AVOCENT CORP
Form 10-K
March 01, 2007

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

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

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2006.

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

FOR THE TRANSITION PERIOD FROM TO .

Commission file number: 000-30575

AVOCENT CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**91-2032368**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
4991 Corporate Drive **Huntsville, Alabama**	**35805**
(Address of Principal Executive Offices)	(Zip Code)

256-430-4000
(Registrant s telephone number, including area code)

Securities registered under Section 12(b) of the Exchange Act
Common Stock, $0.001 par value per share

Securities registered under Section 12(g) of the Exchange Act: **None**

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

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 o No x

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and disclosure 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. x

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

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

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

The aggregate market value of the voting and non-voting common stock held by non-affiliates of the registrant as of the last business day of the registrant s most recently completed second fiscal quarter was approximately $1,172,764,399.

The number of shares outstanding of the registrant s common stock as of February 22, 2007 was 50,796,732.

DOCUMENTS INCORPORATED BY REFERENCE

Information with respect to items 10 to 14 of Part III of this Form 10-K may be found in the definitive proxy statement to be delivered to stockholders in connection with the 2007 Annual Meeting of Stockholders. Such information is incorporated herein by reference.

PART I

Item 1. Business.

THIS ANNUAL REPORT CONTAINS FORWARD-LOOKING STATEMENTS THAT INVOLVE RISKS AND UNCERTAINTIES. THE STATEMENTS CONTAINED IN THIS ANNUAL REPORT THAT ARE NOT PURELY HISTORICAL ARE 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. THESE FORWARD-LOOKING STATEMENTS INCLUDE, WITHOUT LIMITATION, STATEMENTS RELATING TO FUTURE ECONOMIC CONDITIONS IN GENERAL AND STATEMENTS ABOUT:

- *OUR FUTURE STRATEGY, STRUCTURE, AND BUSINESS PROSPECTS;*
- *PLANNED ENGINEERING AND DESIGN ACTIVITIES, DEVELOPMENT AND ENHANCEMENT OF CURRENT PRODUCTS, AND INTRODUCTION OR ACQUISITION OF NEW PRODUCTS AND TECHNOLOGIES;*
- *THE SIZE, GROWTH, AND LEADERSHIP OF THE POTENTIAL MARKETS FOR OUR PRODUCTS AND TECHNOLOGIES;*
- *THE ADEQUACY OF CURRENT, AND THE DEVELOPMENT OF NEW, OEM, DISTRIBUTOR, RESELLER, AND SUPPLIER RELATIONSHIPS;*
- *OUR FUTURE SALES, EARNINGS, INCOME, EXPENSES, OPERATING RESULTS, TAX RATES, OPERATING AND GROSS PROFIT AND MARGINS, INVENTORY LEVELS AND VALUATIONS, RECEIVABLES, RESERVES AND INVESTMENT INCOME;*
- *OUR FUTURE LIQUIDITY, THE IMPACT OF CURRENCY RATES, AND OUR PLANS REGARDING EQUITY-BASED COMPENSATION, CAPITAL RESOURCE NEEDS, SHARE REPURCHASES, BORROWINGS AND REPAYMENTS;*
- *OUR CUSTOMERS, SEASONALITY AND COMPETITIVE ENVIRONMENT;*
- *OUR EFFORTS TO EXPAND RELATIONSHIPS WITH DISTRIBUTORS AND RESELLERS;*
- *OUR ABILITY TO OBTAIN AND PROTECT OUR INTELLECTUAL PROPERTY AND PROPRIETARY RIGHTS;*
- *ANTICIPATED EXPANSION OF INTERNATIONAL SALES AND OPERATIONS; AND*
- *POTENTIAL ACQUISITIONS, CONTINGENT PURCHASE CONSIDERATION RELATED TO OUR ACQUISITION OF LANDESK, INTEGRATION COSTS, AND TRANSACTION COSTS AND ADJUSTMENTS.*

ALL OF THESE FORWARD-LOOKING STATEMENTS ARE BASED ON INFORMATION AVAILABLE TO US ON THE DATE OF THIS ANNUAL REPORT. OUR ACTUAL RESULTS COULD DIFFER MATERIALLY FROM THOSE DISCUSSED IN THIS ANNUAL REPORT. THE FORWARD-LOOKING STATEMENTS CONTAINED IN THIS ANNUAL REPORT, AND OTHER WRITTEN AND ORAL FORWARD-LOOKING STATEMENTS MADE BY US FROM TIME TO TIME, ARE SUBJECT TO CERTAIN RISKS AND UNCERTAINTIES THAT COULD CAUSE ACTUAL RESULTS TO DIFFER MATERIALLY FROM THOSE ANTICIPATED IN THE FORWARD-LOOKING STATEMENTS. FACTORS THAT MIGHT CAUSE SUCH A DIFFERENCE INCLUDE, BUT ARE NOT LIMITED TO, THOSE DISCUSSED IN ITEM 1A RISK FACTORS.

Overview

Avocent Corporation designs, manufactures, licenses, and sells software and hardware products and technologies that provide connectivity and centralized management of information technology (IT) infrastructure. We (meaning Avocent and its wholly-owned subsidiaries) provide connectivity and systems management products and technologies that centralize control of servers, desktop computers, serial devices, wireless devices, mobile devices, and network appliances, thus increasing the efficiency of IT personnel. Server manufacturers resell private-labeled Avocent KVM (keyboard, video, and mouse) switches and embedded software and hardware technology in their systems, and companies large and small depend on our software and hardware products and technologies for managing their growing IT infrastructure.

Our technological innovations include Internet protocol (IP) based switching, centralized management, and intuitive software interfaces. With more than two decades of experience, we have grown through product innovations, global expansion, and strategic acquisitions. Formed as a result of the merger in 2000 between Apex Inc. and Cybex Computer Products Corporation, we subsequently acquired Equinox Systems Inc. in 2001, 2C Computing, Inc. in 2002, Soronti, Inc. in 2003, Crystal Link Technologies, OSA Technologies, Inc., and Sonic Mobility, Inc. in 2004, and Cyclades Corporation and LANDesk Group Limited in 2006.

We market our products around the world to a diversified group of original equipment manufacturers (OEMs), dealers, distributors, resellers, and end users, primarily through our sales and customer support staff, advertisements in trade publications, on-line sponsorships, and participation in major industry trade shows. A substantial portion of our sales is to major server OEMs that purchase our switching systems on a private-label or branded basis.

Our corporate Internet address is *www.avocent.com*. At this website, we make available free of charge our annual report on Form 10-K, our annual proxy statement, our quarterly reports on Form 10-Q, any current reports on Form 8-K, and any amendments to these reports, as soon as reasonably practicable after we electronically file them with, or furnish them to, the Securities and Exchange Commission. Also available at this website are our Code of Business Conduct and Ethics, our Corporate Governance Guidelines, our Whistleblower Policy, the Nominating and Governance Committee s Policies and Procedures for Director Candidates, and the Charters for our Acquisition and Strategy Committee, Audit Committee, Compensation Committee, and Nominating and Governance Committee. If any amendment to our Code of Business Conduct and Ethics or any waiver granted under it is applicable to our principal executive officer, our principal financial officer, our principal accounting officer or controller (or any persons performing similar functions) and relates to the code of ethics definition enumerated in the SEC s regulations, we will disclose such amendment or waiver at this website within five business days after the date of such amendment or waiver. The information found on our website is not part of this Form 10-K. In addition to our website, the SEC maintains an Internet site at *www.sec.gov* that contains reports, proxy and information statements, and other information regarding us and other issuers that file electronically with the SEC.

ACS, Apex, AMX, AMWorks, Avocent, the Avocent logo, AutoView, Cybex, Cyclades, DSR, DSView, Emerge, Equinox, LANDesk, the LANDesk logo, LongView, PM, The Power of Being There, and SwitchView are trademarks or registered trademarks owned by us. This annual report also includes trademarks of other companies.

Industry Background

Information technology is critical to most business operations as computers perform multiple and diverse functions throughout many different types of organizations. Many corporations have decentralized computing power while sharing technology resources and providing broad access to enterprise data. This has resulted in the widespread adoption of distributed network computing environments using a network-based architecture of interconnected computers that span from the data center to the corporate office. Businesses are increasingly faced with a growing number of challenges. These challenges include:

Data Center Growth. The typical data center installation consists of a local area network (LAN), with a large number of computers operating as servers dedicated to performing specific functions for the many client computers connected to the LAN and, in many cases, a wide-area network (WAN). With the shift of software applications to a web services model, the demand for servers and storage is growing. Users are accessing more data and resources using intranets and the Internet. This growth causes a proliferation of servers and increases the administration, environmental, power, and space challenges of managing data centers containing growing networks of servers, consoles, peripherals, and cables, and other network devices.

Corporate Office Growth. The corporate office environment is made up of both central office and distributed or branch locations. These environments typically consist of a large number of connected devices that include servers, desktop computers, laptops, handheld devices, printers, and other networked devices. The explosion in the number of these devices in the office environment and the distributed nature of them pose many significant challenges in system, security, service, and process management.

Increasingly Mobile Workforce. As the workforce continues to become more mobile, handheld devices and laptop computers are increasingly used outside of the corporate LAN. This proliferation of networked devices and the difficulty in controlling these devices outside of the corporate LAN pose many significant management and security challenges.

Heterogeneous Environment. Corporate IT departments may manage hundreds or thousands of servers, clients, and other networked devices, must identify and access relevant devices, add or delete users, add, change, or upgrade applications, tune systems for better performance, and diagnose and correct network failures. These network devices are generally purchased from multiple vendors and are designed to operate as stand-alone systems, each with its own console. IT professionals must therefore deal with a large number of consoles and workflow processes, whether centrally located or dispersed throughout the organization, when performing administration and management tasks.

Always-On Infrastructure. Information technology resources are critical to organizations. Accordingly, constant availability is crucial to the operation of many businesses. The time that an Internet service provider (ISP), an application service provider (ASP), a data center, a server farm, a corporate network, or a desktop computer, a laptop, or a mobile device is down or degraded can cause significant inconvenience, loss of productivity, and financial loss. Quick and efficient diagnosis and the correction of problems can be difficult, and the ability of a facilities manager or network administrator to quickly and efficiently diagnose and correct the problem may be hampered by the inability to access the software.

Products and Technologies

As of the first quarter of 2007, our four divisions provide the following software and hardware products and technologies. The products and technologies we provide solve many of the network administration, systems, security, device management, and storage problems faced by facilities managers, network administrators, and IT managers.

- The Management Systems Division consists of our branded and OEM IT infrastructure management products, which include KVM, serial console, power control, management appliances, management software, and our embedded manageability technologies, such as intelligent platform management infrastructure (IPMI) and embedded KVM systems.

This division focuses on IT infrastructure management solutions and technologies for (i) data centers, (ii) remote access and distributed branch office environments, (iii) mid-size server rooms for the small and medium business (SMB) market, and (iv) desktop switching and universal serial bus (USB) hubs for simplified control of desktops, small offices, and home-based businesses. This division also provides the technology that links our embedded technologies and our DSView management software.

The products and technologies offered by our Management Systems Division include:

- Our *DS Series* products, which allow users to control servers from remote locations using an Internet or network connection without the necessity of remote access hardware or software on the computers or servers being accessed. The *DS Series* KVM products digitize keyboard, video, and mouse information and compress and transport that information in packets over traditional network connections optimizing performance for busy data centers. Our *DSR®* switching systems feature a digital console connection that allows facilities managers and network administrators access to servers utilizing standard networking infrastructure and our *KVM over IP* technology. Our *DS Series* appliances are managed with *DSView®* centralized management software, providing access and control of servers and serial devices in the network operations center or from almost any location in the world using TCP/IP connectivity. IT administrators can securely manage all connected data center devices and gain point-and-click access and control over these devices using a browser interface.

- Our *AutoView®* switch family, which offers users a variety of analog and digital KVM switches. Our AutoView switches provide small to medium size businesses with a 1U-high design saving valuable rack space in the server room. Our *AutoView 1415, 1515, and 2015* switches provide KVM support for USB, PS/2, Sun, and serial target devices. Our *AutoView 2020 and 2030* switches have a virtual media feature that allows sharing of a directly-connected USB storage device to all servers connected to the switch. Our *AutoView 3100 and 3200* switches are 16-port switches that provide server access for up to two remote digital users and one local analog user. All our *AutoView switches* offer an on-screen display and a web-based interface, which means that no additional software is required for remote server access.

- Our *SwitchView®* switching products includes our *SwitchView SC* family of secure switches, built for the secure environment and designed to make it impossible to transfer data between connected computers. Our *SwitchView* 1000 rack mounted KVM switches are available in 4, 8 and 16 port models with an on-screen display that supports 2048 x 1536 video resolutions and can be cascaded to support up to 256 target devices. Our compact, space-saving *SwitchView* desktop KVM switches support multiple computers and allow users to control multiple PCs and share access to a digital camera, CD-ROM, PDA, scanner, printer, speakers, and a microphone.

- Our *AMX* analog matrix switching systems, which provide simpler access and easier manageability of servers in multi-rack, multi-platform environments. Our *AMX* switches increase the number of users with simultaneous access and offer efficient scalability with an architecture that makes it easy to add and support additional servers. Our advanced *AMWorks*® software is also included with our *AMX* switches for central administration.

- Our KVM extension product lines, including our CAT 5 extension products, fiber optic and copper extension products, and wireless extension products. The *LongView*® extender allows users to extend a keyboard, monitor, mouse, speakers, microphone, and serial port up to 500 feet away from the computer or KVM switch with one CAT 5 UTP cable. Our *LongView Wireless* product is a KVM extender, which can wirelessly connect monitors (VGA, SVGA, and XGA), keyboards, mice, and audio devices to a computer up to 1,000 feet away.

- Our ACS appliances, which deliver secure, serial over IP access to console ports of command line driven operating systems such as LINUX or UNIX servers and other serially-managed devices such as power management systems, storage elements, firewalls, and network switches and routers. These serial appliances and attached devices can be centrally managed using our *DSView 3* management software.

- Our *PM* series of intelligent power control and distribution devices, which provide control over any connected device s AC power source. These devices are critical in certain situations when the connected devices require a full hardware level reset to restore operational service. Our *PM* devices are connected to DSR or ACS appliances and can be managed by the user interface of these appliances or centrally managed using our DSView 3 management software.

- Our embedded products, which are provided as a combination of hardware products and licensed technologies. These technologies consist of IPMI firmware, drivers, and utilities, KVM switching and compression technologies, virtual media firmware and utilities, software for graphical user interfaces (GUI), and desktop management applications. These technologies are licensed to our OEM customers for inclusion in their servers, desktops, notebooks, and other devices. Our hardware products consist of remote access and management cards, chassis management cards, and KVM designs that are also sold to our OEMs for integration with their systems.

