AMERICAN PETRO-HUNTER INC
Form 424B3
November 18, 2013

Filed Pursuant to Rule 424(b)(3)
Registration No. 333-190287

PROSPECTUS SUPPLEMENT

16,182,230 SHARES OF COMMON STOCK

AMERICAN PETRO-HUNTER INC.

This Prospectus Supplement supplements and amends our Prospectus dated September 11, 2013, as amended and supplemented. This Prospectus Supplement includes our attached Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2013, as filed with the Securities and Exchange Commission on November 18, 2013.

The Prospectus, any prospectus supplements filed before the date hereof, and this Prospectus Supplement relate to the resale of up to an aggregate of 16,182,230 shares of our common stock, par value $0.001 per share, by Hanover Holdings I, LLC, a New York limited liability company ("Hanover" or "Selling Stockholder"), 14,417,524 of which (the "Purchase Shares") are issuable to Hanover pursuant to the terms of the Common Stock Purchase Agreement, between the Company and Hanover, dated March 22, 2013 (the "Purchase Agreement") and 1,764,706 of which were issued to Hanover on March 22, 2013 in satisfaction of a $150,000 commitment fee paid to Hanover for entering into the Purchase Agreement, based upon a price per share equal to $0.085 per share.

This Prospectus Supplement should be read in conjunction with the Prospectus and any prospectus supplements filed before the date hereof. Any statement contained in the Prospectus and any prospectus supplements filed before the date hereof shall be deemed to be modified or superseded to the extent that information in this Prospectus Supplement modifies or supersedes such statement. Any statement that is modified or superseded shall not be deemed to constitute a part of the Prospectus except as modified or superseded by this Prospectus Supplement.

Our common stock is quoted on the OTC Bulletin Board under the symbol "AAPH" The shares of our common stock registered hereunder are being offered for sale by Selling Stockholder at prices established on the OTC Bulletin Board during the term of this offering. On November 14, 2013, the closing bid price of our common stock was $0.017 per share. These prices will fluctuate based on the demand for our common stock.

INVESTING IN OUR COMMON STOCK INVOLVES A HIGH DEGREE OF RISK. SEE "RISK FACTORS" BEGINNING ON PAGE 6 OF THE PROSPECTUS.

NEITHER THE SECURITIES AND EXCHANGE COMMISSION NOR ANY STATE SECURITIES COMMISSION HAS APPROVED OR DISAPPROVED OF THESE SECURITIES OR DETERMINED IF THE PROSPECTUS OR THIS PROSPECTUS SUPPLEMENT IS TRUTHFUL OR COMPLETE. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

The date of this Prospectus Supplement is November 18, 2013.

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

FORM 10-Q

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

For the quarterly period ended: **September 30, 2013**

[ ] **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 **0-22723**

AMERICAN PETRO-HUNTER INC.
(Exact name of registrant as specified in its charter)

Nevada	**90-0552874**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification Number)

250 N. Rock Rd., Suite 365
Wichita KS, 67206
(Address of principal executive offices) (Zip Code)

(316) 201-1853
(Registrant s telephone number, including area code)

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

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

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

[ ] Large accelerated filer	[ ] Accelerated filer
[ ] Non-accelerated filer (Do not check if smaller reporting company)	[X] Smaller Reporting company

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Class	Outstanding at November 14, 2013
Common stock, $.001 par value	81,267,441

AMERICAN PETRO HUNTER INC.
FORM 10-Q
September 30, 2013
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FORWARD-LOOKING STATEMENTS

This Report on Form 10-Q contains forward-looking statements within the meaning of the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Reference is made in particular to the description of our plans and objectives for future operations, assumptions underlying such plans and objectives, and other forward-looking statements included in this report. Such statements may be identified by the use of forward-looking terminology such as may, expect, believe, estimate, anticipate, intend, continue, or similar terms, variations of such t negative of such terms. Such statements are based on management s current expectations and are subject to a number of factors and uncertainties, which could cause actual results to differ materially from those described in the forward-looking statements. Such statements address future events and conditions concerning, among others, capital expenditures, earnings, litigation, regulatory matters, liquidity and capital resources, and accounting matters. Actual results in each case could differ materially from those anticipated in such statements by reason of factors such as future economic conditions, changes in consumer demand, legislative, regulatory and competitive developments in markets in which we operate, results of litigation, and other circumstances affecting anticipated revenues and costs, and the risk factors set forth under the heading Risk Factors in our Annual Report on Form 10-K for the fiscal year ended December 31, 2012, filed on April 15, 2013.

As used in this Form 10-Q, we, us and our refer to American Petro-Hunter Inc., which is also sometimes referred t as the Company.

YOU SHOULD NOT PLACE UNDUE RELIANCE ON THESE FORWARD LOOKING STATEMENTS

The forward-looking statements made in this report on Form 10-Q relate only to events or information as of the date on which the statements are made in this report on Form 10-Q. Except as required by law, we undertake no obligation to update or revise publicly any forward-looking statements, whether as a result of new information, future events, or otherwise, after the date on which the statements are made or to reflect the occurrence of unanticipated events. You should read this report and the documents that we reference in this report, including documents referenced by incorporation, completely and with the understanding that our actual future results may be materially different from what we expect or hope.

Item 1. Financial Statements.

American Petro-Hunter, Inc.
Condensed Balance Sheets

	(Unaudited) September 30, 2013	December 31, 2012
Assets		
Current assets:		
Cash	$ 1,454	$ 16,216
Accounts receivable	20,242	13,735
Total current assets	21,696	29,951
Investments in mineral properties, net of accumulated amortization of $185,457 and $132,499, respectively	400,000	1,582,324
Capitalized financing costs, net of amortization of $38,724 and $6,737, respectively	171,353	41,263
Total assets	$ 593,049	$ 1,653,538
Liabilities and Stockholders' Equity (Deficit)		
Current liabilities:		
Accounts payable and other liabilities	$ 827,441	$ 567,629
Short term note from officer	-	39,200
Note payable - current, net of discount of $81,041 and $0 at September 30, 2013 and December 31, 2012, respectively	110,259	-
Accrued interest	117,599	41,073
Derivative liability	-	559
Total current liabilities	**1,055,299**	**648,461**
Long term liabilities:		
Note payable, net of discount of $161,916 and $178,471 at September 30, 2013 and December 31, 2012, respectively	538,425	359,529
Convertible debenture	428,306	633,306
Total long term liabilities	966,731	992,835
Total liabilities	2,022,030	1,641,296
Stockholders' equity:		
Common stock, $0.001 par value, 200,000,000 shares authorized, 72,067,441 and 47,620,406 shares issued and outstanding as of September 30, 2013 and December 31, 2012, respectively	72,068	47,621
Common stock to be issued; 11,918,020 and 6,423,708 shares as of September 30, 2013 and December 31, 2012	11,918	6,424
Additional paid-in capital	14,481,090	13,731,097
Accumulated comprehensive gain (loss)	-	4,706
Accumulated deficit	(15,994,057)	(13,777,606)
Total stockholders' equity	(1,428,981)	12,242

Total liabilities and stockholders' equity	$	593,049	$	1,653,538

The accompanying notes are an integral part of these condensed financial statements

American Petro-Hunter, Inc.
Condensed Statements of Operations

	For the three months ended September 30, 2013	For the three months ended September 30, 2012	For the nine months ended September 30, 2013	For the nine months ended September 30, 2012
Revenue	$ 32,934	$ 78,671	$ 107,943	$ 266,348
Cost of Goods Sold				
Production and amortization	42,487	52,006	107,044	172,226
Gross profit (loss)	(9,553)	26,665	899	94,122
General and administrative	143,577	157,681	429,600	414,777
Executive compensation	51,000	69,000	153,000	430,000
Impairment expense	1,172,547	-	1,172,547	256,737
Total expenses	1,367,124	226,681	1,755,147	1,101,514
Net loss before other income (expense)	(1,376,677)	(200,016)	(1,754,248)	(1,007,392)
Other income (expense):				
Gain (loss) on sale of mineral properties	-	(33,530)	-	(33,530)
Gain on forgiveness of debt	-	-	-	322,731
Gain (loss) on derivative liability	-	(138,073)	-	(138,073)
Interest expense	(166,164)	(1,220,898)	(462,203)	(1,681,602)
Total other income (expense)	(166,164)	(1,392,501)	(462,203)	(1,530,474)
Net loss before income taxes	(1,542,841)	(1,592,517)	(2,216,451)	(2,537,866)
Provision for income taxes	-	-	-	-
Net loss	(1,542,841)	(1,592,517)	(2,216,451)	(2,537,866)
Other comprehensive income (expense)	12,131	-	(4,706)	8,114
Comprehensive loss	$ (1,530,710)	$ (1,592,517)	$ (2,221,157)	$ (2,529,752)
Weighted average common shares outstanding - basic and fully diluted	64,021,355	47,470,406	56,380,005	42,307,840
Net loss per common share basic and fully diluted	$ (0.024)	$ (0.034)	$ (0.039)	$ (0.060)

The accompanying notes are an integral part of these condensed financial statements

American Petro-Hunter, Inc.
Condensed Statement of Cash Flows

	For the nine months ended September 30,	
	2013	2012
Cash flows from operating activities		
Net (loss)	$ (2,216,451)	$ (2,537,866)
Adjustments to reconcile net (loss) to net cash used in operating activities:		
Shares issued for compensation	-	189,000
Amortization of discount	251,238	225,306
Impairment expense	1,172,547	256,737
Amortization of mineral properties	52,957	86,218
Amortization of prepaid financing costs	31,987	2,477
Recognized (gain) loss on fair market value of derivative liability		138,073
Stock and warrants issued for financing	43,886	1,107,886
Gain on forgiveness of debt	-	(322,731)
Loss on sale of mineral properties	-	33,530
Changes in operating assets and liabilities:		
(Increase) decrease in accounts receivable	(6,507)	15,528
(Increase) decrease in prepaid expenses	-	29,100
Increase (decrease) in accounts payable and accrued liabilities	295,469	204,222
Increase (decrease) in accrued interest	76,526	175,980
Net cash provided (used) by operating activities	(298,348)	(396,540)
Cash flows from investing activities		
Proceeds from sale of mineral properties	-	110,500
Acquisition of mineral properties	(43,180)	(406,744)
Net cash provided (used) by investing activities	(43,180)	(296,244)
Cash flows from financing activities		
Short-term note from officer, net	-	39,200
Proceeds from sale of common stock	14,500	-
Proceeds from note payable, net	312,266	473,350
Proceeds from convertible debenture	-	198,000
Net cash provided (used) by financing activities	326,766	710,550
Net increase (decrease) in cash	(14,762)	17,766
Cash - beginning	16,216	2,609
Cash - ending	$ 1,454	$ 20,375
Supplemental disclosures:		
Interest paid	$ 55,959	$ 107,517
Income taxes paid	$ -	$ -
Non-cash transactions:		
Shares issued for compensation	$ -	$ 189,000
Shares issued for capitalized financing costs	$ 150,000	$ -
Accounts payable converted to stock	$ 35,800	$ 239,469

Note payable and accrued interest converted to stock	$	218,200	$	3,375,846

The accompanying notes are an integral part of these condensed financial statements

American Petro-Hunter Inc.
Notes to Condensed Financial Statements
September 30, 2013

1. Nature and Continuance of Operations

American Petro-Hunter Inc. (the Company) was incorporated in the State of Nevada on January 24, 1996 as Wolf Exploration Inc. On March 17, 1997, Wolf Exploration Inc. changed its name to Wolf Industries Inc.; on November 21, 2000, they changed its name to Travelport Systems Inc., and on August 17, 2001, changed its name to American Petro- Hunter Inc.

The Company is evaluating the acquisition of certain natural resource projects with the intent of developing such projects. The Company focus is currently in locating and assessing potential acquisition targets, including real property, oil and gas companies.

Basis of presentation

The accompanying unaudited condensed financial statements contain all adjustments (consisting only of normal recurring adjustments) which, in the opinion of management, are necessary to present fairly the financial position of the Company as of September 30, 2013, and the results of its operations and cash flows for the nine months ended September 30, 2013 and 2012. Certain information and footnote disclosures required under accounting principles generally accepted in the United States of America (U.S. GAAP) have been condensed or omitted from the following condensed financial statements pursuant to the rules and regulations of the SEC. In the opinion of management, the accompanying financial statements include all adjustments, which are of a normal and recurring nature, necessary to present fairly our financial position and results of operations. Certain reclassifications have been made to prior periods to conform to current presentations.

It is suggested that the following financial statements be read in conjunction with the financial statements and notes thereto included in the Company s annual report on Form 10-K for the year ended December 31, 2012. The Company does not believe there are any recently issued, but not yet effective, accounting standards that would have a significant impact on the Company s financial position or results of operations as of and for the nine months ended September 30, 2013.

The results of operations for the nine months ended September 30, 2013 and 2012 are not necessarily indicative of the results of the entire fiscal year or for any other period.

Going Concern

These financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) applicable to a going concern, which contemplates the realization of assets and the satisfaction of liabilities and commitments in the normal course of business. The Company has an accumulated deficit of $15,994,057 as of September 30, 2013 and has current liabilities that are $1,033,603 in excess of its current assets. The Company has limited assets and requires additional funds to maintain its operations. Management s plan in this regard is to raise equity financing as required. There can be no assurance that sufficient funding will be obtained. The foregoing matters raise substantial doubt about the Company s ability to continue as a going concern. The financial statements do not include any adjustments relating to the recoverability and classification of recorded assets, or the amounts of and classification of liabilities that might be necessary in the event the Company cannot continue in existence.

