered public accounting firm relating to fiscal periods 2001 through 2006, and the first fiscal quarter of 2007, should no longer be relied upon.

As a result of the findings of the Special Committee detailed below, the Company has recognized $32.3 million in additional share-based compensation expense arising from stock grants to executive officers and employees. Of this amount, approximately $9.3 million related to options granted to executive officers who, at the time of the grant, were subject to the reporting requirements under Section 16 of the Exchange Act of 1934. The Special Committee arrived at the following principal findings with respect to the stock option practices of the Company:

The Company s stock plan administrative deficiencies between January 1, 1997 and December 31, 2005 led to a number of misdated option grants.

- o New hire and other promotion and retention option grants were generally made the first Wednesday of each month through the use of unanimous written consents (UWCs) of the Company s Compensation Committee. However, prior to 2006, many of these monthly grants were misdated, as grant dates were routinely established before the receipt of all the signed UWCs authorizing those grants. Of the $32.3 million in additional share-based compensation expense, $6.1 million related to these types of errors.

- o Many other off-cycle and broad-based annual option grants that were granted through Board or Compensation Committee resolutions were also misdated due to administrative issues in that grant dates were sometimes established before the list of option award recipients had been finalized. Of the $32.3 million in additional share-based compensation expense, $4.2 million related to these types of errors.

- Beginning in late 2002, the Company formally documented and updated its existing processes and procedures with respect to the granting of options. In 2005, the Company further refined the process and, in 2006, a formal written policy was approved by the Compensation Committee.

- Approximately 97% of the potential stock-based compensation charges identified as a result of the Special Committee investigation resulted from grants that were made prior to December 31, 2002.

Prior to 2003, the limited controls and the lack of definitive processes for stock option granting and approval allowed for potential abuse, including the use of hindsight, in the establishment of more favorable grant dates for certain options.

- The Special Committee identified three grant dates prior to 2003 on which three management-level employees received new-hire option grants on dates other than when they began rendering services to the Company. Of the $32.3 million in additional share-based compensation expense, $1.4 million related to these types of errors.
- The grant date for one grant in 2000 is different from the date the grant appears to have been approved by the Board. While no definitive evidence has been identified to clarify this inconsistency, the selected grant date was at a lower closing stock price than the price on the date of apparent board approval.

- Based on the evidence developed in the investigation, the Special Committee believes that certain executive officers had knowledge of and participated in the selection of three grant dates for broad-based employee option grants in the 2000 through 2002 timeframe, either with hindsight or prior to completing the formal approval process. Of the $32.3 million in additional share-based compensation expense, $12.0 million related to these types of errors.

- The executive officers involved in the option grant process prior to 2003, and in particular the grants described above in the 2000 through 2002 timeframe, were no longer with the Company as of the date of the findings with the exception of David D. French, the Company s President and Chief Executive Officer.

- In light of the findings, as of March 5, 2007, David D. French resigned as President and Chief Executive Officer and as a director of the Company. The Company has entered into a resignation agreement with Mr. French.

The Special Committee believes that Mr. French was significantly involved in the grant approval process for certain grants and that he influenced the grant process with a view toward the stock price, and therefore the selection of grant dates, through his control over how quickly or slowly the process was completed. However, the Special Committee does not believe that Mr. French appreciated the significance of the procedural inadequacies or the accounting implications of the grant approval process or grant date selections, or that he was advised by his executive staff of any such inadequacies or implications.

The Special Committee did not find any irregularities associated with any grants to independent directors or the Company s two broad-based options exchanges during the relevant period.

The Special Committee found no documentary or testimonial evidence that the Company s independent directors were aware of any attempts by the Company s executive officers to backdate or to otherwise select a favorable grant date, and consequently, had no reason to and did not believe that the accounting or other disclosures were inaccurate.

The Special Committee further found that the evidence indicates that the independent directors relied upon management to ensure that all grant approvals complied with the Company s stock option plans and applicable laws and accounting rules.

Based on the results of its investigation, the Special Committee has recommended a number of remedial actions. The Company is currently reviewing these recommendations and developing and implementing a remediation plan associated with historical stock option grants and the grant of future equity awards. Based on its review of the Special Committee s findings, the Company does not believe that, in the few instances when stock grant dates were selected by management either with hindsight or

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prior to receiving all required approvals, that any employee, who at the time of the grant was an executive officer, has exercised or made any profit from those grants.

