

TERAYON COMMUNICATION SYSTEMS

Form PREM14A

May 11, 2007

**Table of Contents**

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
SCHEDULE 14A**

Proxy Statement Pursuant to Section 14(a) of the Securities  
Exchange Act of 1934 (Amendment No. )

Filed by the Registrant

Filed by a Party other than the Registrant

Check the appropriate box:

Preliminary Proxy Statement

**Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**

Definitive Proxy Statement

Definitive Additional Materials

Soliciting Material Pursuant to §240.14a-12

Terayon Communication Systems, Inc.

(Name of Registrant as Specified In Its Charter)

N/A

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

No fee required.

Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

(1) Title of each class of securities to which transaction applies:

Common stock, par value \$0.001 per share, of Terayon ( Terayon common stock )

(2) Aggregate number of securities to which transaction applies:

77,637,177 shares of Terayon common stock

1,824,835 options to purchase shares of Terayon common stock

(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

The filing fee was determined by multiplying 0.00003070 by the sum of (i) 77,637,177 shares of Terayon common stock multiplied by the merger consideration of \$1.80 per share and (ii) the product of (A) the 1,824,835 shares of Terayon common stock issuable upon exercise of all options to purchase Terayon common stock that have an exercise price of less than the merger consideration of \$1.80 per share, and (B) the excess of the merger consideration of \$1.80 per share over \$1.6972, which is the weighted average exercise price of such options.

(4) Proposed maximum aggregate value of transaction:

\$139,934,511.60

(5) Total fee paid:

\$4,295.99

- o Fee paid previously with preliminary materials.
- o Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

(1) Amount Previously Paid:

(2) Form, Schedule or Registration Statement No.:

(3) Filing Party:

(4) Date Filed:

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**Table of Contents**

**MERGER PROPOSAL YOUR VOTE IS VERY IMPORTANT**

[ ], 2007

Dear Stockholder:

You are cordially invited to attend the special meeting of stockholders of Terayon Communication Systems, Inc., to be held on [ ], 2007, at 10:00 a.m., local time, at our corporate headquarters located at 2450 Walsh Avenue, Santa Clara, California 95051.

At the special meeting, we will ask you to consider and vote upon (i) a proposal to adopt the merger agreement among our company, Motorola, Inc. and a wholly owned subsidiary of Motorola, and approve the merger of this subsidiary with us, and (ii) a proposal to approve the adjournment of the special meeting, if necessary, to solicit additional proxies if there are insufficient votes at the time of the special meeting to adopt the merger agreement and approve the merger. If the merger is completed, you will be entitled to receive \$1.80 in cash, without interest, for each share of our common stock that you own, unless you have properly exercised your appraisal rights.

Our board of directors has carefully reviewed and considered the terms and conditions of the proposed merger. Based on its review, the board of directors has determined that the merger agreement is fair, advisable to, and in the best interests of, our stockholders. **ACCORDINGLY, OUR BOARD OF DIRECTORS HAS UNANIMOUSLY APPROVED AND DECLARED ADVISABLE THE MERGER AGREEMENT AND UNANIMOUSLY RECOMMENDS THAT YOU VOTE FOR THE ADOPTION OF THE MERGER AGREEMENT AND APPROVAL OF THE MERGER AND FOR THE ADJOURNMENT OF THE SPECIAL MEETING, IF NECESSARY, TO SOLICIT ADDITIONAL PROXIES.**

Your vote is important. We cannot complete the merger unless the merger agreement is adopted and the merger is approved by the affirmative vote of the holders of a majority of our shares of common stock outstanding at the close of business on May 18, 2007, the record date for the special meeting. The proposal to adjourn the special meeting for the purpose of soliciting additional proxies, if necessary, will be approved if the votes cast in favor of the proposal by shares of common stock, present in person or represented by proxy and entitled to vote on the subject matter, exceed the votes cast against the proposal. The obligations of Terayon and Motorola to complete the merger are also subject to the satisfaction or waiver of certain conditions, including receiving clearance from regulatory agencies. Failure to submit a signed proxy or vote in person at the special meeting will have the same effect as a vote against the adoption of the merger agreement and approval of the merger and it will have no effect on the proposal to adjourn the special meeting for the purpose of soliciting additional proxies. Only stockholders who owned shares of our common stock at the close of business on May 18, 2007 will be entitled to vote at the special meeting.

**PLEASE COMPLETE, SIGN, DATE AND RETURN YOUR PROXY.** If you hold your shares in street name, you should instruct your broker how to vote in accordance with your voting instruction form.

If you sign, date and mail your proxy and do not indicate how you want to vote, your proxy will be voted **FOR** the adoption of the merger agreement and the approval of the merger and **FOR** the proposal to adjourn the special meeting to solicit additional proxies, provided that no proxy that is specifically marked **AGAINST** the proposal to adopt the merger agreement and approve the merger will be voted in favor of the adjournment proposal, unless it is specifically marked **FOR** the adjournment proposal.

This proxy statement explains the proposed merger and merger agreement and provides specific information concerning the special meeting. Please review this document carefully.

Sincerely,

Jerry D. Chase  
*Chief Executive Officer*

**Neither the Securities and Exchange Commission nor any state securities regulatory agency has approved or disapproved the merger, passed upon the merits or fairness of the merger agreement or the transactions contemplated thereby, including the proposed merger, or passed upon the adequacy or accuracy of the information contained in this document. Any representation to the contrary is a criminal offense.**

This proxy statement is dated [ ], 2007, and is first being mailed to stockholders of Terayon on or about [ ], 2007.

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**Table of Contents**

**NOTICE OF SPECIAL MEETING OF STOCKHOLDERS  
To be Held on [ ], 2007  
10:00 a.m.**

To the Stockholders of Terayon Communication Systems, Inc.:

Notice is hereby given that a special meeting of the stockholders of Terayon Communication Systems, Inc. will be held at our corporate headquarters located at 2450 Walsh Avenue, Santa Clara, California 95051 on [ ], 2007, at 10:00 a.m., local time, for the following purposes:

1. To consider and vote upon a proposal to adopt the merger agreement among Motorola, Inc., Motorola GTG Subsidiary VI Corp., a wholly owned subsidiary of Motorola, and us, and to approve the merger of Motorola GTG Subsidiary VI Corp. with and into us, in connection with which we will become a wholly owned subsidiary of Motorola, and each outstanding share of our common stock will be converted into the right to receive \$1.80 in cash, without interest;
2. To approve the adjournment of the special meeting, if necessary, to solicit additional proxies if there are insufficient votes at the time of the special meeting to adopt the merger agreement and approve the merger; and
3. To transact such other business that may properly come before the special meeting or any adjournments or postponements of the special meeting.

Holders of record of shares of our common stock at the close of business on May 18, 2007, the record date for the special meeting, are entitled to notice of, and to vote at, the special meeting and any adjournments or postponements of the special meeting.

**Our board of directors unanimously recommends that you vote FOR the adoption of the merger agreement and the approval of the merger and FOR the adjournment of the special meeting, if necessary, to solicit additional proxies.**

We cannot complete the merger unless the merger agreement is adopted and the merger is approved by the affirmative vote of the holders of a majority of the shares of our common stock outstanding at the close of business on May 18, 2007.

Under Delaware law, holders of shares of our common stock who do not vote in favor of the adoption of the merger agreement and approval of the merger will have the right to seek appraisal of the fair value of their shares as determined by the Delaware Court of Chancery if the merger is completed, but only if they submit a written demand for an appraisal prior to the vote on the merger agreement and if they comply with the Delaware law procedures explained in the accompanying proxy statement. See The Merger Appraisal Rights beginning on page 35 and Annex C of the accompanying proxy statement, which contains the text of Section 262 of the Delaware General Corporation Law.

Whether or not you plan to attend the special meeting, please vote your shares as soon as possible. You can vote your shares prior to the special meeting (1) by mail with the enclosed proxy card, in accordance with the instructions on the proxy card, (2) by telephone by calling the toll-free number that appears on the enclosed proxy card and following the instructions given, or (3) by means of the Internet, by following the Internet voting instructions provided on the enclosed proxy card. Executed proxy cards with no instructions indicated thereon will be voted FOR the adoption of the merger agreement and approval of the merger and FOR the proposal to adjourn the special meeting to solicit

additional proxies, provided that no proxy that is specifically marked **AGAINST** the proposal to adopt the merger agreement and approve the merger will be voted in favor of the adjournment proposal, unless it is specifically marked **FOR** the adjournment proposal. Even if you have returned your proxy, you may still vote in person if you attend the special meeting. Please note, however, that if your shares are held of record by a broker, bank or other nominee and you wish to vote at the meeting, you must obtain from the record holder a proxy issued in your name. If you fail to return your proxy or to vote in person at the special meeting, your shares will not be counted for purposes of determining whether a quorum is present at the special meeting, and will have the same effect as voting against the adoption of the merger agreement and approval of the merger and will have no effect on the proposal to adjourn the special meeting for the purpose of soliciting additional proxies.

**Please do not send any stock certificates at this time.**

By order of the Board of Directors,

/s/ Zaki Rakib

Zaki Rakib  
*Secretary*

Santa Clara, California  
[ ], 2007

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**Table of Contents**

**TABLE OF CONTENTS**

	<b>Page</b>
<u>QUESTIONS AND ANSWERS ABOUT THE MERGER</u>	1
<u>SUMMARY</u>	4
<u>The Companies</u>	4
<u>The Merger</u>	5
<u>Conditions to Completion of the Merger</u>	5
<u>No Solicitation of Other Acquisition Proposals by Terayon</u>	7
<u>Termination of the Merger Agreement</u>	7
<u>The Special Meeting</u>	8
<u>Recommendation of Our Board of Directors</u>	9
<u>Opinion of Our Financial Advisor</u>	9
<u>Interests of Our Directors and Executive Officers in the Merger</u>	10
<u>Treatment of Our Stock Options</u>	10
<u>Material U.S. Federal Income Tax Consequences</u>	10
<u>Appraisal Rights</u>	11
<u>Regulatory Approvals</u>	11
<u>Paying Agent</u>	12
<u>Help In Answering Questions</u>	12
<u>CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS</u>	13
<u>THE COMPANIES</u>	14
<u>Terayon</u>	14
<u>Motorola</u>	14
<u>Motorola GTG Subsidiary VI Corp</u>	15
<u>THE SPECIAL MEETING</u>	15
<u>Date, Time and Place</u>	15
<u>Purpose of the Special Meeting</u>	15
<u>Recommendation of our Board Directors</u>	15
<u>Record Date; Shares Entitled to Vote; Quorum</u>	15
<u>Vote Required</u>	16
<u>Shares Owned by Our Directors and Executive Officers</u>	16
<u>Voting of Proxies</u>	16
<u>Revocability of Proxies</u>	17
<u>Solicitation of Proxies</u>	17
<u>Other Business</u>	18
<u>Assistance</u>	18
<u>THE MERGER</u>	19
<u>Background of the Merger</u>	19
<u>Reasons for the Merger</u>	23
<u>Recommendation of Our Board of Directors</u>	24
<u>Opinion of Our Financial Advisor</u>	25
<u>Financial Projections</u>	30
<u>Interests of Our Directors and Executive Officers in the Merger</u>	32
<u>Material United States Federal Income Tax Consequences</u>	34
<u>Regulatory Approvals</u>	35





**Table of Contents**

	<b>Page</b>
<u>Appraisal Rights</u>	35
<u>Structure of the Merger</u>	38
<u>Effective Time of the Merger</u>	38
<u>Merger Consideration</u>	39
<u>Treatment of Our Stock Options</u>	39
<u>Surrender of Stock Certificates</u>	39
<u>Lost Certificates</u>	40
<u>Unclaimed Amounts</u>	40
<u>THE MERGER AGREEMENT</u>	40
<u>Representations and Warranties</u>	40
<u>Covenants</u>	42
<u>Directors and Officers Indemnification, Advancement of Expenses, Exculpation and Insurance</u>	44
<u>Options and Employee Stock Purchase Plans; Employee Benefits Matters</u>	44
<u>Efforts to Complete the Merger</u>	45
<u>Conditions to the Completion of the Merger</u>	46
<u>No Solicitation of Other Acquisition Proposals by Terayon</u>	48
<u>Termination; Payment of Termination Fee</u>	50
<u>Fees and Expenses</u>	52
<u>Amendment, Extension and Waiver</u>	52
<u>PROPOSAL TO ADJOURN THE SPECIAL MEETING</u>	52
<u>The Adjournment Proposal</u>	52
<u>Vote Required and Board Recommendation</u>	53
<u>SECURITY OWNERSHIP OF MANAGEMENT AND PRINCIPAL SHAREHOLDERS</u>	53
<u>OTHER MATTERS</u>	54
<u>FUTURE STOCKHOLDER PROPOSALS</u>	54
<u>HOUSEHOLDING OF PROXY STATEMENT</u>	55
<u>WHERE YOU CAN FIND ADDITIONAL INFORMATION</u>	55
<b>ANNEXES</b>	
<u>ANNEX A</u>	A-1
Agreement and Plan of Merger, dated as of April 21, 2007, by and among Motorola, Inc., Motorola GTG Subsidiary VI Corp., and Terayon Communication Systems, Inc.	
<u>ANNEX B</u>	B-1
Opinion of Goldman, Sachs & Co.	
<u>ANNEX C</u>	C-1
Section 262 of the Delaware General Corporation Law	

**Table of Contents**

**QUESTIONS AND ANSWERS ABOUT THE MERGER**

The following questions and answers address briefly some questions you may have regarding the special meeting and the proposed merger. These questions and answers may not address all questions that may be important to you as a stockholder of Terayon Communication Systems, Inc. Please refer to the more detailed information contained elsewhere in this proxy statement, the annexes to this proxy statement and the documents referred to or incorporated by reference in this proxy statement. In this proxy statement, the terms Terayon, Company, we, our, ours, and to Terayon Communication Systems, Inc. and references to subsidiaries of the Company includes all wholly owned subsidiaries of the Company.

**Q: Why am I receiving this proxy statement?**

A: We have agreed to be acquired by Motorola under the terms of a merger agreement that is described in this proxy statement. A copy of the merger agreement is included as Annex A to this proxy statement. In order to complete the merger, our stockholders must vote to adopt the merger agreement and approve the merger. This proxy statement contains important information about the merger and our special meeting of stockholders.

**Q: Where and when is the special meeting?**

A: The special meeting will take place at our corporate headquarters located at 2450 Walsh Avenue, Santa Clara, California 95051, on [ ], 2007, at 10:00 a.m., local time.

**Q: What matters will I be asked to vote on at the special meeting?**

A: You will be asked to vote on a proposal to adopt the merger agreement and approve the merger and a proposal for the adjournment of the special meeting, if necessary or appropriate, to solicit additional proxies in the event that there are not sufficient votes in favor of adoption of the merger agreement and approval of the merger at the time of the special meeting.

**Q: What will happen to Terayon as a result of the merger?**

A: If the merger is completed, we will become a wholly owned subsidiary of Motorola.

**Q: Who is eligible to vote at the special meeting?**

A: Holders of our common stock at the close of business on May 18, 2007 are entitled to receive notice of the special meeting and to vote the shares of our common stock that they held at that time at the special meeting, or at any adjournments or postponements of the special meeting.

**Q: What will happen to my shares of Terayon common stock after the merger?**

A: At the effective time of the merger, each outstanding share of our common stock will automatically be canceled and will be converted into the right to receive a per share amount equal to \$1.80 in cash, without interest.

**Q: What do I need to do now?**

A:

After carefully reading and considering the information contained in this proxy statement, please vote your shares as soon as possible. You can vote your shares prior to the special meeting (1) by mail with the enclosed proxy card, in accordance with the instructions on the proxy card, (2) by telephone by calling the toll-free number that appears on the enclosed proxy card and following the instructions given, or (3) by means of the Internet, by following the Internet voting instructions provided on the enclosed proxy card. If you hold your shares in street name (which means that you hold your shares through a bank, brokerage firm or other nominee), you should vote in accordance with the directions on the voting instruction card that your bank, brokerage firm or other nominee provides to you.

**Q: Is the merger expected to be taxable to me?**

A: Generally, yes. The receipt of \$1.80 in cash for each share of our common stock pursuant to the merger will be a taxable transaction for U.S. federal income tax purposes. For U.S. federal income tax purposes, you will generally recognize gain or loss as a result of the merger measured by the difference, if any, between \$1.80 per share and your adjusted tax basis in that share.

**Table of Contents**

You should read *The Merger* Material U.S. Federal Income Tax Consequences beginning on page 34 for a more complete discussion of the federal income tax consequences of the merger. Tax matters can be complicated and the tax consequences of the merger to you will depend on your particular tax situation. You should also consult your tax advisor on the tax consequences of the merger to you.

**Q: How does the Terayon board of directors recommend that I vote?**

A: Our board of directors unanimously recommends that our stockholders vote **FOR** the proposal to adopt the merger agreement and approve the merger, and **FOR** the proposal to adjourn the special meeting for the purpose of soliciting additional proxies, if necessary. You should read *The Merger* Reasons for the Merger for a discussion of the factors that our board of directors considered in deciding to recommend the adoption of the merger agreement and approval of the merger.

**Q: What vote of our stockholders is required to adopt the merger agreement and approve the merger?**

A: For us to complete the merger, stockholders holding at least a majority of the shares of our common stock outstanding at the close of business on May 18, 2007 must vote **FOR** the adoption of the merger agreement and approval of the merger.

**Q: What vote of our stockholders is required to approve the adjournment of the special meeting?**

A: The proposal to adjourn the special meeting for the purpose of soliciting additional proxies, if necessary, will be approved if the votes cast in favor of the proposal by shares of our common stock, present in person or represented by proxy and entitled to vote on the subject matter, exceed the votes cast against the proposal.

**Q: Am I entitled to appraisal rights?**

A: Yes. Under the General Corporation Law of the State of Delaware, holders of our common stock who do not vote in favor of adoption of the merger agreement and approval of the merger will have the right to seek appraisal of the fair value of their shares as determined by the Delaware Court of Chancery if the merger is completed, but only if they submit a written demand for an appraisal prior to the vote on the adoption of the merger agreement and approval of the merger, vote against, or abstain from voting for, the proposal to adopt the merger agreement and approve the merger, and otherwise comply with the Delaware law procedures explained in this proxy statement.

**Q: How do I cast my vote?**

A: If you are the holder of record of shares of our common stock, you can vote by any of the following methods:

you may indicate your vote on the enclosed proxy card and complete, sign, date and return the proxy card in the accompanying pre-addressed, postage paid envelope;

you may vote by telephone by calling the toll-free number that appears on the enclosed proxy card and following the instructions given;

you may vote electronically via the Internet by going to the website that appears on the enclosed proxy card and following the instructions given; or

you may attend the special meeting and vote in person.

If you sign, date and mail your proxy and do not indicate how you want to vote, your proxy will be voted FOR the adoption of the merger agreement and the approval of the merger, and FOR the proposal to adjourn the special meeting to solicit additional proxies, provided that no proxy that is specifically marked AGAINST the proposal to adopt the merger agreement and approve the merger will be voted in favor of the adjournment proposal, unless it is specifically marked FOR the adjournment proposal.

