

ALTIGEN COMMUNICATIONS INC
Form 10-K
December 29, 2008

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-K

(Mark
One)

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

For the fiscal year ended September 30, 2008

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 000-27427

ALTIGEN COMMUNICATIONS, INC.

(Exact name of Registrant as specified in its charter)

DELAWARE
(State or other jurisdiction of
incorporation or organization)

94-3204299
(I.R.S. Employer
Identification Number)

4555 Cushing Parkway
Fremont, CA
(Address of principal executive offices)

94538
(Zip Code)

Registrant's telephone number, including area code: **(510) 252-9712**

Securities registered pursuant to Section 12(b) of the Act: **None**

Securities registered pursuant to Section 12(g) of the Act: **Common Stock, \$0.001 par value**
(Title of Class)

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

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

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

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subject to such filing requirements for the past 90 days. Yes No

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

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

Large accelerated
filer

Accelerated
filer

Non-accelerated
filer

Smaller reporting
company

(Do not check if a
smaller reporting
company)

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

The aggregate market value of the common stock held by non-affiliates of the registrant was approximately \$21,839,445 as of March 31, 2008, based on the closing price of our common stock as reported on The NASDAQ Capital Market on such date. Shares of common stock held by each officer and director and by each person known to own 5% or more of our outstanding common stock have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes. As of March 31, 2008, there were 15,624,646 shares of our common stock issued and outstanding.

The number of shares outstanding of the registrant's common stock as of December 22, 2008 was 15,885,480.

DOCUMENTS INCORPORATED BY REFERENCE

Certain sections of AltiGen Communications, Inc.'s definitive Proxy Statement for the 2009 Annual Meeting of Stockholders to be held on February 9, 2009 are incorporated by reference in Part III of this Form 10-K to the extent stated herein.

ALTIGEN COMMUNICATIONS, INC.
Form 10-K for the Year Ended September 30, 2008
TABLE OF CONTENTS

	Page
PART I	
Item 1. Business	3
Item 1A. Risk Factors	14
Item 1B. Unresolved Staff Comments	23
Item 2. Properties	23
Item 3. Legal Proceedings	23
Item 4. Submission of Matters to a Vote of Security Holders	23
PART II	
Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	24
Item 6. Selected Financial Data	27
Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations	27
Item 7A. Quantitative and Qualitative Disclosures About Market Risk	41
Item 8. Financial Statements and Supplementary Data	42
Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure	42
Item 9A. Controls and Procedures	42
Item 9B. Other Information	43
PART III	
Item 10. Directors and Executive Officers of the Registrant	44
Item 11. Executive Compensation	44
Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	44
Item 13. Certain Relationships and Related Transactions	44
Item 14. Principal Accountant Fees and Services	45
PART IV	
Item 15. Exhibits and Financial Statement Schedules	45
SIGNATURES	72

Note About Forward-Looking Statements

Our disclosure and analysis in this Annual Report on Form 10-K contains some forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements give our current expectations or forecasts of future events. You can identify these statements by the fact that they do not relate strictly to historical or current facts. They use words such as "anticipate," "estimate," "expect," "project," "intend," "plan," "believe" and other words and terms of similar meaning in connection with any discussion of future operating or financial performance. These forward-looking statements rely on assumptions, estimates and predictions that could be inaccurate and that are subject to risks and uncertainties that could cause actual results to differ materially. Important factors that may cause our actual results to differ materially from expectations reflected in our forward-looking statements include those described in Item 1A. "Risk Factors." Forward-looking statements speak only as of the date of this report, and we undertake no obligation to update or revise such statements to reflect new circumstances or unanticipated events as they occur.

PART I

Item 1. Business

INTRODUCTION

Altigen Communications, Inc. (NASDAQ: ATGN) is a pioneer and market leader in Voice over Internet Protocol (VoIP) telephone systems and Unified Communications solutions. We design and manufacture advanced phone systems and call center products that use both the Internet and the public telephone network.

Altigen Communications, or Altigen, was founded by current CEO Gilbert Hu in 1994, and the first products began shipping in 1996. Our telephony products are primarily sold to small-to-medium sized businesses, multi-site businesses, corporate branch offices, call centers, credit unions and community banks.

Altigen's products enable an array of applications like VoIP phones and servers, voicemail, call recording, call activity reporting, and mobility solutions that take advantage of the convergence of voice and data communications to achieve cost reduction. Our systems are designed with an open architecture and are built on an industry standard platform. This adherence to widely-used standards allows our products to integrate with and leverage a company's existing technology investment.

Altigen's products are available from independent authorized resellers and strategic partners. Altigen's family of telephony solutions has been recognized for excellence with more than 40 industry awards since 1996.

We generated net revenue of \$18.9 million with a net loss of \$3.9 million during fiscal year 2008. As of September 30, 2008, we had an accumulated deficit of \$56.0 million. Net cash provided by operating activities was \$77,000 for fiscal year 2008.

Our principal executive offices are located at 4555 Cushing Parkway, Fremont, California 94538. Our telephone number is (510) 252-9712. We were incorporated in California in May 1994, and we reincorporated into Delaware in June 1999.

We maintain an Internet website at <http://www.altigen.com>. Our most recent annual report on Form 10-K and certain of our other filings with the Securities and Exchange Commission (SEC) are available through the Investor Relations section of our website. Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and other required filings and amendments to these filings are available on the SEC website at <http://www.sec.gov>, which can be reached from the Investor Relations section of our website. In addition, you may read and copy any

material we file with the SEC at the SEC's Public Reference Room at 450 Fifth Street, NW, Washington, DC 20549. You may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330.

INDUSTRY BACKGROUND

We focus on the small-to-medium sized businesses, multi-site businesses, corporate branch offices, and call centers.

Convergence of Voice and Data

Traditionally, businesses have supported two separate, incompatible networks to handle their communications needs. The first network has been the traditional telephone network, which relies on a technology called "circuit-switching." A circuit-switched network establishes and maintains a dedicated (i.e. not shared) line between calling parties for the duration of a call. The second type of network on which businesses have traditionally relied is a "packet-switched" network, such as an internal local area network or an external network, like the Internet, where voice, video, images or data is divided into small Internet protocol packets of information for transmission that are simultaneously combined with other unrelated packets of information and routed to a final destination where this process is reversed. Packet-switched networks are more efficient than the traditional circuit-switched telephone network, because network paths are not dedicated to a single user, but instead are available to be shared by all users. As a result, network capacity is allocated more efficiently. It is commonplace for networks installed today to be able to support both voice and data usage with Internet protocol packet-switching.

Most telecommunications systems do not address the needs of businesses that need to transmit voice communications over both traditional telephone networks and packet-switching networks. For example, businesses may wish to route internal calls over their existing voice network and route calls between offices over packet-switched networks, all using the same telecommunications system. We believe a significant opportunity exists to provide small-to-medium sized and mid-enterprise businesses with an integrated phone system that delivers the benefits of integrated, multi-function telecommunications systems using Internet protocol packet switching networks as well as traditional circuit-switched telephone networks.

THE ALTIGEN PRODUCT OFFERING

AltiGen's VoIP phone systems are designed with an open architecture, built on industry standard Intel-based servers, Session Initiation Protocol ("SIP") based platform, and Microsoft Windows-based applications. This adherence to widely-used standards allows our solutions to both integrate with and leverage a company's existing technology investment. AltiGen's award winning, integrated IP applications suite provides customers with a complete business communications solution. Voicemail, Unified Messaging, Automatic Call Distribution, Call Recording, Call Activity Reporting, and Mobility solutions take advantage of the convergence of voice and data communications to achieve superior business results.

The AltiGen phone systems work with digital, analog and internet protocol trunks, and internet protocol and analog telephone extensions. The systems can be configured with digital, analog or VoIP, or a combination of the three. By allowing the customer to choose what best fits their current and future requirement, we provide a practical and cost effective solution to future growth.

Each system includes a comprehensive voicemail system with over 2,500 hours of storage, 255 auto attendant menus with unlimited levels, automatic call distribution, call detail reporting, call recording on demand, meet-me conference bridges, and a standard PBX (Private Branch Exchange) functionality. A PBX is a telephone system within an enterprise that switches calls between enterprise users on local lines while allowing all users to share a certain number of external telephone lines. Additionally, the

system provides intuitive and easy to use system administration software to allow for customer self-administration or remote administration by our authorized reseller partners.

AltiGen phone systems can be implemented for businesses requiring as few as eight extensions and supporting up to 1000 users per individual system. Individual systems can be affordably scaled to customer needs, and multiple systems may be networked together for greater expansion. These networked systems can be at a single site, a campus environment or multiple locations throughout the world using Internet protocol technology to link them. AltiGen phone systems allow affordable entry point while maintaining logical system growth.

For customers with more advanced requirements, we provide AltiContact Manager. The product is available as a software upgrade to an existing MAXCommunications Server System (MAXCS System). For additional information regarding MAXCS System, see the Product discussion section of this report. This product is capable of skills-based routing, priority queuing, centralized call recording and advanced monitoring and reporting. This capability may be added on a per agent/supervisor basis as the customer grows. This allows a smaller business or branch office to enjoy the same capability as a large professional call center organization. If a customer has more than one location, call center calls can automatically be routed to other locations based on conditions the customer chooses.

