COMTECH TELECOMMUNICATIONS CORP /DE/
Form 10-Q
June 07, 2011

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

FORM
10-Q

(Mark One)

T Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended April 30, 2011

o Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission File Number: 0-7928

(Exact name of registrant as specified in its charter)

| Delaware<br>(State or other jurisdiction of incorporation /organization) | 11-2139466<br>(I.R.S. Employer Identification Number) |
|---|---|
| 68 South Service Road, Suite 230, Melville, NY<br>(Address of principal executive offices) | 11747<br>(Zip Code) |

(631) 962-7000
(Registrant's telephone number, including area code)

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

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

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

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

As of June 2, 2011, the number of outstanding shares of Common Stock, par value $.10 per share, of the registrant was 26,039,841 shares.

---

COMTECH TELECOMMUNICATIONS CORP.
INDEX


| | | | Page |
|---|---|---|---|
| PART I. FINANCIAL INFORMATION | | | |
| | Item 1. | Condensed Consolidated Financial Statements | |
| | | Condensed Consolidated Balance Sheets – April 30, 2011 (Unaudited) and July 31, 2010 | 2 |
| | | Condensed Consolidated Statements of Operations – Three and Nine Months Ended April 30, 2011 and 2010 (Unaudited) | 3 |
| | | Condensed Consolidated Statements of Stockholders' Equity and Comprehensive Income – Nine Months Ended April 30, 2011 and 2010 (Unaudited) | 4 |
| | | Condensed Consolidated Statements of Cash Flows – Nine Months Ended April 30, 2011 and 2010 (Unaudited) | 5 |
| | | Notes to Condensed Consolidated Financial Statements | 7 |
| | Item 2. | Management's Discussion and Analysis of Financial Condition and Results of Operations | 23 |
| | Item 3. | Quantitative and Qualitative Disclosures about Market Risk | 42 |
| | Item 4. | Controls and Procedures | 42 |
| PART II. OTHER INFORMATION | | | |
| | Item 1. | Legal Proceedings | 43 |
| | Item 1A. | Risk Factors | 43 |
| | Item 2. | Unregistered Sales of Equity Securities and Use of Proceeds | 44 |
| | Item 6. | Exhibits | 45 |
| | | Signature Page | 46 |

PART I
FINANCIAL INFORMATION
COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

Item 1.

| Assets | April 30, 2011 (Unaudited) | July 31, 2010 |
|---|---|---|
| Current assets: | | |
| Cash and cash equivalents | $588,941,000 | 607,594,000 |
| Accounts receivable, net | 70,185,000 | 135,840,000 |
| Inventories, net | 81,428,000 | 73,562,000 |
| Prepaid expenses and other current assets | 7,722,000 | 8,876,000 |
| Deferred tax asset, net | 12,867,000 | 14,947,000 |
| Total current assets | 761,143,000 | 840,819,000 |
| | | |
| Property, plant and equipment, net | 28,177,000 | 33,727,000 |
| Goodwill | 137,354,000 | 137,354,000 |
| Intangibles with finite lives, net | 47,497,000 | 48,091,000 |
| Deferred financing costs, net | 4,169,000 | 4,675,000 |
| Other assets, net | 1,194,000 | 1,896,000 |
| Total assets | $979,534,000 | 1,066,562,000 |
| | | |
| Liabilities and Stockholders' Equity | | |
| Current liabilities: | | |
| Accounts payable | $17,828,000 | 77,844,000 |
| Accrued expenses and other current liabilities | 43,076,000 | 53,398,000 |
| Dividends payable | 6,521,000 | - |
| Customer advances and deposits | 16,416,000 | 12,780,000 |
| Interest payable | 3,031,000 | 1,531,000 |
| Income taxes payable | 3,397,000 | 8,666,000 |
| Total current liabilities | 90,269,000 | 154,219,000 |
| | | |
| Convertible senior notes | 200,000,000 | 200,000,000 |
| Other liabilities | 6,389,000 | 2,518,000 |
| Income taxes payable | 4,914,000 | 5,220,000 |
| Deferred tax liability | 4,047,000 | 2,973,000 |
| Total liabilities | 305,619,000 | 364,930,000 |
| | | |
| Commitments and contingencies (See Note 20) | | |
| | | |
| Stockholders' equity: | | |
| Preferred stock, par value $.10 per share; shares authorized and unissued 2,000,000 | - | - |
| Common stock, par value $.10 per share; authorized 100,000,000 shares; issued 28,662,144 shares and 28,542,535 shares at April 30, 2011 and July 31, 2010, respectively | 2,866,000 | 2,854,000 |
| Additional paid-in capital | 351,984,000 | 347,514,000 |
| Retained earnings | 387,321,000 | 351,449,000 |
| | 742,171,000 | 701,817,000 |

| | | |
|---|---|---|
| Less: | | |
| Treasury stock, at cost (2,576,807 shares and 210,937 shares at April 30, 2011 and July 31, 2010, respectively) | (68,256,000 ) | (185,000 ) |
| Total stockholders’ equity | 673,915,000 | 701,632,000 |
| Total liabilities and stockholders’ equity | $979,534,000 | 1,066,562,000 |

See accompanying notes to condensed consolidated financial statements.

