AVIAT NETWORKS, INC.
Form 10-Q
May 12, 2010

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

(Mark One)

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

For the quarterly period ended April 2, 2010

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 001-33278
AVIAT NETWORKS, INC.
(Exact name of registrant as specified in its charter)

Delaware	**20-5961564**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
637 Davis Drive **Morrisville, North Carolina**	**27560**
(Address of principal executive offices)	(Zip Code)

(919) 767-3250
(Registrant s telephone number, including area code)
Not Applicable
(Former name, former address and former fiscal year, if changed since last report)

Indicate by checkmark whether the registrant (l) 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 þ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes o No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer o	Accelerated filer þ	Non- accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

The number of shares outstanding of the registrant s Common Stock as of May 7, 2010 was 59,679,404 shares.

AVIAT NETWORKS, INC. (FORMERLY HARRIS STRATEX NETWORKS, INC.)
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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

AVIAT NETWORKS, INC. (FORMERLY HARRIS STRATEX NETWORKS, INC.)
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Quarter Ended		Three Quarters Ended	
(In millions, except per common share amounts)	**April 2, 2010**	**April 3, 2009**	**April 2, 2010**	**April 3, 2009**
Revenue from product sales and services:				
Revenue from product sales	$ 93.2	$ 126.6	$ 277.6	$ 437.2
Revenue from services	26.8	31.4	85.0	107.5
Total revenue	120.0	158.0	362.6	544.7
Cost of product sales and services:				
Cost of product sales	(65.4)	(89.0)	(183.1)	(300.6)
Cost of services	(17.4)	(20.9)	(58.1)	(82.2)
Charges for product transition	(16.9)	(29.8)	(16.9)	(29.8)
Amortization of purchased technology	(2.1)	(1.8)	(6.3)	(5.4)
Total cost of product sales and services	(101.8)	(141.5)	(264.4)	(418.0)
Gross margin	18.2	16.5	98.2	126.7
Research and development expenses	(10.2)	(9.9)	(31.0)	(29.6)
Selling and administrative expenses	(35.0)	(34.6)	(101.2)	(104.0)
Total research, development, selling and administrative expenses	(45.2)	(44.5)	(132.2)	(133.6)
Amortization of identifiable intangible assets	(1.3)	(1.4)	(4.3)	(4.2)
Acquired in-process research and development		(2.4)		(2.4)
Software impairment charges		(2.9)		(2.9)
Restructuring charges	(0.7)	(0.5)	(3.3)	(4.9)
Goodwill impairment charges				(279.0)
Trade name impairment charges				(22.0)
Operating loss	(29.0)	(35.2)	(41.6)	(322.3)
Interest income		0.2	0.1	0.9
Interest expense	(0.6)	(0.8)	(1.5)	(2.2)
Loss before provision for income taxes	(29.6)	(35.8)	(43.0)	(323.6)
Benefit from (provision for) income taxes	3.9	(3.6)	1.6	(28.0)
Net loss	$ (25.7)	$ (39.4)	$ (41.4)	$ (351.6)

Net loss per common share of common stock (Note 1):				
Basic and diluted	$ (0.43)	$ (0.67)	$ (0.70)	$ (5.99)
Basic and diluted weighted average shares outstanding	59.7	58.8	59.3	58.7

(1) In fiscal 2009, we had Class A and Class B shares of common stock outstanding. The net loss per common share amounts were the same for Class A and Class B in the quarter and three quarters ended April 3, 2009 because the holders of each class were legally entitled to equal per share distributions whether through dividends or in liquidation. There were no shares of Class B common stock outstanding during the quarter and three quarters ended April 2, 2010. Effective November 19, 2009, under a change to our certificate of incorporation approved by shareholders, all shares of our Class A common stock were reclassified on a

one-to-one basis to shares of Common Stock without a class designation; we no longer have Class A or Class B common stock authorized, issued or outstanding.

See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited).

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AVIAT NETWORKS, INC. (FORMERLY HARRIS STRATEX NETWORKS, INC.)
CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)