**Q: If my Terayon shares are held in street name by my broker or bank, will my broker or bank vote my shares for me?**

A: Your broker or bank will vote your Terayon shares only if you provide instructions on how to vote. You should follow the directions provided by your broker or bank regarding how to instruct your broker or bank to vote your shares. Without instructions, your shares will not be voted, which will have the effect of a vote against the adoption of the merger agreement and approval of the merger.

**Table of Contents**

**Q: What happens if I abstain from voting or fail to vote on the proposals or instruct my broker to vote on the proposals?**

A: If you abstain from voting, fail to cast your vote in person, by proxy, or electronically via the Internet or by telephone, or fail to give voting instructions to your broker, bank or other nominee, it will have the same effect as a vote against the proposal to adopt the merger agreement and approve the merger, and it will have no effect on the proposal to adjourn the special meeting for the purpose of soliciting additional proxies.

**Q: Can I change my vote after I have returned my proxy?**

A: Yes. If you are a shareholder of record, you may revoke your proxy and change your vote at any time before your proxy card is voted at the special meeting. You can do this in one of four ways:

by providing a written instrument or transmission to our corporate secretary prior to the special meeting stating that you revoke your proxy;

by completing and submitting to our corporate secretary a proxy in writing via mail dated later than your original proxy relating to the same shares;

by voting via the Internet or by telephone following the date of your original proxy relating to the same shares;  
or

by attending the special meeting and voting in person, which will automatically cancel any proxy previously given; your attendance at the special meeting alone, however, will not revoke any proxy that you have previously given.

If you have instructed a broker, bank or other nominee to vote your shares, you must follow the directions received from your broker, bank or other nominee to change those instructions.

**Q: Should I send in my stock certificates now?**

A: No. After the merger is completed, you will receive a transmittal form with instructions for the surrender of certificates formerly representing shares of our common stock. Please do not send in your stock certificates with your proxy.

**Q: What should I do if I receive more than one set of voting materials?**

A: You may receive more than one set of voting materials, including multiple copies of this proxy statement and multiple proxy cards or voting instruction cards. For example, if you hold your shares in more than one brokerage account, you will receive a separate voting instruction card for each brokerage account in which you hold shares. If you are a holder of record and your shares are registered in more than one name, you will receive more than one proxy card. Please complete, sign, date and return each proxy card and voting instruction card that you receive.

**Q: When do you expect the merger to be completed?**

A: We are working to complete the merger as quickly as possible. We currently expect to complete the merger in the second or third quarter of 2007. However, we cannot predict the exact timing of the merger because the merger is

subject to regulatory approvals and other closing conditions. While we expect to obtain all required regulatory approvals, we cannot assure you that these regulatory approvals will be obtained and, even if they are ultimately obtained, they might not be obtained for a substantial period of time following the special meeting.

**Q: Who can help answer my questions?**

A: If you need assistance in completing your proxy card or voting your shares or have questions regarding the special meeting, please contact MacKenzie Partners at 800-322-2885 (toll-free) or 212-929-5500 (collect) or write to the following address:

MacKenzie Partners  
105 Madison Avenue  
New York, NY 10016



**Table of Contents**

**SUMMARY**

*This summary highlights selected information from this proxy statement and may not contain all the information that is important to you. You should carefully read this entire proxy statement and the other documents to which we have referred you. See also *Where You Can Find Additional Information* on page 55. We have included page references parenthetically to direct you to a more complete description of the topics presented in this summary.*

**The Companies (Page 14)**

**Terayon Communication Systems, Inc.**

2450 Walsh Avenue  
Santa Clara, California 95051  
(408) 235-5500

Terayon currently develops, markets and sells digital video equipment to network operators and content aggregators who offer video services. Terayon's primary products include the Network CherryPicket<sup>®</sup> line of digital video processing systems and the CP 7600 line of digital-to-analog decoders. Its products are used for multiple digital video applications, including the rate shaping of video content to maximize the bandwidth for standard definition (SD) and high definition (HD) programming, grooming customized channel line-ups, carrying local ads for local and national advertisers and branding by inserting corporate logos into programming. Terayon's products are sold primarily to cable operators, television broadcasters, telecom carriers and satellite providers in the United States, Europe and Asia.

Terayon was incorporated in California in 1993 and reincorporated in Delaware in 1998.

**Motorola, Inc.**

1303 East Algonquin Road  
Schaumburg, Illinois 60196  
(847) 576-5000

Motorola builds, markets and sells products, services and applications that make simple and seamless connections to people, information and entertainment possible through broadband, embedded systems and wireless networks. Motorola's vision is to provide cutting-edge technologies that empower mobile consumers to go anywhere and do anything without sacrificing connectivity. This is seamless mobility.

***Business Segments***

Motorola reports financial results for the following three operating business segments:

***Mobile Devices Segment***

The Mobile Devices segment designs, manufactures, sells and services wireless handsets with integrated software and accessory products, and licenses intellectual property. In 2006, the segment's net sales represented 66% of Motorola's consolidated net sales.

***Networks and Enterprise Segment***

The Networks and Enterprise segment designs, manufactures, sells, installs and services: (i) cellular infrastructure systems and wireless broadband systems to public carriers and other wireless service providers (referred to as the public networks market), and (ii) analog and digital two-way radio, voice and data communications products and systems, as well as wireless broadband systems, to a wide range of public safety, government, utility, transportation and other worldwide enterprise markets (referred to as the private networks market). In January 2007, the segment completed the acquisition of Symbol Technologies, Inc. ( Symbol ), a leader in providing products and systems used in end-to-end enterprise mobility solutions. Symbol will become the cornerstone of the

**Table of Contents**

segment's enterprise mobility strategy. In 2006, the segment's net sales represented 26% of Motorola's consolidated net sales.

***Connected Home Solutions Segment***

The Connected Home Solutions segment designs, manufactures, sells and services: (i) cable television, Internet Protocol (IP) video and broadcast network set-top boxes (digital entertainment devices), (ii) end-to-end digital video system solutions, (iii) broadband access networks, and (iv) IP-based data and voice products (including modems). In 2006, the segment's net sales represented 8% of Motorola's consolidated net sales.

Motorola is a corporation organized under the laws of the State of Delaware as the successor to an Illinois corporation organized in 1928. Motorola's principal executive offices are located at 1303 East Algonquin Road, Schaumburg, Illinois 60196.

**Motorola GTG Subsidiary VI Corp.**

1303 East Algonquin Road  
Schaumburg, Illinois 60196  
(847) 576-5000

Merger Sub is a Delaware corporation and a wholly owned subsidiary of Parent. Merger Sub was organized solely for the purpose of completing a merger. It has not conducted any activities to date other than activities incidental to its formation and in connection with the transactions contemplated by the merger agreement.

**The Merger**

*Structure of the Merger (see page 38).* This proxy statement relates to the proposed acquisition of our company by Motorola pursuant to an agreement and plan of merger, dated as of April 21, 2007, among Motorola, Merger Sub and us. We have attached a copy of this agreement, which we refer to as the merger agreement, as Annex A to this proxy statement. We encourage you to read the merger agreement in its entirety.

Under the terms of the merger agreement, Merger Sub will merge with and into Terayon, with Terayon surviving the merger as a wholly owned subsidiary of Motorola

*Merger Consideration (see page 39).* At the effective time of the merger each share of our common stock (other than shares owned by us, Motorola, or Merger Sub, and other than shares for which appraisal rights have been validly exercised under Delaware law) will be converted into the right to receive \$1.80 in cash, without interest. Based on the number of shares of our common stock outstanding on April 21, 2007, the aggregate consideration paid by Motorola to our stockholders will be approximately \$140 million.

*Completion.* We expect to complete the merger as soon as practicable after the adoption of the merger agreement and approval of the merger by our stockholders and after all other conditions to the merger have been satisfied or waived.

**Conditions to Completion of the Merger (Page 46)**

The obligations of each of Motorola and Merger Sub, on the one hand, and us, on the other hand, to complete the merger depend on the satisfaction or waiver of, on or prior to the effective time of the merger, a number of conditions, including:

receipt of the required vote to adopt the merger agreement and approve the merger by our stockholders at the special meeting;

expiration or termination of the applicable waiting period under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended, and clearance under other applicable antitrust laws;

absence of legal restraints making illegal or prohibiting the completion of the merger or the other transactions contemplated by the merger agreement;

**Table of Contents**

performance in all material respects of the other party's obligations under the merger agreement; and

the representations and warranties of the other party set forth in the merger agreement being true and correct without regard to materiality and material adverse effect qualifiers, as of the date of the merger agreement and as of the completion date (except when made as of an earlier date, in which case as of that date), except to the extent that the aggregate of all inaccuracies with respect to such representations and warranties would not have a material adverse effect on such party, and, solely with respect to us, except for capitalization, corporate authority and takeover statute representations, which must be true and accurate in all material respects.

The obligation of Motorola and Merger Sub to complete the merger are subject to the following additional conditions:

the absence of any pending or threatened governmental actions, investigations or proceedings, or issuance of a related order, challenging the merger, seeking to prohibit Motorola's ability to own or operate either of our or its businesses or assets, or those of our respective subsidiaries, or to exercise ownership rights over the stock of the surviving corporation after the merger;

the absence of any pending or threatened governmental actions, investigations or proceedings that may reasonably be expected to result in (1) criminal sanctions on us or our subsidiaries, or (2) material fines to a governmental entity or restitution to a third party, in each case resulting from the conviction of us or any of our subsidiaries of a crime, or the settlement with a governmental entity for purposes of closing an investigation, being imposed on Motorola or any of its affiliates;

all governmental authorizations, consents, approvals, declarations, notices, filings and waiting period expirations shall have been made or obtained, except those, the failure of which to make or obtain could not reasonably be expected to have a material adverse effect on us or Motorola, or provide a reasonable basis to conclude the parties or any of their affiliates would be subject to the risk of criminal sanctions or any of their representatives would be subject to the risk of criminal or material civil sanctions;

the continued enforceability of specified contracts of ours;

no occurrence since the date of the merger agreement that has had, or could reasonably be expected to have, a material adverse effect (as defined in the merger agreement) on us;

our receipt of all necessary certifications under Sections 302 and 906 of the Sarbanes-Oxley Act on our reports filed with the SEC;

our having filed all required documents with the SEC, and all required amendments to such documents, and the absence of any information in any amendments that is materially and adversely different from the information in the documents amended by such amendments;

the absence of any pending or threatened action, suit, investigation or proceeding challenging the validity and ownership of the intellectual property owned by us, except those that are not expected to have a material adverse effect on us;

the SEC shall not have recommended any charges or enforcement action against us or our officers or directors, authorized such recommendation or issued a Wells Notice to us or our officers or directors, in connection with the SEC investigation relating to certain accounting matters that was commenced in December 2005 and recently discontinued, and there shall not be any pending governmental action, suit, proceeding or investigation

against any of our or our subsidiaries' directors or officers, or certain key employees, relating to the SEC investigation;

our having at least \$15 million of cash and cash equivalents (\$13 million if the merger is completed after July 31, 2007, and, in either case, reduced by the amount of all reasonable merger-related expenses (including payments required on or prior to, or as a result of, completion of the merger) paid after April 21, 2007), net of indebtedness;

**Table of Contents**

three-quarters of a small group of key employees, and 80% of a larger group of employees, still being employed by us and performing their usual and customary duties immediately prior to completion of the merger; and

our having filed specified tax returns and other tax returns, if any, that are identified as being delinquent prior to completion of the merger.

The merger is not conditioned upon Motorola or Merger Sub obtaining financing.

**No Solicitation of Other Acquisition Proposals by Terayon (see page 48)**

The merger agreement contains restrictions on our ability to solicit or engage in discussions or negotiations with a third party with respect to a proposal to acquire a significant interest in our company. Notwithstanding these restrictions, the merger agreement provides that under specified circumstances, if prior to our stockholder vote to adopt the merger agreement and approve the merger we receive an acquisition proposal from a third party that our board of directors determines in good faith, after consultation with legal counsel, is a superior proposal, or is more favorable from a financial point of view than the merger and is reasonably likely to lead to a superior proposal, we may, if our board of directors also determines in good faith (after consultation with outside legal counsel) that such action is required to discharge our board of directors' fiduciary duties to our stockholders, furnish nonpublic information to that third party and engage in negotiations regarding an acquisition proposal with that third party. Our board of directors may change or withdraw its recommendation of the merger agreement or approve or recommend any superior proposal, if a superior proposal is pending, our board of directors has determined in good faith, after receipt of advice of outside counsel, that such action is required to discharge its fiduciary duties to our stockholders, and we have given Motorola three business days to match the superior proposal. We may also terminate the merger agreement and enter into an acquisition agreement with respect to a superior proposal, as described under Termination of the Merger Agreement below.

**Termination of the Merger Agreement (see page 50)**

The merger agreement may be terminated at any time prior to the effective time of the merger, regardless of whether our stockholders have adopted the merger agreement and approve the merger:

by mutual written consent of Motorola and us;

by either Motorola or us, by written notice if:

the merger has not been completed on or before September 21, 2007, or a later date as extended by mutual written consent of Motorola and us, unless the party that seeks to terminate has breached or failed to perform in any material respect its obligations under the merger agreement in any manner that has been the principal cause of, or has primarily resulted in, the merger not being completed by that date;

our stockholders do not adopt the merger agreement and approve the merger at the special meeting, or at any adjournment or postponement thereof, unless the party that seeks to terminate has breached or failed to perform in any material respect its obligations under the merger agreement in any manner that has been the principal cause of, or has primarily resulted in, the merger not being completed by that date; or

any order permanently restraining, enjoining or otherwise prohibiting completion of the merger becomes final and nonappealable (provided that the party that seeks to terminate used commercially reasonable efforts

to have the order lifted).

by Motorola if:

our board fails to recommend approval of the merger agreement and the merger in this proxy statement, changes, or resolves to change, its recommendation to adopt the merger agreement and approve the merger, recommends to the stockholders a competing transaction or publicly announces that it intends to do so, or enters into any alternative acquisition agreement accepting any competing transaction;

a tender offer or exchange offer for our outstanding shares of capital stock is commenced, and our board fails to recommend to our stockholders against accepting the offer;



**Table of Contents**

our board, upon request of Motorola following receipt of a proposal or offer for a competing transaction, fails to reaffirm to Motorola the approval or recommendation of the merger and the merger agreement within five business days of the request;

we or any of our officers, directors, representatives or agents knowingly and materially breached our obligations under the non-solicitation provisions or specified provisions relating to the special meeting of our stockholders in the merger agreement; or

we have breached any of our representations, warranties, covenants or agreements in the merger agreement, or any of our representations or warranties becomes untrue after the date of the merger agreement, so that the related closing condition would not be satisfied, and we do not cure the breach within 20 days after we receive written notice of it from Motorola (although Motorola may not terminate the merger agreement if Motorola or Merger Sub is in material breach of the merger agreement);

by us if:

prior to the stockholder vote with respect to the adoption of the merger agreement and approval of the merger, our board of directors, in compliance with the nonsolicitation provisions of the merger agreement, has approved or recommended to our stockholders a superior proposal, Motorola has failed to match the superior proposal within three business days after we notify Motorola of the superior proposal, and we have paid Motorola the termination fee described below; or

Motorola or Merger Sub has breached any of their representations, warranties, covenants or agreements in the merger agreement, or any of their representations or warranties becomes untrue after the date of the merger agreement, so that the relating closing condition would not be satisfied, and they do not cure the breach within 20 days after they receive written notice of it from us (although we may not terminate the merger agreement if we are in material breach of the merger agreement).

*Termination Fee (see page 50).* The merger agreement provides that, in specified circumstances, we may be required to pay Motorola a termination fee of \$5.25 million.

**The Special Meeting**

*Date, Time and Place (see page 15).* The special meeting of our stockholders will be held at our corporate headquarters located at 2450 Walsh Avenue, Santa Clara, California 95051, at 10:00 a.m., local time, on [ ], 2007. At the special meeting, our stockholders will be asked to vote on the proposal to adopt the merger agreement and approve the merger and the proposal to adjourn the special meeting to solicit additional proxies, if necessary.

*Record Date, Voting Power (see page 15).* Our stockholders are entitled to vote at the special meeting if they owned shares of our common stock as of the close of business on May 18, 2007, the record date. On the record date, there were [ ] shares of our common stock entitled to vote at the special meeting. Stockholders will have one vote at the special meeting for each share of our common stock that they owned on the record date.

*Voting (see page 16).* Holders of record of shares of our common stock can vote by any of the following methods:

by completing, signing, dating and returning the enclosed proxy card in the accompanying pre-addressed, postage paid envelope;

by calling the toll-free number that appears on the enclosed proxy card and following the instructions given;

by going to the Internet website that appears on the enclosed proxy card and following the instructions given;  
or

by appearing and voting in person by ballot at the special meeting.

Brokers or banks holding shares of our common stock in street name may vote the shares only if the underlying stockholders provide instructions on how to vote. Brokers or banks will provide stockholders with directions on how to instruct the broker or bank to vote the shares. All properly completed proxies that we receive prior to the vote at the special meeting, and that are not revoked, will be voted in accordance with the instructions

**Table of Contents**

indicated on the proxies. If no direction is indicated on a properly completed proxy returned to us, the underlying shares will be voted FOR the adoption of the merger agreement and approval of the merger and FOR the proposal to adjourn the special meeting to solicit additional proxies, provided that no proxy that is specifically marked AGAINST the proposal to adopt the merger agreement and approve the merger will be voted in favor of the adjournment proposal, unless it is specifically marked FOR the adjournment proposal.

As of the date of this proxy statement, we know of no matters that will be presented for consideration at the special meeting other than as described in this proxy statement. If, however, other matters are brought before the special meeting, the persons named as proxies will vote in accordance with their judgment on such other matters unless otherwise indicated on the proxy.

*Revocability of Proxies (see page 17).* You may change your vote at any time before your proxy is voted at the special meeting. You can do this in one of four ways:

by providing a written instrument or transmission to our corporate secretary prior to the special meeting stating that you revoke your proxy;

by completing and submitting to our corporate secretary a proxy in writing via mail dated later than your original proxy relating to the same shares;

by voting via the Internet or by telephone following the date of your original proxy relating to the same shares;  
or

by attending the special meeting and voting in person, which will automatically cancel any proxy previously given; your attendance at the special meeting alone, however, will not revoke any proxy that you have previously given.

If you instructed your broker to vote your shares, you must follow directions from your broker to change these instructions.

*Vote Required (see page 16).* Approval of the proposal to adopt the merger agreement and approve the merger requires the affirmative vote of stockholders holding a majority of the shares of our common stock outstanding at the close of business on May 18, 2007. Approval of the proposal to adjourn the special meeting for the purpose of soliciting additional proxies, if necessary, requires the affirmative vote of the holders of a majority of the outstanding shares voted on such proposal.

*Shares Owned by Our Directors and Executive Officers (see page 16).* On May 18, 2007, the record date, our directors and executive officers beneficially owned and were entitled to vote approximately [ ] percent of the shares of our common stock outstanding on that date.

**Recommendation of Our Board of Directors (see page 15)**

Our board of directors has unanimously determined that the merger agreement is advisable, fair to and in the best interests of, our stockholders. The board of directors unanimously recommends that our stockholders vote FOR the adoption of the merger agreement and approval of the merger, and FOR the proposal to adjourn the special meeting to solicit additional proxies, if necessary.

