

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 28, 2002

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: _____

SILICON LABORATORIES INC.

(Exact name of registrant as specified in its charter)

Delaware

74-2793174

(State or other jurisdiction of incorporation or
organization)

(I.R.S. Employer
Identification No.)

4635 Boston Lane, Austin, Texas

78735

(Address of principal executive offices)

(Zip Code)

(512) 416-8500

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year,
if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports
required to be filed by Sections 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

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY
PROCEEDINGS DURING THE PRECEDING FIVE YEARS:

Indicate by check mark whether the registrant has filed all documents and
reports required to be filed by Sections 12, 13 or 15(d) of the Securities
Exchange Act of 1934 subsequent to the distribution of securities under a
plan confirmed by a court. Yes No

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer's classes of
common stock, as of the latest practicable date. As of October 9, 2002,
48,792,338 shares of common stock of Silicon Laboratories Inc. were outstanding.

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PART I: FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

SILICON LABORATORIES INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS, EXCEPT PER SHARE DATA)

SEPTEMBER 28, 2002	DECEMBER 29, 2002	2001	-----	----
----- (UNAUDITED) ASSETS				
Current assets: Cash and cash equivalents..... \$				
	68,943	\$ 82,346	Short-term	
investments.....				35,339
18,902	Accounts receivable, net of allowance for doubtful accounts of \$795 at September 28, 2002 and \$490 at December 29,			
2001.....	29,038	10,543		
Inventories.....	13,046	5,221	Deferred income	
taxes.....		2,268	2,268	
Prepaid expenses and				
other.....	2,065	3,073	-----	
----- Total current				
assets.....				150,699
122,353	Property, equipment and software, net.....	30,556	20,038	Goodwill and other intangible assets.....
424	199			
assets.....				
3,243	2,431	-----	-----	Total
----- LIABILITIES AND STOCKHOLDERS' EQUITY				
Current liabilities: Accounts payable..... \$				
	20,088	\$ 6,999	Accrued	
expenses.....				9,139
3,897	Deferred income on shipments to distributors.....	6,511	2,862	Current portion of long-term obligations.....
1,455	2,039			
Income taxes				
payable.....	1,957	--	--	
----- Total current				
liabilities.....				39,150
15,797	Long-term debt and leases.....	410	1,363	
	Other long-term obligations.....	2,725		
2,454	-----	-----	-----	Total
liabilities.....				
42,285	19,614	Stockholders' equity: Common stock -- \$.0001 par value; 250,000 shares authorized; 48,791 and 48,640 shares issued and outstanding at September 28, 2002 and December 29, 2001, respectively.....	5	5
	Additional paid-in			
capital.....	172,203	170,567		
	Stockholder notes			
receivable.....	(337)	(794)		
	Deferred stock			
compensation.....	(14,359)			

(18,603) Retained earnings (accumulated deficit).....	(14,875)	(25,768)	-----	--
----- Total stockholders' equity.....				
142,637				
125,407	----- Total liabilities and stockholders' equity.....			
\$184,922				
\$145,021	=====			

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.

SILICON LABORATORIES INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)
(IN THOUSANDS, EXCEPT PER SHARE DATA)

THREE MONTHS ENDED	NINE MONTHS ENDED		
-----	-----		
	----- SEPTEMBER 28,		
SEPTEMBER 29,	SEPTEMBER 28,	SEPTEMBER	SEPTEMBER
29, 2002	2001	2002	2001
-----	-----	-----	-----

Revenues.....				
\$51,786	\$ 19,925	\$121,819	\$ 50,482	
	Cost of			
revenues.....	22,747			
8,544	54,144	22,347	-----	-----
	----- Gross			
profit.....				
29,039	11,381	67,675	28,135	Operating
	expenses: Research and			
	development.....			
7,379	7,672			
23,637	21,251	Selling, general and		
	administrative.....			
8,653	5,362	23,627	14,197	Goodwill
	amortization.....			
				-- -- --
4,187	Impairment of goodwill and			
	other intangible			
assets.....	--	34,885	--	
34,885	Amortization of deferred stock			
	compensation.....			
1,293	1,319	3,906	3,981	-----
	----- Operating			
expenses.....	17,325			
49,238	51,170	78,501	-----	-----
	----- Operating income			
(loss).....	11,714	(37,857)		
	16,505 (50,366) Other income			
	(expense): Interest and other			
income.....	378	857	1,194	2,940
	Interest expense.....			
	(150)	(179)	(450)	(578)
	Equity			
	investment loss.....			
(313)	(313)	--	--	--
	----- Income (loss) before income			
taxes.....	11,629	(37,179)	16,936	
	(48,004) Provision (benefit) for			
	income			
taxes.....				
3,747	(651)	6,044	(2,002)	-----
	----- Net income			
(loss).....	\$ 7,882			
\$(36,528)	\$ 10,892	\$(46,002)	=====	=====
	===== Net income			
	(loss) per share:			
Basic.....	\$			
0.17	\$ (0.79)	\$ 0.23	\$ (1.01)	
Diluted.....	\$			
0.16	\$ (0.79)	\$ 0.21	\$ (1.01)	
	Weighted-average common shares			
	outstanding:			
Basic.....				
47,703	46,210	47,288	45,698	
Diluted.....				
50,519	46,210	50,902	45,698	THE

ACCOMPANYING NOTES ARE AN INTEGRAL

SILICON LABORATORIES INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)
(IN THOUSANDS)

NINE MONTHS ENDED -----	
SEPTEMBER 28, 2002	SEPTEMBER 29, 2001 -----
----- OPERATING ACTIVITIES Net income	
(loss).....	
\$10,892	\$(46,002) Adjustments to reconcile net income
(loss) to cash provided by operating activities:	
Depreciation and amortization of property, equipment	
and	
software.....	244
8,233	5,897 Amortization of goodwill, other
	intangible assets and other
assets.....	244
4,580	Impairment of goodwill and other intangible
assets.....	-- 34,885 Amortization of deferred stock
compensation.....	3,906 3,981 Amortization of
	note/lease end-of-term interest
payments.....	
144	242 Equity investment
loss.....	313 -- Income
tax benefit from exercise of stock options.....	374
212	Changes in operating assets and liabilities:
Accounts receivable.....	
(18,495)	2,927
Inventories.....	
(7,825)	1,386 Prepaid expenses and
other.....	(1,191) 108 Income
tax receivable.....	2,086
(1,467)	Other
assets.....	(12)
40	Accounts
payable.....	11,864
(1,496)	Accrued
expenses.....	5,115
941	Deferred income on shipments to
distributors.....	3,649 (103) Deferred income
taxes.....	-- (359) Income
taxes payable.....	1,957
(912)	----- Net cash provided by operating
activities.....	21,254 4,860 INVESTING
	ACTIVITIES Purchases of short-term
investments.....	(43,986)
(43,314)	Maturities of short-term
investments.....	27,663 62,538
	Purchases of property, equipment and
software.....	(17,528) (4,122) Equity
investment.....	
(1,326)	-- Purchases of other
assets.....	-- (821) --
-----	----- Net cash provided by (used in)
investing activities.....	(35,177) 14,281
	FINANCING ACTIVITIES Payments on long-term
debt.....	(1,261)
(1,130)	Payments on capital
leases.....	(276) (401)
	Proceeds from repayment of stockholder
notes.....	457 193 Proceeds from Employee
	Stock Purchase Plan..... 631 566 Net
	proceeds from exercises of stock
options.....	1,067 248 Repurchase and
cancellation of common stock.....	(98) --
-----	----- Net cash provided by (used in)
financing activities.....	520 (524) -----
---	--- Increase (decrease) in cash and cash
equivalents.....	(13,403) 18,617 Cash and cash
equivalents at beginning of period.....	82,346
51,902	----- Cash and cash equivalents at
end of period.....	\$68,943 \$ 70,519
=====	===== SUPPLEMENTAL DISCLOSURE OF CASH FLOW
	INFORMATION: Interest
paid.....	\$
221	\$ 332 ===== Income taxes

paid..... \$
 1,617 \$ 793 ===== THE ACCOMPANYING NOTES
 ARE AN INTEGRAL PART OF THESE CONDENSED CONSOLIDATED
 FINANCIAL STATEMENTS.

SILICON LABORATORIES INC.
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
 (UNAUDITED)
 SEPTEMBER 28, 2002

1. SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION

The condensed consolidated financial statements, other than the condensed consolidated balance sheet as of December 29, 2001, included herein are unaudited; however, they contain all normal recurring accruals and adjustments which, in the opinion of management, are necessary to present fairly the consolidated financial position of Silicon Laboratories Inc. and its subsidiaries (collectively, the "Company") at September 28, 2002, the consolidated results of its operations for the three and nine months ended September 28, 2002 and September 29, 2001 and the consolidated statements of cash flows for the nine months ended September 28, 2002 and September 29, 2001. All intercompany accounts and transactions have been eliminated. The results of operations for the three and nine months ended September 28, 2002 are not necessarily indicative of the results to be expected for the full year.

The accompanying unaudited condensed consolidated financial statements do not include certain footnotes and financial presentations normally required under accounting principles generally accepted in the United States. Therefore, these financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto for the year ended December 29, 2001, included in the Company's Form 10-K filed with the Securities and Exchange Commission on January 22, 2002.

INVENTORIES

Inventories are stated at the lower of cost, determined using the first-in, first-out method, or market. Inventories consist of the following (in thousands):

	SEPTEMBER 28, 2001	DECEMBER 29, 2001	SEPTEMBER 28, 2002
	-----	-----	-----
	(UNAUDITED)		Work in
progress.....	\$10,063	\$3,582	Finished
goods.....	2,983	1,639	\$13,046
	\$5,221	=====	=====

EQUITY METHOD INVESTMENTS

Where the Company has investments in affiliated companies in which it has the ability to exercise significant influence over operating and financial policies, but not control, these investments are accounted for using the equity method. When special conditions warrant, for example when the Company is the sole funding source for an affiliated company and the affiliated company has not generated sufficient cash flows to sustain its operations, the Company determines equity income measurement by using the Hypothetical Liquidation at Book Value (HLBV) method. The HLBV method is a balance-sheet oriented approach to equity method accounting and is calculated as the amount that the Company would receive or be obligated to pay if the affiliated company were to liquidate all of its assets at recorded amounts and distribute the cash to creditors and investors in accordance with their respective priorities.

The Company records investment loss under the caption "equity investment loss" in its condensed consolidated statement of operations.

OTHER COMPREHENSIVE INCOME

There were no material differences between net income (loss) and comprehensive income (loss) during any of the periods presented.

RECENT ACCOUNTING PRONOUNCEMENTS

In July 2001, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) Nos. 141 and 142, BUSINESS COMBINATIONS and GOODWILL AND OTHER INTANGIBLE ASSETS. SFAS No. 141 replaces Accounting Principles Board Opinion (APB) No. 16 and eliminates pooling-of-interests accounting prospectively. It also provides guidance on purchase accounting related to the recognition of intangible assets and accounting for negative goodwill. SFAS No. 142 changes the accounting for goodwill from an amortization method to an impairment-only approach. Under SFAS No. 142, goodwill will be tested annually and whenever events or circumstances occur indicating that goodwill might be impaired. SFAS No. 141 and SFAS No. 142 are effective for all business combinations completed after June 30, 2001. Upon a company's adoption of SFAS No. 142, a company ceases to amortize goodwill recorded for business combinations consummated prior to July 1, 2001, and intangible assets acquired prior to July 1, 2001 that do not meet the criteria for recognition under SFAS No. 141 are reclassified to goodwill. Companies are required to adopt SFAS No. 142 for fiscal years beginning after December 15, 2001. The Company adopted SFAS No. 142 on December 30, 2001, the beginning of fiscal 2002. In connection with the adoption of SFAS No. 142, the Company has performed a transitional goodwill impairment assessment. The adoption of SFAS No. 141 and SFAS No. 142 did not have a material impact on the Company's results of operations and financial position since the Company's existing balances of goodwill and other intangible assets were not significant.

