FINISAR CORP
Form 424B3
August 15, 2005

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Filed Pursuant to Rule 424(b)(3)
Registration No. 333-124879

19,496,177 Shares
FINISAR CORPORATION
Common Stock

This prospectus relates to the public offering of a maximum of 19,496,177 shares of common stock of Finisar Corporation registered for sale under this prospectus that will be owned by Data Transit Corp., a Delaware corporation, upon their issuance. Data Transit Corp. is the holder of a $16,270,000 8% convertible installment note, which was issued to it in connection with our acquisition of substantially all of its assets. The terms of the convertible installment note provide for automatic conversion of the outstanding principal and interest into shares of our common stock. Since the number of shares to be issued to Data Transit Corp. is based upon the market price of our common stock at the time of conversion, we are unable to determine the exact number of shares that may be issued pursuant to the convertible installment note. As of July 29, 2005, the outstanding principal amount of the convertible installment note was $12,044,771.45.

The shares of our common stock may be offered from time to time by the selling stockholder. All of the expenses of registration incurred in connection with this offering are being borne by us, but all selling and other expenses incurred by the selling stockholder will be borne by the selling stockholder. The common stock offered in this prospectus may be offered and sold by the selling stockholder directly or through broker-dealers acting as agents or principals. The distribution of the common stock may be effected in one or more of the following types of transactions:

- transactions on any national securities exchange or quotation service on which the common stock may be listed or quoted at the time of the sale, including the Nasdaq National Market;
- transactions in the over-the-counter market; or
- transactions otherwise than on such exchanges or services or in the over-the-counter market.

We will receive no part of the proceeds of the sale of the shares offered in this prospectus.

Our common stock is traded on the Nasdaq National Market under the symbol FNSR. On August 11, 2005, the last reported sales price for the common stock was $1.03 per share.

INVESTING IN THE COMMON STOCK OFFERED IN THIS PROSPECTUS INVOLVES A HIGH DEGREE OF RISK. SEE RISK FACTORS BEGINNING ON PAGE 4.

The selling stockholder and any brokers executing selling orders on behalf of the selling stockholder may be deemed to be underwriters within the meaning of the Securities Act of 1933. Commissions received by a broker executing selling orders may be deemed to be underwriting commissions under the Securities Act.

NEITHER THE SECURITIES AND EXCHANGE COMMISSION NOR ANY STATE SECURITIES COMMISSION HAS APPROVED OR DISAPPROVED OF THESE SECURITIES OR PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

The date of this Prospectus is August 12, 2005.

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You should rely only on the information contained or incorporated by reference in this prospectus. We have not authorized anyone to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. The selling stockholder is not making an offer to sell these securities in any jurisdiction where the offer or sale is not permitted. You should assume that the information appearing in this prospectus is accurate only as of the date on the front cover of this prospectus. Our business, financial condition, results of operations and prospects may have changed since that date.

Finisar is a registered trademark of Finisar Corporation. This prospectus contains product names, trade names and trademarks of Finisar and other organizations.

The terms Finisar, we, us, our, and the company, as used in this prospectus, refer to Finisar Corporation and consolidated subsidiaries.

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DISCLOSURE REGARDING FORWARD-LOOKING STATEMENTS

Some of the statements in this prospectus and in the documents incorporated by reference constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. We use words like anticipates, believes, plans, expects, future, intends and similar expressions to identify these forward-loo statements. We have based these forward-looking statements on our current expectations and projections about future events; however, our business and operations are subject to a variety of risks and uncertainties, including those listed under Risk Factors and elsewhere in this prospectus, and, consequently, actual results may materially differ from those projected by any forward-looking statements. You should not place undue reliance on these forward-looking statements. Factors that could cause actual results to differ from those projected include, but are not limited to, the following:

- uncertainty regarding our future operating results;
- our ability to introduce new products in a cost-effective manner that are accepted in the marketplace;
- delays or loss of sales due to long product qualification cycles for our products;
- the possibility of lower prices, reduced gross margins and loss of market share due to increased competition;
- increased demands on our resources due to the integration of several companies and product lines that we have acquired or may acquire;
- cost reductions related to our current or future operations which may further reduce our available resources and negatively impact our competitive market position; and
- the sufficiency of cash flow to meet our debt service obligations and the potential dilution that would result from the conversion of our outstanding subordinated convertible notes.

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SUMMARY

This summary highlights selected information contained elsewhere in this prospectus. You should read the entire prospectus and the documents incorporated by reference in this prospectus carefully before making an investment decision.

Finisar Corporation

We are a leading provider of optical subsystems and components and network performance test and monitoring systems. These products enable high-speed data communications over local area networks, or LANs, storage area networks, or SANs, and metropolitan area networks, or MANs. Optical subsystems consist primarily of transceivers sold to manufacturers of storage and networking equipment for SAN, LAN and MAN applications. Optical subsystems also include multiplexers, demultiplexers and optical add/drop modules used in MAN applications. We are focused on the application of digital fiber optics to provide a broad line of high-performance, reliable, value-added optical subsystems for data networking and storage equipment manufacturers. Our line of optical subsystems supports a wide range of network protocols, transmission speeds, distances, physical mediums and configurations. Our line of optical components consists primarily of packaged lasers and photodetectors used in transceivers, primarily for LAN and SAN applications. We also provide network performance test and monitoring systems to original equipment manufacturers for testing and validating equipment designs and to operators of networking and storage data centers for testing, monitoring and troubleshooting the performance of their installed systems. We sell our products primarily to leading storage and networking equipment manufacturers such as Brocade, Cisco Systems, EMC, Emulex, Hewlett-Packard Company and Qlogic.

We were incorporated in California in April 1987 and reincorporated in Delaware in November 1999. Our principal executive offices are located at 1308 Moffett Park Drive, Sunnyvale, California 94089, and our telephone number is (408) 548-1000 and our website is located at www.finisar.com. Information on our website is not a part of this prospectus.

Recent Developments

During our fiscal year ended April 30, 2005, we acquired one company and certain assets and businesses of two other companies. In the first quarter of fiscal 2006, we completed the acquisition of another company. These acquisitions have enabled us to broaden our product offerings, add new sources of revenues and obtain advanced technologies.

Acquisition of Assets of Data Transit Corp.

On August 6, 2004, we completed the purchase of substantially all the assets of Data Transit Corp. in exchange for a cash payment of $500,000 and the issuance of a convertible installment note in the original principal amount of approximately $16.3 million, convertible into shares of our common stock. The acquired business, previously based in San Jose, California, manufactures protocol analyzers and traffic generators and is now operated as a part of our Network Tools Division at our facility in Sunnyvale, California.

Acquisition of Transceiver and Transponder Product Line from Infineon Technologies AG

On April 29, 2004, we entered into an agreement with Infineon Technologies AG to acquire Infineon s fiber optics business unit. On October 11, 2004, we entered into an amended purchase agreement under which the terms of the original acquisition agreement were modified. On January 25, 2005, we and Infineon terminated the amended purchase agreement and entered into a new agreement under which we acquired certain assets of Infineon s fiber optics business unit associated with the design, development and manufacture of optical transceiver and transponder products in exchange for 34 million shares of our common stock. The closing of the acquisition took place on January 31, 2005, the first day of our fourth quarter of fiscal 2005. The transaction involved the acquisition of product lines, equipment and intellectual property related to Infineon s optical transceiver and transponder products.

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Acquisition of I-TECH CORP.

On April 8, 2005, we completed the acquisition of I-TECH CORP., a privately-held network test and monitoring company based in Eden Prairie, Minnesota in exchange for promissory notes in the aggregate principal amount of approximately $12.1 million, convertible into shares of our common stock. The acquired business is being consolidated with the other operations of our Network Tools Division located in Sunnyvale, California.

Acquisition of InterSAN, Inc.

On May 12, 2005, we completed the acquisition of InterSAN, Inc., a privately-held company located in Scotts Valley, California in exchange for approximately 7.1 million shares of our common stock. InterSAN provides network testing and monitoring software and is now operated as a part of our Network Tools Division located in Sunnyvale, California.

The Offering

All of the shares of common stock registered for sale under this prospectus will be owned by Data Transit Corp., a Delaware corporation, upon their issuance. Data Transit Corp. is the holder of a $16,270,000 8% convertible installment note, which was issued to it in connection with our acquisition of substantially all of its assets in August 2004. The terms of the convertible installment note provide for automatic conversion of the outstanding principal and interest. Since the number of shares to be issued to Data Transit Corp. is based upon the market price of our common stock at the time of conversion, we are unable to determine the exact number of shares that may be issued pursuant to the convertible installment note.