**Opinion of Our Financial Advisor (see page 25)**

Goldman, Sachs & Co. rendered its opinion to our board of directors that, as of April 21, 2007, and based upon and subject to the factors and assumptions set forth therein, the \$1.80 per share of common stock in cash to be received by the holders of shares of our common stock pursuant to the merger agreement was fair from a financial point of view to such holders.

The full text of the written opinion of Goldman Sachs, dated April 21, 2007, which sets forth the assumptions made, procedures followed, matters considered and limitations on the review undertaken in connection with the opinion, is attached as Annex B to this proxy statement. We urge you to read the opinion carefully and in its entirety. Goldman Sachs provided its opinion for the information and assistance of our board of directors in connection with its consideration of the transaction. The Goldman Sachs opinion is not a recommendation as to how any holder of

**Table of Contents**

shares of our common stock should vote with respect to the transaction. Pursuant to an amended letter agreement between Goldman Sachs and us, we have agreed to pay Goldman Sachs a transaction fee of approximately \$4.0 million in connection with the transaction. \$1.0 million of the transaction fee, net of retainer fees paid by us to Goldman Sachs through the end of December 2006, became due upon the signing of the merger agreement based on our request that Goldman Sachs undertake a study in order to enable it to render its opinion as to the fairness from a financial point of view of the \$1.80 per share of common stock in cash to be received by the holders of shares of our common stock pursuant to the merger agreement. The remaining \$3.0 million of the transaction fee is due upon the consummation of the transaction. In addition, retainer fees in the amount of \$50,000 per month from January 2007 onwards have been deferred under the amended letter agreement, and will become due upon the earlier of the consummation of the transaction or the termination of Goldman Sachs' engagement under the amended letter agreement. Our board of directors was aware that Goldman Sachs is providing and has provided certain investment banking services to Motorola.

**Interests of Our Directors and Executive Officers in the Merger (see page 32)**

In considering the recommendation of our board of directors to vote for the proposal to adopt the merger agreement and approve the merger, you should be aware that all of our directors and executive officers have personal interests in the merger that are, or may be, different from, or in addition to, our stockholders' interests. Our executive officers (including Jerry Chase, who is also a member of our board of directors) are entitled to benefits under their employment agreements pursuant to which they will receive severance benefits if their employment is terminated following the completion of the merger under specified circumstances. Additionally, all options held by our directors and executive officers to purchase shares of our common stock granted under our 1995 Stock Option Plan, 1997 Equity Incentive Plan, 1998 Non-Employee Director's Stock Option Plan, and 1999 Non-Officer Equity Incentive Plan, including any unvested portion of such options, will be cashed out in the merger, as described under "Treatment of Our Stock Options," below. In addition, the terms of the merger agreement provide for the continued indemnification of our directors and officers following the effective time of the merger.

Our board of directors was aware of these interests and considered them, among other matters, when approving the merger.

**Treatment of Our Stock Options (see page 39)**

All options to purchase shares of our common stock granted under our 1995 Stock Option Plan, 1997 Equity Incentive Plan, 1998 Non-Employee Director's Stock Option Plan, and 1999 Non-Officer Equity Incentive Plan, as well as all options granted outside of any plan, including any unvested portion of such options, will be cashed out in the merger. For these purposes, "cashed out in the merger" means that the option, whether vested or unvested, will be cancelled in the merger in exchange for a cash payment equal to the product of (i) the excess, if any, of \$1.80 over the applicable per share option exercise price and (ii) the number of shares of our common stock subject to the option at such time, without interest and less any applicable withholding taxes. The aggregate "cash-out" value of all of our options that are in-the-money is approximately \$188,000.

**Material U.S. Federal Income Tax Consequences (see page 34)**

The receipt of \$1.80 in cash in exchange for each share of our common stock pursuant to the merger will be a taxable transaction for U.S. federal income tax purposes. For U.S. federal income tax purposes, you will generally recognize gain or loss as a result of the merger measured by the difference, if any, between \$1.80 per share of common stock and your adjusted tax basis in that share.

You should read **The Merger – Material U.S. Federal Income Tax Consequences** beginning on page 34 for a more complete discussion of the federal income tax consequences of the merger. Tax matters can be complicated, and the tax consequences of the merger to you will depend on your particular tax situation. We urge you to consult your tax advisor on the tax consequences of the merger to you.

**Table of Contents**

**Appraisal Rights (see page 35)**

Holders of record of shares of our common stock who do not wish to accept the cash consideration payable pursuant to the merger may seek, under Section 262 of the General Corporation Law of the State of Delaware, judicial appraisal of the fair value of their shares by the Delaware Court of Chancery. This value could be more or less than or the same as the merger consideration for the common stock. This right to appraisal is subject to a number of restrictions and technical requirements. Generally, in order to properly demand appraisal, among other things:

you must not vote in favor of the proposal to adopt the merger agreement and approve the merger;

you must make a written demand on us for appraisal in compliance with the General Corporation Law of the State of Delaware before the vote on the proposal to adopt the merger agreement and approve the merger at the special meeting; and

you must hold your shares of record continuously from the time of making a written demand for appraisal through the effective time of the merger.

Merely voting against the merger agreement and the merger will not preserve your right to appraisal under Delaware law. Also, because a submitted proxy not marked  against or  abstain will be voted for the proposal to adopt the merger agreement and approve the merger, the submission of a proxy not marked  against or  abstain will result in the waiver of appraisal rights. If you hold shares in the name of a broker or other nominee, you must instruct your nominee to take the steps necessary to enable you to demand appraisal for your shares. If you or your nominee fails to follow all of the steps required by Section 262 of the General Corporation Law of the State of Delaware, you will lose your right of appraisal.

Annex C to this proxy statement contains the full text Section 262 of the General Corporation Law of the State of Delaware, which relates to your right of appraisal. We encourage you to read these provisions carefully and in their entirety.

**Regulatory Approvals (see page 35)**

The merger is subject to discretionary review by the Antitrust Division of the U.S. Department of Justice and the Federal Trade Commission to determine whether it is in compliance with applicable antitrust laws. The Hart-Scott-Rodino Antitrust Improvements Act of 1976 and the rules promulgated thereunder prohibits us from completing the merger until we have furnished certain information and materials to the Antitrust Division of the Department of Justice and the Federal Trade Commission, and the required waiting period has ended. Both Motorola and we filed the required notification and report forms on [ ], 2007. The waiting period will expire at 11:59 p.m. on [ ], 2007, unless extended by a request for more information or shortened by an early termination notice. In addition, filings are required to be made with, and regulatory approvals are required to be obtained from, antitrust or competition authorities in other nations, including Germany, Israel and the Ukraine. All of these filings have been made or will be made shortly. Until approvals have been received from antitrust or competition authorities, or required waiting periods have ended in each of those jurisdictions, we are prohibited from completing the merger. Neither we nor Motorola have yet obtained any of the governmental or regulatory approvals required to complete the merger. The completion of the merger also is subject to compliance with the General Corporation Law of the State of Delaware.

While we expect to obtain all required regulatory approvals, we cannot assure you that these regulatory approvals will be obtained or that the granting of these regulatory approvals will not involve the imposition of conditions on the completion of the merger or require changes to the terms of the merger that would have a materially adverse effect on the combined company. These conditions or changes could require the grant of a complete or partial license, a divestiture or spin-off, or the holding separate of assets or businesses and could result in the conditions to Motorola's obligation to complete the merger not being satisfied.



**Table of Contents**

**Paying Agent**

[ ] or another comparable institution will act as the paying agent in connection with the merger.

**A COPY OF THE MERGER AGREEMENT IS INCLUDED IN THIS PROXY STATEMENT AS ANNEX A. YOU ARE STRONGLY ENCOURAGED TO READ IT CAREFULLY AND IN ITS ENTIRETY.**

**Help in Answering Questions**

If you have questions about the special meeting or the merger after reading this document, please contact MacKenzie Partners, which is assisting us in the solicitation of proxies, at 800-322-2885 (toll-free) or 212-929-5500 (collect), or write to the following address:

MacKenzie Partners  
105 Madison Avenue  
New York, NY 10016

**Table of Contents**

**CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS**

This proxy statement contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. Statements other than statements of historical fact, including the expected timetable for completing the proposed merger between us and Motorola, and any other statements regarding our future expectations, beliefs, goals or prospects, are forward-looking statements for the purposes of federal and state securities laws. Forward-looking statements are commonly identified by words such as may, will, should, would, expects, anticipates, believes, estimates, predicts, future, intends, contemplates, anticipates and other terms with meanings. These forward-looking statements, including without limitation statements relating to our projected financial and operating results under the heading Financial Projections, reflect our management's current expectations, estimates, forecasts and projections, and are subject to a number of risks and uncertainties that may cause actual results or events to differ materially from those expressed in, or implied by, such statements. Our future financial condition and results of operations, as well as any forward-looking statements, are subject to change and to inherent risks and uncertainties. Risks and uncertainties pertaining to the following factors, among others, could cause actual results or events to differ materially from those indicated by such forward-looking statements:

we may be unable to complete the merger due to failure to obtain stockholder approval or required regulatory clearances, to satisfy other conditions to completion of the merger, or for other reasons;

the retention of certain of our key employees;

the impact or outcome of any legal proceeding that may be instituted against us and others relating to the merger, and other uncertainties relating to the proposed merger;

unexpected costs or liabilities resulting from the proposed transaction;

diversion of management's attention from the operations of the business as a result of preparations for the proposed merger;

the risk that announcement of the proposed merger may negatively affect our relationship with our customers, suppliers, and employees;

the risk that we are unable to achieve the financial projections set forth under Financial Projections below, for the reasons set forth in that section;

risks associated with any failure to obtain intellectual property licenses that may be required and to pay associated royalties, including our recent failure to do so with respect to Dolby Laboratories, as identified in our Quarterly Report on Form 10-Q for the quarter ended March 31, 2007; and

other factors described in our Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and our most recent Quarterly Report on Form 10-Q filed with the SEC.

You should consider the cautionary statements contained or referred to in this section in connection with any subsequent written or oral forward-looking statements that may be issued by us or persons acting on our behalf. We do not undertake any obligation to release publicly any revisions to any forward-looking statements contained herein to reflect events or circumstances that occur after the date of this proxy statement or to reflect the occurrence of unanticipated events, except as we are required to do by law.



**Table of Contents**

**THE COMPANIES**

**Terayon Communication Systems, Inc.**

2450 Walsh Avenue  
Santa Clara, California 95051  
(408) 235-5500

Terayon currently develops, markets and sells digital video equipment to network operators and content aggregators who offer video services. Terayon's primary products include the Network CherryPicker® line of digital video processing systems and the CP 7600 line of digital-to-analog decoders. Its products are used for multiple digital video applications, including the rate shaping of video content to maximize the bandwidth for standard definition (SD) and high definition (HD) programming, grooming customized channel line-ups, carrying local ads for local and national advertisers and branding by inserting corporate logos into programming. Terayon's products are sold primarily to cable operators, television broadcasters, telecom carriers and satellite providers in the United States, Europe and Asia.

Terayon was incorporated in California in 1993 and reincorporated in Delaware in 1998.

**Motorola, Inc.**

1303 East Algonquin Road  
Schaumburg, Illinois 60196  
(847) 576-5000

Motorola builds, markets and sells products, services and applications that make simple and seamless connections to people, information and entertainment possible through broadband, embedded systems and wireless networks. Motorola's vision is to provide cutting-edge technologies that empower mobile consumers to go anywhere and do anything without sacrificing connectivity. This is seamless mobility.

***Business Segments***

Motorola reports financial results for the following three operating business segments:

***Mobile Devices Segment***

The Mobile Devices segment designs, manufactures, sells and services wireless handsets with integrated software and accessory products, and licenses intellectual property. In 2006, the segment's net sales represented 66% of Motorola's consolidated net sales.

***Networks and Enterprise Segment***

The Networks and Enterprise segment designs, manufactures, sells, installs and services: (i) cellular infrastructure systems and wireless broadband systems to public carriers and other wireless service providers (referred to as the public networks market), and (ii) analog and digital two-way radio, voice and data communications products and systems, as well as wireless broadband systems, to a wide range of public safety, government, utility, transportation and other worldwide enterprise markets (referred to as the private networks market). In January 2007, the segment completed the acquisition of Symbol Technologies, Inc. (Symbol), a leader in providing products and systems used in end-to-end enterprise mobility solutions. Symbol will become the cornerstone of the segment's enterprise mobility strategy. In 2006, the segment's net sales represented 26% of Motorola's consolidated net sales.

***Connected Home Solutions Segment***

The Connected Home Solutions segment designs, manufactures, sells and services: (i) cable television, Internet Protocol ( IP ) video and broadcast network set-top boxes ( digital entertainment devices ), (ii) end-to-end digital video system solutions, (iii) broadband access networks, and (iv) IP-based data and voice products (including modems). In 2006, the segment's net sales represented 8% of Motorola's consolidated net sales.

**Table of Contents**

Motorola is a corporation organized under the laws of the State of Delaware as the successor to an Illinois corporation organized in 1928. Motorola's principal executive offices are located at 1303 East Algonquin Road, Schaumburg, Illinois 60196.

**Motorola GTG Subsidiary VI Corp.**

1303 East Algonquin Road  
Schaumburg, Illinois 60196  
(847) 576-5000

Merger Sub is a Delaware corporation and a wholly owned subsidiary of Parent. Merger Sub was organized solely for the purpose of completing a merger. It has not conducted any activities to date other than activities incidental to its formation and in connection with the transactions contemplated by the merger agreement.

**THE SPECIAL MEETING**

We are furnishing this proxy statement to our stockholders, as of May 18, 2007, the record date, as part of the solicitation of proxies by our board of directors for use at the special meeting.

**Date, Time and Place**

The special meeting of our stockholders will be held at our corporate headquarters located at 2450 Walsh Avenue, Santa Clara, California 95051, at 10:00 a.m., local time, on [ ], 2007.

**Purpose of the Special Meeting**

At the special meeting, we are asking holders of record of our common stock on May 18, 2007, to consider and vote on the following proposals:

1. The adoption of the Agreement and Plan of Merger, dated as of April 21, 2007, by and among Terayon Communication Systems, Inc., Motorola, Inc. and Motorola GTG Subsidiary VI Corp., and the approval of the merger of Motorola GTG Subsidiary VI Corp. with and into Terayon Communication Systems, Inc., in connection with which Terayon Communication Systems, Inc. will become a wholly owned subsidiary of Motorola, Inc. and each outstanding share of the common stock of Terayon Communication Systems, Inc. will be converted into the right to receive a per share amount equal to \$1.80 in cash, without interest;
2. The approval of the adjournment of the special meeting, if necessary, to solicit additional proxies if there are insufficient votes at the time of the special meeting to adopt the merger agreement and approve the merger; and
3. The transaction of any other business as may properly come before the special meeting or any adjournment or postponement of the special meeting.

**Recommendation of our Board of Directors**

Our board of directors has unanimously approved the merger agreement and determined that it is advisable, fair to and in the best interests of, our stockholders, and unanimously recommends that our stockholders vote **FOR** the adoption of the merger agreement and approval of the merger and **FOR** any proposal to adjourn the special meeting to solicit additional proxies, if necessary.

**Record Date; Shares Entitled to Vote; Quorum**

Only holders of record of shares of our common stock at the close of business on May 18, 2007, the record date, are entitled to notice of and to vote at the special meeting. On the record date, [ ] shares of our common stock were issued and outstanding and held by approximately [ ] holders of record. A quorum is present at the special meeting if a majority of all the shares of our common stock issued and outstanding on the record date are represented at the special meeting in person or by a duly authorized and properly completed proxy. Abstentions and broker non-

## **Table of Contents**

votes, discussed below, count as present for establishing a quorum. Holders of record of shares of our common stock on the record date are entitled to one vote per share on each matter submitted to a vote at the special meeting.

### **Vote Required**

The adoption of the merger agreement and approval of the merger requires the affirmative vote of stockholders holding a majority of the shares of our common stock outstanding on the record date. Because the required vote of our stockholders is based upon the number of outstanding shares of our common stock, rather than upon the shares actually voted, the failure by the holder of any such shares to submit a proxy or to vote via telephone or the Internet or in person at the special meeting, including abstentions and broker non-votes (described under **Voting of Proxies** below), will have the same effect as a vote against the adoption of the merger agreement and approval of the merger.

The proposal to adjourn the special meeting for the purpose of soliciting additional proxies, if necessary, will be approved if the votes cast in favor of the proposal by shares of our common stock, present in person or represented by proxy and entitled to vote on the subject matter, exceed the votes cast against the proposal. The failure to submit a proxy or to vote, including abstentions and broker non-votes, will have no effect on the proposal to adjourn the special meeting.

### **Shares Owned by Our Directors and Executive Officers**

At the close of business on May 18, 2007, the record date, our directors and executive officers beneficially owned and were entitled to vote [ ] percent of the shares of our common stock outstanding on that date.

### **Voting of Proxies**

We are offering you four methods of voting:

by completing, signing, dating and returning the enclosed proxy card in the accompanying pre-addressed, postage paid envelope;

by calling the toll-free number that appears on the enclosed proxy card and following the instructions given;

by going to the Internet website that appears on the enclosed proxy card and following the instructions given;  
or

by appearing and voting in person by ballot at the special meeting.

Brokers or banks who hold shares of our common stock in street name for customers who are the beneficial owners of such shares may not submit a proxy to vote those customers' shares in the absence of specific instructions from those customers. The brokers and banks will provide their customers with directions on how to instruct the broker or bank to vote their shares. In addition, a large number of brokers and banks participate in the ADP Investor Communication Services online program. This program provides eligible stockholders who receive a paper copy of this proxy statement the opportunity to vote via the Internet or by telephone. If your broker or bank participates in ADP's program, your broker or bank will provide instructions.

If no instructions are given to the broker or bank holding shares, or if instructions are given to the broker or bank indicating that the broker or bank does not have authority to vote on the proposal to adopt the merger agreement and approve the merger, then, in either case, a broker non-vote will generally occur and the shares will be counted as present for purposes of determining whether a quorum exists, but will not be voted on the proposal to adopt the



merger agreement and approve the merger and will therefore have the same effect as voting against the adoption of the merger agreement and approval of the merger. Similarly, broker non-votes will not be voted on the proposal to adjourn the special meeting to solicit additional proxies, but will have no effect on that proposal. Brokers and other nominees will not have discretionary authority to vote on the proposal to adopt the merger agreement and approve the merger or the proposal to adjourn the special meeting to solicit additional proxies, if necessary.

All shares represented by properly completed proxies received prior to the special meeting will be voted at the special meeting in the manner specified in the proxies. Properly completed proxies that do not contain voting instructions will be voted FOR the adoption of the merger agreement and approval of the merger and FOR the

## **Table of Contents**

proposal to adjourn the special meeting to solicit additional proxies, if necessary, provided that no proxy that is specifically marked **AGAINST** the proposal to adopt the merger agreement and approve the merger will be voted in favor of the adjournment proposal, unless it is specifically marked **FOR** the adjournment proposal.

