AGERE SYSTEMS INC
Form 10-Q
May 05, 2006

As filed with the Securities and Exchange Commission on May 4, 2006

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2006

OR

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

For the transition period from _____________to _____________

Commission file number 001-16397

AGERE SYSTEMS INC.

A Delaware Corporation	I.R.S. Employer No. 22-3746606

1110 American Parkway NE, Allentown, PA 18109

Telephone - 610-712-1000

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

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

Large accelerated filer x Accelerated filer o Non-accelerated filer o

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

At May 1, 2006, 169,359,906 shares of common stock were outstanding.

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Form 10-Q
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PART I Financial Information

Item 1. Financial Statements

AGERE SYSTEMS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Dollars in Millions Except Per Share Amounts)
(Unaudited)

	Three Months Ended March 31,		Six Months Ended March 31,	
	2006	**2005**	**2006**	**2005**
Revenue	$ 397	$ 417	$ 800	$ 827
Costs	208	263	418	537
Gross profit	189	154	382	290
Operating expenses:				
Selling, general and administrative	60	60	121	115
Research and development	118	113	237	232
Amortization of acquired intangible assets	1	3	2	4
Purchased in-process research and development		55		55
Restructuring and other charges net	28	4	59	18
Gain on sale of operating assets net	(3)	(2)	(4)	(4)
Total operating expenses	204	233	415	420
Operating loss	(15)	(79)	(33)	(130)
Other income net	6	3	12	1
Interest expense	6	8	13	16
Loss from continuing operations before provision for income taxes	(15)	(84)	(34)	(145)
Provision (benefit) for income taxes	6	(16)	10	(10)
Loss from continuing operations	(21)	(68)	(44)	(135)
Income from discontinued operations (net of taxes)			4	
Net Loss	$ (21)	$ (68)	$ (40)	$ (135)
Basic and diluted loss per share information:				
Loss from continuing operations	$ (0.11)	$ (0.38)	$ (0.24)	$ (0.77)
Income from discontinued operations (net of taxes)			.02	
Net loss	$ (0.11)	$ (0.38)	$ (0.22)	$ (0.77)
Weighted average shares outstanding basic and diluted (in thousands)	177,609	175,382	179,212	174,207

See Notes to Condensed Consolidated Financial Statements.

AGERE SYSTEMS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS
(Dollars in Millions Except Per Share Amounts)
(Unaudited)

	March 31, 2006	September 30, 2005
ASSETS		
Current Assets		
Cash and cash equivalents	$ 620	$ 698
Trade receivables, less allowances of $2 as of March 31, 2006 and $3 as of September 30, 2005	227	251
Inventories	132	130
Other current assets	38	38
Total current assets	1,017	1,117
Property, plant and equipment net of accumulated depreciation and amortization of $1,298 as of March 31, 2006 and $1,280 as of September 30, 2005	423	420
Goodwill	196	196
Acquired intangible assets net of accumulated amortization	13	9
Other assets	93	139
Total assets	$ 1,742	$ 1,881
LIABILITIES AND STOCKHOLDERS EQUITY		
Current Liabilities		
Accounts payable	$ 188	$ 200
Payroll and related benefits	108	87
Income taxes payable	71	84
Restructuring reserve	21	28
Deferred income	26	35
Other current liabilities	42	54
Total current liabilities	456	488
Pension and postretirement benefits	521	522
Long-term debt	372	372
Other liabilities	73	72
Total liabilities	1,422	1,454
Commitments and contingencies		
Stockholders Equity		
Preferred stock, par value $1.00 per share, 250,000,000 shares authorized and no shares issued and outstanding		
Common stock, par value $0.01 per share, 1,000,000,000 shares authorized and 174,955,821 shares outstanding as of March 31, 2006 and 181,627,917 shares outstanding as of September 30, 2005	2	2
Additional paid-in capital	7,594	7,561
Accumulated deficit	(6,829)	(6,789)
Accumulated other comprehensive loss	(347)	(347)
Treasury stock, at cost, 7,839,439 common shares at March 31, 2006 and 10,939 common shares at September 30, 2005	(100)	
Total stockholders equity	320	427

Total liabilities and stockholders equity	$ 1,742	$ 1,881

See Notes to Condensed Consolidated Financial Statements.

