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

Form 10-Q

(Mark One)

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

For the quarter ended March 27, 2005

OR

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

For the transition period from ______ to ______

Commission file number 000-25711

EXTREME NETWORKS, INC.
(Exact name of Registrant as specified in its charter)

DELAWARE **[State or other jurisdiction of incorporation or organization]**	**77-0430270** **[I.R.S. Employer Identification No.]**
3585 Monroe Street **Santa Clara, California** **[Address of principal executive offices]**	**95051** **[Zip Code]**

Registrant's telephone number, including area code: (408) 579-2800

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

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes ☒ No ☐

The number of shares of the Registrant's Common Stock, $.001 par value, outstanding at May 3, 2005 was 121,858,503.

EXTREME NETWORKS, INC.
FORM 10-Q
QUARTERLY PERIOD ENDED MARCH 27, 2005

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Part I. Financial Information

Item 1. Financial Statements

EXTREME NETWORKS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands)

	March 27, 2005	June 27, 2004
	(Unaudited)	(Note 1)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 65,542	$ 59,164
Short-term investments	140,725	162,078
Accounts receivable, net	31,575	32,998
Inventories	22,104	25,889
Prepaid expenses and other current assets	17,383	8,051
Total current assets	277,329	288,180
Property and equipment, net	51,760	59,767
Marketable securities	237,057	204,430
Other assets	22,640	26,896
TOTAL ASSETS	$ 588,786	$ 579,273
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 22,040	$ 18,995
Accrued compensation and benefits	17,017	15,827
Restructuring liabilities	6,139	6,085
Lease liability	942	2,355
Accrued warranty	7,873	8,297
Deferred revenue	48,840	53,674
Other accrued liabilities	24,678	22,921
Total current liabilities	127,529	128,154
Restructuring liabilities, less current portion	15,459	20,478
Deferred income taxes	777	762
Long-term deposit	59	321
Convertible subordinated notes	200,000	200,000
Commitments and contingencies (Note 2 and 7)		
Stockholders' equity:		
Common stock and capital in excess of par value	691,479	687,216
Deferred stock-based compensation	—	(69)
Accumulated other comprehensive loss	(4,135)	(2,388)
Accumulated deficit	(442,382)	(455,201)
Total stockholders' equity	244,962	229,558
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 588,786	$ 579,273

See accompanying notes to the unaudited condensed consolidated financial statements.

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EXTREME NETWORKS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share amounts)
(Unaudited)

	Three Months Ended		Nine Months Ended	
	March 27, 2005	March 28, 2004	March 27, 2005	March 28, 2004
Net revenues:				
Product	$ 76,835	$ 76,059	$ 243,770	$ 224,315
Service	15,073	12,815	43,525	35,375
Total net revenues	91,908	88,874	287,295	259,690
Cost of revenues:				
Product	35,692	34,422	109,951	101,959
Service	8,954	8,979	25,568	26,913
Total cost of revenues	44,646	43,401	135,519	128,872
Gross margin:				
Product	41,143	41,637	133,819	122,356
Service	6,119	3,836	17,957	8,462
Total gross margin	47,262	45,473	151,776	130,818
Operating expenses:				
Sales and marketing	23,946	23,343	70,941	68,779
Research and development	15,329	15,001	45,586	42,867
General and administrative	7,254	8,043	21,918	22,934
Amortization of deferred stock compensation	2	198	69	931
Restructuring charge	—	—	—	962
Technology agreement	2,000	—	2,000	—
Total operating expenses	48,531	46,585	140,514	136,473
Operating income (loss)	(1,269)	(1,112)	11,262	(5,655)
Other income, net	829	345	4,582	2,707
Income (loss) before income taxes	(440)	(767)	15,844	(2,948)
Provision for income taxes	817	339	3,025	1,149
Net income (loss)	$ (1,257)	$ (1,106)	$ 12,819	$ (4,097)
Net income (loss) per share – basic	$ (0.01)	$ (0.01)	$ 0.11	$ (0.03)
Net income (loss) per share –diluted	$ (0.01)	$ (0.01)	$ 0.10	$ (0.03)
Shares used in per share calculation - basic	121,444	118,832	121,041	117,706
Shares used in per share calculation - diluted	121,444	118,832	124,211	117,706

See accompanying notes to the unaudited condensed consolidated financial statements.

EXTREME NETWORKS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Nine Months Ended	
	March 27, 2005	March 28, 2004
Cash flows from operating activities:		
Net income (loss)	$ 12,819	$ (4,097)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation	12,605	15,550
Provision for doubtful accounts (reversal)	—	(200)
Provision for excess and obsolete inventory	795	—
Deferred income taxes	15	—
Amortization of deferred stock-based compensation	69	931
Amortization of warrant-related costs	5,675	3,153
Restructuring charge	—	962
Loss on disposal of property and equipment	50	—
Net changes in operating assets and liabilities:		
Accounts receivable	1,422	(3,754)
Inventories	2,990	(5,516)
Prepaid expenses and other current and noncurrent assets	(10,751)	5,388
Accounts payable	3,045	3,540
Accrued compensation and benefits	1,190	(307)
Restructuring liabilities	(4,965)	(6,425)
Lease liability	(1,413)	(1,570)
Accrued warranty	(424)	(1,264)
Deferred revenue	(4,834)	6,395
Other accrued liabilities	1,809	(2,722)
Net cash provided by operating activities	20,097	10,064
Cash flows from investing activities:		
Capital expenditures	(4,647)	(5,641)
Purchases of investments	(247,516)	(215,027)
Sales and maturities of investments	234,180	219,514
Net cash used in investing activities	(17,983)	(1,154)
Cash flows from financing activities:		
Proceeds from issuance of common stock	4,264	11,145
Net cash provided by financing activities	4,264	11,145
Net increase in cash and cash equivalents	6,378	20,055
Cash and cash equivalents at beginning of period	59,164	44,340
Cash and cash equivalents at end of period	$ 65,542	$ 64,395

See accompanying notes to the unaudited condensed consolidated financial statements.

EXTREME NETWORKS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. Summary of Significant Accounting Policies

Basis of Presentation

The unaudited condensed consolidated financial statements of Extreme Networks, Inc (referred to as “Extreme Networks” and as “we”, “us” and “our”) included herein have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”). Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. The condensed consolidated balance sheet at June 27, 2004 was derived from audited financial statements as of that date but does not include all disclosures required by U.S. generally accepted accounting principles for complete financial statements. These interim financial statements and notes should be read in conjunction with our audited consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the fiscal year ended June 27, 2004.

The unaudited condensed consolidated financial statements reflect all adjustments, consisting only of normal recurring adjustments, that, in the opinion of management, are necessary for a fair presentation of our results of operations and cash flows for the interim periods presented and our financial condition at March 27, 2005. The results of operations for the third quarter of fiscal 2005 are not necessarily indicative of the results that may be expected for fiscal 2005 or any future periods.

Revenue Recognition

We derive the majority of our revenue from sales of our modular and stackable networking equipment, with the remaining revenue generated from service fees relating to the service contracts and training on our products. We generally recognize product revenue from our Value-Added Resellers and end-users at the time of shipment, provided that persuasive evidence of an arrangement exists, delivery has occurred, the price of the product is fixed or determinable and collection of the sales proceeds is reasonably assured. Revenue from service obligations under service contracts is deferred and recognized on a straight-line basis. Service contracts typically range from one to five years. When sales arrangements contain multiple deliverables, such as hardware, service contracts and other services, we determine whether the deliverables represent separate units of accounting and then allocate revenue to each unit of accounting based on their relative fair values. We recognize revenue for each unit of accounting when the revenue recognition criteria for each unit of accounting are met.

We make certain sales to partners in two-tier distribution channels. The first tier consists of a limited number of independent distributors that sell primarily to resellers and, on occasion, to end-user customers. We defer recognition of revenue on all sales to these distributors until the distributors sell the product, as evidenced by monthly “sales-out” reports that the distributors provide to us. We grant these distributors the right to return a portion of unsold inventory to us for the purpose of stock rotation, provide them with credits for changes in selling prices, and allow them to participate in cooperative marketing programs. Cooperative marketing expenses paid to distributors are recorded as a reduction of revenue. The second tier of the distribution channel consists of a large number of third-party resellers that sell directly to end-users and are not granted return privileges, except for defective products during the warranty period. We reduce product revenue for certain price protection rights that may occur under contractual arrangements we have with our customers.

Inventories

Inventories consist of (in thousands):

	March 27, 2005	June 27, 2004
Raw materials	$ 288	$ 695
Finished goods	21,816	25,194
Total	$22,104	$25,889

Sales to Distributors

We defer recognition of revenue on all sales to distributors until the distributor successfully resells the product, typically to an authorized Value-Added Reseller. Distributors regularly provide us with reporting of their “sales-out” for this purpose. Until it is sold, inventory held by distributors is included in our reported finished goods inventory and was $3.8 million and $5.1 million at March 27, 2005 and June 27, 2004, respectively. The accounts receivable owed us by distributors, net of the deferred revenue from sales to distributors, is recorded in other current assets, as reflected in the following table (in thousands):

	March 27, 2005	June 27, 2004
Accounts receivable from distributors, net of allowance for doubtful accounts of $97 at March 27, 2005 ($724 at June 27, 2004)	$ 26,050	$ 20,350
Deferred revenue	(16,068)	(20,151)
Net	$ 9,982	$ 199

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Guarantees and Product Warranties

Financial Accounting Standards Board ("FASB") Interpretation No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others* ("FIN 45") requires that upon issuance of a guarantee, the guarantor must disclose and recognize a liability for the fair value of the obligation it assumes under that guarantee.

We have determined that the requirements of FIN 45 apply to our standard product warranty liability. The following table summarizes the activity related to our product warranty liability during the nine months ended March 27, 2005 and March 28, 2004 (in thousands):

	Nine Months Ended	
	March 27, 2005	March 28, 2004
Balance beginning of period	$ 8,297	$ 10,200
Warranties issued	8,779	8,573
Settlements made	(10,331)	(9,837)
Change in estimate	1,128	—
Balance end of period	$ 7,873	$ 8,936

Our standard warranty period is typically 12 months from the date of purchase by end-users. Upon shipment of products to our customers, we estimate expenses for the cost to repair or replace products that may be returned under warranty and accrue a liability in cost of product revenue for this amount. The determination of our warranty requirements is based on actual historical experience with the product or product family, estimates of repair and replacement costs and any product warranty problems that are identified after shipment. We estimate and adjust these accruals at each balance sheet date in accordance with changes in these factors. There was no change in estimate for the first nine months of fiscal 2004. The change in estimate in the first quarter of fiscal 2005 results from a change in the method to accumulate the warranty return rates.

In the normal course of business to facilitate sales of our products, we indemnify our resellers and end-user customers with respect to certain matters. We have agreed to hold the customer harmless against losses arising from a breach of intellectual property infringement or other claims made against certain parties. These agreements may limit the time within which an indemnification claim can be made and the amount of the claim. It is not possible to estimate the maximum potential amount under these indemnification agreements due to the limited history of prior indemnification claims and the unique facts and circumstances involved in each particular agreement. Historically, payments made by us under these agreements have not had a material impact on our operating results or financial position.

The requirements of FIN 45 are applicable to a guarantee of a lease obligation of one of our former contract manufacturers and to letters of credit issued under our line of credit. As of March 27, 2005, the lease obligation in the amount of $0.9 million has been recognized as a lease liability on the condensed consolidated balance sheet and the letters of credit totaled $0.8 million.

Deferred Service Revenue

We offer renewable service contracts, including extended warranty contracts, to our customers that range generally from one to five years. The change in our deferred service revenue balance in relation to these arrangements was as follows (in thousands):

	Nine Months Ended	
	March 27, 2005	March 28, 2004
Balance beginning of period	$ 50,178	$ 44,223
New service arrangements	36,066	37,810
Recognition of service revenue	(39,243)	(31,681)
Balance end of period	$ 47,001	$ 50,352

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Stock-Based Compensation

As provided by Statement of Financial Accounting Standards ("SFAS") No. 123, *Accounting for Stock Based Compensation* ("SFAS 123"), we have elected to follow APB Opinion No. 25, *Accounting for Stock Issued to Employees ("APB No. 25")*, in accounting for our employee stock options. Under APB No. 25, when the exercise price of our employee stock options equals the market price of the underlying stock on the date of grant, no compensation expense is recognized in our financial statements.

Pro forma information regarding net income (loss) and earnings (loss) per share is required by SFAS 123. This information is required to be determined as if we had accounted for our employee stock options and shares issued under the Employee Stock Purchase Plan under the fair value method of that statement. The fair value of options and shares granted in the three and nine months ended March 27, 2005 and March 28, 2004 was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted average assumptions:

	Stock Option Plan				Employee Stock Purchase Plan			
	Three Months Ended		Nine Months Ended		Three Months Ended		Nine Months Ended	
	March 27, 2005	March 28, 2004	March 27, 2005	March 28, 2004	March 27, 2005	March 28, 2004	March 27, 2005	March 28, 2004
Expected life	3.3 yrs	3.3 yrs	3.2 yrs	2.9 yrs	0.6 yrs	0.6 yrs	0.6 yrs	0.6 yrs
Risk-free interest rate	3.5%	2.4%	3.1%	2.3%	2.4%	1.0%	2.1%	1.1%
Volatility	47%	63%	48%	78%	47%	63%	47%	78%
Expected dividend yield	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%

The Black-Scholes option valuation model requires the input of highly subjective assumptions, including the expected life of the stock-based award and stock price volatility. The assumptions listed above represent management's best estimates, but these estimates involve inherent uncertainties. As a result, if other assumptions had been used, our pro forma stock-based compensation expense could have been materially different from that depicted above.

The weighted-average estimated per share fair values of options granted in the third quarter of fiscal 2005 and fiscal 2004 were $2.22 and $3.61, respectively. The weighted-average estimated per share fair values of shares issued under the Employee Stock Purchase Plan in the third quarter of fiscal 2005 and fiscal 2004 were $1.92 and $1.93, respectively. Pro forma information regarding net income (loss) and earnings (loss) per share is required by SFAS 123. This information is required to be determined as if we had accounted for employee stock options and shares issued under the Employee Stock Purchase Plan under the fair value method of that statement. For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the options' vesting periods. The following pro forma information sets forth our net income (loss) and net income (loss) per share assuming that we had used the SFAS 123 fair value method in accounting for employee stock options and share purchases (in thousands, except per share amounts):

	Three Months Ended		Nine Months Ended	
	March 27, 2005	March 28, 2004	March 27, 2005	March 28, 2004
Net income (loss) – as reported	$ (1,257)	$ (1,106)	$ 12,819	$ (4,097)
Add: APB 25 stock-based employee compensation expense, as reported	2	111	69	696
Less: Stock-based employee compensation expense determined under fair value based method, net of tax	(4,300)	(2,912)	(16,465)	(15,679)
Pro forma net loss	$ (5,555)	$ (3,907)	$ (3,577)	$(19,080)
Basic net income (loss) per share:				
As reported	$ (0.01)	$ (0.01)	$ 0.11	$ (0.03)
Pro forma	$ (0.05)	$ (0.03)	$ (0.03)	$ (0.16)
Diluted net income (loss) per share:				
As reported	$ (0.01)	$ (0.01)	$ 0.10	$ (0.03)
Pro forma	$ (0.05)	$ (0.03)	$ (0.03)	$ (0.16)

See Recently Issued Accounting Standards for a discussion of SFAS 123R.