2

COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

| | Three months ended April 30, | | Nine months ended April 30, | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| Net sales | $131,081,000 | 216,303,000 | 472,052,000 | 521,251,000 |
| Cost of sales | 74,110,000 | 141,512,000 | 289,937,000 | 333,185,000 |
| Gross profit | 56,971,000 | 74,791,000 | 182,115,000 | 188,066,000 |
| Expenses: | | | | |
| Selling, general and administrative | 22,552,000 | 25,628,000 | 69,742,000 | 70,256,000 |
| Research and development | 10,328,000 | 11,383,000 | 31,546,000 | 34,138,000 |
| Amortization of intangibles | 2,173,000 | 1,754,000 | 6,064,000 | 5,283,000 |
| Merger termination fee, net | - | - | (12,500,000) | - |
| | 35,053,000 | 38,765,000 | 94,852,000 | 109,677,000 |
| Operating income | 21,918,000 | 36,026,000 | 87,263,000 | 78,389,000 |
| Other expenses (income): | | | | |
| Interest expense | 2,135,000 | 1,980,000 | 6,288,000 | 5,913,000 |
| Interest income and other | (557,000) | (315,000) | (1,877,000) | (728,000) |
| Income before provision for income taxes | 20,340,000 | 34,361,000 | 82,852,000 | 73,204,000 |
| Provision for income taxes | 6,085,000 | 12,565,000 | 26,845,000 | 26,043,000 |
| Net income | $14,255,000 | 21,796,000 | 56,007,000 | 47,161,000 |
| Net income per share (See Note 6): | | | | |
| Basic | $0.54 | 0.77 | 2.05 | 1.67 |
| Diluted | $0.47 | 0.67 | 1.79 | 1.48 |
| Weighted average number of common shares outstanding – basic | 26,577,000 | 28,291,000 | 27,310,000 | 28,254,000 |
| Weighted average number of common and common equivalent shares outstanding – diluted | 32,378,000 | 34,086,000 | 33,069,000 | 34,074,000 |
| Dividends declared per issued and outstanding common share as of the applicable dividend record date | $0.25 | - | 0.75 | - |

See accompanying notes to condensed consolidated financial statements.

3

COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY AND COMPREHENSIVE INCOME
NINE MONTHS ENDED APRIL 30, 2011 AND 2010
(Unaudited)

| | Common Stock | | Additional | | Treasury Stock | | | |
|---|---|---|---|---|---|---|---|---|
| | | | Paid-in | Retained | | | Stockholders' | Comprehensive |
| | Shares | Amount | Capital | Earnings | Shares | Amount | Equity | Income |
| Balance July 31, 2009 | 28,390,855 | $2,839,000 | $335,656,000 | $290,819,000 | 210,937 | $(185,000 ) | $629,129,000 | |
| Equity-classified stock award compensation | - | - | 5,770,000 | - | - | - | 5,770,000 | |
| Proceeds from exercise of options | 91,697 | 9,000 | 1,468,000 | - | - | - | 1,477,000 | |
| Proceeds from issuance of employee stock purchase plan shares | 35,925 | 4,000 | 989,000 | - | - | - | 993,000 | |
| Excess income tax benefit from stock-based award exercises | - | - | 259,000 | - | - | - | 259,000 | |
| Net income | - | - | - | 47,161,000 | - | - | 47,161,000 | $47, |
| Balance April 30, 2010 | 28,518,477 | $2,852,000 | $344,142,000 | $337,980,000 | 210,937 | $(185,000 ) | $684,789,000 | $47, |
| | | | | | | | | |
| Balance July 31, 2010 | 28,542,535 | $2,854,000 | $347,514,000 | $351,449,000 | 210,937 | $(185,000 ) | $701,632,000 | |
| Equity-classified stock award compensation | - | - | 3,926,000 | - | - | - | 3,926,000 | |
| Proceeds from exercise of options | 82,795 | 8,000 | 1,297,000 | - | - | - | 1,305,000 | |
| Proceeds from issuance of employee stock purchase plan shares | 36,814 | 4,000 | 853,000 | - | - | - | 857,000 | |
| Cash dividends | - | - | - | (20,135,000 ) | - | - | (20,135,000 ) | |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Excess income tax benefit from stock-based award exercises | - | - | 154,000 | - | - | - | 154,000 | |
| Reversal of deferred tax assets associated with expired and unexercised stock-based awards | - | - | (1,760,000 ) | - | - | - | (1,760,000 ) | |
| Repurchases of common stock | - | - | - | - | 2,365,870 | (68,071,000) | (68,071,000 ) | |
| Net income | - | - | - | 56,007,000 | - | - | 56,007,000 | $56,( |
| Balance April 30, 2011 | 28,662,144 | $2,866,000 | $351,984,000 | $387,321,000 | 2,576,807 | $(68,256,000) | $673,915,000 | $56,( |

See accompanying notes to condensed consolidated financial statements.