AGERE SYSTEMS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in Millions)
(Unaudited)

	Six Months Ended March 31,	
	2006	**2005**
OPERATING ACTIVITIES		
Net loss	$ (40)	$ (135)
Less: Income from discontinued operations	4	
Loss from continuing operations	(44)	(135)
Adjustments to reconcile loss from continuing operations to net cash provided (used) by operating activities:		
Purchased in-process R&D		55
Restructuring and other charges net of cash payments	16	(28)
Depreciation and amortization	56	157
Pension plan contributions		(40)
Stock-based compensation expense	20	
Provision (benefit) for deferred income taxes	4	(1)
Provision for inventory write-downs	6	11
Equity loss from investments		5
Dividends received from equity investments		41
Decrease in receivables	25	78
(Increase) decrease in inventories	(8)	16
Decrease in accounts payable	(12)	(17)
Decrease in payroll and benefit liabilities	(3)	(13)
Decrease in tax accruals	(17)	(15)
Changes in other operating assets and liabilities	(11)	(30)
Other adjustments for non-cash items net	1	(3)
NET CASH PROVIDED BY OPERATING ACTIVITIES	33	81
INVESTING ACTIVITIES		
Capital expenditures	(57)	(56)
Acquisition of intangibles	(7)	
Return of capital from investments	39	
Proceeds from the sale or disposal of property, plant and equipment	6	5
Acquisition of businesses, net of cash acquired		(26)
Decrease in cash designated as held in trust		13
NET CASH USED BY INVESTING ACTIVITIES	(19)	(64)
FINANCING ACTIVITIES		
Purchase of treasury stock	(100)	
Proceeds from the issuance of stock net of expense	8	10
Principal repayments on short-term debt		(122)
Principal repayments on long-term debt		(9)
NET CASH USED BY FINANCING ACTIVITIES	(92)	(121)

Effect of exchange rate changes on cash		1
Net decrease in cash and cash equivalents	(78)	(103)
Cash and cash equivalents at beginning of period	698	778
Cash and cash equivalents at end of period	$ 620	$ 675

See Notes to Condensed Consolidated Financial Statements.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in Millions Except Per Share Amounts)
(Unaudited)

1. Basis of Presentation and Summary of Significant Accounting Policies

Agere Systems Inc. (the Company or Agere) is a leading provider of integrated circuit solutions for a variety of applications including high-density storage, mobile wireless communications and enterprise and telecommunications networks. These solutions form the building blocks for a broad range of computing and communications applications. Agere s customers include manufacturers of hard disk drives, mobile phones, high speed communications systems and personal computers. The Company also generates revenue from the licensing of intellectual property.

Effective January 1, 2006, the Company was reorganized into operating segments that focused on three key markets: Storage, Mobility, and Networking. The Company has two reportable segments, Consumer and Networking. Each segment includes product revenue and revenue from the licensing of intellectual property. The Consumer segment includes the Storage and Mobility operating segments. Storage provides integrated circuit solutions for hard disk drives used in computing and consumer electronics. Mobility provides integrated circuit solutions for a variety of end-user applications such as mobile phones and satellite radio. Networking provides semiconductor solutions for enterprise and telecommunications carrier networks, as well as personal computer based consumer communications applications. Certain prior year amounts have been reclassified to conform to the fiscal 2006 presentation.

Internal Use Software

During the first quarter of fiscal 2006 the Company assigned a useful life of seven years to the primary upgrade to its information system used for financial reporting. The useful life of certain capitalized computer software costs is a range of three to seven years.

Interim Financial Information

These condensed financial statements have been prepared in accordance with the rules of the Securities and Exchange Commission for interim financial statements and do not include all annual disclosures required by accounting principles generally accepted in the United States. These financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company s Form 10-K for the fiscal year ended September 30, 2005. The condensed financial information as of March 31, 2006 and for the three and six months ended March 31, 2006 and 2005 is unaudited, but includes all adjustments that management considers necessary for a fair presentation of the Company s consolidated results of operations, financial position and cash flows. Results for the three and six months ended March 31, 2006, are not necessarily indicative of results to be expected for the full fiscal year 2006 or any other future periods.