Pursuant to the terms of the acquisition, we agreed to register for resale the shares of common stock issuable upon conversion of the convertible installment note. This prospectus covers the resale by Data Transit Corp. of the shares of common stock that it will receive upon conversion of the convertible installment note. Except in very limited circumstances, at no time will Data Transit Corp. own more than 4.99% of our outstanding shares of common stock.

Common stock offered by selling stockholder	19,496,177 shares(1).
Common stock outstanding	277,048,404 shares outstanding as of June 30, 2005(2).
Use of proceeds	We will not receive any of the proceeds from the sale of shares by the selling stockholder.
Nasdaq National Market symbol	FNSR

(1) Estimated by multiplying the original principal amount of the convertible installment note plus an estimated amount of interest by 120% (to take into account possible share fluctuations) and dividing by the estimated conversion price of $1.085 (the average of the high and low sales prices of our common stock on June 13, 2005, the day prior to the effective date of the original registration statement which is amended by the registration statement of which this prospectus is a part). At July 29, 2005, the outstanding principal amount of the convertible installment note was $12,044,771.45.

(2) The number of shares that will be outstanding after the offering is based on the number of shares outstanding as of June 30, 2005, and excludes (i) shares of common stock reserved for issuance under our stock option plans and employee stock purchase plan and upon exercise of stock options and warrants assumed in connection with our acquisitions of six privately-held companies; (ii) the shares of common stock issuable upon conversion of the principal amount of $13,964,549.26 outstanding as of June 30, 2005 under the convertible installment note issued as consideration for our acquisition of the assets of Data Transit Corp. in August 2004; (iii) a portion of the shares of common stock issued in connection with the acquisition of InterSAN, Inc. in May 2005; (iv) the shares of common stock issuable upon conversion of the principal amount of $4,776,545.56 outstanding as of June 30, 2005 under the promissory notes issued as consideration for our acquisition of I-TECH CORP in April 2005; and (v) the shares of common stock issuable upon conversion of the principal amount of $937,500 outstanding as of June 30, 2005 under a promissory note issued to CyOptics Inc. in April 2005.

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Summary Financial Data
(In thousands, except per share data)

The following summary financial data should be read together with Management s Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and the notes thereto included elsewhere in this prospectus. The statement of operations data set forth below for the fiscal years ended April 30, 2005, 2004 and 2003 and the balance sheet data as of April 30, 2005 and 2004 are derived from, and are qualified by reference to, our audited consolidated financial statements included elsewhere in this prospectus. The statement of operations data set forth below for the fiscal years ended April 30, 2002 and 2001 and the balance sheet data as of April 30, 2003, 2002 and 2001 are derived from audited financial statements not included in this prospectus. The Management s Discussion and Analysis of Financial Condition and Results of Operations related to the statement of operations and balance sheet data for the fiscal years ended April 30, 2002 and 2001 are not included in this prospectus.

	Fiscal Years Ended April 30,				
	2005	**2004**	**2003**	**2002**	**2001**
Statement of Operations Data:					
Revenues	$ 280,823	$ 185,618	$ 166,482	$ 147,265	$ 188,800
Gross profit (loss)	49,268	22,794	13,998	(16,480)	46,349
Loss from operations	(88,597)	(83,451)	(100,931)	(258,596)	(117,192)
Net loss	$ (114,107)	$ (113,833)	$ (619,753)	$ (218,738)	$ (85,449)
Net loss per share basic and diluted:	$ (0.49)	$ (0.53)	$ (3.17)	$ (1.21)	$ (0.53)
Shares used in per share calculations:					
Basic and diluted	232,210	216,117	195,666	181,136	160,014

	As of April 30,				
	2005	**2004**	**2003**	**2002**	**2001**
Balance Sheet Data:					
Cash, cash equivalents and short-term investments	$ 102,362	$ 143,398	$ 119,438	$ 144,097	$ 146,111
Working capital	120,272	172,892	149,967	222,603	249,000
Total assets	488,985	494,705	423,606	1,041,281	1,029,995
Long-term liabilities	265,274	233,732	101,531	106,869	45,354
Convertible preferred stock					1
Total stockholders equity	144,290	202,845	274,980	879,002	941,851

Net income in fiscal 2003 reflects our adoption of Statements of Financial Accounting Standards 141 and 142 on May 1, 2002. As a result of our adoption, reported net loss decreased by approximately $127.8 million, or $0.65 per share, due to the cessation of the amortization of goodwill and the amortization of acquired workforce and customer base.

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RISK FACTORS

An investment in the securities offered by this prospectus involves a high degree of risk. You should carefully consider the following factors and other information in this prospectus and in the documents incorporated by reference in this prospectus before deciding to purchase shares of our common stock. If any of these risks occur, our business could be harmed, the trading price of our stock could decline and you may lose all or part of your investment.

We are subject to a number of special risks as a result of our recent acquisition of the fiber optics transceiver business of Infineon Technologies AG

On January 25, 2005, we entered into an agreement with Infineon Technologies AG to acquire certain assets associated with the design, development and manufacture of the optical transceiver and transponder products of Infineon s fiber optics business unit in exchange for 34,000,000 shares of Finisar common stock. The acquisition closed on January 31, 2005. Our future results of operation will be substantially influenced by the operations of the new business, and we are subject to a number of risks and uncertainties related to the acquisition, including the following:

The integration of the former Infineon transceiver and transponder products and technology with our products and technology and the transition of the manufacturing operations for such products to our facilities will be complex, time-consuming and expensive. The execution of these activities could potentially disrupt our ongoing business operations and distract management from day-to-day operational matters, as well as other strategic opportunities, and could strain our financial and managerial controls and reporting systems and procedures. In addition, unanticipated costs could arise during the integration of the products and technology and the transition of manufacturing operations to our facilities. If we are unable to successfully integrate the former Infineon products and technology with our products and technology, or if actual integration and transition costs are significantly greater than currently anticipated, we may not achieve the anticipated benefits of the acquisition and our revenues and operating results could be adversely affected.

We will be dependent on Infineon to supply us with finished goods for a transition period of up to one year while we transfer manufacturing operations to our facilities. Infineon s failure to supply us with high quality products in a timely manner could adversely affect our operating results and our ability to retain the former customers of Infineon. In addition, we expect to realize lower gross profit margins on the sale of products supplied by Infineon than on the sale of products we manufacture until such time as those products are manufactured by us.

We plan to transition the manufacture of the former Infineon transceiver and transponder products from Infineon s production facilities to our facilities over a period of time. Some of the former Infineon customers may be unwilling to purchase products manufactured at our facilities without subjecting the products to new qualification testing procedures, and some customers may be unwilling to undertake these procedures and may elect to buy products from other suppliers. Delays in or losses of sales due to these requalification issues could result in lower revenues which could adversely affect our future operating results.

Some of the existing customers for the Infineon products may decide for other reasons to purchase similar products from other competitors. The loss of one or more significant customers of the former Infineon business could result in lower revenues which would adversely affect our future operating results.

Immediately prior to the acquisition, Infineon was engaged in a number of ongoing research and development projects related to its transceiver products and related technologies. We may not be able to successfully complete some or all of these projects, and our inability to do so could prevent us from achieving some of the strategic objectives and other anticipated potential benefits of the acquisition, and could have a material adverse effect on our revenues and operating results.

We may incur charges to operations in amounts that are not currently estimable to reflect costs associated with integrating the acquired business with our company. These costs could adversely affect our future operating results.

At the closing of the acquisition, we issued 34 million shares of our common stock to Infineon, which represented approximately 13% of the outstanding capital stock of Finisar at that time. The issuance of these shares caused a significant reduction in the relative percentage interest of current Finisar stockholders. In April 2005, Infineon sold the 34 million shares to certain funds managed by VantagePoint Venture Partners in a private transaction.

As a result of the acquisition, Finisar has become a substantiality larger organization, and if our management is unable to effectively manage the combined business, our operating results will suffer.