4

COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

| | Nine months ended April 30, 2011 | 2010 |
|---|---|---|
| Cash flows from operating activities: | | |
| Net income | $56,007,000 | 47,161,000 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization of property, plant and equipment | 10,352,000 | 8,780,000 |
| Amortization of intangible assets with finite lives | 6,064,000 | 5,283,000 |
| Amortization of stock-based compensation | 3,977,000 | 5,758,000 |
| Deferred financing costs | 1,045,000 | 1,039,000 |
| (Gain) loss on disposal of property, plant and equipment | (1,000) | 87,000 |
| Provision for allowance for doubtful accounts | 302,000 | 159,000 |
| Provision for excess and obsolete inventory | 1,507,000 | 6,233,000 |
| Excess income tax benefit from stock award exercises | (154,000) | (252,000) |
| Deferred income tax expense (benefit) | 1,394,000 | (935,000) |
| Changes in assets and liabilities, net of effects of acquisitions and sale of certain assets and liabilities: | | |
| Accounts receivable | 65,353,000 | (28,377,000) |
| Inventories | (9,407,000) | 12,129,000 |
| Prepaid expenses and other current assets | 1,154,000 | 3,916,000 |
| Other assets | 702,000 | (715,000) |
| Accounts payable | (60,016,000) | 24,565,000 |
| Accrued expenses and other current liabilities | (9,473,000) | (4,373,000) |
| Customer advances and deposits | 3,478,000 | (8,513,000) |
| Other liabilities | 568,000 | 137,000 |
| Interest payable | 1,500,000 | 1,613,000 |
| Income taxes payable | (5,421,000) | 8,813,000 |
| Net cash provided by operating activities | 68,931,000 | 82,508,000 |
| | | |
| Cash flows from investing activities: | | |
| Purchases of property, plant and equipment | (4,768,000) | (4,202,000) |
| Purchases of other intangibles with finite lives | (50,000) | (113,000) |
| Proceeds from sale of certain assets and liabilities | - | 2,038,000 |
| Payments related to business acquisitions | (2,850,000) | - |
| Net cash used in investing activities | (7,668,000) | (2,277,000) |
| | | |
| Cash flows from financing activities: | | |
| Repurchases of common stock | (68,071,000) | - |
| Cash dividends paid | (13,614,000) | - |
| Proceeds from exercises of stock options | 1,305,000 | 1,477,000 |
| Proceeds from issuance of employee stock purchase plan shares | 857,000 | 993,000 |
| Excess income tax benefit from stock award exercises | 154,000 | 252,000 |
| Payment of contingent consideration related to business acquisition | (8,000) | - |
| Origination fees related to line of credit | (539,000) | (8,000) |
| Transaction costs related to issuance of convertible senior notes | - | (118,000) |

| | | |
|---|---|---|
| Net cash (used in) provided by financing activities | (79,916,000 ) | 2,596,000 |
| | | |
| Net (decrease) increase in cash and cash equivalents | (18,653,000 ) | 82,827,000 |
| Cash and cash equivalents at beginning of period | 607,594,000 | 485,450,000 |
| Cash and cash equivalents at end of period | $588,941,000 | 568,277,000 |

See accompanying notes to condensed consolidated financial statements.

(Continued)

COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)
(Unaudited)

| | Nine months ended April 30, | |
|---|---|---|
| | 2011 | 2010 |
| Supplemental cash flow disclosures: | | |
| Cash paid during the period for: | | |
| Interest | $3,309,000 | 3,132,000 |
| Income taxes | $31,150,000 | 18,436,000 |
| | | |
| Non cash investing and financing activities: | | |
| Cash dividends declared | $6,521,000 | - |
| Accrued business acquisition payments (See Note 18) | $4,066,000 | - |

See accompanying notes to condensed consolidated financial statements.

COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

## (1) General

The accompanying condensed consolidated financial statements of Comtech Telecommunications Corp. and Subsidiaries ("Comtech," "we," "us," or "our") as of and for the three and nine months ended April 30, 2011 and 2010 are unaudited. In the opinion of management, the information furnished reflects all material adjustments (which include normal recurring adjustments) necessary for a fair presentation of the results for the unaudited interim periods. Our results of operations for such periods are not necessarily indicative of the results of operations to be expected for the full fiscal year.

The preparation of our financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions that affect the reported amount of assets and liabilities, and disclosure of contingent assets and liabilities, at the date of the financial statements, and the reported amounts of revenues and expenses during the reported period. Actual results may differ from those estimates.

Our condensed consolidated financial statements should be read in conjunction with our audited consolidated financial statements, filed with the Securities and Exchange Commission ("SEC"), for the fiscal year ended July 31, 2010 and the notes thereto contained in our Annual Report on Form 10-K, and all of our other filings with the SEC.