2. Stock Compensation Plans

Agere has stock-based compensation plans under which employees and non-employee directors receive stock options and other equity-based awards. The plans provide for the granting of stock options, performance awards, restricted stock awards, cash awards, stock appreciation rights and other stock unit awards. The number of shares authorized and available for awards under Agere plans as of March 31, 2006, was 14,813,287. This amount includes 6,000,000 shares approved by Agere stockholders during the second quarter of fiscal 2006. As of March 31, 2006, awards relating to 28,766,110 shares were outstanding, including awards relating to 2,218,606 shares that were granted by Lucent Technologies Inc. (Lucent), or companies acquired by Lucent prior to Agere s spin-off by Lucent, and converted later into Agere awards. During the first six months of fiscal 2006 and 2005, employees and non-employee directors of the Company were granted stock options and other equity-based awards. Agere stock options are granted with an exercise price equal to 100% of the market value of a share of common stock on the date of the grant, generally have seven-year contractual terms, and vest no later than four years from the date of grant. Agere also granted restricted stock units (a form of other stock units), at no cost to the employee, that vest based on completion of a required service period or a combination of required service and satisfaction of a performance test that requires Agere s total stockholder return to exceed that of a market capitalization weighted peer group index of nine companies over a four-year period. If that test is not met, the restricted stock units will expire and any compensation cost recognized previously is not reversed. The time-based restricted stock unit awards vest over a two-year or four-year period and the performance-based awards vest after four years from the date of grant if the performance test has been met at that time.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
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Agere s Employee Stock Purchase Plan (ESPP) has purchase periods that run for six months beginning each May 1 and November 1. Under the terms of the ESPP, participating employees may have up to 10% of eligible compensation (subject to limitations on the number of shares and fair market value of shares that may be acquired each purchase period) deducted from their pay to purchase the Company s common stock. The per share purchase price in any purchase period is equal to 85% of the lower of either the market price on the first trading day of the purchase period, or the last trading day of the purchase period. During the six months ended March 31, 2006, 460,311 shares were purchased under the ESPP. As of March 31, 2006, 5,304,241 shares remained available for purchase under the ESPP.

Effective October 1, 2005, the Company adopted the provisions of Statement of Financial Accounting Standards No. 123R, Share-Based Payment (SFAS 123R), which establishes the financial accounting and reporting standards for stock-based compensation plans. SFAS 123R requires the measurement and recognition of compensation expense for all stock-based awards made to employees and directors, including employee stock options and restricted stock units, and purchases under the ESPP. Under the provisions of SFAS 123R, stock-based compensation cost is measured at the grant date, based on the calculated fair value of the award, and is recognized as an expense on a straight-line basis over the requisite service period of the entire award (generally the vesting period of the award). As a result of adopting SFAS 123R, the Company s net loss before income taxes and net loss for the three and six months ended March 31, 2006 was $10 and $20, respectively, more than if the Company had continued to account for stock-based compensation under Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees (APB 25) and its related interpretations. Basic and diluted net loss per share for the three months ended March 31, 2006 of $(0.11) is $0.06 more than if the Company had not adopted SFAS 123R. Basic and diluted net loss per share for the six months ended March 31, 2006 of $(0.22) is $0.11 more than if the Company had not adopted SFAS 123R.

The Company has elected to use the modified prospective transition method as permitted by SFAS 123R and, therefore, financial results for prior periods have not been restated. Under this transition method, stock-based compensation expense for the three and six months ended March 31, 2006 includes expense for all equity awards granted prior to, but not yet vested as of October 1, 2005. This compensation expense was based on the grant date fair value estimated in accordance with the original provisions of SFAS No. 123, Accounting for Stock-Based Compensation (SFAS 123) as amended by SFAS 148, Accounting for Stock-Based Compensation Transition and Disclosure. Since the adoption of SFAS 123R, there have been no changes to the Company s stock compensation plans or modifications to outstanding stock-based awards which would increase the value of any awards outstanding. Compensation expense for all stock-based compensation awards granted subsequent to October 1, 2005 was based on the grant-date fair value determined in accordance with the provisions of SFAS 123R. During the quarter ended March 31, 2006, the Company recognized compensation expense of $6 for stock options, $3 for restricted stock units and $1 for the ESPP. During the six months ended March 31, 2006, the Company recognized compensation expense of $14 for stock options, $4 for restricted stock units and $2 for the ESPP. All of this expense was recognized in the statements of operations. There were no significant capitalized stock-based compensation costs at March 31, 2006.