Shares of our common stock represented at the special meeting but not voting, including shares of our common stock for which proxies have been received but with respect to which holders have abstained, will be treated as present at the special meeting for purposes of determining whether a quorum exists, but will not be voted on the proposal to adopt the merger agreement and approve the merger, and will effectively count as votes against the adoption of the merger agreement and the approval of the merger. Similarly, shares of our common stock for which proxies have been received but with respect to which holders have abstained will not be voted on the proposal to adjourn the special meeting to solicit additional proxies, but will have no effect on that proposal.

Although it is not currently expected, if the proposal to adjourn the special meeting to solicit additional proxies is approved, the special meeting may be adjourned for the purpose of soliciting additional proxies to approve the proposal to adopt the merger agreement and approve the merger. Other than for the purposes of adjournment to solicit additional proxies, if a quorum exists, then the chairman or a vote by a majority of the shares casting votes, excluding abstentions, at the special meeting may adjourn the meeting. Alternatively, if no quorum exists, then the chairman or a majority of the shares represented at the special meeting may adjourn the meeting.

Any adjournment may be made without notice, other than by an announcement made at the special meeting, unless the adjournment is for more than thirty days or a new record date is fixed for the adjourned meeting. Any adjournment of the special meeting for the purpose of soliciting additional proxies will allow our shareholders who have already sent in their proxies to revoke them at any time prior to their use at the special meeting as adjourned.

## **Revocability of Proxies**

You can change your vote or revoke your proxy at any time before the proxy is voted at the special meeting. You may accomplish this in one of four ways:

by providing a written instrument or transmission to our corporate secretary at our corporate headquarters prior to the special meeting stating that you revoke your proxy;

by completing and submitting to our corporate secretary a proxy in writing via mail dated later than your original proxy relating to the same shares;

by voting via the Internet or by telephone following the date of your original proxy relating to the same shares;  
or

by attending the special meeting and voting in person, which will automatically cancel any proxy previously given; your attendance at the special meeting alone, however, will not revoke any proxy that you have previously given.

If you instructed your broker to vote your shares, you must follow directions from your broker to change these instructions.

## **Solicitation of Proxies**

We will pay the costs of the solicitation of proxies from our stockholders. In addition to solicitation by mail, our directors, officers and employees may solicit proxies from stockholders by telephone or other electronic means or in

person. These persons will not receive additional or special compensation for such solicitation services. We will cause brokerage houses and other custodians, nominees and fiduciaries to forward solicitation materials to the beneficial owners of stock held of record by such persons. We will, upon request, reimburse such custodians, nominees and fiduciaries for their reasonable out-of-pocket expenses in doing so. MacKenzie Partners, Inc. will assist in our solicitation of proxies. We will pay MacKenzie Partners a fee of \$20,000 plus reimbursement of certain out-of-pocket expenses, and will indemnify MacKenzie Partners against any losses arising out of its proxy solicitation services on our behalf.

**Table of Contents**

**Other Business**

We do not expect that any matter other than the proposal to adopt the merger agreement and approve the merger and, if necessary, the proposal to adjourn the meeting will be brought before the special meeting. If, however, other matters are properly presented at the special meeting, the persons named as proxies will vote in accordance with their best judgment with respect to those matters unless otherwise indicated on the proxy.

**Assistance**

If you need assistance in completing your proxy card or voting your shares, or have questions regarding the special meeting, please contact MacKenzie Partners at 800-322-2885 (toll-free) or 212-929-5500 (collect) or write to the following address:

MacKenzie Partners  
105 Madison Avenue  
New York, NY 10016

*YOU SHOULD NOT SEND STOCK CERTIFICATES WITH YOUR PROXIES.* If the merger is approved by our stockholders and ultimately consummated, a transmittal form with instructions for the surrender of certificates formerly representing shares of our common stock will be mailed to you shortly after the effective time of the merger.

**Table of Contents**

**THE MERGER**

*While we believe that the following description covers the material terms of the merger and the related transactions, this summary may not contain all of the information that is important to you. You should carefully read this entire document, including the annexes, and the other documents we refer to for a more complete understanding of the merger and the related transactions.*

**Background of the Merger**

In early 2005, we were nearing completion of our transition to a video company and believed there was a large market opportunity for our video products if we successfully executed on our business plan over the following few years. However, other companies were also starting to develop technology similar to ours with remultiplexing, splicing and ad insertion capabilities. We were faced with the decision between trying to execute on our business plan as a stand-alone company in an industry that would become increasingly competitive, or seeking to maximize value for our stockholders through a strategic transaction, including a potential sale of the company. As a result, towards the middle of 2005, our board of directors began exploring the possibility of a strategic transaction, and engaged Goldman Sachs as financial advisor with respect to the process. Between May 2005 and September 2005, Goldman Sachs contacted 15 parties, including both strategic and financial parties, with respect to a potential strategic transaction, and we entered into confidentiality agreements with seven of them. While Motorola was one of the parties contacted, Motorola declined to pursue a strategic transaction with us at that time based on strategic and valuation considerations. By October 2005, we were in substantive discussions with two of the interested parties, and the other five parties with whom we entered into confidentiality agreements had declined to pursue a strategic transaction further. During the negotiation process, we became aware of potential revenue recognition issues relating to our financial statements, and on November 7, 2005, we issued a press release announcing that our Audit Committee would conduct an investigation into these matters. At a regular meeting of our board of directors held on November 30, 2005, our board decided to place the strategic transaction process on hold until the Audit Committee completed its investigation.

During the first quarter of 2006, our Audit Committee concluded its investigation and determined that we would need to restate certain of our historical financial statements. At meetings of our board of directors in March and May 2006, after considering the advice of Goldman Sachs and our legal advisors, Latham & Watkins LLP, our board of directors instructed management not to reinstate discussions with the two interested parties, or any other potential parties, with respect to a strategic transaction until we were near to completing our restatement.

At a special meeting of our board of directors on October 9, 2006, our board reviewed with representatives of Goldman Sachs our strategic options upon the completion of the restatement process, including remaining as a stand-alone company, and reviewed potential interested parties, including Motorola, and a revised strategy and timing for the strategic transaction process. At the special meeting, representatives of Goldman Sachs advised our board of directors that it is providing and has provided certain investment banking services to some of the potential interested parties, including Motorola. Following discussion, the board directed management to reengage in the strategic transaction process.

During October and November 2006, management and Goldman Sachs contacted the two parties with which we had been engaged in substantive discussions in October 2005, four other parties which we had contacted in 2005, including Motorola, and one additional party. Two of the parties subsequently stated they were not interested in pursuing a strategic transaction. After we had entered into any necessary confidentiality agreements, members of our management gave presentations to the remaining five parties, including Motorola in Santa Clara, California on

October 26, 2006, and including the two parties with which we were in substantive discussions in October 2005. The parties that had agreed to standstill provisions in their confidentiality agreements were also provided access to our online data room at that time.

On November 10, 2006, Goldman Sachs sent bid procedures letters on our behalf to the five remaining prospective bidders indicating that initial non-binding proposals would be due on December 1, 2006. The deadline was based on the assumption that we would have filed restated financial statements prior to that time.

**Table of Contents**

On November 29, 2006, Darren Marino, Vice President of Business Development of the Connected Home Solutions Business of Motorola, contacted representatives of Goldman Sachs to request an extension of the bid deadline and to convey a list of financial and technical due diligence questions for us. Mr. Marino was informed that an extension was possible, but that due diligence materials would not be made available unless Motorola agreed to an amendment to its confidentiality agreement with us that contained standstill and non-solicitation of employee provisions. Following negotiations, we entered into the amendment with Motorola on December 4<sup>th</sup>, and then made the requested information available to it. Given that we had not filed restated financial statements, the other potential bidders were also informed that they should not view December 1<sup>st</sup> as a hard deadline for submitting non-binding proposals. None of the parties submitted a proposal prior to the deadline.

At a December 4<sup>th</sup> board meeting, representatives from Goldman Sachs updated our board on the status of discussions with interested parties, and the fact that none of the interested parties had submitted a proposal as of that date.

During early December, Mr. Marino informed representatives of Goldman Sachs that Motorola expected to deliver a non-binding proposal around the middle of December. At the request of our management, following discussions with individual members of our board of directors, Goldman Sachs contacted three of the other four interested parties and informed them that we might be receiving a preemptive offer from one of the interested parties and requesting that they forward a non-binding proposal as soon as possible in order to be considered in the process. The fourth party was not contacted because it had communicated to Goldman Sachs by that time that it was not interested in pursuing a transaction.

On December 21, 2006, Motorola submitted, in writing, a non-binding all cash proposal to acquire us at a price per share of between \$1.60 and \$1.75, subject to due diligence, negotiation of key employee arrangements and the negotiation of a definitive merger agreement. Motorola also requested a 30-day exclusivity period. At a special meeting of our board of directors the next day, Goldman Sachs updated our board on the status of discussions with interested parties, including Motorola's proposal and the fact that none of the other bidders had submitted a proposal, as well as other strategic alternatives available to the company. With regard to the absence of other bidders, Goldman Sachs informed our board that some of the bidders had expressed concern about bidding because their valuation of the company was significantly below one that was likely to be acceptable to our board, given the current trading price of our shares, which was \$1.63 as of the close of market on December 21<sup>st</sup>. The board directed Goldman Sachs to inform Motorola that it was prepared to continue discussions with Motorola, but that if Motorola wanted exclusivity, it would have to increase its proposed transaction price above \$1.75 per share. Motorola subsequently rescinded its request for exclusivity and confirmed orally a non-binding all cash proposal to acquire us at a price per share no greater than \$1.75, subject to the conditions described above.

On December 29<sup>th</sup>, we filed our Form 10-K for the year ended December 31, 2005, which included the restatement of our financial statements for various prior periods. We filed our Forms 10-Q for each of the first three quarters of 2006 on January 10, 2007.

On December 29, 2006, representatives of Winston & Strawn LLP, Motorola's legal counsel, forwarded us an initial draft merger agreement. Management and the legal and financial advisors of the two companies were in communication regarding the terms of a definitive merger agreement from this time through the signing of the merger agreement, and conducted extensive negotiations regarding the terms through a series of telephonic conference calls and email exchanges during that period. Motorola also continued its due diligence investigation throughout this time.

During January 2007, representatives of Latham & Watkins had several calls with representatives of Winston & Strawn to discuss issues regarding the draft merger agreement. Winston & Strawn circulated a revised draft of the merger agreement on January 19, 2007. During the course of January, several due diligence meetings and conference

calls took place between members of our management and advisors and members of Motorola's deal team to discuss due diligence and transaction planning matters.

At a regularly scheduled meeting of our board of directors held on January 31, 2007, members of management and Goldman Sachs updated the board on the status of discussions with Motorola and the lack of developments with any other party. Representatives of Goldman Sachs discussed with the board financial aspects of Motorola's



**Table of Contents**

proposal. Members of management also updated the board on fourth quarter financial information. The board directed management to continue negotiations with Motorola.

Throughout February, we and our advisors held a number of conference calls with Motorola and its advisors regarding due diligence matters. Further drafts of the merger agreement were exchanged towards the middle of the month and at the beginning of March.

At a special meeting of our board of directors on March 2, 2007, representatives of Goldman Sachs and members of our management updated the board on the status of negotiations with Motorola, including Motorola's due diligence review, and the expected timing of completing a strategic transaction. Representatives of Goldman Sachs discussed with the board financial aspects of the proposed transaction, the status of discussions with other parties and whether, given the passage of time since reengagement in the strategic transaction process and the possibility of changed circumstances, there might be any parties who had previously informed us they were not interested in acquiring us or whom we previously considered unlikely to have an interest, but who now might be interested in acquiring us. One of the companies with which we had been in substantive discussions in 2005 had experienced a setback with regard to a major strategic initiative, and as a result Goldman Sachs stated that in its view it was worth going back to that company to see whether it had a renewed interest in acquiring us. In addition, a company that we had not previously contacted had recently publicly expressed interest in our sector, and Goldman Sachs stated that in its view it was worth approaching that company. After discussing these views, the belief of members of the board and representatives of Goldman Sachs that a broad search for potential acquirers had already been undertaken, and the potential impact that expanding that search would have on discussions with Motorola, our board of directors directed management and Goldman Sachs to approach these two companies and one additional company with which we had been in substantive discussions in 2005.

During March, Motorola sought a number of internal approvals to move forward with the transaction. Motorola had substantially completed its due diligence by that time, although it remained focused on a few areas of potential risk to Motorola, including with respect to outstanding litigation matters that we face. We and our legal and other advisors had a few calls with Motorola and its legal and other advisors regarding these matters. In addition, Motorola was waiting to receive our financial statements as of December 31, 2006. For the foregoing reasons, negotiation of the merger agreement slowed down.

At informal meetings during early March, our board of directors received an update from management and representatives of Latham & Watkins as to the status of discussions with Motorola, including material outstanding issues, as well as our alternatives as a stand-alone company. Members of the board directed management to continue negotiations with Motorola.

During the middle of March, Jerry Chase, our Chief Executive Officer, and representatives of Goldman Sachs contacted two of the additional companies, as directed by the board, and requested that they submit an expression of interest by the middle of the following week if they were interested in pursuing a potential transaction. Representatives of Goldman Sachs contacted the third additional company, as directed by the board, requesting that it submit an expression of interest in the same timeframe. None of the companies forwarded an expression of interest.

Towards the end of the month, representatives of Latham & Watkins discussed the material outstanding issues on the merger agreement with representatives of Winston & Strawn. Among the issues that remained outstanding after the call were the merger consideration, the amount of the break-up fee, the existence of a condition relating to the maximum percentage of shares for which appraisal rights could be exercised, a condition relating to the status of a pending investigation by the SEC, various covenants and conditions relating to employees and various representations, covenants and conditions relating to intellectual property and tax matters.

At a special meeting of our board of directors held on April 5<sup>th</sup>, management and representatives of Goldman Sachs updated the board on the status of discussions with Motorola and other parties. Representatives of Goldman Sachs stated that Motorola indicated that it had received some, but not yet all, of its required internal approvals. Management and Goldman Sachs advised the board that none of the three companies contacted in March had expressed an interest in acquiring us. A representative of Latham & Watkins provided a detailed summary of the material terms of the merger agreement and material open issues, including Motorola's request for a break-up fee of 3.5% of equity value plus unlimited expense reimbursement. Following consideration by the board of information

**Table of Contents**

relating to break-up fees in other transactions, including transactions where a third party had publicly announced a higher competing offer after the transaction was announced, the board directed Latham & Watkins not to agree to a break-up fee in excess of 3.75% of equity value with no expense reimbursement, and to continue negotiating the other outstanding issues along the lines outlined. Representatives of Goldman Sachs then discussed with the board financial aspects of the proposed transaction, including the possibility of Motorola increasing its offer price above \$1.75 per share. The board directed Goldman Sachs to continue attempts to negotiate a price per share in excess of \$1.75.

Later that day, a representative of Goldman Sachs spoke with Motorola's Senior Vice President of Mergers and Acquisitions. Motorola's officer indicated that he was reviewing the proposed strategic transaction, but had not yet approved it. The Goldman Sachs representative informed him that our board of directors had expressed significant reservations as to whether it would agree to a transaction unless the price per share were above \$1.75. The parties also discussed various due diligence matters, including litigation matters, of continued concern to Motorola.

From April 10<sup>th</sup> through the signing date, the parties and their advisors held numerous calls to resolve outstanding issues. On April 17<sup>th</sup>, Mr. Marino of Motorola informed a representative of Goldman Sachs that all internal Motorola approvals had been obtained to acquire us at a price no greater than \$1.80 per share, which Motorola informed us they viewed as a significant concession given the litigation risk and other risks it would be assuming in the transaction. During the afternoon of April 19<sup>th</sup>, Motorola provided us with a list of the remaining open items with respect to the merger agreement, and outlined a proposal for resolving the remaining open issues. Among the material terms that Motorola accepted were a break-up fee equal to 3.75% of the equity value of the deal with no expense reimbursement, and the removal of a closing condition relating to appraisal rights.

From April 16<sup>th</sup> through April 19<sup>th</sup>, four of our key employees completed negotiations of their respective offer letters with Motorola, as more fully described below in [Interests of Our Directors and Executive Officers in the Merger Agreement](#) [Offer Letters with Motorola](#).

Members of our management and representatives of Goldman Sachs and Latham & Watkins reviewed and discussed Motorola's April 19<sup>th</sup> proposal, and responded with a counterproposal for resolving the remaining open issues early in the morning of April 20<sup>th</sup>. Motorola responded to our counterproposal shortly before noon on April 20<sup>th</sup>, and significantly narrowed the list of remaining open issues. Our board of directors met at 2:00 p.m. PDT on April 20<sup>th</sup>, to discuss with management and our legal and financial advisors the status of negotiations with Motorola and provide input on the remaining outstanding issues. The board directed management and Latham & Watkins to continue to negotiate various tax and employment conditions in order to minimize the pre-closing risk to us that the transaction would not be completed. Following that meeting, our legal counsel continued to work with Motorola's legal counsel throughout the evening to finalize the merger agreement with Motorola.

The parties continued their negotiations that evening and the following day. During the afternoon of April 21<sup>st</sup>, all outstanding terms of the merger agreement were agreed upon, subject in our case to board approval. Our board of directors met at 6:00 p.m. PDT on April 21<sup>st</sup> to consider the proposed transaction. At the meeting, members of management updated the board on the conclusion of negotiations with Motorola. A representative of Latham & Watkins provided the board with a detailed summary of material terms in the merger agreement. Representatives of Goldman Sachs reviewed with the board its financial analysis with respect to the proposed transaction with Motorola, and delivered its oral opinion, subsequently confirmed by delivery of its written opinion, that as of April 21, 2007, and based upon and subject to the factors and assumptions set forth in its written opinion, the \$1.80 per share of common stock in cash to be received by the holders of shares of our common stock pursuant to the merger was fair from a financial point of view to such holders. Based on these considerations and its prior deliberations, the board of directors, by unanimous vote, approved and declared advisable the merger agreement, determined that the merger agreement and the merger were fair to, and in the best interests of, us and our stockholders, directed that the adoption of the merger agreement be submitted to a vote of our stockholders and unanimously recommended that our

stockholders adopt the merger agreement and approve the merger. Shortly thereafter, the parties executed the definitive merger agreement.

Prior to the opening of the New York Stock Exchange on April 23, 2007, we issued a joint press release with Motorola publicly announcing the execution of the merger agreement.

**Table of Contents**

**Reasons for the Merger**

Our board of directors, at a special meeting held on April 21, 2007, unanimously determined that the merger agreement is advisable, fair to and in the best interests of our stockholders and unanimously approved the merger agreement and the merger. Accordingly, the board of directors unanimously recommends that you vote FOR adoption of the merger agreement and approval of the merger at the special meeting.