Past and future acquisitions could be difficult to integrate, disrupt our business, dilute stockholder value and harm our operating results

Since October 2000, we have completed the acquisition of eight privately-held companies, including our recent acquisitions of I-TECH CORP. in April 2005 and InterSAN, Inc. in May 2005, and certain businesses and assets from five other companies, including our recently completed acquisitions of certain assets related to the transceiver and transponder business of the fiber optics business unit of Infineon. We continue to review opportunities to acquire other businesses, product lines or technologies that would complement our current products, expand the breadth of our markets or enhance our technical capabilities, or that may otherwise offer growth opportunities, and we from time to time make proposals and offers, and take other steps, to acquire businesses, products and technologies. Several of our past acquisitions have been material, and acquisitions that we may complete in the future may be material. In 10 of our 13 acquisitions, we issued stock as all or a portion of the consideration. We will issue additional shares upon conversion of the promissory notes issued as consideration for the acquisitions of Data Transit and I-TECH. The issuance of stock in these and any future transactions has or would dilute stockholders percentage ownership.

Other risks associated with acquiring the operations of other companies include:

problems assimilating the purchased operations, technologies or products;

unanticipated costs associated with the acquisition;

diversion of management s attention from our core business;

adverse effects on existing business relationships with suppliers and customers;

risks associated with entering markets in which we have no or limited prior experience; and

potential loss of key employees of purchased organizations.

Several of our past acquisitions have not been successful. During fiscal 2003, we sold some of the assets acquired in two prior acquisitions, discontinued a product line and closed one of our acquired facilities. As a result of these activities, we have incurred significant restructuring charges and charges for the write-down of assets associated with those acquisitions. We cannot assure you that we will be successful in overcoming future problems encountered in connection with our past or future acquisitions, and our inability to do so could significantly harm our business. In addition, to the extent that the economic benefits associated with any of our acquisitions diminish in the future, we may be required to record additional write downs of goodwill, intangible assets or other assets associated with such acquisitions, which would adversely affect our operating results.

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We have incurred significant net losses, our future revenues are inherently unpredictable, our operating results are likely to fluctuate from period to period, and if we fail to meet the expectations of securities analysts or investors, our stock price could decline significantly

We incurred net losses of $114.1 million, $113.8 million and $619.8 million in our fiscal years ended April 30, 2005, 2004 and 2003, respectively. Our operating results for future periods are subject to numerous uncertainties, and we cannot assure you that we will be able to achieve or sustain profitability.

Our quarterly and annual operating results have fluctuated substantially in the past and are likely to fluctuate significantly in the future due to a variety of factors, some of which are outside of our control. Accordingly, we believe that period-to-period comparisons of our results of operations are not meaningful and should not be relied upon as indications of future performance. Some of the factors that could cause our quarterly or annual operating results to fluctuate include market acceptance of our products, market demand for the products manufactured by our customers, the introduction of new products and manufacturing processes, manufacturing yields, competitive pressures and customer retention.

We may experience a delay in generating or recognizing revenues for a number of reasons. Orders at the beginning of each quarter typically represent a small percentage of expected revenues for that quarter and are generally cancelable at any time. Accordingly, we depend on obtaining orders during each quarter for shipment in that quarter to achieve our revenue objectives. Failure to ship these products by the end of a quarter may adversely affect our operating results. Furthermore, our customer agreements typically provide that the customer may delay scheduled delivery dates and cancel orders within specified timeframes without significant penalty. Because we base our operating expenses on anticipated revenue trends and a high percentage of our expenses are fixed in the short term, any delay in generating or recognizing forecasted revenues could significantly harm our business. It is likely that in some future quarters our operating results will again decrease from the previous quarter or fall below the expectations of securities analysts and investors. In this event, it is likely that the trading price of our common stock would significantly decline.

We may have insufficient cash flow to meet our debt service obligations, including payments due on our subordinated convertible notes

We will be required to generate cash sufficient to conduct our business operations and pay our indebtedness and other liabilities, including all amounts due on our outstanding $2^1/2$% and $5^1/4$% convertible subordinated notes due 2010 and 2008, respectively. The aggregate outstanding principal amount of these notes was $250 million at April 30, 2005. Holders of the notes due in 2010 have the right to require us to repurchase some or all of their notes on October 15, 2007. We may choose to pay the repurchase price in cash, shares of our common stock or a combination thereof. We may not be able to cover our anticipated debt service obligations from our cash flow. This may materially hinder our ability to make payments on the notes. Our ability to meet our future debt service obligations will depend upon our future performance, which will be subject to financial, business and other factors affecting our operations, many of which are beyond our control. Accordingly, we cannot assure you that we will be able to make required principal and interest payments on the notes when due.

We may not be able to obtain additional capital in the future, and failure to do so may harm our business

We believe that our existing balances of cash, cash equivalents and short-term investments will be sufficient to meet our cash needs for working capital and capital expenditures for at least the next 12 months. We may, however, require additional financing to fund our operations in the future or to repay the principal of our outstanding $2^1/2$% and $5^1/4$% convertible subordinated notes due 2010 and 2008, respectively. The significant contraction in the capital markets, particularly in the technology sector, may make it difficult for us to raise additional capital if and when it is required, especially if we continue to experience disappointing operating results. If adequate capital is not available to us as required, or is not available on favorable terms, we could be required to significantly reduce or restructure our business operations.

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Failure to accurately forecast our revenues could result in additional charges for obsolete or excess inventories or non-cancelable purchase commitments

We base many of our operating decisions, and enter into purchase commitments, on the basis of anticipated revenue trends which are highly unpredictable. Some of our purchase commitments are not cancelable, and in some cases we are required to recognize a charge representing the amount of material or capital equipment purchased or ordered which exceeds our actual requirements. In the past, we have sometimes experienced significant growth followed by a significant decrease in customer demand such as occurred in fiscal 2001, when revenues increased by 181% followed by a decrease of 22% in fiscal 2002. Based on projected revenue trends during these periods, we acquired inventories and entered into purchase commitments in order to meet anticipated increases in demand for our products which did not materialize. As a result, we recorded significant charges for obsolete and excess inventories and non-cancelable purchase commitments which contributed to substantial operating losses in fiscal 2002. Should revenue in future periods again fall substantially below our expectations, or should we fail again to accurately forecast changes in demand mix, we could be required to record additional charges for obsolete or excess inventories or non-cancelable purchase commitments.

Our operating expenses may need to be further reduced which could impact our future growth

We experienced a significant decline in revenues and operating results during fiscal 2002. While revenues have recovered to some extent beginning in fiscal 2003, they have not yet reached levels required to operate on a profitable basis due primarily to higher fixed expenses related to a number of acquisitions, low gross margins and continued high levels of spending for research and development in anticipation of future revenue growth. While we continue to expect future revenue growth, we have taken steps to reduce our operating expenses in order to conserve our cash, and we may be required to take further action to reduce expenses. These expense reduction measures may adversely affect our ability to market our products, introduce new and improved products and increase our revenues, which could adversely affect our business and cause the price of our stock to decline. In order to be successful in the future, we must reduce our operating and product expenses, while at the same time completing our key product development programs and penetrating new customers.

We are dependent on widespread market acceptance of two product families, and our revenues will decline if the market does not continue to accept either of these product families

We currently derive substantially all of our revenue from sales of our optical subsystems and components and network performance test and monitoring systems. We expect that revenue from these products will continue to account for substantially all of our revenue for the foreseeable future. Accordingly, widespread acceptance of these products is critical to our future success. If the market does not continue to accept either our optical subsystems and components or our network performance test and monitoring systems, our revenues will decline significantly. Factors that may affect the market acceptance of our products include the continued growth of the markets for LANs, SANs, and MANs and, in particular, Gigabit Ethernet and Fibre Channel-based technologies, as well as the performance, price and total cost of ownership of our products and the availability, functionality and price of competing products and technologies.

Many of these factors are beyond our control. In addition, in order to achieve widespread market acceptance, we must differentiate ourselves from our competition through product offerings and brand name recognition. We cannot assure you that we will be successful in making this differentiation or achieving widespread acceptance of our products. Failure of our existing or future products to maintain and achieve widespread levels of market acceptance will significantly impair our revenue growth.

We depend on large purchases from a few significant customers, and any loss, cancellation, reduction or delay in purchases by these customers could harm our business

A small number of customers have accounted for a significant portion of our revenues. For example, sales to our top three customers represented 39% of our revenues in fiscal 2005, including sales to Cisco Systems, which represented 28%. Our success will depend on our continued ability to develop and manage relationships

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with significant customers. Although we are attempting to expand our customer base, we expect that significant customer concentration will continue for the foreseeable future.