Prior to October 1, 2005, the Company accounted for stock-based compensation in accordance with APB 25 and also followed the disclosure requirements of SFAS 123. Under APB 25, the Company accounted for stock-based awards to employees and directors using the intrinsic value method as allowed under SFAS 123. Under the intrinsic value method, no stock-based compensation expense was recognized in the Company s statements of operations (other than minimal amounts for restricted stock units) because the exercise price of the stock options granted to employees and directors equaled the fair market value of the underlying stock at the date of grant. The following table sets forth the computation of basic and diluted loss per share for the three and six months ended March 31, 2005 and illustrates the effect on net loss and loss per share as if the Company had applied the fair value recognition provisions of SFAS 123 to its stock plans:

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in Millions Except Per Share Amounts)
(Unaudited)

	Three Months Ended March 31, 2005	Six Months Ended March 31, 2005
Net loss:		
As reported	$ (68)	$ (135)
Deduct: Stock-based employee compensation expense determined under SFAS 123 fair value based method (1)	32	61
Pro forma	$ (100)	$ (196)
Basic and diluted loss per share:		
As reported	$ (0.38)	$ (0.77)
Pro forma	$ (0.57)	$ (1.12)

(1) The pro forma stock-based compensation expense was not tax-effected due to the recording of a full valuation allowance against U.S. net deferred tax assets.

The following table presents the total stock-based compensation expense resulting from stock options, restricted stock unit awards, and the ESPP included in the Statement of Operations:

	Three Months Ended March 31, 2006	Six Months Ended March 31, 2006
Costs	$ 1	$ 3
Selling, general and administrative	5	9
Research and development	4	6
Restructuring and other charges net (1)		2
Stock-based compensation expense before income taxes	10	20
Benefit for income taxes (2)		
Net compensation expense	$ 10	$ 20

(1) Represents the total amount of stock-based compensation expense for employees on leave of absence for the period of time during which their awards continue to vest but the employees requisite service period has been completed.

(2) The stock-based compensation expense has not been tax-effected due to the recording of a full valuation allowance against U.S. net deferred tax assets.

The fair value of each stock option grant is estimated as of the grant date using the Black-Scholes option-pricing model with the following assumptions:

	Stock Options		ESPP	
	Three Months Ended		Three Months Ended	
	March 31, 2006	March 31, 2005	March 31, 2006	March 31, 2005
Dividend yield	0.00%	0.00%	0.00%	0.00%

Expected volatility	58%	85%	59%	95%
Risk-free interest rate (range)	4.30%-4.61%	3.23%-3.67%	3.43%	1.0%
Expected term (in years)	4.0	2.7	.5	.5

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
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	Stock Options		ESPP	
	Six Months Ended		Six Months Ended	
	March 31, 2006	March 31, 2005	March 31, 2006	March 31, 2005
Dividend yield	0.00%	0.00%	0.00%	0.00%
Expected volatility	58%	85%	60%	95%
Risk-free interest rate (range)	4.18%-4.61%	2.82%-3.67%	2.76%-3.43%	1.0%
Expected term (in years)	4.0	2.7	.5	.5

Expected Volatility. The Company uses third-party analysis to assist in developing the expected volatility of its stock options. In anticipation of adopting SFAS 123R in October 2005, the Company evaluated the assumptions used in the Black-Scholes model during the third quarter of fiscal 2005. As a result, the Company changed its methodology for computing the expected volatility from being based solely on Company historical volatility to a combination of both Company and peer company historical volatility and peer company market-based implied volatility. For this reason, expected volatility was lower in the three and six months ended March 31, 2006 than in the same periods in the previous fiscal year.

Expected Term. The expected term is based on several factors including historical observations of employee exercise patterns during the Company s history, peer company employee exercise behavior, and expectations of employee exercise behavior in the future giving consideration to the contractual terms of the stock-based awards. The Company also uses third-party analysis to assist in developing the expected term of its stock options. The expected term of ESPP options is determined by the length of the purchase period.

Risk-Free Interest Rate. The interest rate used in valuing awards is based on the yield at the time of grant of a U.S. Treasury security with an equivalent remaining term.

Dividend Yield. The Company has never paid cash dividends and does not currently intend to pay cash dividends, and thus has assumed a 0% dividend yield.