In October 2001, the FASB issued SFAS No. 144, ACCOUNTING FOR THE IMPAIRMENT OR DISPOSAL OF LONG-LIVED ASSETS, which supersedes SFAS No. 121, ACCOUNTING FOR THE IMPAIRMENT OF LONG-LIVED ASSETS AND FOR LONG-LIVED ASSETS TO BE DISPOSED OF; however, it retains the fundamental provisions of that statement related to the recognition and measurement of the impairment of long-lived assets to be "held and used." In addition, the Statement provides more guidance on estimating cash flows when performing a recoverability test, requires that a long-lived asset to be disposed of other than by sale be classified as "held and used" until it is disposed of, and establishes more restrictive criteria to classify an asset as "held for sale." The Company adopted SFAS No. 144 on December 30, 2001. The adoption did not have a material impact on the results of operations or financial position of the Company.

SILICON LABORATORIES INC.
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
 (UNAUDITED)

EARNINGS (LOSS) PER SHARE

The following table sets forth the computation of basic and diluted net income (loss) per share (in thousands, except per share data):

THREE MONTHS ENDED	NINE MONTHS ENDED		---	
-----	-----		-----	
-----	SEPTEMBER 28,		SEPTEMBER	
-----	29, 2002	2001	2002	2001
-----	-----		-----	
--- Net income				
(loss).....	\$7,882	\$(36,528)	\$10,892	\$(46,002)
Basic: Weighted-average shares of common stock				
outstanding.....	48,782	48,455	48,757	48,375
Weighted-average shares of common stock subject to repurchase.....	(1,079)	(2,245)	(1,469)	(2,677)
-----	-----		-----	
Shares used in computing basic net income (loss) per share.....	47,703			
-----	46,210	47,288	45,698	-----
-----	-----		-----	
Effect of dilutive securities: Weighted-average shares of common stock subject to repurchase.....	818	--	1,249	--
-----	-----		-----	
Stock options.....	2,365			
-----	-----		-----	
Shares used in computing diluted net income (loss) per share.....	50,519			
-----	46,210	50,902	45,698	=====

=====	=====	Basic net income (loss)	
per share.....		\$ 0.17	\$ (0.79)
		\$ 0.23	\$ (1.01)
		Diluted net income	
(loss) per share.....		\$ 0.16	\$
		(0.79)	\$ 0.21
			\$ (1.01)

Approximately 3,782,000 and 4,120,000 common shares have been excluded from the diluted loss per share calculation for the three and nine months ended September 29, 2001, respectively, as their impact would have been anti-dilutive.

2. SEGMENT REPORTING

The Company has one operating segment, mixed-signal communication integrated circuits (ICs), consisting of eight product lines. The Company's chief operating decision maker is considered to be the Chief Executive Officer and Chairman of the Board. The chief operating decision maker allocates resources and assesses performance of the business and other activities at the operating segment level.

3. EQUITY INVESTMENT IN A NON-PUBLICLY TRADED COMPANY

On June 14, 2002, the Company made an equity investment in a start-up venture, ASIC Design Services, Inc. (ADS), with an initial investment of \$1.3 million in the form of convertible-preferred stock. ADS is engaged in the design and development of proprietary integrated circuits (ICs) used in networking devices.

The Company has a contingent obligation to make two additional convertible-preferred stock investments in ADS totaling \$2.7 million based on ADS' achievement of certain milestones and the satisfaction of other conditions. Additionally, the Company has an exclusive right, but not the obligation, to purchase ADS for \$15 million in cash or common stock in connection with the occurrence of certain events.

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SILICON LABORATORIES INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(UNAUDITED)

At September 28, 2002, the Company's voting interest in ADS was less than 20% of the total ownership of ADS. However, the Company determined, based on APB Opinion No. 18 "THE EQUITY METHOD OF ACCOUNTING FOR INVESTMENTS IN COMMON STOCK" and other relevant guidance that it has the ability to exercise significant influence, but not control, over the management of ADS as a result of its contractual rights, rights as an equity stockholder and ability to designate a member of ADS' Board of Directors, which the Company has done. Therefore, the Company has accounted for its investment in ADS using the HLBV method under the equity method of accounting. The Company is using the HLBV method to determine its equity investment loss because the Company believes that it is unlikely that the other stockholders could bear their proportionate share of ADS' loss. Under this method, the Company's loss is equivalent to ADS' cash expenditures for the period.

For the three months ended September 28, 2002, the Company recorded an equity investment loss of \$0.3 million from its investment in ADS.

4. COMMITMENTS AND CONTINGENCIES

The Company is involved in various legal proceedings that have arisen in the normal course of business. While the ultimate results of these matters cannot be predicted with certainty, management does not expect them to have a material adverse effect on the consolidated financial position or results of operations.

On August 7, 2001, TDK Semiconductor Corporation commenced a lawsuit against the Company for alleged willful infringement by its direct access arrangement (DAA) products of a TDK-held patent. TDK's complaint seeks unspecified treble damages, costs and attorneys' fees, and an injunction. On September 27, 2001, the Company served and filed an answer to TDK's complaint, in which the Company denied infringement and asserted that TDK's patent is invalid. On March 27, 2002, the Company filed an amended answer and counterclaims in which the Company claimed that the TDK-held patent is unenforceable due to inequitable conduct and asserted counterclaims seeking a declaration that the TDK-held patent is invalid, not infringed and unenforceable. We are currently in the discovery phase of this litigation. This lawsuit has involved, and may continue to involve, significant expense and may also divert management's time and attention from other aspects of the Company's business. The Company intends to vigorously contest this case, however, the Company is unable at this time to determine whether the outcome of the litigation will have a material impact on its results of operations or financial condition in any future period.

On December 6, 2001, a class action complaint for violations of U.S. federal securities laws was filed in the United States District Court, Southern District of New York against the Company, four of its officers individually and the three investment banking firms who served as representatives of the underwriters in connection with the Company's initial public offering of common stock which became effective on March 23, 2000. On April 19, 2002, a consolidated amended complaint was filed in the same court. The action is being coordinated with over 300 other nearly identical actions filed against other companies. These claims are premised on allegations that the registration statement and prospectus for the Company's initial public offering did not disclose that (1) the underwriters solicited and received additional, excessive and undisclosed commissions from certain investors, and (2) the underwriters had agreed to allocate shares of the offering in exchange for a commitment from the customers to purchase additional shares in the aftermarket at pre-determined higher prices. A court order dated October 9, 2002 dismissed without prejudice numerous individual defendants, including the four officers of the Company who had been named individually. The Company intends to vigorously contest this case, however, the Company is unable at this time to determine whether the outcome of the litigation will have a material impact on its results of operations or financial condition in any future period.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

THE FOLLOWING DISCUSSION SHOULD BE READ IN CONJUNCTION WITH THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS AND RELATED NOTES THERETO INCLUDED ELSEWHERE IN THIS QUARTERLY REPORT ON FORM 10-Q AND OUR ANNUAL REPORT ON FORM 10-K FILED JANUARY 22, 2002. EXCEPT FOR THE HISTORICAL FINANCIAL INFORMATION CONTAINED HEREIN, THE MATTERS DISCUSSED IN THIS QUARTERLY REPORT ON FORM 10-Q MAY BE CONSIDERED "FORWARD-LOOKING" STATEMENTS WITHIN THE MEANING OF SECTION 27A OF THE SECURITIES ACT OF 1933, AS AMENDED, AND SECTION 21E OF THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED. SUCH STATEMENTS INCLUDE DECLARATIONS REGARDING THE INTENT, BELIEF OR CURRENT EXPECTATIONS OF OUR COMPANY AND MANAGEMENT AND MAY BE SIGNIFIED BY THE WORDS "EXPECTS," "ANTICIPATES," "INTENDS," "BELIEVES" OR SIMILAR LANGUAGE. PROSPECTIVE INVESTORS ARE CAUTIONED THAT ANY SUCH FORWARD-LOOKING STATEMENTS ARE NOT GUARANTEES OF FUTURE PERFORMANCE AND INVOLVE A NUMBER OF RISKS AND UNCERTAINTIES. ACTUAL RESULTS COULD DIFFER MATERIALLY FROM THOSE INDICATED BY SUCH FORWARD-LOOKING STATEMENTS. FACTORS THAT COULD CAUSE OR CONTRIBUTE TO SUCH DIFFERENCES INCLUDE THOSE DISCUSSED BELOW, AS WELL AS THOSE DISCUSSED IN OUR ANNUAL REPORT ON FORM 10-K FILED WITH THE SECURITIES AND EXCHANGE COMMISSION ON JANUARY 22, 2002. OUR FISCAL YEAR-END FINANCIAL REPORTING PERIODS ARE A 52- OR 53- WEEK YEAR ENDING ON THE SATURDAY CLOSEST TO DECEMBER 31ST. OUR THIRD QUARTER OF FISCAL YEAR 2002 ENDED SEPTEMBER 28, 2002. OUR THIRD QUARTER OF FISCAL YEAR 2001 ENDED SEPTEMBER 29, 2001. ALL OF THE QUARTERLY PERIODS REPORTED IN THIS QUARTERLY REPORT ON FORM 10-Q HAD THIRTEEN WEEKS.

OVERVIEW

We design and develop proprietary, analog-intensive, mixed-signal integrated circuits (ICs) for the communications industry. Our innovative ICs can dramatically reduce the cost, size and system power requirements of the products that our customers sell to consumers. We currently offer ICs that can be incorporated into communications devices, such as wireless phones and modems, as well as cable and satellite set-top boxes, residential communication gateways for cable or DSL, and optical network equipment. Customers during the first nine months of fiscal 2002 or fiscal 2001 included 3Com, Agere Systems, Ambit, Echostar, PC-TEL, Samsung, Sendo, Smart Link, Solectron, Sony, Texas Instruments, Thomson and Wavecom.

Our company was founded in 1996. As of September 28, 2002 we had 343 employees, up from 279 at the end of fiscal 2001, 256 at the end of fiscal 2000 and 148 at the end of fiscal 1999. As a "fabless" semiconductor company, we rely on third-party semiconductor fabricators to manufacture the silicon wafers that reflect our IC designs. Each wafer contains numerous die, which are cut from the wafer to create a chip for an IC. We also rely on third-party assemblers to assemble and package these die prior to final product testing and shipping.

We offer numerous mixed-signal communication ICs across eight product lines. We commenced research and development for our first IC product, the DAA, in October 1996. We introduced our DAA product in the first quarter of fiscal 1998, and first received acceptance of this product for inclusion in a customer's device, which we refer to as a "design win", in March 1998. The first commercial shipment of our DAA product was made in April 1998. Based on the success of our family of DAA products, we achieved profitability in the fourth quarter of fiscal 1998. In 1999, we introduced a voice codec product, an ISModem product and our RF synthesizer product. In 2000, we introduced our ProSLIC product and a clock and data recovery product suitable for SONET physical layer applications. In 2001, we introduced several products, including a GSM transceiver chipset, a digital subscriber line analog front end and added several new optical

networking products. During the first nine months of 2002, our wireless products were responsible for almost half of our revenues. We have made significant progress in our revenue diversity. However, except for quarterly fluctuations, we expect to become more dependent on our wireless products for our future sales as, and to the extent, those products become more widely adopted by GSM handset manufacturers.