Key features of our phone systems include:

Scalability. AltiGen's software based MAXCS 6.0 softswitch architecture was designed to scale in both size and capability to meet the evolving needs of the small and medium-sized business (SMB) market. As a software-based system, AltiGen can rapidly deploy new features to our customers without requiring expensive hardware upgrades.

Native Microsoft Exchange Server Integration. MAXCS 6.0 fully supports native integration into Microsoft Exchange Server 2007 to unlock the embedded Unified Messaging capabilities of Exchange. As the "Voice of Microsoft Exchange", mutual Microsoft and AltiGen customers now have voice access to e-mails, calendar events, and personal and global company contact information via Text-to-Speech services.

Measurable Information to Ensure Best Business Practices. We provide a complete view into individual and group performance. The amount, type and duration of calls can be tracked and analyzed. An individual can record a call for later review, or a company can centrally record all or a percentage of calls for quality control.

Reduced Administration Costs. Our easy to use self administration software allows customers to manage their own telephone system. This reduces or eliminates ongoing operating cost of any business telephone system typically referred to as adds, moves and changes. AltiGen phone systems allow administrators to perform many of these tasks on site or remotely without assistance from third parties.

Lower Toll Costs. By routing voice over data networks, our systems reduce toll charges associated with long-distance calls between locations. Using our products, businesses can send and receive voice communications over the Internet or a private data network.

Unified Company Locations. For companies with AltiGen systems in multiple locations, we provide a seamless dialing plan. Customers calling into one location can automatically be routed to the correct group or individual. This allows a multi-site business to operate under a unified dialing plan and allows users in different sites to operate as if they were supported by a single system rather than an individual system for each location.

Survivability Options. Our systems allow practical and cost efficient options for disaster recovery planning. Redundant system hard drives allow all voicemail and configuration information to be copied to a spare hard drive. The system allows nightly backup to another network drive. If

weather or other problems prevent employees from reaching the office, ExtensionAnywhere, One Number Access and VoIP telephones can be utilized to keep operations running. We provide multiple options based upon what best fits the customer environment.

Innovative Desktop Productivity Software. Our systems provide desktop software applications to increase user productivity. Call control, changes in extension configuration and the ability to view and manage voicemail messages improve an employee's ability to process calls. In addition, we provide software for group supervisors, agents, system administrators and operators. Applications are centrally upgraded from the phone system to allow for quick and efficient deployment.

Integration with Customer Relationship Management Software. The MAXCommunicator and MAXCommunicator, Agent Edition desktop interface provides automatic contact record retrieval and "screen pops" of contact records to a user's desktop. Microsoft Outlook users can type in a name to automatically retrieve telephone numbers and click and dial from an integrated contact record directory. We provide built-in integration with other Microsoft software applications like Microsoft Outlook and Microsoft Exchange.

Ease of Installation, Use and Maintenance. AltiGen phone systems allow easy installation and system maintenance. Administrators can manage call routing, extension management, voice messaging, email and Internet features of our products through a single AltiWare administrator interface. By using industry standards we believe that AltiGen systems make it easier for resellers and end-user customers to implement and maintain systems.

Improved Customer Service Capabilities. AltiGen phone systems provide integrated call center functionality. For more advanced call center or centralized call recording requirements, we offer the AltiContact Manager software application. Both contact center applications are designed to enhance our customers' communications with their customers by employing comprehensive contact center and call center routing, reporting and recording technologies.

Integrated Centralized Call Recording. Voice calls can be recorded on demand by employees, agents and supervisors or automatically centrally recorded by the phone system. Traditional phone systems require a separate system to be tied to a PBX to centrally record calls. Modular feature licensing allows businesses to add capabilities on a per-feature or per-user basis offering a reduced up-front investment.

True Employee Mobility. We provide flexible and useable mobility options while retaining accountability. We provide several powerful options. ExtensionAnywhere allows any phone with a direct telephone number to be enabled as a live extension on the system. Call handling, call transfer, conferencing and voicemail capability are retained. Our "One Number Access" feature allows the system to search and then transfer a call at up to four numbers. For remote employees, we offer a VoIP telephone to connect to an employee's high speed Internet access. Our mobility options are flexible and simple to use.

PRODUCTS

The following is a list of our products that are material to our current operations from a financial standpoint:

Product	Description
MAXCS	MAXCS server software consists of a comprehensive suite of software applications to provide a high value, all-in-one solution. The systems include software and licensing necessary to support analog and VoIP telephones, operator software, and desktop call control software for each extension on the system. By providing a bundled approach, we maintain quality and reliability while providing for easy deployment. The platforms are scalable, and are packaged according to the size of the customer.
AltiContact Manager	AltiContact Manager is available as a software upgrade to an existing AltiGen phone system. This product is capable of skills-based routing, priority queuing, centralized call recording and advanced monitoring and reporting. This capability may be added on a per agent/supervisor basis as a company's needs grow. This allows a smaller business or branch office to enjoy the same capability as a larger organization with a professional call center. If a company has more than one location, calls to call centers can automatically be routed to other locations based on conditions the customer chooses.
AltiTouch 510 Analog Telephone	The AltiTouch 510 telephone is an executive level analog phone with a high quality speaker, a large (7.4 square inch) backlit LCD display with adjustable viewing angle, and LED voicemail waiting indicator. One-touch buttons provide access to features and call control including: volume, mute, voicemail, voice mail greeting management, do not disturb, intercom, headset answering, conference, hold, transfer, redial, call release, speed dial, call directory, extension management, line pickup, account codes and much more.
IP710 Voice over IP Telephone	The IP710 is a fully featured SIP-compatible, IP telephone designed to empower the user. Bringing stylish form and functionality to the desktop, the IP710 makes sophisticated features simple and intuitive to use. Users have single button access to voicemail, activity/presence selection, voicemail greeting selections, call recording, call conferencing, call transferring, and even placing calls to employees in other countries. Our IP710 Telephone was recognized in Internet Telephony Magazine as Product of Year for 2005.
IP705 Voice over IP Telephone	The IP705 provides a subset of the flagship IP710 VoIP telephone's features while offering the same level of voice quality at a reduced price. The IP705 was recognized as a 2006 Product of the Year by Internet Telephony Magazine.

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Product	Description
MAXCommunicator	MAXCommunicator is a Windows-based desktop application that provides call control and visual voice mail management to the desktop. It allows users to receive and place calls, listen to voicemail messages, identify the caller phone number and manage extension configuration. MAXCommunicator is standard with all AltiGen systems.
MAXCommunicator, Agent Edition	MAXCommunicator, Agent Edition is a Windows-based desktop application to bring call control and workgroup information to call center agents. Users can view a call queue, monitor work group status, check caller identification, measure performance, review log-on history, receive and place calls and listen to and manage voicemail messages.
MAXCommunicator, Supervisor Edition	MAXCommunicator, Supervisor Edition is a Windows-based desktop application for call center supervisors. The application allows a call center or workgroup supervisor to effectively manage a workgroup. MAXCommunicator, Supervisor Edition provides four major real time module views for workgroup management: agent status, agent statistics, group statistics, and queue status with a quality of services capability. MAXCommunicator, Supervisor Edition allows coaching, silent monitoring of agents with barge-in call participation and call recording functionality.
Triton IP Board	The Triton IP Board is a microprocessor-controlled board supporting VoIP communications. This allows voice conversations to be carried over public and private data networks that support Internet protocol. The Triton IP Board is a 12-port board that can be software configured to 30 ports. The Triton IP Board can be used for Internet protocol trunks connecting multiple networked MAXCS systems or to support VoIP telephone extensions and VoIP agent extensions.
Triton T1, E1, T1/PRI Board	The Triton T1, E1, T1/PRI Board is a microprocessor-controlled board that allows MAXCS systems to connect to T1, E1 or T1/PRI digital high-capacity central office telephone lines. This board can be configured with software to support provisioning for T1, E1 or T1/PRI communication protocols.
Triton Trunk Board	The Triton Trunk Board is an 8 or 12 port, microprocessor-controlled board that allows MAXCS systems to connect to analog central office telephone lines. This allows outbound and inbound calls to be carried over traditional analog central office telephone lines.
Triton Extension Board	The Triton Extension Board is a 12 port, microprocessor-controlled board that allows MAXCS systems to support 12 analog telephone extensions with each Triton Extension Board.
Triton Conference Board	The Triton Conference Board allows up to 30 simultaneous callers per conference and includes a scheduling application to control access and attendees.

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Product	Description
MAX 4x4xT1 Access Board	The MAX 4x4xT1 Access Board is a microprocessor-controlled board that allows the MAX1000 phone system to connect to four analog trunk lines, four analog telephone extensions, and one (1) T1/E1/PRI digital central office telephone line.
MAX 4x8 Access Board	The MAX 4x8 Access Board is a microprocessor-controlled board that allows the MAX1000 phone system to connect to four analog trunk lines and eight analog telephone extensions.
MAX 8x4 Access Board	The MAX 8x4 Access Board is a microprocessor-controlled board that allows the MAX1000 phone system to connect to eight analog trunk lines and four analog telephone extension.
MAX 0x12 Access Board	The MAX 0x12 Access Board is a microprocessor-controlled board that allows the MAX1000 phone system to connect twelve analog telephone extensions.