Recently Issued Accounting Standards

Share-Based Payment

On December 16, 2004, the Financial Accounting Standards Board ("FASB") issued SFAS 123 (revised 2004), *Share-Based Payment* ("SFAS 123(R)"), which is a revision of SFAS 123. SFAS 123(R) supersedes APB 25 and amends SFAS 95, *Statement of Cash Flows*. Generally, the approach in SFAS 123(R) is similar to the approach described in SFAS 123. However, SFAS 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the statement of operations based on their fair values. Pro forma disclosure is no longer an alternative. We expect to adopt SFAS 123(R) at the beginning of our first quarter of fiscal 2006.

SFAS 123(R) permits public companies to adopt its requirements using one of two methods: 1) a "modified prospective" method in which compensation cost is recognized beginning with the effective date (a) based on the requirements of SFAS 123(R) for all share-based payments granted after the effective date and (b) based on the requirements of SFAS 123 for all awards granted to employees prior to the effective date of SFAS 123(R) that remain unvested on the effective date: or 2) a "modified retrospective" method, which includes the requirements of the modified prospective method described above, but also permits entities to restate based on the amounts previously recognized under SFAS 123 for purposes of pro forma disclosures either (a) all prior periods presented or (b) prior interim periods of the year of adoption. We plan to adopt SFAS 123 (R) using the modified-prospective method.

We are currently evaluating the requirements of SFAS 123(R) and we have not yet fully determined the impact on our consolidated financial statements. We believe the impact to our financial statements will result in a material increase in our stock-based employee compensation expense recognized in our consolidated statements of operations, although it will have no impact on our overall financial position. The stock-based employee compensation expense presented in our pro forma financial results required to be disclosed under SFAS 123 was $4.3 million and $16.5 million in the three and nine month periods ended March 27, 2005. Additionally, SFAS 123(R) also requires the benefits of tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as an operating cash flow as required under current literature. This requirement will reduce net operating cash flows and increase net financing cash flows in periods after adoption.

Identification of Impaired Investments

In March 2004, the FASB approved the consensus reached on EITF Issue No. 03-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments* ("EITF 03-1"). EITF 03-1 provides new guidance for evaluating impairment losses on debt and equity investments, as well as new disclosure requirements for investments that are determined to be other-than-temporarily impaired. In September 2004, the FASB approved the issuance of a FASB Staff Position to delay the requirement to record impairment losses under EITF 03-1. The approved delay applies to all securities within the scope of EITF 03-1 and is expected to end when new guidance is issued and comes into effect. As substantially all of our investments are investment grade government and corporate debt securities that have maturities of less than 3 years, and we have both the ability and intent to hold the investments until maturity, we do not expect EITF 03-1, if and when the requirement to record impairment losses becomes effective, to have a material impact on our financial position and results of operations.

Inventory Costs

In November 2004, the FASB issued SFAS 151, *Inventory Costs – an amendment of ARB No. 43*, *Chapter 4*, which requires companies to expense abnormal freight, handling costs, or spoilage in the period incurred and to allocate fixed overhead based on normal capacity, with adjustment if production is abnormally high. This standard becomes effective on July 1, 2005. We currently account for abnormal freight, handling costs, and spoilage consistent with this standard. We plan to adopt the provisions on a prospective basis in the first fiscal quarter of 2006. We are currently evaluating the effects of implementing this standard, however we do not expect it to have a material impact on our financial position and results of operations.

2. Commitments, Contingencies and Leases

Line of Credit

We have a revolving line of credit for $10.0 million with a major lending institution. Borrowings under this line of credit bear interest at the bank's prime rate, which was 5.75% at March 27, 2005. As of March 27, 2005, there were no outstanding borrowings under this line of credit. The line of credit contains a provision for the issuance of letters of credit not to exceed the unused balance of the line. As of March 27, 2005, we had letters of credit totaling $0.8 million. These letters of credit were primarily issued to satisfy requirements of certain of our customers for performance bonds. The line of credit requires us to maintain specified financial covenants related to tangible net worth and liquidity, with which we were in compliance as of March 27, 2005. The line of credit expires on January 26, 2006.

Lease Liability

As part of our business relationship with MCMS, Inc. ("MCMS"), a former contract manufacturer, we entered into a $9.0 million operating equipment lease for manufacturing equipment in September 2000 with a third-party financing company; we, in turn, subleased the equipment to MCMS. During the first quarter of fiscal 2002, due to the liquidity problems at MCMS and its voluntary filing for protection under Chapter 11, we recorded a charge of $9.0 million related to this lease. The liability, net of payments, related to this lease is included in lease liability on the condensed consolidated balance sheets. The equipment lease with the third-party financing company requires us to make monthly payments through September 2005 and to maintain specified financial covenants, which we were not in compliance as of March 27, 2005. As of March 31, 2005, we obtained a waiver from the third-party financing company, which allowed the lease to remain in effect.

Purchase Commitments

We currently have arrangements with one contract manufacturer and other suppliers for the manufacture of our products. Our arrangements allow them to procure long lead-time component inventory on our behalf based upon a rolling production forecast provided by us. We are obligated to the purchase of long lead-time component inventory that our contract manufacturer procures in accordance with the forecast, unless we give notice of order cancellation outside of applicable component lead-times. As of March 27, 2005, we had non-cancelable commitments to purchase approximately $24.2 million of such inventory during the fourth quarter of fiscal 2005.

Legal Proceedings

On May 27, 2003, Lucent filed suit against Foundry Networks, Inc. ("Foundry") and us. Foundry severed its case from the original case. The complaint against us alleges willful infringement of U.S. Patent Nos. 4,769,810, 4,769,811, 4,914,650, 4,922,486 and 5,245,607 and seeks a judgment: (a) determining that we have willfully infringed each of the five patents; (b) permanently enjoining us from infringement, inducement of infringement and contributory infringement of each of the five patents; and (c) awarding Lucent unspecified amounts of trebled damages, together with expenses, costs and attorneys' fees.

We intend vigorously to defend against Lucent's allegations. We answered Lucent's complaint on July 16, 2003, denying infringement and asserting various affirmative defenses and counterclaims.

The claim construction hearing was held January 14, 2005. The trial has been separated into three parts by court order, with infringement, willfulness and damages to be heard first in a trail that commenced April 28, 2005, to be followed immediately before the same jury on the issue of invalidity, with the equitable defenses and counterclaims to be held in a third trial at a date to be determined. While the outcome of this matter is currently not determinable, the ultimate costs to resolve it, whether through litigation or settlement, and whether we are successful or not, has had, and could continue to have, a material adverse effect on our consolidated financial statements, results of operations, and cash flows.

Beginning on July 6, 2001, purported securities fraud class action complaints were filed in the United States District Court for the Southern District of New York. The cases were consolidated and the litigation is now captioned as In re our Initial Public Offering Securities Litigation, Civ. No. 01-6143 (SAS) (S.D.N.Y.), related to In re Initial Public Offering Securities Litigation, 21 MC 92 (SAS) (S.D.N.Y.).

The operative amended complaint is brought purportedly on behalf of all persons who purchased our common stock from April 8, 1999 through December 6, 2000. It names as defendants Extreme Networks; six of our present and former officers and/or directors, including our CEO (the "Extreme Networks Defendants"); and several investment banking firms that served as underwriters of our initial public offering and October 1999 secondary offering. Subsequently, plaintiffs and one of the individual defendants stipulated to a dismissal of that defendant without prejudice. The complaint alleges liability under Sections 11 and 15 of the Securities Act of 1933 and Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, on the grounds that the registration statement for the offerings did not disclose that: (1) the underwriters had agreed to allow certain customers to purchase shares in the offerings in exchange for excess commissions paid to the underwriters; and (2) the underwriters had arranged for certain customers to purchase additional shares in the aftermarket at predetermined prices. The Securities Act allegations against the Extreme Networks Defendants are made as to the secondary offering only. The amended complaint also alleges that false analyst reports were issued. No specific damages are claimed.

Similar allegations were made in other lawsuits challenging over 300 other initial public offerings and follow-on offerings conducted in 1999 and 2000. The cases were consolidated for pretrial purposes. On February 19, 2003, the Court ruled on all defendants' motions to dismiss. The Court denied the motions to dismiss the claims in our case under the Securities Act of 1933. The Court denied the motion to dismiss the claim under Section 10(a) of the Securities Exchange Act of 1934 against us and 184 other issuer defendants, on the basis that the complaints alleged that the respective issuers had acquired companies or conducted follow-on offerings after their initial public offerings. The Court denied the motion to dismiss the claims under Section 10(a) and 20(a) of the Securities Exchange Act of 1934 against the remaining Extreme Networks Defendants and 59 other individual defendants, on the basis that the respective amended complaints alleged that the individuals sold stock.

We have executed a settlement agreement presented to all issuer defendants. In this settlement, plaintiffs will dismiss and release all claims against the Extreme Network Defendants, in exchange for a contingent payment by the insurance companies collectively responsible for insuring the issuers in all of the IPO cases, and for the assignment or surrender of control of certain claims we may have against the underwriters. The Extreme Networks Defendants will not be required to make any cash payments in the settlement, unless the pro rata amount paid by the insurers in the settlement exceeds the amount of the insurance coverage, a circumstance which we do not believe will occur. The settlement will require approval of the Court, which cannot be assured. On February 15, 2005, the Court issued an order providing preliminary approval of the settlement, except insofar as the settlement would have cut off contractual indemnification claims that underwriters may have against securities issuers, such as the Company. The Court has scheduled a hearing for January 9, 2006 to consider final approval of the settlement. If the settlement is not approved, we cannot assure you that we will prevail in the lawsuit. Failure to prevail could have a material adverse effect on our consolidated financial position, results of operations and cash flows in the future.

We are subject to other legal proceedings, claims and litigation arising in the ordinary course of business. While the outcome of these matters, including the specific matters discussed above, is currently not determinable, the ultimate costs to resolve these matters or future matters could have a material adverse effect on our consolidated financial position, results of operations or cash flows.

3. Comprehensive Income (Loss)

Comprehensive income (loss) was as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	March 27, 2005	March 28, 2004	March 27, 2005	March 28, 2004
Net income (loss)	$ (1,257)	$ (1,106)	$ 12,819	$ (4,097)
Other comprehensive income (loss):				
Change in unrealized gain/loss on investments:				
Net unrealized loss on investments	(1,999)	(66)	(2,062)	(1,295)
Less: Net gain on investments realized and included in interest income	—	6	—	27
Net unrealized loss on investments	(1,999)	(72)	(2,062)	(1,322)
Net unrealized loss on derivatives	—	—	—	(1)
Foreign currency translation adjustments	(25)	20	315	476
Total comprehensive income (loss)	$ (3,281)	$ (1,158)	$ 11,072	$ (4,944)

4. Income Taxes

We recorded an income tax provision of $0.8 million and $0.3 million for the three months ended March 27, 2005 and March 28, 2004, respectively. We recorded an income tax provision of $3.0 million and $1.1 million for the nine months ended March 27, 2005 and March 28, 2004, respectively. The effective tax rates were (186%) and (44%) for the three months ended March 27, 2005 and March 28, 2004, respectively, and 19% and (39%) for the nine months ended March 27, 2005 and March 28, 2004, respectively. The effective tax rates differ from the statutory tax rate due to benefits for U.S. taxes from net operating loss carryforwards and tax credits, offset by the tax impact on income from foreign operations. The change in the effective tax rate from 13% in the first six months of fiscal 2005 to 19% in the first nine months of fiscal 2005 is due primarily to lower projected income before tax, and projected tax expense from foreign operations that does not change in proportion to the consolidated income before tax. We have provided a full valuation allowance against all of our U.S. federal and state deferred tax assets in fiscal 2003 in accordance with the provisions of SFAS No. 109, *Accounting for Income Taxes*.

5. Net Income (Loss) Per Share

Basic earnings (loss) per share is calculated by dividing net income (loss) by the weighted average number of common shares outstanding during the period, less shares subject to repurchase, and excludes any dilutive effects of options, warrants and convertible subordinated notes. Dilutive earnings (loss) per share is calculated by dividing net income (loss) by the weighted average number of common shares used in the basic earnings (loss) per share calculation plus the dilutive effect of shares subject to repurchase, options, warrants and convertible subordinated notes. The computation of diluted net income (loss) per share excludes the impact of the conversion of the convertible subordinated notes due in December 2006, which are convertible into approximately 9.5 million shares of common stock, as the impact of adding back to income the after tax interest expense associated with the convertible subordinated notes, and including the impact of the common shares to be issued, would be anti-dilutive in the periods presented. Diluted net loss per share was the same as basic net loss per share for the three months ended March 27, 2005, and the three and nine months ended March 28, 2004 because we had net losses in those periods.

The following table presents the calculation of basic and diluted net income (loss) per share (in thousands, except per share data):

	Three Months Ended		Nine Months Ended	
	March 27, 2005	March 28, 2004	March 27, 2005	March 28, 2004
Net income (loss)	$ (1,257)	$ (1,106)	$ 12,819	$ (4,097)
Weighted-average shares of common stock outstanding	121,444	118,896	121,046	117,837
Less: Weighted-average shares subject to repurchase	—	(64)	(5)	(131)
Weighted-average shares used in per share calculation — basic	121,444	118,832	121,041	117,706
Incremental shares using the treasury stock method	—	—	3,170	—
Weighted-average shares used in per share calculation — diluted	121,444	118,832	124,211	117,706
Net income (loss) per share — basic	$ (0.01)	$ (0.01)	$ 0.11	$ (0.03)
Net income (loss) per share — diluted	$ (0.01)	$ (0.01)	$ 0.10	$ (0.03)

The following table sets forth potential shares of common stock that are not included in the diluted net income (loss) per share calculations above because to do so would be anti-dilutive for the periods presented (in thousands):

	Three Months Ended		Nine Months Ended	
	March 27, 2005	March 28, 2004	March 27, 2005	March 28, 2004
Stock options outstanding	14,761	2,920	15,694	2,547
Unvested common stock subject to repurchase	—	64	—	131
Warrants outstanding	1,716	2,459	—	1,392
Convertible subordinated notes	9,542	9,542	9,542	9,542
Total potential shares of common stock excluded from the computation of diluted net income (loss) per share	26,019	14,985	25,236	13,612

Stock options outstanding are considered to be anti-dilutive under the treasury stock method when the exercise price of the option exceeds the market value of the shares. The increase in anti-dilutive stock options outstanding from March 28, 2004 to March 27, 2005 is due to two factors: an increase in the number of weighted options outstanding, and a decrease in the market value of the shares, which has increased the number of stock options outstanding that are considered to be anti-dilutive.

6. Restructuring Charges

During fiscal 2004, we recorded restructuring charges of $6.5 million related to excess facilities. The excess facilities charge represented an increase to the charge initially recognized during fiscal 2002. The commercial real estate market continued to deteriorate in fiscal 2004 and we were not able to find suitable tenants to sublease these facilities. The lower projected sublease income necessitated an increase in the related liability that takes into consideration the unfavorable difference between lease obligation payments and projected sublease receipts. The actual cost could differ from this estimate, and additional facilities charges could be incurred if we are unsuccessful in negotiating reasonable termination fees on certain facilities, if facility operating lease rental rates continue to decrease in these markets, if it takes longer than expected to find a suitable tenant to sublease these facilities or if other estimates and assumptions change.