2. Significant Accounting Policies

The following is a summary of significant accounting policies used in the preparation of these financial statements.

Income taxes

The Company accounts for income taxes under FASB Codification Topic 740-10-25 (ASC 740-10-5). Under ASC 740-10-25, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Under ASC 740-10-25, the effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. See footnote 8 for further details.

Revenue Recognition

It is our policy that revenues will be recognized in accordance with ASC subtopic 605-10. Under ASC 605-10, product revenues are recognized when persuasive evidence of an arrangement exists, delivery has occurred, the sales price is fixed and determinable and collectability is reasonably assured.

Use of estimates

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

Cash Equivalents

The Company maintains cash balances in interest and non-interest bearing accounts. For the purpose of these financial statements, all highly liquid cash and investments with a maturity of three months or less are considered to be cash equivalents.

Net loss per share

In accordance with ASC subtopic 260-10, the basic loss per common share is computed by dividing net loss available to common stockholders by the weighted average number of common shares outstanding. Diluted loss per common share is computed similar to basic loss per common share except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potential common shares had been issued and if the additional common shares were dilutive. For the three months and nine months ended September 30, 2013 and 2012, the denominator in the diluted EPS computation is the same as the denominator for basic EPS due to the anti-dilutive effect of the stock warrants and convertible debt on the Company s net loss.

Financial instruments

The Company s financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable, and notes payable. Unless otherwise noted, it is management s opinion that the Company is not exposed to significant interest, or credit risks arising from these financial instruments. The fair values of these financial instruments approximate their carrying values because of their relatively short-term maturities. See Note 5 for further details.

Fair Value of Financial Instruments

The Company has financial instruments whereby the fair value of the financial instruments could be different from that recorded on a historical basis in the accompanying balance sheets. The Company's financial instruments consist of cash, accounts receivable, accounts payable, and notes payable. The carrying amounts of the Company's financial instruments approximate their fair values as of September 30, 2013 and December 31, 2012, due to their short-term nature. See Note 5 for further details.

Reclassifications

Certain reclassifications have been made to the prior years financial statements to conform to the current year presentation. These reclassifications had no effect on previously reported results of operations or retained earnings.

Oil and Gas Properties

We follow the successful efforts method of accounting for oil and gas exploration and production activities. All costs for development wells, related plant and equipment, proved mineral interests in oil and gas properties are capitalized. Costs of exploratory wells are capitalized pending determination of whether the wells found proved reserves. Cost of wells that are assigned proved reserves remain capitalized. All other exploratory wells and costs are expensed.

Depreciation, depletion and amortization of all capitalized costs of proved oil and gas producing properties are expensed using the straight-line method over the estimated life of each well. Period valuation provisions for impairment of capitalized costs of unproved mineral interests are expensed. The costs of unproved properties are excluded from amortization until the properties are proved.

Unproved properties are assessed periodically individually when drilling and flow testing results indicate whether there is an economic resource or not. All capitalized costs associated with properties that have been determined to be a dry-hole or uneconomic are impaired when that determination is made. Proved properties are assessed periodically for impairment on an individual basis. Events that can trigger the test for possible impairment include significant decreases in the market value of a property, significant change in the extent or manner of use or change in property and the expectation that a property will be sold or otherwise disposed of significantly sooner than the previously estimated useful life. The assessment is done by comparing each property s carrying value to their associated estimated undiscounted future net cash flows. Impaired properties are written down to their estimated fair values. The resulting impairment would be expensed to operations as impairment expense in the period in which it was determined that the impairment was indicated and calculated.

3. Recent Accounting Pronouncements

Management has reviewed recent accounting pronouncements issued by the FASB (including its Emerging Issues Task Force), the AICPA, and the SEC and they do not or are not believed by management to have a material impact on the Company's present or future financial statements

4. Investments in Mineral Properties

During the nine months ended September 30, 2013, the Company invested $43,180 in one investment of mineral properties. During the year ended December 31, 2012, the Company invested a total of $355,242 in four mineral properties and exchanged a Poston Prospect well with a book value of $41,000 plus cash in the amount of $6,500 for partial payment on a well located in the Oklahoma prospect. Management reviewed the carrying amount of the Company s investments in its oil and gas properties as of the balance sheet date and recognized an impairment expense in the amount of $1,172,547 and $256,737 for the nine months ended September 30, 2013 and 2012, respectively. As of September 30, 2013 and December 31, 2012, the estimated fair value of mineral properties totaled $400,000 and $1,582,324, net of accumulated amortization of $185,457 and $132,499, respectively. As of September 30, 2013, the Company has total capitalized costs of mineral properties (gross) of $585,457; $367,394 in proved properties and $218,063 in unproved properties. As of December 31, 2012, the Company has total capitalized costs of mineral properties (gross) of $1,714,822; $1,103,205 in proved properties and $611,617 in unproved properties. Capitalized costs of proved properties are amortized using the straight-line method over the estimated useful life of each well. Unproved properties are excluded from amortization. Amortization expense for the nine months ended September 30, 2013 and 2012 was $52,957 and $86,218, respectively. A summary of investments follows:

S&W Oil & Gas, LLC - Poston Prospect

On May 4, 2009, the Company entered into an Agreement with S&W Oil & Gas, LLC (S&W) to participate in the drilling for oil in the Poston Prospect #1 Lutters in Southwest Trego County, Kansas (the Poston Prospect). Pursuant to the agreement, the Company paid $64,500 in exchange for a 25% working interest in the 81.5% net revenue interest in the Poston Prospect. Subsequent to acquiring the working interest, the Company paid $138,615 in capitalized development costs necessary for completion of the initial well and the drilling and completion of a second well in the Poston Prospect. In 2011, the Company recognized an impairment of the investment in the amount of $93,879. During the year ended December 31, 2012, the Company sold its interest in the Poston Prospect for cash in the amount of $69,500, resulting in a gain of $2,621. This well contributed approximately 5% of the Company s 2012 revenue and 0% of the revenue for the nine months ended September 30, 2013.

Oklahoma prospects

During 2010 and 2011, the Company acquired various working interest percentages ranging from 5% to 50%, from Bay Petroleum for mineral properties located in Oklahoma in exchange for cash totaling $1,992,330. During the year ended December 31, 2011, one well was determined to be a dry hole and its full $80,000 carrying value was impaired. During the year ended December 31, 2012, the Company acquired additional working interests in the Oklahoma prospects for cash in the amount of $355,242 and property valued at $41,000. During the year ended December 31, 2012, two of the wells were determined to be uneconomic and $565,737 of impairment was taken to reduce the properties to their fair value. During the nine months ended September 30, 2013, the Company invested $43,180 in these properties. Management reviewed the carrying amount of the Company s investments in its oil and gas properties as of the balance sheet date and recognized an impairment expense in the amount of $1,172,547 for the nine months ended September 30, 2013 related to these properties. The Oklahoma prospects wells contributed approximately 95% of the Company s 2012 revenue and 100% of the revenue for the nine months ended September 30, 2013.

5. Fair Value Measurements

The Company adopted ASC Topic 820-10 at the beginning of 2009 to measure the fair value of certain of its financial assets required to be measured on a recurring basis. The adoption of ASC Topic 820-10 did not impact the Company s financial condition or results of operations. ASC Topic 820-10 establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). ASC Topic 820-10 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants on the measurement date. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability. The three levels of the fair value hierarchy under ASC Topic 820-10 are described below:

Level 1 Valuations based on quoted prices in active markets for identical assets or liabilities that an entity has the ability to access.

Level 2 Valuations based on quoted prices for similar assets and liabilities in active markets, quoted prices for identical assets and liabilities in markets that are not active, or other inputs that are observable or can be corroborated by observable data for substantially the full term of the assets or liabilities.

Level 3 Valuations based on inputs that are supportable by little or no market activity and that are significant to the fair value of the asset or liability.

The following table presents a reconciliation of all assets and liabilities measured at fair value on a recurring basis as of:

	Level 1	Level 2	Level 3	Total
September 30, 2013:				
Cash	$ 1,454	$ -	$ -	$ 1,454
Accounts receivable	-	20,242	-	20,242
Accounts payable and other liab.	-	(945,040)	-	(945,040)
Notes payable, net of discount	-	(1,076,990)	-	(1,076,990)
December 31, 2012:				
Cash	$ 16,216	$ -	$ -	$ 16,216
Accounts receivable	-	13,735	-	13,735
Accounts payable and other liab.	-	(608,702)	-	(608,702)
Derivative liability	-	(559)	-	(559)
Notes payable, net of discount	-	(1,032,035)	-	(1,032,035)

6. Debt and Debt Guarantee

Short term note from Officer

During the year ended December 31, 2012, the Company issued a promissory note in the amount of $39,200 for cash advances received from an officer of the Company. The note is non-interest bearing, unsecured and due on demand. On September 27, 2013, the Company entered into an agreement to issue 3,768,844 restricted shares of stock at $0.0199 for an amount of $75,000 in lieu of payment towards this note and $35,800 in other payables owed. As of September 30, 2013, the balance on this note is $0.

Miscellaneous Notes Payable

On October 18, 2006, the Company issued a promissory note in the amount of $25,000. The note bears interest at a rate of 12% per annum, is unsecured and matured on May 18, 2007. On March 26, 2012, the holder of the note elected to convert the entire principal balance together with accrued interest of $21,819 into 187,277 shares of the Company s common stock at a conversion rate of $0.25 per share. As of December 31, 2012, there was no balance due on this note.

In August 2011, the Company issued a promissory note in the amount of $71,000. The note bears interest at a rate of 24% per annum, is unsecured and due on demand. On April 30, 2012, the holder of the note elected to convert the entire principal balance together with accrued interest of $12,140 into 332,561 shares of the Company s common stock at a conversion rate of $0.25 per share. As of December 31, 2012, there was no balance due on this note.

In December, 2011, the Company issued a promissory note in the amount of $79,980 to Centennial Petroleum Partners LLC (CPP). The note bears interest at a rate of 6% per annum, is unsecured and due on demand. On April 30, 2012, the holder of the note elected to convert the entire principal balance together with accrued interest of $2,688 into 330,671 shares of the Company s common stock at a conversion rate of $0.25 per share. As of December 31, 2012, there was no balance due on this note.

In 2011, CPP was assigned the 6% royalty interest originally granted to Maxum Overseas Fund. The royalty interest was valued at $113,164 utilizing the present value of estimated future payments due over the remaining life of the wells. The liability was recorded with corresponding prepaid financing costs to be amortized over the remaining term of the debt. For the years ended December 31, 2012 and 2011, $42,436 and $35,364, respectively, was amortized into interest expense in relation to this prepaid. During the year ended December 31, 2012, in connection with the royalty termination agreement discussed below, the Company has recorded a gain of $77,800 on the forgiveness of future royalty payments of $108,746 net of the unamortized financing costs of $30,946.

On July 3, 2012 in connection with the Purchase Agreement between the Company and ASYM Energy Opportunities, LLC, CPP agreed to enter into a royalty termination agreement, resulting in the elimination of their 6% royalty interest in exchange for anti-dilution protection with respect to the shares issued in the conversion of their note payable at a conversion rate of $0.25. The anti-dilution protection provides that in the event the Company issues warrants to a third party with an exercise price less than the conversion rate of $0.25, the Company will issue additional shares for the previous conversions equal to the difference between the number of shares calculated utilizing the variable ASYM warrant exercise price less the number of shares previously issued subject to a ceiling of 4.99% of the total outstanding shares of the Company. On July 3, 2012, the Company estimated the potential future number of anti-dilution share issuances required pursuant to the agreements to be 2,385,311 and recorded a derivative liability and corresponding comprehensive income (loss) in the amount of $333,943 representing the fair value of the potential anti-dilutioSTYLE="border-top:1px solid #000000">

Cash flows from financing activities:

Purchase and retirement of treasury stock	(899)	(656)
Proceeds from exercise of stock options	26,647	6,867
Proceeds from issuance of common stock under employee stock purchase plan	1,752	1,202
Excess tax benefit from stock-based compensation	3,426	2,112
Net cash provided by financing activities	30,926	9,525
Net increase (decrease) in cash and cash equivalents	48,105	(73,654)
Cash and cash equivalents, at beginning of period	126,173	172,202

Cash and cash equivalents, at end of period	$174,278	$98,548

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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NETGEAR, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1. The Company and Summary of Significant Accounting Policies

NETGEAR, Inc. (NETGEAR or the Company) was incorporated in Delaware in January 1996. The Company is a global networking company that delivers innovative products to consumers, businesses and service providers. For consumers, the Company makes high performance, dependable and easy-to-use home networking, storage and digital media products to connect people with the Internet and their content and devices. For businesses, the Company provides networking, storage and security solutions without the cost and complexity of Big IT. The Company also supplies leading service providers with retail proven, whole home networking solutions for their customers. The Company s products are built on a variety of proven technologies such as wireless, Ethernet and powerline, with a focus on reliability and ease-of-use. The Company sells products primarily through a global sales channel network, which includes traditional retailers, online retailers, wholesale distributors, direct market resellers, or DMRs, value added resellers, or VARs, and broadband service providers.

The accompanying unaudited condensed consolidated financial statements include the accounts of NETGEAR, Inc., and its wholly owned subsidiaries. They have been prepared in accordance with established guidelines for interim financial reporting and with the instructions of Form 10-Q and Article 10 of Regulation S-X. All significant intercompany balances and transactions have been eliminated in consolidation. The balance sheet dated December 31, 2010 has been derived from audited financial statements at such date. In the opinion of management, the unaudited condensed consolidated financial statements reflect all adjustments considered necessary (consisting only of normal recurring adjustments) to fairly state the Company s financial position, results of operations and cash flows for the periods indicated. These unaudited condensed consolidated financial statements should be read in conjunction with the notes to the consolidated financial statements included in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2010.