AltiGen Hardware and Firmware

We have developed a single base circuit board with high performance digital signal processing technology, which means that the circuit board has an integrated computer built on it that can run special, high-speed software programs, called firmware. Firmware can receive, send and modify digital information for communications with network services. Our digital signal processing boards, Triton and MAX are designed to allow us to create different circuit boards to meet many communication requirements by simply adding a few hardware and/or software components to the basic board. For example, the Triton digital signal processing board can become a T1, E1 or Integrated Services Digital Network communication circuit board or a circuit board supporting VoIP with simple changes in on-board software and, in some cases, new circuits.

This modular design not only enables us to provide new capabilities, but we also believe that it enables our products to achieve a high degree of reliability and cost reduction since the underlying technology is consistent across our products.

AltiGen Modular Software

Our software products are based on modular software components similar to the concept described above for our hardware and firmware. The service provider layer of software is composed of separate software components, each of which communicates with a hardware circuit board within the AltiGen phone system. The middleware layer interacts with all the service providers in the system and manages their resources. This middleware layer communicates with the hardware and allows application programs to provide specific features. The application program layer consists of components that implement the application logic, such as voicemail and auto attendant menus. These applications do not depend on any particular hardware integration.

We believe that the layered architectural structure of our MAXCS products provides important benefits:

New features can be developed without changing hardware.

Development time is generally shorter.

New hardware and software features can be added to installed systems.

Changing one component in the system does not require other components to be changed.

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The following table sets forth percentages of net revenue by product type with respect to such revenue for the periods indicated:

	Fiscal Year Ended September 30,		
	2008	2007	2006
Hardware(1)	86%	91%	92%
Software	14%	9%	8%
Total	100%	100%	100%

(1)

Our hardware revenue includes service support revenue generated primarily from our service support programs starting in September 2007. During fiscal years 2008, 2007 and 2006, revenue generated from these service support programs accounted for less than 10% of our total revenue.

MARKETING, SALES AND CUSTOMER SUPPORT

Marketing

Our marketing efforts currently focus on increasing demand for our products in the Americas, Europe and Asia Pacific. We are working to increase market awareness of our technology and demand for our products in the small-to-medium sized business and call center markets through public relations, print, email and web campaigns.

To assist our distributors, dealers and strategic partners, we provide market development funds, marketing tools and technical and sales training developed specifically for our products. We expect that these programs will allow us to leverage the expertise and contacts of the local and regional reseller channels to create strong lead generation.

Sales

Our sales organization continues to grow. In the United States, in fiscal 2008, we added additional channel sales managers, strategic accounts managers, and business development and marketing personnel. In addition, we added new resellers and a distribution partner.

We are organized and operate as two operating segments, the Americas and International. The Americas segment is comprised of the United States, Canada, Mexico, Central America and the Caribbean. The International segment is comprised of China, the United Kingdom and Norway.

The following table sets forth percentages of net revenue by geographic region with respect to such revenue for the periods indicated:

	Fiscal Year Ended September 30,		
	2008	2007	2006
Americas	87%	90%	90%
International	13%	10%	10%
Total	100%	100%	100%

We currently have sales and support staff in more than 13 locations in the United States. Our inside sales force answers incoming calls from end users and refers new leads to a qualified dealer near each end user's location. The inside sales force is also responsible for account management of our smaller resellers. Our outside sales force, which is primarily based in the Americas, includes regional

sales managers and technology solutions managers who work with our larger resellers and recruit new reseller partners. In fiscal 2008, we continued our expansion to a more scalable reseller community by signing on an increasing number of resellers that currently sell traditional and Internet protocol telephone systems manufactured by companies such as Avaya Communications (Avaya), 3Com Corporation (3Com), Nortel Networks Inc., (Nortel) and NEC Corporation (NEC).

Customers

Our customers are primarily distributors and resellers who sell our products to end-users. We have distribution agreements with AltiSys, Synnex and Jenne in the Americas. Our agreements with AltiSys and Synnex have initial terms of one year and our agreement with Jenne has an initial term of two years. These agreements are renewed automatically for additional one year terms, provided that each party shall have the right to terminate the agreement for convenience upon ninety (90) days' written notice prior to the end of the initial term or any subsequent term of the agreement. In addition, our agreements with AltiSys, Synnex and Jenne also provide for termination, with or without cause, by either party upon 30 days' written notice to the other party without penalty, or upon insolvency or bankruptcy. For a period of 60 days' following termination of the agreement, AltiSys, Synnex and Jenne may distribute any products in their possession at the time of termination or, at their option, return any products to us that are in their inventories. Upon termination of the distribution agreement, all outstanding invoices for the products will become due and payable within 30 days' of the termination. In April 2008, we terminated our distribution agreement with Graybar. This termination of our relationship with Graybar did not have a material impact on our business.

The following table sets forth our net revenue by customers that individually accounted for more than 10% of our revenue for the periods indicated:

	Fiscal Year Ended September 30,		
	2008	2007	2006
AltiSys	12%	16%	15%
Synnex	34%	50%	55%
Jenne(1)	12%		
Graybar(2)		15%	14%
Total	58%	81%	84%

(1) We did not generate revenue from Jenne during fiscal years ended 2007 and 2006.

(2) During fiscal year ended September 30, 2008, revenue generated from Graybar was less than 10% of our total revenue.

We also have over 200 authorized resellers who sell our products directly to a broad range of end-users. We review our resellers' performance quarterly and discontinue distribution for those who do not meet our revenue or technical standards.

Customer Support

We believe that consistent, high-quality service and support are key factors in attracting and retaining customers. Our customer support groups, located in California, Texas, Colorado, Minnesota and Shanghai, China coordinate service and technical support of our products and provide service twenty-four hours a day, seven days a week. Our support personnel assist our distributors and resellers in resolving installation and support issues that arise from their sales to end users and also provide limited support to end-users to supplement dealer support. Resellers and end-user customers can also access technical information and receive technical support through our web site.

RESEARCH AND DEVELOPMENT

The market for our products is characterized by rapidly changing technology, evolving industry standards and frequent product introductions. We believe that our future success depends in large part upon our ability to continue to enhance the functionality and uses of our core technology. We intend to extend the functionality and uses of our hardware and software technology and develop new products by continuing to invest in research and development.

We are currently developing enhancements to our products to provide greater functionality and increased capacity that we expect will enable us to enhance our position in the Internet protocol phone system market space, enter new geographical markets, and allow us to continue to penetrate the call center market.

We currently conduct the majority of our product development in-house. We also use a small number of independent contractors to assist with certain product development and testing activities. We intend to continue working with our strategic partners to enhance our products. As of September 30, 2008, we employed 54 individuals in engineering, research and development and support.

During fiscal years 2008, 2007, and 2006, our research and development expense was approximately \$4.2 million, \$3.4 million, and \$3.7 million, respectively.

COMPETITION

The markets for our products are intensely competitive, continually evolving and subject to changing technologies. We currently compete with Internet protocol and Internet protocol-enabled telecommunications systems, such as Avaya, 3Com, ShoreTel, and Cisco Systems, Inc. Many of our competitors are substantially larger than us and have significantly greater name recognition, financial, sales and marketing, technical, customer support, manufacturing and other resources. These competitors also may have more established distribution channels and stronger relationships with local, long distance and Internet service providers. These competitors may be able to respond more rapidly to new or emerging technologies and changes in customer requirements or to devote greater resources to the development, promotion and sale of their products.

These competitors may enter our existing or future markets with products that may be less expensive, that may provide higher performance or additional features or that may be introduced more quickly than our products. In fiscal 2008, we believe that we continued to be both feature and price competitive. Additionally, we believe we provide a low ongoing cost of ownership. We believe that our principal competitive advantages include:

System designed for small-to-medium sized business budgets;

Ability to reduce communications costs;

Ease of system manageability;

Ease of use;

Simple deployment in single and multi-site implementations;

Ability to achieve rapid product development;

Experience in service and technical support of Internet protocol telephony;

Complete call center application now standard with all MAXCS systems;

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Decentralized voice processing support for advanced and integrated telephony application;

Innovative mobility capabilities supporting mobile telephone devices such as the telephone system extensions; and

Reliable redundant configurations supported.

INTELLECTUAL PROPERTY

We generally rely upon patent, copyright, trademark and trade secret laws to protect and maintain our proprietary rights for our technology and products. As of September 30, 2008, we have been issued three registered trademarks, "AltiGen", "AltiServ" and "Zoomerang". In addition, the AltiGen logo is a trademark of ours in the United States and other jurisdictions. All other trademarks and trade names used in this Form 10-K are the property of their respective owners.

We have filed several U.S. patent applications relating to various aspects of our client and server software, mixed-media communications and computer telephony. As of September 30, 2008, we have been issued sixteen U.S. patents. We expect to continue to file patent applications to protect our technology and products. We cannot be sure that our patent applications will result in the issuance of patents, or that any issued patents will provide commercially significant protection for our technology.