- **The LANDesk Division consists of our systems, security, and service management software for desktops, servers, and mobile devices across an enterprise.**

This division delivers systems, security, and service management software solutions that simplify how corporate enterprises manage desktops, servers, mobile devices, and IT services and processes. These LANDesk solutions allow an IT staff to increase productivity and protect corporate assets from a single, easy-to-use console while leveraging prior investments in database, application, and directory service technologies and across heterogeneous IT environments (Windows, Mac OS, Unix, Linux, and handheld and embedded device operating systems).

The products and technologies offered by our LANDesk Division include:

Systems Management Software

- Our *LANDesk® Management Suite* (LDMS) software, which allows enterprise IT departments to easily and efficiently automate systems management tasks and see, manage, and update desktops, servers and mobile devices from a single console. LDMS provides intelligent and efficient distribution capabilities, such as functional load balancing, fault tolerance, bandwidth minimizing technologies, and local access to packages previously delivered to a subnet, to minimize the impact to corporate systems. With just an Internet connection, corporate IT teams can identify and securely manage computer assets (including assets outside the firewall and at geographically distributed sites), scan, define, track, and audit applications, and provide compliance and usage reports.

- Our *LANDesk Server Manager* software, which provides enterprises with the tools to improve server performance, reliability, and availability through operating system (OS) and application provisioning, real-time hardware health monitoring, automated patching, imaging, and updating, historical data collection, predictive failure analysis and prevention, and remote problem resolution, all through a single console.

- Our *LANDesk System Manager* software, which provides active system monitoring and maintenance (through an intuitive, easy-to-use, browser-independent console), gathering health and status information directly from each computer s hardware, software, and operating system in real-time and giving IT staff customizable e-mail, pager, fax, or console alerts.

- Our *LANDesk Handheld and Embedded Device Manager* software, which is designed and optimized for managing across the low-speed, intermittent connections characteristic of handheld, embedded, and wireless devices, and allows an IT staff the ability to secure moving resources and the information on them, including the option to clear a device s memory card, delete contacts, address book data, and e-mail, and perform a reset of the mobile device.

- Our *LANDesk Asset Manager* software, which allows enterprises to track computer and non-computer resources (and associated users, contracts, maintenance agreements and more) through a single console to ensure full system availability, security, and configuration management.

- Our *LANDesk Inventory Manager* software, which enables IT staff to discover networked computing devices, automatically maintain detailed hardware and software inventories, and gather and track detailed hardware, software, and OS configuration data for license compliance, plan upgrades, identification of security issues, and determination of purchase needs.

Security Management Software

- Our *LANDesk Security Suite,* which includes software and subscription content that allows enterprises to easily perform and automate patch, anti-spyware, and security threat management from a single console with quarantine, antivirus enforcement, vulnerability detection, threat remediation, computer access restriction tools, and a variety of reporting capabilities (including trend graphs, spyware reports, and an executive dashboard with a graphical view of critical enterprise concerns).

- Our *LANDesk Patch Manager* software, which allows corporate IT departments to actively scan managed computers across heterogeneous IT environments to identify application and operating system vulnerabilities and quickly download patches with e-mail or pager alerts when a vulnerability or a specific severity level is detected.

- Our *LANDesk Antivirus* software, which provides enterprises with affordable, real-time virus protection and root kit detection to user endpoints with little or no new infrastructure. *LANDesk Antivirus* can automatically encrypt and quarantine suspicious files and known infections, and allows IT staffs to customize and control alerts, queries, and reports for full security.

Service Management Software

- Our *LANDesk Process Manager,* which integrates, optimizes, and automates IT and business processes, workflow, change management, configuration management, with a graphical process builder, full-featured auditing, customizable reporting capabilities, and support for third-party electronic forms.

- Our *LANDesk Service Desk* software, which provides help desk and IT staff with an Internet-based consolidated service desk solution with process-driven incident management, role-based privilege sets, knowledge base, call logging, assignment, form design, and service level escalation for delivering support services. *LANDesk Service Desk* includes an Internet-based interface that allows service providers and end users or customers to easily and proactively report problems, log incidents, communicate and track service status, and research the intelligent knowledge base for solutions to facilitate faster resolution.

- **The Connectivity and Control Division consists of our serial connectivity products and our professional audio-visual products.**

This division's switching, extension, and control products allow industry professionals to deliver leading-edge connectivity and control solutions to a range of markets including: retail, medical, digital signage, hospitality, AV, and broadcasting. This division offers wired and wireless extension products to simplify connectivity and control of displays, projectors, and AV equipment, LAN-based serial hubs to provide cost-effective device connectivity at the point of need, and matrix switches to help broadcast engineers back-rack and control studio production equipment.

The products and technologies offered by our Connectivity and Control Division include:

- Our *Emerge* family of products, which provide both wired and wireless switching and extension of video, audio, and control data for use in a range of markets. Our *Emerge* multipoint high-definition wired/wireless extender (MPX) allows AV consultants to design managed audio-video extension networks for commercial signage and presentation markets. Our *Emerge Wireless Media Streamer (EWMS)* is ideal for use in boardrooms, classrooms, and commercial digital signage applications, and our *Emerge Media Streamer (EMS)* offers CAT 5 wired video extension for use in similar markets. Our digital *ECMS* product allows responsive extension and switching of digital workstations across IP networks where a high degree of quality is required in markets such as broadcast and digital signage.

- Our *SST* and *ESP* serial products, which offer high-performance, reliable, and managed device connectivity for serial and dial access applications. These product lines include network-based appliances and bus-based adapters for use within security, commercial point-of-sale, process control, industrial automation, data collection, remote access, fax servers, and custom applications.

- **The Desktop Solutions Division consists of newly-developed technologies targeted at desktop users.**

This division s technology allows a personal computer (PC) or blade computer (a self contained personal computer or server reduced in size and designed for high density installations, which is often referred to as a blade) to be centralized while providing remote access to the user of that computer via TCP/IP network infrastructure. This technology is incorporated into Avocent branded extender products. The technology is also licensed as a building block to OEMs to allow large institutions to introduce blades as workstations and take advantage of a centralized computing model and the efficiencies this brings in management and security. This technology is targeted at our channel and our OEM partners as an embedded solution, and has been successfully deployed in hazardous computing environments, manufacturing companies, digital signage applications, and command and control centers.

The products and technologies offered by our Desktop Solutions Division include our digital extension product lines, which feature technology that extends keyboard, video, mouse, audio, and USB over any TCP/IP network and allows administrators to centralize all computers for ease of maintenance while providing users with full Rich-Media PC functionality at the desktop. This extension technology enables a distributed computing environment with access to centralized computer assets from anywhere within the reaches of a corporate network.

Sales and Marketing

We market, sell, and license our hardware and software products through our own sales force and various distribution channels, including OEMs, distributors, and reseller arrangements. We market our products primarily through direct customer sales calls, advertisements in trade publications, online sponsorships, participation in major industry trade shows, promotions with distributors and resellers, direct marketing, telemarketing, publicity programs, and through our website. We also devote a substantial portion of our marketing efforts to developing, monitoring, and enhancing our relationships with our network of OEMs, independent dealers, distributors, resellers, and end users. Our sales personnel are supported by our engineers and our customer service representatives who provide technical support and advice to customers. As of December 31, 2006, we employed 646 people in sales, marketing, and customer support.

We currently sell or license various hardware and software products and technologies to Dell, Hewlett-Packard, IBM, Intel, Lenovo, Fujitsu Siemens, and other OEMs pursuant to private-label, branded, and licensing arrangements. These OEM customers integrate and sell our products and technologies with or within their own products, including networked servers and clients. We devote significant sales, engineering, operations, and customer service resources to our OEM accounts. We have significant experience in working with our OEM and other system manufacturers, and we intend to use that experience to enter into new relationships with other computer manufacturers in the United States, Europe, and Asia. We believe that the architecture, quality, and reliability of our products and technologies, together with our commitment to customer service, are attractive to computer manufacturers worldwide.

We have relationships with a variety of distributors and resellers, value added resellers (VARs), and systems integrators, for the distribution and sale of Avocent, Cybex, Cyclades, Equinox, and LANDesk branded software and hardware products in the United States, Canada, Europe, South America, Asia, and elsewhere. We devote resources to educating our distributors and resellers about the benefits of our products and training them in the proper installation and support of our products. We will continue to devote additional resources to increase these branded sales, and we will pursue additional relationships with distributors and resellers, both domestically and internationally, who have the technical capability and market presence to assist end-user customers in developing network space management, access, and control products and technologies to meet their particular needs. Our future success will depend in part on our ability to attract, train, and motivate additional distributors and resellers.

We provide discounts, other special pricing arrangements, and certain return privileges to our OEMs and our distributors and resellers. Our agreements with our distributors and resellers are generally nonexclusive and may be terminated on short notice by either party without cause. Our distributors and resellers are not within our control, are not obligated to purchase products from us, and frequently offer products from several different manufacturers, including products that compete with our products.

International sales accounted for approximately 43% of net sales in 2006, 43% of net sales in 2005, and 41% of net sales in 2004, and were made primarily to OEMs, distributors, and resellers located in Europe, Canada, Asia, and other foreign countries. No foreign country accounted for more than 10% of 2006 or 2005 sales. Sales to customers in the Netherlands, including the European distribution facility for one of our OEM customers, accounted for 10% of sales in 2004. No other foreign country accounted for more than 10% of 2004 sales. We are expanding our international sales efforts within Europe, Latin America, Asia, and the Pacific Rim through the utilization of our sales offices in Sydney, Australia; São Paulo, Brazil; Beijing, Guangzhou, and Shanghai, China; London, England; Paris, France; Munich, Germany; Rotterdam, Holland; Hong Kong; Shannon, Ireland; Tokyo, Japan; Mexico City, Mexico; Taipei, Taiwan; and Singapore.

Customers

To date, a substantial portion of our net sales has been generated from sales of our switching products and technologies to OEMs for integration with their product offerings. Sales to OEM customers represented 40% of net sales in 2006, 48% of net sales in 2005, and 45% of net sales in 2004. While we have contracts with some of our OEM customers, none of them is obligated to purchase products from us except pursuant to binding purchase orders. Consequently, any OEM customer could cease doing business with us at any time. The loss of, or material decline in orders from, certain of our current OEM customers would have a material adverse effect on our business, financial condition, results of operations, and cash flow.

In addition to our OEM customers, our principal customers include a diversified group of dealers, major distributors, value added resellers (VARs), and direct end users who purchase our branded products (60% of net sales in 2006, 52% of net sales in 2005, and 55% of net sales in 2004). We believe that our broad range of products sold at different price points offers us the opportunity to market our products to customers of all sizes, in different industries, and with varying degrees of technical sophistication.

Sales to Hewlett-Packard, Dell, and Tech Data represented approximately 14%, 14%, and 12%, respectively, of net sales in 2006. Sales to Hewlett-Packard and Dell represented approximately 20% and 15%, respectively, of net sales in 2005. Sales to Tech Data and Ingram Micro represented approximately 11% and 10%, respectively, of net sales in 2005. Sales to Hewlett-Packard and Dell represented approximately 23% and 12%, respectively, of net sales in 2004. Sales to each of Tech Data and Ingram Micro represented approximately 11% of net sales in 2004. No other customer accounted for more than 10% of our net sales in 2006, 2005, or 2004.

Seasonality

Our operating results are affected by seasonal trends and by general conditions in the server market. We have experienced, and expect to continue to experience, some degree of seasonality due to customer buying cycles. We believe that the third and fourth quarters will generally have higher net sales levels due to customer budgeting and procurement cycles, which may depress net sales in other quarters. In the past, revenue in our fourth quarter of each year has typically been higher than revenue in prior quarters for the year. In addition, we typically see a sequential decline in revenue from the fourth quarter of a year to the first quarter of the following year. While it is difficult to predict revenue in any quarter, we expect that this pattern will continue in the future.

Customer Service

We emphasize customer service by developing high quality products, encouraging customer feedback through contact with our key customers, providing technical support and information on our website, and providing a customer hotline that offers technical support for the life of our hardware products. We also offer annual software upgrade protection and maintenance agreements for licensees of our software products. We strive to respond quickly to our customers requests for technical support and service, and our engineering department often works with individual customers to troubleshoot problems and develop custom solutions. We offer warranties for parts and service on all of our hardware products, ranging from one to three years (and, in the case of some of our Equinox branded products, five years). We also offer a 30-day money-back guarantee for all of our appliance products sold in North America. To date, we have not experienced any significant hardware product returns. For our software products, we generally provide a 90-day warranty on the media used to deliver the software, which is not applicable to electronic downloads, and we often provide a limited warranty (usually no more than 90 days) that our software products will function in accordance with the user documentation. We may, as a result of competitive pressures, change our warranty policies in the future to provide coverage that is greater in scope and duration than the coverage we currently offer. If we were to increase our warranty coverage, our risk of warranty claims, and therefore our warranty expense and reserves, would likely increase.

Development of New Products and Technologies

We believe that the timely development of enhancements to our existing hardware and software products and technologies and of new products and technologies is essential to building our competitive position. The market for our products has experienced rapid technological advances, frequent new product introductions and enhancements, and significant price competition. The introduction of products incorporating superior or alternative technologies (such as switching software), the creation or adoption of new technologies (such as the creation of virtual servers using a combination of hardware and software, which is known as virtualization), the emergence of new industry standards, or changes in the market s pricing structure could render our existing products and technologies and the products and technologies we have under development obsolete or unmarketable. Our hardware products generally combine components, such as printed circuit boards, semiconductors, memory, connectors, cable assemblies, power supplies, and enclosures, that are manufactured by other companies and are generally available to our competitors and potential competitors. Our software products combine software or content from third parties, such as open source software or technology, drivers, security, service desk, or anti-virus information, which may also be generally available to our competitors and potential competitors. Our future success will depend in large part upon continued innovative application of commercially available components and third-party software or technologies, together with continued enhancements to our proprietary hardware, software, firmware, and other technologies, the expansion and enhancement of our existing products, and the development and introduction of new technologies and products that address changing customer needs on a cost-effective and timely basis. By emphasizing customer-driven research and development, we have been able to develop innovative, practical, and marketable products that have had immediate application and acceptance. Our failure to respond on a timely basis to technological changes or customer requirements could have a material adverse effect on our business, financial condition, results of operations, and cash flow.

Due to our significant reliance on OEM relationships, some of our product development efforts are focused on developing new hardware and software products or enhancements for OEM customers. At times, these new products or enhancements may not be available to, or readily marketable to, other customers without significant modifications or delay.