In the course of determining that the merger agreement is advisable, fair to and in the best interests of our stockholders, the board of directors consulted with management, as well as its financial and legal advisors, and considered the following factors:

the familiarity of the members of the board of directors with, and information provided by management as to, our business, financial condition and results of operations, including the fact that we have not been profitable in any quarterly period other than the quarter ended June 30, 2006, our competitive position, and the nature of our business and the industry in which we compete;

the opinion of Goldman, Sachs & Co. that, as of April 21, 2007, and based upon and subject to the factors and assumptions set forth in its opinion, the \$1.80 per share of common stock in cash to be received by the holders of shares of our common stock pursuant to the merger agreement was fair from a financial point of view to such holders;

the belief of the board of directors that \$1.80 per share represented the highest consideration that Motorola was willing to pay, and the highest per share value obtainable on the date of signing;

the fact the price per share of our common stock had increased significantly on the day prior to announcement of the acquisition, and the closing price of \$1.84 per share on that day represented a 24.3% increase over the closing price per share on the second trading day prior to announcement;

the familiarity of the members of the board of directors with, and information provided by management and Goldman, Sachs & Co., our financial advisor, as to, economic and market conditions, on both a historical and a prospective basis;

the execution risks associated with our management's financial projections provided to the board of directors, as described in Financial Projections, including the fact that the market and earnings per share growth targets were not reflective of our most recent historical results;

our prior discussions with respect to possible business combinations and the scope and outcome of the process conducted to identify parties having a potential interest and ability to acquire us, as described in Background of the Merger;

the impact on us, our business and employees of our restatement and delisting from Nasdaq;

other strategic alternatives available to us, including the possibility of remaining an independent company if we were unable to sell ourselves;

the ability of our stockholders to exercise appraisal rights in connection with the merger, as described under The Merger Appraisal Rights;

the fact that the merger consideration is all cash, which provides certainty of value to our stockholders, compared to a transaction involving all stock consideration or a mixture of stock and cash; and

the terms and conditions of the merger agreement, including:

that the merger agreement does not include a financing condition and our board's conclusion, after consultation with Goldman, Sachs & Co., our financial advisor, that Motorola has the financial ability to complete the merger;

our ability to furnish information to and conduct negotiations with third parties, and to terminate the merger agreement if a third party makes a superior proposal for a business combination or acquisition,

**Table of Contents**

as described under The Merger Agreement No Solicitation of other Acquisition Proposals by Terayon; and

the nature and scope of the closing conditions, including the likelihood that the merger would receive the necessary regulatory approvals and the anticipated timing of those approvals.

Our board of directors also considered potentially negative factors in its deliberations concerning the merger, including:

that we will no longer exist as an independent company and its stockholders will no longer participate in its growth as an independent company;

the fact that the cash merger consideration of \$1.80 per share is lower than the closing price of \$1.84 per share of our common stock on April 20, 2007, the last trading day immediately prior to the public announcement that we signed the merger agreement, and represents a discount of approximately 2.2 percent;

that, under the terms of the merger agreement, we will be unable to solicit other acquisition proposals;

that, under the terms of the merger agreement, we would be required to pay Motorola a termination fee if we were to terminate the merger agreement to accept a superior proposal for a business combination or acquisition of us, and under a number of other circumstances associated with proposals by third parties to acquire us, and that our obligation to pay the termination fee might discourage other parties from proposing a business combination with, or an acquisition of, us (see The Merger Agreement Termination; Payment of Termination Fee );

that gains from an all-cash transaction would be taxable to our stockholders for U.S. federal income tax purposes;

the interests of our executive officers and directors in the merger described under Interests of Our Directors and Executive Officers in the Merger ;

that, while the merger is expected to be completed, there can be no assurance that all conditions to the parties obligations to complete the merger will be satisfied, and as a result, it is possible that the merger may not be completed even if approved by our stockholders (see The Merger Agreement Conditions to the Completion of the Merger );

the restrictions on the conduct of our business prior to the completion of the merger, requiring us to conduct our business in the ordinary course, subject to specific limitations, which may delay or prevent us from undertaking business opportunities that may arise pending completion of the merger: and

the possibility of disruption to our operations following announcement of the merger, and the resulting effect on us if the merger does not close, including the diversion of management and employee attention, potential employee attrition and the potential effect on business and customer relationships.

While the board of directors considered potentially negative and potentially positive factors, the board of directors concluded that overall, the potentially positive factors outweighed the potentially negative factors.

The foregoing discussion of the factors considered by our board of directors is not intended to be exhaustive, but rather includes the material information and factors considered by our board of directors in its consideration of the

merger. The board of directors collectively reached the unanimous decision to approve the merger agreement in light of the factors described above and other factors that each member of the board of directors felt were appropriate. In view of the variety of factors, many of which are qualitative or difficult to quantify, and the quality and amount of information considered, the board of directors did not find it practicable to and did not make specific assessments of, quantify or otherwise assign relative weights to the specific factors considered in reaching its determination. Individual members of the board of directors may have given different weight to different factors.

**Recommendation of Our Board of Directors**

After careful consideration, our board of directors, by unanimous vote, has determined that the merger, the merger agreement and the transactions contemplated by the merger agreement are advisable, fair to and in the best



**Table of Contents**

interests of Terayon and our stockholders, has approved the merger, the merger agreement and the transactions contemplated by the merger agreement, and recommends that Terayon's stockholders vote FOR the adoption of the merger agreement and approval of the merger.

**Opinion of Our Financial Advisor**

Goldman Sachs rendered its opinion to our board of directors that, as of April 21, 2007, and based upon and subject to the factors and assumptions set forth therein, the \$1.80 per share of common stock in cash to be received by the holders of shares of our common stock in the transaction pursuant to the merger agreement was fair from a financial point of view to such holders.

**The full text of the written opinion of Goldman Sachs, dated April 21, 2007, which sets forth assumptions made, procedures followed, matters considered and limitations on the review undertaken in connection with the opinion, is attached as Annex B to this proxy statement. Goldman Sachs provided its opinion for the information of and assistance of our board of directors in connection with its consideration of the transaction. The Goldman Sachs opinion is not a recommendation as to how any holder of shares of common stock should vote with respect to the transaction.**

In connection with rendering the opinion described above and performing its related financial analyses, Goldman Sachs reviewed, among other things:

the merger agreement;

our Annual Reports on Form 10-K for the five years ended December 31, 2006 and our amended Annual Report on Form 10-K/A for the year ended December 31, 2004;

certain of our interim reports to stockholders and Quarterly Reports on Form 10-Q;

certain other communications from us to our stockholders; and

certain internal financial analyses and forecasts for us prepared by our management. See Financial Projections, below.

Goldman Sachs also held discussions with members of our senior management regarding their assessment of our past and current business operations, financial condition and future prospects. In addition, Goldman Sachs reviewed the reported price and trading activity for the shares of our common stock, compared certain financial and stock market information for us with similar information for certain other companies the securities of which are publicly traded, reviewed the financial terms of certain recent business combinations in the communications technology industry specifically and in other industries generally and performed such other studies and analyses, and considered such other factors, as it considered appropriate.

Goldman Sachs relied upon the accuracy and completeness of all of the financial, accounting, legal, tax and other information discussed with or reviewed by it and assumed such accuracy and completeness for purposes of rendering the opinion described above. In that regard, Goldman Sachs assumed with the consent of our board of directors that the internal financial forecasts prepared by our management had been reasonably prepared on a basis reflecting our best currently available estimates and judgments. In addition, Goldman Sachs did not make an independent evaluation or appraisal of the assets and liabilities (including any contingent, derivative or off-balance-sheet assets and liabilities) of us or any of our subsidiaries, nor was any such evaluation or appraisal furnished to Goldman Sachs.

Goldman Sachs opinion does not address our underlying business decision to engage in the transactions contemplated by the merger agreement. Goldman Sachs opinion is necessarily based on economic, monetary, market and other conditions as in effect on, and the information made available to Goldman Sachs as of, the date of its opinion.

The following is a summary of the material financial analyses delivered by Goldman Sachs to our board of directors in connection with rendering the opinion described above. The following summary, however, does not purport to be a complete description of the financial analyses performed by Goldman Sachs, nor does the order of analyses described represent relative importance or weight given to those analyses by Goldman Sachs. Some of the

**Table of Contents**

summaries of the financial analyses include information presented in tabular format. The tables must be read together with the full text of each summary and are alone not a complete description of Goldman Sachs' financial analyses. Except as otherwise noted, the following quantitative information, to the extent that it is based on market data, is based on market data as it existed on or before April 21, 2007, and is not necessarily indicative of current market conditions.

*Discounted Cash Flow Analysis.* Goldman Sachs performed a discounted cash flow analysis based on forecasts by our management to determine a range of implied present values per share of our common stock. All unlevered cash flows were discounted to March 31, 2007, and illustrative terminal values were based upon perpetuity growth rates ranging from 3.0% to 7.0% for unlevered free cash flows for years 2012 and beyond. In performing the discounted cash flow analysis, Goldman Sachs applied discount rates ranging from 13.0% to 17.0% to our projected unlevered free cash flows for calendar years 2007 to 2011. This analysis resulted in a range of implied present values of \$0.64 to \$1.26 per share of our common stock.

*Selected Companies Analysis.* Goldman Sachs reviewed and compared certain financial information for us to corresponding financial information, ratios and public market multiples for the following publicly traded corporations in the large capitalization communications technology infrastructure, encoding and software driven video technology and hardware driven video technology industries.

**Large Capitalization  
Communications  
Technology Infrastructure**

Alcatel-Lucent  
Cisco Systems, Inc.  
Harris Corporation  
Juniper Networks, Inc.  
Motorola, Inc.  
Thomson

**Encoding and Software Driven  
Video Technology**

Harmonic, Inc.  
Kudelski SA  
Macrovision Corporation

**Hardware Driven Video  
Technology**

ARRIS Group, Inc.  
C-COR Incorporated  
Pace Micro Technology plc  
Westell Technologies, Inc.

Although none of the selected companies is directly comparable to us, the companies included were chosen because they are publicly traded companies with operations that for purposes of analysis may be considered similar to certain of our operations.

Goldman Sachs calculated and compared the enterprise value to estimated 2007 and 2008 revenue and the price per share to estimated 2007 earnings per share and estimated 2008 earnings per share of us and the selected companies listed above based on financial data and shares prices as of April 20, 2007, information obtained from SEC filings, estimates provided by the Institutional Brokers' Estimate System (a data service that compiles estimates issued by securities analysts), or IBES, for the selected companies and us and information and forecasts for us provided by our management.

The results of these analyses are summarized as follows:

**Company**

**Estimated  
2007**

**Estimated  
2008**

	<b>Enterprise Value/Revenue Multiples</b>	<b>Enterprise Value/Revenue Multiples</b>	<b>Estimated 2007 Price/Earnings Multiples</b>	<b>Estimated 2008 Price/Earnings Multiples</b>
Terayon (Management)	1.9x(2)	1.8x(2)	NM(1)	105.6x
Terayon (IBES Median)	2.3(2)	1.7(2)	NM(1)	30.7

**Table of Contents****Large Capitalization Communications Technology Infrastructure**

Selected Company	Estimated 2007	Estimated 2008	Estimated 2007	Estimated 2008
	Enterprise Value/Revenue Multiples	Enterprise Value/Revenue Multiples	Price/Earnings Multiples	Price/Earnings Multiples
Alcatel-Lucent	1.1x	1.1x	20.2x	13.1x
Cisco Systems, Inc.	4.4	3.8	19.0	16.4
Harris Corporation	1.7	1.5	17.0	15.3
Juniper Networks, Inc.	3.7	3.2	25.3	20.9
Motorola, Inc.	1.0	0.9	43.4	18.8
Thomson	0.9	0.8	14.4	11.3
Mean	2.1x	1.9x	23.2x	16.0x
Median	1.4	1.3	19.6	15.9

**Encoding and Software Driven Video Technology**

Selected Company	Estimated 2007	Estimated 2008	Estimated 2007	Estimated 2008
	Enterprise Value/Revenue Multiples	Enterprise Value/Revenue Multiples	Price/Earnings Multiples	Price/Earnings Multiples
Harmonic, Inc.	2.5x	2.4x	29.1x	20.3x
Kudelski SA	2.2	1.9	23.2	19.0
Macrovision Corporation	4.6	4.0	19.9	16.3
Mean	3.1x	2.8x	24.1x	18.5x
Median	2.5	2.4	23.2	19.0

**Hardware Driven Video Technology**

Selected Company	Estimated 2007	Estimated 2008	Estimated 2007	Estimated 2008
	Enterprise Value/Revenue Multiples	Enterprise Value/Revenue Multiples	Price/Earnings Multiples	Price/Earnings Multiples
ARRIS Group, Inc.	1.4x	1.3x	18.0x	15.8x
C-COR Incorporated	2.0	1.7	22.5	18.6
Pace Micro Technology plc	0.5	0.5	NM(1)	17.2
Westell Technologies, Inc.	0.5	0.5	25.8	25.3

Mean	1.1x	1.0x	22.1x	19.2x
Median	1.0	0.9	22.5	17.9

- (1) Not meaningful (projected earnings negative for period).
- (2) Terayon IBES Median and Management 1-year forward revenue estimates represent video revenue estimates only.

*Illustrative Present Value of Hypothetical Future Share Price Analysis:* Goldman Sachs performed an illustrative present value of hypothetical future share price analysis, which is designed to provide an indication of the present value of a theoretical future value of a company's equity as a function of such company's (i) assumed future enterprise value to revenue multiple and (ii) assumed price to future earnings per share multiple. For this analysis, Goldman Sachs used the financial projections prepared by our management for 2009 and 2010 and used assumed enterprise value to revenue multiples and price to future earnings per share multiples based on 2008 enterprise value to revenue multiples and 2008 price to future earnings per share multiples of the selected companies listed above.

Goldman Sachs first calculated the implied values per share of common stock for each of 2009 and 2010 by applying illustrative enterprise value to revenue multiples of 1.0x to 2.0x to estimated revenue for each of 2009 and

**Table of Contents**

2010, adding our net cash balance as of March 31, 2007, discounting the 2009 and 2010 values back to March 31, 2007, using an illustrative discount rate of 15%. This analysis resulted in a range of implied present values of \$1.04 to \$2.00 per share of our common stock.

Goldman Sachs then calculated the implied values per share of common stock for each of 2009 and 2010 by applying illustrative price to earnings per share multiples of 15.0x to 25.0x to earnings per share estimates for each of 2009 and 2010 and discounting the 2009 and 2010 values back to March 31, 2007, using an illustrative discount rate of 15%. This analysis resulted in a range of implied present values of \$0.91 to \$1.86 per share of our common stock.

*Selected Transactions Analysis.* Goldman Sachs reviewed certain publicly available information relating to the following selected transactions in the communications technology industry:

<b>Announcement Date</b>	<b>Acquiror/Target</b>
February 26, 2007	LM Ericsson Telephone Company / Tandberg Television ASA
January 15, 2007	ARRIS Group, Inc. / Tandberg Television ASA
December 22, 2006	Motorola, Inc. / Tut Systems, Inc.
August 22, 2006	Harmonic, Inc. / Entone Technologies, Inc. (Video Networking Software Business)
August 21, 2006	Cisco Systems, Inc. / Arroyo Video Solutions, Inc.
July 25, 2006	Motorola, Inc. / Broadbus Technologies, Inc.
February 8, 2006	Tandberg Television ASA / SkyStream Networks, Inc.
November 18, 2005	Cisco Systems, Inc. / Scientific-Atlanta, Inc.
October 17, 2005	Tandberg Television ASA / GoldPocket Interactive, Inc.
August 31, 2005	Harris Corporation / Leitch Technology Corporation
July 28, 2005	Thomson / PRN Corporation
January 6, 2005	Tandberg Television ASA / N2 Broadband, Inc.
October 20, 2004	C-COR Incorporated / nCUBE Corporation

While none of the companies that participated in the selected transactions are directly comparable to us, the companies that participated in the selected transactions are companies with operations that, for the purposes of analysis, may be considered similar to certain of our operations.

For each of the selected transactions, Goldman Sachs calculated and compared (i) total enterprise value as a multiple of the target company's IBES estimated one year forward revenue; and (ii) equity value as a multiple of the target company's IBES estimated one year forward net income.

The following table presents the results of this analysis:

	<b>Mean</b>	<b>Median</b>
<b>Enterprise Value/1-Year Forward Revenue</b>	2.3x	2.5x
<b>Equity Value/1-Year Forward Net Income</b>	21.9x	22.7x

**Multiple**

**Terayon (IBES Median)**

Enterprise Value/1-Year Forward Revenue	2.4x(2)
Equity Value/1-Year Forward Net Income	NM(1)
Equity Value/2-Year Forward Net Income	30.0x
<b>Terayon (Management)</b>	
Enterprise Value/1-Year Forward Revenue	2.0x(2)
Equity Value/1-Year Forward Net Income	NM(1)
Equity Value/2-Year Forward Net Income	103.3x



**Table of Contents**

- (1) Not meaningful (projected net income negative for period).
- (2) Terayon IBES Median and Management 1-year forward revenue estimates represent video revenue estimates only.

The preparation of a fairness opinion is a complex process and is not necessarily susceptible to partial analysis or summary description. Selecting portions of the analyses or of the summary set forth above, without considering the analyses as a whole, could create an incomplete view of the processes underlying Goldman Sachs' opinion. In arriving at its fairness determination, Goldman Sachs considered the results of all of its analyses and did not attribute any particular weight to any factor or analysis considered by it. Rather, Goldman Sachs made its determination as to fairness on the basis of its experience and professional judgment after considering the results of all of its analyses. No company or transaction used in the above analyses as a comparison is directly comparable to us or the contemplated merger.

Goldman Sachs prepared these analyses for purposes of Goldman Sachs providing its opinion to our board of directors as to the fairness from a financial point of view to the holders of the outstanding shares of common stock of the \$1.80 per share of common stock in cash to be received by holders of the shares of common stock in the transaction pursuant to the merger agreement. These analyses do not purport to be appraisals nor do they necessarily reflect the prices at which businesses or securities actually may be sold. Analyses based upon forecasts of future results are not necessarily indicative of actual future results, which may be significantly more or less favorable than suggested by these analyses. Because these analyses are inherently subject to uncertainty, being based upon numerous factors or events beyond the control of the parties or their respective advisors, none of us, Goldman Sachs or any other person assumes responsibility if future results are materially different from those forecast.

The merger consideration was determined through arms'-length negotiations between us and Motorola and was approved by our board of directors. Goldman Sachs provided advice to us during these negotiations. Goldman Sachs did not, however, recommend any specific amount of consideration to us or our board of directors or that any specific amount of consideration constituted the only appropriate consideration for the transaction.

As described above, Goldman Sachs' opinion to our board of directors was one of many factors taken into consideration by our board of directors in making its determination to approve the merger agreement. The foregoing summary does not purport to be a complete description of the analyses performed by Goldman Sachs in connection with the fairness opinion and is qualified in its entirety by reference to the written opinion of Goldman Sachs attached as Annex B to this proxy statement.