## (2) Adoption of Accounting Standards Updates

The Financial Accounting Standards Board's ("FASB") Accounting Standards Codification ("ASC") is subject to updates by FASB, which are known as Accounting Standards Updates ("ASU"). The following are FASB ASUs which have been issued and incorporated into the FASB ASC and adopted by us:

On August 1, 2010, we adopted FASB ASU No. 2010-17, which is an update of FASB ASC 605 "Revenue Recognition - Milestone Method: Milestone Method of Revenue Recognition." ASU 2010-17 provides guidance on applying the milestone method to milestone payments for achieving specified performance measures when those payments are related to uncertain future events. The scope of ASU 2010-17 is limited to transactions involving research or development. During the nine months ended April 30, 2011, we did not have any research and development transactions with milestone payments that were covered under this ASU; thus, the adoption of this ASU did not have any impact on our Condensed Consolidated Statement of Operations or financial position.

On August 1, 2010, we adopted FASB ASU No. 2009-14, which amends FASB ASC 985 "Software." This FASB ASU indicates that tangible products containing both software and non-software components that function together to deliver the tangible product's essential functionality are no longer within the scope of the software revenue guidance in FASB ASC 985-605. This FASB ASU also requires that hardware components of a tangible product containing software components always be excluded from the software revenue guidance. Our adoption of this ASU did not have a material impact on our Condensed Consolidated Statement of Operations or financial position.

On August 1, 2010, we adopted FASB ASU No. 2009-13 which is an update of FASB ASC 605-25 "Revenue Recognition - Multiple-Element Arrangements." In addition to establishing a hierarchy for determining the selling price of a deliverable, this FASB ASU eliminates the residual method of allocation of arrangement consideration and instead requires use of the relative selling price method. Our adoption of this ASU did not have a material impact on our Condensed Consolidated Statement of Operations or financial position.

(3) Reclassifications

Certain reclassifications have been made to previously reported financial statements to conform to our current financial statement format.

7

## (4) Stock-Based Compensation

We issue stock-based awards to certain of our employees and our Board of Directors and we recognize related stock-based compensation for both equity and liability-classified stock-based awards in our condensed consolidated financial statements. These awards are issued pursuant to our 2000 Stock Option Plan and our 2001 Employee Stock Purchase Plan (the “ESPP”).

Stock-based compensation for equity-classified awards is measured at the date of grant, based on an estimate of the fair value of the award and is expensed over the vesting period of the grant. Stock-based compensation for liability-classified awards is determined the same way, except that the fair value of liability-classified awards is remeasured at the end of each reporting period until the award is settled, with changes in fair value recognized pro-rata for the portion of the requisite service period rendered.

Stock-based compensation for awards issued is reflected in the following line items in our Condensed Consolidated Statements of Operations:

| | Three months ended April 30, | | Nine months ended April 30, | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| Cost of sales | $ 88,000 | 159,000 | 361,000 | 466,000 |
| Selling, general and administrative expenses | 824,000 | 1,827,000 | 2,875,000 | 4,301,000 |
| Research and development expenses | 206,000 | 346,000 | 741,000 | 991,000 |
| Stock-based compensation expense before income tax benefit | 1,118,000 | 2,332,000 | 3,977,000 | 5,758,000 |
| Income tax benefit | (399,000 ) | (839,000 ) | (1,430,000) | (2,134,000) |
| Net stock-based compensation expense | $ 719,000 | 1,493,000 | 2,547,000 | 3,624,000 |

Of the total stock-based compensation expense before income tax benefit recognized in the three months ended April 30, 2011 and 2010, $60,000 and $72,000, respectively, related to awards issued pursuant to our ESPP. Of the total stock-based compensation expense before income tax benefit recognized in the nine months ended April 30, 2011 and 2010, $208,000 and $235,000, respectively, related to awards issued pursuant to our ESPP.

Included in total stock-based compensation expense before income tax benefit in the three months ended April 30, 2011 and 2010 is a benefit of $2,000 and $19,000, respectively, as a result of the required fair value remeasurement of our liability-classified stock appreciation rights (“SARs”) at the end of each of the respective reporting periods. Included in total stock-based compensation expense before income tax benefit in the nine months ended April 30, 2011 and 2010 is an expense of $8,000 and a benefit of $13,000, respectively, related to SARs.

Stock-based compensation that was capitalized and included in ending inventory at April 30, 2011 and July 31, 2010 was $117,000 and $159,000, respectively.

We estimate the fair value of stock-based awards using the Black-Scholes option pricing model. The Black-Scholes option pricing model includes assumptions regarding dividend yield, expected volatility, expected option term and risk-free interest rates. The assumptions used in computing the fair value of stock-based awards reflect our best estimates, but involve uncertainties relating to market and other conditions, many of which are outside of our control. Estimates of fair value are not intended to predict actual future events or the value ultimately realized by the employees who receive stock-based awards.