Our engineering and product development efforts focus on anticipating the needs of our customers by providing innovative, practical, and marketable products and technologies that have immediate applications in their markets. By maintaining contact with customers throughout the installation and technical support process, we are able to identify and test potential design modifications and improvements as well as new applications and extensions for existing products and technologies. We expect this process will enable us to develop new product categories and applications based on existing technology developed to meet specific customer needs. Many of our products and technologies are designed to accommodate future modifications and additional features, which we believe facilitates the development and integration of future modifications and features if we see a market need.

As of December 31, 2006, we employed 613 people in our engineering department. In addition, we use independent contractors from time to time. As of December 31, 2006, we were working with approximately 45 independent contractors on various development projects.

To meet the challenges of the rapidly changing technology in the computer industry, we expect to make substantial investments in product development in the future. There can be no assurance that these new or enhanced versions or any other of our product development efforts will lead to commercially viable products or technologies, will be completed on a timely basis, or will include the features required to achieve market acceptance.

A key component of our engineering and product development strategy is the acquisition of new technologies and companies. We intend to continue to evaluate opportunities to acquire technologies and companies, and it is likely that we will complete additional acquisitions in the future. There can be no assurance that these acquisitions will result in the timely development of commercially viable products or technologies that achieve market acceptance.

Manufacturing

We do not manufacture any of our hardware products in their entirety. Instead, we manage product planning, purchasing, and shipping, and we perform final assembly, quality assurance, and testing on some of our hardware products while we outsource some or all of these functions on other products. In order to avoid the capital investment required to establish and maintain in-house manufacturing capabilities, we rely on subcontractors throughout the world for the assembly of printed circuit board assemblies, subassemblies, chassis, and equipment enclosures. We believe that our chosen subcontractors can typically perform these functions at a lower cost than we can, while maintaining our high standards for quality and delivery. Outsourcing our manufacturing functions allows us to concentrate our resources on research and development, product design, quality assurance, sales and marketing, and customer service. We (or our subcontractors) subject our most critical components and products to automated testing, equipment burn-in procedures, comprehensive quality audits, functional testing, and regulatory screening to assure quality and reliability. As of December 31, 2006, we employed 242 people in our manufacturing, supply chain management, and logistics department.

We currently rely on several third party manufacturers, including Elcoteq Network Corporation, Plexus Corp., Kontron AG, and Likom Computer Products, for subassembly of our hardware products. These outsourcing arrangements, and any future outsourcing arrangements, involve numerous risks, including reduced control over product quality, delivery schedules, manufacturing yields, and costs. In addition, while these third-party manufacturers have arrangements for warranty obligations, we remain primarily responsible to our customers for warranty obligations. We attempt to diversify our outsourced manufacturing operations and believe we have an adequate supply of alternative subcontractors.

We generally purchase industry-standard parts and components, including power supplies, semiconductors, memory, cable assemblies, line filters, enclosures, and printed circuit boards, for the assembly of our products from multiple vendors and suppliers through a worldwide sourcing program. Custom molded cables and certain turn-key products procured from outside sources have significant delivery times (10 to 12 weeks), and failure to obtain adequate supplies could adversely affect our product deliveries. We buy components under purchase orders and generally do not have long-term agreements with our suppliers. Circuit board assemblies are currently obtained from a number of sources, including Elcoteq Network Corporation, Plexus Corp., Kontron AG, and Likom Computer Products. We believe that there are adequate alternative sources for our product components. Any termination of, or significant disruption in, the business or affairs of our suppliers or our third-party manufacturers or in our relationship with them may prevent us from filling customer orders in a timely manner since we generally do not maintain large inventories of our components.

In the past, we have experienced delays in the receipt of certain components, which have resulted in delays in related product deliveries. We attempt to manage these risks through developing alternative sources, committing internal resources to supply chain management, and maintaining relationships and close personal contact with each of our contract manufacturers and suppliers. There can be no assurance, however, that delays in component and product deliveries will not occur in the future, and the inability to obtain sufficient components or to develop alternative sources, if and as required in the future, could result in delays or reductions in product shipments, which, in turn, could have a material adverse effect on our business, financial condition, results of operations, or cash flow. Some of the components for our products are available from a single supplier or a limited number of suppliers. We attempt to maintain quality relationships and close contact with each of our suppliers.

Competition

The market for our hardware and software products is highly fragmented and competitive, and we expect competition to increase in the future. In the market for hardware switching systems, we compete with companies such as Raritan Computer, Rose Electronics, Minicom Advanced Systems, Aten International, Belkin, Lantronix, and Digital V6, and in the market for our systems management products we compete with companies such as Microsoft, Computer Associates, BMC Software, Novell, Tivoli, and Altiris, some of which may have substantially greater financial, marketing, and technical resources than we have. In addition, certain of our OEM customers, such as Dell, Hewlett-Packard, and IBM, offer technologies and products that are competitive with our products, and we expect these technologies and products to remain competitive in the features they offer. Our products and technologies are also in competition with the products and technologies offered by hardware manufacturers and network management companies such as Intel, Microsoft, Cisco, and EMC.

In the market for our products, we compete primarily on the basis of technological capabilities, performance in relation to price, product features, quality, reliability, development capabilities, product availability, and customer service and support. Our future success will be highly dependent upon timely completion, introduction, and distribution of new products, technologies, and features at competitive price and performance levels that address the evolving needs of our customers. We continually experience price competition and expect that pricing pressures could increase in the future.

Proprietary Technology

Our future success is dependent in part upon our ability to protect our intellectual property and our proprietary rights in our products and technologies. We seek to protect our intellectual property rights by invoking the benefits of the patent, trademark, copyright, trade secret, and unfair competition laws of the United States and certain foreign countries, which provide only limited protection. We have been issued over 50 U.S. patents and have over 50 U.S. patent applications pending. We have various corresponding patent applications pending under the provisions of the Patent Cooperation Treaty, which permits the filing of corresponding foreign patent applications in numerous foreign countries within a limited time period. We also have other foreign patent applications pending. There can be no assurance that any additional patents will be issued from any of our pending applications, that any patents will be issued in any additional countries where our products or technologies can be sold or licensed, or that any claims allowed in our patents or in any pending patent applications will be of sufficient scope or strength for, or provide any meaningful protection or any commercial advantage to, us. Moreover, our competitors may challenge the validity of, or be able to design around, these patents or any other patents that may be issued to us. The laws of certain foreign countries in which our products are or may be developed, manufactured, or sold (particularly countries in Asia) may not protect our products or intellectual property rights to the same extent as do the laws of the United States and thus increase the likelihood of piracy of our products and technologies.

In the future, we may file additional lawsuits against other companies regarding the alleged infringement. Patent litigation, and any other litigation relating to our intellectual property to which we become a party, is expensive and subject to numerous risks and uncertainties, and there can be no assurance that we will be successful in any such litigation. There can be no assurance that the steps we take to protect our intellectual property rights will be adequate to prevent misappropriation of our technologies or that we can use our intellectual property rights to successfully prevent competitors from commercializing technologies that are substantially equivalent or superior to our products and technologies. Additionally, current or future competitors could develop their own proprietary technologies or obtain patents that may prevent us from developing or selling our products and technologies.

Employees

As of December 31, 2006, we had 997 full-time employees working in the United States. Of our domestic full-time employees, 346 were in marketing, sales, and customer support, 346 were in engineering, research, and development, 170 were in manufacturing and logistical operations, and 135 were in administration. As of December 31, 2006, we had 710 full-time employees working at our facilities outside of the United States. Of our international full-time employees, 300 were in marketing, sales, and customer support, 267 were in engineering, research, and development, 72 were in manufacturing and logistical operations, and 71 were in administration. Our employees in Brazil (approximately 50) are covered by a collective bargaining agreement. No other employees are covered by collective bargaining agreements relating to their employment by us. We believe that we have good relations with our employees.

Backlog

Backlog consists of purchase orders with delivery dates scheduled within the next six months. None of our customers is obligated to purchase products from us except pursuant to binding purchase orders. Because of the timing of orders and the possibility of customer changes to delivery schedules, our backlog as of any particular date is not representative of actual sales for any succeeding period. Moreover, with recent industry-wide initiatives by OEMs, distributors, and resellers to reduce inventories and shorten lead times, we do not view backlog as an important indicator of our future results, and we do not believe it is a meaningful indicator of actual sales for any succeeding period.

Item 1A. Risk Factors.

THIS ANNUAL REPORT CONTAINS FORWARD-LOOKING STATEMENTS THAT INVOLVE RISKS AND UNCERTAINTIES THAT COULD CAUSE OUR ACTUAL RESULTS TO DIFFER MATERIALLY FROM THOSE DISCUSSED IN THIS ANNUAL REPORT. THESE RISKS AND UNCERTAINTIES INCLUDING THE FOLLOWING:

Our acquisition of LANDesk could disrupt our business, expose us to new risks, and adversely affect the results of our operations.

We acquired LANDesk Group Limited in the third quarter of 2006. This acquisition represents a departure from our core products and technologies and our entry into a new market (systems management software products and services) in which we have very limited experience. The market for systems management products is highly competitive, and we expect competition in this market to continue and intensify. Many of LANDesk s competitors have substantially greater financial, customer support, technical and marketing resources, larger customer bases, longer operating histories, greater name recognition, and more established relationships in the industry than LANDesk has, and we may not have the resources or expertise to compete successfully with them in the future.

The LANDesk acquisition may divert the attention of management and other personnel from our core business operations, which may adversely affect our financial performance in one or more quarters. LANDesk presents us with new and different issues regarding revenue recognition, channel management, and collection of existing or new receivables, any of which could have a material adverse effect on our business, financial condition, and results of operations. We will need to expand and improve our internal systems, including our management information systems, to monitor these items. In particular, we have not yet completed our review and assessment of the internal systems and controls over the LANDesk financial reporting and information systems, and we will also need to expand our operating, administrative, and financial systems and controls to include the LANDesk operations. The acquisition and integration of LANDesk and its software products and services will require significant time, expense, and resources and subject us to the acquisition risks detailed below as we move into this new market. Any failure to successfully integrate and operate LANDesk could thus materially and adversely affect our result of operations, cash flows, and financial position.

We have acquired, and expect to continue to acquire, technologies, and companies and these acquisitions could disrupt our business or expose us to other risks.

A key component of our engineering and product development strategy and our future growth is the investment in or the acquisition of technologies and companies. We acquired Equinox Systems Inc. in 2001, 2C Computing, Inc. in 2002, Soronti, Inc. in 2003, and Crystal Link Technologies, OSA Technologies, Inc., Sonic Mobility, Inc. in 2004, and Cyclades Corporation and LANDesk in 2006. We intend to continue to execute our strategy through the acquisition of technologies or companies or through investments in complementary companies, products, personnel, or technologies, and it is likely we will complete such acquisitions or investments in the future. These acquisitions and investments involve many risks, including the following:

- Difficulty integrating the acquired company s personnel, products, product roadmaps, technologies, systems, processes, and operations, including product delivery, order management, and information systems;

- Difficulty in conforming the acquired company s financial policies and practices to our policies and practices and in implementing and maintaining adequate internal systems and controls over the financial reporting and information systems of the acquired company;

- Diversion of management s attention and disruption of ongoing business;

- Difficulty in combining product and technology offerings and entering into new markets (such as software) or geographical areas in which we have no or limited direct experience and where our competitors may have stronger market positions;

- Loss of management, sales, technical, or other key personnel;

- Revenue from the acquired companies not meeting our expectation, and the potential loss of the acquired companies customers, distributors, resellers, suppliers, or other partners;

- Delays or difficulties and the attendant expense in evaluating, coordinating, and combining administrative, manufacturing, research and development and other operations, facilities, and relationships with third parties in accordance with local laws and other obligations while maintaining adequate standards, controls and procedures, including financial controls and controls over information systems;

- Difficulty in completing projects associated with acquired in-process research and development;

- Incurring amortization expense related to certain intangible assets and recording goodwill and non-amortizable assets that will be subject to impairment testing and possible impairment charges;

- Dilution of existing stockholders as a result of issuing equity securities, including the assumption of any stock options issued by the acquired company;

- Overpayment for any acquisition or investment or unanticipated costs or liabilities;

- Assumption of liabilities of the acquired company, including any potential intellectual property infringement claims or other litigation; and

- Incurring substantial write-offs, restructuring charges, and transactional expenses.

Our failure to manage these risks and challenges could materially harm our business, financial condition, and results of operations. Further, if we do not successfully address these challenges in a timely manner, we may not fully realize all of the anticipated benefits or synergies on which the value of a transaction was based. Future transactions could cause our financial results to differ from expectations of market analysts or investors for any given quarter.

Intense competition from new and existing competitors or consolidation in the server and systems management sectors could impair our ability to grow our business, to sustain our profitability, and to sell our products and technologies.

The markets for our products and technologies are highly fragmented, rapidly evolving, and intensely competitive, and we expect this competition to continue and increase. Aggressive competition from both hardware and software products and technologies could lengthen the customer evaluation process and result in price reductions and loss of sales, which would materially harm our business. Our business is becoming increasingly sensitive to the introduction of new products and technologies (such as virtualization), price changes, and marketing efforts by numerous and varied competitors. Accordingly, our future success will be highly dependent upon our timely completion and introduction of new products and technologies and features at competitive prices and performance levels that address the evolving needs of our customers. We continue to experience aggressive price competition and increased customer sensitivity to product prices, and pricing and margin pressures are likely to increase in the future. Because of this competition, we may have to continue to lower the prices of many of our products and technologies or offer greater functionality within our products to deliver greater value to customers to stay competitive, while at the same time trying to maintain or improve our revenue and gross margin. Because our business model is based on providing innovative and high quality products, we may spend a proportionately greater amount on research and development than some of our competitors. If we cannot proportionately decrease our cost structure on a timely basis in response to competitive price pressures, our gross margin and profitability could be adversely affected. In addition, if our pricing, functionality, and other factors are not sufficiently competitive, or if there is an adverse reaction to our product decisions, we may lose market share in certain areas, which could adversely affect our revenue and prospects.

We compete for sales of switching systems and extension products with companies such as Raritan Computer, Rose Electronics, Minicom Advanced Systems, Aten International, Belkin, Lantronix, and Digital V6. These products also face competition from software providers (such as Microsoft, Computer Associates, Tivoli, Altiris, Novell, and BMC Software), who may be able to offer software products competitive with our hardware products at a much lower cost or even bundled for free, and from server manufacturers (including our OEM customers), who are able to offer their competitive technologies or products at the time of the server sale. These competitive software and hardware products address many of the problems our switching systems and technologies, extension products, and remote access products are designed to address.