Subsequent to our press release dated March 2, 2007, the Company identified two other issues based upon the findings of the Special Committee that led to an increase of $8.6 million in additional share-based compensation expense recognized in the consolidated financial statements in excess of the previous estimate of $22 million to $24 million. These issues are described as follows:

Our previous estimate should have included the intrinsic value of 1.8 million options canceled in relation to a Company wide option exchange in fiscal year 2003, which led to an increase in share-based compensation expense. Under EITF 00-23, *Issues Related to the Accounting for Stock Compensation under APB Opinion No. 25 and FASB Interpretation No. 44,* Issue 37(a), the compensation cost measured on the original grant date of the re-priced stock option grants that remained unrecognized at the time of the option exchange should have been immediately recognized as expense on the day of the exchange and included in our original estimate. Of the $8.6 million in additional share-based compensation expense beyond our previous estimate, $6.5 million related to the correction of this error.

Our previous estimate should have included certain share-based compensation expenses related to certain modifications to the terms of stock options grants for certain individual employees at the time of their termination. Of the $8.6 million in additional share-based compensation expense beyond our previous estimate, $2.1 million related to correction of these types of errors.

As of the date of this filing, the Company has paid a total of approximately $2.9 million to independent legal counsel, independent forensic accountants, and our independent registered public accounting firm in connection with the 8 month investigation into past stock option granting practices.

Share-Based Compensation Summary

For all periods beginning prior to March 25, 2006, the expenses below are calculated in accordance with Accounting Principles Board Opinion No. 25 (APB 25) Accounting for Stock Issued to Employees and, for those periods, our restated consolidated financial statements reflect additional compensation expense to the extent the fair market value of a share of our common stock on the correct measurement date exceeded the exercise price of the option. As of March 26, 2006, we adopted the provisions of Statement of Financial Accounting Standards No. 123(R) (SFAS 123(R)) Accounting for Stock Based Compensation. For all periods beginning on or after that date, our restated consolidated financial statements reflect additional compensation expense to the extent the fair value of the stock option grant on the correct measurement date exceeded the fair value of the stock option grant on the previous measurement date used for financial accounting purposes.

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The additional non-cash compensation expense was amortized over the required service period, generally over the vesting periods of the respective grants. The incremental effect of recognizing additional share-based compensation expense resulting from grants with incorrect measurement dates for the three months ended June 24, 2006 and June 25, 2005 is as follows (in thousands):

	Three Months Ended June 24, 2006			Three Months Ended June 25, 2005		
	Previously Filed	Adjustments	Restated	Previously Filed	Adjustments	Restated
Cost of sales	$ 15	$ (2)	$ 13	$	$ 1	$ 1
Research and development	528	(56)	472	15	27	42
Sales, general, and administrative	809	(86)	723		41	41
Effect on Income from continuing operations (before taxes)	1,352	(144)	1,208	15	69	84
Income Tax						
Total share based compensation expense (net of taxes)	$ 1,352	$ (144)	$ 1,208	$ 15	$ 69	$ 84
Share based compensation effects on basic earnings per share	$ 0.01	$	$ 0.01	$	$	$
Share based compensation effects on diluted earnings per share	$ 0.01	$	$ 0.01	$	$	$
Share based compensation effects on operating activities cash flow	$ 1,352	$ (144)	$ 1,208	$ 15	$ 69	$ 84

A summary of the cumulative effect on the components of stockholders equity resulting from the restatement of share-based compensation as of March 25, 2006 and for the period ending June 24, 2006 is as follows (in thousands):

Cumulative Effect, Summary Schedule	Paid-in Capital	Retained Earnings	Unearned Deferred Compensation	Net Impact to Stockholders Equity
Fiscal Year 2006 & Prior	32,612	(32,423)	(333)	(144)
First Quarter of Fiscal Year 2007	(84)	144	74	134
Total effect all prior periods	$ 32,528	$ (32,279)	$ (259)	$ (10)

The net impact to Stockholder s Equity seen in the table above was, for each period presented, completely offset by a change in accrued liabilities. These were the only adjustments made to our consolidated balance sheet for the periods presented as a result of the restatement. The restatement had no net effect on our consolidated balance sheet. The net book value of our deferred tax assets did not change as a result of the restatement as we continue to provide a full valuation allowance against them. The net book value of our inventory did not change due to the fact that the amount of the additional share-based compensation expense capitalized as inventory was negligible.