The markets in which we sell our products are dominated by a relatively small number of systems manufacturers, thereby limiting the number of our potential customers. Our dependence on large orders from a relatively small number of customers makes our relationship with each customer critically important to our business. We cannot assure you that we will be able to retain our largest customers, that we will be able to attract additional customers or that our customers will be successful in selling their products that incorporate our products. We have in the past experienced delays and reductions in orders from some of our major customers. In addition, our customers have in the past sought price concessions from us, and we expect that they will continue to do so in the future. Cost reduction measures that we have implemented during the past several quarters, and additional action we may take to reduce costs, may adversely affect our ability to introduce new and improved products which may, in turn, adversely affect our relationships with some of our key customers. Further, some of our customers may in the future shift their purchases of products from us to our competitors or to joint ventures between these customers and our competitors. The loss of one or more of our largest customers, any reduction or delay in sales to these customers, our inability to successfully develop relationships with additional customers or future price concessions that we may make could significantly harm our business.

Because we do not have long-term contracts with our customers, our customers may cease purchasing our products at any time if we fail to meet our customers needs

Typically, we do not have long-term contracts with our customers. As a result, our agreements with our customers do not provide any assurance of future sales. Accordingly:

- our customers can stop purchasing our products at any time without penalty;
- our customers are free to purchase products from our competitors; and
- our customers are not required to make minimum purchases.

Sales are typically made pursuant to individual purchase orders, often with extremely short lead times. If we are unable to fulfill these orders in a timely manner, it is likely that we will lose sales and customers.

Our market is subject to rapid technological change, and to compete effectively we must continually introduce new products that achieve market acceptance

The markets for our products are characterized by rapid technological change, frequent new product introductions, changes in customer requirements and evolving industry standards with respect to the protocols used in data communications networks. We expect that new technologies will emerge as competition and the need for higher and more cost-effective bandwidth increases. Our future performance will depend on the successful development, introduction and market acceptance of new and enhanced products that address these changes as well as current and potential customer requirements. The introduction of new and enhanced products may cause our customers to defer or cancel orders for existing products. In addition, a slowdown in demand for existing products ahead of a new product introduction could result in a write-down in the value of inventory on hand related to existing products. We have in the past experienced a slowdown in demand for existing products and delays in new product development and such delays may occur in the future. To the extent customers defer or cancel orders for existing products due to a slowdown in demand or in the expectation of a new product release or if there is any delay in development or introduction of our new products or enhancements of our products, our operating results would suffer. We also may not be able to develop the underlying core technologies necessary to create new products and enhancements, or to license these technologies from third parties. Product development delays may result from numerous factors, including:

- changing product specifications and customer requirements;
- unanticipated engineering complexities;

expense reduction measures we have implemented, and others we may implement, to conserve our cash and attempt to accelerate our return to profitability;

difficulties in hiring and retaining necessary technical personnel;

difficulties in reallocating engineering resources and overcoming resource limitations; and

changing market or competitive product requirements.

The development of new, technologically advanced products is a complex and uncertain process requiring high levels of innovation and highly skilled engineering and development personnel, as well as the accurate anticipation of technological and market trends. We cannot assure you that we will be able to identify, develop, manufacture, market or support new or enhanced products successfully, if at all, or on a timely basis. Further, we cannot assure you that our new products will gain market acceptance or that we will be able to respond effectively to product announcements by competitors, technological changes or emerging industry standards. Any failure to respond to technological change would significantly harm our business.

Continued competition in our markets may lead to a reduction in our prices, revenues and market share

The markets for optical subsystems and components and network performance test and monitoring systems for use in LANs, SANs and MANs are highly competitive. Our current competitors include a number of domestic and international companies, many of which have substantially greater financial, technical, marketing and distribution resources and brand name recognition than we have. Other companies, including some of our customers, may enter the market for optical subsystems and network test and monitoring systems. We may not be able to compete successfully against either current or future competitors. Increased competition could result in significant price erosion, reduced revenue, lower margins or loss of market share, any of which would significantly harm our business. For optical subsystems, we compete primarily with Agilent Technologies, Inc. and JDS Uniphase Corporation and a number of smaller venders. Our competitors continue to introduce improved products with lower prices, and we will have to do the same to remain competitive. In addition, some of our current and potential customers may attempt to integrate their operations by producing their own optical components and subsystems and network test and monitoring systems or acquiring one of our competitors, thereby eliminating the need to purchase our products. Furthermore, larger companies in other related industries, such as the telecommunications industry, may develop or acquire technologies and apply their significant resources, including their distribution channels and brand name recognition, to capture significant market share.

Decreases in average selling prices of our products may reduce gross margins

The market for optical subsystems is characterized by declining average selling prices resulting from factors such as increased competition, overcapacity, the introduction of new products and increased unit volumes as manufacturers continue to deploy network and storage systems. We have in the past experienced, and in the future may experience, substantial period-to-period fluctuations in operating results due to declining average selling prices. We anticipate that average selling prices will decrease in the future in response to product introductions by competitors or us, or by other factors, including price pressures from significant customers. Therefore, in order to achieve and sustain profitable operations, we must continue to develop and introduce on a timely basis new products that incorporate features that can be sold at higher average selling prices. Failure to do so could cause our revenues and gross margins to decline, which would result in additional operating losses and significantly harm our business.

We may be unable to reduce the cost of our products sufficiently to enable us to compete with others. Our cost reduction efforts may not allow us to keep pace with competitive pricing pressures and could adversely affect our margins. In order to remain competitive, we must continually reduce the cost of manufacturing our products through design and engineering changes. We may not be successful in redesigning our products or delivering our products to market in a timely manner. We cannot assure you that any redesign will result in sufficient cost reductions to allow us to reduce the price of our products to remain competitive or improve our gross margins.

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Shifts in our product mix may result in declines in gross margins

Our gross profit margins vary among our product families, and are generally higher on our network test and monitoring systems than on our optical subsystems and components. Our optical products sold for longer distance MAN and telecom applications typically have higher gross margins than our products for shorter distance LAN or SAN applications. Our gross margins are generally lower for newly introduced products and improve as unit volumes increase. Our overall gross margins have fluctuated from period to period as a result of shifts in product mix, the introduction of new products, decreases in average selling prices for older products and our ability to reduce product costs, and these fluctuations are expected to continue in the future.

Our customers often evaluate our products for long and variable periods, which causes the timing of our revenues and results of operations to be unpredictable

The period of time between our initial contact with a customer and the receipt of an actual purchase order may span a year or more. During this time, customers may perform, or require us to perform, extensive and lengthy evaluation and testing of our products before purchasing and using them in their equipment. Our customers do not typically share information on the duration or magnitude of these qualification procedures. The length of these qualification processes also may vary substantially by product and customer, and, thus, cause our results of operations to be unpredictable. While our potential customers are qualifying our products and before they place an order with us, we may incur substantial research and development and sales and marketing expenses and expend significant management effort. Even after incurring such costs we ultimately may not sell any products to such potential customers. In addition, these qualification processes often make it difficult to obtain new customers, as customers are reluctant to expend the resources necessary to qualify a new supplier if they have one or more existing qualified sources. Once our products have been qualified, the agreements that we enter into with our customers typically contain no minimum purchase commitments. Failure of our customers to incorporate our products into their systems would significantly harm our business.

We depend on facilities located outside of the United States to manufacture a substantial portion of our products, which subjects us to additional risks

In addition to our principal manufacturing facility in Malaysia, we operate smaller facilities in China and Singapore and also rely on two contract manufacturers located outside of the United States. We also rely on Infineon to manufacture transceiver and transponder products for us until we are able to transfer manufacturing operations to our production facilities. Each of these facilities and manufacturers subjects us to additional risks associated with international manufacturing, including:

- unexpected changes in regulatory requirements;
- legal uncertainties regarding liability, tariffs and other trade barriers;
- inadequate protection of intellectual property in some countries;
- greater incidence of shipping delays;
- greater difficulty in overseeing manufacturing operations;
- greater difficulty in hiring technical talent needed to oversee manufacturing operations;
- potential political and economic instability;
- currency fluctuations; and
- the outbreak of infectious diseases such as severe acute respiratory syndrome, or SARS, which could result in travel restrictions or the closure of our facilities or the facilities of our customers and suppliers.

Any of these factors could significantly impair our ability to source our contract manufacturing requirements internationally.