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Many of our customers purchase products indirectly from us through distributors and contract manufacturers. A customer purchasing through a contract manufacturer typically instructs such contract manufacturer to obtain our products and incorporate such products with other components for sale by such contract manufacturer to the customer. Although we actually sell the products to, and are paid by, the distributors and contract manufacturers, we refer to such end customer as our customer. During the first nine months of 2002, two customers in aggregate, represented, 26% of our revenues. Samsung, purchasing primarily through Uniquet, represented 15% of revenues, and Wavecom, purchasing through Solectron and other contract manufacturers, represented 11% of revenues. No other single customer accounted for more than 10% of our revenues during the first nine months of 2002. Uniquet, a distributor selling product to Samsung and several other customers, represented 19% of our total revenues. Edom Technology, a distributor selling products to several customers in Asia, represented 13% of our revenues.

The percentage of our revenues to customers located outside of the United States was 78% in the nine months ended September 28, 2002, 66% in fiscal 2001, 21% in fiscal 2000 and 7% in fiscal 1999. All of our revenues to date have been denominated in U.S. dollars. We believe that a large percentage of our revenues will continue to be made to customers outside of the United States as our products receive acceptance in international markets.

The sales cycle for the test and evaluation of our ICs can range from 1 month to 12 months or more. An additional 3 to 6 months or more may be required before a customer ships a significant volume of devices that incorporate our ICs. Due to this lengthy sales cycle, we may experience a significant delay between incurring expenses for research and development and selling, general and administrative efforts, and the generation of corresponding sales, if any. Consequently, if sales in any quarter do not occur when expected, expenses and inventory levels could be disproportionately high, and our operating results for that quarter and, potentially, future quarters would be adversely affected. Moreover, the amount of time between initial research and development and commercialization of a product, if ever, generally is substantially longer than the sales cycle for the product. Accordingly, if we incur substantial research and development costs without developing a commercially successful product, our operating results, as well as our growth prospects, could be adversely affected.

Our limited operating history and rapid growth across our product lines makes it difficult for us to assess the impact of seasonal factors on our business. Because many of our ICs are designed for use in consumer products such as PCs and wireless telephones, we expect that the demand for our products will be subject to seasonal demand resulting in increased sales in the third and fourth quarters of each year when customers place orders to meet holiday demand.

The following describes the line items set forth in our consolidated statements of operations:

REVENUES. Revenues are generated principally by sales of our ICs. We recognize revenue upon the transfer of title, which generally occurs upon shipment to our customers. Revenues are deferred on shipments to distributors until they are resold by such distributors. Our products typically carry a one-year replacement warranty. Our revenues are subject to variation from period to period due to the volume of shipments made within a period and the prices we charge for our products. The vast majority of our revenues were negotiated at prices that reflect a discount from the list prices for our products. These discounts are made for a variety of reasons, including to establish a relationship with a new customer, as an incentive for customers to purchase products in larger volumes, to provide profit margin to our distributors who resell our products or in response to competition. In addition, as a product matures, we expect that the average selling price for our products will decline due to the greater availability of competing products. The sales of our wireless products into the highly competitive GSM handset market are expected to comprise a larger percentage of our revenue, resulting in increased downward pressure on our average selling prices. Our ability to increase revenues in the future is dependent on increased demand for our established products and our ability to ship larger volumes of those products in response to such demand, as well as our ability to develop new products and subsequently achieve customer acceptance of newly introduced products.

COST OF REVENUES. Cost of revenues includes the cost of purchasing finished silicon wafers processed by independent foundries; costs associated with assembly, test and shipping of those products; costs of personnel and equipment associated with manufacturing support, logistics and quality assurance; costs of software royalties and amortization of software license costs associated with certain products; an allocated portion of our occupancy costs; and allocable depreciation of testing equipment and leasehold improvements. Generally, we depreciate equipment over four years on a straight line basis. We also depreciate our leasehold improvements over the shorter of the estimated useful life or the applicable lease term. Recently introduced products tend to have higher cost of revenues per unit due to initially low production volumes required by our customers and higher costs associated with new package variations. Generally, as production volumes for a product increase, unit production costs tend to decrease as our semiconductor fabricators and assemblers, and our internal test operation, achieve greater economies of scale for that product. Additionally, the cost of wafer procurement, which is a significant component of cost of goods sold, varies cyclically with overall demand for semiconductors and availability of supply from our subcontractors and foundries.

RESEARCH AND DEVELOPMENT. Research and development expense consists primarily of compensation and related costs of employees engaged in research and development activities and the related new product mask and wafer costs, as well as an allocated portion of our occupancy costs for such operations. We depreciate our research and development equipment over four years and amortize our purchased software from computer-aided design tool vendors over four years. Development activities include the design of new products and creation of new product masks and wafers and test methodologies to assure compliance with required specifications.

SELLING, GENERAL AND ADMINISTRATIVE. Selling, general and administrative expense consists primarily of personnel-related expenses, related allocable portion of our occupancy costs, sales commissions to independent sales representatives, professional fees, directors' and officers' liability insurance, patent litigation legal fees, other promotional and marketing expenses, and reserves for bad debt. Write offs of uncollectible accounts have been insignificant to date.

GOODWILL AMORTIZATION. Goodwill amortization through December 2001 includes the amortization of goodwill purchased in connection with our acquisitions of Krypton Isolation, Inc. (Krypton) in August 2000 and SNR Semiconductor Incorporated (SNR) in October 2000. Goodwill was amortized over four to five years using the straight line method. We adopted SFAS No. 142, GOODWILL AND OTHER INTANGIBLE ASSETS, at the end of December 2001 and accordingly have ceased amortization of its goodwill.

IMPAIRMENT OF GOODWILL AND OTHER INTANGIBLE ASSETS. Impairment of goodwill and other intangible assets reflects the charge to write-down that portion of the carrying value of goodwill and other intangible assets that are in excess of their fair market value.

AMORTIZATION OF DEFERRED STOCK COMPENSATION. In connection with the grant of stock options and direct issuances of stock to our employees, we recorded deferred stock compensation, representing, for accounting purposes, the difference between the exercise price of option grants, or the issuance price of direct issuances of stock, as the case may be, and the deemed fair value of our common stock at the time of such grants or issuances. The deferred stock compensation is amortized over the vesting period of the applicable options or shares, generally five to eight years. The amortization of deferred stock compensation is recorded as an operating expense.

INTEREST AND OTHER INCOME. Interest and other income reflects interest earned on average cash, cash equivalents and investment balances and the gain on the sale of fixed assets. We may from time to time elect to invest in tax-advantaged short-term investments yielding lower nominal interest proceeds.

INTEREST EXPENSE. Interest expense consists of interest on our long-term debt and capital lease obligations.

EQUITY INVESTMENT LOSS. Equity investment loss reflects our share of losses in our equity investment, ASIC Design Services, Inc. (ADS).

PROVISION (BENEFIT) FOR INCOME TAXES. We accrue a provision (benefit) for federal and state income tax at the applicable statutory rates adjusted for non-deductible expenses, research and development tax credits and interest income from tax-advantaged short-term investments.

RESULTS OF OPERATIONS

The following table sets forth our statement of operations data as a percentage of revenues for the periods indicated:

	THREE MONTHS ENDED		NINE MONTHS ENDED		
	2002	2001	2002	2001	
Revenues.....	100.0%	100.0%	100.0%	100.0%	Cost of revenues..... 43.9
	42.7	44.4	44.4		Gross profit..... 56.1
					57.3 55.6 55.6 Operating expenses:
					Research and development.....
	14.3	38.7	19.4	42.2	Selling, general and administrative... 16.7 27.1 19.4 28.1
					Goodwill amortization..... --
	--	--	8.3		Impairment of goodwill and other intangible assets..... -- 175.4 --
					69.1 Amortization of deferred stock compensation..... 2.5
	6.5	3.3	7.7		Operating expenses..... 33.5
	247.7	42.1	155.4		Operating income (loss)..... 22.6 (190.4)
					13.5 (99.8) Other income (expense):
					Interest and other income.....
					0.7 4.5 0.9 5.9 Interest expense..... (0.3) (1.0)
					(0.4) (1.2) Equity investment loss..... (0.6) -- (0.2) --
					Income (loss) before income taxes..... 22.4 (186.9)
					13.8 (95.1) Provision (benefit) for income taxes..... 7.2 (3.5) 4.9 (4.0) --
					Net income (loss)..... 15.2%
	(183.4)%	8.9%	(91.1)%		====

COMPARISON OF THE THREE AND NINE MONTHS ENDED SEPTEMBER 28, 2002 TO THE THREE AND NINE MONTHS ENDED SEPTEMBER 29, 2001.

REVENUES. Revenues for the three months ended September 28, 2002 were \$51.8 million, an increase of \$31.9 million, or 160%, from revenues of \$19.9 million in the three months ended September 29, 2001. Revenues for the nine months ended September 28, 2002 were \$121.8 million, an increase of \$71.3 million, or 141%, from revenues of \$50.5 million in the nine months ended September 29, 2001. The increases were primarily due to a significant growth in the sales of our non-DAA products, such as the Aero Transceiver, the RF Synthesizer, the ISModem and the ProSLIC, reflecting the growing market acceptance for those products.

GROSS PROFIT. Gross profit for the three months ended September 28, 2002 was \$29.0 million, or 56.1% of revenues, an increase of \$17.6 million, as compared with gross profit of \$11.4 million, or 57.3% of revenues, in the three months ended September 29, 2001. Gross profit for the nine months ended September 28, 2002 was \$67.7 million, or 55.6% of revenues, an increase of \$39.6 million, as compared with gross profit of \$28.1 million, or 55.6% of revenues, in the nine months ended September 29, 2001. The increases in gross profit dollars were primarily due to the substantial increase in sales volume and increased utilization of our testing capacity. The decrease in gross margin in the most recent quarter was primarily due to a greater portion of our sales being comprised of our lower margin wireless products. We anticipate that gross margins may fluctuate significantly in the future due to the effect of many factors including our ability to sell existing inventory on hand, our ability to successfully introduce and sell new products, market forces that impact the selling prices for existing and new products, the extent to which our competitors introduce new products to market, the revenue mix of products, variations in manufacturing production yields and future product cost considerations with our vendors. During fiscal 2002, the sales of our wireless products into the highly competitive GSM handset market have comprised a larger

percentage of our revenues, resulting in increased downward pressure on our average selling prices and gross margins.

RESEARCH AND DEVELOPMENT. Research and development expense for the three months ended September 28, 2002 was \$7.4 million, or 14.3% of revenues, which reflected a decrease of \$0.3 million, or 3.9%, as compared with research and development expense of \$7.7 million, or 38.7% of revenues, for the three months ended September 29, 2001. Research and development expense for the nine months ended September 28, 2002 was \$23.6 million, or 19.4% of revenues, which reflected an increase of \$2.3 million, or 10.8%, as compared with research and development expense of \$21.3 million, or 42.2% of revenues, for the nine months ended September 29, 2001. The decrease in dollar amount for the three month period ended September 28, 2002 was principally due to lower spending for engineering masks and wafers which was caused by the timing of our development cycle for new ICs. The increase in the dollar amount of research and development expense for the nine month period ended September 28, 2002 was principally due to continued product development activities, significant increases in new product development initiatives in wireless and moderate increases in spending in optical networking product development opportunities, usage of more expensive advanced silicon complementary metal oxide semiconductor (CMOS) processes, and increased spending to develop test methodologies for new products. As a percentage of revenues, research and development expense decreased significantly due to the substantial increase in revenues for the three and nine months ended September 28, 2002. We expect that research and development expense will increase in absolute dollars in future periods as we develop new ICs, and may fluctuate as a percentage of revenues due to changes in sales volume and new product development initiatives.