MANUFACTURING AND ASSEMBLY

Our manufacturing operations consist of two phases. In the first phase, we send out components of our products to a third party assembler. The third party assembler auto-inserts the components into the printed circuit boards. In the second phase, we insert the assembled circuit boards into the burn-in process for a minimum of two weeks and after that we perform the final test of the circuit boards. In fiscal year 2008, we engaged All Quality Services in Fremont, California and ISIS Surface Mounting, Inc. in San Jose, California as our third party assemblers. During fiscal 2008, four suppliers, Advantech Corporation, BCM Communications, Inc., Fanstel Corporation, Avnet Electronics and AAEON Electronics, Inc., provided us with approximately 87% of our hardware product components. We purchase fully-assembled chassis from Advantech Corporation, Analog phones from Fanstel Corporation, Internet protocol phones from BCM Communications, Inc., single board computers for our MAX product from AAEON Electronics, Inc. and raw material components from Avnet Electronics. As of September 30, 2008, our in-house manufacturing operations occupied approximately 7,000 square feet of our corporate headquarters in Fremont, California.

We test our products after the assembly process using internally developed product assurance testing procedures, which include visual inspection, functional testing and final systems testing. Although we generally use standard components for our products and try to maintain alternative sources of supply, we purchase some key components from sole source suppliers for which alternative sources are not currently available. We incorporate the following sole-sourced components in our products:

Zarlink Corporation chips are included in all of our boards and are the means by which our boards communicate with each other to enable our products to function correctly.

Texas Instruments' digital signal processor ("DSP") chips are included in our Triton family of boards. The DSP chip is designed to perform the mathematics, data compression and other tasks required to manipulate voice communications that are routed through our products.

Xilinx, Inc provides chips for our Triton family of boards which allow our boards to work with digital communications lines.

Infineon Technologies provides chips for our Triton Analog product line which allow our board to work with analog communications lines.

PMC Sierra, Inc. provides chips for our Triton Digital product line which allow our board to work with digital communications lines.

Advantech Corporation provides the chassis for our MAXCS Office products based on our specifications.

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BCM Communications, Inc. manufactures our Internet protocol phone loaded with customized firmware to work with our system.

Fanstel Corporation manufactures our analog phone loaded with customized firmware to work with our system.

Chiah Jyh Industrial Co. manufactures the chassis for our MAX products.

AAEON Electronics, Inc. manufactures single board computers for our MAX products.

The loss of any key component supplier would adversely impact our business.

EMPLOYEES

As of September 30, 2008, we had 121 full-time employees, including 54 in research and development and support, 46 in marketing and sales, 8 in operations, and 13 in finance and administration. Of these full-time employees, 72 were located in the United States and 49 in China. Our future success will depend, in part, on our ability to continue to attract, retain and motivate highly qualified technical, marketing, engineering and management personnel.

Item 1A. Risk Factors

CERTAIN FACTORS AFFECTING BUSINESS, OPERATING RESULTS, AND FINANCIAL CONDITION

In addition to other information contained in this Form 10-K, investors should carefully consider the following factors that could adversely affect our business, financial condition and operating results as well as adversely affect the value of an investment in our common stock. This Annual Report on Form 10-K includes "forward-looking statements" within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act. All statements other than statements of historical fact are "forward-looking statements" for purposes of these provisions, including any statements regarding: projections of revenues, future research and development expenses, future selling, general and administrative expenses, other expenses, gross profit, gross margin, or other financial items; the plans and objectives of management for future operations; our exposure to interest rate risk; future economic conditions or performance; plans to focus on cost control; In some cases, forward-looking statements can be identified by the use of terminology such as "may," "will," "expects," "plans," "anticipates," "estimates," "potential," or "continue," or the negative thereof or other comparable terminology. Although we believe that the expectations reflected in the forward-looking statements contained herein are reasonable, there can be no assurance that such expectations or any of the forward-looking statements will prove to be correct, and actual results could differ materially from those projected or assumed in the forward-looking statements. Our future financial condition and results of operations, as well as any forward-looking statements, are subject to risks and uncertainties, including but not limited to the factors set forth below and elsewhere in this report. All forward-looking statements and reasons why results may differ included in this Annual Report are made as of the date hereof, and we assume no obligation to update any such forward-looking statement or reason why actual results may differ.

Risks Related to Our Business

Our business could be harmed by adverse global economic conditions in our target markets or reduced spending on information technology and telecommunication products.

Current uncertainty in global economic conditions pose a risk to the overall economy as consumers and businesses may defer purchases in response to tighter credit and negative financial news, which could negatively affect product demand and other related matters. Our business depends on the overall demand for information technology, and in particular for telecommunications systems. The market we

serve is emerging and the purchase of our products involves significant upfront expenditures. In addition, the purchase of our products can be discretionary and may involve a significant commitment of capital and other resources. Weak economic conditions in our target markets, or a reduction in information technology or telecommunications spending even if economic conditions improve, would likely adversely impact our business, operating results and financial condition in a number of ways, including longer sales cycles, lower prices for our products and reduced unit sales.

We have had a history of losses and may incur future losses, which may prevent us from attaining profitability.

We have had a history of operating losses since our inception and, as of September 30, 2008, we had an accumulated deficit of \$56.0 million. We may incur operating losses in the future, and these losses could be substantial and impact our ability to attain profitability. We do not expect to significantly increase expenditures for product development, general and administrative expenses, and sales and marketing expenses; however, if we cannot maintain current revenue or revenue growth, we will not achieve or sustain profitability or positive operating cash flows. Even if we achieve profitability and positive operating cash flows, we may not be able to sustain or increase profitability or positive operating cash flows on a quarterly or annual basis.

Our operating results vary, making future operating results difficult to predict.

Our quarterly and annual operating results have varied significantly in the past and likely will vary significantly in the future. A number of factors, many of which are beyond our control, have caused and may cause our operating results to vary, including:

our ability to respond effectively to competitive pricing pressures;

our ability to establish or increase market acceptance of our technology, products and systems;

our success in expanding our network of distributors, dealers and companies that buy our products in bulk, customize them for particular applications or customers, and resell them under their own names;

market acceptance of products and systems incorporating our technology and enhancements to our product applications on a timely basis;

our success in supporting our products and systems;

our sales cycle, which may vary substantially from customer to customer;

unfavorable changes in the prices and delivery of the components we purchase;

the size and timing of orders for our products, which may vary depending on the season, and the contractual terms of the orders;

the size and timing of our expenses, including operating expenses and expenses of developing new products and product enhancements;

deferrals of customer orders in anticipation of new products, services or product enhancements introduced by us or by our competitors; and

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our ability to attain and maintain production volumes and quality levels for our products.

Our future projected budgets and commitments are based in part on our expectations of future sales. If our sales do not meet expectations, it will be difficult for us to reduce our expenses quickly and, consequently, our operating results may suffer.

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Our dealers often require immediate shipment and installation of our products. As a result, we have historically operated with limited backlog, and our sales and operating results in any quarter primarily depend on orders booked and shipped during that quarter.

Any of the above factors could harm our business, financial condition and results of operations. We believe that period-to-period comparisons of our results of operations are not meaningful, and you should not rely upon them as indicators of our future performance.

Our market is highly competitive and we may not have the resources to adequately compete.

The market for our integrated, multifunction telecommunications systems is new, rapidly evolving and highly competitive. We expect competition to intensify in the future as existing competitors develop new products and new competitors enter the market. We believe that a critical component to success in this market is the ability to establish and maintain strong partner and customer relationships with a wide variety of domestic and international providers. If we fail to establish or maintain these relationships, we will be at a serious competitive disadvantage.

We face competition from companies providing traditional private telephone systems. Our principal competitors that produce these telephone systems are Avaya Communications, NEC and Nortel Networks. We also compete against providers of multi-function telecommunications systems, including 3Com Corporation, ShoreTel and Cisco Systems, Inc., as well as any number of future competitors. Many of our competitors are substantially larger than we are and have significantly greater name recognition, financial resources, sales and marketing teams, technical and customer support, manufacturing capabilities and other resources. These competitors also may have more established distribution channels and stronger relationships with service providers. These competitors may be able to respond more rapidly to new or emerging technologies and changes in customer requirements or to devote greater resources to the development, promotion and sale of their products. These competitors may enter our existing or future markets with products that may be less expensive, provide higher performance or additional features or be introduced earlier than our phone systems. We also expect that other companies may enter our market with better products and technologies. If any technology that is competing with ours is more reliable, faster, less expensive or has other advantages over our technology, then the demand for our products and services could decrease and harm our business.

We expect our competitors to continue to improve the performance of their current products and introduce new products or new technologies. If our competitors successfully introduce new products or enhance their existing products, our sales or market acceptance of our products and services could be reduced, price competition could be increased or our products could become obsolete. To remain competitive, therefore, we must continue to invest significant resources in research and development, sales and marketing and customer support. We may not have sufficient resources to make these investments or to make the technological advances necessary to be competitive, which in turn will cause our business to suffer.