(In millions, except share amounts)	April 2, 2010	July 3, 2009 (1)
Assets		
Current Assets		
Cash and cash equivalents	$ 140.5	$ 136.8
Short-term investments		0.3
Receivables	115.2	142.9
Unbilled costs	29.3	27.8
Inventories	70.8	98.6
Other current assets	33.8	29.7
Total Current Assets	389.6	436.1
Long-Term Assets		
Property, plant and equipment	52.6	57.4
Goodwill	6.2	3.2
Identifiable intangible assets	74.0	84.1
Non-current deferred income taxes	8.2	8.0
Capitalized software and other assets	10.5	11.4
Total Long-Term Assets	151.5	164.1
Total Assets	$ 541.1	$ 600.2
Liabilities and Shareholders Equity		
Current Liabilities		
Short-term debt	$ 10.0	$ 10.0
Accounts payable	57.1	69.6
Compensation and benefits	13.9	16.6
Other accrued items	49.2	55.6
Advance payments and unearned income	38.4	37.3
Restructuring liabilities	4.5	5.3
Total Current Liabilities	173.1	194.4
Long-Term Liabilities		
Restructuring and other long-term liabilities	1.9	4.3
Redeemable preference shares	8.3	8.3
Reserve for uncertain tax positions	5.5	4.4
Deferred income taxes	0.9	0.9
Total Liabilities	189.7	212.3
Commitments and contingencies		
Shareholders Equity		
Preferred stock, $0.01 par value; 50,000,000 shares authorized; none issued		
Common stock, $0.01 par value; 300,000,000 shares authorized; issued and outstanding 59,648,099 shares as of April 2, 2010 and 58,903,177 shares as of July 3, 2009	0.6	0.6

Additional paid-in-capital	785.1	783.2
Accumulated deficit	(432.5)	(391.1)
Accumulated other comprehensive loss	(1.8)	(4.8)
Total Shareholders Equity	351.4	387.9
Total Liabilities and Shareholders Equity	$ 541.1	$ 600.2

(1) Derived from audited consolidated financial statements.

See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited).

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AVIAT NETWORKS, INC. (FORMERLY HARRIS STRATEX NETWORKS, INC.)
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOW
(Unaudited)

	Three Quarters Ended	
	April 2, 2010	April 3, 2009
	(In millions)	
Operating Activities		
Net loss	**$ (41.4)**	$ (351.6)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Amortization of identifiable intangible assets	**10.6**	10.0
Depreciation and amortization of property, plant and equipment and capitalized software	**15.8**	17.6
Non-cash share-based compensation expense	**1.8**	1.8
Goodwill impairment charges		279.0
Trade name impairment charges		22.0
Charges for product transition and related impairments, including software	**13.5**	29.3
Acquired in-process research and development		2.4
Decrease in fair value of warrants		(0.5)
Deferred income tax expense	**0.9**	19.9
Changes in operating assets and liabilities:		
Receivables	**28.1**	60.7
Unbilled costs and inventories	**18.3**	(15.3)
Accounts payable and accrued expenses	**(17.1)**	(30.0)
Advance payments and unearned income	**1.0**	4.8
Refundable income taxes and income taxes payable	**(4.4)**	4.5
Restructuring liabilities and other	**(5.3)**	(9.3)
Net cash provided by operating activities	**21.8**	45.3
Investing Activities		
Cash paid related to acquisition of Telsima	**(4.2)**	(4.0)
Purchases of short-term investments and available for sale securities		(1.2)
Sales of short-term investments and available for sale securities	**0.3**	3.7
Additions of property, plant and equipment	**(13.7)**	(11.2)
Additions of capitalized software	**(2.1)**	(3.1)
Net cash used in investing activities	**(19.7)**	(15.8)
Financing Activities		
Proceeds from exercise of stock options	**0.1**	
Increase in short-term debt		10.0
Payments on long-term debt		(9.8)
Payments on capital lease obligations	**(0.4)**	(0.8)
Net cash used in financing activities	**(0.3)**	(0.6)
Effect of exchange rate changes on cash and cash equivalents	**1.9**	(8.3)

Net increase in cash and cash equivalents	**3.7**	20.6
Cash and cash equivalents, beginning of year	**136.8**	95.0
Cash and cash equivalents, end of quarter	**$ 140.5**	$ 115.6

See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited).

AVIAT NETWORKS, INC. (FORMERLY HARRIS STRATEX NETWORKS, INC.)
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)
April 2, 2010

Note A Corporate Name Change, Basis of Presentation and Nature of Operations

On January 28, 2010, Harris Stratex Networks, Inc. changed its name to Aviat Networks, Inc. (we, us, and our) to more effectively reflect our business and communicate our brand identity to customers. Additionally, we changed our corporate name to comply with the termination of the Harris Corporation (Harris) trademark licensing agreement resulting from the spin-off by Harris of its interest in our stock to its shareholders in May 2009.

The accompanying condensed consolidated financial statements have been prepared by us, without an audit, in accordance with U.S. generally accepted accounting principles for interim financial information and with the rules and regulations of the Securities and Exchange Commission (SEC). Accordingly, they do not include all information and footnotes necessary for a complete presentation of financial position, results of operations and cash flows in conformity with U.S. generally accepted accounting principles. In the opinion of management, such interim financial statements reflect all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation of financial position, results of operations and cash flows for such periods.