The Company s fiscal year begins on January 1 of the year stated and ends on December 31 of the same year. The Company reports its interim results on a fiscal quarter basis rather than on a calendar quarter basis. Under the fiscal quarter basis, each of the first three fiscal quarters ends on the Sunday closest to the calendar quarter end, with the fourth quarter ending on December 31.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect (i) the reported amounts of assets and liabilities, (ii) the disclosure of contingent assets and liabilities at the date of the financial statements, and (iii) the reported amounts of revenues and expenses during the reported period. Actual results could differ materially from those estimates and operating results for the three months and nine months ended October 2, 2011 are not necessarily indicative of the results that may be expected for the year ending December 31, 2011.

The Company has made certain reclassifications to prior period net revenue by geography in order to conform to the current period presentation. For details of these reclassifications, please see Note 12 of the Notes to Unaudited Condensed Consolidated Financial Statements.

The Company s significant accounting policies are disclosed in the Company s Annual Report on Form 10-K for the year ended December 31, 2010. The Company s significant accounting policies have not materially changed during the three and nine months ended October 2, 2011.

2. Recent Accounting Pronouncements

In December 2010, the FASB issued ASU 2010-29, Business Combinations (Topic 805): Disclosure of Supplementary Pro Forma Information for Business Combinations. ASU 2010-29 specifies that, for material business combinations when comparative financial statements are presented, revenue and earnings of the combined entity should be disclosed as though the business combination had occurred as of the beginning of the comparable prior annual reporting period. ASU 2010-29 also expands the supplemental pro forma disclosures to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. ASU 2010-29 is effective prospectively for the Company for business combinations with an acquisition date on or after January 1, 2011. Since the adoption of the update to the authoritative guidance for consolidation only requires additional disclosures, the adoption will not impact the Company s consolidated financial position, results of operations or cash flows.

In May 2011, the FASB issued ASU 2011-04, Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements. ASU 2011-04 contains certain updates to the measurement guidance as well as enhanced disclosure requirements. The most significant change in disclosures is an expansion of the information required for Level 3 measurements, including enhanced disclosure for: (1) the valuation processes used by the reporting entity; and (2) the sensitivity of the fair value measurement to changes in unobservable inputs and the interrelationships between those unobservable inputs, if any. ASU 2011-04 will only impact the Company s Level 3 disclosures. ASU 2011-04 is effective prospectively for the Company in the first quarter of fiscal 2012. The adoption is not expected to have a material impact on the Company s consolidated financial position, results of operations or cash flows.

In June 2011, the FASB issued ASU 2011-05, Presentation of Comprehensive Income. ASU 2011-05 eliminates the current option to report other comprehensive income and its components in the statement of changes in equity. ASU 2011-05 allows two presentation alternatives: present items of net income and other comprehensive income (1) in one continuous statement, referred to as the statement of comprehensive income or (2) in two separate, but consecutive, statements of net income and other comprehensive income. ASU 2011-05 is effective prospectively for the Company in the first quarter of fiscal 2012. The Company is currently evaluating which presentation alternative it will utilize. Since the adoption of the authoritative guidance only requires additional disclosures, the adoption will not impact the Company s consolidated financial position, results of operations or cash flows.

In September 2011, the FASB issued ASU 2011-08, Intangibles Goodwill and Other (Topic 350): Testing Goodwill for Impairment. ASU 2011-08 permits an entity to make a qualitative assessment of whether it is more likely than not that a reporting unit s fair value is less than its carrying amount before applying the two-step goodwill impairment test. If an entity concludes that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, it would not be required to perform the two-step impairment test for that reporting unit. The Company has elected to early adopt ASU 2011-08 in the fourth quarter of fiscal year 2011. The adoption is not expected to have a material impact on the Company s consolidated financial position, results of operations or cash flows.

3. Business Acquisitions

Leaf Networks, LLC

On January 15, 2010, the Company completed the acquisition of certain intellectual property and other assets of Leaf Networks, LLC (Leaf), a developer of virtual networking software. The acquisition qualified as a business acquisition and was accounted for using the purchase method of accounting. The Company believes the acquisition will accelerate the Company s continuing networking technology research and development initiatives. The aggregate purchase price was $2.1 million, of which $2.0 million was paid in cash in the three months ended March 28, 2010 and $100,000 was paid in the three months ended April 3, 2011.

Additionally, the acquisition agreement specified that Leaf shareholders may receive a total additional payout of up to $900,000 in cash over the three years following the closing of the acquisition if developed products pass certain acceptance criteria. During the three months ended March 28, 2010, the Company determined that the present value of the $900,000 potential additional payout was approximately $800,000. For each subsequent quarter, the Company will measure at fair value for each reporting period and record a liability. The Company paid $400,000 for the first portion of this additional payout in the three months ended April 3, 2011. As of October 2, 2011, the Company had determined the remaining acceptance criteria for the final $500,000 portion of the eligible additional payout were nearing completion, and is carrying a liability for the entire $500,000.

The results of Leaf s operations have been included in the consolidated financial statements since the date of acquisition. The historical results of operations of Leaf prior to the acquisition were not material to the Company s results of operations.

In accordance with the acquisition method of accounting for business combinations, the Company allocated the total purchase price to identifiable intangible assets based on each element s estimated fair value. Acquisition costs were expensed as incurred, and were immaterial for this transaction. Purchased intangibles, representing the existing technology acquired from Leaf, will be amortized on a straight-line basis over their respective estimated useful lives. Goodwill was recorded based on the residual purchase price after allocating the purchase price to the fair market value of intangible assets acquired. Goodwill arose as a result of the $800,000 present valuation of the $900,000 potential additional payout, plus $100,000 in additional payment consideration. The allocation of the purchase price was as follows (in thousands):

Intangibles, net	$ 2,000
Goodwill	900

Total purchase price allocation	$ 2,900

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Of the $900,000 of goodwill recorded on the acquisition of Leaf, approximately $471,000 was deductible for federal and state income tax purposes.

The $2.0 million in acquired intangible assets was designated as existing technology. The value was calculated based on the present value of the future estimated cash flows derived from projections of future revenue attributable to existing technology. This $2.0 million will be amortized over its estimated useful life of seven years.

Westell Technologies, Inc.

On April 15, 2011, the Company completed the acquisition of certain intellectual property and other assets of the Customer Networking Solutions division of Westell Technologies, Inc. (Westell) at a purchase price of $37.0 million in cash. The acquisition included inventories, property and equipment, intangible assets, and liabilities that existed at the closing date, including employee bonuses and product warranties. The acquisition qualifies as a business combination and was accounted for using the acquisition method of accounting. The Company believes the acquisition will bolster its service provider revenue growth and strengthen its market position among U.S. telecommunications operators.

The results of Westell s operations have been included in the consolidated financial statements since the date of acquisition. The historical results of operations of Westell prior to the acquisition were not material to the Company s results of operations.

In accordance with the acquisition method of accounting for business combinations, the Company allocated the total purchase price to identifiable intangible assets based on each element s estimated fair value. Acquisition costs were expensed as incurred, and were immaterial for this transaction. Purchased intangibles will be amortized on a straight-line basis over their respective estimated useful lives. Goodwill was recorded based on the residual purchase price after allocating the purchase price to the fair market value of assets acquired and liabilities assumed. Goodwill arises as a result of, among other factors, future unidentified new products and new technologies as well as the implicit value of future cost savings as a result of the combining of entities. The Company may adjust the preliminary purchase price allocation after obtaining more information regarding, among other things, liabilities assumed, and revisions of preliminary estimates.

The following table summarizes the estimated fair values of the assets and liabilities assumed at the acquisition date (in thousands):

Inventories	$ 6,290
Property and equipment, net	119
Intangibles, net	19,500
Current liabilities	(646)
Goodwill	11,746
Total consideration	$ 37,009

Of the $11.7 million of goodwill recorded on the acquisition of Westell, approximately $9.3 million is deductible for U.S. federal and state income tax purposes.

A total of $15.7 million of the $19.5 million in acquired intangible assets was designated as customer contracts and related relationships. The value was calculated based on the present value of the future estimated cash flows derived from projections of future operations attributable to existing customer contracts and related relationships and discounted at 19.0%. This $15.7 million is being amortized over its estimated useful life of eight years.

A total of $3.7 million of the $19.5 million in acquired intangible assets was designated as core technology. The value was calculated based on the present value of the future estimated cash flows derived from estimated savings attributable to the core technology and discounted at 16.0%. This $3.7 million is being amortized over its estimated useful life of four years.

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A total of $100,000 of the $19.5 million in acquired intangible assets was designated as order backlog. The value was calculated based on an estimate of order backlog using the expected cash flow for the orders and discounted at 3.3%. This $100,000 has been fully amortized as of October 2, 2011.

4. Stock-based Compensation

The Company grants options and restricted stock units from the Amended and Restated 2006 Long-Term Incentive Plan, under which awards may be granted to all employees. In addition, the Company s stock option program includes the 2003 Stock Plan, from which the Company does not currently grant awards, but may choose to do so. Award vesting periods for these plans are generally four years. As of October 2, 2011, a total of 790,067 shares were reserved for future grants under these plans.

Additionally, the Company sponsors an Employee Stock Purchase Plan (the ESPP), pursuant to which eligible employees may contribute up to 10% of base compensation, subject to certain income limits, to purchase shares of the Company s common stock. Employees may purchase stock semi-annually at a price equal to 85% of the fair market value on the purchase date.

The following table sets forth the total stock-based compensation expense resulting from stock options, restricted stock awards and the ESPP included in the Company s Unaudited Condensed Consolidated Statements of Operations (in thousands):

	Three Months Ended		Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
Cost of revenue	$ 259	$ 202	$ 737	$ 708
Research and development	606	556	1,873	1,709
Sales and marketing	1,264	1,134	3,949	3,539
General and administrative	1,325	1,055	3,775	3,255
	$ 3,454	$ 2,947	$ 10,334	$ 9,211

The fair value of each option award is estimated on the date of grant using the Black-Scholes-Merton option valuation model and the weighted average assumptions in the following table. The expected term of options granted is derived from historical data on employee exercise and post-vesting employment termination behavior. The risk free interest rate is based on the implied yield currently available on U.S. Treasury securities with an equivalent remaining term. Expected volatility is based on the historical volatility of the Company s stock for the three and nine months ended October 2, 2011 and October 3, 2010:

	Stock Options Three Months Ended		Stock Options Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
Expected life (in years)	4.3	4.4	4.4	4.5
Risk-free interest rate	1.09%	1.49%	1.73%	2.15%
Expected volatility	51%	50%	50%	50%
Dividend yield				

As of October 2, 2011, $23.4 million of total unrecognized compensation cost related to stock options, adjusted for estimated forfeitures, is expected to be recognized over a weighted-average period of 1.51 years. Additionally, $3.2 million of total unrecognized compensation cost related to non-vested restricted stock awards, adjusted for estimated forfeitures, is expected to be recognized over a weighted-average period of 1.14 years.

5. Product Warranties

The Company provides for estimated future warranty obligations at the time revenue is recognized. The Company s standard warranty obligation to its direct customers generally provides for a right of return of any product for a full refund in the event that such product is not merchantable or is found to be damaged or defective. At the time revenue is recognized, an estimate of future warranty returns is recorded to reduce revenue in the amount of the expected credit or refund to be provided to its direct customers. At the time the Company records the reduction to revenue related to warranty returns, the Company includes within cost of revenue a write-down to reduce the carrying value of such products to net realizable value.

The Company s standard warranty obligation to its end-users provides for replacement of a defective product for one or more years. Factors that affect the warranty obligation include product failure rates, material usage and service delivery costs incurred in correcting product failures. The estimated cost associated with fulfilling the Company s warranty obligation to end-users is recorded in cost of revenue. Because the Company s products are manufactured by third party manufacturers, in certain cases the Company has recourse to the third party manufacturer for replacement or credit for the defective products. The Company gives consideration to amounts recoverable from its third party manufacturers in determining its warranty liability.

Changes in the Company s warranty liability, which is included as a component of Other accrued liabilities in the unaudited condensed consolidated balance sheets, are as follows (in thousands):

	Nine Months Ended	
	October 2, 2011	October 3, 2010
Balance as of beginning of the period	$ 40,513	$ 30,610
Provision for warranty liability made during the period	42,961	48,805
Settlements made during the period	(42,898)	(39,954)
Balance at end of period	$ 40,576	$ 39,461

6. Shipping and Handling Fees and Costs

The Company includes shipping and handling fees billed to customers in net revenue. Shipping and handling costs associated with inbound freight are included in cost of revenue and ending inventory. Shipping and handling costs associated with outbound freight are included in sales and marketing expenses and totaled $3.5 million and $10.3 million for the three and nine months ended October 2, 2011, respectively, and $3.0 million and $8.3 million for the three and nine months ended October 3, 2010, respectively.

7. Restructuring and Other Charges

In April 2011, the Company incurred $1.6 million in restructuring costs for employee severance related to the reorganization into three specific business units. Refer to Note 12, Segment Information, Operations by Geographic Area and Significant Customers of the Notes to Unaudited Condensed Consolidated Financial Statements for additional information regarding the reorganization into business units. In addition, the Company incurred $464,000 in transition services in connection with the acquisition of the Customer Networking Solutions division of Westell Technologies, Inc. Refer to Note 3, Business Acquisitions of the Notes to Unaudited Condensed Consolidated Financial Statements for additional information regarding the Westell acquisition. The Company presents expenses related to restructuring and other charges as a separate line item in its unaudited condensed consolidated statements of operations.