We sell our products through dealers and distributors, which limits our ability to control the timing of our sales, and which makes it more difficult to predict our revenue.

We do not recognize revenue from the sale of our products to our distributors until these products are sold to either resellers or end-users. We have little control over the timing of product sales to resellers and end users. Our lack of control over the revenue that we recognize from our distributors' sales to resellers and end-users limits our ability to predict revenue for any given period. Our future projected budgets and commitments are based in part on our expectations of future sales. If our sales do not meet expectations, it will be difficult for us to reduce our expenses quickly, and consequently our operating results may suffer.

We rely on resellers to promote, sell, install and support our products, and their failure to do so or our inability to recruit or retain resellers may substantially reduce our sales and thus seriously harm our business.

We rely on resellers who can provide high quality sales and support services. As with our distributors, we compete with other telecommunications systems providers for our resellers' business as our resellers generally market competing products. If a reseller promotes a competitor's products to the detriment of our products or otherwise fails to market our products and services effectively, we could lose market share. In addition, the loss of a key reseller or the failure of resellers to provide adequate customer service could cause our business to suffer. If we do not properly train our resellers to sell, install and service our products, our business will suffer.

Software or hardware errors may seriously harm our business and damage our reputation, causing loss of customers and revenue.

Users expect telephone systems to provide a high level of reliability. Our products are inherently complex and may have undetected software or hardware errors. We have detected and may continue to detect errors and product defects in our installed base of products, new product releases and product upgrades. End users may install, maintain and use our products improperly or for purposes for which they were not designed. These problems may degrade or terminate the operation of our products, which could cause end users to lose telephone service, cause us to incur significant warranty and repair costs, damage our reputation and cause significant customer relations problems. Any significant delay in the commercial introduction of our products due to errors or defects, any design modifications required to correct these errors or defects or any negative effect on customer satisfaction as a result of errors or defects could seriously harm our business, financial condition and results of operations.

Any claims brought because of problems with our products or services could seriously harm our business, financial condition and results of operations. We currently offer a one-year hardware guarantee to end-users. If our products fail within the first year, we face replacement costs. Our insurance policies may not provide sufficient or any coverage should a claim be asserted. In addition, our introduction of products and systems with reliability, quality or compatibility problems could result in reduced revenue, uncollectible accounts receivable, delays in collecting accounts receivable, warranties and additional costs. Our customers, end users or employees could find errors in our products and systems after we have begun to sell them, resulting in product redevelopment costs and loss of, or delay in, their acceptance by the markets in which we compete. Further, we may experience significant product returns in the future. Any of these events could have a material adverse effect on our business, financial condition and results of operations.

Our market is subject to changing preferences; failure to keep up with these changes would result in our losing market share, thus seriously harming our business, financial condition and results of operations.

Our customers and end users expect frequent product introductions and have changing requirements for new products and features. In order to be competitive, we need to develop and market new products and product enhancements that respond to these changing requirements on a timely and cost-effective basis. Our failure to do so promptly and cost effectively would seriously harm our business, financial condition and results of operations. Also, introducing new products could require us to write-off existing inventory as obsolete, which could harm our results of operations.

We depend on attracting and retaining qualified personnel to maintain and expand our business; our failure to promptly attract and retain qualified personnel may seriously harm our business, financial condition and results of operations.

We depend, in large part, on our ability to attract and retain highly skilled personnel, particularly engineers and sales and marketing personnel. We need highly trained technical personnel to design and

support our server-based telecommunications systems. In addition, we need highly trained sales and marketing personnel to expand our marketing and sales operations in order to increase market awareness of our products and generate increased revenue. Competition for highly trained personnel is intense, especially in the San Francisco Bay Area where most of our operations are located. We cannot be certain that we will be successful in our recruitment and retention efforts. If we fail to attract or retain qualified personnel or suffer from delays in hiring required personnel, our business, financial condition and results of operations may be seriously harmed.

If we fail to establish and maintain proper and effective internal control over financial reporting, our operating results and our ability to operate our business could be harmed.

The Sarbanes-Oxley Act of 2002 requires, among other things, that we establish and maintain internal control over financial reporting and disclosure controls and procedures. In particular, under the current rules of the SEC, beginning with the year ended September 30, 2010, we must perform system and process evaluation and testing of our internal control over financial reporting to allow management to report on the effectiveness of our internal control over financial reporting, as required by Section 404 of the Sarbanes-Oxley Act. Our independent registered public accounting firm is also required to report on our internal control over financial reporting. We have incurred and we expect to continue to incur substantial accounting and auditing expense and expend significant management time in complying with the requirements of Section 404. If we are not able to comply with the requirements of Section 404 in a timely manner, or if we or our independent registered public accounting firm identify deficiencies in our internal control over financial reporting that are deemed to be material weaknesses, the market price of our stock could decline and we could be subject to investigations or sanctions by the SEC, The NASDAQ Capital Market, or NASDAQ, or other regulatory authorities or subject to litigation. To the extent any material weaknesses in our internal control over financial reporting are identified in the future, we could be required to expend significant management time and financial resources to correct such material weaknesses or to respond to any resulting regulatory investigations or proceedings.

If we do not manage our future growth effectively, our business will suffer.

We have experienced a period of rapid growth in our headcount and operation over the last two years; we have substantially increased our workforce and expanded our channel partner network and the number and size of enterprise customers implementing our systems. In the event our products obtain greater market acceptance, we may be required to expand our operations. This growth has placed, and anticipated future growth will place, a significant strain on our management, administrative, operational and financial infrastructure. Our success will depend in part upon our ability to manage this growth effectively. To manage the expected growth of our operations and personnel, we will need to continue to improve our operational, financial and management controls and our reporting systems and procedures. Failure to effectively manage growth could result in difficulty in filling enterprise customer orders, declines in product quality or customer satisfaction, increases in costs or other production and distribution difficulties, and any of these difficulties could adversely impact our business performance and results of operations.

Losing any of our key distributors would harm our business. We also need to establish and maintain relationships with additional distributors and original equipment manufacturers.

Sales through our three key distributors, Altisys, Synnex and Jenne, accounted for 58% of our net revenue in the fiscal year ended September 30, 2008. Our business and operating results will suffer if any one of these distributors does not continue distributing our products, fails to distribute the volume of our products that it currently distributes or fails to expand our customer base. We also need to establish and maintain relationships with additional distributors and original equipment manufacturers.

We may not be able to establish, or successfully manage, relationships with additional distribution partners. In addition, our agreements with distributors typically provide for termination by either party upon written notice to the other party. For example, our agreement with Synnex provides for termination, with or without cause, by either party upon 30 days' written notice to the other party, or upon insolvency or bankruptcy. Generally, these agreements are non-exclusive and distributors sell products that compete with ours. If we fail to establish or maintain relationships with distributors and original equipment manufacturers, our ability to increase or maintain our sales and our customer base will be substantially harmed.

We rely on sole-sourced components and third party technology and products; if these components are not available, our business may suffer.

We purchase technology that is incorporated into many of our products, including virtually all of our hardware products, from a single third-party supplier. We order sole-sourced components using purchase orders and do not have supply contracts for them. One sole-sourced component, a TI DSP chip, is particularly important to our business because it is included in virtually all of our hardware products. If we were unable to purchase an adequate supply of these sole-sourced components on a timely basis, we would be required to develop alternative products, which could entail qualifying an alternative source or redesigning our products based on different components. Our inability to obtain these sole-sourced components, especially the TI DSP chip, could significantly delay shipment of our products, which could have a negative effect on our business, financial condition and results of operations.

Compliance with changing regulations 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 National Market rules, are creating uncertainty for companies such as ours. These new or changed laws, regulations and standards are subject to varying interpretations in many cases due to their lack of specificity, and as a result, their application in practice may evolve over time as new guidance is provided by regulatory and governing bodies, which could result in continuing uncertainty regarding compliance matters and higher costs necessitated by ongoing revisions to disclosure and governance practices. As a result, our efforts to comply with evolving laws, regulations and standards have resulted in, and are likely to continue to result in, increased general and administrative expenses and a diversion of management time and attention from revenue-generating activities to compliance activities. In particular, our efforts to comply with Section 404 of the Sarbanes-Oxley Act of 2002 and the related regulations regarding our required assessment of our internal controls over financial reporting and beginning with the year ended September 30, 2010, our external auditor's audit of the effectiveness of our internal controls over financial reporting has required the commitment of significant financial and managerial resources. We expect these efforts to require the continued commitment of significant resources. Further, our board members, chief executive officer, and chief financial officer could face an increased risk of personal liability in connection with the performance of their duties. As a result, we may have difficulty attracting and retaining qualified board members and executive officers, which could harm our business. If our efforts to comply with new or changed laws, regulations and standards differ from the activities intended by regulatory or governing bodies due to ambiguities related to practice, our reputation may be harmed.

Our facility is vulnerable to damage from earthquakes and other natural disasters and other business interruptions; any such damage could seriously or completely impair our business.