The per share weighted average grant-date fair value of stock-based awards granted during the three months ended April 30, 2011 approximated $7.28. There were no stock-based awards granted during the three months ended April 30, 2010. The per share weighted average grant-date fair value of stock-based awards granted during the nine months ended April 30, 2011 and 2010 approximated $7.24 and $9.32, respectively. In addition to the exercise and grant-date prices of these awards, we utilized certain weighted average assumptions to estimate the initial fair value of stock-based awards. These weighted average assumptions are listed in the table below:

| | Three months ended April 30, | | Nine months ended April 30, | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| Expected dividend yield | 3.59 % | - | 3.59 % | 0 % |
| Expected volatility | 38.00 % | - | 38.00 % | 38.00 % |
| Risk-free interest rate | 2.30 % | - | 2.24 % | 1.33 % |
| Expected life (years) | 5.28 | - | 5.27 | 3.50 |

Included in total stock-based compensation expense before income tax benefit for the three and nine months ended April 30, 2010, is an expense of approximately $494,000 which represents the estimated fair value of an increase in the respective contractual terms of 222,500 previously granted stock-based awards for eight employees. These stock-based awards were fully vested and their respective contractual lives were nearing expiration. In determining the fair value of the increase in contractual terms, we utilized the following weighted average assumptions: (i) expected life (in years) of 0.88; (ii) expected volatility of 32.93%; (iii) risk free interest rate of 0.33%; and (iv) expected dividend yield of 0%. There was no such modification or similar expense recorded in the three or nine months ended April 30, 2011.

Stock-based awards granted have exercise prices equal to the fair market value of the stock on the date of grant, a contractual term of five or ten years and a vesting period of three or five years. We settle employee stock option exercises with new shares. All SARs granted through April 30, 2011 may only be settled with cash. Included in accrued expenses at April 30, 2011 and July 31, 2010 is $82,000 and $74,000, respectively, relating to the cash settlement of SARs.

The expected dividend yield is the expected annual dividend as a percentage of the fair market value of the stock on the date of grant. For the stock-based awards granted during the nine months ended April 30, 2011, the expected dividend yield was equal to our targeted annual dividend of $1.00 per share divided by the quoted market price of our common stock on the date of the grant. We estimate expected volatility by considering the historical volatility of our stock, the implied volatility of publicly traded call options on our stock, the implied volatility of call options embedded in our 3.0% convertible senior notes and our expectations of volatility for the expected life of stock-based awards. The risk-free interest rate is based on the U.S. treasury yield curve in effect at the time of grant for an instrument which closely approximates the expected option term. The expected option term is the number of years we estimate that stock-based awards will be outstanding prior to exercise. Effective August 1, 2007, the expected life of awards issued was determined by employee groups with sufficiently distinct behavior patterns.

The following table provides the components of the actual income tax benefit recognized for tax deductions relating to the exercise of stock-based awards:

| | Nine months ended April 30, | |
|---|---|---|
| | 2011 | 2010 |
| Actual income tax benefit recorded for the tax deductions relating to the exercise of stock-based awards | $ 291,000 | $ 472,000 |
| Less: Tax benefit initially recognized on exercised stock-based awards vesting subsequent to the adoption of accounting standards that require us to expense stock-based awards | (137,000 ) | (213,000 ) |
| Excess income tax benefit recorded as an increase to additional paid-in capital | 154,000 | 259,000 |
| Less: Tax benefit initially disclosed but not previously recognized on exercised equity-classified stock-based awards vesting prior to the adoption of accounting standards that require us to expense stock-based awards | - | (7,000 ) |
| Excess income tax benefit from exercised equity-classified stock-based awards reported as a cash flow from financing activities in our Condensed Consolidated Statements of Cash Flows | $ 154,000 | $ 252,000 |

At April 30, 2011, total remaining unrecognized compensation cost related to unvested stock-based awards was $7,261,000, net of estimated forfeitures of $861,000. The net cost is expected to be recognized over a weighted average period of approximately 3.0 years.

As of April 30, 2011, the amount of hypothetical tax benefits related to stock-based awards was $24,350,000. During the three and nine months ended April 30, 2011, we recorded $523,000 and $1,760,000, respectively, as a reduction to additional paid-in capital, which represented the reversal of unrealized deferred tax assets associated with certain vested equity-classified stock-based awards that expired during the period.

In June 2011, our Board of Directors authorized, in accordance with our 2000 Stock Incentive Plan, the issuance of 648,750 stock-based awards. Total unrecognized stock-based compensation, net of estimated forfeitures, related to these awards was approximately $4,000,000. These awards have exercise prices equal to the fair market value of the stock on the date of grant, a contractual term of ten years and a vesting period of five years (except for 75,000 stock-based awards which have a contractual term of five years and a vesting period of three years).

## (5) Fair Value Measurements and Financial Instruments

We believe that the book value of our current monetary assets and liabilities approximates fair value as a result of the short-term nature of such assets and liabilities.

In accordance with FASB ASC 825, “Financial Instruments,” we determined that, as of April 30, 2011, the fair value of our 3.0% convertible senior notes was approximately $212,500,000 based on a quoted market price in an active market. Our 3.0% convertible senior notes are not marked-to-market and are shown on the accompanying balance sheet at their original issuance value. As such, changes in the estimated fair value of our 3.0% convertible senior notes are not recorded in our condensed consolidated financial statements.

As of April 30, 2011, we have approximately $205,815,000 of money market mutual funds which are classified as cash and cash equivalents in our Condensed Consolidated Balance Sheet. These money market mutual funds are

recorded at our estimate of their current fair value. FASB ASC 820, "Fair Value Measurements and Disclosures," requires us to define fair value as the price that would be received from the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. As such, using the fair value hierarchy described in FASB ASC 820, we valued our money market mutual funds using Level 1 inputs that were based on quoted market prices. As of April 30, 2011 we have no other assets, included in our Condensed Consolidated Balance Sheet, that are recorded at current fair value. If we acquire different types of assets or incur different types of liabilities in the future, we might be required to use different FASB ASC fair value methodologies.