SELLING, GENERAL AND ADMINISTRATIVE. Selling, general and administrative expense for the three months ended September 28, 2002 was \$8.7 million, or 16.7% of revenues, which reflected an increase of \$3.3 million, or 61.1%, as compared to selling, general and administrative expense of \$5.4 million, or 27.1% of revenues, in the three months ended September 29, 2001. Selling, general and administrative expense for the nine months ended September 28, 2002 was \$23.6 million, or 19.4% of revenues, which reflected an increase of \$9.4 million, or 66.2%, as compared to selling, general and administrative expense of \$14.2 million, or 28.1% of revenues, in the nine months ended September 29, 2001. The increases in the dollar amount of selling, general and administrative expense were principally attributable to increased staffing and legal fees incurred during patent litigation. We expect to continue to incur significant legal expenses, fluctuating with case activity, for at least the remainder of this fiscal year as a result of the ongoing infringement lawsuit filed against us by TDK Semiconductor Corporation in August 2001. We expect that selling, general and administrative expense will increase in absolute dollars in future periods as we expand our sales channels, marketing efforts and administrative infrastructure. In addition, we expect selling, general and administrative expense to fluctuate as a percentage of revenues because of (1) the likelihood that indirect sales distribution channels, which typically entail the payment of commissions, will account for a larger portion of our revenues in future periods and, therefore, increase our selling, general and administrative expense relative to a direct sales force performing at satisfactory levels of productivity; (2) fluctuating usage of advertising to promote our products and, in particular, our newly introduced products; and (3) potential significant variability in our future sales volume.

GOODWILL AMORTIZATION. We did not incur goodwill amortization in the three or nine months ended September 28, 2002 due to the adoption of SFAS No. 142. Goodwill amortization for the three and nine months ended September 29, 2001 was zero and \$4.2 million, respectively. During the three months ended September 29, 2001, we wrote off our goodwill balances after determining that they were permanently impaired.

IMPAIRMENT OF GOODWILL AND OTHER INTANGIBLE ASSETS. During fiscal 2001, we performed an assessment of the carrying value of the Company's long-lived assets recorded in connection with our acquisitions of Krypton and SNR. As a result of this assessment, we concluded that the value of these assets had become permanently impaired and recorded charges of \$33.3 million to write off related goodwill and \$1.6 million to reduce the carrying value of related intangible assets to their fair value. There was no impairment of goodwill and other intangible assets for the three and nine months ended September 28, 2002.

AMORTIZATION OF DEFERRED STOCK COMPENSATION. We recorded deferred stock compensation for the difference between the exercise price of option grants or the issuance price of direct issuances of stock, as the case may be, and the deemed fair value of our common stock at the time of such grants or issuances. We are amortizing this amount over the vesting periods of the applicable options or restricted stock, which resulted in amortization expense of \$1.3 million and \$3.9 million for the three and nine months ended September 28, 2002, respectively, as compared to \$1.3 million and \$4.0 million for the three and

nine months ended September 29, 2001, respectively.

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INTEREST AND OTHER INCOME. Interest income for the three and nine months ended September 28, 2002 was \$0.4 million and \$1.2 million, respectively, as compared to \$0.9 million and \$2.9 million for the three and nine months ended September 29, 2001, respectively. The decreases were primarily due to lower interest rates on cash and short-term investments balances during the recent three and nine month periods.

INTEREST EXPENSE. Interest expense for the three and nine months ended September 28, 2002 was \$0.2 million and \$0.5 million, respectively, as compared to \$0.2 million and \$0.6 million for the three and nine months ended September 29, 2001, respectively. The decrease for the nine month period ended September 28, 2002 was due to lower debt and lease payable balances during the recent period.

EQUITY INVESTMENT LOSS. Equity investment loss for the three and nine months ended September 28, 2002 was \$0.3 million with respect to our investment in ADS. We did not have any equity investments, and therefore no corresponding losses, during the three and nine month periods ending September 29, 2001.

PROVISION (BENEFIT) FOR INCOME TAXES. Our effective tax provision rate, excluding the impact of goodwill amortization, impairment of goodwill and other intangible assets, and deferred stock compensation amortization, was 29.0% in the nine months ended September 28, 2002, as compared to our effective tax benefit rate of 40.5% in the nine months ended September 29, 2001. The current period's tax provision rate was lower than the prior comparable tax benefit rate primarily due to the current period's decreased tax benefit from the estimated research and development tax credit in proportion to the amount of the current period's pre-tax income.

LIQUIDITY AND CAPITAL RESOURCES

Our principal sources of liquidity as of September 28, 2002 consisted of \$104.3 million in cash, cash equivalents and short-term investments, in addition to our bank credit facility. Our bank credit facility is a revolving line of credit available for borrowings and letters of credit of up to the lesser of \$5.0 million or 80% of eligible accounts receivable at the bank's prime lending rate, which was 4.75% as of September 28, 2002. At September 28, 2002, a letter of credit for \$0.4 million related to a building lease was outstanding under the revolving line of credit and \$4.0 million was available for new borrowings or letters of credit.

The bank facility is secured by our accounts receivable, inventories, capital equipment and all other unsecured assets (excluding intellectual property). The line of credit prohibits the payment of cash dividends and requires the maintenance of tangible net worth and compliance with financial ratios which measure our immediate liquidity and our ongoing ability to pay back our outstanding obligations. We believe we were in compliance with all covenants at September 28, 2002.

We also have agreements with three institutional lenders for equipment financing to purchase or lease equipment, leasehold improvements and software. At September 28, 2002, the amount outstanding under these agreements was \$1.9 million. This indebtedness bears effective interest rates (including end-of-term interest payments of \$1.2 million) ranging from 12.5% to 14.6% per annum, is secured by certain equipment, and is repayable over approximately the next two years. Based on available liquidity, we anticipate that we may retire these obligations before their scheduled maturities.

During the nine months ended September 28, 2002, cash provided by operating activities was \$21.3 million, as compared to cash provided by operating activities of \$4.9 million during the nine months ended September 29, 2001. This increase in cash flow was primarily due to the net income generated during the period as a result of increased sales volume.

Due to the nature of our business, we experience working capital needs in the area of accounts receivable. Typically, we bill our customers, or their contract manufacturers, on an open account basis with net 30 day payment terms or other specific terms and conditions that may vary from account to account as individually negotiated with customers. As of September 28, 2002, we had a net accounts receivable balance of \$29.0 million. The recent increase in our accounts receivable balance is attributable primarily to increased sales levels rather than to customers delaying their payments.

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We also experience working capital needs in the area of inventory. We believe that in order to maintain an adequate supply of product for our

customers, we must carry a certain level of inventory. This inventory level may vary based principally upon either orders received from customers or our forecast of demand for our products. Other factors influencing inventory levels may include the product life cycle stage of our products, customer demands for consignment inventory arrangements, and competitive situations in the marketplace. To address the difficult, subjective and complex area of judgment in determining appropriate inventory valuation in a consistent manner, we apply a set of methods, assumptions and estimates to arrive at the net inventory amount by completing the following procedures which collectively comprise a critical accounting policy. First, we identify any inventory that has been previously reserved in prior periods. This inventory remains reserved until sold, destroyed or otherwise disposed of. Second, we examine the inventory line items that may have some form of obsolescence due to non-conformance with electrical and mechanical standards as identified by our quality assurance personnel. Third, the remaining inventory not otherwise identified to be reserved is compared to an assessment of product history and forecasted demand, typically over the next six months, or actual firm backlog on hand. Finally, an analysis of the result of this methodology is compared against the product life cycle and competitive situations in the marketplace driving the outlook for the consumption of the inventory and the appropriateness of the resulting inventory levels. As of September 28, 2002, we had a net inventory balance of \$13.0 million, up from \$5.2 million as of December 29, 2001. The recent increase in our inventory balance is attributable primarily to increased levels to fulfill customer purchase orders and maintain an adequate supply based on our forecast of future customer demand.

Capital expenditures increased by \$12.6 million to \$17.5 million for the nine months ended September 28, 2002 from \$4.9 million for the nine months ended September 29, 2001. This increase in capital expenditures was primarily due to the purchase of additional semiconductor test equipment for wireless products for GSM mobile handsets. We anticipate additional capital expenditures of approximately \$2.5 million during fiscal 2002, primarily to fund additional test floor capabilities and new product development activities.

In June 2002, we entered into agreements with a newly-formed, privately-held company, ASIC Design Services, Inc. (ADS). These agreements cover (i) an initial equity investment by us in ADS of \$1.3 million; (ii) a contingent commitment by us to make additional equity investments in increments cumulatively totaling \$2.7 million based on ADS' achievement of certain milestones and the satisfaction of other conditions; (iii) ADS' grant to us of certain manufacturing, sales and marketing rights during ADS' early revenue phase, and; (iv) the right, but not the obligation, to acquire ADS in its entirety at a total acquisition value of \$15 million in cash or our common stock in connection with the occurrence of certain events.

The use of this structure provides us visibility and significant influence, but not control, over the direction of research and development activities of ADS. If we find the results of their development efforts to be desirable or advisable for full ownership, then we could exercise our right to acquire ADS. If we elect not to exercise our right to acquire ADS, we would still hold our preferred stock investment.

Our future capital requirements will depend on many factors, including the rate of sales growth, market acceptance of our products, the timing and extent of research and development projects and the expansion of our sales and marketing activities. We believe our existing cash balances and credit facilities are sufficient to meet our capital requirements through at least the next 12 months, although we could be required, or could elect, to seek additional funding prior to that time. We may enter into acquisitions or strategic arrangements in the future which also could require us to seek additional equity or debt financing. There can be no assurances that additional equity or debt financing, if required, will be available to us on acceptable terms or at all.

RECENT ACCOUNTING PRONOUNCEMENTS

In July 2001, the FASB issued SFAS Nos. 141 and 142, BUSINESS COMBINATIONS and GOODWILL AND OTHER INTANGIBLE ASSETS. SFAS No. 141 replaced APB No. 16 and eliminates pooling-of-interests accounting. It also provides guidance on purchase accounting related to the recognition of intangible assets and accounting for negative goodwill. SFAS No. 142 changes the accounting for goodwill from an amortization method to an impairment-only approach. Under SFAS No. 142, goodwill will be tested annually and whenever events or circumstances occur indicating that goodwill might be impaired. SFAS No. 141 and SFAS No. 142 are effective for all business combinations completed after June 30, 2001. Upon a company's adoption of SFAS No. 142, a company ceases to amortize goodwill recorded for business combinations consummated prior to July 1, 2001, and intangible assets acquired prior to July 1, 2001 that do not meet the criteria for recognition under SFAS No. 141 are reclassified to goodwill. Companies are

required to adopt SFAS No. 142 for fiscal years beginning after December 15, 2001. We adopted SFAS No. 142 on December 30, 2001, the beginning of fiscal 2002. In connection with the adoption of SFAS No. 142, we performed a transitional goodwill impairment assessment. The adoption of SFAS No. 141 and SFAS No. 142 did not have a material impact on our results of operations or financial position.

In October 2001, the FASB issued SFAS No. 144, ACCOUNTING FOR THE IMPAIRMENT OR DISPOSAL OF LONG-LIVED ASSETS, which supersedes SFAS No. 121, ACCOUNTING FOR THE IMPAIRMENT OF LONG-LIVED ASSETS AND FOR LONG-LIVED ASSETS TO BE DISPOSED OF; however, it retains the fundamental provisions of that statement related to the recognition and measurement of the impairment of long-lived assets to be "held and used." In addition, the Statement provides more guidance on estimating cash flows when performing a recoverability test, requires that a long-lived asset to be disposed of other than by sale be classified as "held and used" until it is disposed of, and establishes more restrictive criteria to classify an asset as "held for sale." The Company adopted SFAS No. 144 on December 30, 2001, but the adoption did not have a material impact on our results of operations or financial position.