We perform final assembly, software installation and testing of our products at our facility in Fremont, California. Our facility is located on or near known earthquake fault zones and may be subject to rolling electrical blackouts and is vulnerable to damage or interruption from fire, floods, earthquakes, power loss, telecommunications failures and similar events. If such a disaster or interruption occurs, our ability to perform final assembly, software installation and testing of our products at our facility would be seriously, if not completely, impaired. If we were unable to obtain an alternative place or way to perform these functions, our business, financial condition and results of operations would suffer. The insurance we maintain may not be adequate to cover our losses against fires, floods, earthquakes and general business interruptions.

Our strategy to outsource assembly and test functions in the future could delay delivery of products, decrease quality or increase costs.

We may begin to outsource a substantial amount of our product assembly and test functions. This outsourcing strategy involves certain risks, including the potential lack of adequate capacity and reduced control over delivery schedules, manufacturing yield, quality and costs. In the event that any significant subcontractors were to become unable or unwilling to continue to manufacture or test our products in the required volumes, we would have to identify and qualify acceptable replacements. Finding replacements could take time and we cannot be sure that additional sources would be available to us on a timely basis. Any delay or increase in costs in the assembly and testing of products by third-party subcontractors could seriously harm our business, financial condition and results of operations.

Our expansion in international markets has been slow and steady. However, our plan is to accelerate this growth rate and will involve new risks that our previous domestic operations have not prepared us to address; our failure to address these risks could harm our business, financial condition and results of operations.

For fiscal year 2008, approximately 13% of our net revenue came from customers outside of the Americas. We intend to expand our international sales and marketing efforts. Our efforts are subject to a variety of risks associated with conducting business internationally, any of which could seriously harm our business, financial condition and results of operations. These risks include:

tariffs, duties, price controls or other restrictions on foreign currencies or trade barriers, such as import or export licensing imposed by foreign countries, especially on technology;

potential adverse tax consequences, including restrictions on repatriation of earnings;

fluctuations in foreign currency exchange rates, which could make our products relatively more expensive in foreign markets; and

conflicting regulatory requirements in different countries that may require us to invest significant resources customizing our products for each country.

Any failure by us to protect our intellectual property could harm our business and competitive position.

Our success depends, to a certain extent, upon our proprietary technology. We currently rely on a combination of patent, trade secret, copyright and trademark law, together with non-disclosure and invention assignment agreements, to establish and protect the proprietary rights in the technology used in our products.

Although we have been issued sixteen patents and expect to continue to file patent applications, we are not certain that our patent applications will result in the issuance of patents, or that any patents issued will provide commercially significant protection of our technology. In addition, other individuals

or companies may independently develop substantially equivalent proprietary information not covered by the patents to which we own rights, may obtain access to our know-how or may claim to have issued patents that prevent the sale of one or more of our products. Also, it may be possible for third parties to obtain and use our proprietary information without our authorization. Further, the laws of some countries, such as those in Japan, one of our target markets, may not adequately protect our intellectual property or such protection may be uncertain. Our success also depends on trade secrets that cannot be patented and are difficult to protect. If we fail to protect our proprietary information effectively, or if third parties use our proprietary technology without authorization, our competitive position and business will suffer.

If we are unable to raise additional capital when needed, we may be unable to develop or enhance our products and services.

We may seek additional funding in the future. If we cannot raise funds on acceptable terms, we may be unable to develop or enhance our products and services, take advantage of future opportunities or respond to competitive pressures or unanticipated requirements. We also may be required to reduce operating costs through lay-offs or reduce our sales and marketing or research and development efforts. If we issue equity securities, stockholders may experience additional dilution or the new equity securities may have rights, preferences or privileges senior to those of our common stock.

We may face infringement issues that could harm our business by requiring us to license technology on unfavorable terms or temporarily or permanently cease sales of key products.

We may become parties to litigation in the normal course of our business. Litigation in general, and intellectual property and securities litigation in particular, can be expensive and disruptive to normal business operations. Moreover, the results of complex litigation are difficult to predict. We were previously a defendant in a patent infringement suit brought by Vertical Networks. On October 4, 2007, the parties entered into a stipulation dismissing the lawsuit in its entirety without prejudice. Consequently, Vertical Networks may reassert these or related claims in one or more separate proceedings. For additional information on this suit, see Item 3 "Legal Proceedings."

More generally, litigation related to these types of claims may require us to acquire licenses under third party patents that may not be available on acceptable terms, if at all. We believe that an increasing portion of our revenue in the future will come from sales of software applications for our hardware products. The software market traditionally has experienced widespread unauthorized reproduction of products in violation of developers' intellectual property rights. This activity is difficult to detect, and legal proceedings to enforce developers' intellectual property rights are often burdensome and involve a high degree of uncertainty and substantial costs.

Our products may not meet the legal standards required for their sale in some countries; if we cannot sell our products in these countries, our results of operations may be seriously harmed.

The United States and other countries in which we intend to sell our products have standards for safety and other certifications that must be met for our products to be legally sold in those countries. We have tried to design our products to meet the requirements of the countries where we sell or plan to sell them. We also have obtained or are trying to obtain the certifications that we believe are required to sell our products in these countries. We cannot, however, guarantee that our products meet all of these standards or that we will be able to obtain any certifications required. In addition, there is, and will likely continue to be, an increasing number of laws and regulations pertaining to the products we offer and may offer in the future. These laws or regulations may include, for example, more stringent safety standards, requirements for additional or more burdensome certifications or more stringent consumer protection laws.

If our products do not meet a country's standards or we do not receive the certifications required by a country's laws or regulations, then we may not be able to sell our products in that country. This inability to sell our products may seriously harm our results of operation by reducing our sales or requiring us to invest significant resources to conform our products to these standards.

Risks Related to the Industry

Integrated, multifunction telecommunications systems may not achieve widespread acceptance.

The market for integrated, multifunction telecommunications systems is relatively new and rapidly evolving. Businesses have invested substantial resources in the existing telecommunications infrastructure, including traditional private telephone systems, and may be unwilling to replace these systems in the near term or at all. Businesses also may be reluctant to adopt integrated, multifunction telecommunications systems because of their concern about the current limitations of data networks, including the Internet. For example, end users sometimes experience delays in receiving calls and reduced voice quality during calls when routing calls over data networks. Moreover, businesses that begin to route calls over the same networks that currently carry only their data also may experience these problems if the networks do not have sufficient capacity to carry all of these communications at the same time.

Evolving standards may delay our product introductions, increase our product development costs or cause end users to defer or cancel plans to purchase our products, any of which could adversely affect our business.

The standards in our market are still evolving. These standards are designed to ensure that integrated, multifunction telecommunications products from different manufacturers can operate together. Some of these standards are proposed by other participants in our market, including some of our competitors, and include proprietary technology. In recent years, these standards have changed, and new standards have been proposed, in response to developments in our market. Our failure to conform our products to existing or future standards may limit their acceptance by market participants. We may not anticipate which standards will achieve the broadest acceptance in our market in the future, and we may take a significant amount of time and expense to adapt our products to these standards. We also may have to pay additional royalties to developers of proprietary technologies that become standards in our market. These delays and expenses may seriously harm our results of operations. In addition, customers and users may defer or cancel plans to purchase our products due to concerns about the ability of our products to conform to existing standards or to adapt to new or changed standards, and this could seriously harm our results of operations.

Future regulation or legislation could harm our business or increase our cost of doing business.

The Federal Communications Commission (FCC) has submitted a report to Congress stating that it may regulate certain Internet services if it determines that such Internet services are functionally equivalent to conventional telecommunications services. The increasing growth of the voice over data network market and the popularity of supporting products and services, heighten the risk that national governments will seek to regulate the transmission of voice communications over networks such as the Internet. In addition, large telecommunications companies may devote substantial lobbying efforts to influence the regulation of this market so as to benefit their interests, which may be contrary to our interests. These regulations may include, for example, assessing access or settlement charges, imposing tariffs or imposing regulations based on encryption concerns or the characteristics and quality of products and services. In February 2004, the FCC found that an entirely Internet based voice over Internet protocol service was an unregulated information service. At the same time, the FCC began a broader proceeding to examine what its role should be in this new environment of increased consumer choice and what can be done to meet its role of safeguarding the public interest. Future laws, legal decisions or regulations, as well as changes in interpretations of existing laws and regulations, could

require us to expend significant resources to comply with them. In addition, these future events or changes may create uncertainty in our market that could reduce demand for our products.

Item 1B. Unresolved Staff Comments

Not applicable.

Item 2. Properties

We lease 32,000 square feet of space in Fremont, California in our headquarters for corporate administration, research and development, manufacturing and sales. The lease expires on February 21, 2009, and then on a month to month basis and under the same conditions until terminated by either party. Outside the United States, we lease approximately 9,400 square feet of a facility in Shanghai, China, where we conduct administration, research and development, sales and marketing, and another 1,600 square feet of a facility in Beijing, China to serve sales and marketing functions. We believe that our existing facilities both in the United States and China are adequate for our present needs in all material respects.