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Our business and future operating results are subject to a wide range of uncertainties arising out of the continuing threat of terrorist attacks and ongoing military action in the Middle East

Like other U.S. companies, our business and operating results are subject to uncertainties arising out of the continuing threat of terrorist attacks on the United States and ongoing military action in the Middle East, including the potential worsening or extension of the current global economic slowdown, the economic consequences of the war in Iraq or additional terrorist activities and associated political instability, and the impact of heightened security concerns on domestic and international travel and commerce. In particular, due to these uncertainties we are subject to:

- increased risks related to the operations of our manufacturing facilities in Malaysia;
- greater risks of disruption in the operations of our Asian contract manufacturers and more frequent instances of shipping delays; and
- the risk that future tightening of immigration controls may adversely affect the residence status of non-U.S. engineers and other key technical employees in our U.S. facilities or our ability to hire new non-U.S. employees in such facilities.

We may lose sales if our suppliers fail to meet our needs

We currently purchase several key components used in the manufacture of our products from single or limited sources. We are also dependent on Infineon to supply finished transceiver and transponder products during a transition period of up to one year until we have transitioned the manufacturing operations to other facilities. We depend on these current and future sources to meet our production needs. Moreover, we depend on the quality of the products supplied to us over which we have limited control. We have encountered shortages and delays in obtaining components in the past and expect to encounter shortages and delays in the future. If we cannot supply products due to a lack of components, or are unable to redesign products with other components in a timely manner, our business will be significantly harmed. We generally have no long-term contracts for any of our components. As a result, a supplier can discontinue supplying components to us without penalty. If a supplier discontinued supplying a component, our business may be harmed by the resulting product manufacturing and delivery delays. We are also subject to potential delays in the development by our suppliers of key components which may affect our ability to introduce new products.

We use rolling forecasts based on anticipated product orders to determine our component requirements. Lead times for materials and components that we order vary significantly and depend on factors such as specific supplier requirements, contract terms and current market demand for particular components. If we overestimate our component requirements, we may have excess inventory, which would increase our costs. If we underestimate our component requirements, we may have inadequate inventory, which could interrupt our manufacturing and delay delivery of our products to our customers. Any of these occurrences would significantly harm our business.

We have made and may continue to make strategic investments which may not be successful and may result in the loss of all or part of our invested capital

Through fiscal 2005, we recorded minority equity investments in early-stage technology companies, totaling $52.4 million. Our recent investment of $4.75 million in CyOptics is a similar minority equity investment. Our investments in these early stage companies were primarily motivated by our desire to gain early access to new technology. We intend to review additional opportunities to make strategic equity investments in pre-public companies where we believe such investments will provide us with opportunities to gain access to important technologies or otherwise enhance important commercial relationships. We have little or no influence over the early-stage companies in which we have made or may make these strategic, minority equity investments. Each of these investments in pre-public companies involves a high degree of risk. We may not be successful in achieving the financial, technological or commercial advantage upon which any given investment is premised, and failure by the early-stage company to achieve its own business objectives or to raise capital needed on acceptable economic terms could result in a loss of all or part of our invested capital. In

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fiscal 2003, we wrote off $12.0 million in two investments which became impaired. In fiscal 2004, we wrote off $1.6 million in two additional investments, and in fiscal 2005, we wrote off $10.0 million in another investment. We may be required to write off all or a portion of the $21.4 million in such investments remaining on our balance sheet as of April 30, 2005 in future periods.

We are subject to pending legal proceedings

A securities class action lawsuit was filed on November 30, 2001 in the United States District Court for the Southern District of New York, purportedly on behalf of all persons who purchased our common stock from November 17, 1999 through December 6, 2000. The complaint named as defendants Finisar, Jerry S. Rawls, our President and Chief Executive Officer, Frank H. Levinson, our Chairman of the Board and Chief Technical Officer, Stephen K. Workman, our Senior Vice President and Chief Financial Officer, and an investment banking firm that served as an underwriter for our initial public offering in November 1999 and a secondary offering in April 2000. The complaint, as amended, alleges violations of Sections 11 and 15 of the Securities Act of 1933 and Sections 10(b) and 20(b) of the Securities Exchange Act of 1934. No specific damages are claimed. Similar allegations have been made in lawsuits relating to more than 300 other initial public offerings conducted in 1999 and 2000, which were consolidated for pretrial purposes. In October 2002, all claims against the individual defendants were dismissed without prejudice. On February 19, 2003, our motion to dismiss the complaint was denied. In July 2004, we and the individual defendants accepted a settlement proposal made to all of the issuer defendants. Under the terms of the settlement, the plaintiffs will dismiss and release all claims against participating defendants in exchange for a contingent payment guaranty by the insurance companies collectively responsible for insuring the issuers in all related cases, and the assignment or surrender to the plaintiffs of certain claims the issuer defendants may have against the underwriters. Under the guaranty, the insurers will be required to pay the amount, if any, by which $1 billion exceeds the aggregate amount ultimately collected by the plaintiffs from the underwriter defendants in all the cases. If the plaintiffs fail to recover $1 billion and payment is required under the guaranty, we would be responsible to pay our pro rata portion of the shortfall, up to the amount of the self-insured retention under our insurance policy, which may be up to $2 million. The timing and amount of payments that we could be required to make under the proposed settlement will depend on several factors, principally the timing and amount of any payment that the insurers may be required to make pursuant to the $1 billion guaranty. On February 15, 2005, the Court issued an order providing preliminary approval of the proposed settlement except insofar as the settlement would have cut off contractual indemnification claims that underwriters may have against securities issuers, such as the Company. On April 13, 2005, the Court held a further conference to determine the final form, substance and program of class notice and set a hearing for January 9, 2006 to consider final approval of the settlement. If the settlement is not approved by the Court, we intend to defend the lawsuit vigorously. Because of the inherent uncertainty of litigation, however, we cannot predict its outcome. If, as a result of this dispute, we are required to pay significant monetary damages, our business would be substantially harmed.

We have identified material weaknesses in our internal control over financial reporting which could lead to errors in our financial statements

We identified material weaknesses in our internal control over financial reporting, as discussed in this prospectus in the section of Management s Discussion and Analysis titled Management s Report on Internal Control Over Financial Reporting. Although steps are being taken to remediate these deficiencies, there can be no assurance that these remediation steps will be successful or that, as a result of our ongoing evaluation of our internal control over financial reporting, we will not identify additional material weaknesses. Although management determined that the material weaknesses did not affect the financial results reported in our consolidated financial statements as of, and for the year ended, April 30, 2005, there can be no assurance that unremediated weaknesses in our internal control over financial reporting will not result in errors that are material to the financial results reported in our consolidated financial statements for future periods.

Because of competition for technical personnel, we may not be able to recruit or retain necessary personnel

We believe our future success will depend in large part upon our ability to attract and retain highly skilled managerial, technical, sales and marketing, finance and manufacturing personnel. In particular, we may need to increase the number of technical staff members with experience in high-speed networking applications as we further develop our product lines. Competition for these highly skilled employees in our industry is intense. Our failure to attract and retain these qualified employees could significantly harm our business. The loss of the services of any of our qualified employees, the inability to attract or retain qualified personnel in the future or delays in hiring required personnel could hinder the development and introduction of and negatively impact our ability to sell our products. In addition, employees may leave our company and subsequently compete against us. Moreover, companies in our industry whose employees accept positions with competitors frequently claim that their competitors have engaged in unfair hiring practices. We have been subject to claims of this type and may be subject to such claims in the future as we seek to hire qualified personnel. Some of these claims may result in material litigation. We could incur substantial costs in defending ourselves against these claims, regardless of their merits.

Our products may contain defects that may cause us to incur significant costs, divert our attention from product development efforts and result in a loss of customers

Networking products frequently contain undetected software or hardware defects when first introduced or as new versions are released. Our products are complex and defects may be found from time to time. In addition, our products are often embedded in or deployed in conjunction with our customers products which incorporate a variety of components produced by third parties. As a result, when problems occur, it may be difficult to identify the source of the problem. These problems may cause us to incur significant damages or warranty and repair costs, divert the attention of our engineering personnel from our product development efforts and cause significant customer relation problems or loss of customers, all of which would harm our business.