The results for the quarter ended April 2, 2010 (the third quarter of fiscal 2010) are not necessarily indicative of the results that may be expected for the full fiscal year or any subsequent period. The balance sheet as of July 3, 2009 has been derived from the audited financial statements but does not include all of the information and footnotes required by U.S. generally accepted accounting principles for annual financial statements. We provide complete financial statements in our Annual Report on Form 10-K, which includes information and footnotes required by the rules and regulations of the SEC. The information included in this Quarterly Report on Form 10-Q (this Report) should be read in conjunction with the Management s Discussion and Analysis of Financial Condition and Results of Operations, and the Consolidated Financial Statements and accompanying Notes to Consolidated Financial Statements included in our Annual Report on Form 10-K for the fiscal year ended July 3, 2009 (Fiscal 2009 Form 10-K).

The preparation of financial statements in accordance with U.S. generally accepted accounting principles requires us to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates and assumptions.

Revenue Recognition We generate substantially all of our revenue from the sales or licensing of our microwave radio and wireless access systems, network management software, and professional services including installation and commissioning and training. Principal customers for our products and services include domestic and international wireless/mobile service providers, original equipment manufacturers, distributors, system integrators, as well as private network users such as public safety agencies, government institutions, and utility, pipeline, railroad and other industrial enterprises that operate broadband wireless networks. Our customers generally purchase a combination of our products and services as part of a multiple element arrangement. Our assessment of which revenue recognition guidance is appropriate to account for each element in an arrangement can involve significant judgment.

Revenue from product sales and services, other than from long-term contracts (which are discussed below), generally is recognized when persuasive evidence of an arrangement exists, delivery has occurred and title and risk of loss has transferred or services have been rendered, the fee is fixed or determinable and collectibility is reasonably assured. We often enter into multiple contractual agreements with the same customer. Such agreements are reviewed to determine whether they should be evaluated as one arrangement. As has been applied consistently in the preparation of our financial statements, we utilize a methodology whereby if an arrangement requires the delivery or performance of multiple deliverables or elements, we determine whether the individual deliverables represent separate units of accounting. We recognize the revenue associated with each unit of accounting separately. If sufficient evidence of fair value can be established for all the elements of an arrangement, we allocate revenue to each element in the arrangement based on the relative fair value of each element and recognize that allocated revenue when each element meets the criteria discussed above. However, we generally do not have sufficient evidence of fair value for all elements of our arrangements, but we generally do have sufficient evidence of the fair value of the undelivered elements in our arrangements. In these cases, we allocate revenue using the residual method in which we defer the fair value of the undelivered elements and allocate the remaining arrangement consideration to the delivered elements. If an arrangement involves the delivery of multiple items of the same elements that are only partially delivered at the end of a reporting period, we allocate revenue proportionately between the delivered and undelivered items.

Revenues related to long-term contracts for customized network solutions are recognized using the percentage-of-completion method. In using the percentage-of-completion method, we generally apply the cost-to-cost method of accounting where sales and profits are recorded based on the ratio of costs incurred to estimated total costs at completion. Contracts are combined when specific aggregation criteria are met including when the contracts are in substance an arrangement to perform a single project with a customer; the contracts are negotiated as a package in the same economic environment with an overall profit objective; the contracts require interrelated activities with common costs that cannot be separately identified with, or reasonably allocated to the elements, phases or units of output and the contracts are performed concurrently or in a continuous sequence under the same project management at the same location or at different locations in the same general vicinity. Recognition of profit on long-term contracts requires estimates of the total contract value, the total cost at completion and the measurement of progress towards completion. Significant judgment is required when estimating total contract costs and progress to completion on the arrangements as well as whether a loss is expected to be incurred on the contract. Amounts representing contract change orders, claims or other items are included in sales only when they can be reliably estimated and realization is probable. When adjustments in contract value or estimated costs are determined, any changes from prior estimates are reflected in earnings in the current period. Anticipated losses on contracts or programs in progress are charged to earnings when identified.

For revenue recognition from the sale of software or products which have software which is more than incidental to the product as a whole, the entire fee from the arrangement is allocated to each of the elements based on the individual element s fair value, which must be based on vendor specific objective evidence of the fair value (VSOE). If VSOE cannot be established for the undelivered elements of an arrangement, we defer revenue until the earlier of delivery, or fair value of the undelivered element exists, unless the undelivered element is a service, in which the entire arrangement fee is recognized ratably over the period during which the services are expected to be performed.