We compete for sales of our systems management products with companies such as Microsoft, Computer Associates, BMC Software, Novell, and Altiris, many of whom have greater financial, technical, and marketing resources, a larger customer base, a longer operating history, greater name recognition, and more established relationships in the industry than we do, and may offer their own or third-party competitive software products at a lower cost or bundled for free with their other products. Microsoft, in particular, has delivered competitive systems management products and announced its intention to continue to develop competitive software. If Microsoft is successful in delivering systems management software that is competitive with our products, our ability to grow our systems management business may be limited.

These current and potential competitors may be able to respond more quickly to new or emerging technologies or products and to changes in customer requirements or to devote greater resources to the research, development, promotion, sale, and support of their products and technologies than we do. In addition, current and potential competitors have established or may establish cooperative relationships among themselves or with third parties that expand or enhance the ability of their products and technologies to address the needs of our current and prospective customers. Some of these competitors can also bundle hardware, software, and services together, and offer a more complete set of hardware products and services than we are able to offer. We may not be able to compete successfully against current and future competitors and competitive pressure may materially harm our business, financial condition, operating results, and cash flows, or impair our ability to achieve our desired results.

Certain of our customers, such as Dell, Hewlett-Packard, IBM, Symantec, and Microsoft, presently offer competitive hardware and/or software products and technologies that address many of the problems our products and technologies address. These customers could decide to manufacture or enhance their own switching, IPMI or other embedded technologies, or systems management or security products, or offer products or technologies supplied by competitors. Companies with hardware manufacturing experience or network management products, many of which are substantially larger than we are and have significantly more financial resources than we do, also offer products or technologies that compete with us. Established companies with hardware manufacturing or network management experience (such as Intel, Cisco, or EMC) could also offer new products, new technologies (such as virtualization), or new solutions that compete with, or reduce the demand for, our products and technologies.

There has been consolidation in the markets in which we compete, which we believe will continue and could lead to increased price competition and other forms of competition as companies attempt to maintain or extend their market positions in the rapidly changing IT industry. In addition, we may face competition in the future from large established companies or from emerging companies that have not previously entered the market or that do not currently have products that directly compete with our products. This could lead to more variability in our operating results due to lengthening of the customer evaluation process and/or the loss of business to these competitors, which may adversely affect our business, financial condition, and results of operations.

Our failure to respond to rapid technological change or to introduce successful new products and technologies may result in reduced revenue or revenue growth.

The process of developing or acquiring new products and technologies and enhancing existing products and technologies is complex, costly, and uncertain, and any failure by us to anticipate customers changing needs and emerging technological trends accurately could significantly harm our market share and results of operations. We must make long-term investments, develop or obtain appropriate intellectual property, and commit significant resources before knowing whether our predictions will accurately reflect customer demand for our products and services. After we develop a product, we must then accurately forecast volumes and configurations that meet customer requirements, manufacture appropriate hardware volumes quickly and at low cost and develop cost-effective software solutions, and train our sales force and resellers. Any delay in the development, production, marketing of, or training for new products or technologies could result in our not being among the first to market, which could further harm our competitive position.

Sales of switching, extension, and remote access products and technologies are characterized by rapid technological advances, frequent new product and technological introductions and enhancements, and significant price competition. If we do not keep pace with these changes, we will lose customers, and our business will be adversely affected. The introduction of products or technologies incorporating superior alternatives such as switching software, the emergence of new industry standards, or changes in pricing structure could render our existing products and technologies and those under development obsolete or unmarketable. New technologies offered by us or our competitors could compete with our existing products at a lower price, which could reduce our revenue.

Our hardware products combine components, such as printed circuit boards, connectors, semiconductors, memory, cable assemblies, power supplies and enclosures that are manufactured by other companies and are generally available to competitors and potential competitors. Our software products combine software or content from third parties, such as open source software or technology, drivers, security, or anti-virus information, which may also be generally available to our competitors and potential competitors. Our future success will depend in large part upon continued innovative application of commercially available components and third party software or technology, and continued enhancements to our proprietary hardware, software, firmware, and other technologies, the expansion and enhancement of existing products and technologies, and our development and introduction of new products and technologies that address changing customer needs on a cost-effective and timely basis. If we fail to respond on a timely basis to technological developments, changes in industry standards, customer requirements, competitive products, product localization, or software innovations, we will lose customers, and our business will be greatly harmed. Similar results could occur if we experience significant delays in the development or introduction of new products or technologies.

Due to our significant reliance on OEM relationships, our hardware development efforts may often be focused on developing new products, technologies, or enhancements for OEM customers. As a result, our OEM relationships may negatively affect our ability to develop new and enhanced products and technologies for our non-OEM customers. Moreover, these new products, technologies, or enhancements for OEM customers may not be available to, or readily marketable to, other customers without significant modification and delay. The expansion, termination, or significant disruption of our relationship with certain OEMs or other customers for whom we devote significant product development resources is likely to result in lost opportunities with respect to the development of products, technologies, or enhancements for our other customers.

We have limited protection of proprietary rights and face risks of third party infringements.

Our future success depends in part upon our ability to protect proprietary rights in our products and technologies. We seek to protect our intellectual property rights by invoking the benefits of the patent, trademark, copyright, trade secret, and unfair competition laws of the United States and other countries and protections provided by confidentiality and nondisclosure agreements and other legal agreements. These laws and practices, however, afford only limited protection. There can be no assurance that the steps we have taken to protect our intellectual property rights, or that the steps we take in the future, will be adequate to prevent or detect misappropriation of our intellectual property or technologies or that our competitors will not independently develop proprietary or other technologies that are substantially equivalent or superior to our products or technologies. In addition, our proprietary information may be misused or improperly disclosed by third parties entrusted with this information.

The U.S. Patent and Trademark Office has issued several patents to us for various aspects of our products. We have various corresponding patent applications pending under the provisions of the Patent Cooperation Treaty, which permits the filing of corresponding foreign patent applications in numerous foreign countries within a limited time period. We also have other United States and foreign patent applications pending. There can be no assurance that any additional patents will be issued from any of those pending applications or that any patents will be issued in any additional countries where our products can be sold. Claims allowed in our patents or in any pending patent applications may not be of sufficient scope or strength for, or provide meaningful protection or any commercial advantage to us or such claims may not be upheld if challenged. Also, competitors may develop their own intellectual property or technologies, obtain their own patents, or challenge the validity of, or be able to design around, our patents. The laws of certain foreign countries in which our products are or may be developed, manufactured, or sold (particularly certain countries in Asia) may not protect our products or intellectual property rights to the same extent as do the laws of the United States and thus increase the likelihood of piracy of our technologies and products.

In January 2007, we filed a complaint for patent infringement in the United States District Court for the Western District of Washington against Aten Technology, Inc., Aten International Co., Ltd, Belkin Corporation, Rose Electronics and its general partners, and Trippe Manufacturing Company. Some of the defendants have not yet responded to our complaint.

We may initiate claims or litigation against other third parties for infringement of proprietary rights or to establish the validity of proprietary rights. Similarly, our competitors or other third parties may initiate claims or litigation against us alleging infringement of their proprietary rights or improper use of their intellectual property, and from time to time, third parties notify us that our products may infringe their intellectual property rights, which regardless of merit, requires our time and resources to evaluate and respond. Existing litigation, and any other litigation relating to intellectual property to which we become a party, is subject to numerous risks and uncertainties, including the risk of counterclaims or other litigation against us, and we may not be successful in any such litigation. Litigation is expensive, and the existing litigation or any other litigation by or against us could result in significant additional expense, divert the efforts of technical and management personnel, whether or not such litigation results in a favorable determination, harm our relationships with existing customers, and deter future customers from purchasing or licensing our products. In the event of an adverse result in any such litigation, we could be required to pay substantial damages, suspend or cease the development, manufacture, use, marketing, and sale of any infringing products, expend significant resources to redesign products or develop non-infringing technology, discontinue the use of certain processes, or obtain licenses to the infringing technology. There can be no assurance that we would be successful in such development or that such licenses would be available on reasonable terms, or at all, and any such development or license could require us to expend substantial time and other resources. In the event that any third party makes a successful claim against us, or our customers, and a license is not made available on commercially reasonable terms, our business, financial condition, and results of operations could be adversely affected. In addition, any dispute involving our intellectual property could result in our customers, distributors, or resellers becoming involved in the litigation, which could trigger indemnification obligations in certain of our sales, license, or service agreements.

The IT industry is characterized by vigorous pursuit and protection of intellectual property rights or positions, which has resulted in significant and often protracted and expensive litigation. We have in the past been, and we may from time to time in the future be, a party in proceedings alleging infringement of intellectual property rights owned by third parties. If necessary or desirable, we may seek licenses under such intellectual property rights. However, licenses may not be offered on terms acceptable to us, or at all. The failure to obtain a license from a third party for technology used by us could cause us to incur substantial liabilities and to suspend or cease the manufacture of products requiring such technology. Additionally, current or future competitors could obtain patents that may prevent us from developing or selling our products.

We are likely to experience fluctuations in operating results.

We have in the past experienced substantial fluctuations in revenue, bookings, and operating results, on a quarterly and an annual basis, and we expect these fluctuations will continue in the future. Our operating results will be affected by a number of factors, including, but not limited to:

- The volume, timing, pricing, and contractual terms of orders, particularly from OEMs, resellers, and other large customers, a significant portion of which tend to occur late in each quarter;
- The timing of shipments;
- The timing of new product introductions, new technologies, and enhancements by us and by our competitors, and the possibility that customers may defer purchases of our products in anticipation of these new products, new technologies, and enhancements;
- Changes in or our failure to accurately predict product or distribution and reseller channel mixes, including changes in the mix of software licenses in which revenue is recognized upfront as opposed to deferred over time and changes in the mix of revenue attributable to higher-margin products as opposed to lower-margin sales or services;
- Changes in demand for our products;
- Changes in pricing policies or price reductions;

- Changes in renewal rates for software upgrade protection or maintenance;
- Competition from new products and technologies and price reductions by competitors;
- The availability and cost of supplies, components, or third-party code or content on commercially reasonable terms;
- Compatibility or interoperability of our products with third-party systems and applications;
- Sales and marketing expenses related to entering into new markets, introducing new products, new technologies, and retaining current OEM and other large customers;
- Fluctuations in sales of servers due to changes in technology (such as virtualization), economic conditions, or capital spending levels;
- The amount and timing of operating expenses and capital expenditures relating to the expansion of our business and operations; and

• Costs associated with legal proceedings, including legal fees and any adverse judgments or settlements.

Our operating results will continue to be affected by seasonal trends, by general conditions in the IT market, and by general economic conditions. We have experienced, and we expect to continue to experience, some degree of seasonality due to customer buying cycles. We believe that the third and fourth quarters will generally have higher net sales levels due to customer budgeting and procurement cycles, which may depress net sales in other quarters. In addition, European sales are often weaker during the summer months. In the past, revenue in our fourth quarter of each year has typically been higher than revenue in prior quarters for the year, and we typically see a sequential decline in revenue from the fourth quarter of a year to the first quarter of the following year. While it is difficult to predict revenue in any quarter, we expect that this pattern will continue in the future. Many of the factors that create and affect seasonal trends are beyond our control.

Our quarterly sales have also reflected a pattern in which a disproportionate percentage of each quarter s total sales occur toward the end of the quarter, and this trend has become more pronounced in recent periods. Our acquisition of LANDesk continues this trend with a greater proportion of our software revenue coming from software license and subscriptions booked in the last weeks or days of each quarter. This uneven sales pattern makes prediction of revenue, earnings, and working capital for each financial period difficult, increases the risk of unanticipated variations in quarterly results and financial condition, and places pressure on our hardware inventory management and logistics systems. If predicted demand for hardware is substantially greater than orders, there will be excess inventory. Alternatively, if hardware orders substantially exceed predicted demand, we may not be able to fulfill all of the orders received in the last few weeks of each quarter. Other developments late in a quarter, such as a systems failure, component pricing movements, actions or announcements from our competitors, global logistics disruptions, or large sales opportunities not being completed when predicted, could adversely impact inventory levels and results of operations in a manner that is disproportionate to the number of days in the quarter affected. In addition, accounting requirements associated with satisfying the various elements necessary to recognize software revenue may result in significant fluctuations in our quarterly results.

In order to remain competitive and provide our increasingly sophisticated customers with more options, we have made and expect to continue to make new software purchasing and licensing options available to our customers. These options may result in an increase in contracts where software revenue is deferred or cash is received over time as opposed to recognition of revenue or payment at or about the time of the purchase or license.

We believe that quarter-to-quarter comparisons of our historical financial results are not meaningful indicators of our future operating results, and you should not rely on them as an indication of our future performance. If our quarterly operating results fail to meet the expectations of equity research analysts, the price of our common stock could be negatively affected.

Our gross margins are expected to vary and may decline.

Gross margins may vary or decline from period-to-period depending on a number of factors, including:

• The ratio of OEM sales to branded sales, since OEM sales typically have lower gross margins than branded sales;

• The ratio of sales through indirect channels to direct sales, since indirect sales typically have lower gross margins than direct sales;

• Product mix, because sales of some of our products and technologies will have lower gross margins than sales of other products or technologies (e.g. our software products tend to have higher gross margins);

- Raw materials, freight, and labor costs;
- Introduction of new products, services, and technologies by us and by our competitors; and
- The level of outsourcing of our manufacturing and assembly services for our hardware products.

We expect that our gross margins may vary and may decline in the future primarily due to the factors listed above and to increased competition and the introduction of new products and technologies that may affect product prices and demand for our products.

A substantial portion of our business consists of sales to a limited number of OEM customers that are not obligated to continue doing business with us, and these sales vary considerably from quarter to quarter.

A substantial portion of our sales is concentrated among a limited number of OEM customers. Sales to these OEMs represented approximately 40% of net sales in 2006, 48% of net sales in 2005, and 45% of net sales in 2004. Sales to Hewlett-Packard represented approximately 14% of our net sales in 2006, 20% of our net sales in 2005, and 23% of our net sales in 2004. Sales to Dell represent approximately 14% of net sales in 2006, 15% of our net sales in 2005, and 12% of our net sales in 2004.

We have experienced, and we expect to continue to experience, period-to-period variability in sales to these OEM customers. Any cancellation, rescheduling, or reduction of orders by OEM customers in the future could materially adversely affect our operating results. Although our OEM customers typically place orders for products up to several months prior to scheduled shipment dates, these orders are subject to cancellation.