## (6) Earnings Per Share

Our basic earnings per share (“EPS”) is computed based on the weighted average number of shares outstanding. Our diluted EPS reflects the dilution from potential common stock issuable pursuant to the exercise of equity-classified stock-based awards and convertible senior notes, if dilutive, outstanding during each period. When calculating our diluted earnings per share, we consider (i) the amount an employee must pay upon assumed exercise of stock-based awards; (ii) the amount of stock-based compensation cost attributed to future services and not yet recognized; and (iii) the amount of excess tax benefits, if any, that would be credited to additional paid-in capital assuming exercise of in-the-money stock-based awards. This excess tax benefit is the amount resulting from a tax deduction for compensation in excess of compensation expense, based on the Black Scholes option pricing model, recognized for financial reporting purposes.

Equity-classified stock-based awards to purchase 2,342,000 and 2,019,000 shares, for the three months ended April 30, 2011 and 2010, respectively, were not included in our diluted EPS calculation because their effect would have been anti-dilutive. Equity-classified stock-based awards to purchase 2,424,000 and 2,042,000 shares, for the nine months ended April 30, 2011 and 2010, respectively, were not included in our diluted EPS calculation because their effect would have been anti-dilutive. Liability-classified stock-based awards do not impact and are not included in the denominator for EPS calculations.

The following table reconciles the numerators and denominators used in our basic and diluted EPS calculations:

| | Three months ended April 30, | | Nine months ended April 30, | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| Numerator: | | | | |
| Net income for basic calculation | $ 14,255,000 | 21,796,000 | 56,007,000 | 47,161,000 |
| Effect of dilutive securities: | | | | |
| Interest expense (net of tax) on 3.0% convertible senior notes | 1,117,000 | 1,117,000 | 3,351,000 | 3,351,000 |
| Numerator for diluted calculation | $ 15,372,000 | 22,913,000 | 59,358,000 | 50,512,000 |
| Denominator: | | | | |
| Denominator for basic calculation | 26,577,000 | 28,291,000 | 27,310,000 | 28,254,000 |
| Effect of dilutive securities: | | | | |
| Stock options | 210,000 | 307,000 | 219,000 | 332,000 |
| Conversion of 3.0% convertible senior notes | 5,591,000 | 5,488,000 | 5,540,000 | 5,488,000 |
| Denominator for diluted calculation | 32,378,000 | 34,086,000 | 33,069,000 | 34,074,000 |

## (7) Accounts Receivable

Accounts receivable consist of the following:

| | April 30, 2011 | July 31, 2010 |
|---|---|---|
| Billed receivables from the U.S. government and its agencies | $ 23,349,000 | 89,843,000 |
| Billed receivables from commercial customers | 36,311,000 | 35,230,000 |
| Unbilled receivables on contracts-in-progress | 11,905,000 | 11,894,000 |
| Total accounts receivable | 71,565,000 | 136,967,000 |
| Less allowance for doubtful accounts | 1,380,000 | 1,127,000 |

| Accounts receivable, net | $ | 70,185,000 | 135,840,000 |
|---|---|---|---|

Unbilled receivables on contracts-in-progress include $2,735,000 and $11,430,000 at April 30, 2011 and July 31, 2010, respectively, due from the U.S. government and its agencies. There was $28,000 of retainage included in unbilled receivables at both April 30, 2011 and July 31, 2010. In the opinion of management, substantially all of the unbilled balances will be billed and collected within one year.

## (8) Inventories

Inventories consist of the following:

| | April 30, 2011 | July 31, 2010 |
|---|---|---|
| Raw materials and components | $ 59,903,000 | 55,380,000 |
| Work-in-process and finished goods | 35,226,000 | 31,973,000 |
| Total inventories | 95,129,000 | 87,353,000 |
| Less reserve for excess and obsolete inventories | 13,701,000 | 13,791,000 |
| Inventories, net | $ 81,428,000 | 73,562,000 |

At April 30, 2011 and July 31, 2010, the amount of total inventories expected to be used for long-term contracts (including contracts-in-progress) was $11,188,000 and $12,063,000, respectively.

Our MTS and BFT-1 contracts are known as "indefinite delivery/indefinite quantity" type contracts; thus, the U.S. Army is not obligated to purchase any additional products or services from us in the future. At April 30, 2011, $6,787,000 of our long-term contract inventory relates to our MTS and BFT-1 contracts. Almost all of this amount relates to MTS or BFT-1 orders already in our backlog. The remaining portion is expected to be used for incidental purchases and customer repairs. If we are left with inventories of unusable parts, we would likely have to write-off the remaining balance in the period that we make such determination.

At April 30, 2011 and July 31, 2010, $2,123,000 and $1,976,000, respectively, of the total inventory balance above related to contracts from third party commercial customers who outsource their manufacturing to us.