The incremental effect of recognizing additional share-based compensation expense resulting from grants with incorrect measurement dates is as follows (in thousands):

	Pre-Tax Expense	After-Tax Expense
Fiscal Year 2005 & Prior	30,704	30,704
Quarter Ended June 25, 2005	69	69
Quarter Ended September 30, 2005	1,010	1,010
Quarter Ended December 31, 2005	149	149
Quarter Ended March 25, 2006	491	491
Quarter Ended June 24, 2006	(144)	(144)
Total 2006 2007 effect	1,575	1,575
Total effect	$ 32,279	$ 32,279

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Litigation Summary

On January 5, 2007, a purported stockholder filed a derivative lawsuit in state district court in Travis County, Texas against current and former officers and directors of Cirrus Logic and against the Company, as a nominal defendant, alleging various breaches of fiduciary duties, conspiracy, improper financial reporting, insider trading, violations of the Texas Securities Act, unjust enrichment, accounting, gross mismanagement, abuse of control, rescission, and waste of corporate assets related to certain prior grants of stock options by the Company. Our response to the lawsuit is currently due on April 20, 2007.

On March 19, 2007, another purported stockholder filed a derivative lawsuit related to the Company s prior stock option grants in the United States District Court for the Western District of Texas Austin Division against current and former officers and directors of Cirrus Logic and against the Company, as a nominal defendant. The individual defendants named in this lawsuit overlap, but not completely, with the state suit. The lawsuit alleges many of the causes of action alleged in the Texas state court suit, but also includes claims for alleged violations of Section 10(b) of the Exchange Act and Rule 10b-5, violations of Section 14(a) of the Exchange Act and violations of Section 20(a) of the Exchange Act. On April 10, 2007, we filed a motion to dismiss the complaint on the grounds that the plaintiff was supposed to make demands on the Board before filing the lawsuit. The plaintiff has not filed a response and no hearing before the court is currently set on the motion to dismiss.

On March 30, 2007, a different purported stockholder filed a nearly identical derivative lawsuit to the March 19, 2007 derivative lawsuit in the United States District Court for the Western District of Texas Austin Division with identical allegations against the same defendants. We are currently evaluating this plaintiff s claims.

CIRRUS LOGIC, INC.
FORM 10-Q/A QUARTERLY REPORT
QUARTERLY PERIOD ENDED JUNE 24, 2006
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PART I FINANCIAL INFORMATION

PART II OTHER INFORMATION

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Part I.

ITEM 1. FINANCIAL STATEMENTS

CIRRUS LOGIC, INC.
CONSOLIDATED CONDENSED BALANCE SHEET
(in thousands)

	June 24, 2006 Restated (unaudited)	March 25, 2006 Restated
Assets		
Current assets:		
Cash and cash equivalents	$ 103,053	$ 116,675
Restricted investments	5,755	5,755
Marketable securities	137,123	102,335
Accounts receivable, net	21,518	20,937
Inventories	21,391	18,708
Other current assets	5,634	7,747
Total current assets	294,474	272,157
Long-term marketable securities	5,972	18,703
Property and equipment, net	13,263	14,051
Intangibles, net	2,593	2,966
Non-marketable securities	7,947	7,947
Other assets	3,293	3,217
Total assets	$ 327,542	$ 319,041
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 11,943	$ 14,129
Accrued salaries and benefits	6,813	6,460
Other accrued liabilities	9,704	10,053
Deferred income on shipments to distributors	6,199	7,098
Income taxes payable	1,990	2,228
Total current liabilities	36,649	39,968
Other long-term obligations	14,005	14,803
Stockholders equity:		
Capital stock	919,339	914,235
Accumulated deficit	(641,250)	(649,075)
Accumulated other comprehensive loss	(1,201)	(890)
Total stockholders equity	276,888	264,270

Total liabilities and stockholders equity	$ 327,542	$ 319,041

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

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CIRRUS LOGIC, INC.
CONSOLIDATED CONDENSED STATEMENT OF OPERATIONS
(in thousands, except per share amounts; unaudited)