Our OEM business is subject to many risks, including:

- Contract termination or reduced or delayed orders;
- Short order cycles and difficulty in predicting sales because our OEM customers do not have long-term commitments to purchase from us;
- Changes in the OEMs internal product life cycles including the delay of planned new product introductions and uncertainty over product end-of-life decisions;
- Adoption of competing products or technologies developed by third parties for the OEMs, acquisition or internal development of competing products or technologies by the OEMs, or changes in the OEMs marketing of competing products or reduced marketing of our products;
- Changes in corporate ownership, financial condition, business direction, sales compensation related to our products, or product mix by the OEMs.

Any of these risks could have a material adverse effect on our business, financial condition, and results of operations. We have experienced, and expect to continue to experience, pricing pressures and significant variability in orders from our OEM customers, which may in the future have a material adverse effect on our quarterly sales and operating results.

The loss of one or more large OEM customers would materially harm our business. While we have contracts with some of our existing OEM customers, none of our OEM customers is obligated to purchase products from us except pursuant to binding purchase orders. Consequently, any OEM customer could cease doing business with us at any time. Our dependence upon a few OEMs also results in a significant concentration of credit risk, thus a substantial portion of our trade receivables outstanding from time to time may be concentrated among a limited number of customers. In addition, OEM customers have longer payment cycles that increase the likelihood of aged or problem accounts receivable.

We use multiple warehouses for many of our OEM customers to fulfill their hardware orders under a just-in-time inventory management system, which requires us to maintain sufficient inventory levels of our hardware products at each of these warehouses to satisfy our OEMs anticipated customer demand, and we generally recognize revenue only when these OEM customers take possession of our hardware products. We are required to plan production, order components, and undertake our manufacturing activities prior to the time that these orders become firm or the products are accepted. In addition, our OEM customers have requested, and are likely to continue to request from time to time, that we delay shipment dates or cancel orders for hardware products that are subject to firm orders. As a result, at any time we may be holding a significant amount of OEM-branded hardware products in inventory, and our sales to OEMs for future quarters are difficult to predict. The inability to accurately predict the timing and volume of hardware orders for our OEM customers during any given quarter could adversely affect operating results for that quarter and, potentially, for future quarters. If we underestimate sales, we may not be able to fill orders on a timely basis. This could cause customer dissatisfaction and loss of future business. If we overestimate sales, we may experience increased costs from inventory storage, waste, and obsolescence.

A substantial portion of our business consists of sales to a limited number of resellers and distributors that are not obligated to continue doing business with us, and these sales vary considerably from quarter to quarter.

A substantial portion of our sales consists of sales of our branded products to a limited number of resellers and distributors. Sales to resellers and distributors represented approximately 56% of net sales in 2006,48% of net sales in 2005, and 52% of net sales in 2004. The loss of significant revenue opportunities with these resellers and distributors could negatively impact our results of operations. In addition, many of these customers also have or distribute competing products. If resellers and distributors elect to increase the marketing of competing products or reduced marketing of our products, our ability to grow our business will be negatively impacted and will impair one of our substantial revenue sources.

Our reseller and distributor business is subject to many risks, including:

- Concentration of business in a limited number of resellers and distributors could result in significant damage to our business upon the termination of our reseller relationship;
- Termination of our reseller and distributor agreements or reduced or delayed orders;
- Difficulty in predicting sales to reseller and distributors who do not have long-term commitments to purchase from us, which requires us to maintain sufficient inventory levels to satisfy anticipated demand;

- Lack of visibility of end user customers and revenue recognition and channel inventory issues related to sales by resellers and distributors;
- Resellers and distributors electing to resale or increase their marketing of competing products or technologies or reduced marketing of our products; and
- Changes in corporate ownership, financial condition, business direction, sales compensation related to our products, or product mix by the resellers and distributors.

Any of these risks could have a material adverse effect on our business, financial condition, and results of operations. We have experienced, and expect to continue to experience, pricing pressures and significant variability in orders from our resellers and distributors, which may in the future have a material adverse effect on our quarterly sales and operating results.

The loss of one or more large reseller and distributors would materially harm our business. While we have reseller and distributor agreements, none of our resellers or distributors are obligated to purchase products from us. Consequently, any reseller or distributor could cease doing business with us at any time. Our dependence upon a few resellers and distributors could result in a significant concentration of credit risk, thus a substantial portion of our trade receivables outstanding from time to time may be concentrated among a limited number of customers. In addition, the inability to accurately forecast the timing and volume of orders for sales of branded products to resellers and distributors during any given quarter could adversely affect operating results for such quarter and, potentially, for future periods. If we underestimate sales, we will not be able to fill orders on a timely basis. This could cause customer dissatisfaction and loss of future business. If we overestimate sales, we will experience increased costs from inventory storage, waste, and obsolescence.

We will need to expand sales through distributors and resellers in order to develop our business and increase revenue.

We expect to rely increasingly on distributors and resellers, VARs (including LANDesk VARs who are also referred to as Expert Service Providers or ESPs), and systems integrators for the distribution and sale of our branded hardware and software products. Our strategy contemplates the expansion of our distributor and reseller network both domestically and internationally, particularly in Asia, and an increase in the number of customers licensing our products through these expanded channels. Our future success will depend in part on our ability to attract, train, and motivate new distributors and resellers and expand our relationships with current distributors and resellers. We may not be successful in expanding our distributor and reseller relationships. We will be required to invest significant additional resources in order to expand these relationships, and the cost of this investment may exceed the margins generated from this investment. Conducting business through indirect sales channels presents a number of risks, including:

- Difficulties in replacing any lost or terminated distributors or resellers;
- Existing or new distributors and resellers may not be able to effectively sell our current or future products or services;
- Potential distributors and resellers deciding not to enter into relationships with us because of our existing relationships with other distributors and resellers with which they compete;
- Our ability to provide proper training and technical support to our distributors and resellers;
- Distributors and resellers electing to place greater emphasis on products or services offered by our competitors; and

- The lack of direct control over the business practices, marketing, sales and services offered by distributors and resellers;

As we expand our distribution and reseller channels, we will also need to expand our sales organization and invest substantial resources toward this expansion. We may experience difficulty recruiting, training, and retaining qualified sales personnel, and any failure to obtain, train, and keep qualified personnel could limit our ability to sell products.

In addition, distributors and resellers of our hardware products often have rights of return, and in the future, these returns from our existing or any new distributors and resellers may have a material adverse effect on our business, financial condition, and results of operations. Our agreements with our current distributors and resellers are generally nonexclusive and may be terminated on short notice by either party without cause, and any new distributor or reseller agreements are likely to contain similar provisions. Distributors and resellers are not obligated to purchase products from us and frequently offer products from several different companies, including competitors products, and distributors and resellers may give higher priority to the sale of our competitors products. A reduction in sales efforts or efficiency by our distributors or resellers could lead to a reduction in our sales and could materially adversely affect our business, financial condition, and results of operations.

We are dependent upon third-party suppliers and outsourced manufacturing for our hardware products. Disruption of our access to these supplies and services, or problems with the quality of supplies or services, could prevent us from filling customer orders and harm our business.

The principal components of our hardware products are electronic components, power supplies, semiconductors, memory, cable assemblies, line filters, enclosures, and printed circuit boards, all of which are purchased from outside vendors. We generally buy components under purchase orders and generally do not have long-term agreements with our suppliers. Also, we generally do not maintain large inventories of components. Any termination of, or significant disruption of, our relationships with the suppliers of our product components may prevent us from filling customer orders in a timely manner which could result in customer dissatisfaction and lost sales.

We have occasionally experienced, and we may in the future experience, shortages or delays in delivery of components. Although alternate suppliers are available for most of the components and services needed to produce our products, the number of suppliers of some components is limited, and qualifying a replacement supplier and receiving components from alternate suppliers could take several months.

We have limited ability to control quality issues (particularly with respect to faulty components manufactured by third parties), and we depend upon suppliers to deliver components that are free from defects, competitive in functionality and cost, and in compliance with specifications and delivery schedules. Disruption in supply, a significant increase in the cost of one or more components, failure of a third party supplier to remain competitive in functionality or price, or the failure of a supplier to comply with any of our procurement needs could delay or interrupt our ability to manufacture and deliver our products to customers on a timely basis, thereby delaying our revenue recognition and adversely affecting our business, financial condition, and results of operations.

We rely on third party manufacturers for subassembly of products and for final assembly, quality assurance, and testing of some of our products. These outsourcing arrangements and any future outsourcing arrangements involve numerous risks, including the economic and financial viability of these manufacturers, reduced control over product quality, delivery schedules, manufacturing yields, and costs. Moreover, although arrangements with such manufacturers may contain provisions for warranty obligations on the part of such manufacturers, we are primarily responsible to our customers for warranty obligations.

Our hardware products are subject to warranty claims and returns. Increased warranty claims or returns could harm our business.

We typically offer a 30-day unconditional money-back guarantee on our appliance products sold in North America. We also offer warranties for parts and service on all our hardware products, ranging from one to three years (and, in the case of some of our Equinox branded products, five years). Although our historical return experience has not been significant, our returns may increase in the future. An increase in returns would have an adverse effect on our sales and could negatively affect our financial results.

For our software products, sales are final and we do not generally allow any returns. We provide a ninety day warranty on the media used to deliver the software, which is not applicable to electronic downloads, and we often provide a limited warranty (usually no more than ninety days) that our products will function in accordance with the user documentation.

In the future, we may, as a result of competitive pressures or customer demands, change our warranty policies or our warranty terms to provide coverage that is greater in scope and duration than the coverage we currently offer. If we were to increase our warranty coverage, our risk of warranty claims, and therefore our warranty expense and reserves, would likely increase.

We must meet the increased demands on customer service operations or customer satisfaction and sales could suffer.

Continued growth of our sales is likely to be accompanied by increasing demands on customer service operations. As a result of our commitment to a high level of customer service, we will need to invest significant resources in the maintenance and improvement of our customer service resources. Any failure to maintain adequate customer service could cause customer dissatisfaction, result in reduced sales of products and, accordingly, materially adversely affect our business, financial condition, and results of operations.

If we are unable to successfully develop our international distribution and reseller networks and international sales efforts, results of operations may suffer.

We are working to develop, integrate, and expand our international distribution and reseller networks in an effort to increase international sales of switching, extension, remote access, systems management and security software, and other products. We may not be successful in developing or expanding the international distribution and reseller network or in marketing and selling products in foreign markets, particularly Asia. If the revenue generated by our international sales is not adequate to recover the expense of establishing, expanding, and maintaining an international distribution and reseller network, our business, financial condition, and results of operations could be materially adversely affected. If international sales become a more significant component of net sales, our business could become more vulnerable to the risks inherent in doing business on an international level, including:

- Difficulties in managing foreign distributors and resellers;
- Longer payment cycles and problems in collecting accounts receivable;
- The effects of seasonal customer demand;
- Changes in regulatory requirements;
- Difficulties in meeting the requirements of different international product regulations, including import and export requirements;
- Risks relating to the protection of our intellectual property rights;
- The impact on our marketing expenses and our research and development resources as we localize our product offerings to meet local user requirements such as language translations and hardware compatibility issues;
- Export restrictions, tariffs, and other trade barriers;
- Fluctuations in currency exchange rates; and
- Potentially adverse tax consequences and political instability.

The existence or occurrence of any one of these factors could have a material adverse effect on our business, financial condition, and results of operations.

Due to the international nature of our business, political or economic changes or other factors could harm our future revenue, increase our costs and expenses, and impair our financial condition.

We are a global company with sales, manufacturing, and research and development efforts around the world. Sales outside the United States generate approximately half of our revenue, over half of our manufacturing takes place outside the United States, and we have research and development centers in several locations outside the United States. Accordingly, our business, operating results, future revenue, gross margin, expenses, and financial condition could suffer due to a variety of international factors, including:

- Ongoing instability or changes in a country s or region s economic or political conditions, including inflation, recession, interest rate fluctuations, and actual or anticipated military or political conflicts, particularly in areas where we have offices or other facilities;
- Currency fluctuations, which could contribute to variations in sales of products and technologies and could also affect our reported results expressed in U.S. dollars;
- Longer accounts receivable cycles and financial instability among customers;

- Tax or trade regulations, tariffs, duties, and procedures and actions affecting production, pricing, and marketing of or payments for products;

- Local labor conditions and other regulations;

- Differing technology standards or customer requirements;

- Limited or unfavorable intellectual property protection in certain foreign countries including the loss of proprietary information due to piracy or misappropriation;

- Fluctuations in freight costs and disruptions at important geographic points of exit and entry;

- Natural or manmade disasters, such as earthquakes, tsunamis, hurricanes, typhoons, fires, power shortages, blackouts, or telecommunications failures;

- Medical epidemics, such as avian flu or Severe Acute Respiratory Syndrome (SARS);

- Seasonal reductions in business activity in certain foreign countries, such as the summer months in Europe;

- Compliance with a wide variety of complex laws, treaties, and regulations that increase the risks of doing business in certain foreign countries;

- Restrictions against repatriation of earnings from our international operations;

- Difficulties in staffing and managing international operations, including the difficulty in managing a geographically dispersed workforce;
- Possible non-compliance with our Code of Conduct or other corporate policies due to inconsistent laws, interpretations, and/or application of corporate standards in foreign countries;
- Increased financial accounting and reporting burdens and complexities; and
- The need to localize our products.

The factors described above also could disrupt our product development and manufacturing, key suppliers, and OEMs and resellers located outside of the United States. For example, we rely on manufacturers in Asia and Europe for the assembly and manufacture of many of our hardware products, and we conduct substantial software development and testing operations in China. Accordingly, we are directly affected by economic, political, and military conditions in China. Any interruption or curtailment of trade between China and its present trading partners could materially adversely affect our product development, product releases, support, business, operating results, and financial condition.

Continued or increased international political instability, evidenced by the threat or occurrence of terrorist attacks, enhanced national security measures in the United States, sustained military action or other conflicts, or strained international relations may impair our ability to do business, increase our costs and adversely affect our stock price. Increased international instability may negatively impact our ability to obtain adequate insurance at reasonable rates or require us to take extra security precautions for our domestic and international operations.

Fluctuations in the value of foreign currencies could result in currency exchange losses.

Currently, a majority of our international business is conducted in U.S. dollars. However, as we expand our international operations, it is likely that international business will increasingly be conducted in foreign currencies. In particular, the introduction of the euro has led many of our European customers to request or insist that our sales to them be denominated in euros instead of U.S. dollars and sales from our software operations are frequently conducted in foreign currencies. Fluctuations in the value of foreign currencies relative to the U.S. dollar have caused, and are expected to increasingly cause, currency transaction gains and losses. In addition, currency fluctuations could also affect our reported results expressed in U.S. dollars. While we attempt to hedge our foreign currency exposure, we cannot predict the effect of exchange rate fluctuations upon future quarterly and annual operating results, and we may experience currency losses in the future.