## (9) Accrued Expenses and Other Current Liabilities

Accrued expenses and other current liabilities consist of the following:

| | April 30, 2011 | July 31, 2010 |
|---|---|---|
| Accrued wages and benefits | $ 18,084,000 | 21,607,000 |
| Accrued warranty obligations | 8,846,000 | 10,562,000 |
| Accrued commissions and royalties | 4,329,000 | 2,997,000 |
| Accrued business acquisition payments | 492,000 | 1,350,000 |
| Other | 11,325,000 | 16,882,000 |
| Accrued expenses and other current liabilities | $ 43,076,000 | 53,398,000 |

We provide warranty coverage for most of our products for a period of at least one year from the date of shipment. We record a liability for estimated warranty expense based on historical claims, product failure rates and other factors. Some of our product warranties are provided under long-term contracts, the costs of which are incorporated into our estimates of total contract costs.

Changes in our product warranty liability during the nine months ended April 30, 2011 and 2010 were as follows:

| | April 30, 2011 | April 30, 2010 |
|---|---|---|
| Balance at beginning of period | $ 10,562,000 | 14,500,000 |
| Provision for warranty obligations | 5,976,000 | 5,330,000 |
| Reversal of warranty liability | (1,120,000 ) | (888,000 ) |
| Warranty obligation transferred with sale of certain assets and liabilities | - | (400,000 ) |
| Charges incurred | (6,572,000 ) | (6,677,000 ) |

| | | | |
|---|---|---|---|
| Balance at end of period | $ | 8,846,000 | 11,865,000 |

12

## (10) Cost Reduction Actions

Fiscal 2011 Cost Reduction Actions

During the nine months ended April 30, 2011, we began implementing certain cost reduction actions in all of our reportable operating segments. These cost reduction actions are expected to continue through the remainder of our fiscal 2011. In our mobile data communications segment, we continue to align staffing levels with expected future business activity. We are also continuing to reduce our manufacturing headcount in our telecommunications transmission segment to align with the expected lower level of manufacturing of products for our mobile data communications segment. In our RF microwave amplifiers segment we have reduced headcount and have yet to pay certain merit raises. In our unallocated or corporate segment, we have reduced headcount and continue to substantially reduce the use of outside consultants. To-date, all costs related to these actions (including severance), which are included in our Condensed Consolidated Statements of Operations for the three and nine months ended April 30, 2011, have not been material.

Fiscal 2010 Cost Reduction Actions

In August 2009, in connection with cost reduction actions we adopted in July 2009, we sold a small product line to a third party for $2,038,000.

Fiscal 2009 Radyne Acquisition-Related Restructuring Plan

In connection with our August 1, 2008 acquisition of Radyne, we immediately adopted a restructuring plan to achieve operating synergies for which we recorded approximately $2,713,000 of estimated restructuring costs. Of this amount, $613,000 relates to severance for Radyne employees which was paid in fiscal 2009. The remaining estimated amounts relate to facility exit costs and were determined as follows:

| | At August 1, 2008 |
|---|---|
| Total non-cancelable lease obligations | $ 12,741,000 |
| Less: Estimated sublease income | (8,600,000 ) |
| Total net estimated facility exit costs | 4,141,000 |
| Less: Interest expense to be accreted | (2,041,000 ) |
| Present value of estimated facility exit costs | $ 2,100,000 |

Our total non-cancelable lease obligations were based on the actual lease term which runs from November 1, 2008 through October 31, 2018. We estimated sublease income based on (i) the terms of a fully executed sublease agreement, whose lease term runs from November 1, 2008 through October 31, 2015 and (ii) our assessment of future uncertainties relating to the commercial real estate market. Based on our assessment of commercial real estate market conditions, we currently believe that it is not probable that we will be able to sublease the facility beyond the current sublease terms. As such, in accordance with grandfathered accounting standards that were not incorporated into the FASB's ASC, we recorded these costs, at fair value, as assumed liabilities as of August 1, 2008, with a corresponding increase to goodwill.

As of April 30, 2011, the amount of acquisition-related restructuring reserve is as follows:

| | Cumulative Activity Through April 30, 2011 |
|---|---|
| Present value of estimated facility exit costs at August 1, 2008 | $ 2,100,000 |
| Cash payments made | (3,050,000 ) |
| Cash payments received | 2,982,000 |

| | | |
|---|---|---|
| Accreted interest recorded | | 388,000 |
| Net liability as of April 30, 2011 | | 2,420,000 |
| Amount recorded as prepaid expenses in the Condensed Consolidated Balance Sheet | | 395,000 |
| Amount recorded as other liabilities in the Condensed Consolidated Balance Sheet | $ | 2,815,000 |

As of July 31, 2010, the present value of the estimated facility exit costs was $2,136,000. During the nine months ended April 30, 2011, we made cash payments of $736,000 and we received cash payments of $901,000. Interest accreted during the three and nine months ended April 30, 2011 was approximately $41,000 and $119,000, respectively, as compared to $34,000 and $113,000, respectively, for the three and nine months ended April 30, 2010, and is included in interest expense for each respective fiscal period.