Pre-Vesting Forfeitures. Estimates of pre-vesting option forfeitures are based on Company experience and industry trends. The Company will adjust its estimate of forfeitures over the requisite service period based on the extent to which actual forfeitures differ, or are expected to differ, from such estimates. Changes in estimated forfeitures will be recognized through a cumulative catch-up adjustment in the period of change and will also impact the amount of compensation expense to be recognized in future periods. The cumulative effect resulting from initially applying the provisions of SFAS 123R to nonvested equity awards was not significant.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in Millions Except Per Share Amounts)
(Unaudited)

Stock Options

The following table summarizes the Company s stock option activity during fiscal 2006:

Stock Options	Shares (000 s)	Weighted Average Exercise Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at September 30, 2005	25,461	$ 56.93		
Granted	3,679	$ 12.69		
Exercised	(203)	$ 9.97		
Forfeited or Expired	(1,566)	$ 59.76		
Outstanding at December 31, 2005	27,371	$ 51.34	4.27	$ 2
Granted	348	$ 13.11		
Exercised	(129)	$ 10.61		
Forfeited or Expired	(1,579)	$ 98.68		
Outstanding at March 31, 2006	26,011	$ 48.16	4.14	$ 7
Vested or expected to vest at March 31, 2006	25,155	$ 48.16	4.14	$ 7
Exercisable at March 31, 2006	17,974	$ 63.48	3.32	$ 3

The weighted-average grant-date fair value of options granted during the three and six months ended March 31, 2006 was $6.41 and $6.21, respectively, and in the three and six months ended March 31, 2005 was $7.66 and $7.34, respectively. The total fair value of stock options vested during the three and six months ended March 31, 2006 was $12 and $41, respectively. As of March 31, 2006, there was a total of $55 of unrecognized compensation cost related to nonvested stock options. That cost is expected to be recognized over a weighted-average period of 1.9 years.

The total intrinsic value of options exercised during the three and six months ended March 31, 2006 and March 31, 2005 was less than $1 in all periods. Cash received from option exercises for the three and six months ended March 31, 2006 was $1 and $3, respectively.

Restricted Stock Units

The value of time-based restricted stock units is determined by their intrinsic value (as if the underlying shares were vested and issued) on the grant date. The following table summarizes the Company s time-based nonvested share activity during fiscal 2006:

Nonvested Shares (Time-based)	Shares (000 s)	Weighted Average Grant-Date Fair Value
Nonvested at October 1, 2005	13	$ 11.62
Granted	2,277	$ 13.05
Vested	(1)	$ 11.20
Forfeited	(5)	$ 13.32
Nonvested at December 31, 2005	2,284	$ 13.04

Granted	31	$ 12.83
Vested		
Forfeited	(35)	$ 13.32
Nonvested at March 31, 2006	2,280	$ 13.04

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
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(Unaudited)

As of March 31, 2006, there was a total of $24 of unrecognized compensation cost related to time-based nonvested restricted stock unit awards. That cost is expected to be recognized over a weighted-average period of 1.9 years.

The fair value of performance-based restricted stock units is determined by a Monte Carlo simulation technique. The following table summarizes the Company s performance-based, nonvested share activity during fiscal 2006:

Nonvested Shares (Performance-based)	Shares (000 s)	Weighted Average Grant-Date Fair Value
Nonvested at October 1, 2005		
Granted	475	$ 8.06
Vested		
Forfeited		
Nonvested at December 31, 2005	475	$ 8.06
Granted		
Vested		
Forfeited		
Nonvested at March 31, 2006	475	$ 8.06

As of March 31, 2006, there was a total of $3 of unrecognized compensation cost related to performance-based, nonvested restricted stock unit awards. That cost is expected to be recognized equally over a period of 3.5 years.

3. Restructuring and Other Charges Net

The Company has implemented restructuring and consolidation actions to improve gross profit, reduce expenses and streamline operations. These actions include workforce reductions, rationalization and consolidation of manufacturing capacity and the exit of certain businesses, including the optoelectronic components business. At March 31, 2006, the Company was engaged in three separate restructuring programs. The first restructuring program was a resizing and consolidation of the business which began in fiscal 2001 and includes actions to improve gross profit, reduce expenses and streamline operations. This program was substantially complete as of December 31, 2004. The second restructuring program was announced on September 23, 2004 and consists of a further resizing of the business to align the cost structure with revenue expectations and improve profitability. This program was substantially complete as of September 30, 2005. The third restructuring program was announced on September 29, 2004 and relates to the closure of the Company s manufacturing facility in Orlando, Florida. In September 2005, the Company ceased manufacturing operations at its Orlando facility. In addition to these restructuring programs, at March 31, 2006, the Company was engaged in activities to resize its business, which began in fiscal 2005 and fiscal 2006.