The sales cycle for our software products is unpredictable, making it difficult to forecast operating results for any given period.

The sales cycle for our software products is typically ninety to one hundred eighty days or longer. This sales cycle is subject to a number of significant risks over which we have little or no control, including:

- Customers budgetary constraints, internal acceptance requirements, and procurement procedures;
- Concerns about the actions or announcements of our competitors and their products;
- Concerns about the future or performance of our company; and
- Changes in economic conditions generally and in the technology market specifically.

For large opportunities, especially for enterprise-wide sales, the sales cycle is often significantly longer than our average sales cycle. In addition, these large opportunities are more difficult to forecast, and if we do not correctly forecast the timing in a given period, the amount of revenue we recognize in a period could be lower than we expect, which could negatively affect our operating results for the then current period and future periods over which revenue would have been recognized. In addition, the terms and conditions of the legal agreements for these large opportunities are often based on our customers purchase agreements and may contain terms that are generally less favorable to us than our standard terms and conditions. As a result, revenue recognition may be delayed.

Our software revenue is dependent on sales to existing customers or the renewal of annual software upgrade protection or maintenance services by existing customers.

Our LANDesk Division has historically derived, and plans to continue to derive, a significant portion of our total software revenue from existing customers who purchase additional products or annual maintenance or upgrade protection. We depend on our installed base of software customers for future revenue from the purchase of annual software upgrade protection or maintenance services. As we introduce new software products, our current customers may not require or desire the functionality of our new products and may choose not to license these products or renew their agreements for maintenance or upgrade protection. If our customers do not purchase additional products or increased numbers of products already in use, or renew annual software upgrade protection or maintenance services, our ability to increase or maintain revenue levels could be limited to only new customers.

Maintenance revenue related to the licensing of our software products is a significant part of our current and future operating revenue. In general, maintenance fees increase with the increase in the use of our software. Accordingly, we receive higher maintenance fees with new license agreements and as existing customers install more of our software products on additional systems. Due to increased discounting for larger sales opportunities, maintenance fees on a per unit basis for such large deals can be lower than average. In addition, customers are generally provided reduced annual maintenance percentages for entering into long-term maintenance agreements. Declines in our license bookings, increases in long-term maintenance agreements, customers electing to migrate to competitive products of find alternatives to our products, and/or increased discounting could lead to reduced software maintenance revenue and reduced gross margins.

Our software products are designed with interoperability or compatibility with many third-party platforms, systems, and applications, the absence of which may harm our business.

Our software products are designed for use with specific third-party platforms, systems, and applications. We believe the breadth of our integration with such platforms, systems and applications is a significant competitive advantage. Any significant change in these third party products could result in the loss of interoperability or compatibility with our products, making our products less attractive, increasing our research and development costs in order to modify our products, license new solutions, or develop new products, and potentially harming our future revenue. Our failure to anticipate, manage and adapt to these risks could result in significant delays in our product releases, changes in our product roadmaps, loss of current customers for whom the lost compatibility is an issue, and damage to our operating results.

Our software products include third-party content or code upon which we rely for the interoperability, integration, development, or updates of our products, and disruption of our access to such code or content could delay product releases, inhibit our compatibility with third party products, and harm our business.

The principal components of our software products are proprietary code and content. We do, however, rely on some third-party code or content, and we expect to use such third-party code or content in future products. Although we believe that there are adequate alternative sources for the technology licensed to us, any significant interruption in the availability of these third-party software products on commercially acceptable terms or any defects in these products could delay development of future products or enhancement of our future products and harm our revenue. Use of such third party code or content presents risks such as:

- Owners or licensees of third-party systems could adopt more restrictive policies or impose unfavorable terms and conditions for access to their products making it more difficult for us to make our products compatible with their products and resulting in higher research and development costs for us for the enhancement or modification of our existing products and the development of new products;

- Functionality provided by third-party code or content in our products may become obsolete, defective, or incompatible with future versions of our products, may not be adequately maintained or updated, and we may be unable to find viable alternatives or develop our own proprietary solution;

- Quality, warranty, and support terms vary dramatically when licensing third party code and content, and we have limited ability to control quality issues with third-party code and content and must we depend on our own research and development personnel to evaluate and select third-party code that we believe is of the most value to our customers; and

- Technical difficulties in integrating our products and third party code or content to create a combined solution, and the risk that customers will not perceive the need for such integrated solutions.

Any significant termination of a third-party license, change in third-party license provisions, increase in the cost of such third-party code or content, failure of a code or content provider to remain competitive in functionality, or defect in or quality issue with third-party code could delay or interrupt our ability to develop and deliver software products to customers on a timely basis. This could delay our revenue recognition and adversely affect our business, financial condition, and results of operations and possibly expose us to claims under license agreements with our customers. Our failure to anticipate, manage, and adapt to these risks could result in significant delays in our products releases, changes in our product roadmaps, and damage to our operating results.

Software errors or bugs, and possible product liability claims related to such errors or bugs, could result in increased costs, damage to our reputation, and loss of market share.

Our software products are generally large and intricate programs. As a result, our current software products, updates, upgrades or future products may contain errors, failures, or bugs, some of which may not become known until after the product has been released by us for use by customers. While we routinely test our products for such errors and identify and correct bugs through our customer support group, these problems are inevitable. Any significant errors may result in, among other things, loss of, or delay in, the market acceptance or our products, lost revenue and sales of our products, reallocation of, or increases in, development and customer support resources, impairment to our reputation, loss of future renewal or maintenance revenue, and increased service and warranty costs. Errors could also result in significant delays in the release of updates, upgrades, or new products while such errors are corrected. Moreover, because our products primarily support other systems and applications, any software errors or bugs in these other systems or applications may affect the performance of our software, and it may be difficult or impossible to determine where the errors reside. As a result, product errors, failures, or bugs could result in significant harm to our business and have a material adverse effect on our results of operations.

We may be subject to legal actions or claims for damages related to product errors which could, whether or not successful, increase costs and distract our management and our development and support teams and could harm our business, result in unexpected expenses and damage our reputation. Our license agreements with our customers typically contain provisions designed to limit exposure to potential product liability claims, and our standard agreements in many jurisdictions also provide that we will not be liable for indirect or consequential damages caused by the failure of our products. In certain jurisdictions, however, warranty and limitation of liability provisions are not effective.

Use of open source software or technology in our products may reduce our ability to control the quality and support for products and may result in damage to our operating results.

Open source software is software that is made widely available by its authors or other third parties and is often licensed on an as is for a nominal fee or, in some cases, at no charge. We have incorporated some open source software into our products, allowing us to enhance certain solutions without incurring substantial additional research and development costs. While we have not experienced any material problems as a result of our use of open source software, use of open source software entails significant risks including:

- Open source software or technology becoming competitive with our proprietary technology, which could cause sales of our products to decline or force us to reduce the fees we charge for our products, which could have a material adverse impact on our revenue and operating margins;
- Requiring that we make available the source code for any modifications or derivative works we make to or from the open source software, and that we license or contribute such modifications or derivative works under the terms of a particular open source license or other license granting third parties certain rights of further use;
- Our proprietary software could be combined with open source software in such a way that we would be required to release the source code of our proprietary software; and
- The lack of any warranty, maintenance, or support for most open source software or technology.

We have established processes to help minimize these risks to the extent within our control, including a review process for screening requests from our development organizations for the use of open source, but we cannot be sure that all open source software or technology is submitted for approval prior to use in our products or that all use is in compliance with our corporate policies. These risks, if not eliminated, could negatively affect our business.

Executive officers and other key personnel may depart, which could adversely affect our results of operations and harm our ability to grow the business.

We are greatly dependent on the ability to retain key management, sales, and technical personnel, and our future success is highly dependent upon the personal efforts of our management, sales, and technical personnel and other key employees. The loss of services of key personnel, including those who recently joined us a result of the Cyclades and LANDesk acquisitions, could have a material adverse effect on our business, financial condition, and results of operations. We have attempted to mitigate these risks by offering key Cyclades and LANDesk employees retention bonuses (payable only if they continue employment with us for specified periods) and equity awards, but there is the risk that we could nevertheless lose key management, sales, and technical employees.

We have historically used stock options and are currently using restricted stock units as a key component in our executive and employee compensation programs in order to align employees interests with the interests of our stockholders, encourage employee retention, and provide competitive compensation packages. Many of our employee stock options are fully vested. This could affect our ability to retain present employees. In addition, we are now required to record a charge to earnings for employee stock option grants and other equity incentives. Moreover, applicable stock exchange listing standards relating to obtaining stockholder approval of equity compensation plans could make it more difficult or expensive for us to grant options to employees in the future. As a result, we may incur increased compensation costs, change our equity compensation strategy, or find it difficult to attract, retain, and motivate employees, any of which could materially adversely affect our business.

As we expand our international operations, we will be required to recruit and retain experienced management, sales and technical personnel in our international offices, and we expect that the identification, recruitment, training and retention of such personnel will require significant management time and effort and resources. Competition for employees with the skills required, particularly engineering and other technical personnel, is intense, and there can be no assurance that we will be able to attract and retain highly skilled employees in sufficient numbers to sustain our current business or to support future growth. We may need to pay recruiting or agency fees and offer additional compensation or incentives to attract and retain these and other employees, resulting in an increase to our operating expenses.

Difficulties encountered during changing economic conditions could adversely affect our results of operations.

For the last several years, we have experienced rapid revenue and customer growth and expansion in the number of employees, product offerings, customers, operating locations, and suppliers. In addition, we have acquired a number of companies in the same time period. This growth and these acquisitions have resulted in increased responsibilities and placed significant strain on our managerial, operational, and financial resources and resulted in new and increased responsibilities for management personnel. There can be no assurance that our management, personnel, systems, procedures, and controls are, or will be, adequate to support our existing and future operations or that we will continue to grow. If we fail to recruit and retain sufficient and qualified managerial, operational, or financial personnel or to implement or maintain internal systems that enable us to effectively manage our growing business and operations worldwide, our financial results in any given period may be adversely affected and our business and financial condition could be materially harmed.

Our ability to effectively manage during changing economic conditions will require us to continue to implement and improve our operational, financial, and information systems and internal controls and will likely require additional management personnel. In addition, we believe that we must continue to develop greater engineering, financial, marketing, sales, and customer service capabilities in order to develop new products and technologies, secure new customers, and effectively serve the evolving needs of present and future customers. We may not be successful in strengthening these capabilities. Without adequate management, engineering, financial, product development, marketing, sales, and customer service capabilities, our ability to effectively manage during changing economic conditions, expand and enhance our product lines, further penetrate existing markets, and develop new markets will be significantly limited. If we are unable to effectively manage during changing economic conditions, our business, financial condition, and results of operations could be materially adversely affected.

Because our business and operating results depend to a significant extent on the general conditions in the server market, any adverse change in the server market due to adverse economic conditions, declining capital spending levels, or other factors could have a material adverse effect on our business, financial condition, and results of operations. In addition, we continue to see industry-wide initiatives by OEMs and by distributors and resellers of our hardware products to reduce their inventories and to shorten their lead times, thereby reducing early commitments to firm orders by our major OEM and our distributor and reseller customers.

Our reorganization efforts may disrupt our business or affect our profitability.

In the first quarter of 2006 we reorganized into five business divisions in an effort to streamline our operations and put vital decisions closer to our customers. With the acquisition of LANDesk, we have merged our Mobile Solutions Division into the LANDesk operations, and we are making other management changes within the LANDesk Division. These reorganization efforts could confuse and distract our customers, suppliers, and employees. In addition, these reorganization efforts could adversely affect or delay our development and introduction of new products and technologies, result in the loss of management, technical, or other key personnel, disrupt our supplier or customer relationships, jeopardize our supplier or sales channels and our branding and marketing efforts, and increase our administrative expense, all of which could affect our profitability.

Our line of credit could adversely affect us and our operations.

In the second quarter of 2006, we obtained a $250,000,000 unsecured, five-year, revolving, bank line of credit, and we used borrowings under this line of credit to fund a portion of the LANDesk acquisition and the purchase of our shares under our recently-expanded stock repurchase program. Interest expense on borrowings and additional future borrowings under the line of credit could adversely affect our future net income, margins, expenses, and financial conditions by:

- Requiring us to dedicate a substantial portion of our cash flow from operations to payments on our indebtedness, which would reduce the availability of our cash flow to fund internal growth through working capital and capital expenditures and for other general corporate purposes;

- Increasing our vulnerability to economic downturns in our industry;

- Increasing our vulnerability to interest rate increases to the extent any of our variable rate debt is not hedged;

- Placing us at a competitive disadvantage compared to our competitors that have less debt in relation to cash flow;

- Limiting our flexibility in planning for or reacting to changes in our business and our industry;

- Limiting, among other things, our ability to borrow additional funds, refinance the line of credit, or obtain other financing capacity; and

- Subjecting us to a risk of noncompliance with financial and other restrictive covenants in our indebtedness.

The line of credit contains affirmative and negative covenants, including limitations on our ability to (i) make distributions, investments, and other payments unless we satisfy certain financial tests or other criteria, (ii) incur additional indebtedness, and (iii) make acquisitions and capital expenditures. All of these restrictions could affect our ability to operate our business and may limit our ability to take advantage of potential business opportunities as they arise. The failure to comply with these covenants could result in an event of default which, if not cured or waived, could have a material adverse effect on us.

Our ability to comply with these provisions of our line of credit may be affected by changes in the economic or business conditions or other events beyond our control. If we do not comply with these covenants and restrictions, we could be in default under our line of credit, and our debt, together with accrued interest, could then be declared immediately due and payable. There can be no assurance that we will be able to obtain sufficient funds to enable us to repay or refinance our debt obligations on commercially reasonable terms or at all. We also face interest rate risk on our bank line of credit which currently bears interest at a variable rate of LIBOR plus 87.5 basis points. We have partially hedged this exposure to interest rate risk with an interest rate swap, which has a notional amount of $125 million, through a well established financial institution.

Unanticipated changes in our tax rates or exposure to additional income tax liabilities could affect our profitability.

We are subject to income taxes in both the United States and various foreign jurisdictions, and our domestic and international tax liabilities are subject to the allocation of expenses in different jurisdictions. Our effective tax rates could be adversely affected by changes in the mix of earnings in countries with differing statutory tax rates, in the valuation of deferred tax assets and liabilities, in tax laws, or by material audit assessments, which could affect our profitability. In addition, the amount of income taxes we pay is subject to audit in various jurisdictions, and a material assessment by a governing tax authority could affect our profitability.