Royalty income is recognized on the basis of terms specified in the contractual agreements.

Revenue from product sales is generated predominately from the sales of products manufactured by us and by third party manufacturers with whom we have outsourced our manufacturing processes. In general, printed circuit assemblies, mechanical housings, and packaged modules are manufactured by contract manufacturing partners, with periodic business reviews of material levels and obsolescence. Product assembly, product test, complete system integration and system test may either be performed within our own facilities or at partner locations.

Revenue from services includes certain installation, extended warranty, customer support, consulting, training and education. It also can include certain revenue generated from the resale of equipment purchased on behalf of customers for installation service contracts we perform for customers. Such equipment may include towers, antennas, and other related materials.

Out of Period Adjustments During the closing of our fiscal year 2009 accounts, we determined the need for an out-of-period adjustment related to the calculation of our currency translation expense that affected our previously reported Cost of product sales in each of the first three quarters of fiscal 2009. As disclosed in Note T of the Fiscal 2009 Form 10-K, our previously filed quarterly reports on Form 10-Q during 2009 required an adjustment for cumulative currency translation expense, which we concluded did not have a material impact on the previously filed quarterly reports on Form 10-Q during fiscal 2009. We have corrected the amount of cumulative currency translation expense for comparable prior periods in fiscal 2009 included in this Quarterly Report on Form 10-Q. The impact of this translation adjustment increased Cost of product sales by $1.1 million, increased net loss per common share by $0.02 in the third quarter of fiscal 2009, increased Cost of product sales by $3.5 million and increased net loss per common share by $0.06 in the first three quarters of fiscal 2009.

During the closing of our books for the first quarter of fiscal 2010, we determined the need for an out-of-period adjustment in the classification of revenue on our Condensed Consolidated Statement of Operations between the line items of Revenue from services and Revenue from product sales and in the classification of cost of sales between Cost of services and Cost of product sales. This reclassification had no impact on gross margin. For the third quarter of fiscal 2009, the impact of this reclassification decreased Revenue from services by $0.7 million, increased Revenue from product sales by $0.7 million, decreased Cost of services by $0.5 million and increased Cost of product sales by $0.5 million. For the first three quarters of fiscal 2009, the impact of this reclassification decreased Revenue from services by $3.9 million, increased Revenue from product sales by $3.9 million, decreased Cost of services by $2.0 million and increased Cost of product sales by $2.0 million. We are correcting our fiscal 2009 reported amounts as we file our fiscal 2010 periodic reports.

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Reclassification Prior to May 27, 2009, Harris owned approximately 56% of our outstanding common stock. As such, Harris was our majority stockholder and a related party for financial reporting purposes. Effective May 27, 2009, Harris distributed its entire ownership of our common stock to its shareholders. Accordingly, effective with the first quarter of fiscal 2010, Harris ceased to be considered a related party for financial reporting purposes. We have reclassified all amounts previously disclosed as related party transactions with Harris on our Statements of Operations, Balance Sheets and Statements of Cash Flows to the appropriate line items in the current presentation.

For the third quarter and first three quarters of fiscal 2009, and as of April 3, 2009, these reclassifications from the previously disclosed line item to the current presentation included:

Condensed Consolidated Statement of Operations (third quarter and first three quarters of fiscal 2009):

Revenue from product sales with Harris to Revenue from product sales ($0.8 million and $2.7 million); Cost of product sales with Harris to Cost of product sales ($0.7 million and $2.6 million); Cost of sales billed from Harris to Cost of product sales ($0.4 million and $0.7 million); Selling and administrative expenses with Harris to Selling and administrative expenses ($1.2 million and $4.5 million)

Condensed Consolidated Balance Sheet as of April 3, 2009:

Current portion of long-term capital lease obligation to Harris of $0.8 million to Other accrued items; Due from Harris Corporation of $3.8 million to Other current assets; Long-term portion of capital lease obligation to Harris of $1.0 million to Restructuring and other long-term liabilities

Condensed Consolidated Statement of Cash Flows (first three quarters of fiscal 2009):

Changes in operating assets and liabilities, Due to Harris of $20.7 million to changes in Restructuring liabilities and other.

Nature of Operations We design, manufacture and sell a range of wireless networking products, solutions and services to mobile and fixed telephone service providers, private network operators, government agencies, transportation and utility companies, public safety agencies and broadcast system operators across the globe. Our products include broadband wireless access base stations and customer premises equipment based upon the IEEE 802.16d-2004 and 16e-2005 standards for fixed and mobile WiMAX, point-to-point digital microwave radio systems for access, backhaul, trunking and license-exempt applications, supporting new network deployments, network expansion, and capacity upgrades.

