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

Form 10-K

(Mark One)

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

For the fiscal year ended July 1, 2007

OR

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

For the transition period from to .

Commission file number 000-25711

Extreme Networks, Inc.
(Exact name of Registrant as specified in its charter)

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

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

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

Securities registered pursuant to Section 12(g) of the Act:

Common stock, $.001 par value

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

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

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer 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 ☐ Accelerated Filer ☒ Non-Accelerated Filer ☐

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

The aggregate market value of voting stock held by non-affiliates of the Registrant was approximately $478.1 million as of December 29, 2006, the last business day of the Registrant's most recently completed second fiscal quarter, based upon the closing price on The Nasdaq Global Market reported for such date. This calculation does not reflect a determination that certain persons are affiliates of the Registrant for any other purpose.

114,125,589 shares of the Registrant's Common stock, $.001 par value, were outstanding July 29, 2007.

DOCUMENTS INCORPORATED BY REFERENCE

Part III incorporates by reference from the definitive proxy statement for the Company's 2007 Annual Meeting of Stockholders to be filed with the Commission pursuant to Regulation 14A not later than 120 days after the end of the fiscal year covered by this Annual Report on Form 10-K.

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EXTREME NETWORKS, INC.

FORM 10-K

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FORWARD LOOKING STATEMENTS

This annual report on Form 10-K, including the following sections, contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, particularly statements relating to our expectations for the first quarter of fiscal 2008, our expectations regarding results of operations, our ability to expand our market penetration, our ability to expand our distribution channels, customer acceptance of our products, our ability to meet the expectations of our customers, product demand and revenue, cash flows, product gross margins, our expectations to continue to develop new products and enhance existing products, our expectations regarding the amount of our research and development expenses, our expectations relating to our selling, general and administrative expenses, our efforts to achieve additional operating efficiencies and to review and improve our business systems and cost structure, our expectations to continue investing in technology, resources and infrastructure, our expectations concerning the availability of products from suppliers and contract manufacturers, anticipated product costs and sales prices, our expectations that we have sufficient capital to meet our requirements for at least the next twelve months, our expectations regarding the rationalization of our workforce and facilities, and our expectations regarding materials and inventory management. These forward-looking statements involve risks and uncertainties, and the cautionary statements set forth below and those contained in the section entitled "Risk Factors" identify important factors that could cause actual results to differ materially from those predicted in any such forward-looking statements. We caution investors that actual results may differ materially from those projected in the forward-looking statements as a result of certain risk factors identified in this Form 10-K and other filings we have made with the Securities and Exchange Commission. More information about potential factors that could affect our business and financial results is set forth under "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations."

PART I

Item 1. *Business*

Overview

Extreme Networks, Inc., together with its subsidiaries, (collectively referred to as *Extreme* or the *Company* and as *we*, *us* and *our*) is a leading provider of network infrastructure equipment for corporate, government, education and health care enterprises and metropolitan telecommunications service providers. We were established in 1996 to address the issues caused by slow and expensive legacy networks. We endeavored to change the industry by replacing complex software-based routers with simple, fast, highly intelligent, hardware-based network switches. The subsequent and broad acceptance of this innovative, simplified approach to networking has enabled us to become an industry leader. Our technology vision since the founding of the Company has been "Ethernet Everywhere" – a unifying network strategy that uses proven Ethernet technology to simplify each element of the network. Our vision of Ethernet Everywhere helped us deliver easily deployable, highly scalable, comprehensively managed networks with ubiquitous bandwidth for applications and users. The resulting proliferation of applications, users and devices on the network has lead to new opportunities, including securing the network infrastructure. This becomes more critical as voice and video converges on to the data network. An attack on a converged enterprise network exposes the voice services within the company or in the case of a carrier exposes the voice services for their customers, to reliability and availability risks. Realizing the high availability requirement for converged Ethernet networks we have updated our vision of Ethernet Everywhere to 'Insight and Control'. Our vision today is to provide meaningful insight into and greater control over the Ethernet infrastructure.

Extreme Networks recognized in early 2000 that new network operating systems would be needed by the industry as converged IP networks begin to drive more and more mission-critical traffic onto a single network infrastructure. ExtremeXOS™ now delivers revolutionary breakthroughs and industry leading capabilities that further the state-of-the-art in networking technology: Scalability, Resiliency, Security and Extensibility.

ExtremeXOS™ provides a revolutionary foundation that for the first time delivers adaptability, scalability and increased responsiveness for Ethernet networks through its uniquely open, extensible architecture.

Our portfolio of networking products provides insight and control for the network, while enabling greater flexibility and scalability, ease-of-use and a lower cost of ownership. We have achieved these advantages by utilizing Application Specific Integrated Circuits (ASICs) as well as merchant silicon in our products and by creating a common hardware, operating systems and network management architecture for our products.

Industry Background

Businesses, governments, educational institutions, service providers, and other enterprise organizations have become highly dependent on their internal networks and the Internet. These networks serve as a central communications infrastructure connecting internal and external sites, and hosting voice calls and live and streamed video traffic. Computing applications, such as Enterprise Resource Planning (ERP) or Customer Relationship Management (CRM) systems, large enterprise data warehouses and sophisticated online transaction and other e-business applications, require the support of significant network resources as does the increased use of converged communication applications like IP Telephony. The emergence of the desktop Internet browser as a standard user interface as well as the Internet Protocol, or IP, as a common, enabling network technology has enabled bandwidth-intensive applications that integrate voice, video and data over TCP/IP to be deployed extensively throughout organizations. The steady rise in application sophistication, the proliferation of network-delivered services to the residence and the associated bandwidth load demands a fast, flexible and scalable network infrastructure.

Networking environments can be segmented into local area networks, or LANs, wide area networks, or WANs, and metropolitan area networks, or Metros.

LANs. LANs are traditional networks designed for connecting users to many types of application servers, which may be held locally or where they are remotely accessed through either private WANs or through secured public Internet communications. The LAN consists of servers, clients, a network operating system and a communications link to connect the LAN to other networks and to the Internet. The LAN market in which Extreme participates consists primarily of large and medium-sized enterprise customers.

WANs. WANs are communication networks that span across large geographic areas, such as counties, states or countries.

The addition of WAN support to ASIC-based or merchant silicon-based network switches permits encapsulated Ethernet services to reach customers where integration with existing Synchronous Optical Network/Synchronous Digital Hierarchy, or SONET/SDH, infrastructure is required.

The WAN market includes service providers such as local exchange carriers, or ILECs, and competitive local exchange carriers, or CLECs, multiple tenant/dwelling unit service providers, or MTUs, and Internet service providers, or ISPs, as primary customers.

Metros. Metros are networks that link mid-sized geographic areas such as a city or an entire metropolitan area.

Due to wide and steady deployment of increasingly scalable Ethernet technology, LAN traffic has achieved geometric growth in the aggregate amounts of data traffic delivered over networks and bandwidth rates, now delivered at Gigabit and 10 Gigabit speeds. Available bandwidth in WANs has also grown, as infrastructures are built out to accommodate the annual growth in Internet traffic. The Metro network has emerged as the key link between the LAN and the WAN.

In recent years, the Metro network has become a critical and dynamically evolving arena within the overall IP network infrastructure landscape. In addition to steadily rising traffic load, the underlying network technologies, architectures and protocols are experiencing incremental change. The Metro market includes ILECs and CLECs as well as alternative metropolitan service providers such as utility companies, railroads and municipalities that provide Metro network services to connect multiple facilities. For example, a local government might build a Metro network to interconnect agencies, such as city hall, fire departments, road and vehicle maintenance facilities, hospitals and emergency centers, social services and public libraries. The same technologies and network architectures associated with Metros are becoming popular within large and very large corporate enterprises, which can utilize private Metros, by lighting “dark” fiber optic cabling, to create a “super campus” network, connecting facilities spread over a city-size area.

A converged network must meet the following four key requirements:

High Availability. To avoid network outages hardware availability, network operating system availability and network-level availability have to be combined. Simply addressing just one of these is not sufficient to support a converged network. Switch hardware must support redundant management modules with hitless failover, hot swappable line cards and redundant power supplies for hardware high availability. High availability switches used to implement a converged network must have a modular operating system. Switches must also support a variety of link-level resiliency protocols that allows customers to reroute IP Telephony calls in less than 50 milliseconds should a network link fail.

Quality of Service. Network users expect high-quality connections for all converged services, regardless of whether other bandwidth intensive applications are placing heavy demands on the network. Quality of Service (QoS) solutions that allow network administrators and carriers to assign the appropriate amount of bandwidth to the applications deemed most important is crucial in implementing a converged network. Switches must introduce only very low jitter and low latency if they are to be part of a converged network.

Comprehensive security. Trying to manage a secure environment in a world full of threats has consistently increased the demands on all IT organizations. Additionally, regulatory compliance has made enterprise security a critical component of meeting new legislation requirements. A comprehensive security implementation has to make sure that only the authorized users, authorized devices and authorized applications are allowed on the network. Identity based user access control, laptop and desktop scanning and authentication, and network wide coverage for rapidly propagating threats and intrusion prevention are key to achieving comprehensive security.

Ease of management. Proactive network monitoring and ease of network management are key ingredients in the design and successful operation of a converged network. IT administrators must be able to easily monitor converged applications like IP Telephony service and perform other critical operational tasks while accommodating changes quickly.

Opportunity for Next Generation Switching Solutions

Several technology trends have enabled a new generation of networking equipment that is built to meet the key requirements demanded by today’s enterprises and service providers.

A variety of new requirements are now being placed on the enterprise LAN network. The resulting proliferation of applications, users and devices on the network has lead to the challenge of securing the network infrastructure. This becomes more critical as voice and video converges on to the data network. An attack on a converged enterprise network exposes the voice services within the company to reliability and availability risks. Customers are demanding high availability switching solutions that are easy to install, secure and operate. These requirements offer great opportunity for next generation switching solutions in the enterprise LAN market.

Ethernet started as an enterprise technology and when Metro Ethernet took hold in 2000, Extreme Networks pioneered the market by enhancing Ethernet for service providers. We invented technologies such as EAPS and vMANs. Over subsequent years, these technologies have been deployed widely to great success and are being used to deliver network services over fiber, to buildings or a residence. This was great for Internet access where carriers sold and subscribers essentially bought bulk data transfer. But today, individual subscribers – residential or businesses – want tailored services and guarantees driven by new applications such as voice and IPTV. Providing the opportunity for carriers to address individual subscribers through mass customization and deliver valuable services, in a low cost Ethernet network, opens up the market for Ethernet switches in the carrier Ethernet market.

The Extreme Networks Solution

We provide Ethernet networking solutions that meet the requirements of today's enterprises and service providers by providing high performance, solution scalability, advanced policy-based Quality of Service, simplicity of use and lower cost of ownership. Our products share a common hardware, operating system and network management architecture, are based on industry-standard routing and network management protocols and offer open extensibility and interoperability. Our switches can be managed from any browser-equipped computer or the Telnet applet supported in almost all operating systems. The Telnet applet allows access to the Command Line Interface, or CLI, which a system administrator may prefer to use.

The key benefits of our solutions are:

High Availability: Customers can choose redundant management modules with hitless failover, hot swappable line cards and redundant power supplies for hardware high availability; a modular operating system (ExtremeXOS™) for high system availability; and a variety of link-level resiliency protocols, including Ethernet Automatic Protection Switching (EAPS). Developed by Extreme Networks, EAPS is a critical protocol in any converged network. This open protocol allows you to reroute IP Telephony calls in less than 50 milliseconds should a network link fail, allowing businesses to continue uninterrupted even if disaster strikes.

Quality of Service: Extreme Networks offers an excellent and versatile Quality of Service (QoS) solution that allows IT administrators and carriers to assign the appropriate amount of bandwidth to mission critical applications such as IP Telephony and voice over wireless LANs. Policy based QoS offered by Extreme Networks allows network operators to automate and simplify bandwidth control. The ability to precisely deliver the specified bandwidth to a large number of applications and users is a hallmark of our QoS solution.

Comprehensive Security: Extreme Networks' security solution is truly innovative and delivers what all IT professionals seek – a network that has security in its heart, rather than added as an afterthought. Our security solution, which combines secure switches with our powerful security rules engine, enables customers to implement unified wired and wireless network access and IP Telephony in a secure environment. CLEAR-Flow, our wire-speed security rules engine, helps detect and mitigate denial of service attacks. In the case of rapidly propagating Day-Zero threats, such as worm storms, CLEAR-Flow combined with Sentriant, our scalable, virtual security resource, can help protect the network.

Ease of Management: We offer a suite of network management tools that allow network operators to monitor and manage the network in an automated fashion. Using our tools, network administrators can quickly and easily monitor IP Telephony service, accommodate changes and perform other critical operational tasks. Also, software developers can interact directly with our products using a standards-based Application Programming Interface (API) to manage the network and optimize application performance.

The Extreme Networks Strategy

Our goal is to be the provider of the most innovative and effective network solutions that create an improved applications and services infrastructure for enterprises and service providers. We seek to provide our customers with a *best-of-breed alternative* to single-sourced, highly proprietary networking equipment from larger competitors.

Key elements of our strategy include:

Provide simple, easy-to-use, high-performance, cost-effective switching solutions. We offer customers easy-to-use, powerful, cost-effective switching solutions that meet the specific demands of enterprises, and service and content providers. Our products provide customers with scalability from 10 Mbps Ethernet to 10 Gigabit Ethernet combined with the wire-speed, non-blocked routing of ASIC-based or merchant silicon-based Layer 3 switching. We intend to capitalize on our expertise in Ethernet, IP and hardware-based switching technologies to continuously develop new products that will meet the future requirements of a broad range of customers.

Expand market penetration. We continue to market our products to new customers in multiple market segments. The majority of our business is with enterprise customers, including those in government and education sectors. Additionally, we aim to leverage our technology development, service, support and business infrastructure resources to address the metropolitan Ethernet market. These service provider customers include ISPs, content providers and Metro service providers. While currently most of our service provider and Metro-related business is generated outside of the United States, we believe there is a long-term growth opportunity in the metropolitan Ethernet market on a worldwide basis. Once customers deploy our products they obtain the increased benefits of our solution by simplifying their networks, extending policy-based Quality of Service and reducing costs of ownership, while increasing performance.

Extend switching technology leadership. Our technological leadership is based on proprietary switching technology, the ExtremeXOS™ and ExtremeWare® operating systems. We intend to invest our engineering resources in our proprietary switching technology, our operating system and other development areas to create leading-edge technologies that will increase the performance and functionality of our products. We also intend to maintain our active role in industry standards committees such as the Institute for Electrical and Electronics Engineers, or IEEE, and the Internet Engineering Task Force, or IETF.

Leverage and expand multiple distribution channels. We distribute our products through select distributors and a large number of resellers. To quickly reach a broad, worldwide audience, we have more than 800 resellers in approximately 70 countries, including regional networking system resellers, network integrators and wholesale distributors. We maintain a field sales force to support our resellers and to sell directly to a small number of select strategic accounts. We are continually developing and refining our two-tier distribution channel strategy.

Provide high-quality customer service and support. We seek to enhance customer satisfaction and build customer loyalty through high-quality service and support. This includes a wide range of standard support programs that provide the level of service our customers require, from standard business hours to global 24-hour-a-day, 365-day-a-year real-time response support. We intend to continue to enhance the ease of use of our products, and to invest in additional support services by increasing staff and adding new support programs for our distributors and resellers. We are committed to providing customer-driven product functionality through feedback from key prospects, consultants, channel partners and end-user customers.

Products

We deliver wired and wireless networking solutions for enterprises and service providers who are facing tough infrastructure challenges. Our products and services leverage a modern, modular operating system, innovative hardware technologies, and network-integrated security and mobility capabilities to provide simplicity, high performance, and network insight and control at a low cost of ownership.

During the past fiscal year, Extreme Networks introduced a series of new products that support our customers' secure, converged networks. Release 12.0 of ExtremeXOS™, our award-winning modular network operating system, continues to deliver leading capabilities that ease the deployment and management of sophisticated enterprise and service provider networks. The Summit X250 series, powered by ExtremeXOS, breaks new ground in the network switching space. With advanced automation and quality of service features in an economical package, these switches are ideal for connecting simple devices, like IP handsets or security cameras, to an advanced Enterprise network. In addition, we introduced new products and enhancements to both our Security and Wireless product lines.

Our principal products are as follows:

Products	Configuration/Description
Extreme XOS-powered Summit Stackable Product Family	
Summit X250	24 or 48 10/100 Mbps Ethernet ports and 2 Gigabit Ethernet ports with or without Power-Over-Ethernet (POE)
Summit X450	24 or 48 10/100/1000 BaseT Ethernet ports or 24 Gigabit Ethernet fiber ports, including 4 dual personality (fiber or copper) Gigabit Ethernet ports and an optional 2-port 10 Gigabit Ethernet Module
ExtremeWare-powered Summit Stackable Product Family	
Summit5i	12 100/1000 BaseT Ethernet ports and 4 1000BaseX Gigabit Ethernet ports
Summit48si	48 10/100 Mbps Ethernet ports and 2 Gigabit Ethernet ports
Summit 200	48 or 24 10/100 Mbps Ethernet ports and 2 Gigabit Ethernet ports
Summit 300	48 or 24 10/100 Mbps Ethernet ports, supporting Power over Ethernet, and 2 or 4 Gigabit Ethernet ports
Summit 400	48 or 24 10/100/1000 BaseT Ethernet ports, 4 Gigabit Ethernet 1000BaseX ports and an optional 2-port 10 Gigabit Ethernet Module. One version of the 24 port model supports Power over Ethernet
Summit WM Wireless Product Family	
Summit WM 100/1000	Wireless switch controller supporting 4 fast 10/100 ports or 2 Gigabit Ethernet ports and up to 200 wireless Access Points
Summit WM 200/2000	Wireless switch controllers supporting advanced voice over wireless capabilities as well as enhanced failover features for demanding WLAN applications
BlackDiamond Modular Chassis powered by ExtremeXOS	
BlackDiamond 8806	192 10/100/1000 Gigabit Ethernet ports, or 18 10 Gigabit Ethernet ports in one chassis
	6 slots to accommodate a variety of up to 4 connectivity modules and 2 management modules
BlackDiamond 8810	432 10/100/1000 Gigabit Ethernet ports, or 36 10 Gigabit Ethernet ports in one chassis
	10 slots to accommodate a variety of up to 8 connectivity modules and 2 management modules

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Products	Configuration/Description
BlackDiamond 12804C	80 Gigabit Ethernet ports, or 8 10 Gigabit Ethernet ports in one chassis for the enterprise core
	6 slots to accommodate a variety of up to 4 connectivity modules and 2 management modules
BlackDiamond 12804R	80 Gigabit Ethernet ports, or 8 10 Gigabit Ethernet ports in one chassis for carrier Ethernet services
	6 slots to accommodate a variety of up to 4 connectivity modules and 2 management modules
BlackDiamond 10808	480 Gigabit Ethernet ports, or 48 10 Gigabit Ethernet ports in one chassis
	10 slots to accommodate a variety of up to 8 connectivity modules and 2 management modules
BlackDiamond and Alpine Modular Chassis powered by ExtremeWare	
Alpine 3804	Up to 128 10/100 Mbps Ethernet ports or 64 Gigabit Ethernet ports in one chassis
	5 slots to accommodate a variety of up to 4 connectivity modules and 1 management module
Alpine 3808	Up to 256 10/100 Mbps Ethernet ports or 128 Gigabit Ethernet ports in one chassis
	9 slots to accommodate a variety of up to 8 connectivity modules and 1 management module
BlackDiamond 6808	Up to 672 10/100 Mbps Ethernet ports, 168 Gigabit Ethernet ports, or eight 10 Gigabit Ethernet ports in one chassis
	10 slots to accommodate a variety of up to 8 connectivity modules and 2 management modules
Operating Systems	
ExtremeXOS™	A modular, POSIX-compliant modular switch operating system supporting open APIs for device to device collaboration and support for XML type interfaces. ExtremeXOS delivers automated process restart for highly available networks
ExtremeWare®	An embedded switch operating system featuring standard protocols, web-based configuration and policy-based Quality of Service

Summit Stackable Products

Our Summit stackable switch family is designed to meet the demanding requirements of Enterprise and Service Provider customers. With a broad range of Gigabit and 10/100 Mbps speeds and switches built for edge and aggregation roles, these products meet the needs of Enterprises connecting desktops and servers as well as Service Providers connecting large Internet data centers and broadband points of presence in metropolitan-scale service areas.

Extreme Networks was the first networking company to introduce fixed-configuration switches utilizing a modern, modular operating system. As a result, our customers now can enjoy the high availability and extensibility capabilities of ExtremeXOS – a network operating system originally designed to meet the demanding needs of core and service provider applications – at the edge of their networks.

We've moved aggressively to build our ExtremeXOS-based fixed-configuration product portfolio. In 2005, we announced the Summit 450 series of switches for Gigabit connectivity. In 2006 we extended the Summit portfolio again with the addition of the Summit 250 series of switches for 10/100 connectivity. As a result, enterprise and service provider customers can now tailor their solution with a variety of form factors – 24 or 48 ports, powered or non-powered, and 10/100 or 10/100/1000. When combined with our ExtremeXOS-based BlackDiamond core products, our Summit switches deliver a unique value proposition: a single network operating system – running on the same release from the edge to the core – capable of creating high performance converged infrastructure solutions that are simple to deploy and operate.

Our ExtremeWare stackable switch family continues to provide value to our customers in a variety of network connectivity roles, including:

- The Summit 400 product line now includes the Summit 400-24p which offers Power over Ethernet (PoE), integrated stacking, and optional 10 Gigabit uplinks.
- The Summit 300 switch family supports an array of devices including IP phones, laptop and desktop PCs and emerging devices such as IP cameras.
- The Summit 200 series switches offer low entry costs for sophisticated Layer 3 services.
- The Summit48si switch delivers an aggregation switching solution with physical and logical access, security and user mobility features.
- The Summit5i switches support server farms and data centers by maximizing server availability and performance with combining server load-balancing with wire-speed switching.

Other members of the Summit product line address server-switching constraints by providing switched Fast Ethernet or Gigabit Ethernet ports and high speed Gigabit uplinks to servers, delivering required bandwidth between servers, and to clients on attached segments.

The Summit WM Wireless LAN Products

Summit WM-series wireless LAN (WLAN) controllers deliver a high-performance wireless enterprise solution that is both secure and easy to manage. This allows Enterprise network managers to simplify the task of mobilizing their users without sacrificing features or performance. The Summit WM-series switch is ready to support the most advanced wireless applications and mobile voice and multimedia networking challenges. Examples include cross-subnet roaming and sophisticated multicast. With capacities of up to 200 access points per switch, the Summit WM-series can scale to support the largest WLAN installations while also providing centralized management for remote branch office installations.

Sentriant Network-Integrated Security Solutions

The Sentriant product family includes the Sentriant NG product for rapid threat detection and mitigation, and the Sentriant AG product for network access control. Both products integrate with the network infrastructure by leveraging features within Extreme Network's infrastructure portfolio. Sentriant AG and Sentriant NG can also deliver exceptional value as standalone products when used with networking infrastructure equipment from other vendors.

When used in conjunction with the switch-based CLEAR-Flow security rules engine from Extreme Networks, Sentriant NG leverages insight and control from the network to deliver a Virtualized Security Resource (VSR). VSR's can deliver dynamic network security to proactively detect, contain and mitigate network threats including common denial of service attacks and harmful worm 'storms'. The Sentriant NG appliance can be positioned at the core of the network where it eliminates threats in a matter of seconds with its ability to detect storm patterns and contain malicious traffic. Sentriant NG uses behavior-based threat detection methods to detect threats – including new threats for which no signatures exist at the time of attack. It also includes a sophisticated early warning system that employs unused IP space to identify threats. The Sentriant NG VSR and CLEAR-Flow promote higher network availability while reducing the need for numerous security devices across the edge of the network.

Sentriant™ AG provides a complete Network Access Control (NAC) platform that works with a variety of network infrastructures, across all access types (wired, wireless, VPN), and with a wide range of endpoint devices. Sentriant AG automatically tests each endpoint and verifies that its security level meets the organization's security requirements before allowing access to the network. A non-compliant device can be placed in quarantine with restricted access until it can be repaired through several remediation options before being granted full access.

BlackDiamond 10808 Series

The revolutionary BlackDiamond 10808 is the industry's most advanced switch that redefines the intelligent core within the enterprise network—creating a highly available, open converged network that is both cost-effective and simple to operate. The BlackDiamond 10808 delivers security that scales to 10 gigabit rates, voice-class availability and predictable performance, independent of application. Located in the core of some of the most demanding IPv4 and IPv6 networks, the BlackDiamond 10808's CLEAR-Flow Security Rules Engine and Layer 3 Virtual Switching capability has set the bar for core security. With its redundant hardware design, ExtremeWare® XOS™ modular operating system and network resiliency protocol support, the BlackDiamond 10808 provides the network uptime users expect of traditional circuit-based voice networks.

BlackDiamond 12000 Series

The new BlackDiamond 12804R and 12804C modular switches deliver key functionality and performance for Metro Ethernet service providers and corporate enterprises. The switch assures the delivery of convergence applications, known as the "*Triple Play*" of voice, video and data with one network platform. The BlackDiamond 12804R allows Carriers to support tens of thousands of subscribers per I/O blade, control up to eight Quality of Service levels per subscriber and offers unique controls for business and residential subscribers with ASIC-based bandwidth management with an economical Ethernet network infrastructure. An Ethernet cross-connect allows service providers to connect subscribers easily to content networks. The BlackDiamond 12804C delivers deterministic performance for corporate enterprises, independent of what features are enabled and is capable of maintaining this performance under various failure conditions and/or under network attacks. The switch features the ExtremeXOS™ modular operating system, network security monitoring via the CLEAR-Flow security rules engine and network resiliency, all in a compact form factor. This enables enterprises to deliver secure convergence.

BlackDiamond 8800 Series

The BlackDiamond 8800 series switch is designed for full-scale IP telephony deployments and high performance 10 Gigabit Ethernet. The BlackDiamond 8800 modular switching solution enables users to address the critical requirements for voice production deployments: voice quality connectivity, increased uptime, better security and simple management. The BlackDiamond 8800 promotes higher network availability for data and converged communications with its redundant design which is enhanced by a modular, highly-available, operating system, ExtremeXOS™. The BlackDiamond 8800 provides Power over Ethernet connectivity and the industry's only LAN resiliency protocol for voice – Extreme Networks' Ethernet Automatic Protection Switching (EAPS) protocol.

BlackDiamond 6800 Series

The network core is the most critical point in the network, serving as the convergence point for the majority of network traffic, including desktop, aggregation and server traffic. Network core switching involves switching traffic from desktops, segments and servers within the network. Owing to the high-traffic nature of the network core, the critical elements in core switching include wire-speed Layer 3 switching and routing, scalability, non-blocking hardware architecture, fault-tolerant mission-critical features, redundancy, and link aggregation capabilities. The ability to support a variety of high-density port speeds and to accommodate an increasing number of high-capacity backbone connections is also important.

The BlackDiamond 6800 series switch delivers carrier-class scalability, redundancy and high reliability for core switching in high-density Ethernet/IP enterprise and service provider networks. These modular switches include the fault-tolerant features associated with mission-critical enterprise-class Layer 3 core switching, including redundant system management and switch fabric modules, hot-swappable modules and chassis components, load-sharing power supplies and management modules, up to eight 10 Mbps, 100 Mbps or Gigabit aggregated links, dual software images and system configurations, spanning tree and multipath routing, and redundant router protocols for enhanced system and network reliability. The BlackDiamond 6800 series switch is certified to be compliant with Network Equipment Building Systems, or NEBS Level 3.

Alpine 3800 Series

The Alpine 3800 series switch provides a simple, resilient broadband infrastructure for Metros, ISPs and mid-range enterprise networks. The Alpine 3800 series provides total Ethernet coverage with support for both standard category 5 and fiber optic media.

ExtremeXOS™

ExtremeXOS is an open network operating system that delivers meaningful insight and unprecedented control for mission-critical applications. With exceptional support for voice over IP, integrated security, and high availability, ExtremeXOS stands out as a real alternative to closed, proprietary products that limit choice and compromise performance.

Four powerful capabilities combine to make ExtremeXOS an exceptional operating system for solving the toughest networking challenges: 1) modularity enhances availability by isolating software processes to limit the impact of changes, attacks, or instabilities; 2) open interfaces allow applications to effectively control the network without unnecessarily tight integration that can limit flexibility and force system-wide upgrade cycles; 3) ExtremeXOS is a POSIX-compliant operating system, making on-switch application integration straightforward and fast; and 4) wire-rate instrumentation provides deep insight into critical network activities to build sophisticated security and voice applications.

ExtremeXOS™ now delivers revolutionary breakthroughs and industry leading capabilities that further the state-of-the-art in networking technology. We pioneered an innovative approach for communicating with the network control plane using an application programming interface or API. The extensible markup language or XML based APIs can be used by third parties to access processes within the switch in a secure fashion. For example, a security appliance can utilize ExtremeXOS™ to limit access, control bandwidth or redirect traffic from a client that is attempting to connect to the network. This XML infrastructure embraces the concept of open yet secure communications to allow business applications to easily interact with the network for security policy enforcement, regulatory compliance and performance management, and improved security.

ExtremeWare®

ExtremeWare® represents our first generation of Operating System and is embedded on specific switches. It delivers the robust switching and routing protocol support, management, control and security needed on current enterprise and service provider networks. Its standards-based, multi-layer switching and policy-based Quality of Service give network managers the tools needed to optimize network capacity with consistent fault-tolerant behavior.

Sales, Marketing and Distribution

We conduct our sales and marketing activities on a worldwide basis through a two-tier product/solution distribution channel utilizing distributors, value-added resellers and our field sales organization. A majority of our sales are currently made to partners in our distributor and reseller channels. The first tier consists of a limited number of independent distributors that sell primarily to resellers. The second tier of the distribution channel is comprised of a large number of independent resellers that sell directly to end-user customers. In addition, Extreme utilizes its field sales organization to sell direct to end-user customers, including large global accounts.

Strategic Alliances. In October 2003 we entered into a mutual, non-exclusive, comprehensive strategic alliance with Avaya Inc. Avaya designs, builds and manages communications networks for more than one million businesses worldwide, including 90 percent of the Fortune 500. Focused on businesses large to small, Avaya is a world leader in secure and reliable IP telephony systems and communications software applications and services. Avaya and Extreme Networks are jointly developing and marketing converged communications solutions as part of this multi-year, multimillion-dollar strategic alliance.

Avaya is also reselling Extreme Networks' data networking products and will provide customers with comprehensive planning, design, implementation and management services support through Avaya Global Services.