Failure to maintain adequate internal systems and effective internal controls over our financial reporting and information systems could result in our management and auditors being unable to certify the effectiveness of our internal controls over financial reporting and information systems, which could harm our business reputation and cause our stock price to decline.

Section 404 of the Sarbanes-Oxley Act of 2002 requires that we implement and maintain adequate internal systems and effective internal controls over financial reporting and information systems. We have not yet completed our review and assessment of the internal systems and controls over the LANDesk financial reporting and information systems, and we have until December 31, 2007 to do so. The absence of such controls could have a material adverse effect on our business, financial condition, and results of operations. In addition, correction of any significant deficiencies or material weaknesses (as defined under PCAOB guidelines) could require additional remedial measures including hiring additional personnel which could be costly and time-consuming. If a significant deficiency or material weakness exists as of a future period year-end (including a material weakness identified prior to year-end for which there is an insufficient period of time to evaluate and confirm the effectiveness of the corrections or related new procedures), our management and our auditors will be unable to report favorably as to the effectiveness of our control over financial reporting or information systems. This could result in a loss of investor confidence in the accuracy and completeness of our financial reports and our management, which could result in a decline of our stock price, damage to our business reputation, and potential litigation.

Changes in accounting standards or the interpretation of accounting standards, especially changes related to revenue recognition, could cause significant impact on our revenue or earnings.

Based on our interpretation of current accounting standards, we believe we have properly reported our current sales and license revenue. New accounting standards or regulations, changes to current accounting standards, or different interpretations of existing accounting standards in the future could result in corresponding changes in our revenue recognition or other accounting policies that could have a material adverse effect on our financial condition and operating results.

Unforeseen environmental costs could negatively affect our future earnings.

Some of our operations use substances regulated under various federal, state, and international laws governing the environment, including those governing the discharge of pollutants into the air and water, the management and disposal of hazardous substances and wastes, and the cleanup of contaminated sites. Many of our products are subject to various federal, state, and international laws governing chemical substances in products, including those regulating the manufacture and distribution of chemical substances and those restricting the presence of certain substances in electronics products. We could incur substantial costs, including cleanup costs, fines, civil or criminal sanctions, third-party property damage, or personal injury claims if we were to violate or become liable under environmental laws or if our products become non-compliant with environmental laws. We also face increasing complexity in our product design and procurement operations as we adjust to new and future requirements relating to the materials composition of our products, including the restrictions on lead and certain other substances that will apply to specified electronics products put on the market in the European Union as of July 1, 2006 (Restriction of Hazardous Substances Directive) and similar legislation currently proposed in China and other countries. The ultimate costs under environmental laws and the timing of these costs are difficult to predict, and liability under some environmental laws relating to contaminated sites can be imposed retroactively and on a joint and several basis.

We could also face significant costs and liabilities in connection with product take-back legislation. The European Union has finalized the Waste Electrical and Electronic Equipment Directive (WEEE), which makes producers of electrical goods, including computers and peripherals, financially responsible for specified collection, recycling, treatment, and disposal of past and future covered products. This deadline to enact and implement the directive by individual European Union governments generally was August 13, 2004, although extensions were granted to some countries (such legislation, together with the directive, the WEEE Legislation), and producers are financially responsible under the WEEE Legislation beginning in August 2005. Similar legislation has been or may be enacted in other geographies, including in the United States and Japan, the cumulative impact of which could be significant for us. We have incurred some costs and will continue to incur costs under the WEEE legislation but the amount and timing of these costs are difficult to predict.

Provisions in our charter documents and in Delaware law may discourage potential acquisition bids for us and may prevent changes in management that stockholders may favor.

Provisions in our charter documents could discourage potential acquisition proposals and could delay or prevent a change in control transaction that stockholders may favor. These provisions could have the effect of discouraging others from making tender offers for shares, and as a result, these provisions may prevent the market price of our common stock from reflecting the effects of actual or rumored takeover attempts and may prevent stockholders from reselling their shares at or above the price at which they purchased their shares. These provisions may also prevent changes in management that stockholders may favor. Our charter documents do not permit stockholders to act by written consent, limit the ability of stockholders to call a stockholders meeting, and provide for a classified board of directors, which means stockholders can only elect, or remove, a limited number of directors in any given year. Furthermore, the board of directors has the authority to issue up to five million shares of preferred stock in one or more series. The board of directors can fix the price, rights, preferences, privileges, and restrictions of such preferred stock without any further vote or action by our stockholders. The issuance of shares of preferred stock may delay or prevent a change in control transaction without further action by our stockholders.

In addition, Delaware law may inhibit potential acquisition bids for us. Delaware law prevents certain Delaware corporations, including Avocent, from engaging, under certain circumstances, in a business combination with any interested stockholder for three years following the date that such stockholder became an interested stockholder.

Item 1B. Unresolved Staff Comments.

None

Item 2. Properties.

Our world-wide headquarters, occupying approximately 181,000 square feet and containing administrative, sales, marketing, research and development, manufacturing, and distribution facilities, is located in Huntsville, Alabama, on a 24-acre tract of land owned by us in Cummings Research Park.

Our Redmond, Washington facility, which consists of approximately 82,000 square feet of leased space in an industrial office building, contains administrative, sales, marketing, research and development, and distribution operations and is leased through March 2009. The base rent under the lease is approximately $740,000 per year, plus taxes, insurance, and maintenance of approximately $200,000 per year.

Our LANDesk facility in Salt Lake City, Utah, consists of approximately 56,500 square feet in an office building, and contains administrative, sales, marketing, and research and development operations. The current base rent under the lease is approximately $653,000 per year, plus taxes, insurance, and maintenance of approximately $327,000 per year and is leased through July 2008.

Our primary international administrative, sales, marketing, research and development, manufacturing, and distribution operations are located in a 129,000 square foot building owned by us in the free trade zone in Shannon, Ireland.

We also own a 45,000 square foot building on 6.5 acres of land in Sunrise, Florida. Our Sunrise facility contains sales, marketing, research and development operations. In addition, we lease office space in Fremont, California (administrative, sales, marketing, and research and development), Austin, Texas (sales, marketing, and technical), Taipei, Taiwan (administrative, sales, marketing, and research and development operations), São Paulo, Brazil (administrative, sales, marketing, and research and development operations) and Beijing and Shanghai, China (sales, marketing, and research and development operations).

We also lease sales offices in various United States and international locations, none of which is material to our operations.

We believe that these facilities are sufficient to support our current operations.

Item 3. Legal Proceedings.

In January 2007, we filed a complaint for patent infringement in the United States District Court for the Western District of Washington against Aten Technology, Inc., Aten International Co., Ltd, Belkin Corporation, Rose Electronics and its general partners, and Trippe Manufacturing Company. Some of the defendants have not yet responded to our complaint.

PART II

Item 5. Market For Registrant s Common Equity and Related Stockholder Matters and Issuer Purchases of Equity Securities.

Price Range of Common Stock; Holders of Record

Our common stock is quoted on The NASDAQ National Market System under the symbol AVCT. The following table shows the high and low sales prices of our common stock for each quarterly period within the last two fiscal years as reported by the NASDAQ National Market System.

	High	Low
Quarter ended December 31, 2006	$ 38.50	$ 29.37
Quarter ended September 29, 2006	$ 31.71	$ 23.82
Quarter ended June 30, 2006	$ 34.40	$ 21.98
Quarter ended March 31, 2006	$ 34.86	$ 27.15
Quarter ended December 31, 2005	$ 33.88	$ 26.84
Quarter ended September 30, 2005	$ 35.38	$ 26.48
Quarter ended July 1, 2005	$ 29.09	$ 23.05
Quarter ended April 1, 2005	$ 40.70	$ 22.99

As of February 22, 2007, Avocent had approximately 17,100 stockholders including 300 shareholders of record and 16,800 shareholders in nominee name.

Stock Performance Graph

The following graph compares the cumulative total stockholder return data for our common stock to the cumulative return of (i) the NASDAQ US Index and (ii) the NASDAQ Computer Index for the period beginning January 1, 2002, and ending on December 30, 2006. The graph assumes that $100 was invested at a per share price of $24.25 on January 1, 2002, the closing price on December 31, 2001, and the reinvestment of any dividends. The stock price performance on the following graph is not necessarily indicative of future stock price performance.

* $100 invested on 12/31/01 in stock or index-including reinvestment of dividends. Fiscal year ending December 31.

	12/01	12/02	12/03	12/04	12/05	12/06
AVOCENT CORPORATION	100.00	91.63	150.60	167.46	112.12	139.59
NASDAQ STOCK MARKET (U.S.)	100.00	69.66	99.71	113.79	114.47	124.20
NASDAQ COMPUTER MFG S	100.00	67.48	109.37	115.04	107.28	134.84

The information contained above under the caption Stock Performance Graph is being furnished to the Securities and Exchange Commission and shall not be deemed to be soliciting material or to be filed with the Securities and Exchange Commission, nor shall such information be incorporated by reference into any future filing under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, except to the extent that we specifically incorporate it by reference into such filing.

Dividend Policy

We have not declared or paid any cash dividends in the past and, for the foreseeable future, we expect to retain earnings to finance the expansion and development of our business. The payment of dividends is within the discretion of our Board of Directors and will depend on our earnings, capital requirements and operating and financial condition, among other factors.

Equity Compensation Plan Information

Please see Item 12 of this Annual Report on form 10-K for disclosures relating to our equity compensation plans. Such information is incorporated by reference from our 2007 proxy statement.

Recent Purchases of Treasury Stock

In the fourth quarter of 2004 our Board of Directors approved a stock repurchase program whereby we may, from time to time, purchase up to 2 million shares of our common stock in the open market, in privately negotiated transactions or otherwise, at prices that we deem appropriate. Since the programs initial approval, our Board has added 10 million shares to this program and now a total of 12 million shares is authorized to be repurchased, including 2 million additional shares approved by our Board in February 2007. The plan has no expiration date. Details of purchases under the plan during 2006 are as follows:

Period:	**Total Number of Shares Purchased During the Period**	**Average Price Paid Per Share for Period Presented**		**Total Cumulative Number of Shares Purchased as Part of Publicly Announced Plan**	**Maximum Number of Shares Remaining to Purchase Under the Plan (1)**
January 1, 2006 January 27, 2006	50,000	$	29.35	2,825,000	1,175,000
January 28, 2006 February 24, 2006	250,000	$	33.59	3,075,000	925,000
February 25, 2006 March 31, 2006	525,000	$	32.55	3,600,000	400,000
Quarter ended March 31, 2006	825,000	$	32.67		
April 1, 2006 April 28, 2006		$		3,600,000	400,000
April 29, 2006 May 26, 2006	1,169,488	$	23.64	4,769,488	2,230,512
May 27, 2006 June 30, 2006	2,793,887	$	24.22	7,563,375	2,436,625
Quarter ended June 30, 2006	3,963,375	$	24.05		
July 1, 2006 July 28, 2006	948,600	$	25.11	8,511,975	1,488,025
July 29, 2006 August 25, 2006	451,758	$	25.54	8,963,733	1,036,267
August 26, 2006 September 29, 2006		$		8,963,733	1,036,267
Quarter ended September 29, 2006	1,400,358	$	25.23		
September 30, 2006 October 27, 2006	200,000	$	35.85	9,163,733	836,267
October 28, 2006 November 24, 2006	410,000	$	36.83	9,573,733	426,267
November 25, 2006 December 31, 2006	240,000	$	35.13	9,813,733	186,267
Quarter ended December 31, 2006	850,000	$	36.12		
Totals for 2006	7,038,733	$	26.75		

(1) The total shares available for repurchase of 186,267 as of December 31, 2006 does not reflect the additional 2 million shares approved in February 2007.

In August 2006, we re-issued approximately 7,073,000 shares of the repurchased stock above in conjunction with the LANDesk acquisition.

Item 6. Selected Financial Data.

(Amounts in thousands, except per share data and amounts in note (1) below.)

	2006		**2005**		**2004**		**2003**		**2002**	
Net sales	$	519,195	$	369,888	$	365,255	$	304,238	$	260,600
Net income (1)	$	45,532	$	48,349	$	18,040	$	38,547	$	10,738
Basic net income per share	$	0.94	$	0.98	$	0.37	$	0.83	$	0.24
Diluted net income per share	$	0.92	$	0.96	$	0.36	$	0.81	$	0.24
Total assets	$	1,158,854	$	773,751	$	770,781	$	660,763	$	568,607
Unsecured bank line of credit	$	150,000	$		$		$		$	

(1) For the periods presented, we recognized charges for acquired in-process research and development expenses for the following acquisitions: $6.0 million for 2C Computing, Inc. in 2002, $3.9 million for Soronti, Inc. in

2003, and $6.5 million for Crystal Link Technologies, $21.7 million for OSA Technologies, Inc. and $1.1 million for Sonic Mobility Inc. in 2004, $2.1 million for Cyclades Corporation and $18.6 million for LANDesk Group Limited in 2006 (*see Note 3 to the consolidated financial statements*).

Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations.

Overview

Avocent Corporation designs, manufactures, licenses, and sells software and hardware products and technologies that provide connectivity and centralized management of information technology (IT) infrastructure. We (meaning Avocent and its wholly-owned subsidiaries) provide connectivity and systems management products and technologies that centralize control of servers, desktop computers, serial devices, wireless devices, mobile devices, and network appliances, thus increasing the efficiency of IT personnel. Server manufacturers resell private-labeled Avocent KVM (keyboard, video, and mouse) switches and embedded software and hardware technology in their systems, and companies large and small depend on our software and hardware products and technologies for managing their growing IT infrastructure.

Our technological innovations include Internet protocol (IP) based switching, centralized management, and intuitive software interfaces. With more than two decades of experience, we have grown through product innovations, global expansion, and strategic acquisitions. Formed as a result of the merger in 2000 between Apex Inc. and Cybex Computer Products Corporation, we subsequently acquired Equinox Systems Inc. in 2001, 2C Computing, Inc. in 2002, Soronti, Inc. in 2003, Crystal Link Technologies, OSA Technologies, Inc., and Sonic Mobility, Inc. in 2004, and Cyclades Corporation and LANDesk Group Limited in 2006.