Item 3. Legal Proceedings

On September 6, 2002, Vertical Networks, Inc. filed suit against us in the United States District Court for the Northern District of California, alleging infringement of U.S. Patents Nos. 6,266,341, 6,289,025, 6,292,482, 6,389,009, and 6,396,849. On October 28, 2002, Vertical Networks amended its complaint to add allegations of infringement of U.S. Patents Nos. 5,617,418 and 5,687,174. Vertical Networks filed a second amended complaint on November 20, 2002 to identify products and/or activities that allegedly infringe the seven patents-in-suit. Vertical Networks' Complaint seeks an injunction against future patent infringement, an award of damages, including treble damages for alleged willful infringement, and attorneys' fees and costs. On December 9, 2002, we filed an answer and counterclaims for declaratory relief, and on December 26, 2002, Vertical Networks filed its reply to those counterclaims. On October 4, 2007, the parties entered into a stipulation dismissing the lawsuit in its entirety without prejudice.

From time to time, we may become party to litigation and subject to various routine claims and legal proceedings that arise in the ordinary course of our business. To date, these actions have not had a material adverse effect on our financial position, result of operations or cash flows. Although the results of litigation and claims cannot be predicted with certainty, we believe that the final outcome of such matters would not have a material adverse effect on our business, financial position, results of operation and cash flows.

Item 4. Submission of Matters to a Vote of Security Holders

No matters were submitted to a vote of security holders during the fourth quarter of the Company's fiscal year ended September 30, 2008.

PART II**Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities**

The information required by this item regarding equity compensation plans is incorporated by reference to the information set forth in Item 12 of this Annual Report on Form 10-K.

COMMON STOCK PRICE RANGE

From October 4, 1999, the date of our initial public offering, to June 11, 2002, our common stock was traded on the NASDAQ National Market under the symbol "ATGN". Since June 12, 2002, our common stock has traded on the NASDAQ Capital Market under the symbol "ATGN." The following table sets forth, for the periods indicated, the high and low closing prices of our common stock on the NASDAQ Capital Market. As of September 30, 2008, we had approximately 80 stockholders of record of our common stock. We have never declared or paid any cash dividends on our capital stock. We currently expect to retain future earnings, if any, to support operations and to finance the growth and development of our business. We do not expect to pay cash dividends in the foreseeable future.

	Fiscal 2008		Fiscal 2007	
	High	Low	High	Low
1st Quarter	\$1.64	\$1.27	\$1.70	\$1.51
2nd Quarter	\$1.66	\$1.36	\$1.98	\$1.50
3rd Quarter	\$1.56	\$1.15	\$1.97	\$1.62
4th Quarter	\$1.27	\$0.80	\$1.75	\$1.46

COMPANY STOCK PERFORMANCE

The following graph compares the cumulative total stockholder return data for our stock for the period beginning September 30, 2003 and ending on September 30, 2008 to the cumulative return over such period of (i) The NASDAQ National Market Composite Index and (ii) the NASDAQ Telecommunications Index. The graph assumes \$100 was invested on September 30, 2003 in our Common Stock and in each of the comparative indices, assuming the reinvestment of any dividends. Note that the historic stock price performance on the following graph is not necessarily indicative of future stock price performance.

COMPARISON OF 5 YEAR CUMULATIVE TOTAL RETURN*
Among AltiGen Communications, Inc., The NASDAQ Composite Index
and The NASDAQ Telecommunications Index

*\$100 invested on 9/30/03 in stock & index-including reinvestment of dividends.
Fiscal year ending September 30.

STOCK REPURCHASE PLAN

On October 23, 2007, our Board of Directors approved the repurchase of up to \$2.0 million of our common stock in the open market, which repurchases may be made from time to time at our management's discretion through November 14, 2008. When exercising such discretion, management will consider a variety of factors such as our stock price, general business and market conditions and other investment opportunities. The repurchase will be made in the open market and will be funded from available working capital. Under such authority, we repurchased 231,135 shares in fiscal 2008 at an aggregate cost of \$367,000. Current cash balances and the proceeds from stock option exercises and purchases in the Company's 1999 Employee Stock Purchase Plan have funded these stock repurchases. In November of 2008, the Board of Directors extended the repurchase program by another year to November 14, 2009 and the Company intends to continue repurchasing shares under this program over time depending upon price and share availability.

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Repurchases of our common stock under the latest Board of Directors' authorization is represented in the following table:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Shares Purchased as Part of Publicly Announced Program	Approximate Dollar Value of Shares that May Yet be Purchased as Part of the Program
November 1, 2007 through November 30, 2007	16,413	\$ 1.59	16,413	\$ 1,973,965
December 1, 2007 through December 31, 2007	92,965	1.60	92,965	1,825,685
February 1, 2008 through February 29, 2008	80,218	1.66	80,218	1,692,660
March 1, 2008 through March 31, 2008	23,919	1.61	23,919	1,654,084
August 1, 2008 through August 31, 2008	7,211	1.21	7,211	1,645,374
September 1, 2008 through September 30, 2008	10,409	1.16	10,409	1,633,338
Total	231,135	\$ 1.59	231,135	\$ 1,633,338

(1)

On November 19, 2007, AltiGen announced the implementation of a stock repurchase program whereby it may repurchase up to \$2.0 million of its outstanding Common Stock from time to time through November 14, 2008. On November 12, 2008, AltiGen announced the extension of the repurchase program by one (1) year to November 14, 2009.

Item 6. Selected Financial Data

This section presents selected historical financial data of AltiGen Communications, Inc. This section should be read carefully in conjunction with "Management's Discussion and Analysis of Financial Conditions and Results of Operations" and the consolidated financial statements included in this Form 10-K, including the notes to the consolidated financial statements. The selected data in this section is not intended to replace our consolidated financial statements.

	Fiscal Year Ended September 30,				
	2008	2007	2006	2005	2004
	(In thousands, except per share data)				
Consolidated Statements of Operations Data:					
Net revenue	\$ 18,897	\$ 17,888	\$ 17,896	\$ 15,441	\$ 14,842
Cost of revenue	8,059	8,123	8,082	6,592	5,607
Gross profit	10,838	9,765	9,814	8,849	9,235
Operating expenses:					
Research and development	4,216	3,373	3,740	3,496	3,288
Sales and marketing	7,552	5,277	4,353	3,943	4,130
General and administrative	3,322	2,497	2,058	1,946	1,894
Total operating expenses	15,090	11,147	10,151	9,385	9,312
Loss from operations	(4,252)	(1,382)	(337)	(536)	(77)
Equity in net income (loss) of investee	5	(4)	(36)	(12)	
Interest and other income, net	310	461	380	237	105
Net income (loss) before income taxes	(3,937)	(925)	7	(311)	28
Income taxes		(11)	(19)		
Net income (loss)	\$ (3,937)	\$ (936)	\$ (12)	\$ (311)	\$ 28
Basic and diluted net income (loss) per share	\$ (0.25)	\$ (0.06)	\$ (0.00)	\$ (0.02)	\$ 0.00
Weighted average shares used in computing					
basic net income (loss) per share	15,745	15,363	14,964	14,605	14,242
Weighted average shares used in computing					
diluted net income (loss) per share	15,745	15,363	14,964	14,605	15,725

	2008	2007	2006	2005	2004
	(In thousands)				
Consolidated Balance Sheets Data:					
Cash, cash equivalents and short-term investments	\$ 9,867	\$ 9,907	\$ 9,922	\$ 9,422	\$ 10,034
Working capital	8,687	11,551	11,027	10,133	10,314
Total assets	14,776	15,250	14,644	13,335	13,516
Accumulated deficit	(56,031)	(52,094)	(51,158)	(51,146)	(50,835)
Total stockholders' equity	9,297	12,345	11,837	10,718	10,669

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations**FORWARD-LOOKING INFORMATION**

This report contains certain forward-looking statements (within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended) and information relating to us that are based on the beliefs of our management as well as assumptions made by and information currently available to our management. Additional forward-

looking statements may be identified by the words "anticipate," "believe," "expect," "intend," "plan," or the negative of such terms, or similar expressions, as they relate to us or our management.

The forward-looking statements contained herein reflect our judgment as of the date of this report with respect to future events, the outcome of which is subject to certain risks that may have a significant impact on our business, operating results or financial condition. You are cautioned that these forward-looking statements are inherently uncertain. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results or outcomes may vary materially from those described herein. Although we believe that the expectations reflected in these forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. You should carefully review the cautionary statements contained in this Form 10-K, including the "Certain Factors Affecting Business, Operating Results and Financial Condition" above.

OVERVIEW

We are a pioneer and market leader in Internet protocol telephony systems for small-to-medium sized businesses. We design, manufacture and market next generation, Internet protocol phone systems and contact centers that use both the Internet and the public telephone network to take advantage of the convergence of voice and data communications. Unlike traditional proprietary phone systems, our systems are designed with open architecture and are built on an industry standard platform. This adherence to industry standards allows our products to play an important role in the small-to-medium sized business market by delivering phone systems that can integrate with other technologies and provide integrated voice and data solutions, which enables our customers to implement communication systems that have an increased return on investment. We generated net revenue of \$18.9 million, for a net loss of \$3.9 million, during fiscal year 2008. As of September 30, 2008, we had an accumulated deficit of \$56.0 million. Net cash provided by operating activities was \$77,000 for fiscal year 2008.