Distributors. We have established several key relationships with leading distributors in the electronics and computer networking industries. We intend to maintain these relationships with distributors who may offer products or distribution channels that complement our own channels. Each of our distributors primarily resells our products to resellers. The distributors enhance our ability to sell and provide support to resellers, especially global accounts, who may benefit from the broad service and product fulfillment capabilities offered by these distributors. One distributor, Tech Data, accounted for 12%, 12% and 11% of our net revenues in fiscal 2007, 2006 and 2005, respectively. Distributors are generally given privileges to return a portion of inventory to us for the purpose of stock rotation and participate in various cooperative marketing programs to promote the sale of our products and services. We defer recognition of revenue on all sales to these distributors until the distributors sell the product, as evidenced by monthly "sales-out" reports that the distributors provide to us. (See "Revenue Recognition" in Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operations*.)

Value-Added Resellers, or VARs. We have entered into agreements to sell our products through more than 800 resellers in approximately 70 countries. Our value-added resellers include regional networking system resellers, resellers who focus on specific vertical markets, network integrators and wholesale distributors. We provide training and support to our resellers and our resellers generally provide the first level of support to end-users of our products. Our relationships with resellers are generally on a non-exclusive basis. Our resellers are not given privileges to return inventory and do not automatically participate in any cooperative marketing programs. We generally recognize product revenue from our reseller and end-user customers at the time of shipment, provided that persuasive evidence of an arrangement exists, delivery has occurred, the price of the product is fixed or determinable and collection of the sales proceeds is reasonably assured. When significant obligations or contingencies remain after products are delivered, such as installation or customer acceptance, revenue and related costs are deferred until such obligations or contingencies are satisfied. (See "Revenue Recognition" in Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operations*.)

Field sales. We have trained our field sales organization to support and develop leads for our value-added resellers and to establish and maintain a limited number of key accounts and strategic end user customers. To support these objectives, our field sales force:

- assists end-user customers in finding solutions to complex network system and architecture problems;

- differentiates the features and capabilities of our products from competitive offerings;
- continually monitors and understands the evolving networking needs of enterprise and service provider customers;
- promotes our products and ensures direct contact with current and potential customers;
- partners with our key resellers to drive closure of business opportunities; and
- monitors the changing requirements of our customers.

As of July 1, 2007, our worldwide sales and marketing organization consisted of 299 individuals, including directors, managers, sales representatives, and technical and administrative support personnel. We have domestic sales offices located in 16 states and international sales offices located in 22 countries.

International sales

International sales are an important portion of our business. In fiscal 2007, sales to customers outside of the United States accounted for 60% of our consolidated net revenues, compared to 59% in fiscal 2006 and 56% in fiscal 2005. These sales are conducted primarily through foreign-based distributors and resellers managed by our worldwide sales organization, in addition to direct sales to end-user customers, including large global accounts. The primary markets for sales outside of the United States include the countries in Western Europe, the Asia- Pacific region and Japan. Although not a significant component of total revenues to date, we also sell our products in South America, Canada and Mexico.

Marketing

We have a number of marketing programs to support the sale and distribution of our products and to inform existing and potential customers and our distributors and resellers about the features and performance of our products. Our marketing efforts include participation in industry tradeshows, technical conferences and technology seminars, preparation of competitive analyses, sales training, and publication of technical and educational articles in industry journals, a publicly available website, web-based training courses, advertising and public relations. In addition, we are developing e-commerce processes and systems for our resellers, distributors and end-user customers. We also submit our products for independent product testing and evaluation.

Backlog

Our products are often sold on the basis of standard purchase orders that are cancelable prior to shipment without significant penalties. In addition, purchase orders are subject to changes in quantities of products and delivery schedules in order to reflect changes in customer requirements and manufacturing capacity. Our business is characterized by seasonal variability in demand and short lead-time orders and delivery schedules. Actual shipments depend on the then-current capacity of our contract manufacturer and the availability of materials and components from our vendors. We believe that only a small portion of our order backlog is non-cancelable and that the dollar amount associated with the non-cancelable portion is not material. Accordingly, we do not believe that backlog at any given time is a meaningful indicator of future revenue.

Customer Support and Service

We offer modular and comprehensive extended warranty service contracts under our ExtremeWorks service solutions to help protect our customers' network investments and support their business goals. The markets we address, including enterprises and service providers, all seek high reliability and maximum uptime. Our goal is to serve as a knowledgeable and experienced service partner who can tailor service solutions to meet the specific business needs of our customers. For the provision of on-site hardware support to customers we have agreements in place with International Business Machines, Inc. and Equant N.V. Expenses related to these agreements are recorded in cost of service revenue on our consolidated statements of operations. We also maintain relationship with Flextronics International, Ltd. for the handling of product returns and repairs covered by our warranty and service contracts in various locations worldwide. We provide our customers with our standard, limited hardware warranty, which is typically 12 months from the date of shipment to end-users and our 90-day software warranty. Warranty expenses related to these relationships are recorded in cost of product revenue on our consolidated statements of operations.

Our service offerings are as follows:

- ExtremeWorks and PartnerWorks Support Programs
- ExtremeWorks Professional Services
- ExtremeWorks Education

ExtremeWorks and PartnerWorks Support Programs. Our support programs are designed to support a broad range of customer service requirements for our resale partners and direct customers. We meet the service requirements of our customers and channel partners through Technical Assistance Centers, or TACs, located in Santa Clara, California; Utrecht, Holland; Research Triangle Park, North Carolina; and Tokyo, Japan. Our technical engineers assist in diagnosing and troubleshooting technical issues regarding customer networks. This is part of our effort to ensure maximum network uptime and performance. Regional systems engineers serve as on-site engineering resources to provide consultative support and advice for network operation on an as needed basis. Development engineers work with the TACs to resolve product functionality issues specific to each customer.

We utilize the Internet to distribute and obtain information from our customer base as an integral part of our service solution. This allows us to keep customers informed of the latest updates and developments at Extreme Networks, and contains up-to-date information and technical documentation enabling customers to research issues and find answers to technical questions. Special features include a TAC database to obtain troubleshooting assistance and information for diagnosing hardware and researching network issues. On-site support services are available in most locations worldwide for customers who require a more comprehensive level of service and support.

ExtremeWorks Professional Services. We specialize in providing solutions and consultative services to improve network productivity in all phases of the network lifecycle – planning, design, implementation, operations and optimization management. The professional services include customized and packaged consulting services that assist customers in meeting their objectives for applications support, uptime and cost control. Our network architects develop and execute customized hardware deployment plans to meet individualized network strategies. These activities include the management and coordination of the design and network configuration, resource planning, staging, logistics, migration and deployment. We also provide customized training and operational best practices documentation to assist customers in the transition and sustaining of their networks.

We offer our customers a variety of technical consulting services, including:

- Analysis – detailed audit and analysis of customer networks
- Policy-Based QoS – analysis and recommendation for deploying advanced traffic management and bandwidth prioritization features to match actual traffic patterns
- Multicasting – strategy for deploying PIM-DM, PIM-SM, or DVMRP to best suit streaming media requirements
- Voice over IP – strategy and recommendations to deploy voice-over-IP utilizing our technology
- Wireless LAN – site surveys, WLAN design and implementation of Unified Access solutions

- Security – analysis of customer security needs and recommendations on how to implement advanced security features to meet those needs
- Resident engineering services – dedicated on-site technical engineering resources providing high level staff expertise

ExtremeWorks Education. Leveraging our Authorized Training Partner strategy, Extreme Networks licenses partners to provide education through certified technical experts that teach classes dealing with all of our products. The classes cover a wide range of topics such as installation, configuration, operation, management and optimization – providing customers with the necessary knowledge and experience to successfully deploy and manage our products in various networking environments. Classes are scheduled and available at numerous locations worldwide. We also deliver customized training using Extreme Networks staff upon customer request.

Manufacturing

We outsource the majority of our manufacturing and supply chain management operations as part of our strategy to maintain global manufacturing capabilities and to reduce our costs. We conduct quality assurance, manufacturing engineering, document control and test development at our main campus in Santa Clara, California. This approach enables us to reduce fixed costs and to flexibly respond to changes in market demand.

We have a strategic partnership with Flextronics International, Ltd. for the manufacture of our OEM products in San Jose, California and Guadalajara, Mexico. Flextronics' manufacturing processes and procedures are ISO 9001 certified. Our commitment with Flextronics is formalized through a one-year contract. We design and develop the key components of our products, including ASICs and printed circuit boards. We determine the components that are incorporated in our products and select the appropriate suppliers of such components. Flextronics utilizes automated testing equipment to perform product testing and burn-in with specified tests. Together we rely upon comprehensive inspection testing and statistical process controls to assure the quality and reliability of our products.

We also maintain a strategic relationship with Alpha Networks, Inc. headquartered in Hsinchu, Taiwan. Alpha Networks is a global networking Original Design Manufacturer (ODM) leader with core competencies in areas such as Ethernet, LAN/MAN, Wireless, Broadband and Voice Over Internet Protocol (VoIP). Alpha has over 6,000 employees worldwide and maintains relationships with players such as Broadcom and Marvell. Alpha trades on the Taiwan Stock Exchange under stock code T3380. Extreme Networks partners with Alpha Networks to build key product lines including the XOS based Summit Product Family. Following review of Extreme's design specifications, Alpha manufactures and tests to those specifications. Extreme Networks is one of Alpha's top five strategic partners (as measured by revenue).

We intend to regularly introduce new products and product enhancements that will require us to rapidly achieve volume production by coordinating our efforts with those of our suppliers and contract manufacturer.

Although we use standard parts and components for our products where it is appropriate, we currently purchase several key components used in the manufacture of our products from single or limited sources. Our principal single-source components include:

- ASICs;
- merchant silicon;
- microprocessors;
- programmable integrated circuits;
- selected other integrated circuits;

- custom power supplies; and
- custom-tooled sheet metal.

Our principal limited-source components include:

- flash memory;
- dynamic and static random access memories, or DRAMS and SRAMS respectively;
- printed circuit boards; and
- content addressable memories (CAMs).

Purchase commitments with our single or limited-source suppliers are generally on a purchase order basis. A number of vendors supply standard product integrated circuits and microprocessors for our products. Any interruption or delay in the supply of any of these components, or the inability to procure these components from alternate sources at acceptable prices and within a reasonable time, may have a material adverse effect on our business, operating results and financial condition. Qualifying additional suppliers can be time-consuming and expensive and may increase the likelihood of errors.

We use our forecast of expected demand to determine our material requirements. Lead times for materials and components vary significantly, and depend on factors such as the specific supplier, contract terms and demand for a component at a given time. We order most of our materials and components on an indirect basis through our contract manufacturer.

Research and Development

The success of our products to date is due in large part to our focus on research and development. We believe that continued success in the marketplace will depend on our ability to develop new and enhanced products employing leading-edge technology. Accordingly, we are undertaking development efforts with an emphasis on increasing the reliability, performance and features of our family of products, and designing innovative products to reduce the overall network operating costs of customers.

Our product development activities focus on solving the needs of enterprises, service providers and Metro markets. Current activities include the continuing development of our proprietary switching technology aimed at extending the capabilities of our products. Our ongoing research activities cover a broad range of areas, including, in particular, 10 Gigabit Ethernet, Metro and Internet routing, ASIC design, network security, network management software, broadband access equipment and wireless networking equipment.

We continued to enhance the functionality of our modular operating system (ExtremeXOS™) which has been designed to provide high reliability and availability. This architecture allows us to leverage common operating system architecture across different hardware and ASIC implementation.

As of July 1, 2007, our research and development organization consisted of 288 individuals. Research and development efforts are conducted in several locations in the U.S., including our headquarters in Santa Clara, California and Raleigh, North Carolina. In fiscal 2005, we opened a research and development center in Chennai, India focusing on the development and verification of our operating systems. Our research and development expenses in fiscal 2007, fiscal 2006 and fiscal 2005 were $67.1 million, $62.0 million, and $61.5 million, respectively.

Competition

The market for switches is part of the broader market for networking equipment, which is dominated by a few large companies, particularly Cisco Systems. In addition, there are a number of large telecommunications equipment providers, including Alcatel and Nortel Networks, which have entered the market for network equipment, particularly through acquisitions of public and privately held companies. We expect to face increased competition, particularly price competition, from these and other telecommunications equipment providers. We also compete with other public and private companies that offer switching solutions, including Enterasys Networks, Inc., Foundry Networks, Inc., Huawei Technologies Corporation, 3Com Corporation, Hewlett-Packard Company and Dell Computer Corporation. These vendors offer products with functionality similar to our products or provide alternative network solutions. Current and potential competitors have established or may establish cooperative relationships among themselves or with third parties to develop and offer competitive products. Furthermore, we compete with numerous companies that offer routers and other technologies and devices that traditionally have managed the flow of traffic on the enterprise or Metro networks.

Some of our current and potential competitors have longer operating histories and substantially greater financial, technical, sales, marketing and other resources, as well as greater name recognition and a larger installed customer base, than we do. As a result, these competitors are able to devote greater resources to the development, promotion, sale and support of their products. In addition, competitors with a large installed customer base may have a significant competitive advantage over us. We have encountered, and expect to continue to encounter, many potential customers who are confident in and committed to the product offerings of our principal competitors, including Cisco Systems. Accordingly, these potential customers may not consider or evaluate our products. When such potential customers have considered or evaluated our products, we have in the past lost, and expect in the future to lose, sales to some of these customers as large competitors have offered significant price discounts to secure these sales.

We believe the principal competitive factors in the network switching market are:

- expertise and familiarity with network protocols, network switching and network management;
- product performance, features, functionality and reliability;
- price/performance characteristics;
- timeliness of new product introductions;
- adoption of emerging industry standards;
- customer service and support;
- size and scope of distribution network;
- brand name;
- access to customers; and
- size of installed customer base.

We believe that we compete favorably with our competitors with respect to each of the foregoing factors. However, because many of our existing and potential competitors have longer operating histories, greater name recognition, larger customer bases, broader product lines and substantially greater financial, technical, sales, marketing and other resources, they may have larger distribution channels, stronger brand names, access to more customers and a larger installed customer base than we do. Such competitors may, among other things, be able to undertake more extensive marketing campaigns, adopt more aggressive pricing policies and make more attractive offers to distribution partners than we can. To remain competitive, we believe that we must, among other things, invest significant resources in developing new products and enhancing our current products and maintain customer satisfaction worldwide. If we fail to do so, our products will not compete favorably with those of our competitors and that may have a material adverse effect on our business.

Intellectual Property

We rely on a combination of patent, copyright, trademark and trade secret laws and restrictions on disclosure to protect our intellectual property rights. Based on our commitment to build a patent portfolio, we have in process a number of patent applications relating to our proprietary technology. We have filed patent applications in selected countries abroad as deemed appropriate. There can be no assurance that these applications will be approved, that any issued patents will protect our intellectual property, or that third parties will not challenge these patents or applications. Furthermore, there can be no assurance that others will not independently develop similar or competing technology or design around any patents that we may obtain. With respect to trademarks, we have a number of pending and registered trademarks in the United States and abroad.

We enter into confidentiality or license agreements with our employees, consultants and corporate partners, and control access to, and distribution of, our software, documentation and other proprietary information. In addition, we provide our software products to end-user customers primarily under "shrink-wrap" license agreements included within the packaged software. These agreements are not negotiated with or signed by the licensee, and thus these agreements may not be enforceable in some jurisdictions. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy or otherwise obtain and use our products or technology. There can be no assurance that these precautions will prevent misappropriation or infringement of our intellectual property. Monitoring unauthorized use of our products is difficult, and we cannot be certain that the steps we have taken will prevent misappropriation of our technology, particularly in foreign countries where the laws may not protect our proprietary rights as fully as in the United States.

As detailed below under "Legal Proceedings," we are currently engaged in litigation with Enterasys Networks, Inc ("Enterasys"). Enterasys is asserting claims that allege infringement of certain patent rights, against which we are defending vigorously, but we cannot assure you that we will prevail in this litigation. In addition to the litigation with Enterasys, in the normal course of our business from time to time, we are in discussions with companies that assert certain of our products require a license under a number of patents. Due to the number of companies with extensive patent portfolios in our industry who are or may be actively involved in licensing programs, we believe that even if we do not infringe any patents, we may incur significant expenses in the future due to disputes or licensing negotiations, though the amounts and timing of such expenses cannot be determined with any reasonable certainty. As the functionality and features of our products expand, these disputes and discussions could increase or become harder to resolve.

Employees

As of July 1, 2007, we employed 825 people, including 299 in sales and marketing, 288 in engineering, 50 in operations, 94 in customer support and service, and 94 in finance and administration. We have never had a work stoppage and no personnel are represented under collective bargaining agreements. We consider our employee relations to be good.

We believe that our future success depends on our continued ability to attract, integrate, retain, train and motivate highly qualified personnel, and upon the continued service of our senior management and key personnel. None of our personnel is bound by an employment agreement. The market for qualified personnel is competitive, particularly in the San Francisco Bay Area, where our headquarters is located. At times, we have experienced difficulties in attracting new personnel and we have experienced attrition that has affected our operating results.

Organization

We were incorporated in California in May 1996 and reincorporated in Delaware in March 1999. Our corporate headquarters are located at 3585 Monroe Street, Santa Clara, CA 95051 and our telephone number is (408) 579-2800. Our website can be found at www.extremenetworks.com. Investors can obtain copies of our SEC filings from this website free of charge, or on the SEC's website at www.sec.gov.

Our corporate governance guidelines, the charters of our audit committee, our compensation committee and our nominating and corporate governance committee and our code of ethics policy (including code of ethics

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provisions that apply to our principal executive officer, principal financial officers, controller and senior financial officers) are available on our website at www.extremenetworks.com under "Corporate Governance." These items are also available to any stockholder who requests them by calling (408) 579-2800.

Executive Officers of the Registrant

The following table sets forth information regarding our executive officers as of August 1, 2007:

Name	Age	Position
Mark Canepa	52	President, Chief Executive Officer, Director
Karen M. Rogge	52	Senior Vice President, Chief Financial Officer
Alexander J. Gray	50	Senior Vice President and General Manager of Scalable Products
Helmut Wilke	55	Senior Vice President of Worldwide Sales

Mark Canepa. Mr. Canepa joined Extreme as President and Chief Executive Officer on August 30, 2006. Prior to joining Extreme, he was with Sun Microsystems where he served as Executive Vice President of the Network Storage Products Group. Prior to that role, he served in multiple vice president and general manager roles at Sun, after joining the company in 1996. Mr. Canepa's prior experience also includes several general manager positions at Hewlett-Packard Company, including development and marketing of the firm's workstation products. Mr. Canepa holds a B.S. and an M.S. in Electrical Engineering from Carnegie Mellon University, and he has also completed the University of Pennsylvania's Advanced Management Program at the Wharton School.

Karen Rogge. Ms Rogge joined Extreme as Senior Vice President and Chief Financial Officer on April 2, 2007. Prior to joining Extreme, she was with Seagate Technology where she served as Vice President, Corporate Finance and Treasurer from January 2004 to November 2006. From January 2001 to December 2003, Ms. Rogge was an independent consultant providing business strategy and interim executive management services to high-tech companies. From January 2000 to July 2000, Ms Rogge served as Vice President and General Manager for the internet search division at Inktomi Corporation. From November 1976 to February 2000, Ms. Rogge served in various executive roles at Hewlett-Packard Company in financial management, information technology management and general management. Ms. Rogge holds an M.B.A. from Santa Clara University and a Bachelor of Science in Business Administration, with a concentration in accounting from California State University Fresno.

Alexander J. Gray. Mr. Gray joined Extreme as Chief Operating Officer in September 2002, and has served as Senior Vice President and General Manager of Scalable Products since January 2007. From January 2001 through August 2002, Mr. Gray was Chief Operating Officer at LGC Wireless, a telecommunications provider. From November 1999 until January 2001, Mr. Gray worked for Replay TV, a digital media provider, as Executive Vice President of Business Operations. From December 1992 through October 1999, Mr. Gray held senior management positions with Lucent Technologies, Inc. and Octel Communications Corporation, both telecommunications providers. Prior to that time, Mr. Gray held positions as Director of Information Services for American President Lines, a container shipping company, from September 1991 to November 1992 and NEXT Computer, a computer and equipment manufacturer, from July 1988 to August 1991. He also spent four years as a research and development engineer for Hewlett-Packard Company, a computer and equipment manufacturer. Mr. Gray holds a B.S. and an M.S. in Electrical Engineering from Washington University in St. Louis, Missouri.

Helmut Wilke. Mr. Wilke joined Extreme as Senior Vice President of Worldwide Sales in April 2007. From May 2001 to March 2007, Mr. Wilke held various positions with Sun Microsystems where most recently he served as Senior Vice President of Operations and Field Support. His prior positions with Sun Microsystems include Vice President of Sales and President of Sun Microsystems, Germany. From 1997 to 2001, Mr. Wilke was the CEO and president of Software AG, a leading manufacturer of software and systems for large corporations. Mr. Wilke holds a PhD in Social Sciences from the University of Berlin, Germany.

Item 1A. *Risk Factors*

We are subject to a number of risks. Some of these risks are endemic to the networking industry and are the same or similar to those disclosed in our previous SEC filings. The following is a list of risks and uncertainties which may have a material and adverse effect on our business, financial condition or results of operations. The risks and uncertainties set out below are not the only risks and uncertainties we face.

We were not in compliance with SEC reporting requirements during fiscal year 2007, and Nasdaq listing requirements during portions of fiscal years 2007 and 2008, and we may continue to face compliance issues with both. If we are unable to remain in compliance with SEC reporting requirements and Nasdaq listing requirements, there may be a material adverse effect on the Company and our stockholders.

On September 11, 2006, based on information developed by Company management and at the Audit Committee's recommendation, the Board of Directors appointed a special committee of the Board (the "Special Committee") to conduct an independent investigation of our historical practices for granting and accounting for stock options and to present findings and recommendations to the Board. Pending completion of our Special Committee investigation, we were delinquent in filing certain of our periodic reports with the SEC during fiscal year 2007, and we were unable to hold our annual meeting of stockholders within the time required under Nasdaq Marketplace Rules. Although such delinquent reports were filed with the SEC on June 28, 2007, and our annual meeting of stockholders occurred on July 30, 2007, we were not in compliance with Nasdaq's Marketplace Rules during portions of fiscal years 2007 and 2008. As a result, we underwent a review and hearing process with Nasdaq to determine our listing status. Nasdaq ultimately permitted our securities to remain listed on the Nasdaq Global Select Market, but our securities could be delisted in the future if we do not maintain compliance with applicable listing requirements in the future. If this happens, the price of our stock, the ability of our stockholders to trade in our stock, and our ability to raise capital could be adversely affected. If we are unable to remain in compliance with the SEC reporting requirements, we would be subject to a number of restrictions regarding the registration of our stock under federal securities laws, and we may not be able to issue stock options or other equity awards to our employees or allow them to exercise their outstanding options, which would adversely affect our business and results of operations.

We have been named as a party to shareholder derivative lawsuits relating to our historical stock option practices, and we may be named in additional lawsuits in the future. This litigation could become time consuming and expensive and could result in the payment of significant judgments and settlements, which could have a material adverse effect on our financial condition and results of operations.

In connection with our historical stock option practices and resulting restatement of our financial statements for the fiscal years 2000 through 2005, derivative actions were filed against certain of our current and former directors and officers purporting to assert claims on the Company's behalf. There may be additional lawsuits filed in the future. We cannot predict the outcome of these lawsuits, nor can we predict the amount of time and expense that will be required to resolve these lawsuits. If these lawsuits become time consuming and expensive, or if there are unfavorable outcomes in any of these cases, there could be a material adverse effect on our business, financial condition and results of operations.

Our insurance coverage will not cover all of our liabilities and expenses in these lawsuits, in part because we have a significant deductible on certain aspects of the coverage. In addition, subject to certain limitations, we may be obligated to indemnify our current and former directors, officers and employees. We currently hold insurance policies for the benefit of our directors and officers, however our insurance coverage may not be sufficient in some or all of these matters to cover all of the costs the Company may need to incur. Furthermore, the insurers may seek to deny or limit coverage in some or all of these matters, in which case we may have to self-fund all or a substantial portion of our indemnification obligations. If we need to self-fund, there is no assurance that we will prevail in our efforts to recover payment from our insurers.

The Special Committee investigation of our historical stock option practices and resulting restatements has been time consuming and expensive, and may have a material adverse effect on us.

The Special Committee investigation and the activities related to the restatement of our fiscal 2000 through fiscal 2005 financial statements have required us to expend significant management time and to incur significant accounting, legal, and other expenses. Although the Special Committee has concluded its investigation, the Special Committee may continue to assist the Company with follow-up activities arising from the restatement or otherwise related to its investigation. The issues surrounding the historical stock option grant practices were complex and required substantial resources to resolve. The cost and time associated with concluding any follow-up activities by the Special Committee may have a material adverse effect on our operating results or our common stock price. The period of time necessary to resolve any such follow-up matters is uncertain, and these matters could require significant additional attention and resources.

The discovery that we had not accounted correctly for historical stock option grants has had, and may continue to have, a material adverse effect on our financial results.

We cannot predict the outcome of any government inquiry or the pending shareholder derivative lawsuits, and we may face future government actions, shareholder lawsuits and other legal proceedings related to our historical stock option practices. All of these events have required us, and will continue to require us, to expend significant management time and to incur significant accounting, legal, and other expenses. This has and could continue to divert attention and resources from the operation of our business and adversely affects our financial condition and results of operations.

Any government inquiry relating to our historical stock option practices may be time consuming and expensive and could result in injunctions, fines and penalties that may have a material adverse effect on our financial condition and results of operations.

The SEC issued an informal request to us for information relating to our historical stock option grant practices. We have responded to the SEC's inquiry and will respond to inquiries from other government authorities if made. The SEC and/or other government authorities may conduct a formal investigation into our historical stock option grant practices. The period of time necessary to resolve any such inquiry is uncertain, and we cannot predict the outcome of any such inquiry or whether we will face additional government inquiries, investigations or other actions related to our historical stock option practices, or otherwise. These matters will likely require us to continue to expend significant management time and incur significant legal and other expenses, and could result in civil and criminal actions seeking, among other things, injunctions against the Company and the payment of significant fines and penalties by the Company, which may have a material adverse effect on our financial condition, results of operations and cash flow. A formal investigation by the SEC and/or other government authorities could adversely affect our business, results of operations, financial position and cash flows.

It may be difficult or costly to obtain director and officer insurance coverage as a result of our stock option related issues.

We expect that the issues arising from our previous historical stock option grant practices and related accounting may make it more difficult to obtain director and officer insurance coverage in the future. If we are able to obtain this coverage, it could be significantly more costly than in the past, which would have an adverse effect on our financial results and cash flow. As a result of this and related factors, our directors and officers could face increased risks of personal liability in connection with the performance of their duties. As a result, we may have difficultly attracting and retaining qualified directors and officers, which could adversely affect our business.

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

We reported losses for fiscal 2007, 2004, 2003, 2002 and 2001 and our revenue declined in fiscal 2007. In addition, while we have reported profits in both fiscal 2006 and 2005, we were not profitable in each quarter during those years. We anticipate continuing to incur significant sales and marketing, product development and general and administrative expenses and, as a result, we will continue to need to rationalize expense levels and increase revenue levels to achieve profitability in future fiscal periods.

Failure to maintain effective internal control over financial reporting may cause us to delay filing our periodic reports with the SEC, affect our Nasdaq listing, and adversely affect our stock price.

The Securities and Exchange Commission, as directed by Section 404 of the Sarbanes-Oxley Act of 2002, adopted rules requiring public companies to include a report of management on internal control over financial reporting in their annual reports on Form 10-K. In addition, our independent registered public accounting firm must attest to and report on our internal control over financial reporting. Although we review our internal control over financial reporting in order to ensure compliance with the Section 404 requirements, if our independent registered public accounting firm is not satisfied with our internal control over financial reporting or the level at which these controls are documented, designed, operated or reviewed, or if the independent registered public accounting firm interprets the requirements, rules and/or regulations differently from our interpretation, then they may decline to attest to management's assessment or may issue a report that is qualified. This could result in an adverse reaction in the financial marketplace due to a loss of investor confidence in the reliability of our financial statements, which ultimately could negatively impact our stock price.

Federal securities laws, rules and regulations, as well as Nasdaq rules and regulations, require companies to maintain extensive corporate governance measures, impose comprehensive reporting and disclosure requirements, set strict independence and financial expertise standards for audit and other committee members and impose civil and criminal penalties for companies and their chief executive officers, chief financial officers and directors for securities law violations. These laws, rules and regulations have increased and will continue to increase the scope, complexity and cost of our corporate governance, reporting and disclosure practices, which could harm our results of operations and divert management's attention from business operations.

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

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

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

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

- changes in general and/or specific economic conditions in the networking industry;
- seasonal fluctuations in demand for our products and services, particularly in Asia-Pacific and Europe;

- the level of attrition of our employees, and of our sales force in particular;
- a disproportionate percentage of our sales occurring in the last month of the quarter;
- reduced visibility into the implementation cycles for our products and our customers' spending plans;
- our ability to forecast demand for our products, which in the case of lower-than-expected sales, may result in excess or obsolete inventory in addition to non-cancelable purchase commitments for component parts;
- product returns or the cancellation or rescheduling of orders;
- our ability to develop, introduce, ship and support new products and product enhancements and manage product transitions;
- announcements and new product introductions by our competitors;
- our ability to develop and support relationships with enterprise customers, service providers and other potential large customers;
- our ability to achieve targeted cost reductions;
- fluctuations in warranty or other service expenses actually incurred;
- our ability to obtain sufficient supplies of sole- or limited-source components for our products on a timely basis;
- increases in the prices of the components that we purchase;
- decreases in the prices of the products that we sell;
- our ability to achieve and maintain desired production volumes and quality levels for our products;
- the mix of products sold and the mix of distribution channels through which products are sold;
- impairment charges associated with long-lived assets;
- restructuring costs associated with adjustments to the size of our operations;
- costs relating to possible acquisitions and the integration of technologies or businesses;
- the effect of amortization of purchased intangibles resulting from new transactions; and
- costs relating to the recognition of share-based payments.

In fiscal 2007 and fiscal 2006, we reported revenues below our expectations. Our results were particularly impacted by lower sales in most regions in fiscal 2007. We believe that revenues will increase in coming quarters; however, our future results could be adversely affected if longer term economic or industry trends are unfavorable.

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

Intense Competition in the Market for Networking Equipment Could Prevent Us from Increasing Revenue and Achieving Profitability.