Goldman Sachs and its affiliates, as part of their investment banking business, are continually engaged in performing financial analyses with respect to businesses and their securities in connection with mergers and acquisitions, negotiated underwritings, competitive biddings, secondary distributions of listed and unlisted securities, private placements and other transactions as well as for estate, corporate and other purposes. Goldman Sachs has acted as financial advisor to us in connection with, and has participated in certain of the negotiations leading to, the transaction contemplated by the merger agreement. Goldman Sachs is providing and has provided certain investment banking services to Motorola from time to time, including having acted as remarketing agent in connection with the remarketing of \$1,200,000,000 in principal amount of Motorola's 4.608% notes due 2007 in August 2004, as dealer-manager in connection with the sale of Motorola's 16.4% stake in Pantech Co. in November 2004, as dealer-manager in September 2005 in connection with the tender offer for up to a total of \$1,000,000,000 in principal amount of Motorola's outstanding debt securities including Motorola's 6.5% notes due 2008, Motorola's 5.8% notes due 2008, Motorola's 7.625% notes due 2010 and Motorola's 8.0% notes due 2011 in September 2005, as exclusive financial advisor in connection with Motorola's investment in Clearwire Corporation and associated acquisition of

NextNet Wireless, Inc. announced in July 2006, as exclusive financial advisor in connection with Motorola's acquisition of Symbol Technologies, Inc. announced in September 2006 and as exclusive financial advisor in connection with a proxy contest relating to Motorola's 2007 Annual Meeting of Stockholders. Goldman Sachs has also acted for Motorola in various stock repurchase activities from time to time. In addition, Goldman Sachs is providing and has provided certain investment banking services to Freescale Semiconductor, Inc. ( Freescale ), a former subsidiary of Motorola, including having acted as global coordinator and joint bookrunning manager in connection with the initial public offering of 121,621,622 shares of Freescale's class A common stock in July 2004, as lead manager in connection with the offering of \$400,000,000 in principal amount of

**Table of Contents**

Freescale's floating rate notes due 2009 in July 2004, as co-manager in connection with the offering of \$350,000,000 of Freescale's 6.875% notes due 2011 and \$500,000,000 in principal amount of Freescale's 7.125% notes due July 2014 in July 2004.

Goldman Sachs also may provide investment banking services to us and Motorola in the future. In connection with the above-described investment banking services Goldman Sachs has received, and may receive, compensation.

Goldman, Sachs & Co. is a full service securities firm engaged, either directly or through its affiliates, in securities trading, investment management, financial planning and benefits counseling, risk management, hedging, financing and brokerage activities for both companies and individuals. In the ordinary course of these activities, Goldman, Sachs & Co. and its affiliates may provide such service to us, Motorola and their respective affiliates, may actively trade the debt and equity securities (or related derivative securities) of us and Motorola for their own account and for the accounts of their customers and may at any time hold long and short positions of such securities.

Our board of directors selected Goldman Sachs as its financial advisor because it is an internationally recognized investment banking firm that has substantial experience in transactions similar to the transaction. Pursuant to a letter agreement dated May 30, 2005, as amended by a letter agreement dated April 19, 2007, we engaged Goldman Sachs to act as our financial advisor in connection with the contemplated transactions. Pursuant to the amended letter agreement, between Goldman Sachs and us, we have agreed to pay Goldman Sachs a transaction fee of approximately \$4.0 million in connection with the transaction. \$1.0 million of the transaction fee, net of retainer fees paid by us to Goldman Sachs through the end of December 2006, became due upon the signing of the merger agreement based on our request that Goldman Sachs undertake a study in order to enable it to render its opinion as to the fairness from a financial point of view of the \$1.80 per share of common stock in cash to be received by the holders of shares of our common stock pursuant to the merger agreement. The remaining \$3.0 million of the transaction fee is due upon the consummation of the transaction. In addition, retainer fees in the amount of \$50,000 per month from January 2007 onwards have been deferred under the amended letter agreement, and will become due upon the earlier of the consummation of the transaction or the termination of Goldman Sachs' engagement under the amended letter agreement. In addition, we have agreed to reimburse Goldman Sachs for its expenses, including attorneys' fees and disbursements, and to indemnify Goldman Sachs and related persons against various liabilities, including certain liabilities under the federal securities laws.

**Financial Projections**

Our management does not as a matter of course make public projections as to future performance or earnings beyond the current fiscal year and is especially wary of making projections for extended periods due to the unpredictability of the underlying assumptions and estimates. However, certain financial projections prepared by management were made available to Motorola, the other potential acquirors that signed confidentiality agreements with us, our board of directors and Goldman Sachs in connection with a potential transaction. We have included below the material financial projections (on a consolidated basis) to provide our stockholders access to certain nonpublic information that was provided to Motorola, the other potential acquirors that signed confidentiality agreements with us, our board of directors and Goldman Sachs in connection with a potential transaction. The inclusion of this information should not be regarded as an indication that Motorola, the other potential acquirors, our board of directors, Goldman Sachs or any other recipient of this information considered, or now considers, it to be a reliable prediction of future results. Our board of directors considered the execution risks associated with the financial projections below in considering and evaluating the merger, including the fact that the market and earnings per share growth targets were not reflective of our recent historical results.

The financial projections reflect numerous estimates and assumptions with respect to industry performance, general business, economic, regulatory, market and financial conditions, as well as matters specific to our business, all of

which are difficult to predict and many of which are beyond our control. As a result, there can be no assurance that the projected results will be realized or that actual results will not be significantly higher or lower than projected. The financial projections cover multiple years and such information by its nature becomes less reliable with each successive year. The financial projections were prepared solely for internal use and for the use of Motorola, the other potential acquirors that signed confidentiality agreements with us, our board of directors and Goldman Sachs in connection with a potential transaction and not with a view toward public disclosure or toward

**Table of Contents**

complying with GAAP, the published guidelines of the SEC regarding projections or the guidelines established by the American Institute of Certified Public Accountants for preparation and presentation of prospective financial information. For example, the first assumption listed in the second footnote below relating to calculation of gross profit indicates that gross profit was not calculated in accordance with GAAP. The financial projections included below were prepared by, and are the responsibility of, our management. Neither our independent registered public accounting firm, nor any other independent accountants, have compiled, examined or performed any procedures with respect to the prospective financial information contained herein, nor have they expressed any opinion or any other form of assurance on such information or its achievability, and assume no responsibility for, and disclaim any association with, the prospective financial information. The financial projections do not take into account any circumstances or events occurring after the date they were prepared.

The inclusion of financial projections in this proxy statement should not be regarded as an indication that such targets will be an accurate prediction of future events, and they should not be relied on as such. Except as required by applicable securities laws, we do not intend to update, or otherwise revise the financial projections to reflect circumstances existing after the date when made or to reflect the occurrence of future events, even in the event that any or all of the assumptions are shown to be in error. See Cautionary Statement Regarding Forward-Looking Statements.

	<b>Fiscal Year End(1)</b>			
	<b>Estimated</b>	<b>Estimated</b>	<b>Estimated</b>	<b>Estimated</b>
	<b>12/31/2007(2)</b>	<b>12/31/2008(2)</b>	<b>12/31/2009(2)</b>	<b>12/31/2010(2)</b>
<b>Revenue</b>	\$ 63.5	\$ 69.3	\$ 76.9	\$ 83.2
<b>Cost of goods sold</b>	19.7	21.6	23.4	26.0
<b>Gross profit</b>	43.8	47.7	53.3	57.2
<b>Operating Expenses</b>	43.4	47.1	49.0	50.8
<b>Operating Income</b>	0.3	0.6	4.3	6.4
<b>Other Income</b>	0.7	1.0	1.2	1.3
<b>Income before taxes</b>	1.0	1.6	5.5	7.7
<b>Income tax expense</b>	0.4	0.2	0.2	0.2
<b>Net Income</b>	0.6	1.4	5.3	7.5
<b>Diluted EPS</b>	\$ 0.01	\$ 0.02	\$ 0.07	\$ 0.09

- (1) Financial projections for all years were provided to our board of directors and Goldman Sachs. Financial projections for fiscal year 2007 were provided to Motorola and the other potential acquirors that signed confidentiality agreements with us. For purposes of the discounted cash flow analysis performed by Goldman Sachs, financial projections for fiscal year 2011 were derived assuming projected video revenue growth for fiscal year 2011 equal to average projected video revenue growth for fiscal years 2008 through 2010 and projected operating margins for fiscal year 2011 equal to projected operating margins for fiscal year 2010.

- (2) All dollars in the above chart are in millions, except per share data. The principal assumptions of our management preparing the projections are as follows:

Gross profit equals revenue for products shipped plus service recognized during the period less cost of goods sold during the period, and excludes hardware revenue and cost of goods sold from prior periods;

Revenue projections are based on introduction and market acceptance of new video technology products;

Net cash is assumed to be \$21.6 million as of March 31, 2007;

Diluted earnings per share assumes 78 million shares outstanding; and

Effective tax rate is not meaningful, given availability of federal and state net operating losses.

**Table of Contents**

**Interests of Our Directors and Executive Officers in the Merger**

In considering the recommendation of our board of directors with respect to the merger, you should be aware that all of our directors and executive officers have personal interests in the merger that are, or may be, different from, or in addition to, your interests. Our board of directors was aware of the interests described below and considered them, among other matters, when approving the merger agreement and the merger.

*Employment Agreements.* In July 2005, we entered into employment agreements with Jerry Chase, our Chief Executive Officer and a member of our board of directors; Mark Richman, our Chief Financial Officer and Vice President of Finance and Administration; and Matthew Aden, our Vice President of Global Sales and Customer Support, who constitute our executive officers and whom we sometimes refer to as our named executive officers. The employment agreements for each of these executive officers provide for certain severance payments and benefits if their employment terminates following a change in control under certain circumstances. The completion of the merger will constitute a change in control for purposes of the employment agreements. In addition, Motorola has informed us that it intends at this time to terminate the employment of Mr. Chase and Mr. Richman around the time the merger is completed. Motorola has informed us that it is considering the role, if any, of Mr. Aden after the completion of the merger, but no arrangements have been made at this time.

The employment agreements, as amended as discussed below, provide for the following severance benefits in the event that the employment of these officers is involuntarily terminated (as defined in each employment agreement and set forth below), within twelve months after a change in control (as defined in each employment agreement), provided the executive officer has executed a general form of release:

Mr. Chase and Mr. Richman are entitled to a lump-sum cash payment of 2.5 times and two times, respectively, the sum of (1) the executive officer's base salary (at the greater of the rate in effect at the time of termination or the rate in effect immediately prior to the change in control) and (2) the greater of the executive officer's annual performance bonus for the most recent calendar year prior to the date of termination or the executive officer's target performance bonus in effect for the year in which the executive officer's employment is terminated;

Mr. Aden is entitled to a lump-sum cash payment of two times the sum of (1) his base salary (at the greater of the rate in effect at the time of termination or the rate in effect immediately prior to the change in control) and (2) the greater of his annual sales commission payment for the most recent calendar year prior to the date of termination or his target sales commission payment in effect for the year in which his employment is terminated;

Mr. Chase, Mr. Richman and Mr. Aden are entitled to continuation for up to 24 months (30 months in the case of Mr. Chase), but no longer than the expiration of the applicable continuation coverage period under COBRA, at our cost of the health care benefits that were being provided by us to each executive officer and his dependents immediately prior to the termination of employment;

Mr. Chase, Mr. Richman and Mr. Aden are entitled to full option vesting acceleration; and

In the event any payment or distribution to or for the benefit of Mr. Chase or Mr. Richman under the employment agreements or otherwise is deemed to constitute an excess parachute payment within the meaning of Section 280G of the Internal Revenue Code, and such payments and benefits will cause Mr. Chase and Mr. Richman to incur an excise tax under Section 4999 of the Internal Revenue Code, then the executive officer will be responsible for the first \$200,000 in excise tax imposed and, if the amount of excise tax exceeds

\$200,000, then the executive officer will be entitled to receive from the Company as additional payment equal to the amount of any excise tax in excess of \$200,000.

In general involuntary termination (as defined in the employment agreements) means:

The involuntary discharge of the employee by the Company for reasons other than cause or permanent disability (each as defined in the employment agreements); or

the voluntary resignation of the employee within 30 days following:

a material adverse change to the employee's title, authority or responsibilities with the Company;



**Table of Contents**

a material reduction in the employee's base salary; or

receipt of notice that the employee's principal workplace will be relocated by more than 25 miles.

In addition to the severance payments and benefits that Mr. Chase, Mr. Richman and Mr. Aden are entitled to under their employment agreements, we will pay for the cost of employment outplacement counseling services upon the involuntary termination of their employment under the circumstances described for purposes of their employment agreements.

Our other non-executive officers and certain of our key employees are also entitled to severance benefits similar to the types of severance benefits to which our named executive officers are entitled to receive (as described above) in the event that their employment is involuntarily terminated within twelve months after a change in control, including the completion of the merger.

On April 21, 2007, our Board of Directors approved amendments to the employment agreements of certain of our employees, including our named executive officers, revising the formulation that will be applied to determine the bonus amount used for calculating the severance amount payable under the employment agreements. As previously written, the formula was based on the greater of the annual performance bonus paid in the prior year or the current year's bonus target. As no bonus targets have been established for 2007 due to our decision to delay the implementation of our 2007 corporate bonus plans, the formulation was amended to provide that the bonus amount would be equal to the greater of (i) the annual performance bonus (or, for Mr. Aden, the annual sales commission payments) paid in 2006 or (ii) a specified percentage of the employee's base salary in 2007. The specified percentages are the same as the bonus target percentages currently set forth in the respective employment agreements for such employees. The amendments to the employment agreements are effective immediately prior to, and are conditioned upon, the completion of the merger.

*Retention Transaction Plan.* In May 2006, we adopted the Retention Transaction Plan, which provides for the payment of transaction bonuses to certain non-executive officers and key employees who remain employed with us following a change in control (as the term is defined in the plan document). The completion of the merger will constitute a change in control for purposes of the Retention Transaction Plan. Under the Retention Transaction Plan, a participant is eligible to receive a transaction bonus equal to a specified percentage of the bonus pool. The bonus pool is equal to 2% of the total merger consideration less \$5,000,000 and less certain incurred expenses and other reductions, and subject to certain limitations, as contemplated in the plan document. None of our named executive officers participates in the Retention Transaction Plan.

*Options.* All options, including options held by our executive officers and directors, to purchase shares of our common stock granted under our 1995 Stock Option Plan, 1997 Equity Incentive Plan, 1998 Non-Employee Director's Stock Option Plan, and 1999 Non-Officer Equity Incentive Plan, as well as all options granted outside of any plan, including any unvested portion of such options, will be cashed out in the merger. For these purposes, "cashed out in the merger" means that the option, whether vested or unvested, will be cancelled in the merger in exchange for a cash payment equal to the product of (i) the excess, if any, of \$1.80 over the applicable per share option exercise price and (ii) the number of shares of our common stock subject to the option at such time, without interest and less any applicable withholding taxes. The aggregate cash-out value of all of our options that are in-the-money is approximately \$188,000.

*Offer Letters with Motorola.* Contemporaneously with the execution of the merger agreement, four of our key employees who are not executive officers entered into employment offer letters with Motorola that become effective and are conditioned upon, the completion of the merger. These employment offer letters, which do not provide for

employment with Motorola for any specified period, supersede any employment and compensation arrangements in effect between the employee and us, except for our Retention Transaction Plan, which is described above, and in the case of one of the key employees, an additional performance plan applicable only to him.

Motorola has informed us that it intends to enter into additional employment offer letters with other key employees prior to the completion of the merger.

*Indemnification.* The terms of the merger agreement provide for the continued indemnification of our directors and officers and provision of insurance for their benefit as more fully described below under The Merger Agreement Directors and Officers Indemnification, Advancement of Expenses, Exculpation and Insurance.

**Table of Contents**

**Material United States Federal Income Tax Consequences**

The following discussion is a summary of certain material U.S. federal income tax consequences of the merger to United States Holders (as defined below) of our common stock whose shares are converted into the right to receive cash at the effective time of the merger. This summary is based on the Internal Revenue Code of 1986, as amended (the Code), applicable Treasury Regulations, and administrative and judicial interpretations thereof, each as in effect as of the date hereof, all of which may change, possibly with retroactive effect.

This summary is limited to United States Holders who hold our shares of common stock as capital assets. This summary also does not address tax considerations applicable to a holder's particular circumstances or to holders who may be subject to special tax rules, including, without limitation:

banks, insurance companies or other financial institutions;

broker-dealers;

traders;

expatriates;

tax-exempt organizations;

persons subject to alternative minimum tax;

partnerships, S-corporations or other pass-through entities;

persons who hold their shares of common stock as a position in a hedging transaction, straddle, conversion transaction, or other risk reduction transaction;

persons deemed to sell their shares of common stock under the constructive sale provisions of the Code;

persons who have a functional currency other than the United States dollar; or

persons who acquired their shares of our common stock upon the exercise of stock options or otherwise in connection with the performance of services.

In addition, this summary does not address any U.S. federal estate or gift tax consequences, nor any state, local or foreign tax consequences, of the merger, and this summary does not address the tax consequences to holders of our common stock who exercise appraisal rights under Delaware law.

**THIS SUMMARY DOES NOT PURPORT TO BE A COMPLETE ANALYSIS OF THE POTENTIAL TAX CONSIDERATIONS RELATING TO THE MERGER, AND IS NOT TAX ADVICE. THEREFORE, YOU ARE URGED TO CONSULT YOUR TAX ADVISOR WITH RESPECT TO THE APPLICATION OF THE U.S. FEDERAL INCOME TAX LAWS TO YOUR PARTICULAR SITUATION, AS WELL AS ANY TAX CONSEQUENCES OF THE MERGER ARISING UNDER THE FEDERAL ESTATE OR GIFT TAX RULES OR UNDER THE LAWS OF ANY STATE, LOCAL OR FOREIGN TAXING JURISDICTION OR UNDER ANY APPLICABLE TAX TREATY.**

For purposes of this discussion, a United States Holder means a holder that is:

an individual citizen or resident of the United States;

a corporation (or an entity treated as a corporation for U.S. federal income tax purposes) created or organized in or under the laws of the United States, any state thereof or the District of Columbia;

an estate the income of which is subject to U.S. federal income taxation regardless of its source; or

a trust (a) the administration over which a U.S. court can exercise primary supervision and all of the substantial decisions of which one or more U.S. persons have the authority to control and (b) certain other trusts considered United States Holders for U.S. federal income tax purposes.

**Table of Contents**

***Consequences of the Merger***

The receipt of cash in exchange for shares of our common stock pursuant to the merger will be a taxable transaction for U.S. federal income tax purposes. In general, a United States Holder who receives cash in exchange for shares of our common stock pursuant to the merger will recognize capital gain or loss for U.S. federal income tax purposes equal to the difference, if any, between the amount of cash received and the holder's adjusted tax basis in the shares of our common stock exchanged for that cash. Any such gain or loss would be long-term capital gain or loss if the holding period for the shares of our common stock exceeded one year. Long-term capital gains of noncorporate taxpayers are generally taxable at reduced rates. The deductibility of capital losses is subject to limitations. Gain or loss must be calculated separately for each block of common stock (i.e., shares acquired at the same cost in a single transaction) exchanged for cash in the merger.

***Backup Withholding***

Backup withholding may apply to payments made in connection with the merger. Backup withholding will not apply, however, to a holder who (1) furnishes the holder's correct taxpayer identification number and certifies that the holder is not subject to backup withholding on the substitute Form W-9 or successor form included in the letter of transmittal to be delivered to holders of our common stock prior to completion of the merger, or (2) is otherwise exempt from backup withholding. Backup withholding is not an additional tax, but rather, is a method of tax collection. Any amounts withheld under the backup withholding rules may be allowed as a refund or a credit against such holder's U.S. federal income tax liability provided the required information is furnished to the Internal Revenue Service.