We derive our revenue from sales of our telephone systems. Product revenue is comprised of direct sales to end-users and resellers and sales to distributors. Revenue from product sales to end users and resellers are recognized upon shipment. We defer recognition of revenue for sales to distributors until they resell our products to their customers. Upon shipment, we also provide a reserve for the estimated cost that may be incurred for product warranty. Under our distribution contracts, a distributor has the right, in certain circumstances, to return products it determines are overstocked, so long as it provides an offsetting purchase order for products in an amount equal to or greater than the dollar value of the returned products. In addition, we provide distributors protection from subsequent price reductions.

Our cost of revenue consists of component and material costs, direct labor costs, provisions for excess and obsolete inventory, warranty costs and overhead related to the manufacturing of our products. Several factors that have affected and will continue to affect our revenue growth are the state of the economy, the market acceptance of our products, our ability to add new resellers and our ability to design, develop, and release new products. We engage third-party assemblers, which in fiscal year 2008 were All Quality Services in Fremont, California and ISIS Surface Mounting, Inc. in San Jose, California to insert the hardware components into the printed circuit board. We purchase fully-assembled chassis from Advantech Corporation, Analog phones from Fanstel Corporation, Internet protocol phones from BCM Communications, Inc., single board computers for our MAX product from AAEON Electronics, Inc. and raw material components from Avnet Electronics. We selected our manufacturing partners with the goals of ensuring a reliable supply of high-quality finished products and lowering per unit product costs as a result of manufacturing economies of scale. We cannot assure you that we will maintain the volumes required to realize these economies of scale or when or if such cost reductions will occur. The failure to obtain such cost reductions could materially adversely affect our gross margins and operating results.

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We continue to focus on developing enhancements to our current products to provide greater functionality and increased capabilities, based on our market research, customer feedback and our competitors' product offerings, as well as creating new product offerings to both enhance our position in our target market segment and enter new geographical markets. Additionally, we intend to continue selling our products to small- to medium-sized businesses, enterprise businesses, multisite businesses, corporate and branch offices and call centers. Also, we plan to continue to recruit additional resellers and distributors to focus on selling phone systems to our target customers. We believe that the adoption rate for this Internet telephony is much faster with small- to medium-sized businesses because many of these businesses have not yet made a significant investment for a traditional phone system. Also, we believe that small- to medium-sized businesses are looking for call center-type administration to increase the productivity and efficiency of their contacts with customers.

CRITICAL ACCOUNTING POLICIES

Revenue Recognition. Net sales consist primarily of revenue from direct sales to end-users, including resellers, and sales to distributors. We recognize revenue pursuant to SEC Staff Accounting Bulletin ("SAB") No. 104, Revenue Recognition, ("SAB No. 104"). Revenue from sales to end-users is recognized upon shipment, when risk of loss has passed to the customer, collection of the receivable is reasonably assured, persuasive evidence of an arrangement exists, and the sales price is fixed and determinable. We provide for estimated sales returns and allowances and warranty costs related to such sales at the time of shipment in accordance with SFAS No. 48, Revenue Recognition when Right of Return Exists ("SFAS No. 48"). Net revenue consists of product revenue reduced by estimated sales returns and allowances. Sales to distributors are made under terms allowing certain rights of return and protection against subsequent price declines on our products held by the distributors. Upon termination of such distribution agreements, any unsold products may be returned by the distributor for a full refund. These agreements may be canceled without cause for convenience following a specified notice period. As a result of the above provisions, we defer recognition of distributor revenue until such distributors resell our products to their customers. The amounts deferred as a result of this policy are reflected as "deferred revenue" in the accompanying consolidated balance sheets. The related cost of revenue is also deferred and reported in the consolidated balance sheets as inventory. Our total deferred revenue was \$2.5 million and \$565,000 as of September 30, 2008 and September 30, 2007, respectively. The \$1.9 million increase in deferred revenue in fiscal 2008 versus fiscal 2007 was primarily due to our service support plans, which added \$1.6 million to deferred revenue and an increase of \$335,000 in deferred channel revenue. The deferred channel revenue increase was due to the volume of products shipped to distribution as opposed to what was sold. We work closely with our distributors to monitor channel inventory levels and attempt to ensure that appropriate levels of products are available to resellers and end users.

Service Support Programs. In September 2007, we introduced our Software Assurance Program which provides our customers with the latest updates, new releases, and technical support for the applications they are licensed to use. In fiscal 2008, we initiated our Premier Service Plan, which includes software assurance and extended hardware warranty. These programs have an annual subscription and can range from one to three years. Sales from our service support programs are recorded as deferred revenue and recognized as revenue over the terms of their subscriptions. The total number of customers who have enrolled in these service programs at fiscal year end increased to more than 3,700 and of the total enrollments added over the course of the year, approximately 2,500 came from our existing customer base, which we see as validation of the value of our new product and service releases.

Software components are generally not sold separately from our hardware components. Software revenue consists of license revenue that is recognized upon delivery of the application products or features. We provide Software Assurance consisting primarily of the latest software updates, patches, new releases and technical support. In accordance with SOP 97-2, revenue earned on software

arrangements involving multiple elements is allocated to each element based upon the relative fair value of the elements. The revenue allocated on this element is recognized with the initial licensing fee on delivery of the software. This Software Assurance revenue is in addition to the initial license fee and is recognized over a period of one to three years. The estimated cost of providing Software Assurance during the arrangement is insignificant and unspecified upgrades and enhancements offered at no cost during Software Assurance arrangements have historically been, and are expected to continue to be, minimal and infrequent. All estimated costs of providing the services, including upgrades and enhancements, are spread over the life of the Software Assurance term.

Cash and Cash Equivalent. We consider all highly liquid investments purchased with an initial maturity of three months or less to be cash equivalents. Cash and cash equivalents are invested in various investment grade institutional money market accounts, bank term deposits, U.S. Agency securities and commercial paper. The Company's investment policy requires investments to be rated single-A or better. As further discussed in "Liquidity and Capital Resources," our cash and cash equivalents balance increased by \$3.4 million to \$9.4 million as of September 30, 2008. We ended the fourth quarter of fiscal year 2008 with positive cash flow from operations.

Short-Term Investment. The Company's policy is to invest in highly-rated securities with strong liquidity and requires investments to be rated single-A or better. Short-term investments are comprised of U.S. Agency securities, corporate bonds and notes and commercial paper. Short-term investments are highly liquid financial instruments with original maturities greater than three months but less than one year and are classified as "available-for-sale" investments. We classify our available-for-sale securities as current assets and report them at their fair value. Further, we recognize unrealized gains and losses related to these securities as an increase or reduction in shareholders' equity. We evaluate our available-for-sale securities for impairment quarterly. During fiscal year 2008, we did not record any impairment on outstanding securities.

Inventory. Inventory is stated at the lower of cost (first-in, first-out method) or market. Our inventory balance was \$1.5 million and \$1.6 million as of September 30, 2008 and September 30, 2007, respectively. We perform a detailed review of inventory each fiscal quarter, with consideration given to future customer demand for our products, obsolescence from rapidly changing technology, product development plans, and other factors. If future demand or market conditions for our products are less favorable than those projected by management, or if our estimates prove to be inaccurate due to unforeseen technological changes, we may be required to record additional inventory provision which would negatively affect gross margins in the period when the write-downs were recorded. In prior periods, we had established a reserve to write off excess inventory that management believed would not be sold. In fiscal year 2008, we disposed of fully-reserved inventory with a carrying value of zero and an original cost at \$1.5 million. We attribute this overall reduction in obsolete inventory to physically disposing of a portion of the reserved inventory. The disposal of such inventory had no material impact on our revenue, gross margins and net loss. For the year ended September 30, 2008, we recognized a provision of \$12,000 for excess and obsolete inventories as compared to \$96,000 for fiscal year ended September 30, 2007. Inventory allowance was \$850,000 and \$2.4 million as of September 30, 2008 and 2007, respectively.

Warranty Cost. We accrue for warranty costs based on estimated product return rates and the expected material and labor costs to provide warranty services. If actual products return rates, repair cost or replacement costs differ significantly from our estimates, then our gross margin could be adversely affected. The reserve for product warranties was \$137,000 and \$148,000 as of September 30, 2008 and September 30, 2007, respectively. This change was the result of a significant decline in the product return rate caused by changes in our management of the return programs. As a consequence of the Company's standardized manufacturing processes and product testing procedures, returns of defective product are infrequent and the quantities have not been significant. Accordingly, historical warranty costs have not been material.

Results of Operations

The following table sets forth consolidated statements of operations data for the periods indicated as a percentage of net revenue.

	Fiscal Year Ended September 30,		
	2008	2007	2006
Consolidated Statements of Operations Data:			
Net revenue:			
Hardware	86.2%	90.7%	92.1%
Software	13.8	9.3	7.9
Total net revenue	100.0	100.0	100.0
Cost of revenue:			
Hardware	41.4	44.7	44.6
Software	1.2	0.7	0.6
Total cost of revenue	42.6	45.4	45.2
Gross profit	57.4		