QUALITATIVE AND QUANTITATIVE DISCLOSURE ABOUT MARKET RISK

Our interest income is sensitive to changes in the general level of U.S. interest rates, particularly since the majority of our investments are in short-term instruments. Due to the nature of our short-term investments, we have concluded that there is no material market risk exposure.

FACTORS AFFECTING OUR FUTURE OPERATING RESULTS

RISKS RELATED TO OUR BUSINESS

WE MAY NOT BE ABLE TO MAINTAIN OUR HISTORICAL GROWTH RATE AND MAY EXPERIENCE SIGNIFICANT PERIOD-TO-PERIOD FLUCTUATIONS IN OUR REVENUES AND OPERATING RESULTS, WHICH MAY RESULT IN VOLATILITY IN OUR STOCK PRICE

Although we have experienced revenue and earnings growth in our two most recent quarterly periods, we may not be able to sustain these growth rates. We may also experience significant period-to-period fluctuations in our revenues and operating results in the future due to a number of factors, and any such variations may cause our stock price to fluctuate. It is likely that in some future period our operating results will be below the expectations of public market analysts or investors. If this occurs, our stock price may drop, perhaps significantly.

A number of factors, in addition to those cited in other risk factors applicable to our business, may contribute to fluctuations in our revenues and operating results, including:

- the timing and volume of orders received from our customers;
 - the rate of acceptance of our products by our customers, including the acceptance of new products we may develop for integration in the products manufactured by such customers, which we refer to as "design wins";
 - the time lag between "design wins" and production orders;
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- the demand for, and life cycles of, the products incorporating our ICs;
 - the rate of adoption of mixed-signal ICs in the markets we target;
 - deferrals of customer orders in anticipation of new products or product enhancements from us or our competitors or other providers of ICs;
 - changes in product mix; and
 - the rate at which new markets emerge for products we are currently developing or for which our design expertise can be utilized to develop products for these new markets.

The mobile telephone market is characterized by rapid fluctuations in demand which results in corresponding fluctuations in the demand for our wireless products that are incorporated in mobile telephones. Additionally, the rate of technology acceptance by our customers results in fluctuating demand for our products as customers are reluctant to incorporate a new IC into their products until the new IC has achieved market acceptance. Once a new IC achieves market acceptance, demand for the new IC can quickly accelerate to a point and then level off such that rapid historical growth in sales of a product should not be viewed as indicative of continued future growth. In addition, demand can quickly decline for a product when a new IC product is introduced and receives market

acceptance. Accordingly, you should not rely on the results of any prior quarterly or annual periods as an indication of our future operating performance.

OUR INABILITY TO MANAGE GROWTH COULD MATERIALLY AND ADVERSELY AFFECT OUR BUSINESS

In recent periods, we have significantly increased the scope of our operations and expanded our workforce from 42 employees at January 2, 1999 to 343 employees at September 28, 2002. This growth has placed, and any future growth of our operations will continue to place, a significant strain on our management personnel, systems and resources. We anticipate that we will need to implement a variety of new and upgraded operational and financial systems, procedures and controls, including the improvement of our accounting and other internal management systems. We also expect that we will need to continue to expand, train, manage and motivate our workforce. All of these endeavors will require substantial management effort. If we are unable to effectively manage our expanding operations, our business could be materially and adversely affected.

IF WE ARE UNABLE TO DEVELOP NEW AND ENHANCED PRODUCTS THAT ACHIEVE MARKET ACCEPTANCE IN A TIMELY MANNER, OUR OPERATING RESULTS AND COMPETITIVE POSITION COULD BE HARMED

Our future success will depend on our ability to reduce our dependence on a few products by developing new ICs and product enhancements that achieve market acceptance in a timely and cost-effective manner. The development of mixed-signal ICs is highly complex, and we occasionally have experienced delays in completing the development and introduction of new products and product enhancements. Successful product development and market acceptance of our products depend on a number of factors, including:

- changing requirements of customers within the communications markets;
- accurate prediction of market requirements;
- timely completion and introduction of new designs;
- timely qualification and certification of our ICs for use in our customers' products;
- commercial acceptance and volume production of the products into which our ICs will be incorporated;
- availability of foundry, assembly, and test capacity;
- achievement of high manufacturing yields;
- quality, price, performance, power use and size of our products;

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- availability, quality, price and performance of competing products and technologies;
- our customer service and support capabilities and responsiveness;
- successful development of our relationships with existing and potential customers;
- changes in technology, industry standards or end-user preferences; and
- cooperation of software partners and semiconductor partners to support our chips within a system.

We cannot provide any assurance that products which we recently have developed or may develop in the future will achieve market acceptance. We have introduced to market or are in development of many ICs including:

- a new generation of direct access arrangement (DAA) products, which provide enhanced computer modem functionality;
- a family of RF synthesizers, which are used to generate high frequency signals that are used in wireless communications systems to select a particular radio channel;
- an Aero Transceiver chipset, providing a highly integrated radio communication section of a GSM wireless handset with versatile interfaces to other electronic sections of the handset;
- an ISModem, which is a miniaturized modem that can be embedded in

electronic devices with low-speed transmission requirements, such as credit card verification devices, to provide quick network access;

- a family of higher speed ISModem products to serve additional embedded modem markets where faster transmission is required such as next generation set-top boxes;
- a family of ProSLIC products, which provides dial tone, busy tone, caller ID and ring signal functions at the source end of the telephone line addressing long-haul and short-haul applications;
- a Digital Subscriber Line, or DSL, Analog Front End providing a highly integrated interface for DSL; and
- a family of optical networking products, which features highly integrated physical layer and clock circuits designed for SONET/ATM routers, multiplexers, digital cross connects and optical transceiver modules.

We also are actively developing other ICs. If our recently introduced or other ICs fail to achieve market acceptance, our growth prospects, operating results and competitive position could be adversely affected.

WE HAVE INCREASED OUR INTERNATIONAL SALES ACTIVITIES SIGNIFICANTLY AND PLAN TO CONTINUE SUCH EFFORTS, WHICH SUBJECTS US TO ADDITIONAL BUSINESS RISKS INCLUDING INCREASED LOGISTICAL COMPLEXITY, POLITICAL INSTABILITY AND CURRENCY FLUCTUATIONS

We have opened additional sales offices in international markets to expand our international sales activities in Europe and the Pacific Rim region and intend to increase our staffing in international sales. The percentage of our revenues to customers located outside of the United States was 78% in the nine months ended September 28, 2002, 66% in fiscal 2001, 21% in fiscal 2000 and 7% in fiscal 1999. Our planned international sales growth will be limited if we are unable to hire additional personnel and develop relationships with international distributors. We may not be able to maintain or increase international market demand for our products. Our international operations are subject to a number of risks, including:

- increased complexity and costs of managing international operations;

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- protectionist laws and business practices that favor local competition in some countries;
- multiple, conflicting and changing laws, regulations and tax schemes;
- longer sales cycles;
- greater difficulty in accounts receivable collection and longer collection periods;
- high levels of distributor inventory subject to rights of return to us; and
- political and economic instability.

To date, all of our sales to international customers and purchases of components from international suppliers have been denominated in U.S. dollars. As a result, an increase in the value of the U.S. dollar relative to foreign currencies could make our products more expensive for our international customers to purchase, thus rendering them less competitive.

WE ARE SUBJECT TO CREDIT RISKS RELATED TO OUR ACCOUNTS RECEIVABLE, ESPECIALLY WHEN CUSTOMERS PURCHASE PRODUCTS THROUGH DISTRIBUTORS AND CONTRACT MANUFACTURERS.

We do not generally obtain letters of credit or other security for payment from customers, distributors or contract manufacturers. Accordingly, we are not protected against accounts receivable default or bankruptcy by these entities. If we are unable to collect our accounts receivable, our operating results could be materially harmed. A significant and increasing portion of our revenues are realized through indirect channels such as distributors and contract manufacturers. At September 28, 2002, gross receivable balances from distributors and contract manufacturers totaled \$21.8 million versus \$5.9 million at December 29, 2001. Distributors and contract manufacturers are frequently thinly capitalized and operate at very low profit margins, and are accordingly subject to a greater risk of insolvency. Typically, distributors and contract manufacturers are dependent on receiving payment from the ultimate customers for the resources necessary to pay us. None of our shipments to distributors and contract manufacturers are guaranteed by the ultimate customer.

If for any reason a customer does not pay the distributor or contract manufacturer, there are no assurances that our direct contractual customers will have adequate working capital to enable the collection of our accounts receivable. We continue to monitor the credit worthiness and payment practice of each of the distributors or contract manufacturers, and to date have not had any significant write offs of receivable balances from them.

WE ARE SUBJECT TO INCREASED INVENTORY RISKS AND COSTS BECAUSE WE BUILD OUR PRODUCTS BASED ON FORECASTS PROVIDED BY CUSTOMERS BEFORE RECEIVING PURCHASE ORDERS FOR THE PRODUCTS

In order to assure availability of our products for some of our largest customers, we start the manufacturing of our products in advance of receiving purchase orders based on forecasts provided by these customers. However, these forecasts do not represent binding purchase commitments and we do not recognize sales for these products until they are shipped to the customer. As a result, we incur inventory and manufacturing costs in advance of anticipated sales. Because demand for our products may not materialize, manufacturing based on forecasts subjects us to increased risks of high inventory carrying costs and increased obsolescence and may increase our operating costs. These inventory risks are exacerbated when our customers purchase indirectly through contract manufacturers because we have less direct interaction with such contract manufacturers, and less visibility regarding their accumulated levels of inventory.

WE RELY ON THIRD PARTIES TO MANUFACTURE, ASSEMBLE AND TEST OUR PRODUCTS AND THE FAILURE TO SUCCESSFULLY MANAGE OUR RELATIONSHIPS WITH OUR MANUFACTURERS AND ASSEMBLERS WOULD NEGATIVELY IMPACT OUR ABILITY TO SELL OUR PRODUCTS

We do not have our own wafer fab manufacturing facilities. Therefore, we must rely on third-party vendors to manufacture the ICs we design. We also currently rely principally on two third-party assembly contractors, Advanced Semiconductor Engineering and Amkor, to assemble and package the silicon chips provided by the wafers for use in final products. Additionally, we rely on third-party vendors for a portion of the testing requirements of our products prior to shipping.

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There are significant risks associated with relying on these third-party contractors, including:

- failure by us, our customers or their end customers to qualify a selected supplier;
- capacity shortages during periods of high demand;
- potential insolvency of the third-party contractors;
- reduced control over delivery schedules and quality;
- limited warranties on wafers or products supplied to us;
- potential increases in prices;
- their inability to supply or support new or changing packaging technologies; and
- low test yields.

We currently do not have long-term supply contracts with any of our third-party vendors, and, therefore, they are not obligated to perform services or supply products to us for any specific period, or in any specific quantities, except as may be provided in a particular purchase order. Although we believe that other semiconductor foundries or assembly contractors can adequately address our needs, we expect that it would take approximately two to nine months to transition performance of these services from our current providers to new providers. Such a transition may also require a qualification process by our customers or their end customers. We generally place orders for products with some of our suppliers approximately four months prior to the anticipated delivery date, with order volumes based on our forecasts of demand from our customers. Accordingly, if we do not accurately forecast demand for our products, we may be unable to obtain adequate foundry or assembly capacity from our third-party contractors to meet our customers' delivery requirements, or we may accumulate excess inventories. On occasion, we have been unable to adequately respond to unexpected increases in customer purchase orders, and, therefore, were unable to benefit from this incremental demand. None of our third-party foundry or assembly contractors have provided assurances to us that adequate capacity will be available to us within the time required to meet additional demand for our products.