**Regulatory Approvals**

Under the Hart-Scott-Rodino Antitrust Improvements Act of 1976 and the rules promulgated thereunder by the Federal Trade Commission, certain transactions, including the merger, may not be completed unless waiting period requirements have been satisfied. We and Motorola filed notification and report forms with the Antitrust Division of the Department of Justice and the Federal Trade Commission on [ ], 2007. The waiting period will expire at 11:59 p.m. on [ ], 2007, unless extended by a request for more information or shortened by an early termination notice. In addition, filings are required to be made with, and regulatory approvals are required to be obtained from, antitrust or competition authorities in other nations, including Germany, Israel and the Ukraine. All of these filings have been made or will be made shortly. Until approvals have been received from antitrust or competition authorities, or required waiting periods have ended in each of those jurisdictions, we are prohibited from completing the merger. Neither we nor Motorola have yet obtained any of the governmental or regulatory approvals required to complete the merger.

While we expect to obtain all required regulatory approvals, we cannot assure you that these regulatory approvals will be obtained or that the granting of these regulatory approvals will not involve the imposition of conditions on the completion of the merger or require changes to the terms of the merger that would have a material adverse effect on the combined company. These conditions or changes could require the grant of a complete or partial license, a divestiture or spin-off, or the holding separate of assets or businesses and could result in the conditions to Motorola's obligation to complete the merger not being satisfied.

In addition, at any time before or after the effective time of the merger, the Antitrust Division, the Federal Trade Commission or others could take action under the antitrust laws, including seeking to prevent the merger, to rescind the merger or to conditionally approve the merger upon the divestiture by us or Motorola of substantial assets. In addition, in some jurisdictions, a competitor, customer or other third party could initiate a private action under the antitrust laws challenging or seeking to enjoin the merger, before or after it is completed. There can be no assurance that a challenge to the merger on antitrust grounds will not be made or, if such a challenge is made, that it would not

be successful.

**Appraisal Rights**

Holders of record of shares of our common stock who do not vote in favor of the adoption of the merger agreement and approval of the merger and who properly demand appraisal of their shares will be entitled to

**Table of Contents**

appraisal rights in connection with the merger under Section 262 of the General Corporation Law of the State of Delaware.

**The following discussion is not a complete statement of the law pertaining to appraisal rights under Section 262 and is qualified in its entirety by the full text of Section 262 which is attached to this proxy statement as Annex C. All references in Section 262 and in this summary to a stockholder are to the record holder of the shares of our common stock as to which appraisal rights are asserted. A person having a beneficial interest in shares of our common stock held of record in the name of another person, such as a broker, fiduciary, depositary or other nominee, must act promptly to cause the record holder to follow the steps summarized below properly and in a timely manner to perfect appraisal rights.**

Under Section 262, stockholders who follow the procedures set forth in Section 262 will be entitled to have their shares appraised by the Delaware Court of Chancery and to receive payment of the fair value of the shares, exclusive of any element of value arising from the accomplishment or expectation of the merger, together with a fair rate of interest, if any, as determined by the court.

Under Section 262, where a merger is to be submitted for approval at a meeting of stockholders, as in the case of the adoption of the merger agreement and approval of the merger by our stockholders, the corporation, not less than 20 days prior to the meeting, must notify each of its stockholders entitled to appraisal rights that appraisal rights are available and include in the notice a copy of Section 262. This proxy statement shall constitute the notice, and the full text of Section 262 is attached to this proxy statement as Annex C. Any stockholder who wishes to exercise appraisal rights or who wishes to preserve such stockholder's right to do so, should review the following discussion and Annex C carefully because failure to timely and properly comply with the procedures specified will result in the loss of appraisal rights.

Any stockholder wishing to exercise appraisal rights must deliver to us, before the vote on the adoption of the merger agreement and approval of the merger at the special meeting, a written demand for the appraisal of the stockholder's shares, and must not vote in favor of the adoption of the merger agreement and approval of the merger. A stockholder wishing to exercise appraisal rights must hold of record the shares on the date the written demand for appraisal is made and must continue to hold the shares of record through the effective time of the merger. A vote against the adoption of the merger agreement and approval of the merger will not in and of itself constitute a written demand for appraisal satisfying the requirements of Section 262. The written demand for appraisal must be in addition to and separate from any proxy or vote. The demand must reasonably inform us of the identity of the stockholder as well as the intention of the stockholder to demand an appraisal of the fair value of the shares held by the stockholder. A stockholder's failure to make the written demand prior to the taking of the vote on the adoption of the merger agreement and approval of the merger at the special meeting of stockholders will constitute a waiver of appraisal rights.

Only a holder of record of shares of our common stock is entitled to assert appraisal rights for the shares registered in that stockholder's name. A demand for appraisal should be executed by or on behalf of the holder of record, fully and correctly, as the stockholder's name appears on the stockholder's stock certificates, and must state that the person intends thereby to demand appraisal of the stockholder's shares in connection with the merger. If the shares are owned of record in a fiduciary capacity, such as by a trustee, guardian or custodian, execution of the demand should be made in that capacity, and if the shares are owned of record by more than one person, as in a joint tenancy and tenancy in common, the demand should be executed by or on behalf of all joint owners. An authorized agent, including an agent for two or more joint owners, may execute a demand for appraisal on behalf of a holder of record; however, the agent must identify the record owner or owners and expressly disclose the fact that, in executing the demand, the agent is acting as agent for the record owner or owners. A record holder such as a broker who holds shares as nominee for several beneficial owners may exercise appraisal rights with respect to the shares held for one or more beneficial

owners while not exercising the rights with respect to the shares held for other beneficial owners; in such case, however, the written demand should set forth the number of shares as to which appraisal is sought and where no number of shares is expressly mentioned the demand will be presumed to cover all shares of our common stock held in the name of the record owner. **Stockholders who hold their shares in brokerage accounts or other nominee forms and who wish to exercise appraisal rights are urged to promptly**



**Table of Contents**

**consult with their brokers to determine the appropriate procedures for the making of a demand for appraisal by such a nominee.**

All written demands for appraisal pursuant to Section 262 should be sent or delivered to us at Terayon Communication Systems, Inc., 2450 Walsh Avenue, Santa Clara, California 95051, Attention: Secretary.

Within ten days after the effective time of the merger, the surviving corporation must notify each stockholder who has complied with Section 262 and who has not voted in favor of the adoption of the merger agreement and approval of the merger that the merger has become effective. Within 120 days after the effective time of the merger, but not thereafter, the surviving corporation or any stockholder who has so complied with Section 262 and is entitled to appraisal rights under Section 262 may file a petition in the Delaware Court of Chancery demanding a determination of the fair value of the stockholder's shares. The surviving corporation is under no obligation to and has no present intention to file a petition. Accordingly, it is the obligation of our stockholders to initiate all necessary action to perfect their appraisal rights within the time prescribed in Section 262.

Within 120 days after the effective time of the merger, any stockholder who has complied with the requirements for exercise of appraisal rights will be entitled, upon written request, to receive from the surviving corporation a statement setting forth the aggregate number of shares not voted in favor of the adoption of the merger agreement and approval of the merger and with respect to which demands for appraisal have been received and the aggregate number of holders of such shares. The statement must be mailed within ten days after a written request therefor has been received by the surviving corporation or within ten days after the expiration of the period for delivery of demands for appraisal, whichever is later.

If a petition for an appraisal is timely filed and a copy thereof is served upon the surviving corporation, the surviving corporation will then be obligated within 20 days to file with the Delaware Register in Chancery a duly verified list containing the names and addresses of all stockholders who have demanded an appraisal of their shares and with whom agreements as to the value of their shares have not been reached. After notice to the stockholders as required by the Court, the Delaware Court of Chancery is empowered to conduct a hearing on the petition to determine those stockholders who have complied with Section 262 and who have become entitled to appraisal rights thereunder. The Delaware Court of Chancery may require the stockholders who demanded payment for their shares to submit their stock certificates to the Register in Chancery for notation thereon of the pendency of the appraisal proceeding; and if any stockholder fails to comply with the direction, the Court of Chancery may dismiss the proceedings as to the stockholder.

After determining the stockholders entitled to appraisal, the Delaware Court of Chancery will appraise the fair value of their shares, exclusive of any element of value arising from the accomplishment or expectation of the merger, together with a fair rate of interest, if any, to be paid upon the amount determined to be the fair value. Stockholders considering seeking appraisal should be aware that the fair value of their shares as so determined could be more than, the same as or less than the consideration they would receive pursuant to the merger if they did not seek appraisal of their shares and that an investment banking opinion as to fairness from a financial point of view is not necessarily an opinion as to fair value under Section 262. We do not anticipate offering more than \$1.80 per share to any stockholder exercising appraisal rights and we reserve the right to assert, in any appraisal proceeding, that for purposes of Section 262, the fair value of a share of our common stock is less than \$1.80. The Delaware Supreme Court has stated that proof of value by any techniques or methods which are generally considered acceptable in the financial community and otherwise admissible in court should be considered in the appraisal proceedings. In addition, Delaware courts have decided that the statutory appraisal remedy, depending on factual circumstances, may or may not be a dissenter's exclusive remedy. The Delaware Court of Chancery will also determine the amount of interest, if any, to be paid upon the amounts to be received by persons whose shares of our common stock have been appraised. The costs of the action may be determined by the Court and taxed upon the parties as the Court deems equitable. The

Court may also order that all or a portion of the expenses incurred by any stockholder in connection with an appraisal, including, without limitation, reasonable attorneys' fees and the fees and expenses of experts utilized in the appraisal proceeding, be charged pro rata against the value of all the shares entitled to be appraised.

Any stockholder who has duly demanded an appraisal in compliance with Section 262 will not, after the effective time of the merger, be entitled to vote the shares subject to the demand for any purpose or be entitled to the

## **Table of Contents**

payment of dividends or other distributions on those shares (except dividends or other distributions payable to holders of record of our common stock as of a record date prior to the effective time of the merger).

If any stockholder who demands appraisal under Section 262 fails to perfect, or effectively withdraws or loses, such holder's right to appraisal, the stockholder's shares will be deemed to have been converted at the effective time of the merger into the right to receive \$1.80 in cash per share. A stockholder will fail to perfect, or effectively lose or withdraw, the holder's right to appraisal if no petition for appraisal is filed within 120 days after the effective time of the merger, or if the stockholder delivers to the surviving corporation a written withdrawal of the holder's demand for appraisal and an acceptance of the merger, except that any attempt to withdraw made more than 60 days after the effective time of the merger will require the written approval of the surviving corporation and, once a petition for appraisal is filed, the appraisal proceeding may not be dismissed as to any holder absent court approval.

**Stockholders are urged to read Section 262, which is included in this proxy statement as Annex C, carefully and in its entirety. Failure to follow the steps required by Section 262 for perfecting appraisal rights may result in the loss of such rights.**

## **Structure of the Merger**

The merger agreement provides that, upon the terms and subject to the conditions of the merger agreement, Merger Sub will be merged with and into us and the separate corporate existence of Merger Sub will thereupon cease, and we will be the surviving corporation of the merger and will be a wholly owned subsidiary of Motorola. At the effective time of the merger (as defined below), all of our property, rights, privileges, powers and franchises and those of the Merger Sub will vest in the surviving corporation, and all of our debts, obligations, claims, liabilities and duties and those of the Merger Sub will become the debts, obligations, claims, liabilities and duties of the surviving corporation. We will continue as the surviving corporation and will be unaffected by the merger, except that all of our then outstanding common stock will be owned by Motorola.

## **Effective Time of the Merger**

The merger will become effective when a certificate of merger is duly filed with the Secretary of State of the State of Delaware or at such later time as the parties agree to and specify in the certificate of merger, which we refer to as the effective time of the merger. Such filing will be made no later than the second business day after the satisfaction or waiver of the conditions to the completion of the merger described in the merger agreement, unless otherwise agreed by Motorola and us. See *The Merger Agreement - Conditions to the Completion of the Merger*.

The merger agreement also provides that:

our restated certificate of incorporation will be amended and restated in its entirety to be in the form of Exhibit A to the merger agreement and, as so amended, will be the restated certificate of incorporation of the surviving corporation until later amended;

after the effective time of the merger, the authorized capital stock of the surviving corporation will consist of 1,000 shares of common stock, par value \$0.01 per share;

our bylaws will be amended and restated in their entirety to be in the form of the bylaws of Merger Sub at the effective time of the merger until later amended;

the directors of Merger Sub immediately prior to the effective time of the merger will be the directors of the surviving corporation; and

the officers of Merger Sub immediately prior to the effective time of the merger will be the officers of the surviving corporation.

**Table of Contents**

**Merger Consideration**

Each share of our common stock issued and outstanding immediately before the effective time of the merger, other than:

treasury shares or shares held by Motorola or Merger Sub or any direct or indirect subsidiary of Motorola, all of which will be cancelled in the merger, and

shares held by stockholders who comply with all of the provisions of the General Corporation Law of the State of Delaware concerning the right to require appraisal of their shares, whom we refer to as dissenting stockholders,

will be automatically converted into and represent the right to receive \$1.80 in cash, without interest. After the merger is effective, stockholders will no longer have any rights with respect to their shares, except for the right to receive the \$1.80 per share merger consideration. No interest will accrue or be paid with respect to the merger consideration. At the effective time of the merger, shares of our common stock will no longer be outstanding, will automatically be cancelled and will cease to exist. Stockholders will not receive the merger consideration until they surrender their stock certificates to the paying agent for exchange (as described below).

After the merger is effective, each dissenting stockholder will also no longer have any rights as a stockholder, except for the right to receive payment of the judicially-determined fair value of his or her shares pursuant to Delaware law if the stockholder has validly perfected and not withdrawn or lost such right.

**YOU SHOULD NOT RETURN STOCK CERTIFICATES WITH THE ENCLOSED PROXY.**

**Treatment of Our Stock Options**

If we complete the merger, at the effective time of the merger, each outstanding stock option to purchase our common stock, whether vested or unvested, will be cancelled, and holders of in-the-money options will be entitled to receive a cash payment for each option equal to the product of (a) the excess of \$1.80 over the exercise price per share of such option, multiplied by (b) the total number of shares of our common stock underlying such option at the effective time of the merger. The cash payment will be reduced by applicable withholding taxes. The aggregate cash-out value of all of our options that are in-the-money is approximately \$188,000.

**Surrender of Stock Certificates**

At or prior to the effective time of the merger, Motorola will deposit or cause to be deposited, for the benefit of our stockholders, the aggregate merger consideration into an exchange fund with [ ] or another comparable institution, as paying agent.

As soon as practicable (but within five business days) after the effective time of the merger, the paying agent will mail to each holder of record of shares of our common stock a letter of transmittal and instructions for effecting the surrender of the certificates to the paying agent in exchange for the merger consideration payable in respect of the shares formerly represented by such certificates. After the paying agent has received a stockholder's certificate(s), together with a properly completed letter of transmittal, the paying agent will deliver to the stockholder the \$1.80 per share merger consideration for shares of common stock multiplied by the number of shares formerly represented by the certificate(s) surrendered by the stockholder, subject to any required withholding taxes. In the event a transfer of

ownership of our common stock is not registered in our transfer records, payment of the merger consideration will be conditioned upon:

the certificate being properly endorsed with signature guaranteed, or otherwise in proper form for transfer; and

the person requesting payment of the merger consideration paying any transfer or other taxes required as a result of the transfer or establishing to the satisfaction of Motorola that such taxes have been paid or are not applicable.

## **Table of Contents**

### **Lost Certificates**

If any certificate representing shares of our common stock is lost, stolen or destroyed, the paying agent will deliver the merger consideration for the shares if:

the stockholder asserting the claim of a lost, stolen or destroyed certificate makes an affidavit of that fact; and

if required by Motorola, the stockholder posts a bond in a reasonable amount, determined by Motorola, as indemnity against any claim that may be made against Motorola with respect to the lost certificate.

### **Unclaimed Amounts**

Any portion of the exchange fund which remains undistributed to our stockholders on the date that is 180 days after the effective time of the merger will be delivered by the paying agent to Motorola, and any of our stockholders who have not previously surrendered their stock certificates will be entitled to receive, upon delivery of such certificates to Motorola, payment of the merger consideration from Motorola. Subject to the other terms of the merger agreement, Motorola will remain liable for the payment of the merger consideration to these stockholders.

## **THE MERGER AGREEMENT**

*The following description summarizes the material provisions of the merger agreement and is qualified in its entirety by reference to the complete text of the merger agreement. The merger agreement included in this proxy statement as Annex A contains the complete terms of that agreement and stockholders should read it carefully and in its entirety.*

### **Representations and Warranties**

The merger agreement contains representations and warranties made by us to Motorola and Merger Sub, including those relating to:

due organization, existence, corporate power and standing, and other corporate matters of us and our subsidiaries;

the capital structure of us and of our subsidiaries;

the authorization, execution, delivery and enforceability of the merger agreement and the applicable stockholder voting requirements;

our receipt of a fairness opinion from Goldman Sachs;

required governmental consents, approvals, authorizations, notices and filings, the absence of conflicts under our certificate of incorporation or bylaws and the absence of breaches, violations, or defaults under any contracts, arrangements, permits or licenses as a result of the execution, delivery and performance of the merger agreement;

company material contracts, including contracts

relating to employment, service or consulting arrangements,

with major customers,

containing exclusivity rights, most favored customer pricing provisions, or penalties for late delivery, repairs, returns or quality performance,

with major or sole source suppliers,

relating to specified design, manufacturing and development arrangements, containing volume commitments, rights of first refusal or similar provisions,

limiting our rights to engage in business, make, sell or distribute products or services, or use or transfer intellectual property rights,



**Table of Contents**

relating to the disposition or acquisition of assets, provision of source code, indebtedness, settlement agreements,

outlicenses,

relating to the assignment of intellectual property,

relating to future amounts in excess of \$100,000,

with affiliates and advisors,

providing for indemnification by us,

with vendors, resellers and distributors, and

other contracts material to us and our subsidiaries;

compliance with the reporting and filing requirements of the SEC, the accuracy of information, including financial information, contained in documents filed with the SEC and the absence of liabilities other than those set forth on the Company's December 31, 2006 balance sheet and other specified liabilities;

the accuracy of the information supplied by us for inclusion in this proxy statement;

our disclosure controls and procedures and internal controls over financial reporting and compliance with provisions of the Sarbanes-Oxley Act;

the absence of material changes or events since December 31, 2006 concerning us or our subsidiaries;

pending or threatened litigation, investigations or proceedings;

indebtedness and indemnification obligations with respect to our and our subsidiaries' directors and officers;

employment and employee benefits matters, matters affecting us relating to the Employee Retirement Income Security Act of 1974, as amended, and other compliance, compensation and employment matters (including employee benefit plans, collective bargaining or other labor union agreements and excess parachute payments under Section 280G of the Internal Revenue Code of 1986, as amended);

regulatory compliance matters, compliance with applicable labor, environmental, import and export control, anti-bribery and other applicable laws, and material consent decrees;

completion and accuracy of our tax filings, payment or accrual of our tax obligations, absence of other tax liabilities and other tax matters;

insurance matters;

matters relating to our intellectual property;

our title to and interest in material tangible assets and properties, our rights to leased real property, and compliance with the terms of, and absence of disputes or defaults under, our leases and subleases;

contracts with governmental entities;

product liability and recalls;

the inapplicability of anti-takeover statutes with respect to the proposed merger;

amendment and termination of our rights plan; and

our engagement and payment of fees for financial advisors in connection with the merger.