For the three and six months ended March 31, 2006, restructuring and other charges net were $28 and $59, respectively. These amounts include expenses of $22 and $44, respectively, associated with the 2006 resizing, Orlando decommissioning expenses of $6 and $13, respectively and restructuring and related expenses of $0 and $3, respectively, as well as a reversal of $1 associated with the fiscal 2005 business resizing recorded in the first quarter of fiscal 2006. For the three and six months ended March 31, 2005, restructuring and other charges net were $4 and $18, respectively. These amounts include restructuring and related expenses of $4 and $17, respectively, and expenses associated with the reclassification of the classes of common stock of $0 and $1, respectively.

Orlando Decommissioning Activities

For the three and six months ended March 31, 2006, the Company recorded additional charges of $6 and $13, respectively, related to decommissioning activities at the Orlando facility and made cash payments of $7 and $15, respectively, related to this obligation. At March 31, 2006, a reserve balance of $1 was recorded in other current liabilities.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in Millions Except Per Share Amounts)
(Unaudited)

2005 Business Resizing

In the fourth quarter of fiscal 2005, the Company developed plans to resize and discontinue some of its shared business support groups. As part of this program, the Company expects to reduce its workforce by approximately 70 employees, almost all of which were off-roll as of March 31, 2006. For the six months ended March 31, 2006, the Company recorded a non-cash credit of $1 within restructuring and other charges net relating to revised estimates. During the three and six months ended March 31, 2006, the Company paid $1 and $2, respectively, towards this obligation. At March 31, 2006, the Company has recorded a liability of $1 within other current liabilities related to cash charges which are expected to be paid by the end of fiscal 2007.

2006 Business Resizing

On October 26, 2005, the Company announced that it was considering additional actions that would further improve profitability and consolidate its operations. The Company currently estimates that it will reduce its workforce by approximately 435 employees, all of which are expected to be off-roll by the end of fiscal 2006. For the three and six months ended March 31, 2006, the Company recorded charges of $22 and $44, respectively, within restructuring and other charges net. These amounts include $20 and $39, respectively, of cash charges principally related to termination benefits related to workforce reductions and $2 and $5, respectively, of non-cash charges. The non-cash charge of $2 recorded in the three months ended March 31, 2006 primarily relates to increased depreciation resulting from shortening the estimated useful life of a building related to the decision to consolidate operations of two facilities. The non-cash charge of $5 recorded in the six months ended March 31, 2006, relates to stock-based compensation expenses for certain employees on leave of absence, increased depreciation, and a special pension benefit charge. During the three and six months ended March 31, 2006, the Company paid $9 and $13, respectively, towards this obligation. At March 31, 2006, the Company has recorded a liability of $26 within other current liabilities related to cash charges which are expected to be paid by the end of fiscal 2007.

Restructuring Actions

2001 Manufacturing Rationalization and Resizing

Beginning in fiscal 2001, the Company implemented a restructuring and consolidation program in response to significant declines in revenue, particularly from telecommunications network equipment manufacturing customers. These customers were themselves experiencing significant declines in demand from their customers. The actions taken were designed to permit the Company to achieve breakeven at a significantly lower level of quarterly revenue. This program, which is substantially complete, included actions to improve gross profit, reduce expenses, eliminate excess manufacturing capacity and streamline operations. As part of this restructuring program, the Company:

- Sold its optoelectronic components business, including the manufacturing facilities associated with that business;
- Reduced total headcount by approximately 9,700 employees;
- Consolidated operations into fewer facilities, resulting in the closure of over 25 smaller manufacturing, administrative, support and warehouse facilities; and
- Closed integrated circuit wafer manufacturing facilities in Allentown and Reading, Pennsylvania and Madrid, Spain.

Substantially all of the product lines eliminated by this restructuring program were part of the optoelectronic components business, which was sold and reported as discontinued operations.

2004 Business Resizing

On September 23, 2004, the Company announced a restructuring program to resize the business and improve profitability. As part of this program, the Company reduced its workforce by approximately 550 employees across the business, including administrative functions, sales, marketing and product development, and exited the standalone wireless local area networking chipset business, the radio-frequency power transistor business, and all operations in the Netherlands.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in Millions Except Per Share Amounts)
(Unaudited)

Closure of the Orlando Manufacturing Facility

On September 29, 2004, the Company announced that it would close its wafer manufacturing facility in Orlando and in September 2005 operations there ceased. On March 31, 2006, approximately 50 people assigned to the Orlando facility were on roll, primarily engaged in facility decommissioning activities, all of which are expected to be taken off-roll by the end of the second quarter of fiscal 2007.