Our failure to protect our intellectual property may significantly harm our business

Our success and ability to compete is dependent in part on our proprietary technology. We rely on a combination of patent, copyright, trademark and trade secret laws, as well as confidentiality agreements to establish and protect our proprietary rights. We license certain of our proprietary technology, including our digital diagnostics technology, to customers who include current and potential competitors, and we rely largely on provisions of our licensing agreements to protect our intellectual property rights in this technology. Although a number of patents have been issued to us, we have obtained a number of other patents as a result of our acquisitions, and we have filed applications for additional patents, we cannot assure you that any patents will issue as a result of pending patent applications or that our issued patents will be upheld. Any infringement of our proprietary rights could result in significant litigation costs, and any failure to adequately protect our proprietary rights could result in our competitors offering similar products, potentially resulting in loss of a competitive advantage and decreased revenues. Despite our efforts to protect our proprietary rights, existing patent, copyright, trademark and trade secret laws afford only limited protection. In addition, the laws of some foreign countries do not protect our proprietary rights to the same extent as do the laws of the United States. Attempts may be made to copy or reverse engineer aspects of our products or to obtain and use information that we regard as proprietary. Accordingly, we may not be able to prevent misappropriation of our technology or deter others from developing similar technology. Furthermore, policing the unauthorized use of our products is difficult. We are currently engaged in pending litigation to enforce certain of our patents, and additional litigation may be necessary in the future to enforce our intellectual property rights or to determine the validity and scope of the proprietary rights of others. This litigation could result in substantial costs and diversion of resources and could significantly harm our business.

Claims that we infringe third-party intellectual property rights could result in significant expenses or restrictions on our ability to sell our products

The networking industry is characterized by the existence of a large number of patents and frequent litigation based on allegations of patent infringement. We have been involved in the past in patent infringement lawsuits. From time to time, other parties may assert patent, copyright, trademark and other intellectual property rights to technologies and in various jurisdictions that are important to our business. Any claims asserting that our products infringe or may infringe proprietary rights of third parties, if determined adversely to us, could significantly harm our business. Any claims, with or without merit, could be time-consuming, result in costly litigation, divert the efforts of our technical and management personnel, cause product shipment delays or require us to enter into royalty or licensing agreements, any of which could significantly harm our business. Royalty or licensing agreements, if required, may not be available on terms acceptable to us, if at all. In addition, our agreements with our customers typically require us to indemnify our customers from any expense or liability resulting from claimed infringement of third party intellectual property rights. In the event a claim against us was successful and we could not obtain a license to the relevant technology on acceptable terms or license a substitute technology or redesign our products to avoid infringement, our business would be significantly harmed.

Our executive officers and directors and entities affiliated with them own a large percentage of our voting stock, and VantagePoint Venture Partners has recently acquired a large block of our common stock, that has resulted in a substantial concentration of control and could have the effect of delaying or preventing a change in our control

As of June 30, 2005, our executive officers and directors and certain entities affiliated with them beneficially owned approximately 36.7 million shares of our common stock, or approximately 13.1% of the outstanding shares. These stockholders, acting together, may be able to substantially influence the outcome of matters requiring approval by stockholders, including the election or removal of directors and the approval of mergers or other business combination transactions. In addition, certain funds managed by VantagePoint Venture Partners, of which David C. Fries, a director of the Company, is a managing director hold approximately 12.3% of our outstanding common stock. Accordingly, if VantagePoint Venture Partners continues to hold its shares, it may also be able to influence the outcome of matters requiring stockholder approval, and VantagePoint Venture Partners, our executive officers, directors and entities affiliated with them, voting together, may be able to effectively control the outcome of such matters. This concentration of ownership could have the effect of delaying or preventing a change in control or otherwise discouraging a potential acquirer from attempting to obtain control of us, which in turn could have an adverse effect on the market price of our common stock or prevent our stockholders from realizing a premium over the market price for their shares of common stock.

The conversion of our outstanding convertible subordinated notes would result in substantial dilution to our current stockholders

We currently have outstanding $5^1/4$% convertible subordinated notes due 2008 in the principal amount of $100.3 million and $2^1/2$% convertible subordinated notes due 2010 in the principal amount of $150.0 million. The $5^1/4$% notes are convertible, at the option of the holder, at any time on or prior to maturity into shares of our common stock at a conversion price of $5.52 per share. The $2^1/2$% notes are convertible, at the option of the holder, at any time on or prior to maturity into shares of our common stock at a conversion price of $3.705 per share. An aggregate of 58,647,060 shares of common stock would be issued upon the conversion of all outstanding convertible subordinated notes at these exchange rates, which would significantly dilute the voting power and ownership percentage of our existing stockholders. Holders of the notes due in 2010 have the right to require us to repurchase some or all of their notes on October 15, 2007. We may choose to pay the repurchase price in cash, shares of our common stock or a combination thereof. Our right to repurchase the notes, in whole or in part, with shares of our common stock is subject to the registration of the shares of our common stock to be issued upon repurchase under the Securities Act, if required, and registration with or approval of any state or federal governmental authority if such registration or approval is required before such shares may be issued. We have previously entered into privately negotiated transactions with certain holders of our convertible subordinated notes for the repurchase of notes in exchange for a greater number of shares of our common stock than would have been issued had the principal amount of the notes been converted at the original conversion rate specified in the notes, thus resulting in more dilution. Although we do not currently have any plans to enter into similar transactions in the future, if we were to do so there would be additional dilution to the voting power and percentage ownership of our existing stockholders.

Delaware law, our charter documents and our stockholder rights plan contain provisions that could discourage or prevent a potential takeover, even if such a transaction would be beneficial to our stockholders

Some provisions of our certificate of incorporation and bylaws, as well as provisions of Delaware law, may discourage, delay or prevent a merger or acquisition that a stockholder may consider favorable. These include provisions:

- authorizing the board of directors to issue additional preferred stock;
- prohibiting cumulative voting in the election of directors;
- limiting the persons who may call special meetings of stockholders;
- prohibiting stockholder actions by written consent;
- creating a classified board of directors pursuant to which our directors are elected for staggered three-year terms;
- permitting the board of directors to increase the size of the board and to fill vacancies;
- requiring a super-majority vote of our stockholders to amend our bylaws and certain provisions of our certificate of incorporation; and
- establishing advance notice requirements for nominations for election to the board of directors or for proposing matters that can be acted on by stockholders at stockholder meetings.

We are subject to the provisions of Section 203 of the Delaware General Corporation Law which limit the right of a corporation to engage in a business combination with a holder of 15% or more of the corporation s outstanding voting securities, or certain affiliated persons.

In addition, in September 2002, our board of directors adopted a stockholder rights plan under which our stockholders received one share purchase right for each share of our common stock held by them. Subject to certain exceptions, the rights become exercisable when a person or group (other than certain exempt persons) acquires, or announces its intention to commence a tender or exchange offer upon completion of which such person or group would acquire, 20% or more of our common stock without prior board approval. Should such an event occur, then, unless the rights are redeemed or have expired, our stockholders, other than the acquirer, will be entitled to purchase shares of our common stock at a 50% discount from its then-Current Market Price (as defined) or, in the case of certain business combinations, purchase the common stock of the acquirer at a 50% discount.

Although we believe that these charter and bylaw provisions, provisions of Delaware law and our stockholder rights plan provide an opportunity for the board to assure that our stockholders realize full value for their investment, they could have the effect of delaying or preventing a change of control, even under circumstances that some stockholders may consider beneficial.

Our business and future operating results may be adversely affected by events outside of our control

Our business and operating results are vulnerable to events outside of our control, such as earthquakes, fire, power loss, telecommunications failures and uncertainties arising out of terrorist attacks in the United States and overseas. Our corporate headquarters and a portion of our manufacturing operations are located in California. California in particular has been vulnerable to natural disasters, such as earthquakes,

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fires and floods, and other risks which at times have disrupted the local economy and posed physical risks to our property. We are also dependent on communications links with our overseas manufacturing locations and would be significantly harmed if these links were interrupted for any significant length of time. We presently do not have adequate redundant, multiple site capacity if any of these events were to occur, nor can we be certain that the insurance we maintain against these events would be adequate.

Our stock price has been and is likely to continue to be volatile

The trading price of our common stock has been and is likely to continue to be subject to large fluctuations. Our stock price may increase or decrease in response to a number of events and factors, including:

- trends in our industry and the markets in which we operate;
- changes in the market price of the products we sell;
- changes in financial estimates and recommendations by securities analysts;
- acquisitions and financings;
- quarterly variations in our operating results;
- the operating and stock price performance of other companies that investors in our common stock may deem comparable; and
- purchases or sales of blocks of our common stock.

Part of this volatility is attributable to the current state of the stock market, in which wide price swings are common. This volatility may adversely affect the prices of our common stock regardless of our operating performance.

Our future operating results may be subject to volatility as a result of exposure to foreign exchange risks.