During fiscal 2003, we recorded restructuring charges of $15.9 million. The restructuring charges included excess facilities charges of $9.6 million, severance charges of $4.4 million and asset impairments of $1.9 million. The excess facilities charge represented an increase to the charge recognized during fiscal 2002 for the domestic and international facilities. Severance charges of $2.7 million related to a reduction in total staff during the second quarter of fiscal 2003 of approximately 100 people, or 10% of the total workforce, across all departments. Severance charges of $1.7 million related to a reduction in total staff announced at the end of the fiscal year of approximately 70 people, or 8% of the total workforce, across all departments. The asset impairment charge relates to the write-off of leasehold improvements and office furniture related to excess facilities.

Activity with respect to restructuring liabilities is as follows (in thousands):

	Excess Facilities	Asset Impairments	Severance	Total
Balance at June 29, 2003	$26,418	$ —	$ 1,752	$28,170
Charge in first quarter of fiscal 2004	876	122	(36)	962
Charge in fourth quarter of fiscal 2004	5,622	—	(97)	5,525
Write-offs	—	(122)	—	(122)
Cash payments	(6,353)	—	(1,619)	(7,972)
Balance at June 27, 2004	26,563	—	—	26,563
Cash payments	(4,965)	—	—	(4,965)
Balance at March 27, 2005	21,598	—	—	21,598
Less: current portion	(6,139)	—	—	(6,139)
Restructuring liabilities at March 27, 2005, less current portion	$15,459	$ —	$ —	$15,459

7. Subsequent Event

Technology Agreement

On March 31, 2005, we entered into a Patent and Cross License Agreement (“Technology Agreement”) with IBM. The agreement provides for a release of prior claims and a cross license of patents extending into the future from the effective date of the agreement. We charged the estimated value of the release of prior claims of $2 million to operating expenses in the quarter ended March 27, 2005 under the caption “Technology agreement”. The remaining costs payable under this agreement will be charged to cost of product revenue over the license term. We expect these costs to have a small impact on the total cost of product revenue.

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

This quarterly report on Form 10-Q, including the following sections, contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, particularly statements relating to our expectations regarding results of operations, our ability to expand our market penetration, our ability to expand our distribution channels, customer acceptance of our products, our ability to meet the expectations of our customers, product demand and revenue, cash flows, product gross margins, our expectations to continue to develop new products and enhance existing products, our expectations to reduce warranty expenses as a percentage of revenue, our expectations regarding the amount of our research and development expenses, our expectations regarding the amount/level of our selling, general and administrative expenses, our efforts to achieve additional operating efficiencies and to review and improve our business systems and cost structure, our expectations to continue investing in technology, resources and infrastructure, our expectations concerning the availability of products from suppliers and contract manufacturers, anticipated product costs and sales prices, our expected income tax rate, our expectations that we have sufficient capital to meet our requirements for at least the next twelve months, our expectations regarding the rationalization of our workforce and facilities, and our expectations regarding materials and inventory management. These forward-looking statements involve risks and uncertainties, and the cautionary statements set forth below and those contained in the section entitled "Risk Factors" identify important factors that could cause actual results to differ materially from those predicted in any such forward-looking statements. We caution investors that actual results may differ materially from those projected in the forward-looking statements as a result of certain risk factors identified in this Form 10-Q and other filings we have made with the Securities and Exchange Commission.

Business Overview

We develop and sell a family of modular and stackable network infrastructure equipment and offer related service contracts for extended warranty and maintenance agreements. Substantially all of our revenue is derived from the sale of networking equipment and the related service contracts. We believe that understanding the following key developments is helpful to an understanding of our operating results for the third quarter and first nine months of fiscal 2005.

Increased Product Breadth

We believe that continued success in the marketplace will depend on our ability to develop new and enhanced products employing leading-edge technology. In the second quarter of fiscal 2005, we began shipping our new high performance Black Diamond 8800 switch (previously referred to as Aspen), which provides true voice-class availability at the edge of the network. In fiscal 2004 we introduced several new products, including the Black Diamond 10K, the Summit 300-48/Altitude 300 and the Summit 400 series.

Convergence of Voice, Video and Data

We have a vision of providing customers with the systems to build a converged communications infrastructure that can easily accommodate voice, video and data on a seamless wired and wireless network. We believe that these two aspects of convergence, the convergence of voice, video and data, and the convergence of wired and wireless, are important underlying demand creators in the Enterprise market.

In November 2003, we announced our comprehensive strategic alliance with Avaya, Inc. to jointly develop and market converged communications solutions. The goal of the alliance is to bring together Avaya's global market leadership in IP voice and telephony with our expertise in high performance IP data network infrastructure. Under the Joint Development Agreement, the companies plan to develop next generation, standards-based technologies in the areas of network management and provisioning, Quality of Service, security and network resilience. Additionally, Avaya sells, services and supports our entire portfolio of data networking products through its worldwide sales organization and the Avaya Global Services organization.

Expanded Focus on Service Offering

Our service offering is primarily the provision of service contracts for extended warranty and maintenance agreements related to our networking equipment. To a lesser extent, the service revenue includes professional services related to the design and installation of data networks and training. Service revenue increased by 18% in the third quarter of fiscal 2005 compared to the third quarter of fiscal 2004 and represented 16% of total revenues in the third quarter of fiscal 2005 compared to 14% in the third quarter of fiscal 2004. Service revenue increased by 23% in the first nine months of fiscal 2005 compared to the first nine months of fiscal 2004 and represented 15% of total revenues in the first nine months of fiscal 2005 compared to 14% in the first nine months of fiscal 2004. In fiscal 2004, we focused our service sales efforts on increasing the number of service contracts sold on new equipment and in the area of securing renewals on expiring contracts. Cost of service revenue remained flat in the third quarter of fiscal 2005 at $9.0 million and service gross margin improved to 41% in the third quarter of fiscal 2005 from 30% in the third quarter of fiscal 2004 due to efforts to improve and optimize our service supply chain. Cost of service revenue decreased by $1.3 million in the first nine months of fiscal 2005 to $25.6 million and service gross margin improved to 41% in the first nine months of fiscal 2005 from 24% in the first nine months of fiscal 2004 due to efforts to improve product reliability and optimize our service supply chain.

Results of Operations

Net Revenues

The following table presents net product and service revenues for the three and nine months ended March 27, 2005 and March 28, 2004 (dollars in thousands):

	Three Months Ended March 27, 2005		Three Months Ended March 28, 2004		Nine Months Ended March 27, 2005		Nine Months Ended March 28, 2004	
	$	% of Net Revenues	$	% of Net Revenues	$	% of Net Revenues	$	% of Net Revenues
Net revenues:								
Product	$76,835	83.6%	$76,059	85.6%	$243,770	84.9%	$224,315	86.4%
Service	15,073	16.4%	12,815	14.4%	43,525	15.1%	35,375	13.6%
Total net revenues	$91,908	100.0%	$88,874	100.0%	$287,295	100.0%	$259,690	100.0%

Net revenues were $91.9 million in the third quarter of fiscal 2005 and $88.9 million in the third quarter of fiscal 2004, representing an increase of 3% in the third quarter of fiscal 2005 from the third quarter of fiscal 2004. Net revenues were $287.3 million in the first nine months of fiscal 2005 and $259.7 million in the first nine months of fiscal 2004, representing an increase of 11% in the first nine months of fiscal 2005 from the first nine months of fiscal 2004.

Product revenue increased to $76.8 million for the third quarter of fiscal 2005 from $76.1 million for the third quarter of fiscal 2004, an increase of $0.7 million. Product revenue increased by 1% in the third quarter of fiscal 2005 compared to the third quarter of fiscal 2004. Product revenue increased to $243.8 million for the first nine months of fiscal 2005 from $224.3 million for the first nine months of fiscal 2004, an increase of $19.5 million. Product revenue increased by 9% in the nine months of fiscal 2005 compared to the same nine-month period in fiscal 2004. Revenues for our stackable products have increased slightly as a percentage of total product revenue, as have sales of recently introduced modular products, including the Black Diamond 10K and Black Diamond 8800. Revenue for some of our older modular products has declined.

Service revenue increased by 18% to $15.1 million for the third quarter of fiscal 2005 from $12.8 million for the third quarter of fiscal 2004, an increase of $2.3 million. Service revenue increased to $43.5 million for the first nine months of fiscal 2005 from $35.4 million for the first nine months of fiscal 2004, an increase of $8.1 million, or 23%. These increases were primarily due to implementing a focused sales and marketing effort to increase the number of service contracts by increasing the attachment rate of service contract sales on new equipment and on increasing the rate of renewals on existing service contracts.

The following table presents total net revenues geographically for the three and nine months ended March 27, 2005 and March 28, 2004 (dollars in thousands):

	Three Months Ended March 27, 2005		Three Months Ended March 28, 2004		Nine Months Ended March 27, 2005		Nine Months Ended March 28, 2004	
	$	% of Net Revenues	$	% of Net Revenues	$	% of Net Revenues	$	% of Net Revenues
Net revenues:								
United States	$40,689	44.3%	$37,492	42.2%	$123,967	43.1%	$ 98,688	38.0%
Europe, Middle East and Africa	27,400	29.8%	23,500	26.4%	82,500	26.5%	69,000	26.6%
Japan	13,200	14.4%	20,000	22.5%	48,400	19.1%	58,400	22.5%
Other	10,619	11.5%	7,882	8.9%	32,428	11.3%	33,602	12.9%
Total net revenues	$91,908	100.0%	$88,874	100.0%	$287,295	100.0%	$259,690	100.0%

Sales of products and services outside the United States accounted for approximately 55.7% of our business in the third quarter of fiscal 2005, compared to 57.8% in the third quarter of fiscal 2004. Sales of products and services outside the United States accounted for approximately 56.9% of our business in the first nine months of fiscal 2005, compared to 62.0% in the first nine months of fiscal 2004. Net revenues in Japan declined by 34% and 17% in the three and nine months ended March 27, 2005, respectively, as compared to the same periods in the prior fiscal year primarily due to a decline in business with our service provider customer segment. We expect that export sales will continue to represent a significant portion of net revenues, although export sales may fluctuate as a percentage of net revenues. Substantially all sales transactions are denominated in United States dollars.

We rely upon our two-tiered distribution channel for the majority of our revenues. Revenue through the distributor channel as a percentage of total product revenue was 33.5% in the third quarter of fiscal 2005 and 30.6% in the third quarter of fiscal 2004. Revenue through the distributor channel as a percentage of total product revenue was 32.0% in the first nine months of fiscal 2005 and 32.9% in the first nine months of fiscal 2004. The level of sales to any customer may vary from period to period; however, we expect that significant customer concentration will continue for the foreseeable future. None of our customers accounted for greater than 10% of our net revenues for the third quarter of fiscal 2005 or fiscal 2004. None of our customers accounted for 10% of our net revenues for the first nine months of fiscal 2005 or fiscal 2004.

Cost of Revenues and Gross Margin

The following table presents the gross margin on product and service revenues and the gross margin percentage of product and service revenues for the three and nine months ended March 27, 2005 and March 28, 2004 (dollars in thousands):

	Three Months Ended March 27, 2005		Three Months Ended March 28, 2004		Nine Months Ended March 27, 2005		Nine Months Ended March 28, 2004	
	$	Gross Margin %	$	Gross Margin %	$	Gross Margin %	$	Gross Margin %
Gross margin:								
Product	$41,143	53.6%	$41,637	54.7%	$133,819	54.9%	$122,356	54.6%
Service	6,119	40.6%	3,836	29.9%	17,957	41.3%	8,462	23.9%
Total gross margin	$47,262	51.4%	$45,473	51.2%	$151,776	52.8%	$130,818	50.4%

Gross margin was $47.3 million in the third quarter of fiscal 2005 and $45.5 million in the third quarter of fiscal 2004, representing an increase of 4% in the third quarter of fiscal 2005 from the third quarter of fiscal 2004. Gross margin as a percentage of net revenues was 51.4% and 51.2% in the third quarter of fiscal 2005 and the third quarter of fiscal 2004, respectively. Gross margin was $151.8 million in the first nine months of fiscal 2005 and $130.8 million in the first nine months of fiscal 2004, representing an increase of 16% in the first nine months of fiscal 2005 from the first nine months of fiscal 2004. Gross margin as a percentage of net revenues was 52.8% and 50.4% in the first nine months of fiscal 2005 and the first nine months of fiscal 2004, respectively.

Cost of product revenue includes costs of raw materials, amounts paid to third-party contract manufacturers, costs related to warranty obligations, charges for excess and obsolete inventory and internal costs associated with manufacturing overhead, including management, manufacturing engineering, quality assurance, development of test plans and document control. Product gross margin in the third quarter of fiscal 2005 was $41.1 million, representing 53.6% of product revenue as compared to $41.6 million in the third quarter of fiscal 2004, or 54.7% of product revenue. Product gross margin as a percentage of product revenue declined by 1.1 percentage points in the third quarter of fiscal 2005 as compared to the same quarter of the prior year primarily due to changes in the mix of revenue by geography and channel, as well as slightly higher sales discounts. Product gross margin in the first nine months of fiscal 2005 was $133.8 million, representing 54.9% of product revenue as compared to $122.4 million in the first nine months of fiscal 2004, or 54.6% of product revenue. Product gross margin as a percentage of product revenue increased by 30 basis points in the nine months of fiscal 2005 as compared to the same period of fiscal 2004 primarily as a result of a reduction in the average cost of product purchased from our contract manufacturer, offset by slightly higher warranty cost and technology license costs. Some of the costs of product revenue components such as the internal costs associated with certain manufacturing overhead are of a fixed nature and generally do not increase or decrease relative to our revenue base. Other costs, such raw materials and amounts paid to third-party contract manufacturers are of a variable nature and the per-unit costs have remained relatively flat corresponding to our revenue base. Our efforts to maintain fixed costs and lower the per unit variable cost should provide leverage in the growth of product gross margin if we are successful in increasing the product revenue base.

Cost of product revenue in all periods includes the cost of our manufacturing overhead. We outsource the majority of our manufacturing and supply chain operations, and we conduct planning, supply chain management, quality assurance, manufacturing engineering, document control and repair operations and spares logistics management at our facility in Santa Clara, California. Accordingly, a significant portion of our cost of product revenue consists of payments to our contract manufacturer, Flextronics International, Ltd. located in San Jose, California and Guadalajara, Mexico, which manufactures substantially all of our products.

Our cost of service consists primarily of labor, overhead, repair and freight costs and the cost of spares used in providing support under customer service contracts. Service gross margin in the third quarter of fiscal 2005 was $6.1 million, representing 40.6% of service revenue as compared to $3.8 million in the third quarter of fiscal 2004, or 29.9% of service revenue. Service gross margin in the first nine months of fiscal 2005 was $18.0 million, representing 41.3% of service revenue as compared to $8.5 million in the first nine months of fiscal 2004, or 23.9% of service revenue. The increase in service gross margin resulted from a number of programs that we implemented during fiscal 2004 and fiscal 2003 to improve service delivery productivity and to enhance customer satisfaction. These programs included implementing a focused sales and marketing effort to increase the number of service contracts by increasing the attachment rate of service contract sales on new equipment and on increasing the rate of renewals on existing service contracts. In addition, these programs in fiscal 2004 and fiscal 2003 included expenses incurred to reduce service infrastructure, including outsourcing certain service functions. In recent quarters, including the first, second and third quarters of fiscal 2005, the benefits of the programs implemented in fiscal 2004 and fiscal 2003 are being realized in the form of lower cost of service revenue on an increasing revenue base. Some of the costs of service revenue components, such as labor and overhead, are of a fixed nature and have not increased as we have expanded our revenue base. Other costs, such as repairs, freight and cost of spares are of a variable nature and the per unit costs have declined as we have expanded our revenue base. The combination of maintaining fixed costs and lowering the per unit variable cost while increasing the revenue base has provided significant leverage in the growth of gross service margin.