The market for networking equipment is intensely competitive. The market for switches is part of the broader market for networking equipment, which is dominated by a few large companies, particularly Cisco Systems. In addition, there are a number of large telecommunications equipment providers, including Alcatel and Nortel Networks, which have entered the market for network equipment, particularly through acquisitions of public and privately held companies. We expect to face increased competition, particularly price competition, from these and other telecommunications equipment providers. We also compete with other public and private companies that offer switching solutions, including Enterasys Networks, Inc., Foundry Networks, Inc., Huawei Technologies Corporation, 3Com Corporation, Hewlett-Packard Company and Dell Computer Corporation. These vendors offer products with functionality similar to our products or provide alternative network solutions. Current and potential competitors have established or may establish cooperative relationships among themselves or with third parties to develop and offer competitive products. Furthermore, we compete with numerous companies that offer routers and other technologies and devices that traditionally have managed the flow of traffic on the enterprise or Metro networks.

Some of our current and potential competitors have longer operating histories and substantially greater financial, technical, sales, marketing and other resources, as well as greater name recognition and a larger installed customer base, than we do. As a result, these competitors are able to devote greater resources to the development, promotion, sale and support of their products. In addition, competitors with a large installed customer base may have a significant competitive advantage over us. We have encountered, and expect to continue to encounter, many potential customers who are confident in and committed to the product offerings of our principal competitors, including Cisco Systems. Accordingly, these potential customers may not consider or evaluate our products. When such potential customers have considered or evaluated our products, we have in the past lost, and expect in the future to lose, sales to some of these customers as large competitors have offered significant price discounts to secure these sales.

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

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

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

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

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

Our Future Success Will Depend in Part Upon Increasing Our Revenue in the U.S. Market.

Revenues in the U.S. declined 5.8% in fiscal 2007 from fiscal 2006 and declined 12.7% in fiscal 2006 from fiscal 2005. We believe a number of factors have contributed to the decline in our revenues in the U.S., including turnover in our sales and marketing personnel, intense competition, as well as the timing of customer purchase decisions. Our success will depend upon increasing our revenue in the United States and we may need to identify new strategies or markets to increase revenue. We are initiating a number of programs to improve retention of our sales personnel and to compete more effectively in the U.S. market. If these efforts are not successful, our ability to sustain and grow our revenue and to achieve increased profitability would be adversely affected.

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

International sales constitute a significant portion of our net revenues. Our ability to grow will depend in part on the expansion of international sales. Sales to customers outside of the United States accounted for approximately 60%, 59% and 56% of our net revenues for fiscal 2007, fiscal 2006 and fiscal 2005, respectively. Our international sales primarily depend on the success of our resellers and distributors. The failure of these resellers and distributors to sell our products internationally would limit our ability to sustain and grow our revenue. There are a number of risks arising from our international business, including:

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

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

We have entered into foreign exchange forward contracts to offset the impact of payment of operating expenses in local currencies to some of our operating foreign subsidiaries. However, if we are not successful in managing these hedging transactions, we could incur losses from hedging activities.

Conducting our Business on a Global Basis Requires Us to Comply with Various Foreign and Domestic Regulatory Requirements.

Conducting our business on a global basis subjects us to a number of frequently changing and complex regulatory requirements, and as we expand our operations into new territories, we may become subject to an increasing number of such regulatory requirements. These regulatory requirements vary from jurisdiction to jurisdiction, and may be inconsistent with one another. Our efforts to comply with the new and differing requirements increases our costs of goods and other expenses and may delay the production and shipment of our products, which could adversely impact revenue recognition and harm our financial results. In addition, failure to comply with the requirements of a single jurisdiction may adversely impact our ability to do business in that jurisdiction as well as other jurisdictions, which would harm our financial results.

Trade measures, environmental and import and export requirements are among the regulations with which we must comply. Failure to comply with such requirements may result in the imposition of financial penalties and restrictions on our ability to conduct business in and with certain countries, which may harm our business and damage our reputation. In the past, we were subject to an investigation by the U.S. Department of Commerce in connection with the possible violation of certain export regulations. The Department of Commerce has completed an investigation and we were required to pay a fine of $35,000. While this matter was resolved and we have also implemented procedures to reduce the risk of violations in the future, there can be no assurances that we will not become subject to such investigations in the future.

In connection with compliance with regulatory requirements, from time to time, we have been and may in the future become subject to audit by various governmental agencies seeking to review the compliance of our products or business practices with their regulations. When such audits occur and whether or not we are in compliance with the particular regulation, we may be required to cease shipment or production of our product in that particular jurisdiction while we seek to show our compliance with such regulations and our business may be adversely affected as a result.

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

The network equipment industry has traditionally experienced a rapid erosion of average selling prices due to a number of factors, including competitive pricing pressures, promotional pricing and technological progress. We anticipate that the average selling prices of our products will decrease in the future in response to competitive pricing pressures, excess inventories, increased sales discounts and new product introductions by us or our competitors, including, for example, competitive products manufactured with low-cost merchant silicon. We may experience substantial decreases in future operating results due to the erosion of our average selling prices. To maintain our gross margin, we must develop and introduce on a timely basis new products and product enhancements and continually reduce our product costs. Our failure to do so would likely cause our revenue and gross margins to decline, which could have a material adverse effect on our operating results and cause the price of our common stock to decline.

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

As of July 1, 2007, no customers accounted for more than 10% of our accounts receivable balance. Some of our customers are likely to experience serious cash flow problems and, as a result, may find it difficult to obtain financing, if financing is available at all. If our customers are not successful in generating sufficient revenue or securing alternate financing arrangements, they may not be able to pay, or may delay payment of, the amounts that they owe us.

In addition, sales to the service provider market are especially volatile and continued declines or delays in sale orders from this market may harm our financial condition. Furthermore, they may not order as many products from us as originally forecast, or cancel orders with us entirely. The inability of some of our potential customers to pay us for our products may adversely affect our cash flow, the timing of our revenue recognition and the amount of revenue, which may cause our stock price to decline.

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

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

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

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

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

When we announce new products or product enhancements that have the potential to replace or shorten the life cycle of our existing products, customers may defer or cancel orders for our existing products. These actions could have a material adverse effect on our operating results by unexpectedly decreasing sales, increasing inventory levels of older products and exposing us to greater risk of product obsolescence. The market for switching products is evolving and we believe our ability to compete successfully in this market is dependent upon the continued compatibility and interoperability of our products with products and architectures offered by other vendors. We have experienced delays in releasing new products and product enhancements in the past that resulted in lower quarterly revenue than anticipated. We may experience similar delays in product development and releases in the future, and any delay in product introduction could adversely affect our ability to compete, causing our operating results to be below our expectations or the expectations of public market analysts or investors.

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

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

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

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

In addition, products or technologies acquired by us may include so-called “open source” software. Open source software is typically licensed for use at no initial charge, but imposes on the user of the open source software certain requirements to license to others both the open source software as well as the software that relates to, or interacts with, the open source software. Our use of open source software subjects us to certain additional risks for the following reasons:

- open source license terms may be ambiguous and may result in unanticipated obligations regarding our products;
- open source software cannot be protected under trade secret law; and
- it may be difficult for us to accurately determine the developers of the open source code and whether the acquired software infringes third-party intellectual property rights.

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

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

We have received notice from some companies alleging that we may be infringing their patents. One company, Enterasys Networks, Inc., recently filed a claim against us alleging patent infringement. We are evaluating the merits of the claim and have filed counter claims in the matter. Without regard to the merits of this or any other claim, if judgments by a court of law on this or any other claim received in the future were to be upheld, or if we were otherwise to agree to the settlement of such claims, the consequences to us may be severe and could require us, among other actions to:

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

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

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

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

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

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

- the demand for switching products (Gigabit Ethernet and Layer 3 switching technologies in particular) in the enterprise and service provider markets;
- the performance, price and total cost of ownership of our products;
- the availability and price of competing products and technologies;

- our ability to match supply with demand for certain products; and
- the success and development of our resellers, distributors and field sales channels.

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

Our Reliance on Industry Standards, Technological Change in the Marketplace and New Product Initiatives May Cause our Sales to Fluctuate or Decline.

The network equipment industry in which we compete is characterized by rapid changes in technology and customers requirements and evolving industry standards. As a result, our success depends on:

- the timely adoption and market acceptance of industry standards, and timely resolution of conflicting U.S. and international industry standards; and
- our ability to influence the development of emerging industry standards and to introduce new and enhanced products that are compatible with such standards.

Slow market acceptance of new technologies, products or industry standards could adversely affect our sales or overall results of operations. In addition, if our technology is not included in an industry standard on a timely basis or if we fail to achieve timely certification of compliance to industry standards for our products, our sales of such products or our results of operations could be adversely affected.

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

To date, a limited number of resellers, distributors and other customers have accounted for a significant portion of our revenue. One distributor, Tech Data, accounted for greater than 10% of our net revenue in fiscal 2007, 2006 and 2005. In addition, while no other distributor or customer has accounted for 10% or more of revenue in the recent fiscal years, sales to several distributors represent a high percentage of our sales. If any of our large customers stop or delay purchases, our revenue and profitability would be adversely affected.

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

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

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

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

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

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

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

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

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

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

Our principal limited-source components include:

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

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

Our Dependence on Two Contract Manufacturers for All of Our Manufacturing Requirements Could Harm Our Operating Results.

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

We rely on two independent contractors to manufacture all of our products. Flextronics International, Ltd. manufactures products for one of our product lines. This company’s facilities are located in San Jose, California and Guadalajara, Mexico. Our commitment with Flextronics is formalized through a one-year contract. Alpha Networks, located in Hsinchu, Taiwan, manufactures products for our second product line. We have experienced delays in product shipments from contract manufacturers in the past, which in turn delayed product shipments to our customers. These or similar problems may arise in the future, such as products of inferior quality, insufficient quantity of products, or the interruption or discontinuance of operations of a manufacturer, any of which could have a material adverse effect on our business and operating results.

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

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

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

Our ability to successfully implement our business plan and comply with regulations requires an effective planning and management process. We need to continue improving our existing, and implement new, operational and financial systems, procedures and controls. Any delay in the implementation of, or disruption in the transition to, new or enhanced systems, procedures or controls, could harm our ability to record and report financial and management information on a timely and accurate basis, or to forecast future results.

We May Be Unable to Reasonably Anticipate Whether a Change in Our Process Will Have a Material Affect on Our Internal Control Over Financial Reporting.

As we improve our controls and procedures in our ongoing effort to improve our business systems, we may be required to make changes to our internal control over financial reporting. We may be unable to reasonably anticipate, both during the period in which such changes are made and at the time we file the periodic reports covering such period, that such changes will have a material affect on our internal control over financial reporting. If we are unable to reasonably anticipate such material affect, it will have an adverse effect on our ability to accurately report our changes in internal control over financial reporting.

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

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

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

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

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

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

We Have Been Named as a Defendant in a Shareholder Class Action Lawsuit Arising Out of Our Public Offerings of Securities in 1999 and May be Involved in Additional Litigation in the Future.

Beginning on July 6, 2001, purported securities fraud class action complaints were filed in the United States District Court for the Southern District of New York. The cases were consolidated and the litigation is now captioned as In re Extreme Networks, Inc. Initial Public Offering Securities Litigation, Civ. No. 01-6143 (SAS) (S.D.N.Y.), related to In re Initial Public Offering Securities Litigation, 21 MC 92 (SAS) (S.D.N.Y.). The operative amended complaint is brought purportedly on behalf of all persons who purchased Extreme Networks' common stock from April 8, 1999 through December 6, 2000. It names as defendants Extreme Networks; six of our present and former officers and/or directors, including our CEO (the "Extreme Networks Defendants"); and several investment banking firms that served as underwriters of our initial public offering and October 1999 secondary offering. (See "Other Matters" in Item 3 *Legal Proceedings*) We cannot assure you that we will prevail in the lawsuit. Failure to prevail could have a material adverse effect on our consolidated financial position, results of operations and cash flows in the future.

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

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

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

In addition, the continued threat of terrorism and heightened security and military action in response to this threat, or any future acts of terrorism, may cause further disruptions to the economies of the U.S. and other countries. If such disruptions result in delays or cancellations of customer orders for our products, our business and operating results will suffer.

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

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

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

Production and marketing of products in certain states and countries may subject us to environmental and other regulations including, in some instances, the requirement to provide customers the ability to return product at the end of its useful life, and place the responsibility for environmentally safe disposal or recycling with us. Additionally, certain states and countries may pass regulations requiring our products to meet certain requirements to use environmentally friendly components. Such laws and regulations have recently been passed in several jurisdictions in which we operate, including the European Union which issued a Directive 2002/96/EC

Waste Electrical and Electronic Equipment ("WEEE") to mandate funding, collection, treatment, recycling and recovery of WEEE by producers of electrical or electronic equipment into Europe. China is in the final approval stage of compliance programs which will harmonize with the European Union WEEE. In the future, Japan and other countries are expected to adopt environmental compliance programs. If we fail to comply with these regulations, we may not be able to sell our products in jurisdictions where these regulations apply, which would have a material adverse affect on our results of operations.

In addition, the EU also adopted Directive 2002/95/EC on Restriction on the Certain Hazardous Substances in Electrical and Electronic Equipment (the "RoHS Directive"). The RoHS Directive bans in the EU the use of certain hazardous materials in electrical and electronic equipment. The RoHS Directive went into effect on July 1, 2006, the date by which each EU-member country was required to adopt legislation implementing the RoHS Directive in that country. Certain EU-member countries where we import products have adopted such implementing legislation effective July 1, 2006, while other EU-member countries have either not yet adopted implementing legislation or have not yet adopted rules under their implementing legislation. The manner of implementation of the RoHS Directive in each EU country will likely vary, and we will face challenges complying with the differing implementation of the RoHS Directive in each country. Failure to comply with the regulatory requirements in one jurisdiction may adversely impact our ability to do business in that jurisdiction as well as others. We have incurred higher manufacturing costs and increased our European service spare parts inventory by approximately $5.1 million as of July 2, 2006 as a result of complying with the RoHS Directive. During fiscal 2007, we did not increase our European service spare parts inventory further as a result of complying with the RoHS Directive. As of July 1, 2007, we were fully compliant with the RoHS Directive. Similar legislation has been or could be enacted in other countries outside the EU, the cumulative impact of which could similarly impact our financial condition or results of operations.

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

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

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

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

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

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

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

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

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

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

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

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

We have certain long-term real estate lease commitments carrying future obligations for non-cancelable lease payments. Reductions in our workforce and the restructuring of operations since fiscal 2002 have resulted in the need to consolidate certain of these leased facilities, located primarily in Northern California, for which we recorded excess facilities charges of approximately \$4.0 million in fiscal 2007, \$3.3 million in fiscal 2006, \$6.5 million in fiscal 2004, and \$9.6 million in fiscal 2003. For more information, see Note 12 of Notes to Consolidated Financial Statements. We may incur additional charges for excess facilities as a result of additional reductions in our workforce or future restructuring of operations. We will continue to be responsible for all carrying costs of these facilities until such time as we can sublease these facilities or terminate the applicable leases based on the contractual terms of the lease agreements, and these costs may have an adverse effect on our business, operating results and financial condition.

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

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

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

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

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

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

Item 1B. ***Unresolved Staff Comments***

Not applicable.

Item 2. ***Properties***

Our principal administrative, sales, marketing and research and development facilities are located in Santa Clara, California. We also lease office space and executive suites in various other geographic locations domestically and internationally for sales and service personnel and engineering operations. Our aggregate lease expense for fiscal 2007 was approximately $4.8 million, net of sublease income of approximately $0.1 million. We believe our current facilities will adequately meet our growth needs for the foreseeable future, and we are actively engaged in efforts to sublease excess space we acquired in prior years to meet the anticipated growth at that time.

Item 3. ***Legal Proceedings***

Government Inquiries Relating to Historical Stock Option Practices

On June 27, 2006, the Company received an informal inquiry letter from the Staff of the SEC Enforcement Division requesting that the Company voluntarily provide documents related to its policies, practices and procedures for granting stock options for the period since its initial public offering on April 9, 1999 ("IPO"). The Company responded to the request, is cooperating fully with the SEC inquiry, and intends to continue to do so.

This inquiry likely will require the Company to expend significant management time and incur significant legal and other expenses, and could result in civil actions seeking, among other things, injunctions against the Company and the payment of significant fines and penalties by the Company, which may adversely affect the Company's results of operations and cash flow.

The Company cannot predict how long it will take to or how much more time and resources the Company will have to expend to resolve this government inquiry, nor can we predict the outcome of this inquiry. Also, there can be no assurance that other inquiries, investigations or actions will not be started by other United States federal or state regulatory agencies or by foreign governmental agencies.

Late SEC Filings, Failure to Hold Annual Meeting and Nasdaq Delisting Proceedings

Due to the Special Committee investigation and the resulting restatement of our fiscal 2000 through 2005 financial statements, the Company did not timely file its Form 10-K for the fiscal year ending July 2, 2006 or the Quarterly Reports on Forms 10-Q for the quarters ended October 1, 2006, December 31, 2006 and April 1, 2007. The Company initially received Nasdaq Staff Determination notices stating that the Company was not in compliance with Marketplace Rule 4310(c)(14) because it had not timely filed such periodic reports with the SEC. Those filings were made on June 28, 2007. On July 2, 2007, the Company received a written notice from the Nasdaq Stock Market stating that the Nasdaq Listing and Hearing Review Council (the "Listing Council") had determined that as of that date the Company had demonstrated compliance with all Nasdaq Marketplace Rules.

On July 3, 2007, the Company received a further Staff Determination notice from the Nasdaq Stock Market stating that the Company was not in compliance with Nasdaq's Marketplace Rule 4350(e) due to a failure by the Company to hold its annual meeting of shareholders within the time required by Rule 4350(e). On July 30, 2007, the Company had held an annual meeting of shareholders and subsequently received a written notice from the Panel confirming that the Company had demonstrated compliance with all Nasdaq Marketplace Rules, and that the Panel determined to continue the listing of the Company's securities on The Nasdaq Stock Market. Accordingly, the Company believes that the Nasdaq delisting proceedings have concluded.

We cannot predict, however, whether the SEC will review these reports and, if so, whether the SEC will have comments on these reports (or other reports that we previously filed) that may require us to file amended reports with the SEC. In addition, we cannot predict whether the Nasdaq Listing Qualifications Panel or Listing Council will concur that we are in compliance with all relevant listing requirements. If either of those events occurs, we might be unable to remain in compliance with SEC reporting requirements and Nasdaq listing requirements, and, therefore, we might be unable to maintain an effective listing of our common stock on the Nasdaq Global Select Market or any other national securities exchange.

Shareholder Litigation Relating to Historical Stock Option Practices

On April 25, 2007, an individual identifying herself as a shareholder of the Company filed a derivative action in the United States District Court for the Northern District of California purporting to assert claims on behalf of and in the name of the Company against various of our current and former directors and officers relating to our stock option granting practices for stock options issued from 2000 to 2003. The complaint alleges that the individual defendants breached their fiduciary duties and other obligations to the Company and violated federal securities laws in connection with our historical stock option granting process and our accounting for past stock options.

The plaintiff has asserted claims for violations of Sections 10(b) (including Rule 10b-5 thereunder), 14(a), and 20(a) of the Securities Exchange Act of 1934, unjust enrichment, breach of fiduciary duty and aiding and abetting such breach, rescission, and a claim for an accounting of all stock option grants made to the named defendants. Extreme Networks, Inc. is named as a nominal defendant in these actions. On behalf of Extreme Networks, Inc., the plaintiff seeks unspecified monetary and other relief against the named defendants. The plaintiff is Yenna Wu. The individual named defendants are Gordon L. Stitt, Herb Schneider, Stephen Haddock, Paul Romeo, Vito Palermo, Harold Covert, Darrell Scherbarth, Christopher, N. Todd, Alexander J. Gray, Frank C. Carlucci, William R. Slakey, Charles Carinalli, Harry Silverglide, Michael West, Kenneth Levy, Robert L. Corey, Peter Wolken, and Promod Haque.

A similar derivative action was filed in the same court on May 2, 2007, by Linda Erikson, another individual identifying herself as a shareholder of the Company, alleging the same legal claims against the same individual defendants concerning the same subject matter.

A third derivative action was filed in the same court on May 31, 2007 by Frank A. Grucel, Jr., an individual identifying himself as a shareholder of the Company, purporting to assert claims on the Company's behalf relating to the Company's historic stock options granting practices. The complaint seeks unspecified monetary and injunctive relief and asserts claims for violations of Section 14(a) of the Securities Exchange Act of 1934, an accounting of all stock option grants made to the named defendants, breach of fiduciary duty and aiding and abetting such breach, abuse of control, gross mismanagement, constructive fraud, corporate waste, unjust enrichment, rescission, violations of California Corporations Code Section 25402, and breach of fiduciary duties related to insider selling and alleged misappropriation of information. Extreme Networks, Inc. is named as a nominal defendant in this action, and the individual named defendants are Gordon L. Stitt, Herb Schneider, Stephen Haddock, Alexander J. Gray, Frank C. Carlucci, William R. Slakey, Charles Carinalli, Harry Silverglide, Michael West, Kenneth Levy, Robert L. Corey, Peter Wolken, Michael Palu, and Alicia Moore.

The foregoing actions have been related and assigned to the same judge. On June 15, 2007, Yenna Wu filed an amended complaint in her action. The amended complaint names one additional individual defendant, Mark Canepa, as well as the individual defendants named in the derivative complaints filed on April 25, 2007 and May 2, 2007, is purportedly brought both as a derivative action and as a class action on behalf of all current shareholders of the Company, and alleges a claim for violation of Delaware General Corporations Code Section 211(c), seeking an order compelling the Company to hold a shareholder's meeting. The amended complaint otherwise alleges the same claims as the derivative complaints filed on April 25, 2007 and May 2, 2007 by plaintiffs Wu and Erikson, respectively.

On August 2, 2007, the foregoing actions were consolidated for all purposes. Subsequently, on August 13, 2007, plaintiff Frank A. Grucel, Jr. was named lead plaintiff and his attorneys named lead counsel in the consolidated actions. This consolidated action is at an early stage, with a consolidated complaint to be filed by September 27, 2007. Discovery has not yet commenced and the defendants are not required to respond to the complaints currently on file. We cannot at this time predict whether this consolidated action will result in any material recovery by or expense to the Company.

Indemnification Obligations

Subject to certain limitations, we may be obligated to indemnify our current and former directors, officers and employees. These obligations arise under the terms of our certificate of incorporation, our bylaws, applicable contracts, and Delaware and California law. The obligation to indemnify, where applicable, generally means that we are required to pay or reimburse, and in certain circumstances we have paid or reimbursed, the individuals' reasonable legal expenses and possibly damages and other liabilities incurred in connection with these matters. It is not possible to estimate the maximum potential amount under these indemnification agreements due to the limited history of these claims. The cost to defend the Company and the named individuals could have a material adverse effect on our consolidated financial position, results of operations and cash flows in the future. Recovery of such costs under our directors and officers insurance coverage is uncertain.

Other Legal Matters

On April 20, 2007, Extreme Networks filed suit against Enterasys in the United States District Court for the Western District of Wisconsin, Civil Action No. 07-C-0229-C. The complaint alleges willful infringement of U.S. patents Nos. 6,104,700, 6,678,248, and 6,859,438, and seeks injunctive relief against Enterasys' continuing sale of infringing goods and monetary damages. Enterasys responded to the complaint on May 30, 2007. Enterasys also filed a counterclaim alleging infringement of three U.S. patents owned by Enterasys. The case is in its early stages, however a Markman Hearing has been scheduled for October 2007, and a trial date has been set for May 2008.

On December 27, 2005, Broadband Office Inc. ("Broadband") served an amended complaint, adding Extreme Networks as a defendant in its lawsuit against Technology Credit Corporation ("TCC") and Key Equipment Finance, Inc., seeking recovery of an alleged preferential payment in the amount of $0.8 million plus interest, purportedly paid by Broadband to TCC within ninety days prior to Broadband's petition for bankruptcy protection. Extreme disputes that it owes any money to Broadband, and intends vigorously to defend against the claims.

On June 21, 2005, Enterasys filed suit against Extreme Networks and Foundry Networks, Inc. ("Foundry") in the United States District Court for the District of Massachusetts, Civil Action No.05-11298 DPW. The complaint alleges willful infringement of U. S. Patent Nos. 5,251,205; 5,390,173; 6,128,665; 6,147,995; 6,539,022; and 6,560, 236, and seeks: a) a judgment that Extreme willfully infringes each of the patents; (b) a permanent injunction from infringement, inducement of infringement and contributory infringement of each of the six patents; (c) damages and a "reasonable royalty" to be determined at trial; (d) trebled damages; (e) attorneys fees, costs and interest; and (f) equitable relief at the court's discretion. The Markman hearing has been rescheduled for October 2007. We intend vigorously to defend against Enterasys' assertions, which we believe to be without merit.

On May 27, 2003, Lucent filed suit against Extreme Networks and Foundry in the United States District Court for the District of Delaware, Civil Action No. 03-508. The complaint alleged willful infringement of U.S. Patent Nos. 4,769,810, 4,769,811, 4,914,650, 4,922,486 and 5,245,607. After the Markman hearing, Lucent dropped its claims relating to the 5,245,607 patent. The judge split the case into three parts to be tried separately: phase 1 to cover infringement, willfulness and damages; phase 2 to cover invalidity; and phase 3 to cover equitable defenses and our counterclaims. On May 9, 2005, a jury in Delaware awarded a verdict to Extreme in the phase 1 trial of non-infringement on 18 out of the 19 claims asserted. The jury did award Lucent damages of approximately $275,000 on the remaining claim; which covers a feature that is not offered in our current product line. The parties each filed post-trial motions; and on August 16, 2005, the judge granted Lucent's motion for a new trial, ruling that Extreme impermissibly introduced to the jury evidence of its prior relationship with Lucent. Extreme's motion for reconsideration was denied. On August 9, 2006, the parties entered into a settlement agreement to resolve all outstanding claims which includes the dismissal of all claims and a patent cross-license for a defined term.

Beginning on July 6, 2001, purported securities fraud class action complaints were filed in the United States District Court for the Southern District of New York. The cases were consolidated and the litigation is now captioned as In re Extreme Networks, Inc. Initial Public Offering Securities Litigation, Civ. No. 01-6143 (SAS) (S.D.N.Y.), related to In re Initial Public Offering Securities Litigation, 21 MC 92 (SAS) (S.D.N.Y.).The operative amended complaint names as defendants Extreme Networks; six of our present and former officers and/or directors, including our CEO (the “Extreme Networks Defendants”); and several investment banking firms that served as underwriters of our initial public offering and October 1999 secondary offering. The complaint alleges liability under Sections 11 and 15 of the Securities Act of 1933 and Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, on the grounds that the registration statement for the offerings did not disclose that: (1) the underwriters had agreed to allow certain customers to purchase shares in the offerings in exchange for excess commissions paid to the underwriters; and (2) the underwriters had arranged for certain customers to purchase additional shares in the aftermarket at predetermined prices. Similar allegations were made in other lawsuits challenging over 300 other initial public offerings and follow-on offerings conducted in 1999 and 2000. The cases were consolidated for pretrial purposes.

Previously, we executed a settlement agreement presented to all issuer defendants. In that settlement, plaintiffs would dismiss and release all claims against the Extreme Network Defendants, in exchange for a contingent payment by the insurance companies collectively responsible for insuring the issuers in all of the IPO cases, and for the assignment or surrender of control of certain claims we may have against the underwriters. The Extreme Networks Defendants would not be required to make any cash payments in the settlement, unless the pro rata amount paid by the insurers in the settlement exceeded the amount of the insurance coverage. The Court gave preliminary approval to the settlement in February 2005 and held a hearing in April 2006 to consider final approval of the settlement. Before the Court issued a final decision on the settlement, on December 5, 2006 the United States Court of Appeals for the Second Circuit vacated the class certification of plaintiffs’ claims against the underwriters in six cases designated as focus or test cases. Thereafter, on December 14, 2006, the Court ordered a stay of all proceedings in all of the lawsuits pending the outcome of plaintiffs’ petition to the Second Circuit Court of Appeals for a rehearing en banc and resolution of the class certification issue. On April 6, 2007, the Second Circuit Court of Appeals denied plaintiffs’ petition for a rehearing, but clarified that the plaintiffs may seek to certify a more limited class. Accordingly, the plaintiffs and issuers have stated that they are prepared to discuss how the settlement might be amended or renegotiated to comply with the decision of the Second Circuit Court of Appeals. On April 30, 2007, Plaintiffs stated that they intend to present a proposed redefined class to the Court. If the settlement is not amended or renegotiated and then approved by the Court, there is no assurance that we will prevail in the lawsuit. Failure to prevail could have a material adverse effect on our consolidated financial position, results of operations and cash flows in the future.

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

Not applicable.

PART II

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

Common Stock Market Prices and Dividends

Our common stock commenced trading on The Nasdaq Global Market on April 9, 1999 under the symbol "EXTR." The following table sets forth the high and low sales prices as reported by Nasdaq. Such prices represent prices between dealers, do not include retail mark-ups, mark-downs or commissions and may not represent actual transactions.

Stock Prices	High	Low
Fiscal year ended July 1, 2007:		
First quarter	$4.22	$3.39
Second quarter	$4.26	$3.60
Third quarter	$4.65	$3.94
Fourth quarter	$4.47	$3.72
Fiscal year ended July 2, 2006:		
First quarter	$5.14	$4.06
Second quarter	$5.26	$4.34
Third quarter	$5.22	$4.48
Fourth quarter	$5.09	$4.02

At August 15, 2007, there were approximately 358 stockholders of record of our common stock and approximately 25,778 beneficial stockholders. We have never declared or paid cash dividends on our capital stock and do not anticipate paying any cash dividends in the foreseeable future. We currently intend to retain future earnings for the development of our business.

Item 6. *Selected Financial Data*

The following table sets forth selected consolidated financial data for each of the fiscal years ended July 1, 2007, July 2, 2006, July 3, 2005, June 27, 2004 and June 29, 2003. These tables should be reviewed in conjunction with the Consolidated Financial Statements in Item 8 and related Notes, as well as Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations." Historical results may not be indicative of future results.