We are also exposed to foreign exchange risks. Foreign currency fluctuations may affect both our revenues and our costs and expenses and significantly affect our operating results. Prices for our products are currently denominated in U.S. dollars for sales to our customers throughout the world. If there is a significant devaluation of the currency in a specific country relative to the dollar, the prices of our products will increase relative to that country s currency, our products may be less competitive in that country and our revenues may be adversely affected.

Although we price our products in U.S. dollars, portions of both our cost of revenues and operating expenses are incurred in foreign currencies, principally the Malaysian ringit, the Chinese yuan and the Euro. As a result, we bear the risk that the rate of inflation in one or more countries will exceed the rate of the devaluation of that country s currency in relation to the U.S. dollar, which would increase our costs as expressed in U.S. dollars. On July 21, 2005, the People s Bank of China announced that the yuan will no longer be pegged to the U.S. dollar but will be allowed to float in a band (and, to a limited extent, increase in value) against a basket of foreign currencies. This development increases the risk that Chinese-sourced materials and labor could become more expensive for us. To date, we have not engaged in currency hedging transactions to decrease the risk of financial exposure from fluctuations in foreign exchange rates.

USE OF PROCEEDS

We will not receive any proceeds from the sale by the selling stockholder of the common stock offered hereby.

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PRICE RANGE OF OUR COMMON STOCK

Our common stock is traded on the Nasdaq National Market under the symbol FNSR. The following table sets forth the range of high and low closing sales prices of our common stock for the periods indicated:

	High	Low
Fiscal 2006 Quarter Ended:		
October 31, 2005 (through August 11)	$ 1.10	$ 1.03
July 31, 2005	$ 1.30	$ 1.01
Fiscal 2005 Quarter Ended:		
April 30, 2005	$ 1.26	$ 1.12
January 31, 2005	$ 1.78	$ 1.66
October 31, 2004	$ 1.47	$ 1.42
July 31, 2004	$ 1.53	$ 1.41
Fiscal 2004 Quarter Ended:		
April 30, 2004	$ 3.26	$ 1.77
January 31, 2004	$ 4.14	$ 2.80
October 31, 2003	$ 3.41	$ 1.62
July 31, 2003	$ 1.94	$ 1.09

The closing price of our common stock as reported on the Nasdaq National Market on August 11, 2005 was $1.03. The approximate number of stockholders of record on June 30, 2005 was 471. This number does not include stockholders whose shares are held in trust by other entities. The number of beneficial stockholders of our shares is greater than the number of stockholders of record.

DIVIDEND POLICY

We have never declared or paid cash dividends on our common stock and currently intend to retain earnings for use in our business and do not anticipate paying any cash dividends in the foreseeable future. The payment of dividends in the future will be subject to the discretion of our Board of Directors, will be subject to applicable law and will depend on our results of operations, earnings, financial condition, contractual limitations, cash requirements, future prospects and other factors deemed relevant by our Board of Directors.

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CAPITALIZATION

The following table sets forth our total capitalization as of April 30, 2005:

	April 30, 2005 (In thousands, except share data)
Current portion of long-term liabilities	$ 2,242
Convertible notes, net of unamortized portion of beneficial conversion feature, other long-term liabilities and deferred income taxes	265,274
Stockholders equity:	
Preferred stock, $0.001 par value; 5,000,000 shares authorized, no shares issued or outstanding	
Common stock, $0.001 par value; 500,000,000 shares authorized, 258,931,278 shares issued and outstanding(1)	259
Additional paid-in capital	1,314,960
Accumulated other comprehensive income	381
Accumulated deficit	(1,171,310)
Total stockholders equity	144,290
Total capitalization	$ 409,564

(1) Excludes:

shares of common stock reserved for issuance under our stock option plans and employee stock purchase plan and upon exercise of stock options and warrants assumed in connection with our acquisitions of six privately-held companies;

shares of common stock reserved for issuance upon conversion of the convertible installment note issued as consideration for our acquisition of the assets of Data Transit Corp. in August 2004;

shares of common stock issued in connection with the acquisition of InterSAN, Inc. in May 2005;

shares of common stock reserved for issuance upon conversion of promissory notes issued as consideration for our acquisition of I-TECH CORP in April 2005; and

shares reserved for issuance upon conversion of the CyOptics Note.

See Management Equity Compensation Plan Information, Description of Capital Stock and Note 14 to our audited consolidated financial statements included elsewhere in this prospectus.

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SELECTED FINANCIAL DATA

The following summary financial data should be read together with Management s Discussion and Analysis of Financial Condition and Results of Operations and our financial statements and the notes thereto included elsewhere in this prospectus. The statement of operations data set forth below for the fiscal years ended April 30, 2005, 2004 and 2003 and the balance sheet data as of April 30, 2005 and 2004 are derived from, and are qualified by reference to, our audited consolidated financial statements included elsewhere in this prospectus. The statement of operations data set forth below for the fiscal years ended April 30, 2002 and 2001 and the balance sheet data as of April 30, 2003, 2002 and 2001 are derived from audited financial statements not included in this prospectus. The Management s Discussion and Analysis of Financial Condition and Results of Operations related to the statement of operations and balance sheet data for the fiscal years ended April 30, 2002 and 2001 are not included in this prospectus.

	Fiscal Years Ended April 30,				
	2005	2004	2003	2002	2001
	(In thousands, except per share data)				
Statement of Operations Data:					
Revenues	$ 280,823	$ 185,618	$ 166,482	$ 147,265	$ 188,800
Cost of revenues	205,631	143,585	130,501	136,626	131,551
Amortization of acquired developed technology	22,268	19,239	21,983	27,119	10,900
Impairment of acquired developed technology	3,656				
Gross profit (loss)	49,268	22,794	13,998	(16,480)	46,349
Operating expenses:					
Research and development	62,799	62,193	60,295	54,372	33,696
Sales and marketing	29,783	20,063	20,232	21,448	16,673
General and administrative	23,374	16,738	15,201	19,419	10,160
Amortization of (benefit from) deferred stock compensation	162	(105)	(1,719)	11,963	13,542
Acquired in-process research and development	1,558	6,180		2,696	35,218
Amortization of goodwill and other purchased intangibles	1,104	572	758	129,099	53,122
Impairment of tangible assets	18,798				
Impairment of goodwill and intangible assets			10,586		
Restructuring costs	287	382	9,378		
Other acquisition costs		222	198	3,119	1,130
Total operating expenses	137,865	106,245	114,929	242,116	163,541
Loss from operations	(88,597)	(83,451)	(100,931)	(258,596)	(117,192)
Interest income (expense), net	(12,072)	(25,701)	(6,699)	(68)	14,217
Other income (expense), net	(12,582)	(4,347)	(51,314)	1,360	18,546

Loss before income taxes and cumulative effect of an accounting change	(113,251)	(113,499)	(158,944)	(257,304)	(84,429)
Provision (benefit) for income taxes	856	334	229	(38,566)	1,020
Loss before cumulative effect of an accounting change	(114,107)	(113,833)	(159,173)	(218,738)	(85,449)
Cumulative effect of an accounting change to adopt SFAS 142			(460,580)		
Net loss	$ (114,107)	$ (113,833)	$ (619,753)	$ (218,738)	$ (85,449)

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	Fiscal Years Ended April 30,				
	2005	**2004**	**2003**	**2002**	**2001**
	(In thousands, except per share data)				
Net loss per share basic and diluted:					
Before cumulative effect of an accounting change	$ (0.49)	$ (0.53)	$ (0.82)	$ (1.21)	$ (0.53)
Cumulative effect of an accounting change to adopt SFAS 142	$	$	$ (2.35)	$	$
Net loss per share	$ (0.49)	$ (0.53)	$ (3.17)	$ (1.21)	$ (0.53)
Shares used in per share calculations:					
Basic and diluted	232,210	216,117	195,666	181,136	160,014
Pro forma amounts assuming the change in accounting principle was applied retroactively (unaudited):					
Net loss	$ (114,107)	$ (113,833)	$ (619,753)	$ (90,957)	$ (32,857)
Net loss per share basic and diluted	$ (0.49)	$ (0.53)	$ (3.17)	$ (0.50)	$ (0.21)
Shares used in computing pro forma net loss per share:					
Basic and diluted	232,210	216,117	195,666	181,136	160,014

	As of April 30,				
	2005	**2004**	**2003**	**2002**	**2001**
	(In thousands)				
Balance Sheet Data:					
Cash, cash equivalents and short-term investments	$ 102,362	$ 143,398	$ 119,438	$ 144,097	$ 146,111
Working capital	120,272	172,892	149,967	222,603	249,000
Total assets	488,985	494,705	423,606	1,041,281	1,029,995
Long-term liabilities	265,274	233,732	101,531	106,869	45,354
Convertible preferred stock					1
Total stockholders equity	144,290	202,845	274,980	879,002	941,851

Net income in fiscal 2003 reflects our adoption of Statements of Financial Accounting Standards 141 and 142 on May 1, 2002. As a result of our adoption, reported net loss decreased by approximately $127.8 million, or $0.65 per share, due to the cessation of the amortization of goodwill and the amortization of acquired workforce and customer base.