Our product and service gross margins are variable and dependent on many factors, some of which are outside of our control. Some of the primary factors affecting gross margin include demand for our products, changes in our pricing policies and those of our competitors, and the mix of products sold. Our gross margin may be adversely affected by increases in material or labor costs, increases in warranty expense, the cost of providing services under extended service contracts, heightened price competition, obsolescence charges and higher inventory balances. In addition, our gross margin may fluctuate due to the mix of distribution channels through which our products are sold, including the effects of our two-tier distribution model. Any significant decline in sales to our resellers, distributors or end-user customers, or the loss of any of our key resellers, distributors or end-user customers could have a material adverse effect on our business, operating results and financial condition. In addition, an increase in distribution channels generally makes it more difficult to forecast the mix of products sold and the timing of orders from our customers. New product introductions may result in excess or obsolete inventories, which may also reduce our gross margin.

Sales and Marketing Expenses

Sales and marketing expenses consist of salaries, commissions and related expenses for personnel engaged in marketing and sales functions, as well as trade shows and promotional expenses. Sales and marketing expenses increased to $23.9 million for the third quarter of fiscal 2005 from $23.3 million for the third quarter of fiscal 2004, an increase of $0.6 million. This increase was primarily due to increased payroll and related personnel expenses of $0.8 million and increased commission expense of $0.8 million, partially offset by a reduction in marketing expenses of $0.5 million due to cost saving measures implemented in fiscal 2005 and by a reduction in meeting and conference expenses of $0.7 million. Sales and marketing expenses increased to $70.9 million for the first nine months of fiscal 2005 from $68.8 million for the first nine months of fiscal 2004, an increase of $2.1 million. This increase was primarily due to increased payroll and related personnel expenses of $3.8 million due to compensation increases, plus increased commission expense of $1.9 million due to increased commission percentages and higher revenue, offset partially by reduced spending for advertising and marketing programs of $1.7 million. The rate of future spending in our sales and marketing expenses will largely depend on the pace of recovery in the market for networking products as well as new or additional programs or promotions we may choose to implement.

Research and Development Expenses

Research and development expenses consist principally of salaries and related personnel expenses, consultant fees and prototype expenses related to the design, development and testing of our products. Research and development expenses increased to $15.3 million for the third quarter of fiscal 2005 from $15.0 million for the third quarter of fiscal 2004, an increase of $0.3 million. This increase was primarily due to new programs related to corporate wide quality initiatives of $ 0.4 million and an increase of $0.3 million related to professional service costs, offset by a reduction of $0.3 million in depreciation costs. Research and development expenses increased to $45.6 million for the first nine months of fiscal 2005 from $42.9 million for the first nine months of fiscal 2004, an increase of $2.7 million. This result was due to increased payroll and related personnel expenses of approximately $1.1 million primarily from compensation increases, an increase of $2.0 million in the amortization of the warrant allocated to the joint development agreement with Avaya, which commenced on November 1, 2003, and approximately $1.4 million in costs associated with our quality initiative. These cost increases were offset by $1.9 million lower engineering project expenses. We expense all research and development costs as incurred. We believe that continued investment in research and development is critical to attaining our strategic objectives and, as a result, we expect these expenses will continue to be significant in future periods. We expect research and development expenses to increase in the fourth quarter of fiscal 2005.

General and Administrative Expenses

General and administrative expenses consist principally of salaries and related expenses for executive, finance and administrative personnel, professional fees and other general corporate expenses. General and administrative expenses decreased to $7.3 million for the third quarter of fiscal 2005 from $8.0 million for the third quarter of fiscal 2004, a decrease of $0.7 million. The decrease in the third quarter was due to $0.5 million in lower legal fees, $0.4 lower insurance costs, offset by higher expense associated with compliance with the Sarbanes-Oxley Act of 2002. Legal expenses related to intellectual property litigation with Lucent, which is expected to go to trial on April 26, 2005, are expected to continue and may cause general and administrative expenses to increase significantly in the fourth quarter of fiscal 2005. Expenses as a result of compliance with the Sarbanes-Oxley Act of 2002, including Section 404 thereof, are expected to continue and may increase in the remainder of fiscal 2005 as we implement procedures and activities to meet the requirements of this act. General and administrative expenses decreased to $21.9 million for the first nine months of fiscal 2005 from $22.9 million for the first nine months of fiscal 2004, a decrease of $1.0 million. The decrease in the nine-month period was primarily due to a $0.8 million of decreased legal fees and $1.0 million of lower insurance costs, offset by higher costs incurred associated with compliance with Sarbanes-Oxley and increases in payroll and personnel expenses associated with higher headcount and executive compensation. The rate of future spending in our general and administrative expenses is expected to increase. The increase will largely depend upon the cost of outside services and professional fees, including legal fees relating to the Lucent litigation expected to go to trial in the fourth quarter of fiscal 2005, settlement negotiations or licensing transactions and fees associated with compliance with the Sarbanes-Oxley Act of 2002.

Amortization of deferred stock-based compensation

Amortization of deferred stock-based compensation decreased to a nominal amount for the third quarter of fiscal 2005 from $0.2 million for the third quarter of fiscal 2004, a decrease of $0.2 million. Amortization of deferred stock-based compensation decreased to $0.1 million for the first nine months of fiscal 2005 from $0.9 million for the first nine months of fiscal 2004, a decrease of $0.8 million. Amortization of deferred stock-based compensation is attributable to unvested stock options subject to forfeiture issued to employees that we assumed in conjunction with acquisitions during fiscal 2001. Deferred stock-based compensation is amortized as charges to operations, using the graded vesting method, over the vesting periods of the individual stock options, generally four years. Upon termination of an employee, the amount of expense recognized under the graded vesting method that is in excess of the amount actually earned is reversed. For the third quarter and the first nine months of fiscal 2005, there were no reversals of excess compensation expense related to terminated employees. We reversed $0.1 million of excess compensation expense related to terminated employees for the third quarter and $0.3 million for the first nine months of fiscal 2004. As of March 27, 2005, we have expensed all of the deferred stock-based compensation associated with the acquisitions.

Restructuring Charge

There were no restructuring charges in the first nine months of fiscal 2005. During the first quarter of fiscal 2004, we recorded restructuring charges of $1.0 million related to excess facilities. The excess facilities charge represents an increase to the charge initially recognized during the third quarter of fiscal 2002. The commercial real estate market continued to deteriorate in fiscal 2004 and we were not able to find suitable tenants to sublease these facilities necessitating an additional charge due to lower projected sublease receipts. As a result of the excess facilities charges recorded in fiscal 2004, rent expense in fiscal 2005 is expected to remain approximately the same as the fiscal 2004 levels. We regularly evaluate the restructuring liability, and in particular our assumptions associated with sublease income on vacated real estate leases, and if our assumptions change, we will recognize the required changes in the restructuring liability in the period when our assumptions change.

Technology Agreement

On March 31, 2005, we entered into a Patent and Cross License Agreement (“Technology Agreement”) with IBM. The agreement provides for a release of prior claims and a cross license of patents extending into the future from the effective date of the agreement. We charged the estimated value of the release of prior claims of $2 million to operating expenses in the quarter ended March 27, 2005 under the caption “Technology agreement”. The remaining costs payable under this agreement will be charged to cost of product revenue over the license term. We expect these costs to have a small impact on the total product cost of revenue.

Other Income, Net

Other income, net increased to $0.8 million for the third quarter of fiscal 2005 from $0.3 million for the third quarter of fiscal 2004, an increase of $0.5 million. This increase was primarily due to increased interest income of $0.6 million due to higher average interest rates, offset partially by an increase in foreign exchange losses of $0.1 million. Other income, net increased to $4.6 million for the first nine months of fiscal 2005 from $2.7 million for the first nine months of fiscal 2004, an increase of $1.9 million. This increase was primarily due to the receipt of a foreign consumption tax refund of $3.9 million in the second quarter of fiscal 2005 and increased interest income of $1.2 million due to higher average interest rates, offset by increased foreign exchange losses of $0.9 million. The tax holiday in the foreign tax jurisdiction that provided the foreign consumption tax refund has expired, and no further benefits are expected. In the first nine months of fiscal 2004, we recorded other income of $2.2 million related to the settlement of litigation, net of related expenses.

Provision for Income Taxes

We recorded an income tax provision of $0.8 million and $0.3 million for the third quarter of fiscal 2005 and fiscal 2004, respectively. We recorded an income tax provision of $3.0 million and $1.1 million for the first nine months of fiscal 2005 and fiscal 2004, respectively. The effective tax rates were (186%) and 44% for the third quarter of fiscal 2005 and fiscal 2004, respectively, and 19% and (39%) for the first nine months of fiscal 2005 and fiscal 2004, respectively. The effective tax rates differ from the statutory tax rate due to benefits for U.S. taxes from net operating loss carryforwards and tax credits, offset by the tax impact from income of foreign operations. The change in the effective tax rate from 13% in the first six months of fiscal 2005 to 19% in the first nine months of fiscal 2005 is due primarily to lower projected income before tax, and projected tax expense from foreign operations that does not change in proportion to the consolidated income before tax. We have provided a full valuation allowance for our net U.S. deferred tax assets. We initially recorded this charge during fiscal 2003 in accordance with SFAS No. 109, *Accounting for Income Taxes* (“SFAS 109”), which places greater weight on previous cumulative losses than the outlook for future profitability when determining whether deferred tax assets can be realized. Based upon our most recent three-year history of losses and relying on other guidance specified in SFAS 109, we continue to believe that it is appropriate to maintain a full valuation allowance against our deferred tax assets. This valuation allowance is evaluated periodically and may be reversed partially or totally if business results sufficiently improve to support realization of our deferred tax assets.

Critical Accounting Policies and Estimates

Our significant accounting policies are more fully described in Note 2 of Notes to Consolidated Financial Statements included in our Form 10-K for the year ended June 27, 2004. The preparation of consolidated financial statements in accordance with U.S. generally accepted accounting principles requires management to make estimates, assumptions and judgments that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenue and expenses during the period reported. By their nature, these estimates, assumptions and judgments are subject to an inherent degree of uncertainty. We base our estimates, assumptions and judgments on historical experience, market trends and other factors that are believed to be reasonable under the circumstances. Estimates, assumptions and judgments are reviewed on an ongoing basis and the effects of revisions are reflected in the consolidated financial statements in the period they are determined to be necessary. Actual results may differ from these estimates under different assumptions or conditions. We believe there have been no material changes to our critical accounting policies and estimates during the nine months ended March 27, 2005 compared to those discussed in our Annual Report on Form 10-K for the year ended June 27, 2004.

Share-Based Payment

On December 16, 2004, the Financial Accounting Standards Board (“FASB”) issued SFAS 123 (revised 2004), *Share-Based Payment* (“SFAS 123(R)”), which is a revision of SFAS 123. SFAS 123(R) supersedes APB 25 and amends FASB SFAS 95, *Statement of Cash Flows*. Generally, the approach in SFAS 123(R) is similar to the approach described in SFAS 123. However, SFAS 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the statement of operations based on their fair values. Pro forma disclosure is no longer an alternative. We expect to adopt SFAS 123(R) at the beginning of our first quarter of fiscal 2006.

SFAS 123(R) permits public companies to adopt its requirements using one of two methods: 1) a “modified prospective” method in which compensation cost is recognized beginning with the effective date (a) based on the requirements of SFAS 123(R) for all share-based payments granted after the effective date and (b) based on the requirements of SFAS 123 for all awards granted to employees prior to the effective date of SFAS 123(R) that remain unvested on the effective date. 2) a “modified retrospective” method which includes the requirements of the modified prospective method described above, but also permits entities to restate based on the amounts previously recognized under SFAS 123 for purposes of pro forma disclosures either (a) all prior periods presented or (b) prior interim periods of the year of adoption. We plan to adopt SFAS 123 using the modified-prospective method.

We are currently evaluating the requirements of SFAS 123(R) and we have not yet fully determined the impact on our consolidated financial statements. We believe the impact to our financial statements will result in a material increase in our stock-based employee compensation expense recognized in our consolidated statements of operations, although it will have no impact on our overall financial position. The stock-based employee compensation expense presented in our pro forma financial results required to be disclosed under SFAS 123 was $4.3 million and $16.5 million in the three and nine month periods ended March 27, 2005. Additionally, SFAS 123(R) also requires the benefits of tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as an operating cash flow as required under current literature. This requirement will reduce net operating cash flows and increase net financing cash flows in periods after adoption.

Identification of Impaired Investments

In March 2004, the FASB approved the consensus reached on EITF Issue No. 03-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments* (“EITF 03-1”). EITF 03-1 provides new guidance for evaluating impairment losses on debt and equity investments, as well as new disclosure requirements for investments that are determined to be other-than-temporarily impaired. In September 2004, the FASB approved the issuance of a FASB Staff Position to delay the requirement to record impairment losses under EITF 03-1. The approved delay applies to all securities within the scope of EITF 03-1 and is expected to end when new guidance is issued and comes into effect. As substantially all of our investments are investment grade government and corporate debt securities that have maturities of less than 3 years, and we have both the ability and intent to hold the investments until maturity, we do not expect EITF 03-1, if and when the requirement to record impairment losses becomes effective, to have a material impact on our financial position and results of operations.

Inventory Costs

In November 2004, the FASB issued SFAS 151, *Inventory Costs – an amendment of ARB No. 43, Chapter 4*, which requires companies to expense abnormal freight, handling costs, or spoilage in the period incurred and to allocate fixed overhead based on normal capacity, with adjustment if production is abnormally high. This standard becomes effective on July 1, 2005. We currently account for abnormal freight, handling costs, and spoilage consistent with this standard. We plan to adopt the provisions on a prospective basis in the first fiscal quarter of 2006. We are currently evaluating the effects of implementing this standard, however we do not expect it to have a material impact on our financial position and results of operations.

Liquidity and Capital Resources

Cash and cash equivalents, short-term investments and marketable securities increased to $443.3 million at March 27, 2005 from $425.7 million at June 27, 2004, an increase of $17.6 million. This increase was primarily due to cash provided by operating activities of $20.1 million and proceeds from issuance of common stock of $4.3 million, partially offset by capital expenditures of $4.6 million.

We generated $20.1 million in cash from operations in the first nine months of fiscal 2005. Accounts receivable decreased to $31.6 million at March 27, 2005 from $33.0 million at June 27, 2004. Days sales outstanding (“DSO”) in receivables decreased to 32 days at March 27, 2005 from 33 days at June 27, 2004. The decrease in our accounts receivable balance, as well as the decrease in DSO, was primarily due to shipment linearity and improvements in collecting past due balances. Inventory levels decreased to $22.1 million at March 27, 2005 from $25.9 million at June 27, 2004 as a result of shipment linearity where we experienced a higher shipment volume in the last four weeks of the third quarter of fiscal 2005 as compared to the fourth quarter of fiscal 2004. Inventory management remains an area of focus as we balance the need to maintain strategic inventory levels to ensure competitive lead times and avoid stock-outs with the risk of excess inventory or obsolescence.