	Three Months Ended	
	June 24, 2006	**June 25, 2005**
	Restated	Restated
Net sales	$ 45,181	$ 52,822
Cost of sales	18,021	25,523
Gross Margin	27,160	27,299
Operating expenses:		
Research and development	11,670	13,678
Selling, general and administrative	11,091	14,342
Litigation settlement, net		(24,758)
Total operating expenses	22,761	3,262
Income (loss) from operations	4,399	24,037
Realized gain on marketable securities	193	388
Interest income, net	2,965	1,136
Other income (expense), net	55	(19)
Income (loss) before income taxes	7,612	25,542
Benefit for income taxes	(213)	(366)
Net income (loss)	$ 7,825	$ 25,908
Basic income (loss) per share:	$ 0.09	$ 0.30
Diluted income (loss) per share:	$ 0.09	$ 0.30
Basic weighted average common shares outstanding:	87,196	85,230
Diluted weighted average common shares outstanding:	88,759	86,183

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

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CIRRUS LOGIC, INC.
CONSOLIDATED CONDENSED STATEMENT OF CASH FLOWS
(in thousands; unaudited)

	Three Months Ended	
	June 24, 2006	**June 25, 2005**
	Restated	Restated
Cash flows from operating activities:		
Net income	$ 7,825	$ 25,908
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,732	2,769
Stock compensation expense	1,342	480
Gain on marketable securities	(193)	(388)
Other non-cash benefits	(511)	(172)
Net change in operating assets and liabilities	(4,701)	5,691
Net cash provided by operating activities	5,494	34,288
Cash flows from investing activities:		
Additions to property, equipment and software	(453)	(243)
Investments in technology	(182)	(425)
Purchase of marketable securities	(52,052)	(65,554)
Proceeds from sale and maturity of marketable securities	29,883	41,978
Increase in restricted investments		(89)
Increase in deposits and other assets	(74)	(313)
Net cash used in investing activities	(22,878)	(24,646)
Cash flows from financing activities:		
Issuance of common stock, net of issuance costs	3,762	1,061
Net cash provided by financing activities	3,762	1,061
Net increase (decrease) in cash and cash equivalents	(13,622)	10,703
Cash and cash equivalents at beginning of period	116,675	79,235
Cash and cash equivalents at end of period	$ 103,053	$ 89,938

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

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CIRRUS LOGIC, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. Basis of Presentation

The consolidated financial statements have been prepared by Cirrus Logic, Inc. (we, us, our, or the Company) pursuant to the rules and regulations of the Securities and Exchange Commission (Commission). The accompanying unaudited consolidated financial statements do not include complete footnotes and financial presentations. As a result, these financial statements should be read along with the audited Consolidated Financial Statements and notes thereto for the year ended March 25, 2006, included in our 2006 amended Annual Report on Form 10-K/A filed with the Commission on April 18, 2007. In our opinion, the financial statements reflect all adjustments, including normal recurring adjustments, necessary for a fair presentation of the financial position, operating results and cash flows, for those periods presented. The preparation of financial statements in conformity with United States generally accepted accounting principles requires management to make estimates and assumptions that affect reported assets, liabilities, revenues and expenses, as well as disclosure of contingent assets and liabilities. Actual results could differ from those estimates and assumptions. Moreover, the results of operations for the interim periods presented are not necessarily indicative of the results that may be expected for the entire year. We maintain a web site at *www.cirrus.com,* which makes available free of charge our recent annual report and all other filings we have made with the Commission.

Recently Issued Accounting Pronouncements

In July 2006, the *Financial Accounting Standards Board (FASB)* issued *FASB Interpretation No. 48 (FIN No. 48) Accounting for Uncertainty in Income Taxes,* which prescribes a recognition threshold and measurement process for recording in the financial statements uncertain tax positions taken or expected to be taken in a tax return. Additionally, FIN No. 48 provides guidance on the derecognition, classification, accounting in interim periods and disclosure requirements for uncertain tax positions. The accounting provisions of FIN No. 48 will be effective for the Company beginning April 1, 2007. The Company is in the process of determining the effect, if any, that the adoption of FIN No. 48 will have on its financial statements.

1A. Restatement of Consolidated Financial Statements

The Consolidated Financial Statements and the related disclosures for the fiscal quarters ended June 25, 2005 and June 24, 2006 have been restated as described below. In addition, the consolidated balance sheet and the related disclosures for the fiscal year ended March 25, 2006 have been restated as described below.