	Year Ended				
	July 1, 2007(1)	July 2, 2006(2)	July 3, 2005(3)	June 27, 2004(4)	June 29, 2003(5)
	(In thousands, except per share amounts)				
Consolidated Statements of Operations Data:					
Net revenues	$342,834	$358,601	$383,347	$351,848	$ 363,276
Net income (loss)	$ (14,197)	$ 8,509	$ 12,519	$ (3,292)	$ (282,171)
Net income (loss) per share – basic	$ (0.12)	$ 0.07	$ 0.10	$ (0.02)	$ (2.45)
Net income (loss) per share – diluted	$ (0.12)	$ 0.07	$ 0.10	$ (0.02)	$ (2.45)
Shares used in per share calculation – basic	114,122	121,286	121,225	118,348	115,186
Shares used in per share calculation – diluted	114,122	123,049	124,166	118,348	115,186

	As of				
	July 1, 2007	July 2, 2006	July 3, 2005	June 27, 2004	June 29, 2003
			(In thousands)		
Consolidated Balance Sheets Data:					
Cash and cash equivalents, short-term investments and marketable securities	$ 215,855	$ 433,105	$ 440,404	$ 425,672	$ 402,157
Deferred tax asset	$ 1,118	$ 500	$ 430	$ 886	$ 609
Total assets	$ 341,897	$ 558,718	$ 583,614	$ 579,273	$ 550,257
Convertible subordinated notes	$ —	$ 200,000	$ 200,000	$ 200,000	$ 200,000
Other long-term liabilities	$ 21,392	$ 23,056	$ 30,698	$ 41,308	$ 22,313
Common stock and capital in excess of par value	$ 934,540	$ 927,835	$ 915,945	$ 910,546	$ 876,186
Accumulated deficit	$(670,585)	$(656,387)	$(664,896)	$(677,415)	$(674,123)

(1) Fiscal 2007 net loss includes share-based compensation expense of $6.2 million and restructuring charge of $4.0 million.

(2) Fiscal 2006 net loss includes share-based compensation expense of $7.0 million and restructuring charge of $3.3 million.

(3) Fiscal 2005 net income includes share-based compensation expense of $0.8 million and other income includes $3.9 million from the relief of a foreign consumption tax obligation.

(4) Fiscal 2004 net loss includes share-based compensation expense of $4.0 million and other income includes $7.9 million in cash settlements from vendors, net of related expenses, and other income of $2.5 million from the relief of a foreign consumption tax obligation.

(5) Fiscal 2003 net loss includes share-based compensation expense of $23.1 million and a $194.8 million charge in our tax provision reflecting our provision of a full valuation allowance against deferred tax assets.

Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operation*

Business Overview

We develop and sell a family of modular and stackable network infrastructure equipment and offer related service contracts for extended warranty and maintenance agreements. Substantially all of our revenue is derived from the sale of our networking equipment and the related service contracts. We believe that understanding the following key developments is helpful to an understanding of our operating results for fiscal 2007.

Increased Product Breadth

We believe that continued success in the marketplace will depend on our ability to develop new and enhanced products employing leading-edge technology. In fiscal 2007 we introduced several new products that allow for the continued deployment of secure, converged networks as well as the expansion of the ExtremeXOS™ operating system from the core to the edge of the network. The following products were released in fiscal 2007: release 12.0 of ExtremeXOS™, our award-winning modular network operating system, the Summit X250 ExtremeXOS™-based fixed switches, and Summit WM 200 and WM 2000 wireless network controllers.

Convergence of Voice, Video and Data

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

We have a comprehensive strategic alliance with Avaya, Inc. to jointly develop and market converged communications solutions. The alliance brings together Avaya's global market leadership in IP voice and telephony with Extreme's expertise in high performance IP data network infrastructure. Under a joint development agreement, the companies develop next generation, standards-based technologies in the areas of network management and provisioning, Quality of Service, security, and network resilience. Additionally, Avaya sells services and supports Extreme's entire portfolio of data networking products through their worldwide sales organization and the Avaya Global Services organization.

Business Environment

The market for network infrastructure equipment is highly competitive and dominated by a few large companies. The layer 2 and layer 3 ethernet switch market growth rates have been in the high single digit to low double digit range over the most recent three years. In fiscal 2006 and fiscal 2007, however, we experienced a significant decline in demand in the service provider segment in Japan and lower revenue in the enterprise segment in the U.S.

Results of Operations

Our operations and financial performance have been affected by the economic factors described above, and during fiscal 2007, we achieved the following results:

- Net revenues of $342.8 million, a decrease of 4.4% over fiscal 2006 net revenues of $358.6 million.
- Service revenue of $62.3 million, a decrease of 2.3% from fiscal 2006 service revenue of $63.8 million.
- Although net revenues decreased in fiscal 2007 from fiscal 2006, total gross margin remained fairly consistent in fiscal 2007 at 54.0% of net revenues (including share-based compensation expense of $1.1 million), compared to 54.1% in fiscal 2006.
- Net loss of $14.2 million (including share-based compensation expense of $6.2 million), a decrease from net income of $8.5 million in fiscal 2006.
- Cash flow used in operating activities was $0.3 million in fiscal 2007, compared with $28.0 million of cash generated in operating activities in fiscal 2006, a decrease of $28.3 million. Cash and cash equivalents, short-term investments and marketable securities were $215.9 million as of July 1, 2007. In December 2006, we retired $200 million of convertible subordinated notes on their maturity date.

Net Revenues

The following table presents net product and service revenues for the fiscal years 2007, 2006 and 2005 (dollars in thousands):

	Year Ended					
	July 1, 2007	% of Net Revenues	July 2, 2006	% of Net Revenues	July 3, 2005	% of Net Revenues
Net revenues:						
Product	$280,497	81.8%	$294,824	82.2%	$324,256	84.6%
Service	62,337	18.2%	63,777	17.8%	59,091	15.4%
Total net revenues	$342,834	100.0%	$358,601	100.0%	$383,347	100.0%

Net revenues were $342.8 million in fiscal 2007, $358.6 million in fiscal 2006 and $383.3 million in fiscal 2005, representing a decrease of 4.4% in fiscal 2007 from fiscal 2006 and a decrease of 6.5% in fiscal 2006 from fiscal 2005. Fiscal 2007 and 2006 had 52 weeks, compared with 53 weeks in fiscal 2005, and we believe that the additional week in fiscal 2005 may have a negative impact on the comparison of our sales from fiscal 2005 to fiscal 2006. However, we are not able to quantify the effect of the additional week of sales on our revenue in fiscal 2005.

Product revenue was $280.5 million in fiscal 2007, $294.8 million in fiscal 2006 and $324.3 million in fiscal 2005, representing a decrease of 4.9% in fiscal 2007 from fiscal 2006, and a decrease of 9.1% in fiscal 2006 from fiscal 2005. The decrease in product revenue in fiscal 2007 from fiscal 2006 was principally due to lower sales volume and an increase in discounts. The decrease in product revenue in fiscal 2006 from fiscal 2005 was primarily due to a decline in volume and to a lesser extent, higher discounts caused by a slight shift in geographic mix of sales. We expect that average selling prices across the industry will continue to be subject to competitive pressure and may decline somewhat going forward.

Service revenue was $62.3 million in fiscal 2007, or a 2.3% decrease over fiscal 2006 service revenue of $63.8 million. Service revenue was $63.8 million in fiscal 2006, or a 7.9% increase over fiscal 2005 service revenues of $59.1 million. The decrease in service revenue in fiscal 2007 from fiscal 2006 was due to a decrease in maintenance contract revenue as a result of lower product revenue. The increase in service revenue in fiscal 2006 from fiscal 2005 was the result of our efforts to focus on increasing the number of service contracts initially sold with new products and increasing contract renewal rates. As a percentage of total net revenues, service revenue was 18.2% in fiscal 2007, 17.8% in fiscal 2006 and 15.4% in fiscal 2005.

The following table presents the total net revenues geographically for the fiscal years 2007, 2006 and 2005 (dollars in thousands):

	Year Ended					
	July 1, 2007	% of Net Revenues	July 2, 2006	% of Net Revenues	July 3, 2005	% of Net Revenues
Net revenues:						
United States	$137,364	40.1%	$145,870	40.7%	$167,027	43.6%
Europe, Middle East and Africa	136,577	39.8%	124,768	34.8%	117,521	30.6%
Japan	17,844	5.2%	35,812	10.0%	58,100	15.2%
Other	51,049	14.9%	52,151	14.5%	40,699	10.6%
Total net revenues	$342,834	100.0%	$358,601	100.0%	$383,347	100.0%

Revenues outside of the United States accounted for 59.9%, 59.3% and 56.4% of net revenues in fiscal 2007, fiscal 2006, and fiscal 2005, respectively. In fiscal 2007, U.S. revenues were $137.4 million, a decrease of $8.5 million, or 5.8% over the fiscal 2006 results. The decline in revenue in the U.S. is primarily a result of lower sales volume. Revenues outside the U.S., as a percentage of total net revenues, in fiscal 2007 decreased by 0.6% compared to fiscal 2006 due to a decrease of 4.8% and 0.4% in net revenues in Japan and other international regions, respectively, offset in part by an increase in net revenues in Europe, the Middle East and Africa of 5.0%. The decline in net revenue in Japan was a result of lower demand for networking products within the service provider customer segment. Revenue in Europe, the Middle East, and Africa increased by $11.8 million, or 9.5%, in fiscal 2007 as compared to fiscal 2006. Revenue in other international regions, primarily Asia Pacific, decreased by $1.1 million in fiscal 2007 as compared to fiscal 2006 due to weak demand from enterprise customers in that region.

In fiscal 2006, U.S. revenues were $145.9 million, a decrease of $21.2 million, or 12.7% over the fiscal 2005 results. The decline in revenue in the U.S. is primarily a result of lower sales volume, in part attributed to a smaller sales force. Revenues outside the U.S., as a percentage of total net revenues, in fiscal 2006 increased by 2.9% compared to fiscal 2005 due to an increase of 4.2% and 3.9% in net revenues in Europe, the Middle East and Africa and other international regions, respectively, offset in part by a decrease in net revenues in Japan of 5.2%. The decline in net revenue in Japan was a result of lower demand for networking products within the service provider customer segment. Revenue in Europe, the Middle East, and Africa increased by $7.2 million, or 6.2%, in fiscal 2006 as compared to fiscal 2005. Revenue in other international regions, primarily Asia Pacific, increased by $11.5 million in fiscal 2006 as compared to fiscal 2005 due to strong demand from enterprise customers in that region.

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We rely upon multiple channels of distribution, including two-tiered distribution in which large distributors purchase our product and make it available to resellers. Revenue through our distributor channel was 49% of total product revenue in fiscal 2007 and 40% in fiscal 2006. The level of sales to any one customer, including a distributor, may vary from period to period; however, we expect that significant customer concentration will continue for the foreseeable future. One distributor, Tech Data, accounted for just over 10% of our net revenues in fiscal 2007, 2006 and 2005.

Cost of Revenues and Gross Margin

The following table presents the gross margin on product and service revenues and the gross margin percentage of net revenues for the fiscal years 2007, 2006 and 2005 (dollars in thousands):

	Year Ended					
	July 1, 2007	% of Net Revenues	July 2, 2006	% of Net Revenues	July 3, 2005	% of Net Revenues
Gross margin:						
Product	$156,199	55.7%	$164,267	55.7%	$177,747	54.8%
Service	28,996	46.5%	29,609	46.4%	24,832	42.0%
Total gross margin	$185,195	54.0%	$193,876	54.1%	$202,579	52.8%

Gross margin was $185.2 million in fiscal 2007, $193.9 million in fiscal 2006 and $202.6 million in fiscal 2005, representing a decrease of 4.5% in fiscal 2007 from fiscal 2006 and 4.3% in fiscal 2006 from fiscal 2005. Gross margin as a percentage of net revenues was 54.0%, 54.1% and 52.8% in fiscal 2007, fiscal 2006 and fiscal 2005, respectively.

Cost of product revenue includes costs of raw materials, amounts paid to third-party contract manufacturers, costs related to warranty obligations, charges for excess and obsolete inventory, royalties under technology license agreements, and internal costs associated with manufacturing overhead, including management, manufacturing engineering, quality assurance, development of test plans, and document control. Product gross margin in fiscal 2007 was $156.2 million, representing 55.7% of product revenues as compared to $164.3 million in fiscal 2006, or 55.7% of product revenue. The product gross margin percentage in fiscal 2007 was influenced negatively by lower sales available to absorb the fixed component of our manufacturing overhead costs and also higher inventory obsolescence costs of $1.8 million, offset positively by lower warranty expense of $1.4 million on lower volume, a reduction in per-unit product costs due to a shift in product mix, and a reduction in operations overhead costs of $3.2 million. The cost of product revenue in fiscal 2007 includes $0.8 million in share-based compensation expense compared with $0.7 million in fiscal 2006.

Product gross margin in fiscal 2006 was $164.3 million, representing 55.7% of product revenues as compared to $177.7 million in fiscal 2005, or 54.8% of product revenue. The increase in product gross margin percentage in fiscal 2006 was due to a reduction in per-unit product costs, a reduction in operations overhead and lower warranty expense on lower volume. The cost of product revenue in fiscal 2006 includes $0.7 million in share-based compensation expense compared with less than $0.1 million in fiscal 2005, as well as a decrease in expenses of $0.7 million from the transfer of a department to research and development to better align costs with current functional activities.

Cost of product revenue in all periods includes the cost of our manufacturing overhead. We outsource substantially all of our manufacturing and supply chain management operations, and we conduct quality assurance, manufacturing engineering and document control at our facility in Santa Clara, California. Accordingly, a significant portion of our cost of product revenue consists of payments to our primary contract manufacturers, Flextronics International, Ltd. located in San Jose, California and Guadalajara, Mexico and Alpha Networks, located in Hsinchu, Taiwan.

Our cost of service revenue consists primarily of labor, overhead, repair and freight costs and the cost of spares used in providing support under customer service contracts. Service gross margin in fiscal 2007 was $29.0 million, a decrease of $0.6 million from fiscal 2006 gross margin of $29.6 million. Service gross margin was 46.5% in fiscal 2007 as compared to 46.4% in fiscal 2006. Service gross margin in fiscal 2007 was negatively impacted by the decrease in service revenue, offset by improved cost control reduction. The cost of service revenue in fiscal 2007 includes $0.4 million in share-based compensation expense, consistent with $0.4 million in fiscal 2006.

Service gross margin in fiscal 2006 was $29.6 million, an increase of $4.8 million from fiscal 2005 gross margin of $24.8 million. Service gross margin was 46.4% in fiscal 2006 as compared to 42.0% in fiscal 2005. Service gross margin in fiscal 2006 was favorably impacted by the increase in service revenue and reduction in cost of service revenue, due primarily to a reduction in the costs associated with processing repairs and replacements. The cost of service revenue in fiscal 2006 includes $0.4 million in share-based compensation expense compared with zero in fiscal 2005.

Our product and service gross margins are variable and dependent on many factors, some of which are outside of our control. Some of the primary factors affecting gross margin include demand for our products, changes in our pricing policies and those of our competitors, and the mix of products sold. Our gross margin may be adversely affected by increases in material or labor costs, increases in warranty expense or the cost of providing services under extended service contracts, heightened price competition, obsolescence charges and higher inventory balances. In addition, our gross margin may fluctuate due to the mix of distribution channels through which our products are sold, including the effects of our two-tier distribution model.

Sales and Marketing Expenses

Sales and marketing expenses consist of salaries, commissions and related expenses for personnel engaged in marketing and sales functions, as well as trade shows and promotional expenses. Sales and marketing expenses were $102.1 million in fiscal 2007, $98.5 million in fiscal 2006 and $97.0 million in fiscal 2005, representing an increase of 3.7% in fiscal 2007 from fiscal 2006, and an increase of 1.5% in fiscal 2006 from fiscal 2005. The increase in fiscal 2007 was primarily due to an increase in salaries, benefits and commission expenses of $3.8 million due to a higher average headcount and employee retention program expenses and an increase in contract labor of $0.9 million, offset by decreases in professional fees of $0.5 million and share-based compensation expense of $0.6 million. The increase in fiscal 2006 was primarily due to share-based compensation expense of $2.6 million, increased information technology costs of $1.0 million, increased outsourcing of the service contract renewal process expenses of $0.6 million, increased expenses of $1.0 million from the inclusion of an additional department to better align costs with current functional activities, which in fiscal 2005 were included under General & Administrative expenses, offset by $3.8 million lower compensation costs due to lower average headcount in our sales force. As a percentage of net revenues, sales and marketing expenses were 29.8% in fiscal 2007, 27.5% in fiscal 2006 and 25.3% in fiscal 2005. The level of our sales and marketing spending in the future, in dollars and as a percentage of net revenues will depend on many factors, including the rate at which we expand our sales force and the rate at which our net revenues change.

Research and Development Expenses

Research and development expenses consist principally of salaries and related personnel expenses, consultant fees and prototype expenses related to the design, development, and testing of our products. Research and development expenses were $67.1 million in fiscal 2007, $62.0 million in fiscal 2006 and $61.5 million in fiscal 2005. The increase in fiscal 2007 was primarily due to $5.5 million increase in employee related expenses as a result of increased headcount, offset by a decrease of $1.0 million in the Avaya warrant amortization cost. The increase in fiscal 2006 was primarily due to share-based compensation expense of $1.6 million and increased engineering project expenses of $2.6 million, offset by $2.0 million lower warrant amortization expense and $1.7 million related to all other research and development expenses. Research and development expenses include $3.0

million, $4.0 million and $6.0 million in fiscal 2007, 2006 and 2005, respectively, in amortization expense related to the fair value of the warrant issued to Avaya as part of the Joint Development Agreement. The fair value of the warrant allocated to the Joint Development Agreement with Avaya is $17.9 million and is being amortized over the term of the agreement (see Note 13 of Notes to Consolidated Financial Statements). The decrease in the warrant amortization in fiscal 2007 compared to fiscal 2006 and 2005 is due to an extension of the development agreement with Avaya signed in fiscal 2006. As a percentage of total net revenues, research and development expenses were 19.6% in fiscal 2007, 17.3% in fiscal 2006 and 16.1% in fiscal 2005. We expense all research and development expenses as incurred. We believe that continued investment in research and development is critical to attaining our strategic objectives and as a result, we expect research and development expenses to increase in absolute dollars.

General and Administrative Expenses

General and administrative expenses consist primarily of salaries and related expenses for executive, finance and administrative personnel, legal fees, professional fees and other general corporate expenses. General and administrative expenses were $33.6 million in fiscal 2007, $25.5 million in fiscal 2006 and $31.7 million in fiscal 2005, representing an increase of 31.9% in fiscal 2007 from fiscal 2006, and a decrease of 19.6% in fiscal 2006 from fiscal 2005. The increase in fiscal 2007 was primarily due to $6.9 million related to the costs of the special investigation into our historical stock option granting practices, $2.3 million in legal fees related to defending claims related to our intellectual property and a shareholder derivative lawsuit related to our historical stock option granting practices, offset by a decrease of $1.2 million in bad debt expense recognized in 2006. The decrease in fiscal 2006 from fiscal 2005 of $6.2 million was primarily due to a $5.9 million decrease in legal expenses as fiscal 2005 included litigation to defend our intellectual property rights. As a percentage of net revenues, general and administrative expenses were 9.8% in fiscal 2007, 7.1% in fiscal 2006 and 8.3% in fiscal 2005. Future general and administrative expense levels will depend significantly on the level of legal expenses related to intellectual property litigation and shareholder derivative lawsuit.

Technology Agreement

On March 31, 2005, we entered into a Patent and Cross License Agreement ("Technology Agreement") with IBM. The agreement provides for a release of prior claims and a cross license of patents extending into the future from the effective date of the agreement. We charged the estimated value of the release of prior claims of $2.0 million to operating expenses in the year ended July 3, 2005 under the caption "Technology agreement". The remaining costs payable under the Technology Agreement will be charged to cost of product revenue over the license term. We expect these costs to have a small impact on the total product cost of revenue.

Amortization of Deferred Stock Compensation

Amortization of deferred stock compensation in accordance with APB 25 was zero in fiscal 2007 and fiscal 2006 and $0.1 million in fiscal 2005, representing no change in fiscal 2007 from fiscal 2006, and a decrease of $0.1 million in fiscal 2006 from fiscal 2005. Amortization of deferred stock compensation is attributable to unvested stock options subject to forfeiture issued to employees that we assumed in conjunction with acquisitions during fiscal 2001. Deferred stock compensation was amortized as charges to operations, using the graded method, over the vesting periods of the individual stock options, generally four years. Upon termination of an employee, the amount of expense recognized under the graded vesting method that is in excess of the amount actually earned is reversed. For fiscal 2007, fiscal 2006 and fiscal 2005 there was no reversal of excess compensation expense related to terminated employees. The deferred stock compensation was fully amortized at the end of fiscal 2005.

Restructuring Charge

During fiscal 2007 and 2006, we recorded restructuring charges of $4.0 million, and $3.3 million, respectively. The charges in fiscal 2007 included $1.1 million in the first through third quarters to rationalize our sales force in Japan, and $2.9 million in the fourth quarter to reduce headcount across several functional areas, terminate certain redundant contracts, and to exit an excess facility. We expect to reduce annual operating costs by $3.0 million to $4.0 million in fiscal 2008 as a result of the June 2007 restructuring charge. The charge in fiscal 2006 was for an excess facilities charge and represented an increase to the charge initially recognized during the third quarter of fiscal 2002. The commercial real estate market continued to deteriorate in fiscal 2006 and we were not able to find suitable tenants to sublease these facilities necessitating an additional charge due to lower projected sublease receipts.

Interest Income

Interest income was $13.6 million in fiscal 2007, $15.1 million in fiscal 2006 and $10.7 million in fiscal 2005, representing a decrease of $1.5 million in fiscal 2007 from fiscal 2006, and an increase of $4.4 million in fiscal 2006 from fiscal 2005. The decrease in interest income in fiscal 2007 from fiscal 2006 was due primarily to a decrease in funds available for investment as a result of our retiring $200 million in convertible subordinated notes. The increase in interest income in fiscal 2006 from fiscal 2005 was due primarily to an increase in average interest rates.

Interest Expense

Interest expense was $3.1 million, $7.3 million and $7.0 million in fiscal 2007, fiscal 2006 and fiscal 2005, respectively. Interest expense in each of the fiscal years presented is primarily attributable to the $200 million of convertible subordinated notes. The notes matured and were fully paid in December 2006. Interest on the notes was payable semi-annually at 3.5% per annum.

Other Income (Expense), net

Other income (expense) net, was expense of $0.9 million in fiscal 2007, expense of $2.3 million in fiscal 2006 and income of $2.1 million in fiscal 2005. Other expense in fiscal 2007 was primarily comprised of amortization of costs associated with the $200 million convertible subordinated notes of $0.7 million and foreign currency losses of $0.2 million.

Other expense in fiscal 2006 was primarily comprised of amortization of costs associated with the $200 million convertible subordinated notes of $1.4 million and foreign currency losses of $0.9 million.

Other income in fiscal 2005 includes income of $3.9 million from the relief of a foreign consumption tax obligation, expense of $1.3 million for amortization of the costs associated with the convertible subordinated notes, and $0.7 million of foreign exchange losses due primarily to the decline in the U.S. dollar relative to the Yen and the Euro. The tax holiday that generated the foreign consumption tax relief expired in fiscal 2005, and no further benefits are expected.

Provision (Benefit) for Income Taxes

The provisions for income taxes of $2.1 million for fiscal 2007 were recorded for taxes due on income generated in certain states and foreign tax jurisdictions. The effective tax rate in fiscal 2007 was negative 17.7% which differs from the statutory tax rate of 35% due primarily to the tax impact of income from foreign operations. As of July 1, 2007, we had net operating loss carryforwards for federal and state tax purposes of $268.5 million and $45.6 million, respectively, of which $53.1 million and $21.3 million, respectively, represent deductions from share-based compensation for which a benefit would be recorded in additional paid-in capital when realized. We also had federal and state tax credit carryforwards of $10.8 million and $14.8 million, respectively, as of July 1, 2007. Federal net operating loss carryforwards of $268.5 million will start to expire beginning 2021 through 2027 and state net operating losses of $45.6 million will expire between 2011 through 2017, if not utilized. Federal tax credits of $10.4 million will expire beginning 2012 through 2027 and state tax credits of $1.4 million will expire beginning 2008 through 2013, if not utilized. Under FAS 123R, the deferred tax asset for net operating losses excludes deductions for excess tax benefits related to share-based compensation.

The provisions for income taxes of $1.8 million and $3.5 million for fiscal 2006 and fiscal 2005, respectively, were recorded for taxes due on income generated in certain states and foreign tax jurisdictions. The effective tax rate was 17.4% and 22.1% for fiscal 2006 and 2005, respectively, which differs from the statutory tax rate of 35% due primarily to benefits for U.S. taxes from net operating loss carryforwards and tax credits, offset by the tax impact of income from foreign operations.

Critical Accounting Policies and Estimates

Our significant accounting policies are more fully described in Note 2 of Notes to Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K. The preparation of consolidated financial statements in accordance with generally accepted accounting principles requires management to make estimates, assumptions and judgments that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenue and expenses during the period reported. By their nature, these estimates, assumptions and judgments are subject to an inherent degree of uncertainty. We base our estimates, assumptions and judgments on historical experience, market trends and other factors that are believed to be reasonable under the circumstances. Estimates, assumptions and judgments are reviewed on an ongoing basis and the effects of revisions are reflected in the consolidated financial statements in the period they are determined to be necessary. Actual results may differ from these estimates under different assumptions or conditions. Our significant accounting policies have been discussed with the Audit Committee of the Board of Directors. We believe the critical accounting policies stated below, among others, affect our more significant judgments and estimates used in the preparation of our consolidated financial statements. We believe there have been no material changes to our critical accounting policies during the year ended July 1, 2007 compared to the prior years.

Share-based Payments

On July 4, 2005, we adopted the fair value recognition provisions of Financial Accounting Standards Board ("FASB") Statement No. 123(R), *Share-Based Payment*, ("FAS 123R"). Prior to July 4, 2005, we accounted for share-based payments under the recognition and measurement provisions of APB Opinion No. 25, *Accounting for Stock Issued to Employees* ("APB 25"), and related Interpretations, as permitted by FASB Statement No. 123, *Accounting for Share-based Compensation* ("FAS 123"). In accordance with APB 25 no compensation cost was required to be recognized for options granted that had an exercise price equal to the market value of the underlying common stock on the date of grant.

We adopted FAS 123R using the modified-prospective-transition method. Under that transition method, compensation cost recognized in the year ended July 2, 2006 includes: a) compensation cost for all share-based payments granted prior to, but not yet vested as of July 4, 2005, based on the grant-date fair value estimated in accordance with the original provisions of FAS 123, and b) compensation cost for all share-based payments granted subsequent to July 4, 2005, based on the grant-date fair value estimated in accordance with the provisions of FAS 123R. The results for the prior periods have not been restated.

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Share-based compensation recognized in the financial statements by line item caption is as follows (dollars in thousands):

	Year Ended July 1, 2007	Year Ended July 2, 2006	Year Ended July 3, 2005
Cost of product revenue	$ 771	$ 718	$ 65
Cost of service revenue	359	417	40
Sales and marketing	2,173	2,764	195
Research and development	1,834	1,993	438
General and administrative	1,046	1,103	(45)
Amortization of deferred stock compensation	—	—	69
Total share-based compensation expense	6,183	6,995	762
Share-based compensation cost capitalized in inventory	(1)	25	—
Total share-based compensation cost	$ 6,182	$ 7,020	$ 762

In accordance with FAS 123R, the fair value of each option award is estimated on the date of grant using the Black-Scholes-Merton option valuation model with the weighted average assumptions noted in the table in Note 7 of Notes to Consolidated Financial Statements. The expected term of options granted is derived from historical data on employee exercise and post-vesting employment termination behavior. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant. Expected volatility is based on both the implied volatilities from traded options on our stock and historical volatility on our stock.

For options granted prior to July 4, 2005, and valued (on a pro forma basis) in accordance with FAS 123, the expected volatility used to estimate the fair value of the options was based solely on the historical volatility on our stock; we used the graded vesting method for expense attribution, and we recognized option forfeitures as they occurred as allowed by FAS 123.

For options granted after July 4, 2005, and valued in accordance with FAS 123R, the expected volatility used to estimate the fair value of the options was based on a combination of the historical volatility on our stock and the implied volatility; we used the straight-line method for expense attribution and we estimate forfeitures and only recognize expense for those shares expected to vest. Our estimated forfeiture rate in fiscal 2007, based on our historical forfeiture experience, is approximately 9%. We modified our estimated forfeiture rate in the fourth quarter of fiscal 2007 and recognized the cumulative effect of the change, as an increase in compensation expense, in that quarter of approximately $0.1 million.

The Black-Scholes-Merton option valuation model requires the input of highly subjective assumptions, including the expected life of the share-based award and stock price volatility. The assumptions used in calculating the fair value of share-based compensation represent management's best estimates, but these estimates involve inherent uncertainties and the application of management judgment. As a result, if other assumptions had been used, our share-based compensation expense could have been materially different. In addition, we are required to estimate the expected forfeiture rate and only recognize expense for those shares expected to vest. If our actual forfeiture rate is materially different from our estimate, the share-based compensation expense could be materially different.

In the fourth quarter of fiscal 2005, the compensation committee of the Board of Directors approved the acceleration of vesting of certain unvested stock options with exercise prices equal to or greater than $7.00 per share previously awarded to employees, including executive officers, and directors. Options to purchase approximately 4,544,000 shares of common stock were subject to acceleration. In accordance with APB 25, no compensation expense was required to be recorded in our consolidated statement of operations in fiscal 2005 in connection with the acceleration of the vesting of these options, as the exercise price of the employee stock options was higher than the market price of our stock on the date of the modification of the options. We believe that such options had limited economic value and were not offering sufficient incentive to the employees when compared to the potential future expense of approximately $11.4 million that would have been required to be recorded in future periods under FAS 123R had the options not been accelerated.

Revenue Recognition

We derive the majority of our revenue from sales of our modular and stackable networking equipment, with the remaining revenue generated from service fees relating to the service contracts and training on our products. We generally recognize product revenue from our value-added resellers and end-user customers at the time of shipment, provided that persuasive evidence of an arrangement exists, delivery has occurred, the price of the product is fixed or determinable and collection of the sales proceeds is reasonably assured. In instances where the criteria for revenue recognition are not met, revenue is deferred until all criteria have been met. Our total deferred product revenue was $0.6 million and $2.5 million as of July 1, 2007 and July 2, 2006, respectively. Revenue from service obligations under service contracts is deferred and recognized on a straight-line basis over the contractual service period. Our total deferred revenue for services, primarily from service contracts, was $40.8 million and $41.7 million as of July 1, 2007 and July 2, 2006, respectively. Service contracts typically range from one to five years.

When sales arrangements contain multiple deliverables, such as hardware, service contracts and other services, we determine whether the deliverables represent separate units of accounting and then allocate revenue to each unit of accounting based on their relative fair values. We recognize revenue for each unit of accounting when the revenue recognition criteria for each unit of accounting are met. The amount of product revenue recognized is impacted by our judgments as to whether an arrangement includes multiple units of accounting and if so, whether fair value exists for those units of accounting. The ability to establish fair value for any unit of accounting could affect the timing of the revenue recognition.