We have a revolving line of credit for $10.0 million with a major lending institution. Borrowings under this line of credit bear interest at the bank's prime rate, which was 5.75% at March 27, 2005. As of March 27, 2005, there were no outstanding borrowings under this line of credit. The line of credit contains a provision for the issuance of letters of credit not to exceed the unused balance of the line. As of March 27, 2005, we had letters of credit totaling $0.8 million. These letters of credit were primarily issued to satisfy requirements of certain of our customers for performance bonds. The line of credit requires us to maintain specified financial covenants related to tangible net worth and liquidity, with which we were in compliance as of March 27, 2005. The line of credit expires on January 26, 2006. It is our intention to renew this line of credit when it expires.

As part of our business relationship with MCMS, Inc. ("MCMS"), the predecessor-in-interest to Plexus Corp., we entered into a $9.0 million operating equipment lease for manufacturing equipment in September 2000 with a third-party financing company; we, in turn, subleased the equipment to MCMS. During the first quarter of fiscal 2002, due to the liquidity problems at MCMS and its voluntary filing for protection under Chapter 11, we recorded a charge of $9.0 million related to this lease. The liability, net of payments, related to this lease is included in lease liability on the condensed consolidated balance sheets. The equipment lease with the third-party financing company requires us to make monthly payments through September 2005 and to maintain specified financial covenants related to profitability and our cash to debt ratio with which we were not in compliance as March 27, 2005. As of March 31, 2005, we obtained a waiver from the third-party financing company, which allowed the lease to remain in effect.

In December 2001, we completed a private placement of $200.0 million of convertible subordinated notes. The notes mature on December 1, 2006. Interest is payable semi-annually at 3.5% per annum. The notes are convertible at the option of the holders into our common stock at an initial conversion price of $20.96 per share, subject to adjustment. The notes are redeemable in cash at our option at an initial redemption price of 101.4% of the principal amount on or after December 1, 2004 through November 30, 2005, and at a redemption price of 100.7% of the principal amount on or after December 1, 2005 through November 30, 2006, if not converted to common stock prior to the redemption date. Each holder of the notes has the right to cause us to repurchase all of such holder's convertible notes at 100% of the principal amount plus accrued interest upon a change of control of ownership of us, as defined in the offering circular.

The following summarizes our contractual obligations (including interest payments) at March 27, 2005, and the effect such obligations are expected to have on our liquidity and cash flow in future periods (in thousands):

	Total	Less Than 1 Year	1 – 3 Years	3 – 5 Years	After Five Years
Contractual Obligations:					
Convertible subordinated notes	$214,000	$ 7,000	$207,000	$ —	$ —
Non-cancelable inventory purchase commitments	24,182	24,182	—	—	—
Non-cancelable operating lease obligations	29,138	8,381	11,640	5,491	3,625
Other commitments	7,500	4,000	3,000	500	
Total contractual obligations	$274,820	$ 43,564	$221,640	$5,991	$ 3,625

We did not have any material commitments for capital expenditures or other non-cancelable purchase commitments not included above as of March 27, 2005. Other commitments include multiple technology agreements. We did not have any off-balance sheet financing arrangements as of March 27, 2005.

We require substantial capital to fund our business, particularly to finance inventories and accounts receivable and for capital expenditures. As a result, we could be required to raise substantial additional capital at any time. To the extent that we raise additional capital through the sale of equity or convertible debt securities, the issuance of such securities could result in dilution to existing stockholders. If additional funds are raised through the issuance of debt securities, these securities may have rights, preferences and privileges senior to holders of common stock and the terms of such debt could impose restrictions on our operations. If we are unable to obtain such additional capital, we may be required to reduce the scope of our planned product development and marketing efforts, which would materially adversely affect our business, financial condition and operating results.

We believe that our current cash and cash equivalents, short-term investments, marketable securities and cash available from credit facilities and future operations will enable us to meet our working capital requirements for at least the next 12 months.

Risk Factors

We Cannot Assure You That We Will Be Profitable in the Future

While we have reported a profit for the nine months ended March 27, 2005, we were not profitable in the current quarter. Fiscal 2000 was the only year in which we have achieved profitability for the full year. We reported losses for fiscal 2004, fiscal 2003, and fiscal 2002. We anticipate continuing to incur significant sales and marketing, product development and general and administrative expenses and, as a result, we will continue to need to rationalize expense levels and increase revenue levels to return to profitability in future fiscal quarters.

A Number of Factors Could Cause Our Quarterly Financial Results to Be Worse Than Expected, Resulting in a Decline in Our Stock Price

Our ability to control our operating expenses at a level that is consistent with anticipated revenue is significant to our financial results. A high percentage of our expenses are fixed in the short term, so any delay in generating or recognizing revenue could cause our quarterly operating results to fall below the expectations of public market analysts or investors, which could cause the price of our stock to fall, as occurred upon our announcement of the results for the third quarter of fiscal 2005.

Orders in our backlog at the beginning of each quarter do not equal expected revenue for that quarter and are generally cancelable at any time. Accordingly, we are dependent upon obtaining orders during a quarter and shipping those orders in the same quarter to achieve our revenue objectives. In addition, the timing of product releases and purchase orders, and product availability, often results in a majority of our product shipments being scheduled near the end of a quarter. Failure to ship these products by the end of a quarter may adversely affect our operating results. Our customer agreements generally allow customers to delay scheduled delivery dates or to cancel orders within specified timeframes without significant charges to the customers. Furthermore, some of our customers require that we provide installation or inspection services that may delay the recognition of revenue for both products and services, and some of our customer agreements include acceptance provisions that prevent our ability to recognize revenue upon shipment.

We may experience a delay in generating or recognizing revenue for a number of reasons and our quarterly revenue and operating results have varied significantly in the past and may vary significantly in the future due to a number of factors, including, but not limited to, the following:

- changes in general and/or specific economic conditions in the networking industry;
- seasonal fluctuations in demand for our products and services, particularly in Asia-Pacific and Europe;
- linearity of quarterly sales have historically reflected a pattern in which a disproportionate percentage of such sales occur in the last month of the quarter;
- reduced visibility into the implementation cycles for our products and our customers' spending plans;
- our ability to accurately forecast demand for our products, which in the case of lower-than-expected sales, may result in excess or obsolete inventory in addition to non-cancelable purchase commitments for component parts;
- product returns or the cancellation or rescheduling of orders;
- our ability to develop, introduce, ship and support new products and product enhancements and manage product transitions;
- announcements and new product introductions by our competitors;
- our ability to develop and support relationships with enterprise customers, service providers and other potential large customers;
- our ability to achieve targeted cost reductions;
- our ability to obtain sufficient supplies of sole- or limited-source components for our products on a timely basis;
- increases in the prices of the components that we purchase;
- decreases in the prices of the products that we sell;
- our ability to achieve and maintain desired production volumes and quality levels for our products;
- the mix of products sold and the mix of distribution channels through which products are sold;
- downward adjustments resulting from other-than-temporary declines in the carrying value of long-lived assets;
- costs associated with adjustments to the size of our operations;
- costs relating to possible acquisitions and the integration of technologies or businesses; and
- the effect of amortization of deferred compensation and purchased intangibles resulting from existing or new transactions.

In the third quarter of fiscal 2005 we, and a number of our competitors, reported revenues below expectations. Our results were particularly impacted by lower sales in Japan compared to the prior quarter, offset in part by increased service revenue and increased product revenue in North America and Europe and the Middle East. We believe that revenues will increase in coming quarters, however our future results could be adversely affected if longer term economic or industry trends are unfavorable.

Due to the foregoing factors, we believe that period-to-period comparisons of our operating results should not be relied upon as an indicator of our future performance.

Intense Competition in the Market for Networking Equipment Could Prevent Us from Increasing Revenue and Returning to Profitability on a Fiscal Year Basis

The market for networking equipment is intensely competitive. Our principal competitors include Cisco Systems, Enterasys Networks, Foundry Networks, Inc., Nortel Networks and 3Com Corporation. In addition, a number of private companies and foreign competitors have announced plans for new products, or have introduced products, that may compete with our own products. Some of our current and potential competitors have superior market leverage, longer operating histories and substantially greater financial, technical, sales and marketing resources, in addition to wider name recognition and larger installed customer bases. Foreign competitors may have competitive advantages due to significantly lower costs or strong ties to customers in their home countries. These competitors may have developed, or may in the future develop, new competing products based on technologies that compete with our own products or render our products obsolete. Furthermore, a number of these competitors may merge or form strategic partnerships that enable them to offer or bring to market competitive products. Consolidation within our industry could lead to increased competition and could harm our operating results.

The pricing policies of our competitors impact the overall demand for our products and services. Some of our competitors are capable of operating at significant losses, or reducing margins on competitive products, for extended periods of time, increasing pricing pressure on our products and services. If we do not maintain competitive pricing, the demand for our products and services, as well as our market share, may decline. From time to time, we may lower the prices of our products and services. When this happens, if we are unable to reduce our component costs or improve operating efficiencies, our revenues and margins are adversely affected.

To remain competitive, we believe that we must, among other things, invest significant resources in developing new products, improve our current products and maintain customer satisfaction. Such investment will increase our expenses and affect our profitability. In addition, if we fail to make this investment, we may not be able to compete successfully with our competitors, which could have a material adverse effect on our revenue and future profitability.

When Our Products Contain Undetected Errors, We Incur Significant Unexpected Expenses and Could Lose Sales

Network products frequently contain undetected errors when new products or new versions or updates of existing products are released to the marketplace. In the past, we have experienced such errors in connection with new products and product updates. We have experienced component problems that caused us to incur higher than expected warranty and service costs and expenses, and to take an accrual for anticipated expenses. In the future, we expect that, from time to time, such errors or component failures will be found in new or existing products after the commencement of commercial shipments. These problems have adversely affected our business and may have a material adverse effect on our business by causing us to incur significant warranty and repair costs, diverting the attention of our engineering personnel from new product development efforts, delaying the recognition of revenue and causing significant customer relations problems. Further, if products are not accepted by customers due to such defects, and such returns exceed the amount we accrued for defect returns based on our historical experience, our operating results would be adversely affected.

Our products must successfully interoperate with products from other vendors. As a result, when problems occur in a network, it may be difficult to identify the sources of these problems. The occurrence of errors, whether or not caused by our products, could result in the delay or loss of market acceptance of our products and any necessary revisions may cause us to incur significant expenses. The occurrence of any such problems would likely have a material adverse effect on our business, operating results and financial condition.

We Depend Upon International Sales for a Significant Portion of Our Revenue and Our Ability to Grow Our International Sales Depends on Successfully Expanding Our International Operations

International sales constitute a significant portion of our net revenues. Our ability to grow will depend in part on the continued expansion of international sales. Sales to customers outside of the United States accounted for approximately 57% and 62% of our net revenues, respectively, for the first nine months of fiscal 2005 and fiscal 2004. Our international sales primarily depend on the success of our resellers and distributors. The failure of these resellers and distributors to sell our products internationally would limit our ability to sustain and grow our revenue. We have recently experienced a significant decline in revenue in our Japan market due to a decline in business with service provider customer segment. There are a number of risks arising from our international business, including:

- longer accounts receivable collection cycles;
- difficulties in managing operations across disparate geographic areas;
- difficulties associated with enforcing agreements through foreign legal systems;
- the payment of operating expenses in local currencies, which exposes us to risks of currency fluctuations;
- higher credit risks requiring cash in advance or letters or credit;
- difficulty in safeguarding intellectual property;
- political and economic turbulence;
- potential adverse tax consequences; and
- unexpected changes in regulatory requirements, including compliance with U.S. and foreign export laws and regulations.

In addition, conducting our business on a global basis subjects us to a number of frequently changing and complex trade protection measures and import or export regulatory requirements. Our failure to comply with these measures and regulatory requirements may result in the imposition of financial penalties and restrictions on our ability to conduct business in and with certain countries, which may harm our business and damage our reputation. Pursuant to regulations of the U.S. Department of Commerce providing for voluntary disclosure, in the fourth quarter of fiscal 2002 we disclosed information regarding a possible violation of certain export regulations. The Department of Commerce has completed an investigation of these transactions, but has not yet advised us of the action, if any, that it proposes to take in this matter. The company intends to work with the Department to resolve the matter. While it is possible that the Department will seek civil penalties and/or other administrative sanctions, we believe that these matters will be resolved without a material adverse affect on our business. We have also implemented procedures to reduce the risk of violations in the future.

Our international sales currently are U.S. dollar-denominated. Recently the U.S. dollar exchange rate has fallen against foreign currencies, in particular the Euro. However, future increases in the value of the U.S. dollar relative to foreign currencies could make our products less competitive in international markets. In the future, we may elect to invoice some of our international customers in local currency which will expose us to fluctuations in exchange rates between the U.S. dollar and the particular local currency. If we do so, we may decide to engage in hedging transactions to minimize the risk of such fluctuations.

We have entered into foreign exchange forward contracts to offset the impact of payment of operating expenses in local currencies to some of our operating foreign subsidiaries. However, if we are not successful in managing these hedging transactions, we could incur losses from hedging activities, or could incur higher than expected expenses from operations that are not covered by a forward contract.

We Expect the Average Selling Prices of Our Products to Decrease, Which May Reduce Gross Margin and/or Revenue

The network equipment industry has traditionally experienced a rapid erosion of average selling prices due to a number of factors, including competitive pricing pressures, promotional pricing and technological progress. We anticipate that the average selling prices of our products will decrease in the future in response to competitive pricing pressures, excess inventories, increased sales discounts and new product introductions by us or our competitors, including, for example, competitive products manufactured with low-cost merchant silicon. We may experience substantial decreases in future operating results due to the erosion of our average selling prices. Competitive pressures increased as a result of the industry slowdown that began in the first half of 2001, and pressures could increase further as a result of lower than expected revenues in the third quarter of fiscal 2005, and a potential slow-down in the broader economy. To maintain our gross margin, we must develop and introduce on a timely basis new products and product enhancements and continually reduce our product costs.

Our failure to do so would likely cause our revenue and gross margins to decline, which could have a material adverse effect on our operating results and cause the price of our common stock to decline.

Some of Our Customers May Not Have the Resources to Pay for Our Products as a Result of the Current Economic Environment

At March 27, 2005, one customer, Algol Deutschland, accounted for greater than 10% of our accounts receivable balance. Some of our customers are likely to experience serious cash flow problems and, as a result, may find it increasingly difficult to obtain financing, if financing is available at all. If our customers are not successful in generating sufficient revenue or securing alternate financing arrangements, they may not be able to pay, or may delay payment of, the amounts that they owe us. In particular, sales to the service provider market are especially volatile and continued declines or delays in sale orders from this market may harm our financial condition. Furthermore, they may not order as many products from us as originally forecast, or cancel orders with us entirely. The inability of some of our potential customers to pay us for our products may adversely affect our cash flow, the timing of our revenue recognition and the amount of revenue, which may cause our stock price to decline.

The Market in Which We Compete is Subject to Rapid Technological Progress and to Compete We Must Continually Introduce New Products that Achieve Broad Market Acceptance

The network equipment market is characterized by rapid technological progress, frequent new product introductions, changes in customer requirements and evolving industry standards. If we do not regularly introduce new products in this dynamic environment, our product lines will become obsolete. Developments in routers and routing software could also significantly reduce demand for our products. Alternative technologies could achieve widespread market acceptance and displace the Ethernet technology on which we have based our product architecture. We cannot assure you that our technological approach will achieve broad market acceptance or that other technologies or devices will not supplant our own products and technology.