Since our inception, substantially all of the silicon wafers for the products that we have shipped were manufactured either by Taiwan Semiconductor Manufacturing Co. or its affiliates. Our customers typically complete their own qualification process. If we fail to properly balance customer demand across the existing semiconductor fabrication facilities that we utilize or are required by our foundry partners to increase, or otherwise change the number of fab lines that we utilize for our production, we might not be able to fulfill demand for our products and may need to divert our engineering resources away from new product development initiatives to support the fab line transition, which would adversely affect our operating results. Additionally, a resulting write off of unusable or excess inventories would contribute to a decline in earnings.

THE SEMICONDUCTOR MANUFACTURING PROCESS IS HIGHLY COMPLEX AND, FROM TIME TO TIME, MANUFACTURING YIELDS MAY FALL BELOW OUR EXPECTATIONS, WHICH COULD RESULT IN OUR INABILITY TO TIMELY SATISFY DEMAND FOR OUR PRODUCTS.

The manufacture of silicon wafers for our products is a highly complex and technologically demanding process. Although we work closely with our foundries to minimize the likelihood of reduced manufacturing yields, our foundries from time to time have experienced lower than anticipated manufacturing yields. Changes in manufacturing processes or the inadvertent use of defective or contaminated materials by our foundries could result in lower than anticipated manufacturing yields or unacceptable performance deficiencies. If our foundries fail to deliver fabricated silicon wafers of satisfactory quality in a timely manner, we will be unable to meet our customers' demand for our products in a timely manner, which would adversely affect our operating results and damage our customer relationships.

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OUR CURRENT MANUFACTURERS, ASSEMBLERS, TEST SERVICE PROVIDERS, AND CUSTOMERS ARE CONCENTRATED IN THE SAME GEOGRAPHIC REGION WHICH INCREASES THE RISK THAT A NATURAL DISASTER, LABOR STRIKE, WAR OR POLITICAL UNREST COULD DISRUPT OUR OPERATIONS OR SALES

Our current semiconductor manufacturers are located in the same region within Taiwan and our assembly contractors are located in the Pacific Rim region. In addition, many of our customers, particularly mobile telephone manufacturers, are located in the Pacific Rim region. The risk of earthquakes in Taiwan and the Pacific Rim region is significant due to the proximity of major earthquake fault lines in the area. We are not currently covered by insurance against business disruption caused by earthquakes as such insurance is not currently available on terms that we believe are commercially reasonable. Earthquakes, fire, flooding or other natural disasters in Taiwan or the Pacific Rim region, or political unrest, war, labor strikes or work stoppages in countries where our semiconductor manufacturers' and assemblers' facilities are located, likely would result in the disruption of our foundry or assembly capacity. Any disruption resulting from these events could cause significant delays in shipments of our products until we are able to shift our manufacturing or assembling from the affected contractor to another third-party vendor. There can be no assurance that such alternate capacity could be obtained on favorable terms, if at all. In addition, a natural disaster, labor strike, war or political unrest where our customers' facilities are located would likely reduce our sales to such customers.

A SUBSTANTIAL PORTION OF THE FINAL TESTING OF OUR PRODUCTS IS PERFORMED INTERNALLY BY US, WHICH INCREASES OUR FIXED COSTS

In fiscal 2001, substantially all of our test operations were performed in-house. During the first nine months of 2002, we significantly expanded our internal test capabilities to support our wireless products. However, during this same period we also outsourced a portion of test operations to our contract manufacturers or other third parties. While we expect that performing a substantial portion of testing in-house provides us with advantages in terms of quality control and shorter time required to bring a product to market, we may encounter difficulties and delays in maintaining or expanding our internal test capabilities. In addition, final testing of complex semiconductors requires substantial resources to acquire state-of-the-art testing equipment and hiring additional qualified personnel, which has increased our fixed costs. If demand for our products does not support the effective utilization of these employees and additional equipment, we may not realize any benefit from performing the final testing internally. Any decrease in the demand for our products could result in the underutilization of our testing equipment and personnel. If our internal test operations are underused or mismanaged, we may incur significant costs that could adversely affect our operating results.

WE HAVE DEPENDED ON OUR WIRELESS FAMILY OF PRODUCTS FOR A SIGNIFICANT AMOUNT OF OUR REVENUES IN FISCAL 2002, AND SUBSTANTIAL REDUCTIONS IN ORDERS FOR WIRELESS PRODUCTS WOULD SIGNIFICANTLY REDUCE OUR REVENUES

During the first nine months of 2002, a significant amount of our sales were

derived from sales of our wireless family of ICs. This product family, in turn, is highly dependent on sales to the GSM segment of the wireless phone industry. Continued diversification of our sales through the introduction and commercial acceptance of products other than wireless products will be required to reduce our reliance on sales of our wireless products. A decline in overall demand for wireless phones or the introduction by our competitors of products with superior price/performance characteristics could significantly reduce our sales. In addition, substantially all of our wireless products that we have sold include technology related to one or more of our issued U.S. patents. If these patents are found to be invalid or unenforceable, our competitors could introduce competitive products that could reduce both the volume and price per unit of our products.

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WE HAVE DEPENDED ON OUR DAA FAMILY OF PRODUCTS FOR A SIGNIFICANT AMOUNT OF OUR REVENUES IN FISCAL 2002, AND SUBSTANTIAL REDUCTIONS IN ORDERS FOR DAA PRODUCTS WOULD SIGNIFICANTLY REDUCE OUR REVENUES

During the first nine months of 2002, a significant amount of our sales were derived from sales of our DAA family of ICs. This product family, in turn, is highly dependent on sales to the personal computer industry. Continued diversification of our sales through the introduction and commercial acceptance of products other than DAA products will be required to reduce our reliance on sales of our DAA products. A decline in overall demand for personal computers or the introduction by our competitors of products with superior price/performance characteristics could significantly reduce our sales. In addition, substantially all of our DAA products that we have sold include technology related to one or more of our issued U.S. patents. If these patents are found to be invalid or unenforceable, our competitors could introduce competitive products that could reduce both the volume and price per unit of our products.

In August 2001, TDK Semiconductor Corporation filed suit against us alleging that certain of our DAA products infringe a TDK-held patent. We have filed a response denying the alleged infringement. If our DAA products are found to infringe TDK's patent, our future operating results and financial condition could be substantially adversely affected. For further information regarding this litigation, please see "Part II, Item 1. Legal Proceedings."

WE DEPEND ON A LIMITED NUMBER OF CUSTOMERS FOR A SUBSTANTIAL PORTION OF OUR REVENUES, AND THE LOSS OF, OR A SIGNIFICANT REDUCTION IN ORDERS FROM, ANY KEY CUSTOMER COULD SIGNIFICANTLY REDUCE OUR REVENUES

The loss of any of our key customers, or a significant reduction in sales to any one of them, would significantly reduce our revenues and adversely affect our business. During the first nine months of 2002, two customers, in aggregate represented 26% of our revenues. Samsung, purchasing primarily through Uniquet, represented 15% of revenues and Wavecom, purchasing through Solectron and other contract manufacturers, represented 11% of revenues. No other single customer accounted for more than 10% of our revenues during the first nine months of 2002. Uniquet, a distributor selling products to Samsung and several customers, represented 19% of our revenues. Edom Technology, a distributor selling products to several customers in Asia, represented 13% of our revenues. Most of the markets for our products are dominated by a small number of potential customers. Therefore, our operating results in the foreseeable future will continue to depend on our ability to affect sales to these dominant customers, as well as the ability of these customers to sell products that incorporate our IC products. In the future, these customers may decide not to purchase our ICs at all, purchase fewer ICs than they did in the past or alter their purchasing patterns, particularly because:

- we do not have any material long-term purchase arrangements with these or any of our other customers;
- substantially all of our sales to date have been made on a purchase order basis, which permits our customers to cancel, change or delay product purchase commitments with little or no notice to us and without penalty; and
- some of our customers have sought or are seeking relationships with current or potential competitors which may affect our customers' purchasing decisions.

While we have been the sole supplier of the direct access arrangement, or DAA, ICs used in many of our customers' soft modem DAA products, we anticipate that our customers will regularly evaluate alternative sources of supply in the future in order to diversify their supplier base, which would increase their negotiating leverage with us and protect their ability to secure DAA components. We believe that any second source of DAA ICs for our customers could have an adverse effect on the prices we are able to charge our customers and the volume of DAA ICs that we sell to our customers, which would negatively affect our

revenues and operating results.

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DUE TO OUR LIMITED OPERATING HISTORY, WE MAY HAVE DIFFICULTY BOTH IN ACCURATELY PREDICTING OUR FUTURE SALES AND APPROPRIATELY BUDGETING FOR OUR EXPENSES

We were incorporated in 1996, did not begin generating revenues until the second quarter of 1998 and have rapidly expanded our product lines in recent years. As a result, we have only a short history from which to predict future revenues. This limited operating experience, combined with the rapidly evolving nature of the markets in which we sell our products and other factors which are beyond our control, reduce our ability to accurately forecast quarterly or annual revenues. Additionally, because most of our expenses are fixed in the short term or incurred in advance of anticipated revenues, we may not be able to decrease our expenses in a timely manner to offset any shortfall of revenues.

OUR RESEARCH AND DEVELOPMENT EFFORTS ARE FOCUSED ON A LIMITED NUMBER OF NEW TECHNOLOGIES AND PRODUCTS, AND ANY DELAY IN THE DEVELOPMENT, OR ABANDONMENT, OF THESE TECHNOLOGIES OR PRODUCTS BY INDUSTRY PARTICIPANTS, OR THEIR FAILURE TO ACHIEVE MARKET ACCEPTANCE, COULD COMPROMISE OUR COMPETITIVE POSITION

Our ICs are used as components in communications devices in various markets. As a result, we have devoted and expect to continue to devote a large amount of resources to develop products based on new and emerging technologies and standards that will be commercially introduced in the future. For the nine months ended September 28, 2002, our research and development expense was \$23.6 million, which represented 19.4% of our revenues, compared to \$21.3 million, or 42.2% of our revenues, for the nine months ended September 29, 2001. A number of large companies in the communications industry are actively involved in the development of these new technologies and standards. Should any of these companies delay or abandon their efforts to develop commercially available products based on new technologies and standards, our research and development efforts with respect to these technologies and standards likely would have no appreciable value. In addition, if we do not correctly anticipate new technologies and standards, or if the products that we develop based on these new technologies and standards fail to achieve market acceptance, our competitors may be better able to address market demand than would we. Furthermore, if markets for these new technologies and standards develop later than we anticipate, or do not develop at all, demand for our products that are currently in development would suffer, resulting in lower sales of these products than we currently anticipate. For example, we have introduced to market a RF synthesizer product for use in wireless phones operating on the GSM standard. The RF synthesizer is also compatible with GPRS standard, which we believe is the emerging data communications protocol for GSM based wireless phones. We cannot be certain whether these standards will not change, thereby making our products unsuitable or impractical. Additionally, despite the published GSM/GPRS specifications, mobile phone network operators may demand increased performance beyond specifications for this highly competitive market. In the area of optical networking, our clock and data recovery integrated circuit operates within stringent specifications for high speed communications systems known as SONET. Changes to this standard could make our products uncompetitive or unsuitable to changing system requirements and result in our inability to sell these products.

WE DEPEND ON OUR CUSTOMERS TO SUPPORT OUR PRODUCTS

Our products are currently used by our customers to produce modems, telephony equipment, mobile telephones, various wireless devices and optical networking equipment. We rely on our customers to provide hardware, software, intellectual property indemnification and other technical support for the devices that use our products. If our customers do not provide the required functionality or if our customers do not provide satisfactory support for their products, the demand for these devices that incorporate our products may diminish. Any reduction in the demand for these devices would significantly reduce our revenues.