Note B Accounting Changes and Recent Accounting Pronouncements

Initial Application of Accounting Standards

In the first quarter of fiscal 2010, we adopted the following accounting standards, none of which had a material impact on our financial position, results of operations or cash flows:

The Financial Accounting Standards Board (FASB) Accounting Standards Codification(tm) (Codification), which is now the source of authoritative U.S. generally accepted accounting principles (GAAP) recognized by the FASB to be applied for financial statements issued for periods ending after September 2009. Additionally, we are using the new guidelines prescribed by the Codification when referring to GAAP, including the elimination of pre-Codification GAAP references unless accompanied by Codification GAAP references.

The accounting standard deferring the effective date of the fair value measurement standard for disclosures related to nonfinancial assets and nonfinancial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis. See *Note M Fair Value Measurements of Financial Assets and Financial Liabilities* in these Notes to Condensed Consolidated Financial Statements for fair value disclosures required by this standard.

The accounting standard requiring interim disclosures about fair value of financial instruments, which extends the annual disclosure requirements about fair value of financial instruments to interim reporting periods. See *Note M Fair Value Measurements of Financial Assets and Financial Liabilities* in these Notes to Condensed Consolidated Financial Statements for fair value disclosures required by this standard.

The accounting standard for determining whether instruments granted in share-based payment transactions are participating securities. There was no material change to our calculations of basic and diluted weighted average shares outstanding for prior periods.

The accounting standards for accounting for business combinations, which significantly change the accounting and reporting requirements related to business combinations, including the recognition of acquisition-related transaction and post-acquisition restructuring costs in our results of operations as incurred. While the adoption of these standards did not have a material impact on our financial position, results of operations or cash flows directly in the first quarter of fiscal 2010, it is expected to have a significant effect on the accounting for any future acquisitions we make.

Accounting Standards Issued But Not Yet Effective

In October 2009, the FASB issued two new accounting standards updates that:

Revise accounting and reporting requirements for arrangements with multiple deliverables. This update allows the use of an estimated selling price to determine the selling price of a deliverable in cases where neither vendor-specific objective evidence nor third-party evidence is available, which is expected to increase the ability for entities to separate deliverables in multiple-deliverable arrangements and, accordingly, to decrease the amount of revenue deferred in these cases. Additionally, this update requires the total selling price of a multiple-deliverable arrangement to be allocated at the inception of the arrangement to all deliverables based on relative selling prices.

Clarify which revenue allocation and measurement guidance should be used for arrangements that contain both tangible products and software, in cases where the software is more than incidental to the tangible product as a whole. More specifically, if the software sold with or embedded within the tangible product is essential to the functionality of the tangible product, then this software, as well as undelivered related software elements are excluded from the scope of existing software revenue guidance, which is expected to decrease the amount of revenue deferred in these cases.

These two new accounting standards updates can be applied prospectively or retrospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010, which for us is our fiscal 2011, and must be adopted at the same time. Early adoption is permitted, and if these updates are adopted early in other than the first quarter of our fiscal year, then they must be applied retrospectively to the beginning of that fiscal year. We are currently evaluating the impact the adoption of these updates will have on our financial position, results of operations and cash flows.

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Note C Accumulated Other Comprehensive Loss and Comprehensive Loss

The changes in components of our accumulated other comprehensive loss during the three quarters ended April 2, 2010 and April 3, 2009 were as follows:

	Foreign Currency Translation	Hedging Derivatives	Short-Term Investments	Total Accumulated Other Comprehensive Income (Loss)
		(In millions)		
Balance as of July 3, 2009	**$ (4.4)**	**$ (0.4)**	**$**	**$ (4.8)**
Foreign currency translation gain	**2.6**			**2.6**
Net unrealized gain on hedging activities		**0.4**		**0.4**
Balance as of April 2, 2010	**$ (1.8)**	**$**	**$**	**$ (1.8)**
Balance as of June 27, 2008	$ 4.1	$ (0.3)	$	$ 3.8
Foreign currency translation loss	(16.3)			(16.3)
Net unrealized gain on hedging activities		0.7		0.7
Balance as of April 3, 2009	$ (12.2)	$ 0.4	$	$ (11.8)

Total comprehensive loss for the quarter and three quarters ended April 2, 2010 and April 3, 2009 was comprised of the following:

	Quarter Ended		Three Quarters Ended	
	April 2, 2010	April 3,	April 2,	April 3,