When we announce new products or product enhancements that have the potential to replace or shorten the life cycle of our existing products, customers may defer or cancel orders for our existing products. These actions could have a material adverse effect on our operating results by unexpectedly decreasing sales, increasing inventory levels of older products and exposing us to greater risk of product obsolescence. The market for switching products is evolving and we believe our ability to compete successfully in this market is dependent upon the continued compatibility and interoperability of our products with products and architectures offered by other vendors.

In particular, the networking industry has been characterized by the successive introduction of new technologies or standards that have dramatically reduced the price and increased the performance of switching equipment. To remain competitive, we need to introduce products in a timely manner that incorporate, or are compatible with, these emerging technologies. We are particularly dependent upon the successful introduction of new products. We cannot ensure that any new products we introduce will be commercially successful. We have experienced delays in releasing new products and product enhancements in the past that resulted in lower quarterly revenue than anticipated. We may experience similar delays in product development and releases in the future, and any delay in product introduction could adversely affect our ability to compete, causing our operating results to be below our expectations or the expectations of public market analysts or investors.

Our Limited Ability to Protect Our Intellectual Property May Adversely Affect Our Ability to Compete

We rely on a combination of patent, copyright, trademark and trade secret laws and restrictions on disclosure to protect our intellectual property rights. However, we cannot ensure that the actions we have taken will adequately protect our intellectual property rights or that other parties will not independently develop similar or competing products that do not infringe on our patents. We generally enter into confidentiality or license agreements with our employees, consultants and corporate partners, and control access to and distribution of our products, documentation and other proprietary information. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy or otherwise misappropriate or use our products or technology, which would adversely affect our ability to compete.

Claims of Infringement by Others May Increase and the Resolution of Such Claims May Adversely Affect our Ability to Compete and Our Operating Results

Our industry is characterized by the existence of a large number of patents and frequent claims and related litigation regarding patent and other intellectual property rights. Because of the existence of a large number of patents in the networking field, the secrecy of some pending patents and the issuance of new patents as a rapid pace, it is not possible to determine in advance if a product or component might infringe the patent rights of others. Because of the potential for courts awarding substantial damages and the lack of predictability of such awards, it is not uncommon for companies in our and similar industries to settle even potentially unmeritorious claims with very substantial amounts. We expect to increasingly be subject to infringement claims asserted by third parties as the numbers of products and competitors in the market for network switches grow and product functionality overlaps.

We are actively involved in disputes and licensing discussions with, and have received notices from, others regarding their claimed proprietary rights, and as the functionality and features of our products expands, these disputes and discussions could increase or become harder to resolve. The corporations with whom we have or could have disputes or discussions include corporations with extensive patent portfolios and substantial financial assets who are actively engaged in programs to generate substantial revenues from their patent portfolios, and who are seeking or may seek significant payments or royalties from us and others in our industry. We cannot ensure that we will always be able successfully to defend ourselves against such claims or conclude licensing discussions on favorable terms. If we are found to infringe the proprietary rights of others, or if we otherwise settle such claims or enter into licensing arrangements to resolve potential disputes, we could be compelled to pay damages, royalties or other payments and either obtain a license to those intellectual property rights or alter our products so that they no longer infringe upon such proprietary rights. Any license could be very expensive to obtain or may not be available at all. Similarly, changing our products or processes to avoid infringing the rights of others may be costly or impractical. Litigation, licensing discussions or settlement negotiations resulting from claims that we are infringing the proprietary rights of others has resulted and could in the future result in substantial costs and a diversion of resources, and could have a material adverse effect on our business, financial condition and results of operations, in any particular period, or on an ongoing basis. Due to the number of companies with extensive patent portfolios in our industry who are or may be actively involved in licensing programs, we believe that even if we do not infringe any patents, we will incur significant expenses in the future due to disputes or licensing negotiations, though the amounts can not be determined. We cannot assure you that any such expenses will not be material or otherwise adversely affect our operating results.

We Are Engaged in Litigation Regarding Intellectual Property Rights, and an Adverse Outcome Could Harm Our Business and Require Us to Incur Significant Costs

We have received notice from several companies alleging that we may be infringing their patents. One of these companies, Lucent Technologies, Inc., filed a claim against us alleging patent infringement, and we are in litigation as of the date of this filing. A trial date has been set for April 26, 2005. Following examination of this claim, we believe it is without merit and we have responded accordingly. Without regard to the merits of this or any other claim, if judgments by a court of law on this or any other claim received in the future were to be upheld, or if we were otherwise to agree to the settlement of such claims, the consequences to us may be severe and could require us, among other actions to:

- stop selling our products that incorporate the challenged intellectual property;
- obtain a royalty bearing license to sell or use the relevant technology, which license may not be available on reasonable terms or available at all;
- pay damages; or
- redesign those products that use the disputed technology.

If we are compelled to take any of the foregoing actions, our business could be severely harmed.

Adjustments to the Size of Our Operations May Require Us to Incur Unanticipated Costs

Prior to the quarter ended April 1, 2001, we experienced rapid growth and expansion that placed a significant strain on our resources. Subsequent to that period, we have from time to time incurred unanticipated costs to downsize our operations to a level consistent with lower forecast sales. Even if we manage the current period of instability effectively, as well as possible expansion in the future, we may make mistakes in restructuring or operating our business, such as inaccurate sales forecasting or incorrect material planning. Any of these mistakes may lead to unanticipated fluctuations in our operating results. We cannot assure you that we will be able to size our operations in accordance with fluctuations of our business in the future.

We Must Continue to Develop and Increase the Productivity of Our Indirect Distribution Channels to Increase Net Revenues and Improve Our Operating Results

Our distribution strategy focuses primarily on developing and increasing the productivity of our indirect distribution channels. If we fail to develop and cultivate relationships with significant resellers, or if these resellers are not successful in their sales efforts, sales of our products may decrease and our operating results could suffer. Many of our resellers also sell products from other vendors that compete with our products. We cannot assure you that we will be able to enter into additional reseller and/or distribution agreements or that we will be able to successfully manage our product sales channels. Our failure to do any of these could limit our ability to grow or sustain revenue. In addition, our operating results will likely fluctuate significantly depending on the timing and amount of orders from our resellers. We cannot assure you that our resellers and/or distributors will continue to market or sell our products effectively or continue to devote the resources necessary to provide us with effective sales, marketing and technical support.

Most of Our Revenue is Derived From Sales of Three Product Families, So We are Dependent on Widespread Market Acceptance of These Products

We derive substantially all of our revenue from sales of our Summit, BlackDiamond and Alpine products and related services. We expect that revenue from these product families will account for a substantial portion of our revenue for the foreseeable future. Accordingly, widespread market acceptance of our product families is vital to our future success. Factors that may affect the sales of our products, some of which are beyond our control, include:

- the demand for switching products (Gigabit Ethernet and Layer 3 switching technologies in particular) in the enterprise and service provider markets;
- the performance, price and total cost of ownership of our products;
- the availability and price of competing products and technologies;
- our ability to match supply with demand for certain products; and
- the success and development of our resellers, distributors and field sales channels.

We may not be able to achieve widespread market acceptance of our product families, which could reduce our revenue.

Our Future Performance Will Depend on the Introduction and Acceptance of New Products

Our future performance will also depend on the successful development, introduction, and market acceptance of new and enhanced products that address customer requirements in a timely and cost-effective manner. In the past, we have experienced delays in product development and such delays may occur in the future. The introduction of new and enhanced products may cause our customers to defer or cancel orders for existing products. Therefore, to the extent customers defer or cancel orders in the expectation of new product releases, any delay in the development or introduction of new products could cause our operating results to suffer. The inability to achieve and maintain widespread levels of market acceptance for our current and future products may significantly impair our revenue growth.

If a Key Reseller, Distributor, or Other Significant Customer Cancels or Delays a Large Purchase, Our Net Revenues May Decline and the Price of Our Stock May Fall

To date, a limited number of resellers, distributors and other customers have accounted for a significant portion of our revenue. None of our customers accounted for greater than 10% of our revenues for the third quarter of fiscal 2005 or fiscal 2004. None of our customers accounted for 10% of our net revenues for the first nine months of fiscal 2005 or fiscal 2004. If any of our large customers stop or delay purchases, our revenue and profitability would be adversely affected.

Our expense levels are based on our expectations as to future revenue and to a large extent are fixed in the short term, so a substantial reduction or delay in sales of our products to a significant reseller, distributor or other customer could harm our business, operating results and financial condition. Although our largest customers may differ from period-to-period, we anticipate that our operating results for any given period will continue to depend to a significant extent on large orders from a relatively small number of customers.

While our financial performance depends on large orders from a limited number of key resellers, distributors and other significant customers, we do not have binding purchase commitments from any of them. For example:

- our service providers and enterprise customers can stop purchasing, and our resellers and distributors can stop marketing, our products at any time;
- our reseller agreements are non-exclusive and are for one-year terms, with no obligation upon the resellers to renew the agreements; and
- our reseller, distributor and end-user customer agreements generally do not require minimum purchases.

Under specified conditions, some third-party distributors are allowed to return products to us. We do not recognize revenue on sales to distributors until the distributors sell the product to their customers.

The Sales Cycle for Our Products is Long and We May Incur Substantial Non-Recoverable Expenses or Devote Significant Resources to Sales that Do Not Occur When Anticipated

The use of indirect sales channels may contribute to the length and variability of our sales cycle. Our products represent a significant strategic decision by a customer regarding its communications infrastructure. The decision by customers to purchase our products is often based on the results of a variety of internal procedures associated with the evaluation, testing, implementation and acceptance of new technologies. Accordingly, the product evaluation process frequently results in a lengthy sales cycle, typically ranging from three months to longer than a year, and as a result, our ability to sell products is subject to a number of significant risks, including:

- the risk that budgetary constraints and internal acceptance reviews by customers will result in the loss of potential sales;
- the risk of substantial variation in the length of the sales cycle from customer to customer, making decisions on the expenditure of resources difficult to assess;
- the risk that we may incur substantial sales and marketing expenses and expend significant management time in an attempt to initiate or increase the sale of products to customers, but not succeed;
- the risk that, if a sales forecast from a specific customer for a particular quarter is not achieved in that quarter, we may be unable to compensate for the shortfall, which could harm our operating results; and
- the risk that downward pricing pressures could occur during this lengthy sales cycle.

We Purchase Several Key Components for Products From Single or Limited Sources and Could Lose Sales if These Suppliers Fail to Meet Our Needs

We currently purchase several key components used in the manufacture of our products from single or limited sources and are dependent upon supply from these sources to meet our needs. Certain components such as tantalum capacitors, static random access memory, or SRAM, dynamic random access memory, or DRAM, and printed circuit boards, have been in the past, and may in the future be, in short supply. We have encountered, and are likely in the future to encounter, shortages and delays in obtaining these or other components, and this could have a material adverse effect on our ability to meet customer orders. Our principal sole-source components include:

- ASICs;
- microprocessors;
- programmable integrated circuits;
- selected other integrated circuits;
- custom power supplies; and
- custom-tooled sheet metal.

Our principal limited-source components include:

- flash memories;
- DRAMs and SRAMs; and
- printed circuit boards.

We use our forecast of expected demand to determine our material requirements. Lead times for materials and components we order vary significantly, and depend on factors such as the specific supplier, contract terms and demand for a component at a given time. If forecasts exceed orders, we may have excess and/or obsolete inventory on hand or under non-cancelable purchase commitments that could have a material adverse effect on our operating results and financial condition. If orders exceed forecasts, we may have inadequate supplies of certain materials and components, which could have a material adverse effect on our operating results and financial condition. We do not have agreements fixing long-term prices or minimum volume requirements from suppliers. From time to time we have experienced shortages and allocations of certain components, resulting in delays in filling orders. Qualifying new suppliers to compensate for such shortages may be time-consuming and costly, and may increase the likelihood of errors in design or production. In addition, during the development of our products, we have experienced delays in the prototyping of our chipsets, which in turn has led to delays in product introductions. We cannot ensure that similar delays will not occur in the future. Furthermore, we cannot ensure that the performance of the components as incorporated in our products will meet the quality requirements of our customers.

Our Dependence on One Contract Manufacturer for All of Our Manufacturing Requirements Could Harm Our Operating Results

If the demand for our products grows, we will need to increase our material purchases, contract manufacturing capacity, and internal test and quality functions. Any disruptions in product flow could limit our revenue, adversely affect our competitive position and reputation, and result in additional costs or cancellation of orders under agreements with our customers.

We rely on an independent contractor to manufacture our products. The sole company we currently utilize for the manufacture of our products is Flextronics International, Ltd., located in San Jose, California and Guadalajara, Mexico. Our commitment with Flextronics is formalized through a one-year contract. We have experienced delays in product shipments from contract manufacturers in the past, which in turn delayed product shipments to our customers. These or similar problems may arise in the future, such as products of inferior quality, insufficient quantity of products, or the interruption or discontinuance of operations of a manufacturer, any of which could have a material adverse effect on our business and operating results.

We do not know whether we will effectively manage our contract manufacturer or that this manufacturer will meet our future requirements for timely delivery of products of sufficient quality and quantity. We intend to introduce new products and product enhancements, which will require that we rapidly achieve volume production by coordinating our efforts with those of our suppliers and contract manufacturer. The inability of our contract manufacturer to provide us with adequate supplies of high-quality products may cause a delay in our ability to fulfill orders and may have a material adverse effect on our business, operating results and financial condition. Moreover, our current dependence on a single manufacturer makes us particularly vulnerable to these risks.

As part of our cost-reduction efforts, we will need to realize lower per unit product costs from our contract manufacturer by means of volume efficiencies and the utilization of manufacturing sites in lower-cost geographies. However, we cannot be certain when or if such price reductions will occur. The failure to obtain such price reductions would adversely affect our gross margins and operating results.

If We Do Not Adequately Manage and Evolve Our Financial Reporting and Managerial Systems and Processes, Our Ability to Manage and Grow Our Business May Be Harmed

Our ability to successfully implement our business plan and comply with regulations requires an effective planning and management process. We need to continue improving our existing, and implement new, operational and financial systems, procedures and controls. Any delay in the implementation of, or disruption in the transition to, new or enhanced systems, procedures or controls, could harm our ability to record and report financial and management information on a timely and accurate basis, or to forecast future results. In addition, rules adopted by the Securities and Exchange Commission pursuant to Section 404 of the Sarbanes-Oxley Act of 2002 require an annual review and evaluation of our internal control over financial reporting, and an annual audit of our internal control over financial reporting by our independent registered public accounting firm. We are currently undergoing a review of our internal control systems and procedures and implementing improvements that will be necessary in order for us to comply with the requirements of Section 404 by the end of fiscal 2005. This process has required and will continue to require us to hire additional personnel and retain outside advisory services and has resulted and will continue to result in additional accounting and legal expenses, which has and may continue to cause our operating expenses to increase.

If We Are Unable To Favorably Assess The Effectiveness Of Our Internal Control Over Financial Reporting, or If Our Independent Registered Public Accounting Firm Is Unable To Provide An Unqualified Attestation Report On Our Assessment, Our Stock Price Could Be Adversely Affected.