The merger agreement also contains representations and warranties made by Motorola and Merger Sub to us, including those relating to:

due organization, existence, corporate power and standing, and other corporate matters of Motorola and Merger Sub;

**Table of Contents**

the authorization, execution, delivery of the merger agreement, the corporate power and authority to consummate the merger and enforceability of the merger agreement;

required governmental consents, approvals, authorizations, notices and filings, the absence of conflicts under governing documents, the absence of breaches, violations, or defaults under any contracts, arrangements, permits or licenses and the absence of a required vote of Motorola securityholders as a result of the execution, delivery and performance of the merger agreement;

the accuracy of the information supplied by Motorola and Merger Sub for inclusion in this proxy statement;

Merger Sub's operations;

the absence of brokers' and finders' fees for which we would be liable in connection with the merger; and

the immediate availability of Motorola funds to pay the merger consideration.

The representations and warranties of each of the parties to the merger agreement described above will expire upon completion of the merger. The representations included in the merger agreement were made by each of us and Motorola to each other. These representations and warranties were made as of specific dates, may (along with the conduct of business covenants also described) be subject to important qualifications and limitations agreed to by us and Motorola in connection with negotiating the terms of the merger agreement, and may have been included in the merger agreement for the purpose of allocating risk between us and Motorola rather than to establish matters of fact. This description of the representations and warranties, and their reproduction in the copy of the merger agreement attached to this document as Annex A, are included solely to provide investors with information regarding the terms of the merger agreement, and not to provide any other factual information regarding us or our business. Accordingly, the representations and warranties and other provisions of the merger agreement should not be read alone, but instead should be read in conjunction with the information provided elsewhere in this document and the information we file with the SEC, as described under "Where You Can Find Additional Information," below.

**Covenants**

Under the merger agreement, we have agreed that, prior to the completion of the merger (unless Motorola provides its consent in writing, which will not be unreasonably withheld or delayed), subject to specified exceptions, we and our subsidiaries will:

carry on our business in the ordinary and usual course; and

use commercially reasonable efforts to preserve our respective current business organizations and maintain our respective existing relations and goodwill with customers, suppliers, distributors, strategic partners, creditors, lessors, employees and business associates.

In addition, we have agreed that, among other things and subject to specified exceptions, neither we nor any of our subsidiaries may, without Motorola's prior written consent, which will not be unreasonably withheld or delayed, take any of the following actions:

issue, sell, pledge, dispose of or otherwise encumber any of the capital stock of our subsidiaries;

amend our certificate of incorporation or bylaws or equivalent governing instruments of our subsidiaries;

split, combine or reclassify outstanding shares of any of our capital stock;

declare, set aside or pay any dividend in respect of our capital stock (other than dividends from our direct or indirect wholly owned subsidiaries);

purchase, redeem or otherwise acquire any shares of our and our subsidiaries capital stock or securities convertible into or exchangeable or exercisable for any shares of our or our subsidiaries capital stock (other than the acquisition of shares of our common stock from our optionholders in payment of the exercise price payable by these optionholders pursuant to their exercise of options);

authorize, issue, sell, pledge, dispose of or encumber our or any of our subsidiaries capital stock, securities convertible into or exchangeable for, or rights of any kind to acquire, any shares of our or our subsidiaries

**Table of Contents**

capital stock, securities having the right to vote, or other property or assets (other than shares of our common stock and associated rights issuable pursuant to options and stock-based awards outstanding on the date of this agreement);

transfer, lease, license, guarantee, sell, mortgage, pledge, dispose of, abandon, cancel, surrender or allow to lapse or expire or encumber any material property or material assets (other than the sale of inventory in the ordinary course of business);

restructure, recapitalize, reorganize, liquidate, adopt a plan of liquidation, or otherwise enter into any agreement that imposes material changes or restrictions on the operation of our or any of our subsidiaries' assets or businesses, or adopt any resolutions for such actions;

acquire by merging or consolidating with, or by purchasing all or a substantial portion of the assets or securities of, any business or entity or any material assets, except for purchases of inventory and raw material in the ordinary course of business;

incur or guarantee any indebtedness for borrowed money, issue, sell or amend any debt securities or rights to acquire debt securities, or enter into any "keep well" or similar agreement;

other than accounts receivable in the ordinary course of business, make any loans, advances (other than routine advances to employees in the ordinary course of business), or capital contributions to, or investments in, any other person (other than us or any of our direct or indirect wholly owned subsidiaries), or enter into any hedging agreements or similar arrangements other than in the ordinary course of business;

make any capital expenditures or other expenditures with respect to property, plant or equipment in excess of \$200,000 in the aggregate for us and our subsidiaries, other than as set forth in our budget for capital expenditures;

make any material changes in accounting methods, principles or practices, or change any assumption underlying, or method calculating, any bad debt, contingency or other reserve, except as required by a change in GAAP or applicable law;

other than in the ordinary course of business consistent with past practice, enter into, renew, modify, amend, terminate, waive, delay the exercise of, release or assign any material rights or claims under, any material contract or lease;

except to comply with law or existing agreements and arrangements,

take any action with respect to, adopt, enter into, terminate or amend any employment, severance, change in control, retirement, retention, welfare, incentive or similar agreement, arrangement or benefit plan for the benefit or welfare of any current or former director, officer, employee or consultant or any collective bargaining agreement;

increase the compensation or fringe benefits of, or pay bonus to, any director, officer, employee or consultant;

amend or accelerate the payment, right to payment or vesting of compensation or benefits;

pay any benefit not provided for under any company benefit plan as of the date of the merger agreement;

grant any awards under any bonus, incentive, performance or other compensation plan or benefit plan or arrangement, including the grant of any equity awards, or the removal of existing restrictions in any benefit plans or agreements or awards made under the aforementioned plans or arrangements;

take any action to fund or in any other way secure the payment of compensation or benefits under any company benefit plan;

initiate, settle or compromise any intellectual property litigation or material litigation, claim, grievance, charge or proceeding;

**Table of Contents**

make or rescind any material tax election, amend any material tax return or permit any insurance policy naming us as a beneficiary to be cancelled or terminated, except in a manner consistent with past practice or as required by law; or

authorize, commit, resolve or agree to do any action described above.

In addition, we have agreed that we and our subsidiaries will timely file all material tax returns required to be filed by us and such subsidiaries, as the case may be, and timely pay or accrue all material taxes due and payable by us and such subsidiaries, except with respect to matters contested in good faith.

We and Motorola have agreed to notify each other promptly after learning of the following:

the occurrence of various claims, communications or investigations relating to the merger or initiated by or against the notifying party or threatened against the notifying party, or its officers, directors, employees or stockholders;

changes or events that are reasonably likely to cause the conditions to completion of the merger not to be satisfied;

any claim or written inquiry by a taxing authority regarding a material deficiency to pay taxes payable by us;

matters relating to our disclosure controls and procedures, internal controls and other corporate governance representations; and

offers received by us to settle or compromise claims or proceedings.

We and Motorola have agreed to use commercially reasonable efforts to notify each other promptly of matters that relate to the accuracy of our representations and warranties or compliance with our covenants and agreements.

In addition, prior to the completion of the merger, we have agreed to provide Motorola with reasonable access to our properties, books, contracts and records, and such information concerning our business, properties and personnel as may reasonably be required by Motorola and that we are legally able to provide.

**Directors and Officers Indemnification, Advancement of Expenses, Exculpation and Insurance**

Motorola has agreed to cause the surviving corporation to indemnify and hold harmless, through the sixth anniversary of the merger, to the fullest extent permitted under Delaware law, each current and former director or officer of us or our subsidiaries, against all claims, losses, liabilities, damages, judgments, fines and reasonable fees, costs and expenses, arising out of or incurred by any of them in connection with any claim, action, suit, proceeding, demand or investigation arising out of or pertaining to their service as an officer or director of us or any of our subsidiaries. Each director or officer will be entitled to advancement of expenses incurred in the defense of any such claim, action, suit, proceeding or investigation from the surviving corporation, provided that the third party to whom expenses are advanced provides an undertaking to repay such advances if it is ultimately determined that such third party is not entitled to indemnification.

Motorola has also agreed to cause the surviving corporation to purchase tail coverage under our current officers and directors liability insurance for a period of six years after the completion of the merger in respect of matters existing or occurring at or prior to the merger. In the event that the premium for tail coverage for a period of six years exceeds

a specified maximum amount, Motorola will cause the surviving corporation to obtain the longest tail coverage that can be obtained for a premium not in excess of that specified amount.

**Options and Employee Stock Purchase Plans; Employee Benefits Matters**

All options to purchase shares of our common stock granted under our 1995 Stock Option Plan, 1997 Equity Incentive Plan, 1998 Non-Employee Director's Stock Option Plan, and 1999 Non-Officer Equity Incentive Plan, as well as options granted outside of any plan, including any unvested portion of such options, will be cashed out in the merger. For these purposes, cashed out in the merger means that the option, whether vested or unvested, will be cancelled in the merger in exchange for a cash payment equal to the product of (i) the excess, if any, of \$1.80 over the applicable per share option exercise price and (ii) the number of shares of our common stock subject to the



**Table of Contents**

option at such time, without interest and less any applicable withholding taxes. The aggregate cash-out value of all of our options that are in-the-money is approximately \$188,000.

Immediately prior to the completion of the merger, we have agreed to terminate our 1998 Employee Stock Purchase Plan and our 1998 Employee Stock Purchase Plan for Foreign Employees (collectively, our ESP Plans). Our ESP Plans are currently suspended and no offering is currently outstanding under our ESP Plans.

Under the merger agreement, we have agreed that, if requested by Motorola in writing, we will terminate any or all existing employee benefit programs effective immediately prior to the completion of the merger, except for certain specified arrangements.

**Efforts to Complete the Merger**

Upon the terms and subject to the conditions set forth in the merger agreement, each party has agreed to use its commercially reasonable efforts to take all actions and do all things necessary, proper or advisable, to complete the merger as promptly as practicable, including using commercially reasonable efforts to accomplish the following:

as promptly as practicable, to obtain any consents, licenses, permits, waivers, approvals, authorizations or orders that are either required or reasonably requested by Motorola in connection with the merger agreement and the merger;

as promptly as practicable, and on a mutually agreed date, make all necessary filings, and thereafter make any other required submissions, with respect to the merger agreement and the merger required under applicable law;

execute and deliver any additional instruments necessary to complete the merger and to carry out fully the purposes of the merger agreement; and

to obtain any government clearances or approvals required to complete the merger under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended, and other applicable antitrust laws, and contest and resist any action, and have any decree or order vacated or overturned, that restricts or prohibits the merger; however, the foregoing shall not require Motorola or any of its affiliates to transfer, encumber or hold separate any assets or businesses or agree to any restriction on Motorola's ability to own or operate any assets or businesses or exercise ownership rights with respect to the stock of the surviving corporation, or to take any other action if a governmental entity seeks a preliminary injunction or restraining order to enjoin the merger.

We and Motorola have agreed to consult and cooperate with each other in connection with obtaining all required consents, licenses, permits, waivers, approvals, authorizations or orders and to use commercially reasonable efforts to furnish one another with all information required for any application or filing made pursuant to any applicable law.

We have agreed to cooperate with Motorola to help Motorola assess the desirability of obtaining additional insurance coverage relating to specified litigation matters. In addition, if requested by Motorola at least 10 business days before completion of the merger, we have agreed to use our reasonable best efforts to apply for and to purchase, immediately prior to or concurrent with the merger, a litigation insurance policy with respect to these litigation matters, naming us and our subsidiaries as the named insureds and Motorola and its affiliates as additional insureds. In the event that Motorola unilaterally terminates the merger agreement in accordance with its terms, Motorola has agreed to reimburse us for the premium paid by us for the policy.

We have also agreed to provide to Motorola our tax apportionment schedule for 2005 and similar available apportionment information for other years as reasonably requested by Motorola, which will include jurisdictions in which we had sales, owned property, employed individuals or filed income tax returns for such relevant year. Our Chief Financial Officer must deliver a certificate to Motorola certifying that, to the best of his knowledge, the apportionment information delivered to Motorola for 2002 and each taxable year thereafter is true, correct and complete, and the apportionment information delivered to Motorola for all other years is true, correct and, to the extent available, complete. We must supplement the apportionment information if we become unable to deliver the certificate referenced below. We have also agreed to cooperate with Motorola as necessary to assist Motorola in

**Table of Contents**

reviewing the apportionment information. Motorola may notify us in writing within 20 days after receipt of the certificate, or five days after receipt of the supplemental information, if Motorola reasonably believes that we have been delinquent in filing any income tax return not disclosed to Motorola. To the extent that a tax return identified by Motorola is considered delinquent under the merger agreement, we are required to file that tax return unless we and Motorola agree that it does not need to be filed. If Motorola provides us with such a notice within 30 days of the outside termination date, September 21, 2007, and the delinquent tax return is the only condition to closing that is not satisfied as of the outside termination date, then the outside termination date of the merger agreement will be extended to the 30<sup>th</sup> day after we receive the notice from Motorola. At least five days before the merger, our Chief Financial Officer must deliver an additional certificate to Motorola certifying that the apportionment information previously provided to Motorola (as supplemented) remains, to the best of his knowledge, true, correct and complete, and that we have filed all U.S. federal income tax returns and all other delinquent income tax returns.

**Conditions to the Completion of the Merger**

The obligations of each of Motorola and Merger Sub, on the one hand, and us, on the other hand, to complete the merger depend on the satisfaction or waiver, on or prior to the effective time of the merger, of a number of conditions:

the merger agreement has been adopted and the merger approved by the affirmative vote of stockholders holding a majority of the shares of our common stock outstanding at the close of business on the record date for the special meeting;

expiration or termination of the applicable waiting period under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended, and the making of filings, receipt of approvals, and expiration or termination of applicable waiting periods under any other applicable antitrust laws;

no order, stay, decree, judgment or injunction or statute, rule or regulation by any governmental entity prohibits or makes illegal the completion of the merger or the other transactions contemplated by the merger agreement;

each of the obligations of the other party required to be performed on or prior to the closing date of the merger have been performed in all material respects; and

the representations and warranties of the other party set forth in the merger agreement being true and correct without regard to materiality and material adverse effect qualifiers, as of the date of the merger agreement and as of the completion date (except when made as of an earlier date, in which case as of that date), except to the extent that the aggregate of all inaccuracies with respect to such representations and warranties would not have a material adverse effect on such party, and solely with respect to us, except for capitalization, corporate authority and takeover statute representations, which must be true and accurate in all material respects.

The obligations of each of Motorola and Merger Sub to complete the merger depend on the satisfaction or waiver of, on or prior to the effective time of the merger, a number of additional conditions, including:

no action, investigation, proceeding or litigation has been instituted, commenced, pending or threatened:

or related order enacted or entered in which a governmental entity challenges or seeks to restrain or prohibit the completion of the merger or to prohibit or impair Motorola's ability to own or operate any of our businesses and assets after the merger or any of the businesses or assets of Motorola or its subsidiaries, including through any divestiture, licensing, lease or hold separate arrangement, or to limit Motorola's ability to exercise ownership rights with respect to the stock of the surviving corporation, or

which may reasonably be expected to result in the imposition of (1) criminal sanctions on us or our subsidiaries, or (2) material penalties or fines to a governmental entity, or restitution to a third party, in each case as a result of any conviction of us or our subsidiaries of a crime, or settlement with a governmental entity for the purpose of closing an investigation, being imposed on Motorola or the surviving corporation or any of their respective affiliates;

**Table of Contents**

all authorizations, consents, orders or approvals of, or declarations, notices or filings with, or expirations of waiting periods imposed by, any governmental entity in connection with the merger having been made or obtained, except those that the failure to make or obtain could not have a material adverse effect on Motorola or a material adverse effect (as defined below) on us or provide a reasonable basis to conclude that the parties to the merger agreement or any of their affiliates would be subject to risk of criminal sanctions or any of their representatives would be subject to the risk of criminal or material civil sanctions;

the continued enforceability of specified contracts of ours;

since the date of the merger agreement, no occurrence of any change, event, circumstance or development that has had, or could reasonably be expected to have, a material adverse effect (as defined below) on us;

neither our principal executive officer nor our principal financial officer has failed to provide the necessary certifications required under Section 302 and Section 906 of the Sarbanes-Oxley Act on any of our reports filed with the SEC since the date of the merger agreement;

we have filed all registration statements, forms, reports and other documents required to be filed by us with the SEC on or prior to the closing date, and all required amendments, and the amendments shall not contain any information that is materially and adversely different from the information in the documents amended by such amendments;

since the date of the merger agreement, no action has been instituted or threatened challenging the validity and ownership of our intellectual property, other than actions the outcomes of which is not reasonably expected to result in a material adverse effect (as defined below) on us;

the SEC shall not have recommended any charges or enforcement action against us or our officers or directors, authorized such recommendation or issued a Wells Notice to us or our officers or directors, in connection with the SEC investigation relating to certain accounting matters that was commenced in December 2005 and recently discontinued, and there shall not be any pending governmental action, suit, proceeding or investigation against any of our or our subsidiaries directors, officers or certain key employees relating to the SEC investigation;

we must have at least \$15 million of cash and cash equivalents (\$13 million if the merger is completed after July 31, 2007, and, in either case, reduced by the amount of all reasonable merger-related expenses (including payments required on or prior to, or as a result of, completion of the merger) paid after April 21, 2007), net of indebtedness;

three-quarters of a small group of key employees, each of whom entered into a retention agreement with Motorola on April 21, 2007, and 80% of a larger group of employees, still being employed by us and performing their usual and customary duties immediately prior to completion of the merger; and

we must have filed specified tax returns and other tax returns, if any, that are identified as being delinquent prior to completion of the merger.

The merger agreement provides that a material adverse effect on us means any change or effect on us that is reasonably likely to prevent us from completing the merger and other transactions contemplated by the merger agreement, or any material adverse change in, or materially adverse effect on, either individually or in the aggregate with all such other adverse changes in or effects on, the condition (financial or otherwise), results of operations,

operations, business, assets (including intangible assets) or liabilities of us and our subsidiaries taken as a whole.

In determining whether a material adverse effect has occurred, none of the following, in and of themselves, will constitute a material adverse effect on us:

changes or effects that are primarily the result of general economic or business conditions, or conditions in financial or securities markets, in the United States;

changes or effects that are primarily the result of factors generally affecting the industries or markets in which we operate;

**Table of Contents**

changes or effects that result from the public announcement or pendency of the merger on our employees or the public announcement by Motorola with respect to our or our subsidiaries' businesses;

changes resulting from or arising out of actions taken pursuant to (and/or required by) the merger agreement or at the request of Motorola, or the failure to take any actions due to restrictions set forth in the merger agreement (provided that only if we (i) reasonably believe that taking any action required by the merger agreement or at the request of Motorola, or failing to take action prohibited by the agreement, could reasonably be expected to result in a material adverse effect on us, and (ii) provide timely prior written notification to Motorola of such belief and Motorola does not provide timely relief from the provisions of the merger agreement or its request, will the changes or effects resulting from such action or inaction be deemed not to constitute a material adverse