Most of our revenue is derived from sales to a limited number of OEMs (who purchase our switching systems on a private-label or branded basis for integration and sale with their own products), sales through our reseller and distributor network, and sales to a limited number of direct customers. Sales to our OEM customers accounted for 40% of sales in 2006, 48% of sales in 2005, and 45% in 2004. Sales to our branded customers accounted for 60% of sales in 2006, 52% of sales in 2005, and 55% of sales in 2004. We do not have contracts with many of our branded customers, and in general, our OEM and branded business customers are obligated to purchase products from us only pursuant to binding purchase orders. The loss of, or material decline in orders from, these customers would have a material adverse effect on our business, financial condition, results of operations, and cash flows. Our top five customers include both OEM and branded customers and accounted for 56% of sales in 2006 and 64% of sales in 2005 and 2004.

We sell products to resellers, distributors, end-users, and OEMs in the United States, Canada, Europe, and Asia as well as in other foreign markets. Sales within the United States accounted for approximately 57% of both 2006 and 2005 sales and 59% of 2004 sales. Sales outside of the United States accounted for 43% of both 2006 and 2005 sales and 41% of 2004 sales. Sales to customers in the Netherlands, including the European distribution facility for one of our OEM customers, accounted for 10% of sales in 2004. No country outside the United States accounted for more than 10% of 2006 or 2005 sales.

With continued industry-wide initiatives to reduce all channel inventories and to shorten lead times, trends with our major customers are, generally, to reduce the number of weeks of forward-committed firm orders. This trend continues to affect our business with certain distributors, OEMs, and other server manufacturers, and we believe that it will continue to make our future sales more difficult to predict and inventory levels more difficult to manage.

We continue to experience significant price competition in the market for all of our products, and we expect that pricing pressures will continue in the future. In addition, general economic conditions are not predictable and we expect our revenue growth rate to fluctuate in relation to economic conditions and IT related spending trends.

Many of our executive officers and directors are vested in significant amounts of options to purchase shares of our common stock and continue to vest in additional shares on a regular basis. These officers and directors have informed us that they have sold, and may sell additional, shares of our common stock to provide liquidity and diversify their portfolios. Additionally, many of the stock options previously granted to employees are now fully vested. During 2006 our board of directors granted both time-based and performance-based restricted stock units (RSUs) with two and three year vestings as our Board moved our equity award program away from traditional stock options.

In the first quarter of 2006, we reorganized our business into five divisions and in the third quarter of 2006, we acquired our sixth division, LANDesk. As of December 31, 2006, we had the following divisions:

- Management Systems Division, which includes our branded and OEM KVM, serial console, power control, and management appliance businesses;

- Embedded Software and Solutions Division, focused on developing and marketing embedded systems and software, including IPMI and embedded KVM technologies, primarily for our OEM customers;

- Connectivity and Control Division, focused on expanding the markets for our serial, extension, and wireless broadcast, point of sale, and audio-visual products;

- Desktop Solutions Division, which is developing new technologies to enable desktop over IP solutions, including blade computers;

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- Mobile Technologies Division, which includes mobile device management and secure wireless systems administration; and

- LANDesk Division, which includes systems, security, and service management solutions for desktops, servers, and mobile devices across the enterprise.

Our largest division on a revenue basis, Management Systems Division, comprised 82% of our consolidated net revenue in 2006 and 89% in 2005, LANDesk, our newest division acquired in August, 2006, contributed 7% of net revenue to 2006 despite only being part of Avocent for four months. Our Embedded Software and Solutions Division, contributed 7% of net revenue in 2006 and 6% in 2005. The other three divisions and unallocated revenues comprised the remaining 4% of our consolidated net revenues in 2006 and 5% in 2005. See Note 16 in the notes to the consolidated financial statements contained in Item 8 of this document.

In the first quarter of 2007, we merged the Mobile Technologies Division into the LANDesk Division and the Embedded Software and Solutions Division into the Management Systems Division to better focus on the respective customer needs and sales channels. We believe our new divisions allow us to focus on new technology and growth opportunities to add product and shareholder value in the future. We believe this structure enhances customer service, speeds delivery of products to market and better focuses Avocent s research, development and marketing expenditures.

Results of Operations

Our consolidated statements of income, stockholders equity, and cash flows reflect the results of acquired companies from the respective dates of acquisition. The following table sets forth, for the periods indicated, selected statement of income data expressed as a percentage of net sales:

	Years Ended December 31,					
	2006		2005		2004	
Net sales	100.0	%	100.0	%	100.0	%
Cost of sales	38.0		40.8		41.7	
Gross profit	62.0		59.2		58.3	
Operating expenses:						
Research and development expenses	12.3		15.4		12.4	
Acquired in-process research and development expense	4.0				8.0	
Selling, general and administrative expenses	28.6		24.4		23.2	
Acquisition integration expenses	0.8					
Amortization of intangible assets	4.4		5.0		6.7	
Total operating expenses	50.1		44.8		50.3	
Income from operations	11.9		14.4		8.0	
Income from settlement of lawsuit			1.4			
Net investment income	1.6		2.5		1.4	
Net realized investment losses	(0.1	)	(0.1	)	(1.1	)
Interest expense	(0.6	)				
Other income (expense), net	(0.1	)	(0.1	)		
Income before provision for income taxes	12.7		18.1		8.3	
Provision for income taxes	3.9		5.0		3.4	
Net income	8.8	%	13.1	%	4.9	%

Revised to Earnings Release

On January 25, 2007, we announced our fourth quarter and year ended December 31, 2006 financial results. In connection with the announcement, we reported net sales for the fourth quarter 2006 increased 57.0% from the fourth quarter 2005 to $167.7 million, and net sales for the year increased to $522.0 million in 2006 from $369.9 million in 2005. In the earnings release, we noted that one of the contributing factors to our increase in net sales was the LANDesk acquisition. As announced, LANDesk comprised $28.5 million of total revenues reported for the fourth quarter. Subsequent to the earnings release, we identified certain transactions that did not meet the necessary revenue recognition criteria and determined that revenues from LANDesk should be lowered by $2.8 million. As a result, fourth quarter net sales were revised to $164.9 million and our net sales for the year ended December 31, 2006 were $519.2 million. This revision of revenue, combined with a related approximate $272,000 reduction in sales, general and administrative expense as well as the identification of a $1.2 million tax benefit related to certain 2006 employee stock option exercises not previously recorded, netted to a reduction in net income by approximately $677,000, or approximately $0.01per share. All necessary corrections to our consolidated financial statements are reflected in the consolidated financial statements included in this Annual Report on Form 10-K.

Years Ended December 31, 2006 and 2005

Net sales. Our net sales consist of sales of keyboard, video, and mouse console switching systems, digital connectivity products and technologies, software licenses and subscriptions, support and maintenance agreements, serial connectivity devices, wireless extension products, IPMI, extension, and remote access and management products and technologies, and royalties from licensing our intellectual property. In 2006, net sales increased to $519.2 million from $369.9 million in 2005. The increase in sales resulted directly from the contribution of revenue from our Cyclades acquisition, completed March 31, 2006, our LANDesk acquisition, completed August 31, 2006, and increased revenue from our traditional products. Branded sales increased 63% from $191.9 million in 2005 to $311.9 million in 2006. As a percentage of sales, branded revenue accounted for 60% of sales in 2006 and 52% of revenue in 2005. OEM sales grew 16% from $178.0 million in 2005 to $207.3 million in 2006. OEM sales were 40% of sales in 2006, compared to 48% of sales in 2005. The Cyclades and LANDesk businesses have a significantly smaller portion of their sales to OEM customers than Avocent has historically had, which explains the change in the percentage mix of our sales. The continued growth of our digital product line contributed to our sales growth for 2006. Sales of our digital products and technologies accounted for $280.4 million or 54% of sales in 2006 compared with $196.7 million or 53% of sales in 2005.

From a divisional perspective, revenue from our Management Systems Division, which is comprised primarily of our traditional KVM business as well as revenue from acquired Cyclades serial management products, increased to $426.4 million in 2006 from $330.2 million in 2005 and accounted for 82% of our revenue in 2006 and 89% of our revenue in 2005. Within our Management Systems Division, revenue from our traditional KVM products increased to $351.3 million in 2006 from $311.7 million 2005. Additionally, revenue from our serial management products, consisting mostly of our Cyclades products, increased to $46.5 million in 2006 from $4.1 million in 2005. Sales by product line for our Management Systems Division for the years ended December 31, 2006 and 2005 are as follows:

	For the years ended December 31, 2006	December 31, 2005
Management Systems Division (MSD) net revenue:		
KVM	$ 351,298	$ 311,734
Serial Management	46,533	4,124
Other	28,581	14,355
Total MSD net revenue	$ 426,412	$ 330,213

The LANDesk Division, resulting from our most recent acquisition on August 31, 2006, contributed $38.7 million of net revenue during 2006 or 7% of our net revenue. LANDesk s revenue and bookings are comprised of both license based revenue, primarily LANDesk Management Suite, and subscription based revenue, primarily LANDesk Security Suite, with the growth in bookings from the subscription based revenue outpacing the license based revenue. This change in mix has an impact on revenue recognized as subscription revenue is deferred and amortized over the subscription term. Sales by product line for our LANDesk Division for the years ended December 31, 2006 and 2005 are as follows:

	For years ended December 31, 2006	December 31, 2005
LANDesk Division net revenue:		
Licenses and royalties	$ 26,596	$
Maintenance and services	12,086	
Total LANDesk net revenue	$ 38,682	$

Revenue from our Embedded Software and Solutions Division, which includes our embedded KVM and IPMI solutions and the Agilent product line acquired in the first quarter of 2006, increased to $33.8 million in 2006 from $21.9 million in 2005 and accounted for 6% of our revenue in both 2006 and 2005. The increase in revenue can be attributed primarily to the increased contribution of the embedded KVM solutions as adoption of these platforms by our OEM customers increases and to the Agilent product line, which we acquired late in the first quarter of 2006. Our other business units, which are more entrepreneurial in nature, continue to work on product development and creating markets for those products already developed. Combined, these business units grew from $14.5 million in revenue during to 2005 to $16.7 million in revenue during 2006.

International sales accounted for 43% of sales in 2006 and 43% of sales in 2005, while sales within the United States were 57% of sales in 2006 and 57% of sales in 2005. Both International and U.S. sales increased 40% from 2005 to 2006. International sales grew to $223.4 million in 2006 from $159.0 million in 2005. Sales in the U.S. grew to $295.8 million in 2006 from $210.8 million in 2005. The Cyclades and LANDesk acquisitions and increased sales of our digital products were again the primary drivers for our revenue growth in both the U.S. and internationally.

We traditionally experience a sequential decline in revenue from the fourth quarter to the first quarter of the following year, and we expect the trend to continue from the fourth quarter of 2006 to the first quarter of 2007. From our experience, many enterprises tend to increase spending for purchases of servers and IT infrastructure equipment and software as a result of year-end capital budget spending, and they tend not to spend as much in the following quarter.

Gross profit. Gross profit is affected by a variety of factors, including the ratio of sales among our distribution channels, as OEM sales typically have lower gross margins than our branded sales; absorption of fixed costs as sales levels fluctuate; product mix, raw materials; labor costs; new product introductions by us and by our competitors; increasing sales of our software products which tend to have higher gross margins; and our outsourcing of manufacturing and assembly services. Gross margin improved to 62.0% in 2006 from 59.2% in 2005. This increase in gross margins resulted from the following factors:

- Higher revenue from our digital and serial products as our digital KVM solutions typically carry higher margins than our analog solutions (sold through our Management Systems Division);

- Added sales from our LANDesk acquisition, whose products are primarily software with related service and maintenance revenue and the gross margins typically exceed 90%;

- Added sales from our Cyclades branded products, which are sold primarily through our branded channel and, as a result, have a higher gross margin; and

- Increased revenue from our embedded solutions in which have higher margins than our traditional KVM products (sold through our Embedded Software and Solutions Division).

These increases to gross margins were somewhat offset by these factors:

- Additional costs included in cost of sales from amortization of other intangible assets recorded as a result of the LANDesk acquisition related to developed technology and internally developed software for resale;

- Additional costs incurred to transition the manufacturing of Cyclades products to Avocent contract manufacturers and transition order fulfillment of Cyclades products to Avocent facilities, which will result in cost savings; and

- Additional product costs from implementing recent environmental regulations, particularly in Europe.

We expect that the contributions from our LANDesk division and continued strong sales of our digital KVM and serial products, along with cost savings realized through our integration efforts of the Cyclades acquisition will continue to offset price declines and the additional costs we expect from our environmental regulation compliance efforts in the first quarter of 2007.

Research and development expenses. Research and development expenses include compensation for engineers, support personnel, outside contracted services and materials costs, and are expensed as incurred. Research and development expenses were $63.9 million, or 12.3% of net sales, in 2006, compared to $56.9 million, or 15.4% of net sales, in 2005. The increase in the amount spent on research and development is due to the additional costs from the Cyclades and LANDesk acquisitions, including costs related to the Cyclades product integration efforts and the inclusion of equity-based compensation in 2006, following our adoption of SFAS 123R on January 1, 2006. The additional costs from the acquisitions were partially offset by reduced headcount and certain research and development site closings undertaken during the second half of 2005. As previously stated, we continue to believe that the timely development of innovative products and enhancements to existing products is essential to maintaining our competitive position.

Acquired in-process research and development expense. Acquisition related expenses in 2006 were comprised solely of the write-off of in-process research and development expenses related to our acquisitions, including $2.1 million for Cyclades and $18.6 million for LANDesk. There were no acquired in-process research and development expenses during 2005.

Selling, general and administrative expenses. Selling, general and administrative expenses include personnel costs for administration, finance, information systems, human resources, sales and marketing and general management, certain merger and acquisition related expenses, rent, utilities, legal and accounting expenses, bad debts, advertising, promotional material, trade show expenses and related travel costs. Selling, general and administrative expenses were $148.6 million, or 28.6% of net sales, in 2006 compared to $90.4 million, or 24.4% of net sales, in 2005. The increase in selling, general and administrative expenses is primarily related to increased headcount as a result of the acquisitions we completed during 2006. We also experienced higher costs as a result of expensing equity-based compensation awards in 2006 and adding Cyclades and LANDesk s selling, general and administrative expenses. However, these higher costs were somewhat offset by the savings resulting from our Cyclades integration efforts later in 2006. In 2007, we expect selling, general and administrative expenses to benefit from cost savings related to our integration efforts.

Acquisition integration expenses. We recorded $3.9 million of expenses, or 0.8% of net sales, in 2006 related to costs associated with the integration of Cyclades people, processes, and products into Avocent. These costs also include severance accruals resulting from the headcount reductions associated with duplicate positions eliminated during the year. We expect integration costs and severance accruals will be immaterial in the first quarter of 2007. There were no such charges incurred during 2005.

Amortization of intangible assets. Amortization of $23.0 million in 2006 includes primarily the amortization of the identifiable intangible assets created as a result of the acquisitions of Equinox, 2C, So