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The following is a summary of the accrued restructuring charges:

	Accrued Restructuring and Other Charges at December 31, 2010	Additions	Cash Payments	Accrued Restructuring and Other Charges at October 2, 2011
		(In thousands)		
Reorganization in business units	$	$ 1,630	$ (1,630)	$
Westell acquisition transition costs		464	(464)	
Current portion	$	$ 2,094	$ (2,094)	$

8. Derivative Financial Instruments

The Company s subsidiaries have had and will continue to have material future cash flows, including revenue and expenses, which are denominated in currencies other than the Company s functional currency. The Company and all its subsidiaries designate the U.S. dollar as the functional currency. Changes in exchange rates between the Company s functional currency and other currencies in which the Company transacts business will cause fluctuations in cash flow expectations and cash flow realized or settled. Accordingly, the Company uses derivatives to mitigate its business exposure to foreign exchange risk. The Company enters into foreign currency forward contracts in euros, British pounds, Australian dollars and Japanese yen to manage the exposures to foreign exchange risk related to expected future cash flows on certain forecasted revenue, costs of revenue, operating expenses and existing assets and liabilities. The Company does not enter into derivatives transactions for trading or speculative purposes.

Cash flow hedges

To help manage the exposure of operating margins to fluctuations in foreign currency exchange rates, the Company hedges a portion of its anticipated foreign currency revenue, costs of revenue and certain operating expenses. These hedges are designated at the inception of the hedge relationship as cash flow hedges under the authoritative guidance for derivatives and hedging. Effectiveness is tested at least quarterly both prospectively and retrospectively using regression analysis to ensure that the hedge relationship has been effective and is likely to remain effective in the future. The Company typically hedges portions of its anticipated foreign currency exposure for three to five months. The Company enters into about six forward contracts per quarter with an average size of about $6 million USD equivalent related to its cash flow hedging program.

The Company expects to reclassify to earnings all of the amounts recorded in other comprehensive income associated with its cash flow hedges over the next 12 months. Other comprehensive income associated with cash flow hedges of foreign currency revenue is recognized as a component of net revenue in the same period as the related revenue is recognized. Other comprehensive income associated with cash flow hedges of foreign currency costs of revenue and operating expenses are recognized as a component of cost of revenue and operating expense in the same period as the related costs of revenue and operating expenses are recognized.

Derivative instruments designated as cash flow hedges must be de-designated as hedges when it is probable the forecasted hedged transaction will not occur within the designated hedge period or if not recognized within 60 days following the end of the hedge period. Deferred gains and losses in other comprehensive income associated with such derivative instruments are reclassified immediately into earnings through other income and expense. Any subsequent changes in fair value of such derivative instruments also are reflected in current earnings unless they are re-designated as hedges of other transactions. The Company did not recognize any material net gains or losses related to the loss of hedge designation on discontinued cash flow hedges during the three and nine months ended October 2, 2011 and October 3, 2010, respectively.

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Non-designated hedges

The Company enters into non-designated hedges under the authoritative guidance for derivatives and hedging to manage the exposure of non-functional currency monetary assets and liabilities held on its financial statements to fluctuations in foreign currency exchange rates, as well as to reduce volatility in other income and expense. The non-designated hedges are generally expected to offset the changes in value of its net non-functional currency asset and liability position resulting from foreign exchange rate fluctuations. Foreign currency denominated accounts receivable and payable are hedged with non-designated hedges when the related anticipated foreign revenue and expenses are recognized in the Company s financial statements. The Company also hedges certain non-functional currency monetary assets and liabilities that may not be incorporated into the cash flow hedge program. The Company adjusts its non-designated hedges monthly and enters into about 11 non-designated derivatives per quarter. The average size of its non-designated hedges is about $2 million USD equivalent and these hedges range from one to five months in duration.

The Company may choose not to hedge certain foreign exchange exposures for a variety of reasons, including, but not limited to, immateriality, accounting considerations and the prohibitive economic cost of hedging particular exposures. There can be no assurance the hedges will offset more than a portion of the financial impact resulting from movements in foreign exchange rates. The Company s accounting policies for these instruments are based on whether the instruments are designated as hedge or non-hedge instruments in accordance with the authoritative guidance for derivatives and hedging. The Company records all derivatives on the balance sheet at fair value. The effective portions of cash flow hedges are recorded in other comprehensive income until the hedged item is recognized in earnings. Derivatives that are not designated as hedging instruments and the ineffective portions of its designated hedges are adjusted to fair value through earnings in Other income (expense), net.

The Company s foreign currency forward contracts do not contain any credit-risk-related contingent features. The Company is exposed to credit losses in the event of nonperformance by the counter-parties of its forward contracts. The Company enters into derivative contracts with high-quality financial institutions and limits the amount of credit exposure to any one counter-party. In addition, the derivative contracts are limited to a time period of less than six months and the Company continuously evaluates the credit standing of its counter-party financial institutions. The counter-parties to these arrangements are large highly rated financial institutions and the Company does not consider non-performance a material risk.

The fair values of the Company s derivative instruments and the line items on the Unaudited Condensed Consolidated Balance Sheet to which they were recorded as of October 2, 2011 and December 31, 2010 are summarized as follows (in thousands):

Derivative Assets	**Balance Sheet Location**	**Fair Value at October 2, 2011**	**Balance Sheet Location**	**Fair Value at December 31, 2010**
Derivative assets not designated as hedging instruments	Prepaid expenses and other current assets	$ 1,970	Prepaid expenses and other current assets	$ 1,381
Derivative assets designated as hedging instruments	Prepaid expenses and other current assets		Prepaid expenses and other current assets	8
Total		$ 1,970		$ 1,389

Derivative Liabilities	**Balance Sheet Location**	**Fair Value at October 2, 2011**	**Balance Sheet Location**	**Fair Value at December 31, 2010**
Derivative liabilities not designated as hedging instruments	Other accrued liabilities	$ (532)	Other accrued liabilities	$ (770)
Derivative liabilities designated as hedging instruments	Other accrued liabilities	(41)	Other accrued liabilities	(19)
Total		$ (573)		$ (789)

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For details of the Company s fair value measurements, please see Note 14 of the Notes to Unaudited Condensed Consolidated Financial Statements.

The effects of the Company s derivatives not designated as hedging instruments in other income (expense), net on the Statement of Operations for the three and nine months ended October 2, 2011 and October 3, 2010 is as follows (in thousands):

Derivatives Not Designated as Hedging Instruments	Location of Gains or (Losses) Recognized in Income on Derivative	Amount of Gains or (Losses) Recognized in Income on Derivative Three Months Ended October 2, 2011	Nine Months Ended October 2, 2011
Foreign currency forward contracts	Other income (expense), net	$ 1,602	$ (1,294)

Derivatives Not Designated as Hedging Instruments	Location of Gains or (Losses) Recognized in Income on Derivative	Amount of Gains or (Losses) Recognized in Income on Derivative Three Months Ended October 3,2010	Nine Months Ended October 3,2010
Foreign currency forward contracts	Other income (expense), net	$ (3,378)	$ 48

The effects of the Company s derivative instruments on other comprehensive income and the Unaudited Condensed Consolidated Statement of Operations for the three and nine months ended October 2, 2011 are summarized as follows (in thousands):

	Three Months Ended October 2, 2011				
Derivatives Designated as Hedging Instruments	Gain or (Loss) Recognized in OCI - Effective Portion (a)	Location of Gain or (Loss) Reclassified from OCI into Income - Effective Portion	Gain or (Loss) Reclassified from OCI into Income - Effective Portion (a)	Location of Gain or (Loss) Recognized in Income and Excluded from Effectiveness Testing	Amount of Gain or (Loss) Recognized in Income and Excluded from Effectiveness Testing
Cash flow hedges:					
Foreign currency forward contracts	$ 190	Net revenue	$ 280	Other income (expense), net	$ (94)
Foreign currency forward contracts		Cost of revenue		Other income (expense), net	
Foreign currency forward contracts		Operating expenses	(20)	Other income (expense), net	
Total	$ 190		$ 260		$ (94)

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Derivatives Designated as Hedging Instruments	Nine Months Ended October 2, 2011				
	Gain or (Loss) Recognized in OCI - Effective Portion (a)	**Location of Gain or (Loss) Reclassified from OCI into Income - Effective Portion**	**Gain or (Loss) Reclassified from OCI into Income - Effective Portion (a)**	**Location of Gain or (Loss) Recognized in Income and Excluded from Effectiveness Testing**	**Amount of Gain or (Loss) Recognized in Income and Excluded from Effectiveness Testing**
Cash flow hedges:					
Foreign currency forward contracts	$ 174	Net revenue	$ 511	Other income (expense), net	$ (222)
Foreign currency forward contracts		Cost of revenue	(2)	Other income (expense), net	
Foreign currency forward contracts		Operating expenses	(18)	Other income (expense), net	
Total	$ 174		$ 491		$ (222)

The effects of the Company s derivative instruments on other comprehensive income and the Unaudited Condensed Consolidated Statement of Operations for the three and nine months ended October 3, 2010 are summarized as follows (in thousands):

Derivatives Designated as Hedging Instruments	Three Months Ended October 3, 2010				
	Gain or (Loss) Recognized in OCI - Effective Portion (a)	**Location of Gain or (Loss) Reclassified from OCI into Income - Effective Portion**	**Gain or (Loss) Reclassified from OCI into Income - Effective Portion (a)**	**Location of Gain or (Loss) Recognized in Income and Excluded from Effectiveness Testing**	**Amount of Gain or (Loss) Recognized in Income and Excluded from Effectiveness Testing**
Cash flow hedges:					
Foreign currency forward contracts	$ (5)	Net revenue	$ 220	Other income (expense), net	$ (66)
Foreign currency forward contracts		Cost of revenue	(9)	Other income (expense), net	
Foreign currency forward contracts		Operating expenses	(176)	Other income (expense), net	
Total	$ (5)		$ 35		$ (66)

Derivatives Designated as Hedging Instruments	Nine Months Ended October 3, 2010				
	Gain or (Loss) Recognized in OCI - Effective Portion (a)	**Location of Gain or (Loss) Reclassified from OCI into Income - Effective Portion**	**Gain or (Loss) Reclassified from OCI into Income - Effective Portion (a)**	**Location of Gain or (Loss) Recognized in Income and Excluded from Effectiveness Testing**	**Amount of Gain or (Loss) Recognized in Income and Excluded from Effectiveness Testing**
Cash flow hedges:					
Foreign currency forward contracts	$ 1,391	Net revenue	$ 1,860	Other income (expense), net	$ (160)
Foreign currency forward contracts		Cost of revenue	(23)	Other income (expense), net	
Foreign currency forward contracts		Operating expenses	(610)	Other income (expense), net	
Total	$ 1,391		$ 1,227		$ (160)

(a) Refer to Note 15, Comprehensive Income and Cumulative Other Comprehensive Income, Net of the Notes to Unaudited Condensed Consolidated Financial Statements, which summarizes the activity in other comprehensive income related to derivatives.

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The Company did not recognize any net gain or loss related to the ineffective portion of cash flow hedges during the nine months ended October 2, 2011 and October 3, 2010.

9. Balance Sheet Components

Accounts receivable, net (in thousands):

	October 2, 2011	December 31, 2010
Gross accounts receivable	$ 235,395	$ 241,632
Less: Allowance for doubtful accounts	(1,480)	(1,481)
Allowance for sales returns	(11,484)	(10,273)
Allowance for price protection	(3,778)	(3,147)
Total allowances	(16,742)	(14,901)
Accounts receivable, net	$ 218,653	$ 226,731

Inventories (in thousands):

	October 2, 2011	December 31, 2010
Raw materials	$ 2,225	$ 1,591
Finished goods	133,738	125,803
Total	$ 135,963	$ 127,394

The Company records provisions for excess and obsolete inventory based on forecasts of future demand. While management believes the estimates and assumptions underlying its current forecasts are reasonable, there is risk that additional charges may be necessary if current forecasts are greater than actual demand.

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Property and equipment, net (in thousands):

	October 2, 2011	December 31, 2010
Computer equipment	$ 7,036	$ 6,057
Furniture, fixtures and leasehold improvements	9,663	9,450
Software	19,839	18,553
Machinery and equipment	20,028	17,465
Construction in progress	360	30
	56,926	51,555
Less: accumulated depreciation and amortization	(40,847)	(34,052)
Property and equipment, net	$ 16,079	$ 17,503

Goodwill (in thousands):

	Goodwill at December 31, 2010	Westell Acquisition	Goodwill at October 2, 2011
Goodwill	$ 74,198	11,746	$ 85,944

Goodwill increased $11.7 million during the nine months ended October 2, 2011 due to the acquisition of the Customer Networking Solutions division of Westell Technologies, Inc. (Westell). For additional discussion of the Westell acquisition, please refer to Note 3 of the Notes to Unaudited Condensed Consolidated Financial Statements.

In the fourth quarter of 2010, the Company completed its annual goodwill impairment test based on the Company operating in one segment. The Company determined that goodwill was not impaired at December 31, 2010 since the estimated fair value of the Company exceeded its carrying value.

In the three months ended July 3, 2011, the Company reorganized its reporting structure which resulted in changes to its segment reporting from one reporting segment, which comprised the development, marketing and sale of networking products for the commercial business and home markets, to three reporting segments: retail, commercial and service provider. Refer to Note 12 of the Notes to Unaudited Condensed Consolidated Financial Statements for additional information regarding the change in segment reporting.