We are restating our Consolidated Financial Statements to reflect the results of our voluntary review of our stock option granting practices. Our decision to restate our Consolidated Financial Statements was based on the results of a voluntary internal review and independent investigation into past stock option granting practices. In October 2006, we announced that an internal review of past practices related to grants of stock options had revealed information that raised potential questions about the dates used to account for certain stock option grants. We also announced that, at the recommendation of the Audit Committee of the Company s Board of Directors (the Board), the Board appointed an independent director to serve as a Special Committee to conduct an investigation into our historic stock option granting practices.

The Special Committee retained independent legal counsel to assist in the investigation. During the eight-month investigation, the Special Committee and its independent counsel, assisted by independent forensic accountants, reviewed the facts and circumstances surrounding annual stock option grants made to executive officers, employees and non-employee directors, searched relevant physical and electronic documents and interviewed current directors, officers and employees. This review included an examination of all stock option grants from January 1, 1997 to December 31, 2006, encompassing approximately 42.3 million stock options granted to employees and non-employee directors on 148 different grant dates. The Special Committee s legal and accounting advisors identified, preserved, collected, and reviewed over 104 gigabytes of electronic information, including approximately 1.6 million pages of electronic and hard copy files, and conducted 25 interviews of current and former employees and members of the Board.

In March 2007, we announced that the Special Committee had reported its principal findings to the Board relating to the above investigation. Based on the report of the Special Committee and on management s preliminary conclusions and recommendations, the Board concluded that incorrect measurement dates were used for financial accounting purposes for certain stock options granted between January 1, 1997 and December 31, 2005. We disclosed the fact that the anticipated non-cash charges required to correct the discrepancy would be material and that we expected to restate our financial statements for the fiscal years 2001 through 2006 and for the first quarter of fiscal year 2007. Accordingly, we announced that based on the findings of the Special Committee, and the recommendations of management and the Audit Committee, the Board had concluded that the financial statements, related notes and selected financial data and all financial press releases and similar communications issued by us and the related reports of the Company s independent registered public accounting firm relating to fiscal periods 2001 through 2006, and the first fiscal quarter of 2007, should no longer be relied upon.

As a result of the findings of the Special Committee detailed below, the Company has recognized $32.3 million in additional share-based compensation expense arising from stock grants to executive officers and employees. Of this amount, approximately $9.3 million related to options granted to executive officers who, at the time of the grant, were subject to the reporting requirements under Section 16 of the Exchange Act of 1934. The Special Committee arrived at the following principal findings with respect to the stock option practices of the Company:

The Company s stock plan administrative deficiencies between January 1, 1997 and December 31, 2005 led to a number of misdated option grants.

- New hire and other promotion and retention option grants were generally made the first Wednesday of each month through the use of unanimous written consents (UWCs) of the Company s Compensation Committee. However, prior to 2006, many of these monthly grants were misdated, as grant dates were routinely established before the receipt of all the signed UWCs authorizing those grants. Of the $32.3 million in additional share-based compensation expense, $6.1 million related to these types of errors.

- Many other off-cycle and broad-based annual option grants that were granted through Board or Compensation Committee resolutions were also misdated due to administrative issues in that grant dates were sometimes established before the list of option award recipients had been finalized. Of the $32.3 million in additional share-based compensation expense, $4.2 million related to these types of errors.

- Beginning in late 2002, the Company formally documented and updated its existing processes and procedures with respect to the granting of options. In 2005, the Company further refined the process and, in 2006, a formal written policy was approved by the Compensation Committee.

- Approximately 97% of the potential stock-based compensation charges identified as a result of the Special Committee investigation resulted from grants that were made prior to December 31, 2002.

Prior to 2003, the limited controls and the lack of definitive processes for stock option granting and approval allowed for potential abuse, including the use of hindsight, in the establishment of more favorable grant dates for certain options.

- The Special Committee identified three grant dates prior to 2003 on which three management-level employees received new-hire option grants on dates other than when they began rendering services to the Company. Of the $32.3 million in additional share-based compensation expense, $1.4 million related to these types of errors.

- The grant date for one grant in 2000 is different from the date the grant appears to have been approved by the Board. While no definitive evidence has been identified to clarify

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this inconsistency, the selected grant date was at a lower closing stock price than the price on the date of apparent board approval.

o Based on the evidence developed in the investigation, the Special Committee believes that certain executive officers had knowledge of and participated in the selection of three grant dates for broad-based employee option grants in the 2000 through 2002 timeframe, either with hindsight or prior to completing the formal approval process. Of the $32.3 million in additional share-based compensation expense, $12.0 million related to these types of errors.