As of April 30, 2011, future cash payments associated with our restructuring plan are summarized below:

| | As of April 30, 2011 |
|---|---|
| Future lease payments to be made in excess of anticipated sublease payments | $ 2,815,000 |
| Less expected net cash to be received in next twelve months | (395,000 ) |
| Interest expense to be accreted in future periods | 1,653,000 |
| Total remaining net cash payments | $ 4,073,000 |

(11) Credit Facility

We have a committed $150,000,000 unsecured revolving credit facility ("Credit Facility") with a syndicate of bank lenders. The Credit Facility, as amended on September 21, 2010, expires on January 31, 2014 and provides for the extension of credit to us in the form of revolving loans, including letters of credit, at any time and from time to time during its term, in an aggregate principal amount at any time outstanding not to exceed $150,000,000 for both revolving loans and letters of credit, with sub-limits of $15,000,000 for commercial letters of credit and $35,000,000 for standby letters of credit. The Credit Facility may be used for acquisitions, stock repurchases, dividends, working capital and other general corporate purposes.

At our election, borrowings under the Credit Facility will bear interest either at LIBOR plus an applicable margin or at the base rate plus an applicable margin. The interest rate margin over LIBOR ranges from 2.25 percent, up to a maximum amount of 2.75 percent. The base rate is a fluctuating rate equal to the highest of (i) the Prime Rate; (ii) the Federal Funds Effective Rate from time to time plus 0.5 percent; and (iii) two hundred (200) basis points in excess of the floating rate of interest determined, on a daily basis, in accordance with the terms of the agreement. The interest rate margin over the base rate ranges from 1.25 percent up to a maximum amount of 1.75 percent. In both cases, the applicable interest rate is based on the ratio of our consolidated total indebtedness to our consolidated earnings before interest, taxes, depreciation and amortization ("Consolidated EBITDA"). As defined in the Credit Facility, Consolidated EBITDA is adjusted for certain items.

The Credit Facility contains covenants, including covenants limiting certain debt, certain liens on assets, certain sales of assets and receivables, certain payments (including dividends), certain repurchases of shares of our common stock, certain sale and leaseback transactions, certain guaranties and certain investments. The Credit Facility also contains financial condition covenants including that we (i) maintain a minimum Consolidated EBITDA (as defined in the Credit Facility), measured on a consolidated basis based on the four prior consecutive fiscal quarters then ending; (ii) not exceed a maximum ratio of consolidated total indebtedness to Consolidated EBITDA (each as defined in the Credit Facility), and; (iii) maintain a minimum fixed charge ratio (as defined in the Credit Facility); in each case measured on the last day of each fiscal quarter.

The Credit Facility includes certain events of default, including: failure to make payments; failure to perform or observe terms, covenants and agreements; material inaccuracy of any representation or warranty; payment default relating to any indebtedness, as defined, with a principal amount in excess of $7,500,000 or acceleration of such indebtedness; occurrence of one or more final judgments or orders for the payment of money in excess of $7,500,000 that remain unsatisfied; incurrence of certain liabilities in connection with failure to maintain or comply with the Employee Retirement Income Security Act of 1974 ("ERISA"); any bankruptcy or insolvency; or a change of control, including if a person or group becomes the beneficial owner of 50 percent or more of our voting stock. If an event of default occurs, the interest rate on outstanding borrowings increases by an incremental default rate and the lenders may, among other things, terminate their commitments and declare all outstanding borrowings to be immediately due and payable together with accrued interest and fees. All amounts borrowed or outstanding under the Credit Facility are due and mature on January 31, 2014, unless the commitments are terminated earlier either at our

request or if certain events of default occur.

14

---

At April 30, 2011, we had $1,488,000 of standby letters of credit outstanding related to our guarantees of future performance on certain customer contracts and no outstanding commercial letters of credit.

At April 30, 2011, had borrowings been outstanding under the Credit Facility, the applicable interest rate margin above LIBOR and base rate borrowings would have been 2.50 percent and 1.50 percent, respectively. We are also subject to an undrawn line fee based on the ratio of our consolidated total indebtedness to our Consolidated EBITDA, as defined and adjusted for certain items in the Credit Facility. Interest expense, including amortization of deferred financing costs, related to our credit facility recorded during the three and nine months ended April 30, 2011 was $203,000 and $571,000, respectively, as compared to $165,000 and $464,000 during the three and nine months ended April 30, 2010, respectively.

The Credit Facility currently provides for, among other things, (i) an allowance of dividend payments of up to $30,000,000 during any four consecutive fiscal-quarter period (and the related exclusion of such amount from the calculation of the fixed charge coverage ratio), and (ii) an allowance of cash dividends (the portion of which amount is in excess of $30,000,000 during any four consecutive fiscal-quarter period) and equity security repurchases of $100,000,000 (and the related exclusion of such amount from the calculation of the fixed charge coverage ratio). The Credit Facility requires us to maintain $100,000,000 of unrestricted cash and cash equivalents and achieve certain amounts of Consolidated EBITDA (as defined in the Credit Facility) during any four consecutive fiscal-quarter period beginning with the fiscal quart