On the first day of the second fiscal quarter of 2011, the Company performed a goodwill impairment assessment as a result of the change in reportable segments. The Company initially determined the fair value of the new business units and allocated goodwill to each segment based on their relative fair values. The Company compared the fair value of the new reporting units to the reporting unit s carrying value and determined that goodwill was not impaired at July 3, 2011 since the estimated fair values of each of the Company s reporting units exceeded the carrying values. As the Company has not been aware of any changed conditions or situations since the last impairment testing performed that might call into question whether the current balances are fairly recorded, no impairment testing was performed in the three months ended October 2, 2011. In the fourth quarter of 2011, the Company will perform its annual goodwill impairment test based on the Company operating in three segments.

The fair value of the new business units was determined using an income approach and a market approach, which were weighted equally. Under the income approach, the fair value of an asset is based on the value of the estimated cash flows that the asset can be expected to generate in the future. These estimated future cash flows were discounted at rates ranging from 13 to 15 percent to arrive at their respective fair values. Under the market approach, the fair value of the unit is based on an analysis of financial data for publicly traded companies engaged in the same or similar lines of business.

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The following table presents the changes in carrying amount of goodwill in each of the Company s recast reportable segments at October 2, 2011 (in thousands):

	Old Segment	New Segments Retail	Commercial	Service Provider	Total
Goodwill at December 31, 2010	$ 74,198	$	$	$	$ 74,198
Relative fair value approach	(74,198)	33,546	32,043	8,609	
Goodwill at April 4, 2011		33,546	32,043	8,609	74,198
Westell acquisition goodwill				11,746	11,746
Goodwill at October 2, 2011	$	$ 33,546	$ 32,043	$ 20,355	$ 85,944

Other accrued liabilities (in thousands):

	October 2, 2011	December 31, 2010
Sales and marketing programs	$ 36,232	$ 37,020
Warranty obligation	40,576	40,513
Freight	6,683	7,174
Other	24,335	25,706
Other accrued liabilities	$ 107,826	$ 110,413

10. Net Income Per Share

Basic net income per share is computed by dividing the net income for the period by the weighted average number of common shares outstanding during the period. Diluted net income per share is computed by dividing the net income for the period by the weighted average number of shares of common stock and potentially dilutive common stock outstanding during the period. Potentially dilutive common shares include outstanding stock options and unvested restricted stock awards, which are reflected in diluted net income per share by application of the treasury stock method. Under the treasury stock method, the amount that the employee must pay for exercising stock options, the amount of stock-based compensation cost for future services that the Company has not yet recognized, and the amount of tax benefit that would be recorded in additional paid-in capital upon exercise are assumed to be used to repurchase shares.

Net income per share for the three and nine months ended October 2, 2011 and October 3, 2010 are as follows (in thousands, except per share data):

	Three Months Ended		Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
Net income	$ 26,747	$ 13,095	$ 68,533	$ 37,287
Weighted average shares outstanding:				
Basic	37,483	35,441	36,967	35,218
Dilutive potential common shares	597	568	845	673
Total diluted	38,080	36,009	37,812	35,891

Basic net income per share	$	0.71	$	0.37	$	1.85	$	1.06
Diluted net income per share	$	0.70	$	0.36	$	1.81	$	1.04

Weighted average stock options and unvested restricted stock awards to purchase 1,860,645 and 1,897,788 shares of the Company s stock for the three and nine months ended October 2, 2011, respectively, and 2,728,227 and 2,808,503 shares for the three and nine months ended October 3, 2010, respectively, were excluded from the computation of diluted net income per share because their effect would have been anti-dilutive.

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11. Income Taxes

The income tax provision for the three and nine months ended October 2, 2011 was $6.2 million, or an effective tax rate of 18.8 percent, and $22.1 million, or an effective tax rate of 24.4 percent, respectively. The tax provision for the three and nine months ended October 3, 2010 was $8.4 million or an effective tax rate of 39.2 percent and $28.9 million or an effective tax rate of 43.6 percent, respectively. The decrease in income tax expense and effective tax rate for the three and nine month period ended October 2, 2011 compared to the same periods in the prior year was primarily caused by higher forecasted pre-tax earnings in foreign jurisdictions with tax rates lower than the U.S. federal rate and the tax benefit from the reversal of tax accruals for uncertain tax positions from various tax jurisdictions where the statutes of limitation have closed. Additionally, the tax provision for the nine months ended October 2, 2011 was further reduced by discrete tax benefits recorded for the exercise of employee stock options during the period.

The higher tax expense and effective tax rate for the three months and nine months ended October 3, 2010, was caused by a loss incurred in a country where such loss provided no tax benefit. Accordingly, tax was accrued ratably on the profitable operations based on the income earned during that period while no tax benefit was accrued on the loss. The Company is subject to income taxes in the U.S. and numerous foreign jurisdictions. The Company s future foreign tax rate could be affected by changes in the composition in earnings in countries with tax rates differing from the U.S. federal rate.

The Company has recorded its liability for uncertain tax positions as part of its long-term liability as payments are not anticipated over the next 12 months. The existing tax positions of the Company continue to generate an increase in the liability for uncertain tax positions. The liability for uncertain tax positions may be reduced for liabilities that are settled with taxing authorities or on which the statute of limitations could expire without assessment from tax authorities. The possible reduction in liabilities for uncertain tax positions in multiple jurisdictions in the next 12 months is approximately $0.7 million, excluding the interest, penalties and the effect of any related deferred tax assets or liabilities.

12. Segment Information, Operations by Geographic Area and Significant Customers

Operating segments are components of an enterprise about which separate financial information is available and is regularly evaluated by management, namely the Chief Operating Decision Maker (CODM) of an organization, in order to determine operating and resource allocation decisions. By this definition, the Company has through the first fiscal quarter of 2011 operated in one business segment, which comprises the development, marketing and sale of networking products for the commercial business and home markets.

In the three months ended July 3, 2011, the Company made organizational changes that have resulted in changes to the way in which the CODM manages and evaluates the business. The Company s business is now managed in three specific business units: retail, commercial, and service provider. The retail business unit consists of high performance, dependable and easy-to-use home networking, storage and digital media products to connect people with the Internet and their content and devices. The commercial business unit consists of business networking, storage and security solutions without the cost and complexity of Big IT. The service provider business unit consists of products sold to service providers with retail proven, whole home networking solutions for their customers. Each business unit is managed by a Senior Vice President/General Manager. There is no change in the CODM before and after the reorganization of the segments.

The Company believes this new structure enables the Company to better focus its efforts on the Company s core customer segments and allows it to be more nimble and opportunistic as a company overall. The business units are determined in accordance with how management views and evaluates the Company s business and based on the criteria as outlined in the authoritative guidance. As a result, beginning in the three months ended July 3, 2011, the Company changed its segment reporting accordingly, and revised its prior period presentation to conform to the new segments.

The results of the reportable segments are derived directly from the Company s management reporting system. The results are based on the Company s method of internal reporting and are not necessarily in conformity with accounting principles generally accepted in the United States. Management measures the performance of each segment based on several metrics, including contribution income. Refer to the reconciliation of segment information to the Company s consolidated totals below to see the reconciliation of segment data to earnings prepared in conformity with accounting principles generally accepted in the United States.

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Asset data is not reviewed by the Company s CODM at the segment level and therefore is not presented. Discrete financial information on individual products and services within the respective segments is not reviewed by the Company s CODM, and therefore a separate disclosure of similar classes of products and services below the segment level is not presented.

Financial information for each reportable segment is as follows (in thousands, except percentage data):

	Three Months Ended					
	October 2, 2011			October 3, 2010		
	Net Revenue	Contribution Income	Contribution Margin	Net Revenue	Contribution Income	Contribution Margin
Retail	$ 127,082	$ 19,958	15.7%	$ 115,165	$ 18,346	15.9%
Commercial	91,059	23,013	25.3%	75,532	16,910	22.4%
Service Provider	83,659	6,662	8.0%	45,320	997	2.2%
Total	$ 301,800	$ 49,633	16.4%	$ 236,017	$ 36,253	15.4%

	Nine Months Ended					
	October 2, 2011			October 3, 2010		
	Net Revenue	Contribution Income	Contribution Margin	Net Revenue	Contribution Income	Contribution Margin
Retail	$ 352,076	$ 60,843	17.3%	$ 316,819	$ 51,189	16.2%
Commercial	247,793	56,716	22.9%	211,766	48,433	22.9%
Service Provider	271,994	24,063	8.8%	114,936	9,199	8.0%
Total	$ 871,863	$ 141,622	16.2%	$ 643,521	$ 108,821	16.9%

Segment contribution income includes all product line segment revenues less the related cost of sales, research and development and sales and marketing costs. Contribution income is used, in part, to evaluate the performance of, and allocate resources to, each of the segments. Certain operating expenses are not allocated to segments because they are separately managed at the corporate level. These unallocated indirect costs include corporate costs, such as corporate research and development, general and administrative costs, stock-based compensation expenses, amortization of intangibles, acquisition-related integration costs, restructuring costs, litigation reserves and interest and other income (expense), net.

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The reconciliation of segment information to the Company s consolidated totals is as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
Segment contribution income	$ 49,633	$ 36,253	$ 141,622	$ 108,821
Corporate and unallocated costs	(11,994)	(10,226)	(33,986)	(28,608)
Amortization of intangible assets	(1,064)	(1,344)	(3,610)	(3,970)
Stock-based compensation expense	(3,454)	(2,947)	(10,334)	(9,211)
Restructuring and other charges		8	(2,094)	76
Acquisition related compensation		(20)	(40)	(666)
Impact to cost of sales from acquisition accounting adjustments to inventory			(609)	
Litigation reserves, net	(44)		234	(211)
Interest income	115	132	350	302
Other income (expense), net	(267)	(326)	(938)	(388)
Income before income taxes	$ 32,925	$ 21,530	$ 90,595	$ 66,145

The Company s corporate headquarters and a significant portion of its operations are located in the United States. The Company also conducts sales, marketing, customer service activities and certain distribution center activities through several small sales offices in Europe, the Middle-East and Africa (EMEA) and Asia as well as outsourced distribution centers.

In the three months ended April 3, 2011, in order to achieve operational efficiencies, the Company combined its North American, Central American and South American sales forces to form the Americas territory. Previously, North America was its own geographic region and the Central American and South American territories were categorized within the Asia Pacific geographic region. Following this change, the Company is organized into the following three geographic territories: Americas, EMEA and Asia Pacific. The Company has reclassified the disclosure of net revenue by geography for prior periods to conform to the current period s presentation. The change did not result in material differences from what was previously reported. Net revenue by geography comprises gross revenue less such items as end-user customer rebates and other sales incentives deemed to be a reduction of net revenue per the authoritative guidance for revenue recognition, sales returns and price protection. For reporting purposes revenue is attributed to each geographic region based on the location of the customer. The following table shows net revenue by geography for the periods indicated (in thousands):

	Three Months Ended		Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
United States	$ 144,969	$ 120,063	$ 419,460	$ 323,774
Americas (excluding U.S.)	4,040	1,345	11,022	8,487
United Kingdom	38,010	30,590	124,831	71,087
EMEA (excluding U.K.)	81,725	58,975	227,855	167,623
Asia Pacific	33,056	25,044	88,695	72,550
Total net revenue	$ 301,800	$ 236,017	$ 871,863	$ 643,521

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Long-lived assets, comprising fixed assets, are reported based on the location of the asset. Long-lived assets by geographic location are as follows (in thousands):

	October 2, 2011	December 31, 2010
United States	$ 10,531	$ 11,808
Americas (excluding U.S.)	46	22
EMEA	321	205
China	4,411	4,848
Asia Pacific (excluding China)	770	620
	$ 16,079	$ 17,503

Significant customers are as follows (as a percentage of net revenue):

	Three Months Ended		Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
Best Buy Co., Inc. and Affiliates (Retailer)	11%	16%	11%	16%
Ingram Micro, Inc. and Affiliates (Distributor)	10%	11%	10%	12%
All others	79%	73%	79%	72%
	100%	100%	100%	100%

13. Commitments and Contingencies

Litigation and Other Legal Matters

Wi-Lan Inc. v. NETGEAR

In October 2007, a lawsuit was filed against the Company by Wi-Lan Inc. (Wi-Lan), a patent-holding company existing under the laws of Canada, in the U.S. District Court, Eastern District of Texas. Wi-Lan alleged that the Company infringed U.S. Patent Nos. 5,282,222, RE37,802 and 5,956,323. Wi-Lan accused the Company of infringement with respect to its wireless networking products compliant with the IEEE 802.11 standards and ADSL products compliant with the ITUG.992 standards. Wi-Lan also sued 21 other technology companies alleging similar claims of patent infringement. The Company filed its answer to the lawsuit in the first quarter of 2008. A claim construction hearing took place for the 222 and 802 Patents on March 11, 2010, and on May 11, 2010, the Court issued its order interpreting the claims of these patents (claim construction order). The claim construction hearing on the 323 patent occurred on September 1, 2010, and the Court subsequently issued its claim construction order for this patent. The Court ordered that infringement of the RE37,802 and 5,282,222 (Wi-Fi) patents would be tried first, as to all defendants, and infringement of the 5,956,323 (DSL) patent would be addressed in a second trial. Shortly before the beginning of the first trial, the Company and Wi-Lan entered into settlement discussions. Without admitting any wrongdoing or violation of law and to avoid the distraction and expense of continued litigation and the uncertainty of a jury verdict on the merits, the Company and Wi-Lan signed a binding release agreement in which the Company agreed to make a one-time lump sum payment to be paid by May 15, 2011 in consideration for mutual general releases. In the agreement, each party agreed to release the other party from all claims, known or unknown, under any of the 222, 802 and 323 Patents with respect to the manufacture, use, sale, etc. of products by the Company. Each party agreed to bear its own costs and attorneys fees. The Company made the required one-time lump sum payment that was due by May 15, 2011. This arrangement is not expected to have a material impact on the Company s consolidated financial position, results of operations, or cash flows. The Court has dismissed all claims between Wi-Lan and the Company, including all claims presented by Wi-Lan s complaint and all of the Company s counterclaims, and neither of the scheduled trials between Wi-Lan and the Company will occur. This litigation matter is now concluded.