We make certain sales to partners in two distribution channels, or tiers. The first tier consists of a limited number of independent distributors that sell primarily to resellers and, on occasion, to end-user customers. We defer recognition of revenue on all sales to these distributors until the distributors sell the product, as evidenced by monthly “sales-out” reports that the distributors provide to us. We grant these distributors the right to return a portion of unsold inventory to us for the purpose of stock rotation. We also grant these distributors certain price protection rights. The distributor-related deferred revenue and receivables are adjusted at the time of the stock rotation return or price reduction. We also provide distributors with credits for changes in selling prices, and allow them to participate in cooperative marketing programs. We maintain estimated accruals and allowances for these exposures based upon our historical experience. If actual credits to distributors for changes in selling prices and cooperative marketing programs were to deviate significantly from our estimates, which are based on contractual arrangements and historical experience, our future revenue could be adversely affected.

The second tier of the distribution channel consists of a large number of third-party value-added resellers that sell directly to end-users and are generally not granted return privileges, except for defective products during the warranty period. We reduce product revenue for certain price protection rights that may occur under contractual arrangements we have with our resellers.

We provide an allowance for sales returns based on our historical returns, analysis of credit memo data and our return policies. The allowance for sales returns was $2.1 million and $1.7 million as of July 1, 2007 and July 2, 2006, respectively, for estimated future returns that were recorded as a reduction of our accounts receivable. The provision for returns is charged to net revenues in the accompanying consolidated statements of operations, and was $3.2 million in fiscal 2007, $0.7 million in fiscal 2006 and $1.0 million in fiscal 2005. If the historical data we use to calculate the estimated sales returns and allowances does not properly reflect future levels of product returns, these estimates will be revised, thus resulting in an impact on future net revenues. We estimate and adjust this allowance at each balance sheet date.

Inventory Valuation

Our inventory balance was $25.3 million as of July 1, 2007, compared with $19.3 million as of July 2, 2006. We value our inventory at lower of cost (determined on a first-in, first-out basis) or replacement cost. The networking industry is characterized by rapid technological change, frequent new product introductions, changes in customer requirements and evolving industry standards. We perform a detailed assessment of inventory at each balance sheet date, which includes a review of, among other factors, demand requirements, product lifecycle and product development plans and quality issues. Based on this analysis, we record adjustments, when appropriate, to reflect inventory at net realizable value. Inventory write-downs charged to cost of product revenue were $3.0 million in fiscal 2007, $1.3 million in fiscal 2006 and $1.1 million in fiscal 2005. Although we make every effort to ensure the accuracy of our forecasts of product demand, any significant unanticipated changes in demand or technological developments would significantly impact the value of our inventory and our reported operating results. In the future, if we find that our estimates are too optimistic and we determine that our inventory needs to be written down, we will be required to recognize such costs in our cost of product revenue at the time of such determination. Conversely, if we find our estimates are too pessimistic and we subsequently sell product that has previously been written down, our operating margin in that period will be favorably impacted.

Accrued Warranty

Networking products may contain undetected hardware or software errors when new products or new versions or updates of existing products are released to the marketplace. We have experienced such errors in connection with products and product updates. Our standard hardware warranty period is typically 12 months from the date of shipment to end-users and 90 days for software. Upon shipment of products to our customers, including both end-users and channel partners, we estimate expenses for the cost to repair or replace products that may be returned under warranty and accrue a liability through charges to cost of product revenue for this amount.

Our accrued warranty balance was $7.2 million as of July 1, 2007, compared with $7.0 million as of July 2, 2006. The determination of our warranty requirements is based on our actual historical experience with the product or product family, estimates of repair and replacement costs and any product warranty problems that are identified after shipment. We estimate and adjust this accrual at each balance sheet date in accordance with changes in these factors. The cost of new warranties issued that was charged to cost of product revenue was $8.8 million in fiscal 2007, $10.2 million in fiscal 2006 and $12.3 million in fiscal 2005. While we believe that our warranty accrual is adequate and that the judgments applied in calculating this accrual are appropriate, the assumptions used are based on estimates and these estimated amounts could differ materially from our actual warranty expenses in the future. In fiscal 2005, we recognized $1.1 million in additional warranty expense due to a change in the method we use to accumulate the warranty return rates. If actual expenses exceed those we have estimated, our future cost of product revenue would be adversely affected.

Accounts Receivable and Allowance for Doubtful Accounts

Our accounts receivable balance, net of allowance for doubtful accounts, was $23.1 million and $27.7 million as of July 1, 2007 and July 2, 2006, respectively. The allowance for doubtful accounts for trade accounts receivable as of July 1, 2007 was $0.7 million, compared with $0.7 million as of July 2, 2006. The distributor accounts receivable balance, net of allowance for doubtful accounts, recorded in prepaid expenses and other current assets, was $23.3 million and $17.2 million as of July 1, 2007 and July 2, 2006, respectively. The allowance for doubtful distributor accounts, also recorded in prepaid expenses and other current assets, as of July 1, 2007 was $0.2 million, compared with $0.3 million as of July 2, 2006. We continually monitor and evaluate the collectibility of our trade receivables based on a combination of factors. We record specific allowances for bad debts in general and administrative expense when we become aware of a specific customer's inability to meet its financial obligation to us, such as in the case of bankruptcy filings or deterioration of financial position. Estimates are used in determining our allowances for all other customers based on factors such as current trends in the length of time the receivables are past due and historical collection experience. We mitigate some collection risk by requiring most of our customers in the Asia-Pacific region, excluding Japan and Australia, to pay cash in advance or secure letters of credit when placing an order with us. Our provision for doubtful accounts was an expense of $0.1 million in fiscal 2007, expense of $1.2 million in fiscal 2006 and an expense of $0.4 million in fiscal 2005. If a major customer's creditworthiness deteriorates, or if actual defaults are higher than our historical experience, or if other circumstances arise, our estimates of the recoverability of amounts due to us could be overstated, and additional allowances could be required. We write-off receivables to the allowance after all collection efforts are exhausted. In the fourth quarter of fiscal 2005, one large distributor in Europe became delinquent in its payments to us due to cash flow problems and difficulty in obtaining financing. We increased our allowance for doubtful accounts to cover a higher percentage of this customer's outstanding balance in fiscal 2005 and ultimately wrote off $1.8 million in receivables in fiscal 2006.

Deferred Tax Asset Valuation Allowance

We recognize deferred tax assets and liabilities based on the differences between the financial statement carrying amounts and the tax bases of assets and liabilities. Significant management judgment is required in determining our valuation allowance recorded against our net deferred tax assets. We make an assessment of the likelihood that our net deferred tax assets will be recovered from future taxable income, and to the extent that recovery is not believed to be likely, a valuation allowance is established. We provided a full valuation allowance against all of our U.S. federal and state net deferred tax assets in fiscal 2003 in the amount of $194.8 million in accordance with the provisions of SFAS No. 109, *Accounting for Income Taxes*. In fiscal 2007, the valuation allowance increased by $8.0 million to $166.6 million, and in fiscal 2006, the valuation allowance decreased by $17.2 million to $158.6 million.

The valuation allowance is determined in accordance with the provisions of SFAS 109, which requires an assessment of both negative and positive evidence when measuring the need for a valuation allowance. In accordance with SFAS 109, evidence, such as operating results during the most recent three-year period at the time the charge was incurred, was given more weight than our expectations of future profitability, which is inherently uncertain. Our losses during those periods represented sufficient negative evidence to require a full valuation allowance against our net deferred tax assets under SFAS 109. This valuation allowance will be evaluated periodically and can be reversed partially or totally if business results have sufficiently improved to support realization of our deferred tax assets.

Legal Contingencies

We are currently involved in various claims and legal proceedings, including negotiations regarding potential licenses from third parties who have notified us that they believe our products may infringe certain patents. Periodically, we review the status of each significant matter, whether litigation or licensing negotiation, and assess our potential financial exposure. If the potential loss from any claim or legal proceeding is considered probable and the amount can be estimated, we accrue a liability for the estimated loss. Because of uncertainties related to these matters, accruals, if any, are based only on the most current and dependable information available at any given time. As additional information becomes available, we may reassess the potential liability from pending claims and litigation and the probability of claims being successfully asserted against us. As a result, we may revise our estimates related to these pending claims and litigation. Such revisions in the estimates of the potential liabilities could have a material impact on our consolidated results of operations, financial position and cash flows in the future. For further detail, see Note 4 of Notes to Consolidated Financial Statements for a description of legal proceedings.

Liquidity and Capital Resources

Cash and cash equivalents, short-term investments and marketable securities were $215.9 million and $433.1 million at July 1, 2007 and July 2, 2006, respectively, representing a decrease of $217.2 million. This decrease was primarily due to cash used to repay the principal payment of convertible subordinated notes of $200.0 million, repurchase treasury stock of $14.6 million and capital expenditures of $4.6 million, and cash used in operating activities of $0.3 million, partially offset by proceeds from issuance of common stock of $0.5 million and a decrease in the unrealized loss on investments of $1.7 million.

Cash used in operating activities was $0.3 million in fiscal 2007, a decline of $28.3 million compared to cash from operations of $28.0 million in fiscal 2006. The decline in cash from operating activities was primarily due to net loss in fiscal 2007 of $14.2 million, which included significant non-cash charges, including depreciation and amortization of $7.9 million, share-based compensation expense of $6.2 million, and amortization expense related to the warrant issued to Avaya of $4.0 million. Accounts receivable, net, decreased to $23.1 million at July 1, 2007 from $27.7 million at July 2, 2006. Days sales outstanding in receivables decreased to 24 days at July 1, 2007 from 30 days at July 2, 2006. The decrease in accounts receivable and decrease in days sales outstanding were primarily due to improved collection efforts. Inventories increased to $25.3 million at July 1, 2007 from $19.3 million at July 2, 2006. Inventory management remains an area of focus as we balance the need to maintain strategic inventory levels to ensure competitive lead times and avoid stock-outs with the risk of inventory excess or obsolescence because of declining demand, rapidly changing technology, environmental regulations and customer requirements. Deferred revenue decreased to $42.4 million at July 1, 2007 from $45.1 million at July 2, 2006. This decrease was due primarily to lower service contracts booked as a result of lower product sales.

We have a revolving line of credit for $10.0 million with a major lending institution. As of July 1, 2007, there were no outstanding borrowings under this facility. The line of credit contains a provision for the issuance of letters of credit not to exceed the unused balance of the line. At July 1, 2007, we had letters of credit totaling $0.7 million. These letters of credit were primarily issued to satisfy requirements of certain of our customers for performance bonds. The line of credit requires us to maintain specified financial covenants related to tangible net worth and liquidity with which we were in compliance as of July 1, 2007. The line of credit was renewed on January 24, 2007 and expires on January 24, 2008. It is our intention to renew this line of credit when it expires.

In December 2001, we completed a private placement of $200.0 million of convertible subordinated notes. The notes matured on December 1, 2006. Interest was payable semi-annually at 3.5% per annum. The notes were paid off on their maturity date of December 1, 2006.

On October 20, 2005, our Board of Directors authorized the repurchase of up to $50 million of our common stock. In fiscal 2007, we repurchased approximately 3.9 million shares for approximately $14.6 million bringing the cumulative total to 11.1 million repurchased shares for approximately $48.3 million. In fiscal 2006, we repurchased approximately 7.1 million shares for approximately $33.7 million. The repurchases were made in compliance with the Securities and Exchange Commission's Rule 10b-18, and were subject to market conditions as well as applicable legal and other considerations. In October 2006, the Board of Directors terminated the share repurchase program.

We own our corporate headquarters in Santa Clara, California. The campus is located on approximately 16 acres of property in an area that may ultimately be suitable for residential development.

The following summarizes our contractual obligations (including interest payments) at July 1, 2007, and the effect such obligations are expected to have on our liquidity and cash flow in future periods (in thousands):

	Total	Less Than 1 Year	1–3 Years	3–5 Years	More Than 5 Years
Contractual Obligations:					
Non-cancelable inventory purchase commitments	$27,287	$27,287	—	—	—
Non-cancelable operating lease obligations	21,340	7,044	9,969	4,327	—
Other non-cancelable purchase commitments	3,900	1,650	1,500	750	—
Total contractual cash obligations	$52,527	$35,981	$11,469	$5,077	—

We did not have any material commitments for capital expenditures as of July 1, 2007. Other non-cancelable purchase commitments represent OEM and technology agreements. We did not have any off-balance sheet arrangements as of July 1, 2007.

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

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

New Accounting Pronouncements

Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements

In September 2006, the SEC issued Staff Accounting Bulletin No. 108, “Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements” (“SAB 108”). SAB 108 provides interpretative guidance on the process of quantifying financial statement misstatements and is effective for fiscal years ending after November 15, 2006. The adoption of SAB 108 did not have a material impact on our consolidated financial statements.

Accounting for Consideration Given by a Service Provider to a Manufacturer or Reseller of Equipment Necessary for an End-Customer to Receive Service from the Service Provider

In September 2006, the FASB issued Emerging Issues Task Force Issue, or EITF, No. 06-1, *Accounting for Consideration Given by a Service Provider to a Manufacturer or Reseller of Equipment Necessary for an End-Customer to Receive Service from the Service Provider.* EITF No. 06-1 requires companies to provide disclosures regarding the nature of arrangements in which they provide consideration to manufacturers or resellers of equipment necessary for an end-customer to receive service from them, including the amounts recognized in the Consolidated Statements of Operations. EITF 06-1 is effective for fiscal years beginning after June 15, 2007. We do not expect the adoption of EITF No. 06-1 to have a material impact on our consolidated financial statements.

Fair Value Measurements

In September 2006, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 157, *Fair Value Measurements*. SFAS 157 replaces the different definitions of fair value in the accounting literature with a single definition. It defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. SFAS 157 is effective for fair-value measurements already required or permitted by other standards for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. We are currently in the process of determining the impact of adopting the provisions of SFAS 157 on our financial position, results of operations and cash flows.

Fair Value Option for Financial Assets and Liabilities

In February 2007, the FASB issued Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of FASB Statement No. 115* (FAS 159). FAS 159 permits companies to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value and establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities. The provisions of FAS 159 become effective for fiscal years beginning after November 15, 2007. We believe that the adoption of SFAS 159 will not have a material effect on our financial statements.

Accounting for Income Taxes

In July 2006, the Financial Accounting Standards Board (FASB) released its final Interpretation on uncertain tax positions, FIN 48, *Accounting for Uncertainty in Income Taxes—an interpretation of FAS 109.* This Interpretation clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, *Accounting for Income Taxes.* This Interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. The guidance will become effective as of the beginning of a company's fiscal year beginning after December 15, 2006. The Company is currently assessing the impact of adopting this standard.

Item 7A. *Quantitative and Qualitative Disclosures About Market Risk*

Interest Rate Sensitivity

The primary objective of our investment activities is to preserve principal while at the same time maximize the income we receive from our investments without significantly increasing risk. Some of the securities that we have invested in may be subject to market risk. This means that a change in prevailing interest rates may cause the principal amount of the investment to fluctuate. For example, if we hold a security that was issued with a fixed interest rate at the then-prevailing rate and the prevailing interest rate later rises, the principal amount of our investment will probably decline. To minimize this risk, we maintain our portfolio of cash equivalents and short-term investments in a variety of securities, including commercial paper, other non-government debt securities and money market funds. In general, money market funds are not subject to market risk because the interest paid on such funds fluctuates with the prevailing interest rate. The following table presents the amounts of our cash equivalents, short-term investments, marketable securities and long-term debt that are subject to market risk by range of expected maturity and weighted-average interest rates as of July 1, 2007 and July 2, 2006. This table does not include money market funds because those funds are generally not subject to market risk.

	Maturing in				
	Three months or less	Three months to one year	Greater than one year	Total	Fair Value
			(In thousands)		
July 1, 2007:					
Included in cash and cash equivalents	$ 31,091			$ 31,091	$ 31,091
Weighted average interest rate	5.29%				
Included in short-term investments	$ 30,486	$ 61,113		$ 91,599	$ 91,599
Weighted average interest rate	5.32%	4.38%			
Included in marketable securities			$52,683	$ 52,683	$ 52,683
Weighted average interest rate			5.18%		

	Maturing in				
	Three months or less	Three months to one year	Greater than one year	Total	Fair Value
			(In thousands)		
July 2, 2006:					
Included in cash and cash equivalents	$ 31,830			$ 31,830	$ 31,830
Weighted average interest rate	4.76%				
Included in short-term investments	$196,940	$100,786		$297,726	$297,726
Weighted average interest rate	4.41%	3.43%			
Included in marketable securities			$42,781	$ 42,781	$ 42,781
Weighted average interest rate			3.99%		
Long-term debt		$200,000		$200,000	$197,750
Weighted average interest rate		3.50%			

Exchange Rate Sensitivity

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

Foreign Exchange Forward Contracts

We enter into foreign exchange forward contracts to hedge foreign currency forecasted transactions related to certain operating expenses, denominated in Japanese Yen, the Euro, the Swedish Krona and the British Pound. These derivatives are designated as cash flow hedges under SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities, as amended and interpreted* ("SFAS 133"). At July 1, 2007, these forward foreign currency contracts had a notional principal amount and fair value of $5.5 million. These contracts have maturities of less than 60 days.

Additionally, we enter into foreign exchange forward contracts to mitigate the effect of gains and losses generated by the remeasurement of certain assets and liabilities denominated in Japanese Yen, the Euro, the Swedish Krona and the British Pound. These derivatives are not designated as hedges under SFAS 133. At July 1, 2007, we held foreign currency forward contracts with a notional principal amount and fair value of $8.6 million. These contracts have maturities of less than 45 days. Changes in the fair value of these foreign exchange forward contracts are offset largely by remeasurement of the underlying assets and liabilities.

We do not enter into foreign exchange forward contracts for speculative or trading purposes. Foreign currency transaction gains and losses from operations, including the impact of hedging, were a loss of $0.2 million in fiscal 2007, a loss of $0.9 million in fiscal 2006 and a loss of $0.6 million in fiscal 2005.

Item 8. *Financial Statements and Supplementary Data*

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS OF EXTREME NETWORKS, INC.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Extreme Networks, Inc.

We have audited the accompanying consolidated balance sheets of Extreme Networks, Inc. as of July 1, 2007 and July 2, 2006 and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the three years in the period ended July 1, 2007. Our audits also included the financial statement schedule listed in the Index at Item 15(a). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Extreme Networks, Inc. at July 1, 2007 and July 2, 2006, and the consolidated results of its operations and its cash flows for each of the three years in the period ended July 1, 2007, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

As discussed in Note 8 to the consolidated financial statements, in fiscal 2006 the Company adopted the fair value recognition provisions of Statement of Financial Accounting Standards No. 123(R), "*Share-Based Payment*," using the modified-prospective-transition method.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Extreme Networks, Inc.'s internal control over financial reporting as of July 1, 2007, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated August 28, 2007 expressed an unqualified opinion on internal control over financial reporting.

Ernst & Young LLP

Palo Alto, California
August 28, 2007

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EXTREME NETWORKS, INC.

CONSOLIDATED BALANCE SHEETS
(In thousands, except par value and share amounts)

	July 1, 2007	July 2, 2006
ASSETS		
Current assets:		
Cash and cash equivalents	$ 71,573	$ 92,598
Short-term investments	91,599	297,726
Accounts receivable, net of allowances of $2,863 at July 1, 2007 ($2,387 at July 2, 2006)	23,066	27,681
Inventories, net	25,261	19,303
Deferred income taxes	1,118	500
Prepaid expenses and other current assets, net	13,339	8,920
Total current assets	225,956	446,728
Property and equipment, net	43,156	46,499
Marketable securities	52,683	42,781
Other assets, net	20,102	22,710
Total assets	$ 341,897	$ 558,718
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 21,303	$ 20,138
Accrued compensation and benefits	14,841	11,758
Restructuring liabilities	5,532	5,571
Accrued warranty	7,182	7,027
Deferred revenue	32,160	35,406
Convertible subordinated notes	—	200,000
Other accrued liabilities	23,263	19,581
Total current liabilities	104,281	299,481
Restructuring liabilities, less current portion	8,456	11,471
Deferred revenue, less current portion	10,286	9,699
Deferred income taxes	688	579
Other long-term liabilities	1,961	1,307
Commitments and contingencies (Note 4)		
Stockholders' equity:		
Convertible preferred stock, $.001 par value, issuable in series, 2,000,000 shares authorized; none issued	—	—
Common stock, $.001 par value, 750,000,000 shares authorized; 125,105,000 issued and outstanding at July 1, 2007 (124,469,000 July 2, 2006) and capital in excess of par value	934,540	927,835
Treasury stock, 11,053,877 shares at July 1, 2007	(48,303)	(33,700)
Accumulated other comprehensive income (loss)	572	(1,567)
Accumulated deficit	(670,584)	(656,387)
Total stockholders' equity	216,225	236,181
Total liabilities and stockholders' equity	$ 341,897	$ 558,718

See accompanying notes to consolidated financial statements.

EXTREME NETWORKS, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share amounts)

	Year Ended		
	July 1, 2007	July 2, 2006	July 3, 2005
Net revenues:			
Product	$280,497	$294,824	$324,256
Service	62,337	63,777	59,091
Total net revenues	342,834	358,601	383,347
Cost of revenues:			
Product(1)	124,298	130,557	146,509
Service(1)	33,341	34,168	34,259
Total cost of revenues	157,639	164,725	180,768
Gross margin:			
Product	156,199	164,267	177,747
Service	28,996	29,609	24,832
Total gross margin	185,195	193,876	202,579
Operating expenses:			
Sales and marketing(1)	102,052	98,452	96,951
Research and development(1)	67,085	61,966	61,516
General and administrative(1)	33,638	25,498	31,709
Technology agreement	—	—	2,000
Amortization of deferred stock compensation(1)	—	—	69
Restructuring charge	4,003	3,268	—
Total operating expenses	206,778	189,184	192,245
Operating income (loss)	(21,583)	4,692	10,334
Interest income	13,551	15,136	10,713
Interest expense	(3,149)	(7,252)	(7,037)
Other income (expense), net	(876)	(2,269)	2,052
Income before income taxes	(12,057)	10,307	16,062
Provision for income taxes	2,140	1,798	3,543
Net Income (loss)	$ (14,197)	$ 8,509	$ 12,519
Basicand diluted net loss per share:			
Net income (loss) per share – basic	$(0.12)	$0.07	$0.10
Net income (loss) per share – diluted	$(0.12)	$0.07	$0.10
Sharesused in per share calculation – basic	114,122	121,286	121,225
Sharesused in per share calculation – diluted	114,122	123,049	124,166

(1) Includes stock-based compensation expense as follows:

Cost of product revenue	$ 771	$ 718	$ 65
Cost of service revenue	359	417	40
Sales and marketing	2,173	2,764	195
Research and development	1,834	1,993	438
General and administrative	1,046	1,103	(45)
Amortization of deferred stock compensation	—	—	69
Total stock-based compensation expense	$ 6,183	$ 6,995	$ 762

See accompanying notes to consolidated financial statements.

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EXTREME NETWORKS, INC.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(In thousands)

	Common Stock and capital in excess of par value		Treasury Stock		Deferred Stock Compensation	Accumulated Other Comprehensive Income (Loss)	Accumulated Deficit	Total Stockholders' Equity
	Shares	Amount	Shares	Amount				
Balances at June 27, 2004	**120,423**	**$910,546**	**—**	**$ —**	**$ (1,185)**	**$ (2,388)**	**$ (677,415)**	**$ 229,558**
Components of comprehensive income:								
Net income	—	—	—	—	—	—	12,519	12,519
Change in unrealized loss on investments, net of tax expense of $156	—	—	—	—	—	(540)	—	(540)
Change in unrealized gain on derivatives	—	—	—	—	—	12	—	12
Foreign currency translation adjustment	—	—	—	—	—	29	—	29
Total comprehensive income								12,020
Exercise of options to purchase common stock, net of repurchases	542	1,799	—	—	—	—	—	1,799
Issuance of common stock under employee stock purchase plan	943	4,143	—	—	—	—	—	4,143
Stock-based compensation expense	—	(543)	—	—	966	—	—	423
Amortization of deferred stock compensation	—	—	—	—	69	—	—	69
Balances at July 3, 2005	**121,908**	**915,945**	**—**	**—**	**(150)**	**(2,887)**	**(664,896)**	**248,012**
Components of comprehensive income:								
Net income	—	—	—	—	—	—	8,509	8,509
Change in unrealized gain on investments, net of tax expense of $0	—	—	—	—	—	1,313	—	1,313
Change in unrealized gain on derivatives	—	—	—	—	—	(10)	—	(10)
Foreign currency translation adjustment	—	—	—	—	—	17	—	17
Total comprehensive income								9,829
Exercise of options to purchase common stock, net of repurchases	795	1,566	—	—	—	—	—	1,566
Issuance of common stock under employee stock purchase plan	907	3,445	—	—	—	—	—	3,445
Exercise of warrant by Avaya	859	9	—	—	—	—	—	9
Share-based payments, net of repurchases	—	7,020	—	—	—	—	—	7,020
Repurchase of common stock	—	—	(7,136)	(33,700)	—	—	—	(33,700)
Amortization of deferred stock compensation	—	(150)	—	—	150	—	—	—
Balances at July 2, 2006	**124,469**	**927,835**	**(7,136)**	**(33,700)**	**—**	**(1,567)**	**(656,387)**	**236,181**
Components of comprehensive income:								
Net loss	—	—	—	—	—	—	(14,197)	(14,197)
Change in unrealized gain on investments, net of tax expense of $0	—	—	—	—	—	1,737	—	1,737
Change in unrealized loss on derivatives	—	—	—	—	—	(2)	—	(2)
Foreign currency translation adjustment	—	—	—	—	—	404	—	404
Total comprehensive loss								(12,058)
Exercise of options to purchase common stock, net of repurchases	419	(180)	—	—	—	—	—	(180)
Issuance of common stock under employee stock purchase plan	217	702	—	—	—	—	—	702
Share-based payments, net of repurchases	—	6,183	—	—	—	—	—	6,183
Repurchase of common stock	—	—	(3,918)	(14,603)	—	—	—	(14,603)
Balances at July 1, 2007	**125,105**	**$934,540**	**(11,054)**	**$(48,303)**	**$ —**	**$ 572**	**$ (670,584)**	**$ 216,225**

See accompanying notes to consolidated financial statements.

EXTREME NETWORKS, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Year Ended		
	July 1, 2007	July 2, 2006	July 3, 2005
Cash flows from operating activities:			
Net income (loss)	$ (14,197)	$ 8,509	$ 12,519
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Depreciation and amortization	7,926	11,899	16,244
Provision for doubtful accounts	—	1,166	380
Provision for excess and obsolete inventory	3,030	1,259	1,061
Deferred income taxes	64	(249)	451
Amortization of warrant	4,048	4,691	7,566
Restructuring charge	4,003	3,268	—
Amortization of deferred stock compensation	—	—	492
Loss on disposal of assets	54	9	212
Stock-based compensation	6,183	6,995	—
Changes in operating assets and liabilities, net			
Accounts receivable	4,541	3,306	2,271
Inventories	(8,990)	5,405	(1,114)
Prepaid expenses and other assets	(6,358)	(2,075)	(9,558)
Accounts payable	1,165	1,855	(712)
Accrued compensation and benefits	3,083	(2,274)	(1,795)
Restructuring liabilities	(7,057)	(6,182)	(6,607)
Lease liability	—	(471)	(1,884)
Accrued warranty	155	(444)	(825)
Deferred revenue	(2,659)	(5,368)	(3,201)
Other accrued liabilities	4,084	(2,304)	(987)
Other long-term liabilities	655	(958)	1,945
Net cash provided by (used in) operating activities	(270)	28,037	16,458
Cash flows from investing activities:			
Capital expenditures	(4,637)	(7,969)	(7,127)
Purchases of investments	(210,711)	(273,986)	(297,051)
Proceeds from sales and maturities of investments and marketable securities	408,673	247,726	350,084
Net cash provided by (used in) investing activities	193,325	(34,229)	45,906
Cash flows from financing activities:			
Proceeds from issuance of common stock, net of repurchases	523	5,020	5,942
Repurchase of common stock	(14,603)	(33,700)	—
Principal payment on convertible debt	(200,000)	—	—
Net cash provided by (used in) financing activities	(214,080)	(28,680)	5,942
Net increase (decrease) in cash and cash equivalents	(21,025)	(34,872)	68,306
Cash and cash equivalents at beginning of year	92,598	127,470	59,164
Cash and cash equivalents at end of year	$ 71,573	$ 92,598	$ 127,470
Supplemental disclosure of cash flow information:			
Interest paid	$ 3,500	$ 7,000	$ 7,037
Cash paid for income taxes	$ 5,285	$ 587	$ 1,819

See accompanying notes to consolidated financial statements.

EXTREME NETWORKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Description of Business

Extreme Networks, Inc. (“Extreme Networks”, the “Company”, “we” or “our”) is a leading provider of network infrastructure equipment and markets its products primarily to business, governmental, health care, service provider, and educational customers with a focus on large corporate enterprises and metropolitan service providers on a global basis. We conduct our sales and marketing activities on a worldwide basis through a two-tier distribution channel utilizing distributors, resellers and our field sales organization. Extreme Networks was incorporated in California in 1996 and reincorporated in Delaware in 1999.

2. Basis of Presentation and Summary of Significant Accounting Policies

Fiscal Year

Our fiscal year is a 52/53-week fiscal accounting year that closes on the Sunday closest to June 30th every year. Fiscal 2007 and fiscal 2006 were 52-week fiscal years; fiscal 2005 was a 53-week fiscal year. All references herein to “fiscal 2007” or “2007” represent the fiscal year ended July 1, 2007.

Principles of Consolidation

The consolidated financial statements include the accounts of Extreme Networks and its wholly-owned subsidiaries. All inter-company accounts and transactions have been eliminated. Investments in which management intends to maintain more than a temporary 20% to 50% interest, or otherwise has the ability to exercise significant influence, are accounted for under the equity method. Investments in which management has less than a 20% interest and does not have the ability to exercise significant influence are carried at the lower of cost or estimated realizable value.

We use the U.S. dollar predominately as our functional currency. The functional currency for certain of our foreign subsidiaries is the local currency based on the criteria of SFAS No. 52, *Foreign Currency Translation*. For those subsidiaries that operate in a local currency functional environment, all monetary assets and liabilities are translated to United States dollars at current rates of exchange; non-monetary assets and liabilities are translated at historical rates of exchange; and revenues and expenses are translated using average rates. Gains and losses from foreign currency translation are included as a separate component of other comprehensive income (loss). Foreign currency transaction losses from operations, including the impact of hedging, were $0.2 million in fiscal 2007, $0.9 million in fiscal 2006 and $0.6 million in fiscal 2005.