ANY ACQUISITIONS WE MAKE COULD DISRUPT OUR BUSINESS AND HARM OUR FINANCIAL CONDITION

As part of our growth strategy, we will continue to evaluate opportunities to acquire other businesses or technologies that would complement our current offerings, expand the breadth of our markets or enhance our technical capabilities. Acquisitions that we may potentially make in the future entail a

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number of risks that could materially and adversely affect our business and operating results, including:

- problems integrating the acquired operations, technologies or products with our existing business and products;
- diversion of management's time and attention from our core business;
- difficulties in retaining business relationships with suppliers and customers of the acquired company;
- risks associated with entering markets in which we lack prior experience; and
- potential loss of key employees of the acquired company.

WE ARE A RELATIVELY SMALL COMPANY WITH LIMITED RESOURCES COMPARED TO SOME OF OUR CURRENT AND POTENTIAL COMPETITORS AND WE MAY NOT BE ABLE TO COMPETE EFFECTIVELY AND INCREASE MARKET SHARE

Some of our current and potential competitors have longer operating histories, significantly greater resources and name recognition and a larger base of customers than we have. As a result, these competitors may have greater credibility with our existing and potential customers. They also may be able to adopt more aggressive pricing policies and devote greater resources to the development, promotion and sale of their products than we can to ours. In addition, some of our current and potential competitors have already established supplier or joint development relationships with the decision makers at our current or potential customers. These competitors may be able to leverage their existing relationships to discourage their customers from purchasing products from us or persuade them to replace our products with their products. Our competitors may also offer bundled chipset kit arrangements offering a more complete product despite the technical merits or advantages of our products. These competitors may elect not to support our products which could complicate our sales efforts.

In addition, our largest competitors may restructure their operations to create separate companies that are more focused on providing the types of products we produce. For example, Conexant is a significant competitor of ours across multiple product lines. In June 2002, Conexant completed the spin-out of a new company named Skyworks Solutions, Inc., resulting from the combination of Conexant's wireless business merged with Alpha Industries, Inc. Conexant has also re-affirmed their intention to spin-out their Mindspeed entity which is principally focused on optical networking semiconductor components. In July 2000, Lucent Technologies spun off its microelectronics business, which included its optoelectronics components and integrated circuits division, into a separate company named Agere Systems in order to accelerate the growth of the business and alleviate strategic conflicts with Lucent's competitors. Additionally, Siemens spun off its semiconductor business in 1999 to create a more focused company named Infineon Technologies. Increased competition could decrease our prices, reduce our sales, lower our margins or decrease our market share. These and other competitive pressures may prevent us from competing successfully against current or future competitors, and may materially harm our business.

WE DEPEND ON OUR KEY PERSONNEL TO MANAGE OUR BUSINESS EFFECTIVELY IN A RAPIDLY CHANGING MARKET, AND IF WE ARE UNABLE TO RETAIN OUR CURRENT PERSONNEL AND HIRE ADDITIONAL PERSONNEL, OUR ABILITY TO DEVELOP AND SUCCESSFULLY MARKET OUR PRODUCTS COULD BE HARMED

We believe our future success will depend in large part upon our ability to attract and retain highly skilled managerial, engineering, sales and marketing personnel. Specifically, we believe that our future success is highly dependent on Navdeep Sooch, our co-founder, Chief Executive Officer and Chairman of the Board, Daniel Artusi, our Chief Operating Officer, Jeffrey Scott, our co-founder and Vice President, and David Welland, our co-founder and Vice President. There is currently a shortage of qualified personnel with significant experience in the design, development, manufacturing, marketing and sales of analog and mixed-signal communications ICs. In particular, there is a shortage of engineers who are familiar with the intricacies of the design and manufacturability of analog elements, and competition for such personnel is intense. Our key technical personnel represent a significant asset and serve as the primary source for our technological and product innovations. We may not be successful in attracting and retaining sufficient numbers of technical personnel to support our anticipated growth. The loss of any of our key employees or the inability to attract or retain qualified personnel, including engineers and sales and marketing personnel, could delay the development and introduction of, and negatively impact our ability to sell, our products.

OUR PRODUCTS ARE COMPLEX AND MAY REQUIRE MODIFICATIONS TO RESOLVE UNDETECTED

ERRORS WHICH COULD LEAD TO AN INCREASE IN OUR COSTS OR A REDUCTION IN OUR REVENUES

Our products are complex and may contain errors when first introduced or as new versions are released. We rely primarily on our in-house testing personnel to design test operations and procedures to detect any errors prior to delivery of our products to our customers. Because our products are manufactured by third parties, should problems occur in the operation or performance of our ICs, we may experience delays in meeting key introduction dates or scheduled delivery dates to our customers. These errors also could cause us to incur significant re-engineering costs, divert the attention of our engineering personnel from our product development efforts and cause significant customer relations and business reputation problems.

THE PERFORMANCE OF OUR DIRECT ACCESS ARRANGEMENT PRODUCTS MAY BE ADVERSELY AFFECTED BY SEVERE ENVIRONMENTAL CONDITIONS THAT MAY REQUIRE MODIFICATIONS, WHICH COULD LEAD TO AN INCREASE IN OUR COSTS OR A REDUCTION IN OUR REVENUES

Although our DAA products are compliant with published specifications, these established specifications might not adequately address all conditions that must be satisfied in order to operate in harsh environments. This includes environments where there are wide variations in electrical quality, telephone line quality, static electricity and operating temperatures or that may be affected by lightning or improper handling by customers and end users. Our products have had a limited period of time in the field under operation, and these environmental factors may result in unanticipated returns of our products. Any necessary modifications could cause us to incur significant re-engineering costs, divert the attention of our engineering personnel from our product development efforts and cause significant customer relations and business reputation problems.

We have a large installed base of DAA products in the field. As part of our ongoing support of this product line, we verify the performance of our products through regulatory agency qualifications, customer acceptance procedures, evaluation of end customer technical support information, and analysis of field returns. Certain customer modem implementations of our direct access arrangement products have been identified to be susceptible to a particular class of electrical surges originating from lightning strikes that are not adequately described in regulatory agency qualifications. We have provided application guidelines to our customers to enhance their implementation of the modem function to protect our devices from these lightning strike electrical surges.

Damage from these electrical surges could result in product liability claims against our customers that produce these modems or against us. Our customers may seek indemnification or other compensation from us with respect to any liability that they incur. Even if our DAA product is not the source of the problem and we are not contractually liable for such indemnification, we may incur costs in an effort to maintain good relations with our customers. If we are held liable for these claims or incur other costs in order to maintain good relations, this problem could adversely affect our operating results.

WE MAY BE UNABLE TO PROTECT OUR INTELLECTUAL PROPERTY, WHICH WOULD NEGATIVELY AFFECT OUR ABILITY TO COMPETE

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Our products rely on our proprietary technology, and we expect that future technological advances made by us will be critical to sustain market acceptance of our products. Therefore, we believe that the protection of our intellectual property rights is and will continue to be important to the success of our business. We rely on a combination of patent, copyright, trademark and trade secret laws and restrictions on disclosure to protect our intellectual property rights. We also enter into confidentiality or license agreements with our employees, consultants and business partners, and control access to and distribution of our documentation and other proprietary information. Despite these efforts, unauthorized parties may attempt to copy or otherwise obtain and use our proprietary technology. Monitoring unauthorized use of our technology is difficult, and we cannot be certain that the steps we have taken will prevent unauthorized use of our technology, particularly in foreign countries where the laws may not protect our proprietary rights as fully as in the United States. We cannot be certain that patents will be issued as a result of our pending applications nor can we be certain that any issued patents would protect or benefit us or give us adequate protection from competing products. For example, issued patents may be circumvented or challenged and declared invalid or unenforceable. We also cannot be certain that others will not develop effective competing technologies on their own.

SIGNIFICANT LITIGATION OVER INTELLECTUAL PROPERTY IN OUR INDUSTRY MAY CAUSE US TO BECOME INVOLVED IN COSTLY AND LENGTHY LITIGATION WHICH COULD SERIOUSLY HARM OUR BUSINESS

In recent years, there has been significant litigation in the United States involving patents and other intellectual property rights. From time to time, we receive letters from various industry participants alleging infringement of patents, trademarks or misappropriation of trade secrets. The exploratory nature of these inquiries has become relatively common in the semiconductor industry. We typically respond when appropriate and as advised by legal counsel. We have been involved in litigation to protect our intellectual property rights in the past and may become involved in such litigation again in the future. In the future, we may become involved in litigation to defend allegations of infringement asserted by others, both directly and indirectly as a result of certain industry-standard indemnities we may offer to our customers. Legal proceedings could subject us to significant liability for damages or invalidate our proprietary rights. Legal proceedings initiated by us to protect our intellectual property rights could also result in counterclaims or countersuits against us. Any litigation, regardless of its outcome, would likely be time consuming and expensive to resolve and would divert our management's time and attention. Any intellectual property litigation also could force us to take specific actions, including:

- cease selling products that use the challenged intellectual property;
- obtain from the owner of the infringed intellectual property right a license to sell or use the relevant technology, which license may not be available on reasonable terms, or at all;
- redesign those products that use infringing intellectual property; or
- pursue legal remedies with third parties to enforce our indemnification rights, which may not adequately protect our interests.

In August 2001, TDK Semiconductor Corporation commenced a lawsuit against us for alleged willful infringement by our DAA products of a TDK-held patent. TDK's complaint seeks unspecified treble damages, costs and attorneys' fees, and an injunction. In September 2001, we served and filed an answer to TDK's complaint, in which we denied the alleged infringement and asserted that their patent is invalid. On March 27, 2002, we filed an amended answer and counterclaims in which we claimed that the TDK-held patent is unenforceable due to inequitable conduct and asserted counterclaims seeking a declaration that the TDK-held patent is invalid, not infringed and unenforceable. This lawsuit may involve significant expense and may also divert our management's time and attention from other aspects of our business. Due to the inherent uncertainties of litigation, we are unable to predict the outcome of this matter. For further information regarding this litigation, please see "Part II, Item 1. Legal Proceedings."

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FAILURE TO MANAGE OUR DISTRIBUTION CHANNEL RELATIONSHIPS COULD IMPEDE OUR FUTURE GROWTH

The future growth of our business will depend in part on our ability to manage our relationships with current and future distributors and sales representatives, develop additional channels for the distribution and sale of our products and manage these relationships. As we execute our indirect sales strategy, we will need to manage the potential conflicts that may arise with our direct sales efforts. The inability to successfully execute or manage a multi-channel sales strategy could impede our future growth.

RISKS RELATED TO OUR INDUSTRY

COMPETITION WITHIN THE NUMEROUS MARKETS WE TARGET MAY REDUCE SALES OF OUR PRODUCTS AND REDUCE MARKET SHARE

The markets for semiconductors in general, and for mixed-signal ICs in particular, are intensely competitive. We expect that the market for our products will continually evolve and will be subject to rapid technological change. In addition, as we target and supply products to numerous markets and applications, we face competition from a relatively large number of competitors. Across all of our product areas, we compete with Agere Systems, AMCC, Analog Devices, Broadcom, Conexant, Cypress, ESS, Fujitsu, Hitachi, Infineon Technologies, Legerity (formerly the Advanced Micro Devices telecom division), Maxim Integrated Products, National Semiconductor, Philips, Semtech, Skyworks Solutions Inc. (the combination of Conexant's wireless business and Alpha Industries), Texas Instruments, Vitesse Semiconductor Corp, and others. We expect to face competition in the future from our current competitors, other manufacturers and designers of semiconductors, and innovative start-up semiconductor design companies. Some of our customers, such as Agere Systems, Intel, Motorola, Samsung and Texas Instruments, are also large, established semiconductor suppliers. Our sales to and support of these customers may enable them to become a source of competition to us, despite our efforts to protect our intellectual property rights. As the markets for communications products grow, we also may face competition from traditional communications device companies.