Fujitsu et. al v. NETGEAR

In December 2007, a lawsuit was filed against the Company by Fujitsu Limited, LG Electronics, Inc. and U.S. Philips Corporation in the U.S. District Court, Western District of Wisconsin. The plaintiffs allege that the Company infringes U.S. Patent Nos. 6,018,642, 6,469,993 and 4,975,952. The plaintiffs accuse the Company s wireless networking products compliant with the IEEE 802.11

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standards of infringement. The Company filed its answer to the lawsuit in the first quarter of 2008. The District Court held a claim construction hearing on August 15, 2008. On September 10, 2008, the District Court issued a claim construction order. In February 2009, the parties filed numerous motions for summary judgment concerning, among other things, non-infringement, invalidity, and other affirmative defenses. In September 2009, the District Court granted the Company s motion for summary judgment of non-infringement of the three patents-in-suit. The District Court determined that the Company s compliance with the 802.11 standard did not necessarily infringe the patents-in-suit and that the plaintiffs did not provide adequate evidence regarding the function of the Company s products to put the issue of infringement before a jury. In light of the District Court s determination that the patents-in-suit were not infringed, the District Court declined to address the Company s summary judgment claims of the invalidity of the patents in question. On December 23, 2009, the Plaintiffs filed two briefs with the Federal Circuit appealing the District Court s summary judgment rulings. On December 30, 2009, the District Court ordered litigation costs in the amount $175,000 to be reimbursed to the Company, which were never collected or recognized. The Company s opposition brief to the Plaintiff s appeal was submitted on February 18, 2010. The Federal Circuit heard oral arguments on the Plaintiffs appeal on June 7, 2010. On September 20, 2010, the Federal Circuit issued a unanimous ruling that made three separate findings. It affirmed a summary judgment ruling from the District Court that the Company did not infringe the claims of a Fujitsu patent related to wireless communications technology. In addition, the Court affirmed a summary judgment ruling that the Company did not infringe the claims of an LG Electronics Inc. patent also related to wireless communications technology. Further, the court affirmed the lower court's ruling that the Company did not infringe a Philips patent for a method of transmitting data messages in a communications network, except for four products. For those four products, the Court ruled that Philips produced sufficient evidence of direct infringement, so that an infringement trial for these four products could proceed. On October 19, 2010, plaintiff LG Electronics submitted a petition for rehearing to the Federal Circuit requesting that the Federal Circuit s decision be set aside with respect to LG Electronics asserted patent and that a rehearing be granted. The Federal Circuit denied LG Electronics' petition for a rehearing on November 2, 2010, letting stand its September 20, 2010 order affirming the District Court s decision to grant the Company summary judgment of noninfringement on the patent asserted by LG Electronics. Subsequent to the Federal Circuit ruling, the parties began settlement discussions with respect to the four remaining products accused of infringing the Philips patent. On March 8, 2011, the District Court approved the settlement agreement between Philips and the Company. This arrangement is not expected to have a material impact on the Company s consolidated financial position, results of operations or cash flows. This litigation matter is now concluded.

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OptimumPath, L.L.C. v. NETGEAR

In January 2008, a lawsuit was filed against the Company by OptimumPath, L.L.C (OptimumPath), a patent-holding company existing under the laws of the State of South Carolina, in the U.S. District Court, District of South Carolina. OptimumPath claims that certain of the Company s wireless networking products infringe on OptimumPath s U.S. Patent No. 7,035,281. OptimumPath also sued six other technology companies alleging similar claims of patent infringement. The Company filed its answer to the lawsuit in the second quarter of 2008. Several defendants, including the Company, jointly filed a request for *inter partes* reexamination of the OptimumPath patent with the United States Patent and Trademark Office (the USPTO) on October 13, 2008. On January 12, 2009, a reexamination was ordered with respect to claims 1-3 and 8-10 of the patent, but denied with respect to claims 4-7 and 11-32 of the patent. On February 4, 2009, the defendants jointly filed a petition to challenge the denial of reexamination of claims 4-7 and 11-32. In March 2009, the District Court granted defendants motion to transfer the case to the U.S. District Court, Northern District of California. In July 2009, the petition to challenge the denial of reexamination of claims 4-7 and 11-32 was denied. The Company and OptimumPath attended a Court-ordered mediation on September 22, 2009 but were unable to make progress towards settlement. The Company and other defendants filed a combined claim construction/summary judgment brief on December 23, 2010. OptimumPath responded on January 20, 2011, and the defendants replied on February 3, 2011. The oral arguments on claim construction and the summary judgment motion were made on February 17, 2011. On April 12, 2011, the District Court granted defendants motion for summary judgment on OptimumPath s claim for literal infringement and defendants motion to preclude OptimumPath s infringement claims based on the doctrine of equivalents. The Court also found that the accused devices did not infringe under the doctrine of equivalents. The Court also granted defendants motion for summary judgment that asserted claims 1, 2, 6, and 9 through 13 of the 281 patent were invalidated by various prior art. The pretrial conference and trial dates were vacated. OptimumPath filed its notice of appeal to the Federal Circuit of the District Court s rulings on May 18, 2011. On May 23, 2011, the District Court entered the defendants joint request for costs in the amount of $102,554.00, which have not yet been collected or recognized. On June 29, 2011, the Federal Circuit docketed the appeal. OptimumPath submitted its opening brief in its appeal to the Federal Circuit on October 21, 2011, and the Company s answering brief is due on December 2, 2011. OptimumPath reply brief will then be due on December 16, 2011.

Ruckus Wireless v. NETGEAR

In May 2008, a lawsuit was filed against the Company by Ruckus Wireless (Ruckus), a developer of Wi-Fi technology, in the U.S. District Court, Northern District of California. Ruckus alleges that the Company infringes U.S. Patent Nos. 7,358,912 (912 Patent) and 7,193,562 (562 Patent) in the course of deploying Wi-Fi antenna array technology in its WPN824 RangeMax wireless router. Ruckus also sued Rayspan Corporation alleging similar claims of patent infringement. The Company filed its answer to the lawsuit in the third quarter of 2008. The Company and Rayspan Corporation jointly filed a request for *inter partes* reexamination of the Ruckus patents with the USPTO on September 4, 2008. The Court issued a stay of the litigation while the reexaminations proceeded in the USPTO. On November 28, 2008, a reexamination was ordered with respect to claims 11-17 of the 562 Patent, but denied with respect to claims 1-10 and 18-36. On December 17, 2008, the defendants jointly filed a petition to challenge the denial of reexamination of claims 1-10 and 18-36 of the 562 Patent. In July 2009, the petition was denied, and the remaining claims 11-17 were confirmed. The Company is appealing the confirmation of claims 11-17. On December 2, 2008, reexamination was granted with regard to the 912 Patent. In early October 2009, the Company received an Action Closing Prosecution in the reexamination of the 912 Patent. All the claims of the 912 Patent, with the exception of the unchallenged claims 7 and 8, were finally rejected by the USPTO. On October 30, 2009, Ruckus submitted an after-final amendment in the 912 Patent reexamination proceeding. The Company s comments to Ruckus after-final amendment were submitted on November 30, 2009. On December 1, 2009, the Court found that bifurcating the 562 Patent from the 912 Patent and commencing litigation on the 562 Patent while the USPTO reexamination process and appeals are still pending would be an inefficient use of the Court s resources. Accordingly, the Court ruled that the litigation stay should remain in effect. On September 12, 2010, the Company filed the rebuttal brief in its appeals of the USPTO s rulings during the reexamination of the 562 Patent, and the Company requested an oral hearing with the Board of Appeals at the USPTO to discuss this brief. On September 13, 2010, Ruckus filed a notice of appeal of the 912 Patent to appeal the adverse rulings it received from the USPTO in the reexamination of this patent. The Company filed a respondent s brief in the 912 Patent case on January 24, 2011. An oral hearing in the 562 case was set for February 1, 2011, but the Company decided to cancel it and let the USPTO decide the 562 case based solely on the previously submitted papers. On May 13, 2011, the USPTO indicated that the Company was successful in its appeal of the examiner s previous decision to allow claims 11-17 in the 562 reexamination, and the USPTO Board of Appeals reversed the examiner s decision and declared those claims invalid. On June 13, 2011, Ruckus submitted a request for rehearing by the Board of Appeals of its decision to reject claims 11-17 of the 562 Patent. On September 28, 2011, the Board of Patent Appeals and Interferences denied Ruckus s request for a rehearing in the 562 Patent reexamination case. The next step for Ruckus would be to file a notice of appeal to the Court of Appeals for the Federal Circuit. Ruckus has 60 days from September 28, 2011 until November 27, 2011in which to file such a notice.

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On November 4, 2009, Ruckus filed a new complaint in the U.S. District Court, Northern District of California alleging the Company and Rayspan Corporation infringe a patent that is related to the patents previously asserted against the Company and Rayspan Corporation by Ruckus, as discussed above. This newly asserted patent is U.S. Patent No. 7,525,486 entitled Increased wireless coverage patterns. As with the previous Ruckus action, the WPN824 RangeMax wireless router is the alleged infringing device. The Company challenged the sufficiency of Ruckus s complaint in this new action and moved to dismiss the complaint. Ruckus opposed this motion. The Court partially agreed with the Company s motion and ordered Ruckus to submit a new complaint, which Ruckus did. The initial case management conference occurred on February 11, 2010. On March 25, 2010, the Court ordered a stay until the completion of the 562 Patent s reexamination proceedings in the first Ruckus lawsuit against the Company and Rayspan. The Court instructed the parties to submit status reports to the Court every six months, apprising the Court of the status of the pending reexamination proceedings in the USPTO. Upon final exhaustion of all pending reexamination proceedings of the 562 Patent, including any appeals, the Court ordered the parties to jointly submit to the Court a letter indicating that all appeals have been exhausted and requesting a further case management conference.

On November 19, 2010, the Company filed suit against Ruckus in the U.S. District Court, District of Delaware for infringement of four of the Company s patents. The Company alleges that Ruckus s manufacture, use, sale or offers for sale within the United States or importation into the United States of products, including wireless communication products, infringe United States Patent Nos. 5,812,531, 6,621,454, 7,263,143, and 5,507,035, all owned by the Company. The Company granted Ruckus an extension to file its answer to the Company s suit, and on January 11, 2011, Ruckus filed a motion to dismiss the Company s suit based on insufficient pleadings. The Company filed its response to Ruckus s motion on January 31, 2011. In addition, on May 6, 2011, Ruckus filed a motion to transfer venue to the Northern District of California. The Court denied Ruckus motion to transfer the case to the Northern District of California and granted the Company leave to file an amended complaint rather than address the Ruckus motion to dismiss based on insufficient pleadings. The Company filed the proposed amended complaint. Nevertheless, Ruckus filed a second motion to dismiss based on insufficient pleadings by the Company. The Company has filed its opposition to Ruckus s motion, and the Court has not yet ruled on the motion.

Northpeak Wireless, LLC v. NETGEAR

In October 2008, a lawsuit was filed against the Company and 30 other companies by Northpeak Wireless, LLC (Northpeak) in the U.S. District Court, Northern District of Alabama. Northpeak alleges that the Company s 802.11b compatible products infringe certain claims of U.S. Patent Nos. 4,977,577 and 5,987,058. The Company filed its answer to the lawsuit in the fourth quarter of 2008. On January 21, 2009, the District Court granted a motion to transfer the case to the U.S. District Court, Northern District of California. In August 2009, the parties stipulated to a litigation stay pending a reexamination request to the USPTO on the asserted patents. The reexaminations of the patents are proceeding. In March 2011, the USPTO confirmed the validity of the asserted claims of the 577 patent over certain prior art references. In April 2011, the USPTO issued a final office action rejecting both asserted claims of the 058 patent as being obvious in light of the prior art. The case remains stayed by stipulation, and no trial date has been set.

WIAV Networks, LLC v. NETGEAR

In July 2009, a lawsuit was filed against the Company and over 50 other companies by WIAV Networks, LLC (WIAV) in the U.S. District Court, Eastern District of Texas. WIAV alleges that the Company and the other defendants infringe U.S. Patent Nos. 6,480,497 and 5,400,338. WIAV alleges that the Company s wireless networking devices, including various routers and gateways, infringe upon WIAV s patents. The Company filed its answer to the lawsuit in October 2009 and asserted that WIAV s patents were both invalid and not infringed upon by the Company. In March 2010, the Company and its co-defendants filed a motion to transfer the case to the U.S. District Court, Northern District of California. WIAV opposed the motion. On June 3, 2010, the Court heard the defendants motion to transfer the case from the Eastern District of Texas to the Northern District of California. The Court took the motion under consideration, and on July 15, 2010, the Court ruled that it would transfer the case to the U.S. District Court, Northern District of California. Discovery has not commenced. On August 31, 2010, the U.S. District Court, Northern District of California ordered WIAV to demonstrate why the Court should not dismiss all but the first named defendant from the lawsuit. The parties briefed and argued this issue before the Court. In response, the Court dismissed without prejudice all the defendants from the case except Hewlett-Packard Company.