Accounting Estimates

The preparation of financial statements and related disclosures in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Estimates are used for, but are not limited to, the accounting for the allowances for doubtful accounts and sales returns, inventory valuation, depreciation and amortization, impairment of long-lived assets, warranty accruals, restructuring liabilities, measurement of share-based compensation costs and income taxes. Actual results could differ materially from these estimates.

Revenue Recognition

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

We make certain sales to partners in two distribution channels, or tiers. The first tier consists of a limited number of independent distributors that sell primarily to resellers and, on occasion, to end-user customers. We defer recognition of revenue on all sales to these distributors until the distributors sell the product, as evidenced by monthly “sales-out” reports that the distributors provide to us. We grant these distributors the right to return a portion of unsold inventory to us for the purpose of stock rotation. We also grant these distributors certain price protection rights. The distributor-related deferred revenue and receivables are adjusted at the time of the stock rotation return or price reduction. We also provide distributors with credits for changes in selling prices, and allow them to participate in cooperative marketing programs. Cooperative advertising expenses are recorded as marketing expenses to the extent that an advertising benefit separate from the revenue transaction can be identified and the cash paid does not exceed the fair value of that advertising benefit received. We maintain estimated accruals and allowances for these exposures based upon our historical experience. The second tier of the distribution channel consists of a large number of third-party resellers that sell directly to end-users and are not granted return privileges, except for defective products during the warranty period. We reduce product revenue for certain price protection rights that may occur under contractual arrangements we have with our resellers.

Cash Equivalents, Short-Term Investments and Marketable Securities

Highly liquid investment securities with insignificant interest rate risk and with original maturities of three months or less at date of purchase are classified as cash equivalents. Investment securities with original maturities greater than three months and remaining maturities of less than one year are classified as short-term investments. Investment securities with remaining maturities greater than one year are classified as marketable securities. Our investments are primarily comprised of United States and municipal government obligations and corporate securities.

To date, all marketable securities have been classified as available-for-sale and are carried at fair value, with unrealized gains and losses reported net-of-tax as a separate component of stockholders’ equity. Realized gains and losses on available-for-sale securities are recorded in interest income. Declines in value on available-for-sale securities judged to be other than temporary are recorded in other income (expense), net. None of our marketable securities are deemed impaired as of July 1, 2007, as substantially all of our investments are investment grade government and corporate debt securities that have maturities of less than 3 years, and we have both the ability and intent to hold the investments until maturity. The cost of securities sold is based on specific identification. Premiums and discounts are amortized over the period from acquisition to maturity and are included in investment income, along with interest and dividends.

EXTREME NETWORKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Fair Value of Financial Instruments

The carrying amounts and estimated fair values of our financial instruments were as follows (in thousands):

	July 1, 2007		July 2, 2006	
	Carrying amount	Fair value	Carrying amount	Fair value
Financial assets:				
Cash and cash equivalents	$71,573	$71,573	$ 92,598	$ 92,598
Short-term investments	$91,599	$91,599	$297,726	$297,726
Marketable securities	$52,683	$52,683	$ 42,781	$ 42,781
Financial liabilities:				
Convertible subordinated notes	$ —	$ —	$200,000	$197,750
Forward foreign currency contracts	$ (14)	$ (14)	$ (171)	$ (171)

The fair values of short-term investments and marketable securities are determined using quoted market prices for those securities or similar financial instruments. The fair value of the convertible subordinated notes paid off on December 1, 2006 was estimated using quoted market prices.

Concentrations

We may be subject to concentration of credit risk as a result of certain financial instruments consisting principally of marketable investments and accounts receivable. We have placed our investments with high-credit quality issuers. We do not invest an amount exceeding 10% of our combined cash, cash equivalents, short-term investments and marketable securities in the securities of any one obligor or maker, except for obligations of the United States government, obligations of United States government agencies and money market accounts.

We perform ongoing credit evaluations of our customers and generally do not require collateral in exchange for credit. We mitigate some collection risk by requiring most of our customers in the Asia-Pacific region, excluding Japan, to pay cash in advance or secure letters of credit when placing an order with us. One distributor, Tech Data, accounted for 12%, 12% and 11% of our net revenues in fiscal 2007, fiscal 2006 and fiscal 2005, respectively. No customer accounted for more than 10% of our accounts receivable balance at July 1, 2007, July 2, 2006 or July 3, 2005.

One supplier currently manufacturers all of our application specific integrated circuits, or ASICs, used in certain of our hardware products. Any interruption or delay in the supply of any of these or other single source components, or the inability to procure these components from alternate sources at acceptable prices and within a reasonable timeframe, would have a material adverse effect on our ability to meet customer orders, which would negatively impact our business, operating results and financial condition. In addition, qualifying additional suppliers can be time-consuming and expensive, and may increase the likelihood of design or production related errors. We attempt to mitigate these risks by working closely with our ASIC supplier regarding production planning and timing of new product introductions.

We currently derive substantially all of our revenue from sales of our Summit, BlackDiamond and Alpine products. We expect that revenue from these products will account for a substantial portion of our revenue for the foreseeable future. Accordingly, widespread market acceptance of these products is critical to our future success.

Accounts Receivable and Allowance for Doubtful Accounts

Accounts receivable are recorded at the invoiced amount and do not bear interest. Substantially all receivables were trade receivables as of July 1, 2007 and July 2, 2006.

EXTREME NETWORKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

We continually monitor and evaluate the collectibility of our trade receivables based on a combination of factors. We record specific allowances for bad debts in general and administrative expense when we become aware of a specific customer's inability to meet its financial obligation to us, such as in the case of bankruptcy filings or deterioration of financial position. We write-off receivables to the allowance after all collection efforts are exhausted. Estimates are used in determining our allowances for all other customers based on factors such as current trends in the length of time the receivables are past due and historical collection experience. We mitigate some collection risk by requiring most of our customers in the Asia-Pacific region, excluding Japan, to pay cash in advance or secure letters of credit when placing an order with us.

Inventories

Inventories consist of raw materials and finished goods and are stated at the lower of cost, determined on a first-in, first-out basis, or replacement cost. Inventories, net of write-downs for excess and obsolete inventory (which we determine primarily based on future demand forecasts) of $2,932 and $5,136 at July 1, 2007 and July 2, 2006, respectively, consist of (in thousands):

	July 1, 2007	July 2, 2006
Raw materials	$ —	$ 431
Finished goods	25,261	18,872
Total	$ 25,261	$ 19,303

Sales to Distributors

We defer recognition of revenue on all sales to distributors until the distributor successfully resells the product, typically to an authorized reseller. Distributors regularly provide us their "sales-out" reports for this purpose. Until it is sold, inventory held by distributors is included in our reported finished goods inventory and was $3.2 million at July 1, 2007 and July 2, 2006. The accounts receivable owed us by distributors, net of the deferred revenue from sales to distributors, is recorded in prepaid expenses and other current assets, as reflected in the following table (in thousands):

	July 1, 2007	July 2, 2006
Accounts receivable, net of allowance for doubtful accounts of $225 ($300 in fiscal 2006)	$ 23,288	$ 17,158
Deferred revenue	(15,203)	(13,325)
Net, included in Prepaid expenses and other current assets	$ 8,085	$ 3,833

EXTREME NETWORKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Property and Equipment, Net

Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization is computed using the straight-line method over the estimated useful lives of the assets, with the exception of land, which is not depreciated. Estimated useful lives of 25 years are used for buildings. Estimated useful lives of one to four years are used for computer equipment and software. Estimated useful lives of three years are used for office equipment, furniture and fixtures. Depreciation and amortization of leasehold improvements is computed using the lesser of the remaining lease terms or three years. Property and equipment consist of the following (in thousands):

	July 1, 2007	July 2, 2006
Computer equipment	$ 62,651	$ 61,164
Land	20,600	20,600
Buildings and improvements	17,546	17,524
Purchased software	33,775	32,995
Office equipment, furniture and fixtures	4,335	4,205
Leasehold improvements	6,327	6,309
	145,234	142,797
Less accumulated depreciation and amortization	(102,078)	(96,298)
Property and equipment, net	$ 43,156	$ 46,499

In April 2006, we entered into a contract for the sale of our corporate headquarters campus in Santa Clara, California, at a price of $70 million. On October 31, 2006, the Company announced that the Campus Sale Agreement expired under its terms. Accordingly, the parties are no longer bound to proceed with the transaction, and the proposed purchaser has the right not to proceed with the transaction.

Long-Lived Assets

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Determination of recoverability is based on an estimate of undiscounted future cash flows resulting from the use of the asset and its eventual disposition. Measurement of an impairment loss for long-lived assets that management expects to hold and use is based on the fair value of the asset. Long-lived assets to be disposed of are reported at the lower of carrying amount or fair value less costs to sell.

Other assets include technology agreements that are amortized over their contractual periods using the straight-line method of amortization. The related liability for the technology agreement is recorded in other accrued liabilities and other long-term liabilities.

Guarantees and Product Warranties

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

We have determined that the requirements of FIN 45 apply to our standard product warranty liability. The following table summarizes the activity related to our product warranty liability during fiscal 2007, fiscal 2006 and fiscal 2005:

	Year Ended		
	July 1, 2007	July 2, 2006	June 3, 2005
Balance beginning of period	$ 7,027	$ 7,471	$ 8,297
New warranties issued	8,752	10,189	12,251
Warranty expenditures	(8,597)	(10,633)	(14,205)
Change in estimate	—	—	1,128
Balance end of period	$ 7,182	$ 7,027	$ 7,471

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

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

Deferred Support Revenue

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

	Year Ended	
	July 1, 2007	July 2, 2006
Balance beginning of period	$ 41,722	$ 47,849
New support arrangements	55,983	52,149
Recognition of support revenue	(56,918)	(58,276)
Balance end of period	40,787	41,722
Less current portion	30,501	32,023
Non-current deferred revenue	$ 10,286	$ 9,699

EXTREME NETWORKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Other Accrued Liabilities

The following are the components of other accrued liabilities (in thousands):

	July 1, 2007	July 2, 2006
Accrued income taxes	$ 1,877	$ 3,435
Accrued indirect taxes	308	490
Accrued interest on subordinated debt	—	583
Other accrued liabilities	21,078	15,073
Total	$ 23,263	$ 19,581

Derivatives

We use derivative financial instruments to manage exposures to foreign currency. Our objective for holding derivatives is to use the most effective methods to minimize the impact of these exposures. We do not enter into derivatives for speculative or trading purposes. All derivatives, whether designated in hedging relationships or not, are required to be recorded on the balance sheet at fair value. The accounting for changes in the fair value of a derivative depends on the intended use of the derivative and the resulting designation. For a derivative designated as a cash flow hedge, the effective portion of the derivative's gain or loss is initially reported as a component of accumulated other comprehensive income (loss) and, upon occurrence of the forecasted transaction, is subsequently reclassified into the consolidated statement of operations line item to which the hedged transaction relates. The ineffective portion of the gain or loss is reported in other expense immediately. For a derivative not designated as a cash flow hedge, the gain or loss is recognized in other expense in the period of change together with the offsetting gain or loss on the hedged item attributed to the risk being hedged.

Advertising

Cooperative advertising obligations with customers are accrued and the costs expensed at the time the related revenue is recognized. All other advertising costs are expensed as incurred. Cooperative advertising expenses are recorded as marketing expenses to the extent that an advertising benefit separate from the revenue transaction can be identified and the cash paid does not exceed the fair value of that advertising benefit received. Otherwise, such cooperative advertising obligations with customers are recorded as a reduction of revenue. Advertising expenses were $0.2 million, zero and $0.5 million for fiscal 2007, fiscal 2006, and fiscal 2005, respectively.

Recently Issued Accounting Standards

Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements

In September 2006, the SEC issued Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" ("SAB 108"). SAB 108 provides interpretative guidance on the process of quantifying financial statement misstatements and is effective for fiscal years ending after November 15, 2006. The adoption of SAB 108 did not have a material impact on our consolidated financial statements.

EXTREME NETWORKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Accounting for Consideration Given by a Service Provider to a Manufacturer or Reseller of Equipment Necessary for an End-Customer to Receive Service from the Service Provider

In September 2006, the FASB issued Emerging Issues Task Force Issue, or EITF, No. 06-1, *Accounting for Consideration Given by a Service Provider to a Manufacturer or Reseller of Equipment Necessary for an End-Customer to Receive Service from the Service Provider.* EITF No. 06-1 requires companies to provide disclosures regarding the nature of arrangements in which they provide consideration to manufacturers or resellers of equipment necessary for an end-customer to receive service from them, including the amounts recognized in the Consolidated Statements of Operations. EITF 06-1 is effective for fiscal years beginning after June 15, 2007. We do not expect the adoption of EITF No. 06-1 to have a material impact on our consolidated financial statements.

Fair Value Measurements

In September 2006, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 157, *Fair Value Measurements*. SFAS 157 replaces the different definitions of fair value in the accounting literature with a single definition. It defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. SFAS 157 is effective for fair-value measurements already required or permitted by other standards for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. We currently are in the process of determining the impact of adopting the provisions of SFAS 157 on our financial position, results of operations and cash flows.

Fair Value Option for Financial Assets and Liabilities

In February 2007, the FASB issued Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of FASB Statement No. 115* (FAS 159). FAS 159 permits companies to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value and establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities. The provisions of FAS 159 become effective for fiscal years beginning after November 15, 2007. We believe that the adoption of SFAS 159 will not have a material effect on our financial statements.

Accounting for Income Taxes

In July 2006, the Financial Accounting Standards Board (FASB) released its final Interpretation on uncertain tax positions, FIN 48, *Accounting for Uncertainty in Income Taxes – an interpretation of FAS 109.* This Interpretation clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, *Accounting for Income Taxes.* This Interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. The guidance will become effective as of the beginning of a company's fiscal year beginning after December 15, 2006. The Company is currently assessing the impact of adopting this standard.

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3. Available-for-Sale Securities

The following is a summary of available-for-sale securities (in thousands):

	Amortized Cost	Fair Value	Unrealized Holding Gains	Unrealized Holding Losses
July 1, 2007:				
Money market funds	$ 198	$ 198	$ —	$ —
U.S. corporate debt securities	90,436	90,190	—	(246)
U.S. government agency securities	48,309	48,160	—	(149)
U.S. municipal bonds	1,991	1,985	—	(6)
Market auction preferred securities	34,840	34,840	—	$ —
	$175,774	$175,373	$ —	$ (401)
Classified as:				
Cash equivalents	$ 31,109	$ 31,091	$ —	$ (18)
Short-term investments	91,772	91,599	—	(173)
Marketable securities	52,893	52,683	—	(210)
	$175,774	$175,373	$ —	$ (401)
July 2, 2006:				
Money market funds	$ 2,830	$ 2,830	$ —	$ —
U.S. corporate debt securities	150,536	149,432	—	(1,104)
U.S. government agency securities	98,519	97,510	—	(1,009)
U.S. municipal bonds	970	945	—	(25)
Market auction preferred securities	121,620	121,620	—	—
	$374,475	$372,337	$ —	$ (2,138)
Classified as:				
Cash equivalents	$ 31,841	$ 31,830	$ —	$ (11)
Short-term investments	299,043	297,726	—	(1,317)
Marketable securities	43,591	42,781	—	(810)
	$374,475	$372,337	$ —	$ (2,138)

The amortized cost and estimated fair value of available-for-sale investments in debt securities at July 1, 2007, by contractual maturity, were as follows (in thousands):

	Amortized Cost	Fair Value
Due in 1 year or less	$122,882	$122,690
Due in 1-2 years	34,935	34,798
Due in 2-5 years	17,957	17,885
Total investments in available for sale debt securities	$175,774	$175,373

EXTREME NETWORKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The following table presents our investments' gross unrealized losses and fair values, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position.

	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
July 1, 2007:						
U.S. corporate debt securities	$75,470	$ (199)	$14,720	$ (47)	$ 90,190	$ (246)
U.S. government agency securities	19,119	(35)	29,042	(114)	48,160	(149)
U.S. municipal bonds	985	(5)	1,000	(1)	1,985	(6)
	$95,574	$ (239)	$44,762	$ (162)	$140,335	$ (401)

Municipal and corporate bonds. Unrealized losses as of July 1, 2007 on our investments in municipal and corporate bonds were caused by interest rate increases. The contractual terms of the debentures do not permit the issuer to settle the securities at a price less than the amortized cost of the investment. The issuers of our municipal bonds have a credit rating of AAA, and the issuers of our corporate bonds have a credit rating of AA (Moody's and S&P).

Government agency securities. Unrealized losses as of July 1, 2007 on our investments in our government agency securities (i.e., Federal National Mortgage Association and Federal Home Loan Mortgage Corp.) were caused by interest rate increases. The contractual terms of the investments do not permit the issuer to settle the securities at a price less than the amortized cost of the investment. The issuers of our government agency securities have a credit rating of AAA.

The unrealized losses on our investments were caused by interest rate increases. As substantially all of our investments are investment grade government and corporate debt securities that have maturities of less than 3 years, and we have both the ability and intent to hold the investments until maturity, we do not consider these investments to be other-than-temporarily impaired at July 1, 2007.

4. Commitments, Contingencies and Leases

Stock Repurchase Program

On October 20, 2005, our Board of Directors authorized the repurchase of up to $50 million of our common stock. This authorization originally was to expire in October 2007, but on October 25, 2006, the Board of Directors terminated the share repurchase plan. In the quarter ended December 31, 2006, we repurchased approximately 0.9 million shares for approximately $3.4 million, primarily through open market purchases, bringing the cumulative total to 11.1 million repurchased shares for approximately $48.3 million.

Line of Credit

We have a revolving line of credit for $10.0 million with a major lending institution. Borrowings under this line of credit bear interest at the bank's prime rate. As of July 1, 2007, there were no outstanding borrowings under this line of credit. The line of credit contains a provision for the issuance of letters of credit not to exceed the unused balance of the line. As of July 1, 2007, we had letters of credit totaling $0.7 million. These letters of credit were primarily issued to satisfy requirements of certain of our customers for performance bonds. The line of credit requires us to maintain specified financial covenants related to tangible net worth and liquidity with which we were in compliance as of July 1, 2007. The line of credit was renewed on January 24, 2007 and expires on January 24, 2008.

EXTREME NETWORKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Leases

We lease office space for our various United States and international sales offices. Certain leases contain rent escalation clauses and renewal options. We sublease certain of our leased facilities to third party tenants. Future annual minimum lease payments under all noncancelable operating leases and future rental income under all noncancelable subleases having initial or remaining lease terms in excess of one year at July 1, 2007 were as follows (in thousands):

	Future Lease Payments	Future Rental Income
Fiscal 2008	$ 7,044	$ 426
Fiscal 2009	5,363	441
Fiscal 2010	4,606	505
Fiscal 2011	4,004	390
Fiscal 2012	323	—
Total minimum payments	$ 21,340	$ 1,762

Rent expense was approximately $4.8 million, $4.4 million and $5.1 million for fiscal 2007, fiscal 2006, and fiscal 2005, respectively, net of sublease income of $0.1 million, $0.1 million and $0.4 million in the respective periods.

Purchase Commitments

We currently have arrangements with one contract manufacturer and other suppliers for the manufacture of our products. Our arrangements allow them to procure long lead-time component inventory on our behalf based upon a rolling production forecast provided by us. We are obligated to the purchase of long lead-time component inventory that our contract manufacturer procures in accordance with the forecast, unless we give notice of order cancellation outside of applicable component lead-times. As of July 1, 2007, we had non-cancelable commitments to purchase approximately $27.3 million of such inventory during the first quarter of fiscal 2008.

Legal Proceedings

Government Inquiries Relating to Historical Stock Option Practices

On June 27, 2006, the Company received an informal inquiry letter from the Staff of the SEC Enforcement Division requesting that the Company voluntarily provide documents related to its policies, practices and procedures for granting stock options for the period since its initial public offering on April 9, 1999 (“IPO”). The Company responded to the request and is cooperating fully with the SEC inquiry.

Late SEC Filing and Nasdaq Delisting Proceedings

Due to the Special Committee investigation and the resulting restatements, the Company did not timely file its Form 10-K for the fiscal year ending July 2, 2006 or the Quarterly Reports on Forms 10-Q for the quarters ended October 1, 2006, December 31, 2006 and April 1, 2007. The Company initially received Nasdaq Staff Determination notices stating that the Company was not in compliance with Marketplace Rule 4310(c)(14) because it had not timely filed such periodic reports with the SEC. Those filings were made on June 28, 2007. On July 2, 2007, the Company received a written notice from the Nasdaq Stock Market stating that the Nasdaq Listing and Hearing Review Council (the “Listing Council”), after consultation with the Nasdaq Listing Qualification Staff, had determined that as of that date the Company had demonstrated compliance with all

Nasdaq Marketplace Rules. The notice further stated that as of July 2, 2007, the matter was closed and the Company's securities would continue to be listed on The Nasdaq Global Market.

On July 3, 2007, the Company received a further Staff Determination notice from the Nasdaq Stock Market stating that the Company was not in compliance with Nasdaq's Marketplace Rule 4350(e) due to a failure by the Company to hold its annual meeting of shareholders within the time required by Rule 4350(e) and, therefore, that its common stock was again subject to delisting from The Nasdaq Global Market. On July 19, 2007, the Company received a written notice from the Nasdaq Stock Market stating that a Nasdaq Listing Qualifications Panel (the "Panel") had determined that the Company's securities would continue to be listed on The Nasdaq Global Market, subject to the condition that on or before August 1, 2007, the Company inform the Panel that it has held its annual meeting of shareholders. On July 31, 2007, the Company notified the Panel that the Company had held the annual meeting of shareholders on July 30, 2007. On August 3, 2007, the Company received a written notice from the Panel confirming that the Company had demonstrated compliance with all Nasdaq Marketplace Rules, and that the Panel determined to continue the listing of the Company's securities on The Nasdaq Stock Market. Accordingly, the Company believes that the Nasdaq delisting proceedings have concluded.

Shareholder Litigation Relating to Historical Stock Option Practices

On April 25, 2007, an individual identifying herself as a shareholder of the Company filed a derivative action in the United States District Court for the Northern District of California purporting to assert claims on behalf of and in the name of the Company against various of our current and former directors and officers relating to our stock option granting practices for stock options issued from 2000 to 2003. The complaint alleges that the individual defendants breached their fiduciary duties and other obligations to the Company and violated federal securities laws in connection with our historical stock option granting process and our accounting for past stock options.

The plaintiff has asserted claims for violations of Sections 10(b) (including Rule 10b-5 thereunder), 14(a), and 20(a) of the Securities Exchange Act of 1934, unjust enrichment, breach of fiduciary duty and aiding and abetting such breach, rescission, and a claim for an accounting of all stock option grants made to the named defendants. Extreme Networks, Inc. is named as a nominal defendant in these actions. On behalf of Extreme Networks, Inc., the plaintiff seeks unspecified monetary and other relief against the named defendants. The plaintiff is Yenna Wu. The individual named defendants are Gordon L. Stitt, Herb Schneider, Stephen Haddock, Paul Romeo, Vito Palermo, Harold Covert, Darrell Scherbarth, Christopher, N. Todd, Alexander J. Gray, Frank C. Carlucci, William R. Slakey, Charles Carinalli, Harry Silverglide, Michael West, Kenneth Levy, Robert L. Corey, Peter Wolken, and Promod Haque.

A similar derivative action was filed in the same court on May 2, 2007, by Linda Erikson, another individual identifying herself as a shareholder of the Company, alleging the same legal claims against the same individual defendants concerning the same subject matter.

A third derivative action was filed in the same court on May 31, 2007 by Frank A. Grucel, an individual identifying himself as a shareholder of the Company, purporting to assert claims on the Company's behalf relating to the Company's historic stock options granting practices. The complaint seeks unspecified monetary and injunctive relief and asserts claims for violations of Section 14(a) of the Securities Exchange Act of 1934, an accounting of all stock option grants made to the named defendants, breach of fiduciary duty and aiding and abetting such breach, abuse of control, gross mismanagement, constructive fraud, corporate waste, unjust enrichment, rescission, violations of California Corporations Code Section 25402, and breach of fiduciary duties related to insider selling and alleged misappropriation of information. Extreme Networks, Inc. is named as a nominal defendant in this action, and the individual named defendants are Gordon L. Stitt, Herb Schneider, Stephen Haddock, Alexander J. Gray, Frank C. Carlucci, William R. Slakey, Charles Carinalli, Harry Silverglide, Michael West, Kenneth Levy, Robert L. Corey, Peter Wolken, Michael Palu, and Alicia Moore.

The foregoing actions have been related and assigned to the same judge. On June 15, 2007, Yenna Wu filed an amended complaint in her action. The amended complaint names one additional individual defendant, Mark Canepa, as well as the individual defendants named in the derivative complaints filed on April 25, 2007 and May 2, 2007, is purportedly brought both as a derivative action and as a class action on behalf of all current shareholders of the Company, and alleges a claim for violation of Delaware General Corporations Code Section 211(c), seeking an order compelling the Company to hold a shareholder's meeting. The amended complaint otherwise alleges the same claims as the derivative complaints filed on April 25, 2007 and May 2, 2007 by plaintiffs Wu and Erikson, respectively.

On August 2, 2007, the foregoing actions were consolidated for all purposes. Subsequently, on August 13, 2007, plaintiff Frank A. Grucel, Jr. was named lead plaintiff and his attorneys named lead counsel in the consolidated actions. This consolidated action is at an early stage, with a consolidated complaint to be filed no later than September 27, 2007. Discovery has not yet commenced and the defendants are not yet required to respond to the complaints currently on file. We cannot at this time predict whether this consolidated action will result in any material recovery by or expense to the Company.

Indemnification Obligations

Subject to certain limitations, we may be obligated to indemnify our current and former directors, officers and employees. These obligations arise under the terms of our certificate of incorporation, our bylaws, applicable contracts, and Delaware and California law. The obligation to indemnify, where applicable, generally means that we are required to pay or reimburse, and in certain circumstances we have paid or reimbursed, the individuals' reasonable legal expenses and possibly damages and other liabilities incurred in connection with these matters. It is not possible to estimate the maximum potential amount under these indemnification agreements due to the limited history of these claims. The cost to defend the Company and the named individuals could have a material adverse effect on our consolidated financial position, results of operations and cash flows in the future. Recovery of such costs under our directors and officers insurance coverage is uncertain.

Other Legal Matters

On April 20, 2007, Extreme Networks filed suit against Enterasys in the United States District Court for the Western District of Wisconsin, Civil Action No. 07-C-0229-C. The complaint alleges willful infringement of U.S. patents Nos. 6,104,700, 6,678,248, and 6,859,438, and seeks injunctive relief against Enterasys' continuing sale of infringing goods and monetary damages. Enterasys responded to the complaint on May 30, 2007. Enterasys also filed a counterclaim alleging infringement of three U.S. patents owned by Enterasys. The case is in its early stages, however a Markman Hearing has been scheduled for October 2007, and a trial date has been set for May 2008.

On December 27, 2005, Broadband Office Inc. ("Broadband") served an amended complaint, adding Extreme Networks as a defendant in its lawsuit against Technology Credit Corporation ("TCC") and Key Equipment Finance, Inc., seeking recovery of an alleged preferential payment in the amount of $0.8 million plus interest, purportedly paid by Broadband to TCC within ninety days prior to Broadband's petition for bankruptcy protection. Extreme disputes that it owes any money to Broadband, and intends vigorously to defend against the claims.

EXTREME NETWORKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

On June 21, 2005, Enterasys filed suit against Extreme Networks and Foundry Networks, Inc. (“Foundry”) in the United States District Court for the District of Massachusetts, Civil Action No. 05-11298 DPW. The complaint alleges willful infringement of U. S. Patent Nos. 5,251,205; 5,390,173; 6,128,665; 6,147,995; 6,539,022; and 6,560, 236, and seeks: a) a judgment that Extreme willfully infringes each of the patents; (b) a permanent injunction from infringement, inducement of infringement and contributory infringement of each of the six patents; (c) damages and a “reasonable royalty” to be determined at trial; (d) trebled damages; (e) attorneys fees, costs and interest; and (f) equitable relief at the court’s discretion. The Markman hearing has been rescheduled for October 2007. We intend vigorously to defend against Enterasys’ assertions, which we believe to be without merit.

On May 27, 2003, Lucent filed suit against Extreme Networks and Foundry in the United States District Court for the District of Delaware, Civil Action No. 03-508. The complaint alleged willful infringement of U.S. Patent Nos. 4,769,810, 4,769,811, 4,914,650, 4,922,486 and 5,245,607. After the Markman hearing, Lucent dropped its claims relating to the 5,245,607 patent. The judge split the case into three parts to be tried separately: phase 1 to cover infringement, willfulness and damages; phase 2 to cover invalidity; and phase 3 to cover equitable defenses and our counterclaims. On May 9, 2005, a jury in Delaware awarded a verdict to Extreme in the phase 1 trial of non-infringement on 18 out of the 19 claims asserted. The jury did award Lucent damages of approximately $275,000 on the remaining claim; which covers a feature that is not offered in our current product line. The parties each filed post-trial motions; and on August 16, 2005, the judge granted Lucent’s motion for a new trial, ruling that Extreme impermissibly introduced to the jury evidence of its prior relationship with Lucent. Extreme’s motion for reconsideration was denied. On August 9, 2006, the parties entered into a settlement agreement to resolve all outstanding claims which includes the dismissal of all claims and a patent cross-license for a defined term.