Pursuant to Section 404 of the Sarbanes-Oxley Act of 2002 and beginning with our Annual Report on Form 10-K for the fiscal year ending July 3, 2005, our management will be required to report on, and our independent registered public accounting firm to attest to, the effectiveness of our internal control over financial reporting as of the end of fiscal 2005. The rules governing the standards that must be met for management to assess our internal control over financial reporting are new and complex, and require significant documentation, testing and possible remediation. While we are in the process of reviewing, documenting and testing our internal control over financial reporting, we may encounter problems or delays in completing the implementation of any changes necessary to make a favorable assessment of our internal control over financial reporting. In addition, in connection with the attestation process by our independent registered public accounting firm, we may encounter problems or delays in completing the implementation of any requested improvements and receiving a favorable attestation. If we cannot favorably assess the effectiveness of our internal control over financial reporting, or if our independent registered public accounting firm is unable to provide an unqualified attestation report on our assessment, investor confidence and our stock price could be adversely affected.

Future Changes in Financial Accounting Standards May Cause Adverse Unexpected Revenue Fluctuations and Affect Our Reported Results of Operations

A change in accounting policies can have a significant effect on our reported results and may even affect our reporting of transactions completed before the change is effective. New pronouncements and varying interpretations of pronouncements have occurred with frequency and are likely to occur in the future. Changes to existing rules or the questioning of current practices may adversely affect our reported financial results or the way we conduct our business.

In particular, in December 2004 the Financial Accounting Standards Board issued a statement requiring companies to record stock option grants as compensation expense on their income statements. This statement is effective beginning with our first quarter of fiscal 2006. The current methodology for expensing such stock options is based on, among other things, the historical volatility of the underlying stock. Our stock price has been historically volatile. Therefore, the adoption of this accounting standard will negatively impact our profitability and may adversely impact our stock price. In addition, the adoption of this standard could limit our ability to continue to use stock options as an incentive and retention tool, which could, in turn, hurt our ability to recruit employees and retain existing employees.

In addition, various accounting rules and regulations have been established over the recent past relating to revenue recognition. These regulations frequently require judgments in their application, and are subject to numerous subsequent clarifications and interpretations, some of which may require changes in the way we recognize revenue and may require restatement of prior period revenue and results, either of which could adversely affect our reported results.

Our Business Substantially Depends Upon the Continued Growth of the Internet and Internet-Based Systems

A substantial portion of our business and revenue depends on growth of the Internet and on the deployment of our products by customers that depend on the continued growth of the Internet. As a result of the recent economic slowdown and reduction in capital spending, which have particularly affected telecommunications service providers, spending on Internet infrastructure has declined, which has materially harmed our business. To the extent that the recent economic slowdown and reduction in capital spending continue to adversely affect spending on Internet infrastructure, we could continue to experience material harm to our business, operating results, and financial condition.

Because of the rapid introduction of new products, and changing customer requirements related to matters such as cost-effectiveness and security, we believe that there could be certain performance problems with Internet communications in the future, which could receive a high degree of publicity and visibility. As we are a large supplier of networking products, our business, operating results, and financial condition may be materially adversely affected, regardless of whether or not these problems are due to the performance of our own products. Such an event could also result in a material adverse effect on the market price of our common stock independent of direct effects on our business.

Compliance with Changing Regulation of Corporate Governance and Public Disclosure May Result in Additional Expenses

Changing laws, regulations and standards relating to corporate governance and public disclosure, including the Sarbanes-Oxley Act of 2002, new SEC regulations and Nasdaq Stock Market rules, are creating uncertainty for companies such as ours. We are committed to maintaining high standards of corporate governance and public disclosure. As a result, we are investing all reasonably necessary resources to comply with evolving standards, and this investment has and may continue to result in increased general and administrative expenses and a diversion of management time and attention from revenue-generating activities to compliance activities.

We Have Been Named as a Defendant in a Shareholder Class Action Lawsuit Arising Out of Our Public Offerings of Securities in 1999

Beginning on July 6, 2001, purported securities fraud class action complaints were filed in the United States District Court for the Southern District of New York. The cases were consolidated and the litigation is now captioned as In re Extreme Networks, Inc. Initial Public Offering Securities Litigation, Civ. No. 01-6143 (SAS) (S.D.N.Y.), related to In re Initial Public Offering Securities Litigation, 21 MC 92 (SAS) (S.D.N.Y.).

The operative amended complaint is brought purportedly on behalf of all persons who purchased our common stock from April 8, 1999 through December 6, 2000. It names as defendants Extreme Networks; six of our present and former officers and/or directors, including our CEO (the "Extreme Networks Defendants"); and several investment banking firms that served as underwriters of our initial public offering and October 1999 secondary offering. Subsequently, plaintiffs and one of the individual defendants stipulated to a dismissal of that defendant without prejudice. The complaint alleges liability under Sections 11 and 15 of the Securities Act of 1933 and Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, on the grounds that the registration statement for the offerings did not disclose that: (1) the underwriters had agreed to allow certain customers to purchase shares in the offerings in exchange for excess commissions paid to the underwriters; and (2) the underwriters had arranged for certain customers to purchase additional shares in the aftermarket at predetermined prices. The Securities Act allegations against the Extreme Networks Defendants are made as to the secondary offering only. The amended complaint also alleges that false analyst reports were issued. No specific damages are claimed.

Similar allegations were made in other lawsuits challenging over 300 other initial public offerings and follow-on offerings conducted in 1999 and 2000. The cases were consolidated for pretrial purposes. On February 19, 2003, the Court ruled on all defendants' motions to dismiss. The Court denied the motions to dismiss the claims in our case under the Securities Act of 1933. The Court denied the motion to dismiss the claim under Section 10(a) of the Securities Exchange Act of 1934 against us and 184 other issuer defendants, on the basis that the complaints alleged that the respective issuers had acquired companies or conducted follow-on offerings after their initial public offerings. The Court denied the motion to dismiss the claims under Section 10(a) and 20(a) of the Securities Exchange Act of 1934 against the remaining Extreme Networks Defendants and 59 other individual defendants, on the basis that the respective amended complaints alleged that the individuals sold stock.

We have executed a settlement agreement presented to all issuer defendants. In this settlement, plaintiffs will dismiss and release all claims against the Extreme Network Defendants, in exchange for a contingent payment by the insurance companies collectively responsible for insuring the issuers in all of the IPO cases, and for the assignment or surrender of control of certain claims we may have against the underwriters. The Extreme Networks Defendants will not be required to make any cash payments in the settlement, unless the pro rata amount paid by the insurers in the settlement exceeds the amount of the insurance coverage, a circumstance which we do not believe will occur. The settlement will require approval of the Court, which cannot be assured. On February 15, 2005, the Court preliminarily approved the settlement except insofar as the settlement would have cut off contractual indemnification claims that underwriters may have against securities issuers, such as us. The Court has scheduled a hearing for January 9, 2006, to consider final approval of the settlement. If the settlement is not approved, we cannot assure you that we will prevail in the lawsuit. Failure to prevail could have a material adverse effect on our consolidated financial position, results of operations and cash flows in the future.

In addition, we may become subject to other types of litigation in the future. Litigation is often expensive and diverts management's attention and resources, which could materially and adversely affect our business.

Our Headquarters and Some Significant Supporting Businesses Are Located in Northern California and Other Areas Subject to Natural Disasters That Could Disrupt Our Operations and Harm Our Business

Our corporate headquarters are located in Silicon Valley in Northern California. Historically, this region has been vulnerable to natural disasters and other risks, such as earthquakes, fires and floods, which at times have disrupted the local economy and posed physical risks to our property. We have a contract manufacturer located in Northern California and in Mexico where similar natural disasters and other risks may disrupt the local economy and pose physical risks to our property and the property of our contract manufacturer.

In addition, terrorist acts or acts of war targeted at the United States, and specifically Silicon Valley, could cause damage or disruption to us, our employees, facilities, partners, suppliers, distributors and resellers, and customers, which could have a material adverse effect on our operations and financial results.

We currently do not have redundant, multiple site capacity in the event of a natural disaster or catastrophic event. In the event of such an occurrence, our business would suffer.

If We Lose Key Personnel or are Unable to Hire Additional Qualified Personnel as Necessary, We May Not Be Able to Successfully Manage Our Business or Achieve Our Goals

Our success depends to a significant degree upon the continued contributions of our key management, engineering, sales and marketing, service and operations personnel, many of whom would be difficult to replace. We do not have employment contracts with these individuals nor do we carry life insurance on any of our key personnel.

We believe our future success will also depend in large part upon our ability to attract and retain highly skilled managerial, engineering, sales and marketing, service, finance and operations personnel. The market for these personnel is competitive, especially in the San Francisco Bay Area, and we have had difficulty in hiring employees, particularly engineers, in the timeframe we desire. In addition, retention has become more difficult for us and other public technology companies as a result of the stock market decline, which caused the price of many of our employees' stock options to be above the current market price of our stock and we have recently experienced a high level of attrition, particularly in our sales personnel. There can be no assurance that we will be successful in attracting and retaining our key personnel. The loss of the services of any of our key personnel, the inability to attract or retain qualified personnel in the future or delays in hiring desired personnel, particularly engineers and sales personnel, could make it difficult for us to manage our business and meet key objectives, such as new product introductions. In addition, companies in the networking industry whose employees accept positions with competitors frequently claim that competitors have engaged in unfair hiring practices. We have from time to time been involved in claims like this with other companies and, although to date they have not resulted in material litigation, we do not know whether we will be involved in additional claims in the future as we seek to hire and retain qualified personnel or that such claims will not result in material litigation. We could incur substantial costs in litigating any such claims, regardless of the merits.

Failure of Our Products to Comply With Evolving Industry Standards and Complex Government Regulations May Cause Our Products to Not Be Widely Accepted, Which May Prevent Us From Growing Our Net Revenues or Achieving Profitability on a Fiscal Year Basis

The market for network equipment products is characterized by the need to support industry standards as different standards emerge, evolve and achieve acceptance. We will not be competitive unless we continually introduce new products and product enhancements that meet these emerging standards. In the past, we have introduced new products that were not compatible with certain technological standards, and in the future we may not be able to effectively address the compatibility and interoperability issues that arise as a result of technological changes and evolving industry standards. Our products must comply with various United States federal government regulations and standards defined by agencies such as the Federal Communications Commission, in addition to standards established by governmental authorities in various foreign countries and recommendations of the International Telecommunication Union. If we do not comply with existing or evolving industry standards or if we fail to obtain timely domestic or foreign regulatory approvals or certificates we will not be able to sell our products where these standards or regulations apply, which may prevent us from sustaining our net revenues or achieving profitability on a fiscal year basis.

Failure to Successfully Expand Our Sales and Support Teams or Educate Them In Regard to Technologies and Our Product Families May Harm Our Operating Results

The sale of our products and services requires a concerted effort that is frequently targeted at several levels within a prospective customer's organization. We may not be able to increase net revenues unless we expand our sales and support teams in order to address all of the customer requirements necessary to sell our products.

We cannot assure you that we will be able to successfully integrate employees into our company or to educate current and future employees in regard to rapidly evolving technologies and our product families. A failure to do so may hurt our revenue growth and operating results.

We May Engage in Future Acquisitions that Dilute the Ownership Interests of Our Stockholders, Cause Us to Incur Debt and Assume Contingent Liabilities

As part of our business strategy, we review acquisition and strategic investment prospects that we believe would complement our current product offerings, augment our market coverage or enhance our technical capabilities, or otherwise offer growth opportunities. From time to time we review investments in new businesses and we expect to make investments in, and to acquire, businesses, products, or technologies in the future. In the event of any future acquisitions, we could:

- issue equity securities which would dilute current stockholders' percentage ownership;
- incur substantial debt;
- assume contingent liabilities; or
- expend significant cash.

These actions could have a material adverse effect on our operating results or the price of our common stock. Moreover, even if we do obtain benefits in the form of increased sales and earnings, there may be a lag between the time when the expenses associated with an acquisition are incurred and the time when we recognize such benefits. This is particularly relevant in cases where it is necessary to integrate new types of technology into our existing portfolio and new types of products may be targeted for potential customers with which we do not have pre-existing relationships. Acquisitions and investment activities also entail numerous risks, including:

- difficulties in the assimilation of acquired operations, technologies and/or products;
- unanticipated costs associated with the acquisition or investment transaction;
- the diversion of management's attention from other business concerns;
- adverse effects on existing business relationships with suppliers and customers;
- risks associated with entering markets in which we have no or limited prior experience;
- the potential loss of key employees of acquired organizations; and
- substantial charges for the amortization of certain purchased intangible assets, deferred stock compensation or similar items.

We cannot assure you that we will be able to successfully integrate any businesses, products, technologies, or personnel that we might acquire in the future, and our failure to do so could have a material adverse effect on our business, operating results and financial condition.

We May Need Additional Capital to Fund Our Future Operations and, If It Is Not Available When Needed, We May Need to Reduce Our Planned Development and Marketing Efforts, Which May Reduce Our Net Revenues and Prevent Us From Achieving Profitability on a Fiscal Year Basis

We believe that our existing working capital and cash available from credit facilities and future operations, will enable us to meet our working capital requirements for at least the next 12 months. However, if cash from future operations is insufficient, or if cash is used for acquisitions or other currently unanticipated uses, we may need additional capital. The development and marketing of new products and the expansion of reseller and distribution channels and associated support personnel requires a significant commitment of resources. In addition, if the markets for our products develop more slowly than anticipated, or if we fail to establish significant market share and achieve sufficient net revenues, we may continue to consume significant amounts of capital. As a result, we could be required to raise additional capital. To the extent that we raise additional capital through the sale of equity or convertible debt securities, the issuance of such securities could result in dilution of the shares held by existing stockholders. If additional funds are raised through the issuance of debt securities, such securities may provide the holders certain rights, preferences, and privileges senior to those of common stockholders, and the terms of such debt could impose restrictions on our operations. We cannot assure you that additional capital, if required, will be available on acceptable terms, or at all. If we are unable to obtain sufficient amounts of additional capital, we may be required to reduce the scope of our planned product development and marketing efforts, which could harm our business, financial condition and operating results.

We Have Substantial Debt Obligations

In connection with the sale of convertible subordinated notes in December 2001, we incurred $200 million of indebtedness. We will require substantial amounts of cash to fund scheduled payments of interest on the convertible notes, payment of the principal amount of the convertible notes, future capital expenditures, payments on our leases and any increased working capital requirements. If we are unable to meet our cash requirements out of cash flow from operations, there can be no assurance that we will be able to obtain alternative financing. The degree to which we are financially leveraged could materially and adversely affect our ability to obtain financing for working capital, acquisitions or other purposes and could make us more vulnerable to industry downturns and competitive pressures. In the absence of such financing, our ability to respond to changing business and economic conditions, to make future acquisitions, to absorb adverse operating results or to fund capital expenditures or increased working capital requirements would be significantly reduced. Our ability to meet our debt service obligations will be dependent upon our future performance, which will be subject to financial, business and other factors affecting our operations, some of which are beyond our control. If we do not generate sufficient cash flow from operations to repay the notes at maturity, we could attempt to refinance the notes; however, no assurance can be given that such a refinancing would be available on terms acceptable to us, if at all. Any failure by us to satisfy our obligations with respect to the notes at maturity (with respect to payments of principal) or prior thereto (with respect to payments of interest or required repurchases) would constitute a default under the indenture and could cause a default under agreements governing our other indebtedness.