Three and Six Months Ended March 31, 2006

The following tables set forth the Company s restructuring reserve as of March 31, 2006, and the activity affecting the reserve for the three and six months ended March 31, 2006:

		Three Months Ended March 31, 2006			
	December 31, 2005 Restructuring Reserve	Add Charges	Deduct Non-Cash Charges	Deduct Cash Payments	March 31, 2006 Restructuring Reserve
2001 Manufacturing Rationalization and Resizing					
Facility lease terminations	$ 17	$ 1	$	$ 1	$ 17
Other charges	1	(1)			
Total	$ 18	$	$	$ 1	$ 17
2004 Business Resizing					
Workforce reductions	$ 1	$	$	$	$ 1
Closure of the Orlando Manufacturing Facility					
Workforce reductions	$ 4	$	$	$ 1	$ 3
Grand Total	$ 23	$	$	$ 2	$ 21

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in Millions Except Per Share Amounts)
(Unaudited)

	September 30, 2005 Restructuring Reserve	Six Months Ended March 31, 2006 Add Charges	Deduct Non-Cash Charges	Deduct Cash Payments	March 31, 2006 Restructuring Reserve
2001 Manufacturing Rationalization and Resizing					
Workforce reductions	$ 1	$	$	$ 1	$
Facility lease terminations	17	3		3	17
Other charges	1			1	
Total	$ 19	$ 3	$	$ 5	$ 17
2004 Business Resizing					
Workforce reductions	$ 1	$	$	$	$ 1
Closure of the Orlando Manufacturing Facility					
Workforce reductions	$ 8	$	$	$ 5	$ 3
Grand Total	$ 28	$ 3	$	$ 10	$ 21

2001 Manufacturing Rationalization and Resizing

Facility Lease Terminations and Other Charges

During the six months ended March 31, 2006, the Company recorded charges for facility lease terminations and other charges of $3 related to revised estimates for facility lease terminations. During the second quarter of fiscal 2006, $1 of other charges recorded in the first quarter of fiscal 2006, was reclassified to facility lease terminations.

Restructuring Reserve Balances as of March 31, 2006

2001 Manufacturing Rationalization and Resizing

The $17 reserve for facility lease terminations will be paid over the respective lease terms through 2010.

2004 Business Resizing

The Company anticipates the $1 restructuring reserve relating to workforce reductions will be paid by the end of fiscal 2006.

Closure of the Orlando Manufacturing Facility

The Company anticipates that approximately $2 of the $3 restructuring reserve relating to workforce reductions as a result of the exit of operations at the Orlando facility will be paid during fiscal 2006. The remaining amount is expected to be paid in fiscal 2007.

The Company expects to fund the cash payments related to all of the restructuring reserves with cash on hand.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in Millions Except Per Share Amounts)
(Unaudited)

Three and Six Months Ended March 31, 2005

The following tables set forth the Company s restructuring reserve as of March 31, 2005, and the activity affecting the reserve for the three and six months ended March 31, 2005:

		Three Months Ended March 31, 2005			
	December 31, 2004 Restructuring Reserve	Add Charges	Deduct Non-Cash Charges	Deduct Cash Payments	March 31, 2005 Restructuring Reserve
2001 Manufacturing Rationalization and Resizing					
Workforce reductions	$ 2	$	$	$ 1	$ 1
Facility lease terminations	18	1		2	17
Other charges	6	4		6	4
Total	$ 26	$ 5	$	$ 9	$ 22
2004 Business Resizing					
Workforce reductions	$ 9	$ (1)	$	$ 4	$ 4
Other charges	1			1	
Total	$ 10	$ (1)	$	$ 5	$ 4
Closure of the Orlando Manufacturing Facility					
Workforce reductions	$ 7	$	$	$	$ 7
Grand Total	$ 43	$ 4	$	$ 14	$ 33

		Six Months Ended March 31, 2005			
	September 30, 2004 Restructuring Reserve	Add Charges	Deduct Non-Cash Charges	Deduct Cash Payments	March 31, 2005 Restructuring Reserve
2001 Manufacturing Rationalization and Resizing					
Workforce reductions	$ 5	$	$	$ 4	$ 1
Facility lease terminations	20	1		4	17
Other charges	6	8		10	4
Asset impairments		4	4		