Beginning on July 6, 2001, purported securities fraud class action complaints were filed in the United States District Court for the Southern District of New York. The cases were consolidated and the litigation is now captioned as In re Extreme Networks, Inc. Initial Public Offering Securities Litigation, Civ. No. 01-6143 (SAS) (S.D.N.Y.), related to In re Initial Public Offering Securities Litigation, 21 MC 92 (SAS) (S.D.N.Y.). The operative amended complaint names as defendants Extreme Networks; six of our present and former officers and/or directors, including our CEO (the “Extreme Networks Defendants”); and several investment banking firms that served as underwriters of our initial public offering and October 1999 secondary offering. The complaint alleges liability under Sections 11 and 15 of the Securities Act of 1933 and Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, on the grounds that the registration statement for the offerings did not disclose that: (1) the underwriters had agreed to allow certain customers to purchase shares in the offerings in exchange for excess commissions paid to the underwriters; and (2) the underwriters had arranged for certain customers to purchase additional shares in the aftermarket at predetermined prices. Similar allegations were made in other lawsuits challenging over 300 other initial public offerings and follow-on offerings conducted in 1999 and 2000. The cases were consolidated for pretrial purposes. Previously, we executed a settlement agreement presented to all issuer defendants. In that settlement, plaintiffs would dismiss and release all claims against the Extreme Network Defendants, in exchange for a contingent payment by the insurance companies collectively responsible for insuring the issuers in all of the IPO cases, and for the assignment or surrender of control of certain claims we may have against the underwriters. The Extreme Networks Defendants would not be required to make any cash payments in the settlement, unless the pro rata amount paid by the insurers in the settlement exceeded the amount of the insurance coverage. The Court gave preliminary approval to the settlement in February 2005 and held a hearing in April 2006 to consider final approval of the settlement. Before the Court issued a final decision on the settlement, on December 5, 2006 the United States Court of Appeals for the Second Circuit vacated the class certification of plaintiffs’ claims against the underwriters in six cases designated as focus or test cases. Thereafter, on December 14, 2006, the Court ordered a stay of all proceedings in all of the lawsuits pending the outcome of plaintiffs' petition to the Second Circuit Court of Appeals for a rehearing en banc and resolution of the class certification issue. On April 6, 2007, the Second Circuit Court of Appeals denied plaintiffs' petition for a rehearing, but clarified that the plaintiffs may seek to certify a more limited class. Accordingly, the plaintiffs and issuers have stated that they are prepared to discuss how the settlement might be amended or renegotiated to comply with the decision of the Second Circuit Court of Appeals. On April 30, 2007, Plaintiffs stated that they intend to present a proposed redefined class to the Court. If the settlement is not amended or renegotiated and then approved by the Court, there is no assurance that we will prevail in the lawsuit. Failure to prevail could have a material adverse effect on our consolidated financial position, results of operations and cash flows in the future.

We may from time to time be party to litigation arising in the course of our business, including, without limitation, allegations relating to commercial transactions or business relationships or intellectual property rights. Such claims, even if not meritorious, could result in the expenditure of significant financial and managerial resources. Litigation in general, and intellectual property and securities litigation in particular, can be expensive and disruptive to normal business operations. Moreover, the results of legal proceedings are difficult to predict.

5. Convertible Subordinated Notes

In December 2001, we completed a private placement of $200.0 million of convertible subordinated notes. The notes matured and were paid off on December 1, 2006. Interest was payable semi-annually at 3.5% per annum.

6. Stockholders' Equity

Preferred Stock

In April 2001, in connection with our Stockholders' Rights Agreement, we authorized the issuance of preferred stock. The preferred stock may be issued from time to time in one or more series. The board of directors is authorized to provide for the rights, preferences and privileges of the shares of each series and any qualifications, limitations or restrictions on these shares. As of July 1, 2007, no shares of preferred stock were outstanding.

Warrants

On October 30, 2003, Extreme Networks and Avaya, Inc. entered into a strategic alliance to jointly develop and market converged communications solutions, by executing a Joint Development Agreement, and a distribution agreement under which Avaya is entitled to resell Extreme Networks products. Extreme issued to Avaya a warrant with a ten-year expiration period to purchase up to 2,577,794 shares of Extreme Networks common stock at a price of $0.01 per share, with Avaya having the right to exercise the warrant with respect to one third of such shares 90 days after the date of the agreements, and the remaining shares become exercisable based upon the completion of certain milestones by Avaya. Even if the milestones are not completed, however, the warrant will become fully exercisable for all shares 90 days prior to the expiration of the warrant. Avaya exercised the warrant with respect to approximately 859,000 of the shares subject to the warrant on March 17, 2004 and, approximately 859,000 of the shares subject to the warrant on August 8, 2005. See Note 13 for additional details on the Avaya alliance.

EXTREME NETWORKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Deferred Stock Compensation

During fiscal 2001, we recorded deferred share-based compensation expense of $24.4 million associated with unvested stock options subject to forfeiture issued to employees assumed in acquisitions. In addition, in accordance with APB 25, for the year ended July 3, 2005 and prior years, share-based compensation expense is not recorded in connection with stock options granted with exercise prices equal to or greater than the fair market value of our common stock on the date of grant. We recorded deferred stock compensation in connection with stock options granted with exercise prices less than the fair market value of the common stock on the date of grant. The amount of such deferred stock compensation is equal to the excess of fair market value over the exercise price on such date. These amounts were amortized as charges to operations, using the graded method, over the vesting periods of the individual stock options, generally four years. Upon termination of an employee, the amount of expense recognized under the graded vesting method that is in excess of the amount actually earned is reversed. We recorded amortization of deferred stock compensation expense, net of reversals, of zero, zero and $0.5 million for fiscal 2007, fiscal 2006 and fiscal 2005, respectively. Upon adoption of FAS 123R at the beginning of fiscal year 2006, we reclassified the unamortized deferred stock compensation in the amount of $0.2 million against common stock.

Stockholders' Rights Agreement

In April 2001, the board of directors approved a Stockholders' Rights Agreement ("Rights Agreement"), declaring a dividend of one preferred share purchase right for each outstanding share of common stock, par value $0.001 per share, of Extreme Networks common stock. The Rights Agreement is intended to protect stockholders' rights in the event of an unsolicited takeover attempt. It is not intended to prevent a takeover of Extreme Networks on terms that are favorable and fair to all stockholders and will not interfere with a merger approved by the board of directors. In the event the rights become exercisable, each right entitles stockholders to buy, at an exercise price of $150 per right owned, a unit equal to a portion of a new share of Extreme Networks Series A preferred stock. The rights will be exercisable only if a person or a group acquires or announces a tender or exchange offer to acquire 15% or more of our common stock. The rights, which expire in April 2011, are redeemable for $0.001 per right at the approval of the board of directors.

Comprehensive Income (Loss)

The activity of other comprehensive income (loss) was as follows (in thousands):

	Year Ended		
	July 1, 2007	July 2, 2006	July 3, 2005
Change in unrealized loss on investments:			
(Increase) decrease in net unrealized loss on investments	$1,737	$1,313	$(441)
Less: Net gain on investments realized and included in net income (loss)	—	—	99
Net (increase) decrease in unrealized loss on investments	1,737	1,313	(540)
Unrealized gain (loss) on derivatives	(2)	(10)	12
Foreign currency translation adjustments	404	17	29
Other comprehensive income (loss)	$2,139	$1,320	$(499)

EXTREME NETWORKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The following are the components of accumulated other comprehensive income (loss), net of tax (in thousands):

	July 1, 2007	July 2, 2006
Accumulated unrealized loss on investments, net of tax of $0 in fiscal 2007 and $0 in fiscal 2006	$(402)	$(2,138)
Accumulated unrealized gain on derivatives	—	2
Accumulated foreign currency translation adjustments	974	569
Accumulated other comprehensive loss	$ 572	$(1,567)

Shares Reserved for Issuance

The following are shares reserved for issuance (in thousands):

	July 1, 2007	July 2, 2006
Convertible subordinated notes	—	9,544
Warrants	860	860
Employee stock purchase plan	5,583	5,800
Employee stock options	39,968	43,635
Total shares reserved for issuance	46,411	59,839

7. Employee Benefit Plans (including Share-based Compensation)

On July 4, 2005, we adopted the fair value recognition provisions of SFAS No. 123(R), *Share-Based Payment*, (“FAS 123R”). Prior to July 4, 2005, we accounted for share-based payments under the recognition and measurement provisions of APB Opinion No. 25, *Accounting for Stock Issued to Employees* (“APB 25”), and related Interpretations, as permitted by SFAS No. 123, *Accounting for Share-based Compensation* (“FAS 123”). In accordance with APB 25 no compensation cost was required to be recognized for options granted that had an exercise price equal to the market value of the underlying common stock on the date of grant.

We adopted FAS 123R using the modified-prospective-transition method. Under that transition method, compensation cost recognized in the year ended July 2, 2006 includes: a) compensation cost for all share-based payments granted prior to, but not yet vested as of July 4, 2005, based on the grant-date fair value estimated in accordance with the original provisions of FAS 123, and b) compensation cost for all share-based payments granted subsequent to July 4, 2005, based on the grant-date fair value estimated in accordance with the provisions of FAS 123R. The results for the prior periods have not been restated.

As a result of adopting FAS 123R on July 4, 2005 our income before income taxes and net income for the year ended July 1, 2007, are $6.2 million and $6.2 million lower, respectively, than if we had continued to account for share-based compensation under APB 25. Basic and diluted earnings per share for the year ended July 1, 2007 are $0.05 and $0.05 lower, respectively, than if we had continued to account for share-based compensation under APB 25. We have not recognized, and do not expect to recognize in the near future, any tax benefit related to employee share-based compensation cost as a result of the full valuation allowance on our net deferred tax assets and our net operating loss carryforwards. The total compensation cost capitalized in inventory was less than $0.1 million as of July 1, 2007. Share-based compensation cost of $0.8 million was recognized in expense in accordance with APB 25 for the year ended July 3, 2005.

EXTREME NETWORKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

As of July 1, 2007, we have the following share-based compensation plans:

2005 Equity Incentive Plan

The 2005 Equity Incentive Plan (the "2005 Plan") was adopted by our Board of Directors on October 20, 2005, and approved by stockholders on December 2, 2005. The 2005 Plan replaces the 1996 Stock Option Plan (the "1996 Plan"), 2000 Nonstatutory Stock Option Plan (the "2000 Plan") and 2001 Nonstatutory Stock Option Plan (the "2001 Plan").

Under the 2005 Plan, we may grant stock options, stock appreciation rights, restricted stock, restricted stock units, performance shares, performance units, and other share-based or cash-based awards to employees and consultants. The 2005 Plan also authorizes the grant of awards of stock options, stock appreciation rights, restricted stock and restricted stock units to non-employee members of the board of directors and deferred compensation awards to officers, directors and certain management or highly compensated employees. The 2005 Plan authorizes the issuance of up to 12,000,000 shares of our common stock, and up to 11,000,000 shares subject to awards that remain outstanding under the 1996 Plan, 2000 Plan and 2001 Plan as of December 2, 2005 and which subsequently terminate without having been exercised or which are forfeited, will be added to the shares available under the 2005 Plan. As of July 1, 2007, 11,918,924 shares were available for future grant under the 2005 Plan.

1999 Employee Stock Purchase Plan

In January 1999, the Board of Directors approved the adoption of Extreme Network's 1999 Employee Stock Purchase Plan (the "Purchase Plan"). On December 2, 2005, the stockholders approved an amendment to the Purchase Plan to increase the maximum number of shares of common stock that may be issued under the plan by 5,000,000 to a total of 12,000,000 shares. The Purchase Plan permits eligible employees to acquire shares of our common stock through periodic payroll deductions of up to 15% of total compensation. No more than 625 shares may be purchased on any purchase date per employee. Each offering period has a maximum duration of 12 months. The price at which the common stock may be purchased is 85% of the lesser of the fair market value of our common stock on the first day of the applicable offering period or on the last day of the respective purchase period. Through July 1, 2007, 6,416,504 shares had been purchased under the Purchase Plan.

Amended 1996 Stock Option Plan

In January 1999, the Board of Directors approved an amendment to the 1996 Plan to (i) increase the share reserve by 10,000,000 shares, (ii) to remove certain provisions which are required to be in option plans maintained by California privately-held companies and (iii) to rename the 1996 Plan as the "Amended 1996 Stock Option Plan."

Under the 1996 Plan, which was originally adopted in September 1996, options may be granted for common stock, pursuant to actions by the Board of Directors, to eligible participants. A total of 56,387,867 shares were reserved under the 1996 Plan. Options granted are exercisable as determined by the Board of Directors. Options vest over a period of time as determined by the Board of Directors, generally four years. Options have a contractual term of ten years. Effective December 2, 2005, the 1996 Plan was terminated.

2000 Plan

In March 2000, the Board of Directors adopted the 2000 Plan. Options may be granted for common stock, pursuant to actions by the Board of Directors, to eligible participants. Generally, only non-officer employees are eligible to participate in the 2000 Plan, except that options may be granted to officers under this plan in connection with written offers of employment. A total of 4,000,000 shares were reserved under the 2000 Plan. Options vest over a period of time as determined by the Board of Directors, generally four years. Options have a contractual term of ten years. Effective December 2, 2005, the 2000 Plan was terminated.

2001 Plan

In May 2001, the Board of Directors adopted the 2001 Plan. Options may be granted for common stock, pursuant to actions by the Board of Directors, to eligible participants. Generally, only non-officer employees are eligible to participate in the 2001 Plan, except that options may be granted to officers under this plan in connection with written offers of employment. A total of 4,000,000 shares were reserved under the 2001 Plan. Options vest over a period of time as determined by the Board of Directors, generally four years. Options have a contractual term of ten years. Effective December 2, 2005, the 2001 Plan was terminated.

A summary of the status of our non-vested shares as of July 1, 2007 and changes during fiscal 2007 is presented below:

	Number of Shares (000's)	Weighted-Average Grant-Date Fair Value
Non-vested shares at June 2, 2006	162	$ 4.76
Granted	564	3.50
Vested	(162)	4.10
Canceled	(99)	3.96
Non-vested shares at July 1, 2007	465	$ 3.63

During fiscal 2007, fiscal 2006 and fiscal 2005, we granted non-vested stock awards under the 2001 Plan for 564,000, 170,000 and 27,000 shares of common stock with a weighted average grant date fair value per share of $3.50, $4.74 and $5.61, respectively. The shares were placed in an escrow account and will be released to the recipients as the shares vest over periods of up to twenty-four months. If a participant terminates employment prior to the vesting dates, the unvested shares will be canceled and returned to the 2001 Plan. We recognize compensation expense on the awards over the vesting period based on an intrinsic value calculation as of the date of grant. As of July 1, 2007, there were approximately $1.1 million in unrecognized compensation costs related to non-vested stock. This cost is expected to be recognized over a weighted-average period of approximately 1.6 year.

EXTREME NETWORKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The following table summarizes stock option activity under all plans:

	Number of Shares (000's)	Weighted-Average Exercise Price Per Share	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value ($ 000's)
Options outstanding at June 27, 2004	21,451	$ 7.25		
Granted	3,884	$ 5.29		
Exercised	(538)	$ 2.95		
Canceled	(3,659)	$ 7.98		
Options outstanding at July 3, 2005	21,138	$ 6.87		
Granted	4,965	$ 4.52		
Exercised	(513)	$ 3.13		
Canceled	(4,164)	$ 6.94		
Options outstanding at July 2, 2006	21,426	$ 6.59		
Granted	3,687	$ 3.67		
Exercised	(150)	$ 0.62		
Canceled	(3,522)	$ 6.39		
Options outstanding at July 1, 2007	21,441	$ 5.97	6.72	$ 2,948
Exercisable at July 1, 2007	16,290	$ 6.55	6.11	$ 1,869

The following table summarizes significant ranges of outstanding and exercisable options at July 1, 2007:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price	Number Exercisable	Weighted-Average Exercise Price
		(In years)			
$ 0.50 – 3.65	3,832,495	6.66	$ 3.31	1,663,279	$ 2.95
$ 3.66 – 4.49	3,847,357	7.79	$ 4.20	2,295,676	$ 4.24
$ 4.50 – 5.53	3,733,528	7.44	$ 4.88	2,466,017	$ 4.90
$ 5.73 – 6.96	1,153,862	6.89	$ 6.32	992,555	$ 6.31
$ 7.07 – 7.07	3,862,989	6.31	$ 7.07	3,862,989	$ 7.07
$ 7.14 – 46.25	5,009,994	5.70	$ 9.28	5,009,108	$ 9.28
$ 0.50 – 46.25	21,440,225	6.72	$ 5.98	16,289,624	$ 6.56

As of July 1, 2007, there was $7.7 million of total unrecognized compensation cost related to unvested stock options. This cost is expected to be recognized over a weighted-average period of approximately 1.3 years. The total intrinsic value of options exercised in fiscal 2007 and fiscal 2006 were $0.5 million and $0.8 million, respectively. The fair value of options vested in fiscal 2007 and fiscal 2006 are $4.6 million and $4.8 million, respectively.

The fair value of each option award is estimated on the date of grant using the Black-Scholes-Merton option valuation model with the weighted average assumptions noted in the following table. The expected term of options granted is derived from historical data on employee exercise and post-vesting employment termination behavior. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant. Expected volatility is based on both the implied volatilities from traded options on our stock and historical volatility on our stock.

EXTREME NETWORKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

For options granted prior to July 4, 2005, and valued in accordance with FAS 123, the expected volatility used to estimate the fair value of the options was based solely on the historical volatility on our stock; we used the graded vesting method for expense attribution; and we recognized option forfeitures as they occurred as allowed by FAS 123.

For options granted after July 3, 2005, and valued in accordance with FAS 123R, the expected volatility used to estimate the fair value of options was based on a combination of the historical volatility of our stock and the implied volatility; we use the straight-line method for expense attribution, and we estimate forfeitures and only recognize expense for those shares expected to vest. Our estimated forfeiture rate in fiscal 2007, based on our historical forfeiture experience, is approximately 9%.

The fair value of options granted in fiscal 2007, fiscal 2006 and fiscal 2005 was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted average assumptions:

	Stock Option Plan Year Ended			Employee Stock Purchase Plan Year Ended		
	July 1, 2007	July 2, 2006	July 3, 2005	July 1, 2007	July 2, 2006	July 3, 2005
Expected life	2.5 yrs	2.5 yrs	2.5 yrs	0.9 yrs	0.6 yrs	0.8 yrs
Risk-free interest rate	4.9%	4.2%	2.9%	5.0%	4.8%	2.9%
Volatility	50%	60%	81%	37%	38%	47%
Dividend yield	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%

The Black-Scholes-Merton option valuation model requires the input of highly subjective assumptions, including the expected life of the share-based award and stock price volatility. The assumptions listed above represent management's best estimates, but these estimates involve inherent uncertainties and the application of management judgment. As a result, if other assumptions had been used, our recorded and pro forma share-based compensation expense could have been materially different from that depicted above and below. In addition, we are required to estimate the expected forfeiture rate and only recognize expense for those shares expected to vest. If our actual forfeiture rate is materially different from our estimate, the share-based compensation expense could be materially different.

In the fourth quarter of fiscal 2005, the compensation committee of the Board of Directors approved the acceleration of vesting of certain unvested stock options with exercise prices equal to or greater than $7.00 per share previously awarded to employees, including executive officers, and directors. Options to purchase approximately 4,544,000 shares of common stock were subject to acceleration. In accordance with APB 25, no compensation expense was required to be recorded in our consolidated statement of operations in fiscal 2005 in connection with the acceleration of the vesting of these options, as the exercise price of the employee stock options was higher than the market price of our stock on the date of the modification of the options. We believe that such options had limited economic value and were not offering sufficient incentive to the employees when compared to the potential future expense of approximately $11.4 million that would have been required to be recorded in future periods under FAS 123R had the options not been accelerated.

The weighted-average grant-date per share fair value of options granted in fiscal 2007, fiscal 2006 and fiscal 2005 was $1.27, $1.82 and $2.51, respectively. The weighted-average estimated per share fair value of shares granted under the Purchase Plan in fiscal 2006 and fiscal 2005 were $1.28 and $1.49, respectively. The weighted-average estimated per share fair value of shares granted under the Purchase Plan in the first quarter of fiscal 2007 was $1.13. No shares were granted under the ESPP in the second, third and fourth quarter of fiscal 2007.

EXTREME NETWORKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The following table illustrates the effect on net income and earnings per share if we had applied the fair value recognition provisions of FAS 123 to options granted under our stock option plans, non-vested stock awards granted and shares issued under the Purchase Plan in fiscal 2005. For purposes of pro forma disclosures, the value of the options is estimated using a Black-Scholes-Merton option-pricing formula (and the assumptions listed in the table above) and amortized to expense over the options' vesting periods using the graded vested method. The following pro forma information sets forth our net loss and net loss per share assuming that we had used the FAS 123 fair value method in accounting for employee stock options and purchases during fiscal 2005:

	Year Ended July 3, 2005 In thousands, except per share amounts
Net income (loss)	$ 12,519
Add:	
APB 25 stock-based compensation expense, included in net income (loss), net of tax	762
Less:	
Stock-based compensation expense determined under fair value based method, net of tax	(32,894)
Pro forma net loss	$ (19,613)
Basic earnings (loss) per share:	
Net income (loss)	$ 0.10
Net loss – pro forma	$ (0.16)
Diluted earnings (loss) per share:	
Net income (loss)	$ 0.10
Net loss – pro forma	$ (0.16)
Shares – As Reported	
Basic earnings per share	121,225
Diluted earnings per share	124,219
Shares – Pro Forma	
Basic earnings per share	121,225
Diluted earnings per share	121,225

401(k) Plan

We provide a tax-qualified employee savings and retirement plan, commonly known as a 401(k) plan (the "Plan"), which covers our eligible employees. Pursuant to the Plan, employees may elect to reduce their current compensation up to the lesser of 80% or the statutorily prescribed limit of $14,000 for calendar year 2005. Effective January 1, 2005, employees age 50 or over may elect to contribute an additional $4,000. The amount of the reduction is contributed to the Plan on a pre-tax basis.

We provide for discretionary matching contributions as determined by the board of directors for each calendar year. The board of directors set the match at $0.25 for every dollar contributed by the employee up to the first 4% of pay. The same level of match was approved during the 2007, 2006 and 2005 calendar years. All matching contributions vest immediately. In addition, the Plan provides for discretionary contributions as determined by the board of directors each year. Our matching contributions to the Plan totaled $558,739, $531,930 and $543,061 for fiscal 2007, fiscal 2006, and fiscal 2005, respectively. No discretionary contributions were made in fiscal 2007, fiscal 2006 or fiscal 2005.

EXTREME NETWORKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

8. Income Taxes

The provision for (benefit from) income taxes for fiscal 2007, fiscal 2006 and fiscal 2005 consisted of the following (in thousands):

	Year Ended		
	July 1, 2007	July 2, 2006	July 3, 2005,
Current:			
Federal	$ (12)	$ 40	$ —
State	100	100	50
Foreign	1,984	1,751	2,199
Total current	2,072	1,891	2,249
Deferred:			
Federal	—	142	766
State	—	14	76
Foreign	68	(249)	452
Total deferred	68	(93)	1,294
Provision for income taxes	$2,140	$1,798	$3,543

Pretax income from foreign operations was $26.5 million, $18.5 million and $14.4 million in fiscal 2007, fiscal 2006, and fiscal 2005, respectively.

The difference between the provision for income taxes and the amount computed by applying the federal statutory income tax rate (35 percent) to income (loss) before taxes is explained below (in thousands):

	Year Ended		
	July 1, 2007	July 2, 2006	July 3, 2005
Tax at federal statutory rate (benefit)	$(4,220)	$ 3,608	$ 5,622
Federal alternative minimum tax	(15)	40	—
State income tax, net of federal benefit	65	74	81
Unbenefited foreign taxes	83	29	650
Valuation allowance	3,993	(2,765)	20
Foreign earnings taxed at other than U.S. rates	(7,265)	(4,998)	(3,026)
Deferred compensation	568	396	22
Dividends from foreign subsidiary	8,750	5,250	—
Other	181	164	174
Provision for income taxes	$ 2,140	$ 1,798	$ 3,543

Significant components of our deferred tax assets are as follows (in thousands):

	July 1, 2007	July 2, 2006
Deferred tax assets:		
Net operating loss carryforwards	$ 78,358	$ 71,923
Tax credit carryforwards	20,381	19,075
Depreciation	19,407	19,508
Deferred revenue	4,860	5,379
Warrant amortization	16,326	17,167
Inventory write-downs	1,038	1,489
Other allowances and accruals	9,456	8,851
Other	17,932	15,719
Total deferred tax assets	167,758	159,111
Valuation allowance	(166,640)	(158,611)
Total net deferred tax assets	1,118	500
Deferred tax liabilities:		
Unrealized gain on investments	—	—
Deferred tax liability on foreign withholdings	(688)	(579)
Total deferred tax liabilities	(688)	(579)
Net deferred tax assets (liabilities)	$ 430	$ (79)
Recorded as:		
Net current deferred tax assets	$ 1,118	$ 500
Net non-current deferred tax liabilities	(688)	(579)
Net deferred tax assets (liabilities)	$ (430)	$ (79)

Our valuation allowance increased by $8.0 million in fiscal 2007, decreased by $17.2 million in fiscal 2006 and increased by $1.1 million in fiscal 2005. We have provided a full valuation allowance against all of our U.S. federal and state deferred tax assets. The valuation allowance is determined in accordance with the provisions of Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes*, ("SFAS 109"), which requires an assessment of both negative and positive evidence when measuring the need for a valuation allowance. Our losses in recent periods represent sufficient negative evidence to require a valuation allowance under SFAS 109. This valuation allowance will be evaluated periodically and can be reversed partially or totally if business results have sufficiently improved to support realization of our deferred tax assets.

As of July 1, 2007, we had net operating loss carryforwards for federal and state tax purposes of $268.5 million and $45.6 million, respectively, of which $53.1 million and $21.3 million, respectively represent deductions from share-based compensation for which a benefit would be recorded in additional paid-in capital when realized. We also had federal and state tax credit carryforwards of $10.8 million and $14.8 million, respectively, as of July 1, 2007. Federal net operating loss carryforwards of $268.5 million will start to expire beginning 2021 through 2027 and state net operating losses of $45.6 million will expire between 2011 through 2017, if not utilized. Federal tax credits of $10.4 million will expire beginning 2012 through 2027 and state tax credits of $1.4 million will expire beginning 2008 through 2013, if not utilized. Under FAS 123R, the deferred tax asset for net operating losses excludes deductions for excess tax benefits related to share-based compensation.

Utilization of the net operating losses and tax credits may be subject to a substantial annual limitation due to the ownership change limitations provided by the Internal Revenue Code of 1986, as amended, and similar state provisions. The annual limitation may result in the expiration of net operating losses and tax credits before utilization.

EXTREME NETWORKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

9. Disclosure about Segments of an Enterprise and Geographic Areas

Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision makers with respect to the allocation of resources and performance.

We operate in one segment, the development and marketing of network infrastructure equipment. We conduct business globally and are managed geographically. Revenue is attributed to a geographical area based on the location of the customers.

Information regarding geographic areas is as follows (in thousands):

	Year Ended		
	July 1, 2007	July 2, 2006	July 3, 2005
Net revenues:			
United States	$ 137,364	$ 145,870	$ 167,027
Europe, Middle East and Africa	136,577	124,768	117,521
Japan	17,844	35,812	58,100
Other	51,049	52,151	40,699
	$ 342,834	$ 358,601	$ 383,347

Substantially all of our assets were attributable to United States operations at July 1, 2007 and July 2, 2006.

10. Net Income (Loss) Per Share

Basic earnings (loss) per share is calculated by dividing net income (loss) by the weighted average number of common shares outstanding during the period, less shares subject to repurchase, and excludes any dilutive effects of options, warrants and convertible subordinated notes. Dilutive earnings (loss) per share is calculated by dividing net income by the weighted average number of common shares used in the basic earnings (loss) per share calculation plus the dilutive effect of shares subject to repurchase, options, warrants and convertible subordinated notes. The following table presents the calculation of basic and diluted net income (loss) per share (in thousands, except per share data):

	Year Ended		
	July 1, 2007	July 2, 2006	July 3, 2005
Net income (loss)	$ (14,197)	$ 8,509	$ 12,519
Weighted-average shares used in per share calculation – basic	114,122	121,286	121,225
Incremental share using the treasury stock method	—	1,763	2,994
Weighted-average share used in per share calculation – diluted	114,122	123,049	124,219
Net income (loss) per share—basic	$ (0.12)	$ 0.07	$ 0.10
Net income (loss) per share—diluted	$ (0.12)	$ 0.07	$ 0.10

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

	Year Ended		
	July 1, 2007	July 2, 2006	July 3, 2005
Weighted Stock options outstanding:			
In-the-money options	1,552	—	—
Out-of-the-money options	20,366	19,578	15,642
Convertible subordinated notes	—	9,542	9,542
Total potential shares of common stock excluded from the computation of earnings per share	21,918	29,120	25,184

Weighted stock options outstanding representing common stock equivalents under the treasury method with an exercise price lower than the Company's average stock price for the periods presented ("In-the-money options") are excluded from the calculation of diluted net loss per share since the effect would have been anti-dilutive due to the net loss.

Weighted stock options outstanding with an exercise price higher than the Company's average stock price for the periods presented ("Out-of-the-money options") are excluded from the calculation of diluted net income (loss) per share since the effect would have been anti-dilutive under the treasury stock method.

The computation of diluted earnings (loss) per share for fiscal 2006 and fiscal 2005 excludes the impact of the conversion of the convertible subordinated notes, which are convertible into approximately 9.5 million shares of common stock, as the impact of adding back to income the after tax interest expense associated with the convertible subordinated notes, and including the impact of the common shares to be issued, would be anti-dilutive in the periods presented.

11. Foreign Currency Hedging

SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended and interpreted, requires that all derivatives be recorded on the balance sheet at fair value. Changes in the fair value of derivatives that do not qualify, or are not effective as hedges, must be recognized currently in earnings. Accordingly, we record the forward contracts used to manage foreign exchange exposures in prepaid expenses and other current assets on the consolidated balance sheets at fair value.

Foreign Exchange Exposure Management – We denominate substantially all global sales in U.S. dollars. International sales subsidiaries generate operating expenses in foreign currencies. We have a program of hedging forecasted and actual foreign currency risk with forward contracts to eliminate, reduce or transfer selected foreign currency risks that can be confidently identified and quantified. Hedges of anticipated transactions are designated and documented at inception as cash flow hedges and are evaluated for effectiveness at least quarterly. As the critical terms of the forward contract and the underlying are matched at inception, forward contract effectiveness is calculated by comparing the cumulative change in the contract (on a forward to forward basis) to the change in fair value of the anticipated expense, with the effective portion of the hedge recorded in accumulated other comprehensive income ("OCI"). Values accumulated in OCI are subsequently reclassified into the consolidated statement of operations line item to which the hedged transaction relates in the period the anticipated expense is recognized in income. Any ineffectiveness is recognized immediately in other expense. No ineffectiveness was recognized in other expense in fiscal 2007, fiscal 2006, or fiscal 2005.

Forward contracts used to hedge the remeasurement of non-functional currency monetary assets and liabilities are recognized in other expense currently to mitigate reported foreign exchange gains and losses. Forward contracts generally have maturities of 60 days or less.