We Have Entered into Long-Term Lease Agreements for Several Facilities that are Currently Vacant and May be Difficult to Sublease due to Current Real Estate Market Conditions

We have certain long-term real estate lease commitments carrying future obligations for non-cancelable lease payments. Reductions in our workforce and the restructuring of operations since fiscal 2002 have resulted in the need to consolidate certain of these leased facilities, located primarily in Northern California, for which we recorded excess facilities charges of approximately $6.5 million in fiscal 2004, $9.6 million in fiscal 2003 and $25.4 million in fiscal 2002. For more information, see Note 6 of Notes to Condensed Consolidated Financial Statements. We continue to attempt to sublease certain of these facilities and have estimated the amount of sublease income to offset the carrying costs of these facilities when establishing our excess facilities charges. However, we may not be able to sublease these facilities at the times or on the terms we anticipated when we took the excess facilities charge and therefore if the market does not improve, we may incur additional charges in the future. In addition, we may incur additional charges for excess facilities as a result of additional reductions in our workforce or future restructuring of operations. We will continue to be responsible for all carrying costs of these facilities until such time as we can sublease these facilities or terminate the applicable leases based on the contractual terms of the lease agreements, and these costs may have an adverse effect on our business, operating results and financial condition.

Our Stock Price Has Been Volatile In the Past and Our Stock Price and the Price of the Notes May Significantly Fluctuate in the Future

In the past, our common stock price has fluctuated significantly. This could continue as we or our competitors announce new products, our results or those of our customers or competition fluctuate, conditions in the networking or semiconductor industry change, or when investors, change their sentiment toward stocks in the networking technology sector.

In addition, fluctuations in our stock price and our price-to-earnings multiple may make our stock attractive to momentum, hedge or day-trading investors who often shift funds into and out of stock rapidly, exacerbating price fluctuations in either direction, particularly when viewed on a quarterly basis.

Securities We Issue to Fund Our Operations Could Dilute Your Ownership

We may decide to raise additional funds through public or private debt or equity financing to fund our operations. If we raise funds by issuing equity securities, the percentage ownership of current stockholders will be reduced and the new equity securities may have rights prior to those of our common stock, including the common stock issuable upon conversion of the notes. We may not obtain sufficient financing on terms that are favorable to you or us. We may delay, limit or eliminate some or all of our proposed operations if adequate funds are not available.

Provisions in Our Charter Documents and Delaware Law and Our Adoption of a Stockholder Rights Plan May Delay or Prevent Acquisition Of Us, Which Could Decrease the Value of Our Common Stock and the Notes

Our certificate of incorporation and bylaws and Delaware law contain provisions that could make it more difficult for a third party to acquire us without the consent of our board of directors. Delaware law also imposes some restrictions on mergers and other business combinations between us and any holder of 15% or more of our outstanding common stock. In addition, our board of directors has the right to issue preferred stock without stockholder approval, which could be used to dilute the stock ownership of a potential hostile acquirer. Although we believe these provisions of our certificate of incorporation and bylaws and Delaware law and our stockholder rights plan, which is described below, will provide for an opportunity to receive a higher bid by requiring potential acquirers to negotiate with our board of directors, these provisions apply even if the offer may be considered beneficial by some of our stockholders.

Our board of directors adopted a stockholder rights plan, pursuant to which we declared and paid a dividend of one right for each share of common stock held by stockholders of record as of May 14, 2001. Under the plan, each right will entitle stockholders to purchase a fractional share of our preferred stock for $150.00. Each such fractional share of the new preferred stock has terms designed to make it substantially the economic equivalent of one share of common stock. Initially the rights will not be exercisable and will trade with our common stock. Generally, the rights may become exercisable if a person or group acquires beneficial ownership of 15% or more of our common stock or commences a tender or exchange offer upon consummation of which such person or group would beneficially own 15% or more of our common stock. When the rights become exercisable, our board of directors has the right to authorize the issuance of one share of our common stock in exchange for each right that is then exercisable.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Interest Rate Sensitivity

The primary objective of our investment activities is to preserve principal while at the same time maximize the income we receive from our investments without significantly increasing risk. Some of the securities that we have invested in may be subject to market risk. This means that a change in prevailing interest rates may cause the principal amount of the investment to fluctuate. For example, if we hold a security that was issued with a fixed interest rate at the then-prevailing rate and the prevailing interest rate later rises, the principal amount of our investment will probably decline. To minimize this risk, we maintain our portfolio of cash equivalents and short-term investments in a variety of securities, including commercial paper, other non-government debt securities and money market funds. In general, money market funds are not subject to market risk because the interest paid on such funds fluctuates with the prevailing interest rate. The following table presents the amounts of our cash equivalents, short-term investments and marketable securities that are subject to market risk by range of expected maturity and weighted-average interest rates as of March 27, 2005. This table does not include money market funds because those funds are not subject to market risk.

	Maturing in				
(in thousands)	Three months or less	Three months to one year	Greater than one year	Total	Fair Value
Included in cash and cash equivalents	$ 7,552			$ 7,552	$ 7,552
Weighted average interest rate	2.61%				
Included in short-term investments	$63,295	$ 77,429		$140,724	$140,724
Weighted average interest rate	2.67%	2.43%			
Included in marketable securities			$ 237,057	$237,057	$237,057
Weighted average interest rate			2.78%		
Long-term debt			$ 200,000	$200,000	$194,063
Average fixed rate			3.50%		

Exchange Rate Sensitivity

Currently, substantially all of our sales and the majority of our expenses are denominated in United States dollars and as a result, we have experienced no significant foreign exchange gains and losses to date. While we have conducted some transactions in foreign currencies during the first nine months of fiscal 2005 and expect to continue to do so, we do not anticipate that foreign exchange gains or losses will be significant, in part because of our foreign exchange risk management process discussed below.

Significant variability in foreign currencies relative to the U.S. dollar can cause operating expenses to fluctuate. Approximately 26% of our operating expenses are non-U.S. dollar denominated. The decline in the U.S. dollar relative to other major currencies is expected to result in an increase in operating expenses when those non-U.S. dollar-operating expenses are converted into U.S dollars.

Foreign Exchange Forward Contracts

We enter into foreign exchange forward contracts to hedge foreign currency forecasted transactions related to certain operating expenses, denominated in Japanese Yen, the Euro, the Swedish Krona and the British Pound. These derivatives are designated as cash flow hedges under SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities, as amended and interpreted* (“SFAS 133”). At March 27, 2005, these forward foreign currency contracts had a notional principal amount of $5.8 million (fair value of zero). These contracts have maturities of less than 60 days.

Additionally, we enter into foreign exchange forward contracts to mitigate the effect of gains and losses generated by the remeasurement of certain assets and liabilities denominated in Japanese Yen, the Euro, the Swedish Krona and the British Pound. These derivatives are not designated as hedges under SFAS 133. At March 27, 2005, we held foreign currency forward contracts with a notional principal amount of $4.2 million (fair value of $2,000). These contracts have maturities of less than 90 days. Changes in the fair value of these foreign exchange forward contracts are offset largely by remeasurement of the underlying assets and liabilities.

We do not enter into foreign exchange forward contracts for speculative or trading purposes. Foreign currency transaction gains from operations, including the impact of hedging, were $0.2 million for the third quarter of fiscal 2005 and a loss of ($0.6) million for the first nine months of fiscal 2005. Foreign currency transaction gains from operations, including the impact of hedging, were not significant for the third quarter of fiscal 2004 and were $0.3 million for the first nine months of fiscal 2004.

Item 4. Controls and Procedures

Under the supervision and with the participation of our management, including our chief executive officer and chief financial officer, we evaluated the effectiveness of our disclosure controls and procedures, as such term is defined in Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended. Based on this evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this quarterly report in providing reasonable assurance that information required to be disclosed by us in reports that it files under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms.

As required by Section 404 of the Sarbanes Oxley Act of 2002, we continue to test and evaluate our internal control procedures to determine whether our controls are designed and operating effectively. The requirements of Section 404 have caused most public companies to substantially increase the documentation of internal controls and to implement additional controls. As a result of our testing and evaluation performed to date, we have noted that improvements could be made in the design or operation of our internal control structure. We believe adequate compensating controls exist in these areas; however, we are developing plans to implement improvements or additional control procedures. We have disclosed these matters to the audit committee of our board of directors and to our independent registered public accounting firm. There were no changes to our internal controls during our last fiscal quarter that materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

PART II. Other Information

Item 1. Legal Proceedings

On May 27, 2003, Lucent filed suit against Foundry Networks, Inc. (“Foundry”) and us in the United States District Court for the District of Delaware. Foundry severed its case from the original case. The complaint against us alleges willful infringement of U.S. Patent Nos. 4,769,810, 4,769,811, 4,914,650, 4,922,486 and 5,245,607 and seeks a judgment: (a) determining that we have willfully infringed each of the five patents; (b) permanently enjoining us from infringement, inducement of infringement and contributory infringement of each of the five patents; and (c) awarding Lucent unspecified amounts of trebled damages, together with expenses, costs and attorneys’ fees.

We intend vigorously to defend against Lucent’s allegations. We answered Lucent’s complaint on July 16, 2003, denying infringement and asserting various affirmative defenses and counterclaims.

The claim construction hearing was held January 14, 2005. The trial date has been separated into three parts by court order, with infringement, willfulness and damages to be heard first in a trail that commenced April 28, 2005, to be followed immediately before the same jury on the issue of invalidity, with the equitable defenses and counterclaims to be held in a third trial at a date to be determined. While the outcome of this matter is currently not determinable, the ultimate costs to resolve it, whether through litigation or settlement, and whether we are successful or not, could have a material adverse effect on our consolidated financial statements, results of operations, and cash flows.

Beginning on July 6, 2001, purported securities fraud class action complaints were filed in the United States District Court for the Southern District of New York. The cases were consolidated and the litigation is now captioned as In re our Initial Public Offering Securities Litigation, Civ. No. 01-6143 (SAS) (S.D.N.Y.), related to In re Initial Public Offering Securities Litigation, 21 MC 92 (SAS) (S.D.N.Y.).

The operative amended complaint is brought purportedly on behalf of all persons who purchased our common stock from April 8, 1999 through December 6, 2000. It names as defendants Extreme Networks; six of our present and former officers and/or directors, including our CEO (the “Extreme Networks Defendants”); and several investment banking firms that served as underwriters of our initial public offering and October 1999 secondary offering. Subsequently, plaintiffs and one of the individual defendants stipulated to a dismissal of that defendant without prejudice. The complaint alleges liability under Sections 11 and 15 of the Securities Act of 1933 and Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, on the grounds that the registration statement for the offerings did not disclose that: (1) the underwriters had agreed to allow certain customers to purchase shares in the offerings in exchange for excess commissions paid to the underwriters; and (2) the underwriters had arranged for certain customers to purchase additional shares in the aftermarket at predetermined prices. The Securities Act allegations against the Extreme Networks Defendants are made as to the secondary offering only. The amended complaint also alleges that false analyst reports were issued. No specific damages are claimed.

Similar allegations were made in other lawsuits challenging over 300 other initial public offerings and follow-on offerings conducted in 1999 and 2000. The cases were consolidated for pretrial purposes. On February 19, 2003, the Court ruled on all defendants' motions to dismiss. The Court denied the motions to dismiss the claims in our case under the Securities Act of 1933. The Court denied the motion to dismiss the claim under Section 10(a) of the Securities Exchange Act of 1934 against us and 184 other issuer defendants, on the basis that the complaints alleged that the respective issuers had acquired companies or conducted follow-on offerings after their initial public offerings. The Court denied the motion to dismiss the claims under Section 10(a) and 20(a) of the Securities Exchange Act of 1934 against the remaining Extreme Networks Defendants and 59 other individual defendants, on the basis that the respective amended complaints alleged that the individuals sold stock.

We have executed a settlement agreement presented to all issuer defendants. In this settlement, plaintiffs will dismiss and release all claims against the Extreme Network Defendants, in exchange for a contingent payment by the insurance companies collectively responsible for insuring the issuers in all of the IPO cases, and for the assignment or surrender of control of certain claims we may have against the underwriters. The Extreme Networks Defendants will not be required to make any cash payments in the settlement, unless the pro rata amount paid by the insurers in the settlement exceeds the amount of the insurance coverage, a circumstance which we do not believe will occur. The settlement will require approval of the Court, which cannot be assured. On February 15, 2005, the Court issued an order providing preliminary approval of the settlement except insofar as the settlement would have cut off contractual indemnification claims that underwriters may have against securities issuers, such as the Company. The Court has scheduled a hearing for January 9, 2006 to consider final approval of the settlement. If the settlement is not approved, we cannot assure you that we will prevail in the lawsuit. Failure to prevail could have a material adverse effect on our consolidated financial position, results of operations and cash flows in the future.

Other than the proceedings stated above, we are not aware of any pending legal proceedings against us that, individually or in the aggregate, would have a material adverse effect on our business, operating results or financial condition. We may in the future be party to litigation arising in the course of our business, including claims that we allegedly infringe third-party trademarks and other intellectual property rights. Such claims, even if not meritorious, could result in the expenditure of significant financial and managerial resources.

Item 6. Exhibits

a) Exhibits:

31.1 Section 302 Certification of Gordon L. Stitt as Chief Executive Officer

31.2 Section 302 Certification of William R. Slakey as Chief Financial Officer

32.1 Section 906 Certification of Gordon L. Stitt as Chief Executive Officer

32.2 Section 906 Certification of William R. Slakey as Chief Financial Officer

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SIGNATURES

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

EXTREME NETWORKS, INC.
(Registrant)

/S/ WILLIAM R. SLAKEY

WILLIAM R. SLAKEY
Chief Financial Officer

May 5, 2005

EXHIBIT 31.1

SECTION 302 CERTIFICATION OF GORDON L. STITT
AS CHIEF EXECUTIVE OFFICER

I, Gordon L. Stitt, certify that:

1. I have reviewed this Form 10-Q of Extreme Networks, Inc.;

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

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

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

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

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

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

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

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

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

Dated: May 5, 2005

/s/ GORDON L. STITT

Gordon L. Stitt
Chief Executive Officer

EXHIBIT 31.2

SECTION 302 CERTIFICATION OF WILLIAM R. SLAKEY
AS CHIEF FINANCIAL OFFICER

I, William R. Slakey, certify that:

1. I have reviewed this Form 10-Q of Extreme Networks, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   (b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   (c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):
   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: May 5, 2005

/s/ WILLIAM R. SLAKEY

William R. Slakey
Chief Financial Officer

EXHIBIT 32.1

CERTIFICATION OF GORDON L. STITT AS CHIEF EXECUTIVE OFFICER, PURUSANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Extreme Networks, Inc. (the “Company”) on Form 10-Q for the period ended March 27, 2005, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Gordon L. Stitt, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)); and

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

/s/ GORDON L. STITT

Gordon L. Stitt
Chief Executive Officer
May 5, 2005

EXHIBIT 32.2

CERTIFICATION OF WILLIAM R. SLAKEY AS CHIEF FINANCIAL OFFICER, PURUSANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Extreme Networks, Inc. (the "Company") on Form 10-Q for the period ended March 27, 2005, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, William R. Slakey, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(3) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)); and

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

/s/ WILLIAM R. SLAKEY

William R. Slakey
Chief Financial Officer
May 5, 2005