PACid Group, LLC v. NETGEAR

In July 2009, a lawsuit was filed against the Company and 30 other companies by The PACid Group, LLC (PACid) in the U.S. District Court, Eastern District of Texas. PACid alleges that the Company and the other defendants infringe U.S. Patent Nos.

5,963,646 (646 Patent) and 6,049,612 (612 Patent). PACid alleges that certain unnamed NETGEAR products that use encryption methods infringe upon PACid s patents. The Company filed its answer to the lawsuit in September 2009 and asserted that PACid s patents were both invalid and not infringed by the Company. Discovery has not yet commenced. Most of the Company s chipset suppliers have settled out of the lawsuit and obtained a license to the plaintiff s asserted patents. Because most of the accused infringement occurred in the chipset, this settlement by the chipset suppliers limits the claims the plaintiff has against the Company. On March 7, 2011, the Company attended a status conference. On May 17, 2011, the Court held another status conference. At this conference, the Company indicated to the Court that a small percentage of the relevant products have non-licensed chip sets. The Court ordered that within 21 days of the status conference PACid shall produce all license agreements it has entered into; within 30 days of the status conference, all defendants shall produce a declaration on sales data; and within 14 days from that defendant production, PACid shall dismiss without prejudice the appropriate defendants. The parties complied with the order, and PACid did not dismiss the Company. On August 23, 2011, at mediation between the Company and PACid, a settlement of this lawsuit was reached. Without admitting any wrongdoing or violation of law and to avoid the distraction and expense of continued litigation and the uncertainty of a jury verdict on the merits, the Company and PACid signed a binding release agreement in which the Company agreed to make a one-time lump sum payment in consideration for mutual general releases. In the agreement, each party agreed to release the other party from all claims, known or unknown, under any of the 646 and 612 Patents with respect to the manufacture, use, sale, etc. of products by the Company. Each party agreed to bear its own costs and attorneys fees. The Company has made the required one-time lump sum payment. This arrangement is not expected to have a material impact on the Company s consolidated financial position, results of operations or cash flows. The Court has dismissed all claims between PACid and the Company, including all claims presented by PACid s complaint and all of the Company s counterclaims, and the trial in this matter will not occur. This litigation matter is now concluded.

MPH Technologies Oy v. NETGEAR

On February 4, 2010, the Company was sued by MPH Technologies Oy (MPH) for infringement of U.S. patent 7,346,926 entitled Method for Sending Messages Over Secure Mobile Communication Links. MPH alleges that the Company s VPN Client Software, Dual WAN gigabit SSL VPN Firewall, ProSafe Dual WAN VPN Firewall with 8-port 10/100 Switch, ProSafe VPN Firewall with 8-port 10/100 Switch, ProSafe VPN Firewall 8 with 8-Port 10/100 Switch, ProSafe VPN Firewall 8 with 4-Port 10/100 Mbps Switch, ProSafe 802 11 g Wireless ADSL Modem VPN Firewall Router, ProSafe Wireless-N VPN Firewall, and ProSafe 802 11 wireless VPN Firewall 8 with 8-port 10/100 Mbps Switch infringe claims of the 926 Patent. On May 17, 2010, the defendants jointly filed a motion to transfer the case to the U.S. District Court, Northern District of California. In addition, the Company filed its answer, affirmative defenses, and counterclaims on that day. On June 9, 2010, the plaintiff filed its answer to the Company s invalidity counterclaim and its response to the defendants motion to transfer. On June 23, 2010, the defendants filed their joint reply to plaintiff s response to the defendants motion to transfer venue. On July 16, 2010, the Court issued an order transferring the case to the Northern District of California. On September 10, 2010, the Company amended its answer to the complaint. The initial scheduling conference occurred on December 2, 2010. In response to this conference, the Court ordered that the Plaintiff must file its opening claim construction brief no later than May 17, 2011 and that defendants must file their responsive claim construction briefs no later than May 31, 2011. The Court also ordered that a claim construction hearing take place on June 22, 2011. The Company and plaintiff signed a settlement agreement on May 15, 2011. In the agreement, the Company agreed to pay a one-time lump sum payment and grant MPH certain other patent rights in return for each party agreeing to release the other party from all claims, known or unknown, under the patent in suit and related patents with respect to the manufacture, use, sale, etc. of products by the Company. The Company received a fully paid, worldwide, perpetual license to the patent in suit and all foreign counterparts and related patents. Each party agreed to bear its own costs and attorneys fees. The Company has subsequently made the required one-time lump sum payment. This arrangement is not expected to have a material impact on the Company s consolidated financial position, results of operations, or cash flows. On May 16, 2011, the Court dismissed the case with prejudice, with each party to bear its own attorneys fees and costs. The Company has since made the lump sum payment to MPH, and this litigation matter is now concluded.

Ericsson v. NETGEAR

On September 14, 2010, Ericsson Inc. and Telefonaktiebolaget LM Ericsson filed a patent infringement lawsuit against the Company and defendants D-Link Corporation, D-Link Systems, Inc., Acer, Inc., Acer America Corporation, and Gateway, Inc. in the U.S. District Court, Eastern District of Texas alleging that the defendants infringe certain Ericsson patents. The Company has been accused of infringing eight U.S. patents: 5,790,516; 6,330,435; 6,424,625; 6,519,223; 6,772,215; 5,987,019; 6,466,568; and 5,771,468. Ericsson generally alleges that the Company and the other defendants have infringed and continue to infringe the Ericsson patents through the defendants IEEE 802.11-compliant products. In addition, Ericsson alleges that the Company has infringed, and continues to infringe, the claimed methods and apparatuses of the 468 Patent through the Company s PCMCIA routers. The Company filed its answer to the Ericsson complaint on December 17, 2010 where it asserted the affirmative defenses of

noninfringement and invalidity of the asserted patents. On March 1, 2011, the defendants filed a motion to transfer venue to the District Court for the Northern District of California and their memorandum of law in support thereof. On March 21, 2011, Ericsson filed is opposition to the motion, and on April 1, 2011, defendants filed their reply to Ericsson s opposition to the motion to transfer. On June 8, 2011, Ericsson filed an amended complaint that added Dell, Toshiba and Belkin as defendants. At the status conference held on Jun 9, 2011, the Court set a Markman hearing for June 28, 2012 and trial for June 3, 2013. On June 14, 2011, Ericsson submitted its infringement contentions against the Company. On September 29, 2011, the Court denied the defendants motion to transfer venue to the Northern District of California. Discovery is ongoing.

Fujitsu v. NETGEAR

On September 3, 2010, Fujitsu filed a complaint against the Company, Belkin International, Inc., Belkin, Inc., D Link Corporation, D Link Systems, Inc., ZyXEL Communications Corporation, and Zyxel Communications, Inc in the U.S. District Court, Northern District of California alleging that certain of the Company s products infringe upon Fujitsu s U.S. patent Re. 36,769 patent (769 Patent) through various cards and interface devices within the Company s products. The Company answered the complaint denying the allegations of infringement and claiming that the asserted patent is invalid. In addition, the Company filed a motion to disqualify counsel for Fujitsu. The Company s disqualification motion was argued before the Court on December 16, 2010, and on December 22, 2010, the Court granted the Company s motion and disqualified counsel for Fujitsu. In response, Fujitsu requested a stipulation from all parties to reset the case management conference and scheduled hearing dates for the motions to dismiss. The initial case management conference was held on March 18, 2011. A claim construction hearing was held on October 14, 2011. The parties are currently participating in the discovery process.

Data Network Storage, LLC v. NETGEAR

In April 2009, a lawsuit was filed against the Company and 14 other companies by Data Network Storage, LLC (DNS) in the U.S. District Court for the Southern District of California. DNS alleges that the Company and the other third parties infringe U.S. Patent No. 6,098,128. In particular, DNS is alleging that several of the Company s ReadyNAS products infringe upon DNS s patents. The Company filed its answer to the lawsuit in July 2009 and asserted that DNS s patents were both invalid and had not been infringed upon by the Company. In September 2009, at a Court-sanctioned early neutral evaluation, the parties were unable to reach an agreement on a settlement, and discovery continued. On January 27, 2010, the Court denied co-defendant Fujitsu America, Inc. s motion to stay the litigation, and the Company submitted its invalidity contentions on February 1, 2010. The Company and the plaintiff entered into settlement discussions in early March. Without admitting any wrongdoing or violation of law and to avoid the distraction and expense of continued litigation and the uncertainty of a jury verdict on the merits, the Company agreed to make a one-time lump sum payment in consideration for a fully paid and perpetual license to, and a covenant not to sue on, the 128 patent and the plaintiff s entire portfolio of U.S. patents, related patents, and foreign counterparts. The Company has made the required one-time lump sum payment, and the lawsuit by DNS against the Company was dismissed with prejudice on April 23, 2010. This arrangement did not have a material impact on the Company s consolidated financial position, results of operations, or cash flows for the year ended December 31, 2010.

NETGEAR v. CSIRO

In May 2005, the Company filed a complaint for declaratory relief against the Commonwealth Scientific and Industrial Research Organization (CSIRO), in the San Jose division of the United States District Court, Northern District of California. The complaint alleged that the claims of CSIRO s U.S. Patent No. 5,487,069 are invalid and not infringed by any of Company s products. CSIRO had asserted that the Company s wireless networking products implementing the IEEE 802.11a, 802.11g, and 802.11n wireless LAN standards infringe this patent. In July 2006, the United States Court of Appeals for the Federal Circuit affirmed the District Court s decision to deny CSIRO s motion to dismiss the action under the Foreign Sovereign Immunities Act. In September 2006, the Federal Circuit denied CSIRO s request for a rehearing en banc. CSIRO filed a response to the complaint in September 2006. In December 2006, the District Court granted CSIRO s motion to transfer the case to the Eastern District of Texas, where CSIRO had brought and won a similar lawsuit against Buffalo Technology (USA), Inc., which Buffalo appealed and which was partially remanded to the District Court. The District Court consolidated this action with three related actions involving other companies (such as Buffalo) accused of infringing CSIRO s patent. The Company attended a Court-mandated mediation in November 2007 but failed to resolve the litigation. The District Court held a June 26, 2008 claim construction hearing. On August 14, 2008, the District Court issued a claim construction order and denied a motion for summary judgment of invalidity. In December 2008, the parties filed numerous motions for summary judgment concerning, among other things, infringement, validity, and other affirmative defenses. The District Court commenced a jury trial on April 13, 2009 regarding all liability issues for the four consolidated cases. On April 20, 2009, the Company and CSIRO executed a Memorandum of Understanding (MOU) setting forth the terms of a settlement and license

agreement between the Company and CSIRO. Without admitting any wrongdoing or violation of law and to avoid the distraction and expense of continued litigation and the uncertainty of a jury verdict on the merits, the Company agreed to make a one-time lump sum payment in consideration for a fully paid perpetual license and a covenant not to sue with respect to the 069 patent and all foreign counterparts and related patents. Based on the historical and estimated projected future unit sales of the Company s products that were alleged to infringe the asserted patent, the Company allocated a portion of the settlement cost towards product shipments prior to the settlement, which the Company recorded as a litigation settlement expense of $2.4 million, which was primarily recognized in the three months ended March 29, 2009. Additionally, the Company allocated $2.6 million of the settlement cost to prepaid royalties which will be recognized as a component of cost of revenue as the related products are sold. Of this $2.6 million, $413,000 and $551,000 were amortized and expensed in the year ended December 31, 2009 and December 31, 2010, respectively. Additionally, $413,000 was amortized and expensed in the nine months ended October 2, 2011.

Finoc, LLC v. NETGEAR

In February 2009, a lawsuit was filed against the Company and 14 other companies by Finoc Design Consulting OY (Finoc) in the U.S. District Court for the Eastern District of Texas. Finoc alleged that the Company s wireless DSL gateway products infringe U.S. Patent No. 6,850,560. In June 2009, without admitting any patent infringement, wrongdoing or violation of law and to avoid the distraction and expense of continued litigation, the Company agreed to make a one-time lump sum payment of $82,500 in consideration for a fully paid perpetual license to the patent in suit as well as a dismissal with prejudice by Finoc. Based on the historical and estimated projected future unit sales of the Company s products that were alleged to infringe the asserted patents, the Company allocated a portion of the settlement cost towards product shipments prior to the settlement, which the Company recorded as a litigation settlement expense in the three months ended June 28, 2009. Additionally, the Company allocated the balance of the settlement cost to prepaid royalties which will be recognized as a component of cost of revenue as the related products are sold.

Network-1 Security Solutions, Inc. v. NETGEAR

In February 2008, a lawsuit was filed against the Company by Network-1 Security Solutions, Inc. (Network-1), a patent-holding company existing under the laws of the State of Delaware, in the U.S. District Court for the Eastern District of Texas. Network-1 alleged that the Company s power over Ethernet (PoE) products infringed its U.S. Patent No. 6,218,930. Network-1 also sued six other companies alleging similar claims of patent infringement. The Company filed its answer in the second quarter of 2008. In May 2009, without admitting any patent infringement, wrongdoing or violation of law and to avoid the distraction and expense of continued litigation, the Company agreed to make a one-time lump sum payment of $350,000, which the Company recorded as a litigation settlement in fiscal 2009, in consideration for a license to the patent in suit as well as a dismissal with prejudice of the lawsuit. Under the license, the Company will pay future running royalties on certain of its PoE products which will be recognized as a component of cost of revenue as the related products are sold.

Chalumeau Power Systems v. NETGEAR.