12. Restructuring Charges and Technology Agreement

Restructuring Charges

As of July 1, 2007, restructuring liabilities were $14.0 million and consisted of obligations under excess facility operating leases, net of projected future sublease receipts, severance costs associated with a small reduction in force in the fourth quarter of fiscal 2007 impacting several functional areas, and certain contract termination costs to eliminate redundant activities. During fiscal 2007 and 2006, we recorded restructuring charges of $4.0 million and $3.3 million. The charges in fiscal 2007 included $1.1 million in the first through third quarter to rationalize our sales force in Japan, and $2.9 million in the fourth quarter to reduce headcount across several functional areas, terminate certain redundant contracts, and to exit an excess facility. The charge in fiscal 2006 was for an excess facilities charge and represented an increase to the charge initially recognized during the third quarter of fiscal 2002. The commercial real estate market continued to deteriorate in fiscal 2006 and we were not able to find suitable tenants to sublease these facilities necessitating an additional charge due to lower projected sublease receipts. At several of the facilities, we have not yet been able to find suitable tenants to sublease the facilities and the commercial real estate market in these areas continues to be weak. The lower projected sublease income necessitated an increase in the liability to take into consideration the unfavorable difference between lease obligation payments and projected sublease receipts. The actual costs could differ from our estimates, and additional adjustments to the restructuring liability could be recorded if we are able to negotiate reasonable termination fees on certain facilities, if facility sub-lease rental rates change, or if other estimates and assumptions change.

Restructuring liabilities consist of (in thousands):

	Excess Facilities	Asset Impairment	Contract Termination	Severance	Total
Balance at July 2, 2006	$17,042	—	—	—	$17,042
Charge in fiscal 2007	418	83	1,098	2,403	4,003
Cash Payments	(6,065)	—	—	(992)	(7,057)
Balance at July 1, 2007	11,395	83	1,098	1,411	13,988
Less: current portion	2,939	83	1,098	1,411	5,532
Restructuring liabilities at July 1, 2007, less current portion	$ 8,456	—	—	—	$ 8,456

Technology Agreement

On March 31, 2005, we entered into a Patent and Cross License Agreement ("Technology Agreement") with IBM. The agreement provides for a release of prior claims and a cross license of patents extending into the future from the effective date of the agreement. We charged the estimated value of the release of prior claims of $2.0 million to operating expenses in the quarter ended March 27, 2005 under the caption "Technology agreement". The remaining value under this agreement has been recognized in other assets and is being amortized to cost of product revenue over its contractual period using the straight-line method of amortization.

13. Alliance with Avaya

On October 30, 2003, Extreme Networks and Avaya Inc. entered into a strategic alliance to jointly develop and market converged communications solutions, by executing a Joint Development Agreement, and a distribution agreement under which Avaya is entitled to resell Extreme Networks products. Extreme issued to Avaya a warrant with a ten-year expiration period to purchase up to 2,577,794 shares of Extreme Networks common stock at a price of $0.01 per share, with Avaya having the right to exercise the warrant with respect to one third of such shares 90 days after the date of the agreements, and the remaining shares become exercisable based upon the completion of certain milestones by Avaya. Even if the milestones are not completed, however, the warrant will become fully exercisable for all shares 90 days prior to the expiration of the warrant. Avaya exercised the warrant with respect to approximately 859,000 of the shares subject to the warrant on March 17, 2004 and, approximately 859,000 of the shares subject to the warrant on August 8, 2005.

We engaged an independent valuation firm to assist us in estimating the fair value of the warrant and to assist us with the allocation of the fair value to the two agreements entered into. The independent valuation firm estimated the fair value of the warrant at $22.7 million, which has been allocated $17.9 million to the Joint Development Agreement and $4.8 million to the distribution agreement based on the assumptions by management related to the projected revenue and expenses for the respective agreements. The fair value of the warrant, net of accumulated amortization, is recorded in other assets in our consolidated balance sheets. The warrant values assigned to the respective agreements are being amortized over the terms of the agreements.

On October 31, 2005, the Joint Development Agreement was amended to, among other things, extend the term one additional year. The estimated amortization period was changed in the second quarter of fiscal 2006 to extend the amortization period over the remaining term of the amended Joint Development Agreement. The amortization of the warrant cost related to the Joint Development Agreement recorded as research and development expense was $3.0 million in fiscal 2007, as compared to $4.0 million in fiscal 2006. On October 14, 2004, the Distribution Agreement was amended to, among other things, extend the term by one additional year. During the quarter ended January 1, 2006, we determined that the amortization period for the portion of the warrant value assigned to the Distribution Agreement should have been extended when the term of the Distribution Agreement was extended in October 2004. We recorded the cumulative adjustment to the amortization of approximately $0.5 million in the quarter ended January 1, 2006. We concluded that the effect of this adjustment was not material to the affected prior annual or interim periods. The amortization of the warrant value related to the Distribution Agreement, recorded as a reduction of product revenue, was $1.1 million in fiscal 2007, compared to $0.7 million in fiscal 2006.

EXTREME NETWORKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

14. Quarterly Financial Data (Unaudited)

Quarterly results for the years ended July 1, 2007 and July 2, 2006 follow:

	July 1, 2007(1)	Apr 1, 2007(2)	Dec 31, 2006(3)	Oct 1, 2006(4)
	(In thousands, except per share amounts)			
Net revenues	$87,098	$85,119	$86,853	$83,763
Gross margin	$47,703	$47,866	$46,476	$43,151
Net income (loss)	$ (5,045)	$ (2,363)	$ (1,860)	$ (4,927)
Net income (loss) per share-basic	$ (0.04)	$ (0.02)	$ (0.02)	$ (0.04)
Net income (loss) per share-diluted	$ (0.04)	$ (0.02)	$ (0.02)	$ (0.04)

	July 2, 2006(5)	Apr 2, 2006(6)	Jan 1, 2006(7)	Oct 2, 2005(8)
Net revenues	$82,442	$85,450	$92,787	$97,922
Gross margin	$43,594	$46,212	$50,782	$53,288
Net income (loss)	$ (4,335)	$ 2,841	$ 5,650	$ 4,353
Net income (loss) per share-basic	$ (0.04)	$ 0.02	$ 0.05	$ 0.04
Net income (loss) per share-diluted	$ (0.04)	$ 0.02	$ 0.05	$ 0.03

(1) Net loss and net loss per share include the effect of stock-based compensation expense of $1.2 million, of which $0.1 million is the cumulative effect of modifying our estimated forfeiture rate for fiscal 2007 during the fourth quarter of such year, stock-option investigation expense of $1.3 million and a restructuring charge of $2.9 million.
(2) Net loss and net loss per share include the effect of stock-based compensation expense of $1.3 million, stock-option investigation expense of $2.8 million and a restructuring charge of $0.2 million.
(3) Net loss and net loss per share include the effect of stock-based compensation expense of $1.8 million, stock-option investigation expense of $2.8 million and a restructuring charge of $0.2 million.
(4) Net loss and net loss per share include the effect of stock-based compensation expense of $1.9 million and a restructuring charge of $1.5 million.
(5) Net loss and net loss per share include the effect of stock-based compensation expense of $2.2 million, of which $0.6 million is the cumulative effect of modifying our estimated forfeiture rate for fiscal 2006 during the fourth quarter of such year.
(6) Net income and net income per share include the effect of stock-based compensation expense of $1.3 million.
(7) Net income and net income per share include the effect of stock-based compensation expense of $1.6 million.
(8) Net income and net income per share include the effect of stock-based compensation expense of $1.9 million.

Quarterly and year-to-date computations of per share amounts are made independently. Therefore, the sum of per share amounts for the quarters may not agree with per share amounts for the year.

Item 9. ***Changes in and Disagreements with Accountants on Accounting and Financial Disclosure***

Not applicable.

Item 9A. ***Controls and Procedures***

Evaluation of Disclosure Controls and Procedures

Disclosure controls and procedures are controls and procedures designed to reasonably assure that information required to be disclosed in the Company’s reports filed under the Securities Exchange Act of 1934 (the “Exchange Act”), such as this Report, is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms and to reasonably assure that such information is accumulated and communicated to the Company’s management, including the Chief Executive Officer and the Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this Report. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of July 1, 2007.

Management’s Report on Internal Control over Financial Reporting

The Company’s management is responsible for establishing and maintaining adequate internal control over the company’s financial reporting. There are inherent limitations in the effectiveness of any system of internal control, including the possibility of human error and the circumvention or overriding of controls. Accordingly, even effective internal controls can provide only reasonable assurances with respect to financial statement preparation. Further because of changes in conditions, the effectiveness of internal control may vary over time.

The Company assessed the effectiveness of its internal control over financial reporting as of July 1, 2007. In making this assessment, we used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control-Integrated Framework.

Based on our assessment using those criteria, we concluded that, as of July 1, 2007, Extreme Networks Inc.’s internal control over financial reporting is effective.

Extreme Networks Inc.’s independent registered public accounting firm, Ernst & Young LLP, has audited the financial statements included in this Annual Report on Form 10-K and has issued its report on the Company’s internal control over financial reporting as of July 1, 2007. This report appears on page 99 of this Annual Report on Form 10-K.

Material Weakness in Prior Period

As described in our Annual Report on Form 10-K for the fiscal year ended July 1, 2006, management identified a material weakness in the Company’s internal control over financial reporting as of July 2, 2006, in that the design and operation of the Company’s internal controls were not effective to provide reasonable assurance that material errors in the Company’s historical share-based compensation would be detected, in that, in light of the circumstances that existed as of July 2, 2006, the Company lacked effective procedures to retrospectively identify as of that date the material accounting errors in the Company’s historical financial statements that were later discovered and which have now been corrected in connection with the restatement of the Company’s 2000 through 2005 consolidated financial statements in the 2006 Form 10-K. As a result, as of July 2, 2006, the Company’s internal control over financial reporting was not effective as it related to the Company’s ability to retrospectively identify material accounting errors resulting from the Company’s historical stock option grants. Additionally, the Company recorded a material adjustment to its consolidated balance sheet as of July 2, 2006 as a result of these errors. The principal accounts affected by this material weakness as of July 2, 2006 were common stock and accumulated deficit.

As a result of the above material weakness, the Company concluded that, as of July 2, 2006, the Company's internal control over financial reporting was not effective.

Remedial Measures Instituted by Extreme

On September 11, 2006, based on information developed by Company management and at the Audit Committee's recommendation, the Board of Directors formed the Special Committee to conduct an independent review of our historical practices for granting and accounting for stock options and to present findings and recommendations to the Board. The Special Committee completed its independent review and the results of the review, including the restatement of the Company's 2000 through 2005 consolidated financial statements reported in our fiscal 2006 Form 10-K. The completion of the Special Committee's independent review effectively remediated the material weakness in internal controls over financial reporting related to the ability to retrospectively identify the material accounting errors in the Company's historical financial statements that existed as of July 2, 2006.

The Special Committee found that the Company's options granting and documentation processes improved substantially following the passage of the Sarbanes-Oxley Act of 2002 and the implementation of new controls and procedures under the current Vice President of Human Resources (who joined the Company in May 2003) and the current Vice President, Corporate Business Development, General Counsel and Secretary (who joined the Company in February 2004). The Company determined that its procedures were effective in enabling the Company to appropriately determine measurement date(s) for options grants made subsequent to fiscal 2004, and that the Company's controls during the periods from the end of fiscal 2004 through fiscal 2006 were effective in enabling the Company to properly account for stock option grants made during that period. The material weakness identified by the Company as of July 2, 2006 did not affect the Company's internal controls related to recording of and accounting for stock options granted during that period.

The Special Committee recommended, and the Board adopted, new processes with regard to grants of equity compensation awards to Board members, officers, and non-officer employees alike, a summary of which is as follows:

- The general practice for grants to all new hires, and for out of cycle promotions and merit purposes will be to make such grants once per quarter, during open trading windows only, on the second trading day following the public announcement of quarterly financial results, pursuant to a list to be circulated to the appropriate granting authority prior to the proposed approval date.
- All grants to Officers, Vice Presidents and members of the Board of Directors are to be approved by the Board.
- All other grants are to be approved by the Compensation Committee.
- Grants are to be approved at Board or Compensation Committee meetings (not by UWC, except in extraordinary circumstances).
- There is to be no delegated granting authority to management.
- The Board and management are to continue monitoring processes and policies recommended by the SEC, self-regulatory authorities and outside advisors.
- All Board and Committee minutes are to be circulated to the directors as soon as reasonably practicable (generally, within two weeks of meeting). Counsel should attend all Board and Compensation Committee meetings.

- The Board has directed management to propose a mechanism for monitoring compliance with and reporting to the Board on the Company's policies and procedures relating to options grants.

These new processes adopted by the Board in April 2007 are designed to ensure that the Company continues to employ best practices and procedures with respect to equity compensation awards.

Changes in Internal Control over Financial Reporting

Other than the changes described under "Remedial Measures Instituted by Extreme" above, there were no changes in our internal control over financial reporting during the quarter ended July 1, 2007 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 9B. ***Other Information***

Not applicable.

Report of Independent Registered Public Accounting Firm on Internal Control Over Financial Reporting

The Board of Directors and Stockholders
Extreme Networks, Inc.

We have audited Extreme Networks, Inc.'s internal control over financial reporting as of July 1, 2007 based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Extreme Networks, Inc.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of the effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Extreme Networks, Inc. maintained, in all material respects, effective internal control over financial reporting as of July 1, 2007, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Extreme Networks, Inc. as of July 1, 2007 and July 2, 2006 and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the three years in the period ended July 1, 2007 of Extreme Networks, Inc. and our report dated August 28, 2007 expressed an unqualified opinion thereon.

Ernst & Young LLP

Palo Alto, California
August 28, 2007

PART III

Certain information required by Part III is incorporated by reference from Extreme's definitive Proxy Statement to be filed with the Securities and Exchange Commission in connection with the solicitation of proxies for Extreme's 2007 Annual Meeting of Stockholders (the "Proxy Statement") not later than 120 days after the end of the fiscal year covered by this report, and certain information therein is incorporated in this report by reference.

Item 10. *Directors and Executive Officers of the Registrant*

The information required by this section is incorporated by reference from the information in the section entitled "Proposal 1—Election of Directors" in the Proxy Statement. The required information concerning executive officers of Extreme is contained in the section entitled "Executive Officers of the Registrant" in Part I, Item 1 of this Form 10-K.

Item 405 of Regulation S-K calls for disclosure of any known late filing or failure by an insider to file a report required by Section 16 of the Exchange Act. This disclosure is contained in the section entitled "Section 16(a) Beneficial Ownership Reporting Compliance" in the Proxy Statement and is incorporated herein by reference.

Information with respect to Item 406 of Regulation S-K is incorporated by reference to the information contained in the section captioned "Code of Ethics" in the Proxy Statement.

Item 11. *Executive Compensation*

The information required by this section is incorporated by reference from the information in the sections entitled "Directors' Compensation", "Executive Compensation" and "Report of the Compensation Committee on Executive Compensation" in the Proxy Statement.

Item 12. *Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters*

The information required by this section is incorporated by reference from the information in the section entitled "Security Ownership of Certain Beneficial Owners and Management" in the Proxy Statement.

The information required by this section regarding securities authorized for issuance under equity compensation plans is incorporated by reference from the information in the section entitled "Equity Compensation Plan Information" in the Proxy Statement.

Item 13. *Certain Relationships and Related Transactions*

The information required by this section is incorporated by reference from the information in the section titled "Certain Relationships and Related Transactions" in the Proxy Statement.

Item 14. *Principal Accountant Fees and Services*

The information required by this section is incorporated by reference from the information in the section titled "Principal Accountant Fees and Services" in the Proxy Statement.

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PART IV

Item 15. *Exhibits and Financial Statement Schedules*

(a) The following documents are filed as a part of this Form 10-K:

(1) Financial Statements:

Reference is made to the Index to Consolidated Financial Statements of Extreme Networks, Inc. under Item 8 in Part II of this Form 10-K.

(2) Financial Statement Schedules:

The following financial statement schedule of Extreme Networks, Inc. for the fiscal years ended July 1, 2007, July 2, 2006, and July 3, 2005 is filed as part of this Report and should be read in conjunction with the Consolidated Financial Statements of Extreme Networks, Inc.

All other schedules are omitted because they are not applicable or the required information is shown in the financial statements or notes thereto.

(3) Exhibits:

The exhibits listed below are required by Item 601 of Regulation S-K. Each management contract or compensatory plan or arrangement required to be filed as an exhibit to this Form 10-K has been identified.

Exhibit Number	Description of Document	Incorporated by Reference Form	Incorporated by Reference Filing Date	Incorporated by Reference Number	Filed Herewith
2.1	Form of Agreement and Plan of Merger between Extreme Networks, a California corporation, and Extreme Networks, Inc., a Delaware corporation.	S-1/A	03/11/99	2.1	
3.1	Certificate of Incorporation of Extreme Networks, Inc., a Delaware Corporation.	S-1	02/05/99	3.1	
3.2	Form of Certificate of Amendment of Certificate of Incorporation of Extreme Networks, Inc., a Delaware Corporation.	S-1	02/05/99	3.2	
3.4	Amended and Restated Bylaws of Extreme Networks, Inc.	8-K	10/31/06	99.1	
3.5	Restated Certificate of Incorporation of Extreme Networks, Inc.	10-K	09/26/01	3.5	
3.6	Certificate of Amendment of Restated Certificate of Incorporation of Extreme Networks, Inc.	10-K	09/26/01	3.6	
3.7	Certificate of Designation, Preferences and Rights of the Terms of the Series A Preferred Stock.	10-K	09/26/01	3.7	
4.1	Second Amended and Restated Rights Agreement dated January 12, 1998 between Extreme Network and certain stockholders.	S-1	02/05/99	4.1	
4.2	Rights Agreement dated April 27, 2001 between Extreme Networks, Inc. and Mellon Investor Services LLC.	8-K/A	06/07/01	4.2	
4.3	Indenture, dated December 5, 2001 between Extreme Networks, Inc. and State Street Bank and Trust Company of California, N.A.	S-3	02/26/02	4.3	

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Exhibit Number	Description of Document	Incorporated by Reference Form	Filing Date	Number	Filed Herewith
4.4	Registration Rights Agreement dated December 5, 2001 between Extreme Networks, Inc. and Goldman Sachs & Co., as representative.	S-3	02/26/02	4.4	
4.5	Warrant to Purchase Common Stock issued to Avaya, Inc.	S-3	01/28/04	4.1	
10.1	Form of Indemnification Agreement for directors and officers.	S-1	02/05/99	10.1	
10.2*	Amended 1996 Stock Option Plan and forms of agreements thereunder.	S-1	02/05/99	10.2	
10.3*	1999 Employee Stock Purchase Plan.	S-1	02/05/99	10.3	
10.4*	2000 Nonstatutory Stock Option Plan.	10-K	09/24/00	10.7	
10.5	Lease agreement dated July 28, 2000 between San Tomas Properties LLC, a Delaware limited liability company, as Landlord, and Extreme Networks, Inc, a Delaware Corporation, as Tenant.	10-Q	11/14/00	10.14	
10.6	Purchase Agreement dated November 29, 2001 between Extreme Networks, Inc. and Goldman Sachs & Co., as representative.	S-3	02/26/02	10.15	
10.7*	2001 Nonstatutory Stock Option Plan.	Schedule TO	10/31/01	(d)(9)	
10.8*	Consulting Agreement dated August 2, 2006 between Extreme Networks, Inc. and William Slakey	10-Q	6/28/07	10.9	
10.9*	Offer of Employment Letter dated August 18, 2006 from Extreme Networks, Inc. to Mark Canepa	8-K	09/05/06	99.1	
10.10*	Revised compensation policies for non-employee service on the Board of Directors and its committees.	8-K	10/31/06	Item 1.01	
10.11*	Extreme Networks, Inc. Fiscal 2007 Executive Incentive Bonus Plan.	8-K	11/21/06	99.1	
10.12*	Fiscal 2007 commission bonus plan for Senior Vice President, Sales.	8-K	11/21/06	Item 5.02	
10.13*	Offer Letter for Employment between Extreme Networks, Inc. and Karen Rogge dated as of March 13, 2007.	8-K	03/29/07	99.2	
10.14*	Extreme Networks, Inc. Fiscal 2008 Executive Incentive Bonus Plan.	8-K	08/06/07	99.1	
21.1	Subsidiaries of Registrant.				X
23.1	Consent of Independent Registered Public Accounting Firm.				X
24.1	Power of Attorney (see page 104 of this Form 10-K).				X
31.1	Section 302 Certification of Chief Executive Officer.				X
31.2	Section 302 Certification of Chief Financial Officer.				X
32.1	Section 906 Certification of Chief Executive Officer.				X
32.2	Section 906 Certification of Chief Financial Officer.				X

* Indicates management contract or compensatory plan or arrangement.

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SCHEDULE II

VALUATION AND QUALIFYING ACCOUNTS
YEARS ENDED JULY 1, 2007, JULY 2, 2006, AND JULY 3, 2005

Description	Balance at beginning of period	Charges to costs and expenses	Reversals to costs and expenses	Charged to other accounts(1)	(Deductions)	Balance at end of period
Year Ended July 3, 2005:						
Allowance for doubtful accounts	$ 1,378	$ 58	$ (110)	$ —	$ (79)	$ 1,247
Allowance for sales returns	$ 2,226	$ 1,344	$ (300)	$ —	$ (945)	$ 2,325
Allowance for distributor doubtful accounts	$ 724	$ 532	$ (100)	$ —	$ (537)	$ 619
Inventory write-downs	$ 6,365	$ 1,061	$ —	$ —	$ (2,636)	$ 4,790
Allowance for net deferred tax assets	$ 174,740	$ 1,055	$ —	$ —	$ —	$ 175,795
Year Ended July 2, 2006:						
Allowance for doubtful accounts	$ 1,247	$ 603	$ (883)	$ —	$ (280)	$ 687
Allowance for sales returns	$ 2,325	$ 1,014	$ (275)	$ —	$ (1,364)	$ 1,700
Allowance for distributor doubtful accounts	$ 619	$ 1,447	$ —	$ —	$ (1,766)	$ 300
Inventory write-downs	$ 4,790	$ 1,259	$ —	$ —	$ (913)	$ 5,136
Allowance for net deferred tax assets	$ 175,795	$ —	$ (17,184)	$ —	$ —	$ 158,611
Year Ended July 1, 2007:						
Allowance for doubtful accounts	$ 687	$ —	$ 87	$ —	$ (40)	$ 734
Allowance for sales returns	$ 1,700	$ 3,377	$ (221)	$ —	$ (3,087)	$ 1,769
Allowance for distributor doubtful accounts	$ 300	$ —	$ —	$ (75)	$ —	$ 225
Inventory write-downs	$ 5,136	$ 3,030	$ —	$ (1,737)	$ (3,497)	$ 2,932
Allowance for net deferred tax assets	$ 158,611	$ 8,029	$ —	$ —	$ —	$ 166,640

(1) In fiscal 2007, we transferred $1.7 million of non-RoHS compliant inventory to service inventory and $0.1 million from allowance for distributor doubtful accounts to allowance for doubtful accounts.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on August 30, 2007.

EXTREME NETWORKS, INC.

(Registrant)

By: /S/ KAREN M. ROGGE

Karen M. Rogge
Senior Vice President & Chief Financial Officer
August 30, 2007

POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Mark Canepa and Karen M. Rogge, and each of them, his or her true and lawful attorneys-in-fact, each with full power of substitution, for him or her in any and all capacities, to sign any amendments to this report on Form 10-K and to file the same, with exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, hereby ratifying and confirming all that each of said attorneys-in-fact or their substitute or substitutes may do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the date indicated:

/S/ GORDON L. STITT

Gordon L. Stitt
Chairman of the Board
August 30, 2007

/S/ MARK CANEPA

Mark Canepa
President, Chief Executive Officer, Director
(Principal Executive Officer)
August 30, 2007

/S/ KAREN M. ROGGE

Karen M. Rogge
Senior Vice President & Chief Financial Officer
(Principal Financial Officer)
August 30, 2007

/S/ MICHAEL J. PALU

Michael J. Palu
Vice President, Corporate Controller
(Principal Accounting Officer)
August 30, 2007

/S/ MIKE WEST

Mike West
Director
August 30, 2007

/S/ CHARLES CARINALLI

Charles Carinalli
Director
August 30, 2007

/S/ BOB L. COREY

Bob L. Corey
Director
August 30, 2007

/S/ KENNETH LEVY

Kenneth Levy
Director
August 30, 2007

/S/ HARRY SILVERGLIDE

Harry Silverglide
Director
August 30, 2007

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EXHIBIT INDEX

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3.6	Certificate of Amendment of Restated Certificate of Incorporation of Extreme Networks, Inc.	10-K	09/26/01	3.6	
3.7	Certificate of Designation, Preferences and Rights of the Terms of the Series A Preferred Stock.	10-K	09/26/01	3.7	
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4.3	Indenture, dated December 5, 2001 between Extreme Networks, Inc. and State Street Bank and Trust Company of California, N.A.	S-3	02/26/02	4.3	
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10.4*	2000 Nonstatutory Stock Option Plan.	10-K	09/24/00	10.7	
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10.6	Purchase Agreement dated November 29, 2001 between Extreme Networks, Inc. and Goldman Sachs & Co., as representative.	S-3	02/26/02	10.15	
10.7*	2001 Nonstatutory Stock Option Plan.	Schedule TO	10/31/01	(d)(9)	
10.8*	Consulting Agreement dated August 2, 2006 between Extreme Networks, Inc. and William Slakey	10-Q	6/28/07	10.9	

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10.11*	Extreme Networks, Inc. Fiscal 2007 Executive Incentive Bonus Plan.	8-K	11/21/06	99.1	
10.12*	Fiscal 2007 commission bonus plan for Senior Vice President, Sales.	8-K	11/21/06	Item 5.02	
10.13*	Offer Letter for Employment between Extreme Networks, Inc. and Karen Rogge dated as of March 13, 2007.	8-K	03/29/07	99.2	
10.14*	Extreme Networks, Inc. Fiscal 2008 Executive Incentive Bonus Plan.	8-K	08/06/07	99.1	
21.1	Subsidiaries of Registrant.				X
23.1	Consent of Independent Registered Public Accounting Firm.				X
24.1	Power of Attorney (see page 104 of this Form 10-K).				X
31.1	Section 302 Certification of Chief Executive Officer.				X
31.2	Section 302 Certification of Chief Financial Officer.				X
32.1	Section 906 Certification of Chief Executive Officer.				X
32.2	Section 906 Certification of Chief Financial Officer.				X

* Indicates management contract or compensatory plan or arrangement.

EXHIBIT 21.1

SUBSIDIARIES OF REGISTRANT

NAME	LOCATION
Extreme Networks International	Cayman Islands
Extreme Networks Japan K.K.	Japan
Extreme Networks Hong Kong Limited	Hong Kong
Extreme Networks IHC, Inc.	Delaware
Extreme Networks UK Limited	United Kingdom
Extreme Networks B.V.	The Netherlands
Extreme Networks GmbH	Germany
Extreme Networks Sarl	France
Extreme Networks Srl	Italy
Extreme Networks Canada, Inc.	Canada
Extreme Networks Korea, Ltd.	Korea
IHC Networks AB	Sweden
Extreme Networks Australia PTE, Ltd.	Australia
Extreme Networks EMEA	Dubai
Extreme Networks Argentina, SRL	Argentina
Extreme Networks Brasil, Ltda.	Brazil
Extreme Networks Mexico, Ltda.	Mexico
Extreme Networks Chile, Ltda.	Chile
Extreme Networks Singapore PTE, Ltd.	Singapore
Extreme Networks China Ltd.	China
Extreme Networks Spain, SL	Spain
Extreme Networks Switzerland GmbH	Switzerland
Extreme Networks India Private Limited	India
Extreme Networks Mauritius	Mauritius

Exhibit 23.1

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We consent to the incorporation by reference in the following Registration Statements:

Form Number	Registration Statement Number	Description
Form S-8	333-112831	Extreme Networks, Inc. Amended 1996 Stock Option Plan and 1999 Employee Stock Purchase Plan
Form S-3	333-112281	Common Stock Issuable on Exercise of Warrant
Form S-8	333-105767	Extreme Networks, Inc. Amended 1996 Stock Option Plan
Form S-8	333-76798	Extreme Networks, Inc. Amended 1996 Stock Option Plan
Form S-8	333-65636	Extreme Networks, Inc. 2001 Nonstatutory Stock Option Plan
Form S-8	333-58634	Extreme Networks, Inc. Individual Option Agreements Granted Under the Webstacks, Inc. 2000 Stock Option Plan and Assumed by Extreme Networks, Inc.
Form S-8	333-55644	Extreme Networks, Inc. Individual Option Agreements Granted Under the Optranet, Inc. 2000 Option Plan and Assumed by Extreme Networks, Inc.
Form S-8	333-54278	Extreme Networks, Inc. Amended 1996 Stock Option Plan, 1999 Employee Stock Purchase Plan and 2000 Nonstatutory Stock Option Plan
Form S-8	333-131705	Extreme Networks, Inc. 2005 Equity Incentive Plan and 1999 Employee Stock Purchase Plan

of our reports dated August 28, 2007, with respect to the consolidated financial statements and schedule of Extreme Networks, Inc. and Extreme Networks, Inc.'s internal control over financial reporting, included in this Annual Report (Form 10-K) for the year ended July 1, 2007.

Ernst & Young LLP

Palo Alto, California
August 28 , 2007

EXHIBIT 31.1

I, Mark Canepa, Chief Executive Officer of the Company, certify that:

1. I have reviewed this annual report on Form 10-K of Extreme Networks, Inc.;

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

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

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

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

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

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

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

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

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

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

Dated: August 30, 2007

/s/ MARK CANEPA

Mark Canepa
President, Chief Executive Officer

EXHIBIT 31.2

I, Karen M. Rogge, Senior Vice President and Chief Financial Officer, certify that:

1. I have reviewed this annual report on Form 10-K of Extreme Networks, Inc.;

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

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

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

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

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

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

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

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

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

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

Dated: August 30, 2007

/s/ KAREN M. ROGGE
Karen M. Rogge
Senior Vice President and Chief Financial Officer

EXHIBIT 32.1

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Extreme Networks, Inc. (the "Company") on Form 10-K for the fiscal year ended July 1, 2007, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, in the capacities and on the dates indicated below, each hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to the best of their knowledge:

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

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

/s/ MARK CANEPA
Mark Canepa
President, Chief Executive Officer
August 30, 2007

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

EXHIBIT 32.2

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Extreme Networks, Inc. (the "Company") on Form 10-K for the fiscal year ended July 1, 2007, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, in the capacities and on the dates indicated below, each hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to the best of their knowledge:

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

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

/s/ KAREN M. ROGGE

Karen M. Rogge
Senior Vice President and Chief Financial Officer
August 30, 2007

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.