These companies may enter the mixed-signal semiconductor market by introducing their own ICs or by entering into strategic relationships with or acquiring other existing providers of semiconductor products. The sales of our wireless products into the highly competitive GSM handset market are expected to comprise a larger percentage of our future revenues resulting an increasingly competitive marketplace for our aggregate product revenue.

THE AVERAGE SELLING PRICES OF OUR PRODUCTS COULD DECREASE RAPIDLY WHICH MAY NEGATIVELY IMPACT OUR GROSS MARGINS AND REVENUES

We may experience substantial period-to-period fluctuations in future operating results due to the erosion of our average selling prices. We have reduced the average unit price of our products in anticipation of future competitive pricing pressures, new product introductions by us or our competitors and other factors. The highly competitive GSM handset market is extremely cost sensitive due to the potentially very high volumes and stringent expectations placed on consumer electronics component suppliers for aggressive and sustained price reductions which would result in declining average selling prices. We expect that these factors will create downward pressure on our average selling prices and gross margins. If we are unable to offset any such reductions in our average selling prices by increasing our sales volumes, our gross profits and revenues will suffer. To maintain gross margins, we will need to develop and introduce new products and product enhancements on a timely basis and continually reduce our costs. Our failure to do so would cause our revenues and gross margins to decline.

WE ARE SUBJECT TO THE CYCLICAL NATURE OF THE SEMICONDUCTOR INDUSTRY

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The semiconductor industry is highly cyclical and is characterized by constant and rapid technological change, rapid product obsolescence and price erosion, evolving standards, short product life cycles and wide fluctuations in product supply and demand. The industry has experienced significant downturns, often connected with, or in anticipation of, maturing product cycles of both semiconductor companies' and their customers' products and declines in general economic conditions. These downturns have been characterized by diminished product demand, production overcapacity, high inventory levels and accelerated erosion of average selling prices. Specific areas of the communications markets have contributed to the overall decline and volatility of the semiconductor industry. For example, the semiconductor industry has suffered a downturn due to reductions in the actual unit sales of personal computers and wireless phones as compared to previous robust forecasts, and forecasts of excess capacity in the fiber optic networks. Additionally, changing and competing technical standards in airwave interfaces such as GSM and CDMA for mobile handsets, migration to higher speed communication protocols in the optical space and the return to prominence of the traditional bell regional operating companies compared to the competitive local exchange companies all have contributed to the volatility in the communications area of the semiconductor industry. This downturn has resulted in a material adverse effect on our business and operating results. The severity and duration of these industry-wide trends are currently unclear and the material adverse effect on our business may continue in the future.

Due to the cyclical nature of the semiconductor industry, any upturn in business could result in increased competition for access to third-party foundry and assembly capacity. We are dependent on the availability of such capacity to manufacture and assemble our ICs. None of our third-party foundry or assembly contractors have provided assurances that adequate capacity will be available to us.

OUR CUSTOMERS REQUIRE OUR PRODUCTS TO UNDERGO A LENGTHY AND EXPENSIVE QUALIFICATION PROCESS WHICH DOES NOT ASSURE PRODUCT SALES

Prior to purchasing our products, our customers require that our products undergo an extensive qualification process, which involves testing of the products in the customer's system as well as rigorous reliability testing. This qualification process may continue for six months or longer. However, qualification of a product by a customer does not assure any sales of the product to that customer. Even after successful qualification and sales of a product to a customer, a subsequent revision to the IC, changes in its manufacturing process or the selection of a new supplier by us may require a new qualification process, which may result in delays and in us holding excess or obsolete inventory. After our products are qualified, it can take an additional six months or more before the customer commences volume production of components or devices that incorporate our products. Despite these uncertainties, we devote substantial resources, including design, engineering, sales, marketing and management efforts, toward qualifying our products with customers in anticipation of sales. If we are unsuccessful or delayed in qualifying any of our products with a customer, such failure or delay would preclude or delay sales of such product to the customer, which may impede our growth and cause our business to suffer.

OUR PRODUCTS MUST CONFORM TO INDUSTRY STANDARDS IN ORDER TO BE ACCEPTED BY END USERS IN OUR MARKETS

Generally, our products comprise only a part of a communications device. All components of such devices must uniformly comply with industry standards in order to operate efficiently together. We depend on companies that provide other components of the devices to support prevailing industry standards. Many of these companies are significantly larger and more influential in affecting industry standards than we are. Some industry standards may not be widely adopted or implemented uniformly, and competing standards may emerge that may be preferred by our customers or end users. If larger companies do not support the same industry standards that we do, or if competing standards emerge, market acceptance of our products could be adversely affected which would harm our business.

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Products for communications applications are based on industry standards that are continually evolving. Our ability to compete in the future will depend on our ability to identify and ensure compliance with these evolving industry standards. The emergence of new industry standards could render our products incompatible with products developed by other suppliers. As a result, we could be required to invest significant time and effort and to incur significant expense to redesign our products to ensure compliance with relevant standards. If our products are not in compliance with prevailing industry standards for a significant period of time, we could miss opportunities to achieve crucial design wins. We may not be successful in developing or using new technologies or in developing new products or product enhancements that achieve market acceptance. Our pursuit of necessary technological advances may require substantial time and expense.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Information related to quantitative and qualitative disclosures regarding market risk is set forth in Management's Discussion and Analysis of Financial Condition and Results of Operations and the risk factors under Item 2 above. Such information is incorporated by reference herein.

ITEM 4. CONTROLS AND PROCEDURES

We performed an evaluation under the supervision and with the participation of our management, including our Chief Executive Officer (CEO) and Chief Financial Officer (CFO), of the effectiveness of the design and operation of our disclosure controls and procedures. Based on that evaluation, our management, including our CEO and CFO, concluded that our disclosure controls and procedures were effective as of September 28, 2002. There have been no significant changes in our internal controls or other factors that could significantly affect internal controls subsequent to September 28, 2002.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

PATENT INFRINGEMENT LITIGATION

On August 7, 2001, TDK Semiconductor Corporation (TDK) commenced a lawsuit in the United States District Court for the Central District of California against us for alleged infringement of TDK's United States Patent No. 5,654,984. TDK's complaint asserts that we have infringed TDK's '984 patent by making, using and selling in the United States certain DAA semiconductor chipsets, including our Si3035 and Si3044 products, and that the infringement was and continues to be willful. TDK's complaint seeks unspecified treble damages, costs and attorneys' fees, and an injunction.

On September 27, 2001, we served and filed an answer to TDK's complaint, in which we denied infringement and asserted that TDK's '984 patent is invalid.

On March 27, 2002, we filed an amended answer and counterclaims in which we claimed that the TDK-held patent is unenforceable due to inequitable conduct and asserted counterclaims seeking a declaration that the TDK-held patent is invalid, not infringed and unenforceable. We are currently in the discovery phase of this litigation.

We intend to vigorously contest this case, and are unable at this time to determine whether the outcome of the litigation will have a material impact on our results of operations or financial condition in any future period. For a description of risks associated with this pending lawsuit, please see "Risk Factors--Significant litigation over intellectual property in our industry may cause us to become involved in costly and lengthy litigation which could seriously harm our business."

SECURITIES LITIGATION

On December 6, 2001, a class action complaint for violations of U.S. federal securities laws was filed in the United States District Court, Southern District of New York against us, four officers individually and the three investment banking firms who served as representatives of the underwriters in connection with our initial public offering of common stock which became effective on March 23, 2000. On April 19, 2002, a consolidated amended complaint was filed in the same court. The action is being coordinated with over 300 other nearly identical actions filed against other companies. These claims are premised on allegations that the registration statement and prospectus for our initial public offering did not disclose that (1) the underwriters solicited and received additional, excessive and undisclosed commissions from certain investors, and (2) the underwriters had agreed to allocate shares of the offering in exchange for a commitment from the customers to purchase additional shares in the aftermarket at pre-determined higher prices. A court order dated October 9, 2002 dismissed without prejudice numerous individual defendants, including the four officers of our company who had been named individually. We intend to vigorously contest this case, and are unable at this time to determine whether the outcome of the litigation will have a material impact on our results of operations or financial condition in any future period.

We are not currently involved in any other material legal proceedings.

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

Our registration statement (Registration No. 333-94853) under the Securities Act of 1933, as amended, relating to our initial public offering of our common stock became effective on March 23, 2000. A total of 3,680,000 shares of common stock were registered. We sold a total of 3,200,000 shares of our common stock and selling stockholders sold a total of 480,000 shares to an underwriting syndicate. The managing underwriters were Morgan Stanley & Co. Incorporated, Lehman Brothers Inc., and Salomon Smith Barney Inc. The offering commenced and was completed on March 24, 2000, at a price to the public of \$31.00 per share. The initial public offering resulted in net proceeds to us of \$90.6 million, after deducting underwriting commissions of \$6.9 million and offering expenses of \$1.6 million. We used \$15 million of the proceeds as part of the consideration paid in the acquisition of Krypton Isolation, Inc. on August 9, 2000. Another \$4.3 million was used to pay off equipment loans provided by Imperial Bank. We used another \$1.0 million of the proceeds as part of the consideration paid in the acquisition of SNR Semiconductor Incorporated on October 2, 2000. As of September 28, 2002, the remaining proceeds were invested in short-term, investment-grade, interest bearing instruments.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

Not applicable

ITEM 5. OTHER INFORMATION

Not applicable

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) The following exhibits are filed as part of this report:

Exhibit
Number

- 3.1* Form of Fourth Amended and Restated Certificate of Incorporation of Silicon Laboratories Inc. filed as Exhibit 3.1 to the Registrant's Registration Statement on Form S-1 (SEC File No. 333-94853 (the "IPO Registration Statement")).
- 3.2* Form of Amended and Restated Bylaws of Silicon Laboratories Inc. (filed as Exhibit 3.2 to the IPO Registration Statement).
- 4.1* Specimen certificate for shares of common stock (filed as Exhibit 4.1 to the IPO Registration Statement).

* Incorporated herein by reference to the indicated filing.

(b) During the three months ended September 28, 2002, we filed the following Current Reports on Form 8-K:

We filed a Form 8-K on September 12, 2002 (Item 5) announcing the appointment of Russell J. Brennan as chief financial officer.

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SIGNATURES

Pursuant to the requirements 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.

SILICON LABORATORIES INC.
(Registrant)

October 22, 2002

/s/ Navdeep S. Sooch

Date

Navdeep S. Sooch
CHAIRMAN AND
CHIEF EXECUTIVE OFFICER
(PRINCIPAL EXECUTIVE OFFICER)

October 22, 2002

/s/ Russell J. Brennan

Date

Russell J. Brennan
VICE PRESIDENT AND
CHIEF FINANCIAL OFFICER
(PRINCIPAL ACCOUNTING OFFICER)

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CERTIFICATIONS

I, Navdeep S. Sooch, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Silicon Laboratories Inc.;
2. Based on my knowledge, this quarterly 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 quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
 - a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
 - b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
 - c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons fulfilling the equivalent functions):

- a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls;
6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: October 22, 2002

/s/ Navdeep S. Sooch

Navdeep S. Sooch
CHAIRMAN AND
CHIEF EXECUTIVE OFFICER
(PRINCIPAL EXECUTIVE OFFICER)

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CERTIFICATIONS

I, Russell J. Brennan, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Silicon Laboratories Inc.;
2. Based on my knowledge, this quarterly 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 quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
 - a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
 - b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
 - c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons fulfilling the equivalent functions):
 - a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls;

6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: October 22, 2002

/s/ Russell J. Brennan

Russell J. Brennan
VICE PRESIDENT AND
CHIEF FINANCIAL OFFICER
(PRINCIPAL ACCOUNTING OFFICER)