On June 28, 2011, Chalumeau Power Systems LLC (Chalumeau) filed a complaint against several technology companies including the Company, Cisco Systems Inc., Hewlett-Packard Co., D-Link, and Avaya Inc. in Delaware alleging infringement of a patent for a remote device detection method. The patent number is U.S. Patent No. 5,991,885 (885 Patent) and is entitled Method and apparatus for detecting the presence of a remote device and providing power thereto. Chalumeau claims that the defendants have all made or sold devices that make use of infringing PoE technology, which allows electrical power and data to pass safely on Ethernet cabling. The Company is reviewing the complaint and is in the process of retaining outside legal counsel to defend it. The Company answered Chalumeau s complaint on September 1, 2011, and asserted various defenses and counterclaims, including those of noninfringement and invalidity of the 885 Patent. In October 2011, a settlement of this lawsuit was reached between Chalumeau and the Company through non-party RPX Corporation. Without admitting any wrongdoing or violation of law and to avoid the distraction and expense of continued litigation and the uncertainty of a jury verdict on the merits, the Company and Chalumeau signed a binding release agreement in which a payment was made to Chalumeau by RPX Corporation in consideration for mutual general releases from all claims, known or unknown, under the 885 Patent and its foreign counterparts with respect to the manufacture, use, sale, etc. of products by the Company. The Court has since dismissed Chalumeau s claims for relief against the Company and the Company s counterclaims for relief against Chalumeau, with prejudice and with all attorneys fees, costs and expenses levied against the party incurring the same.

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Powerline Innovations, LLC v. NETGEAR

On August 6, 2011 the Company, along with 16 other companies, was sued in the U.S. District Court, Eastern District of Texas, Tyler Division for patent infringement by a non-practicing entity called Powerline Innovations, LLC (Powerline Innovations). This is a single patent case, involving U.S. Patent No. 5,471,190, entitled Method and Apparatus for Resource Allocation in a Communication Network System. On the same day that it filed suit against the Company and 16 other companies, Powerline Innovations sued 14 additional companies in a separate suit in U.S. District Court, Eastern District of Texas for infringement of the same patent. The complaint against the Company alleges that it infringes the 5,471,190 patent based on the Company s use of methods for establishing control relationships between plural devices and names the Company s Powerline AV Ethernet Adapter, Model XAV101, as an accused infringing product. The Company is currently investigating the allegations.

Summit Data Systems LLC v. NETGEAR.

On September 1, 2010, a non-practicing entity, Summit Data Systems LLC (Summit Data Systems), sued the Company and seven other companies alleging infringement of two patents U.S. Patent No. 7,392,291 (291 Patent), entitled Architecture for Providing Block-Level Access over a Computer Network and U.S. Patent No. 7,428,581 (581 Patent), entitled Architecture for Providing Block-Level Access over a Computer Network. The 581 Patent is a continuation of the 291 Patent. The Company s ReadyNAS and NVX products were listed by the plaintiff in the complaint as accused infringing products. The Company answered the complaint on November 1, 2010, asserting that the patents are not infringed and invalid. Subsequently, the Company participated in discovery, and trial for this matter was scheduled for March 2013. In October 2011, a settlement of this lawsuit was reached between Summit Data Systems and the Company through non-party RPX Corporation. Without admitting any wrongdoing or violation of law and to avoid the distraction and expense of continued litigation and the uncertainty of a jury verdict on the merits, the Company and Summit Data Systems signed a binding release agreement in which a payment was made to Summit Data Systems by RPX Corporation in consideration for mutual general releases from all claims, known or unknown, under the 291 Patent and 581 Patents and certain other patents and applications assigned to Summit Data Systems with respect to the manufacture, use, sale, etc. of products by the Company. The Court has since dismissed Summit Data Systems s claims for relief against the Company and the Company s counterclaims for relief against Summit Data Systems, with prejudice and with all attorneys fees, costs and expenses levied against the party incurring the same.

IP Indemnification Claims

In its sales agreements, the Company typically agrees to indemnify its direct customers, distributors and resellers (the Indemnified Parties) for any expenses or liability resulting from claimed infringements of patents, trademarks or copyrights of third parties that are asserted against the Indemnified Parties, subject to customary carve outs. The terms of these indemnification agreements are generally perpetual after execution of the agreement. The maximum amount of potential future indemnification is generally unlimited. From time to time, the Company receives requests for indemnity and may choose to assume the defense of such litigation asserted against the Indemnified Parties.

In June 2006, the Company received a request for indemnification from Charter and Charter Communications Operating, LLC, related to a lawsuit filed in the U.S. District Court, Eastern District of Texas, by Rembrandt Technologies, L.P. (Rembrandt), a patent-holding company. Rembrandt also filed a similar lawsuit in the same jurisdiction against Comcast Corporation, Comcast Cable Communications, LLC and Comcast of Plano, LP. Rembrandt alleged that products implementing the DOCSIS standard, which are supplied to Charter, Comcast Corporation, Comcast Cable Communications, LLC and Comcast of Plano, LP by, among others, the Company, infringe various patents held by Rembrandt. In June 2007, the Judicial Panel on Multidistrict Litigation ordered these and other similar patent cases brought by Rembrandt consolidated and transferred to the U.S. District Court for the District of Delaware. In November 2007, the Company along with Motorola, Inc., Cisco Systems, Inc., Scientific-Atlanta, Inc., ARRIS Group, Inc., Thomson, Inc. and Ambit Microsystems, Inc. filed a complaint for declaratory judgment in the U.S. District Court for the District of Delaware against Rembrandt, seeking a declaration that eight asserted Rembrandt patents asserted in the transferred cases are either invalid or not infringed. The District Court held a claim construction hearing on August 5, 2008. On November 29, 2008, the District Court issued its claim construction order. After the District Court s order, Rembrandt agreed to drop three patents from the case, leaving five patents at issue. The District Court held a mediation on March 3-4, 2009 but the parties were unable to reach a resolution. On July 21, 2009, Rembrandt delivered to the Company and other parties an executed covenant not to sue on any of the eight patents originally in the suit, contending that the execution of the covenant divests the District Court of jurisdiction or renders moot the remaining claims and counterclaims in the action. On July 31, 2009, Rembrandt filed a motion to dismiss the litigation. While Rembrandt s motion was pending, the defendants filed motions for summary judgment, motions for sanctions, and responses to Rembrandt s motion to dismiss. In early October 2009, the District Court suspended all further dates for the case while it reviewed the pending motions and case status. On October 23, 2009, the Court ordered Rembrandt to supplement the covenant not to sue to include any products or services that comply with DOCSIS 1.0, 1.1, 2.0 or 3 and dismissed Rembrandt s various infringement claims on the eight patents with

prejudice. The Court gave Rembrandt five days to withdraw its motion to dismiss the litigation if it found the Court s conditions on dismissal to be unacceptable. Rembrandt did not withdraw its motion to dismiss the litigation, and on October 30, 2009, Rembrandt executed a covenant not to sue on any of the eight patents in the case and any products or services that comply with DOCSIS 1.0, 1.1, 2.0 or 3. The Company and its co-defendants moved for attorneys fees to be paid by Rembrandt. Rembrandt opposed the motion. On July 8, 2011, the Court denied the defendant s unopposed motion for summary judgment of noninfringement of the one patent remaining in the case, the 627 Patent. This ruling did not affect the Company since that patent was not asserted against the Company, other than postponing the Company s possible recovery of attorneys fees. On July 13, 2011, the Court dismissed without prejudice the defendants joint motion for fees because the motion is now not ripe given the Court s denial of the motion for summary judgment of noninfringement of the 627 Patent. The Company is now reviewing its options for recovering attorneys fees.

All of the above described claims against the Company, or filed by the Company, whether meritorious or not, could be time-consuming, result in costly litigation, require significant amounts of management time, and result in the diversion of significant operational resources. Were an unfavorable outcome to occur, there exists the possibility it would have a material adverse impact on the Company s financial position and results of operations for the period in which the unfavorable outcome occurs or becomes probable. In addition, the Company is subject to legal proceedings, claims and litigation arising in the ordinary course of business, including litigation related to intellectual property and employment matters.

Based on currently available information, the Company does not believe that the ultimate outcomes of any unresolved matters, individually and in the aggregate, are likely to have a material adverse effect on the Company s financial position, liquidity or results of operations within the next 12 months. However, litigation is subject to inherent uncertainties, and the Company s view of these matters may change in the future. Were an unfavorable outcome to occur, there exists the possibility of a material adverse impact on the Company s financial position and results of operations or liquidity for the period in which the unfavorable outcome occurs or becomes probable, and potentially in future periods.

Environmental Regulation

The European Union (EU) has enacted the Waste Electrical and Electronic Equipment Directive, which makes producers of electrical goods, including home and commercial business networking products, financially responsible for specified collection, recycling, treatment and disposal of past and future covered products. The deadline for the individual member states of the EU to transpose the directive into law in their respective countries was August 13, 2004 (such legislation, together with the directive, the WEEE Legislation). Producers participating in the market were financially responsible for implementing these responsibilities under the WEEE Legislation beginning in August 13, 2005. Similar WEEE Legislation has been or may be enacted in other jurisdictions, including in the United States, Canada, Mexico, China, India, Australia and Japan. The Company adopted the authoritative guidance for asset retirement and environmental obligations in the third quarter of fiscal 2005 and has determined that its effect did not have a material impact on the Company s consolidated results of operations and financial position for the three months ended October 2, 2011. The Company is continuing to evaluate the impact of the WEEE Legislation and similar legislation in other jurisdictions as individual countries issue their implementation guidance.

Additionally, the EU has enacted the Restriction of Hazardous Substances Directive (RoHS Legislation), the REACH Directive and the Battery Directive. EU RoHS Legislation, along with similar legislation in China, requires manufacturers to ensure certain substances, including polybrominated biphenyls (PBD), polybrominated diphenyl ethers (PBDE), mercury, cadmium, hexavalent chromium and lead (except for allowed exempted materials and applications), are below specified maximum concentration values in certain products put on the market after July 1, 2006. The REACH Directive similarly requires manufacturers to ensure the published list of substances of very high concern in certain products are below specified maximum concentration values. The Battery Directive prohibits use of certain types of battery technology in certain products. The Company believes it has met the requirements of the RoHS Legislation, the REACH Directive and the Battery Directive.

Additionally, the EU has enacted the Energy Using Product (EuP) Directive, which requires manufacturers of certain products to meet minimum energy efficiency limits. These limits are documented in EuP implementing measures issued for specific types of equipment and document minimum power supply efficiencies and may include required equipment standby modes which also reduce energy consumption. The Company believes it has met the requirements of the applicable EuP implementing measures.

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Employment Agreements

The Company has signed various employment agreements with key executives pursuant to which, if their employment is terminated without cause, such employees are entitled to receive their base salary (and commission or bonus, as applicable) for 52 weeks (for the Chief Executive Officer), 39 weeks (for the Senior Vice President of Worldwide Operations and Support) and up to 26 weeks (for other key executives). Such employees will also continue to have stock options vest for up to a one-year period following such termination without cause. If a termination without cause or resignation for good reason occurs within one year of a change in control, such employees are entitled to full acceleration (for the Chief Executive Officer) and up to two years acceleration (for other key executives) of any unvested portion of his or her stock options.

Leases

The Company leases office space, cars and equipment under operating leases, some of which are non-cancelable, with various expiration dates through December 2026. The terms of some of the Company s office leases provide for rental payments on a graduated scale. The Company recognizes rent expense on a straight-line basis over the lease period, and has accrued for rent expense incurred but not paid.

Guarantees and Indemnifications

The Company has entered into various inventory-related purchase agreements with suppliers. Generally, under these agreements, 50% of orders are cancelable by giving notice 46 to 60 days prior to the expected shipment date and 25% of orders are cancelable by giving notice 31 to 45 days prior to the expected shipment date. Orders are non-cancelable within 30 days prior to the expected shipment date. At October 2, 2011, the Company had $161.7 million in non-cancelable purchase commitments with suppliers. The Company establishes a loss liability for all products it does not expect to sell for which it has committed purchases from suppliers. Such losses have not been material to date.

The Company, as permitted under Delaware law and in accordance with its Bylaws, indemnifies its officers and directors for certain events or occurrences, subject to certain limits, while the officer or director is or was serving at the Company s request in such capacity. The term of the indemnification period is for the officer s or director s lifetime. The maximum amount of potential future indemnification is unlimited; however, the Company has a Director and Officer Insurance Policy that enables it to recover a portion of any future amounts paid. As a result of its insurance policy coverage, the Company believes the fair value of these indemnification agreements is minimal. Accordingly, the Company has no liabilities recorded for these agreements as of October 2, 2011.

In its sales agreements, the Company typically agrees to indemnify its direct customers, distributors and resellers for any expenses or liability resulting from claimed infringements of patents, trademarks or copyrights of third parties. The terms of these indemnification agreements are generally perpetual any time after execution of the agreement. The maximum amount of potential future infringement indemnification is generally unlimited. The Company believes the estimated fair value of these agreements is minimal. Accordingly, the Company has no liabilities recorded for these agreements as of October 2, 2011.

14. Fair Value of Financial Instruments

The Company measures certain financial assets and liabilities at fair value on a recurring basis.

The following tables summarize the valuation of the Company s financial instruments as of October 2, 2011 (in thousands):

		As of October 2, 2011		
	Total	**Quoted market prices in active markets (Level 1)**	**Significant other observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**
Cash equivalents money-market funds	$ 24,624	$ 24,624	$	$
Available-for-sale securities U.S. Treasuries (1)				