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MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion contains forward-looking statements that involve risks and uncertainties. Our actual results could differ substantially from those anticipated in these forward-looking statements as a result of many factors, including those set forth under Risk Factors. The following discussion should be read together with our consolidated financial statements and related notes thereto included elsewhere in this document.

Overview

We were incorporated in 1987 and funded our initial product development efforts largely through revenues derived under research and development contracts. After shipping our first products in 1991, we continued to finance our operations principally through internal cash flow and periodic bank borrowings until November 1998. At that time we raised $5.6 million of net proceeds from the sale of equity securities and bank borrowings to fund the continued growth and development of our business. In November 1999, we received net proceeds of $151.0 million from the initial public offering of shares of our common stock, and in April 2000 we received $190.6 million from an additional public offering of shares of our common stock. In October 2001, we sold $125 million aggregate principal amount of 5$^{1}/4$% convertible subordinated notes due October 15, 2008, and in October 2003, we sold $150 million aggregate principal amount of 2$^{1}/2$% convertible subordinated notes due October 15, 2010.

Since October 2000, we have acquired a number of companies and certain businesses and assets of other companies in order to broaden our product offerings and provide new sources of revenue, production capabilities and access to advanced technologies that we believe will enable us to reduce our product costs and develop innovative and more highly integrated product platforms while accelerating the timeframe required to develop such products.

In October 2002, we sold our subsidiary, Sensors Unlimited, Inc. to a new company organized by a management group led by Dr. Greg Olsen, then an officer and director of Finisar and a former majority owner of Sensors Unlimited. The intellectual property developed after the acquisition of Sensors Unlimited was transferred to other operations within Finisar. In November 2002, we discontinued a product line at our Demeter Technologies subsidiary that was not making a significant contribution to our operating results and was no longer considered a key part of our product strategy. Certain assets of Demeter Technologies were sold in conjunction with the product line discontinuation. In April 2003, we acquired Genoa Corporation and announced the closure of Demeter Technologies and the consolidation of all active device development and wafer fabrication operations into the Genoa facility. The consolidation was completed in fiscal 2004. During the second quarter of fiscal 2004, we completed the closure of our German facility associated with the acquisition of AIFOtec, GmbH. The intellectual property, technical know-how and certain assets related to the German operations were consolidated with our operations in Sunnyvale, California, during the second quarter of fiscal 2004.

The principal strategic goal of most of our acquisitions to date related to our optical subsystems and components business has been to gain access to leading-edge technology for the manufacture of optical components in order to improve the performance and reduce the cost of our optical subsystem products. We have also sold these optical components on a stand-alone basis to other manufacturers; however, prior to our acquisition of Honeywell International Inc. s VCSEL Optical Products business unit in March 2004, the sale of these components into this so-called merchant market had not been a strategic priority, and our revenues from the sale of optical subsystems and components consisted predominantly of subsystems sales. As a result of the Honeywell acquisition, we are now selling vertical cavity surface emitting lasers, or VCSELs, in the merchant market, and we intend to evaluate opportunities to increase the sale of these and other components in the merchant market. The principal strategic goal of most of our acquisitions to date related to our network test and monitoring business has been to broaden our product portfolio and to gain access to new distribution channels. The acquisition of assets and intellectual property of Data Transit, Inc. in August 2004, I-TECH CORP. in April 2005, and InterSAN, Inc. in May 2005 were examples of our pursuit of this strategy. As a result of these acquisitions, we have expanded our product offerings for SAN test, analysis and monitoring tools to include additional products which test and monitor storage networks using the SAS and SATA protocols as well as additional tools for testing and reconfiguring SANs.

To date, our revenues have been principally derived from sales of our optical subsystems to networking and storage systems manufacturers and sales of our network performance test systems to these manufacturers as well as end users. Optical subsystems consist primarily of transceivers sold to manufacturers of storage and networking equipment for SANs, LANs, and MAN applications. A large proportion of our sales are concentrated with a relatively small number of customers. Although we are attempting to expand our customer base, we expect that significant customer concentration will continue for the foreseeable future.

We recognize revenue when persuasive evidence of an arrangement exists, title and risk of loss pass to the customer, which is generally upon shipment, the price is fixed or determinable and collectability is reasonably assured. For those arrangements with multiple elements, or in related arrangements with the same customer, we allocate revenue to the separate elements based upon each element s fair value as determined by the list price for such element.

We sell our products through our direct sales force, with the support of our manufacturers representatives, directly to domestic customers and indirectly through distribution channels to international customers. The evaluation and qualification cycle prior to the initial sale for our optical subsystems may span a year or more, while the sales cycle for our test and monitoring systems is usually considerably shorter.

The market for optical subsystems and components is characterized by declining average selling prices resulting from factors such as industry over-capacity, increased competition, the introduction of new products and the growth in unit volumes as manufacturers continue to deploy network and storage systems. We anticipate that our average selling prices will continue to decrease in future periods, although the timing and amount of these decreases cannot be predicted with any certainty.

Our cost of revenues consists of materials, salaries and related expenses for manufacturing personnel, manufacturing overhead, warranty expense, inventory adjustments for obsolete and excess inventory and the amortization of acquired developed technology associated with acquisitions that we have made. Historically, we outsourced the majority of our assembly operations. However, in fiscal 2002, we commenced manufacturing of our optical subsystem products at our subsidiary in Ipoh, Malaysia. We conduct component manufacturing, manufacturing engineering, supply chain management, quality assurance and documentation control at our facilities in Sunnyvale, California and Richardson, Texas and at our subsidiaries facilities in Fremont, California, Shanghai, China and Ipoh, Malaysia. With the transition of most of our production to Malaysia and the added manufacturing infrastructure associated with several acquisitions completed during the past two years, our cost structure has become more fixed, making it more difficult to reduce costs during periods when demand for our products is weak, product mix is unfavorable or selling prices are generally lower. While we undertook measures to reduce our operating costs during fiscal 2003, 2004 and 2005, there can be no assurance that we will be able to reduce our cost of revenues enough to achieve or sustain profitability during periods of weak demand or when average selling prices are low.

Our gross profit margins vary among our product families, and are generally higher on our network test and monitoring systems than on our optical subsystems and components. Our optical products sold for longer distance MAN and telecom applications typically have higher gross margins than our products for shorter distance LAN and SAN applications. Our overall gross margins have fluctuated from period to period as a result of overall revenue levels, shifts in product mix, the introduction of new products, decreases in average selling prices and our ability to reduce product costs.

Research and development expenses consist primarily of salaries and related expenses for design engineers and other technical personnel, the cost of developing prototypes and fees paid to consultants. We charge all research and development expenses to operations as incurred. We believe that continued investment in research and development is critical to our long-term success.

Sales and marketing expenses consist primarily of commissions paid to manufacturers representatives, salaries and related expenses for personnel engaged in sales, marketing and field support activities and other costs associated with the promotion of our products.

General and administrative expenses consist primarily of salaries and related expenses for administrative, finance and human resources personnel, professional fees, and other corporate expenses.

In connection with the grant of stock options to employees between August 1, 1998 and October 15, 1999, we recorded deferred stock compensation representing the difference between the deemed value of our common stock for accounting purposes and the exercise price of these options at the date of grant. In connection with the assumption of stock options previously granted to employees of companies we acquired, we recorded deferred compensation representing the difference between the fair market value of our common stock on the date of closing of each acquisition and the exercise price of the unvested portion of options granted by those companies which we assumed. Deferred stock compensation is presented as a reduction of stockholder s equity, with accelerated amortization recorded over the vesting period, which is typically three to five years. The amount of deferred stock compensation expense to be recorded in future periods could decrease if options for which accrued but unvested compensation has been recorded are forfeited prior to vesting and could increase if we modify the terms of an option grant resulting in a new measurement date.

Acquired in-process research and development represents the amount of the purchase price in a business combination allocated to research and development projects underway at the acquired company that had not reached the technologically feasible stage as of the closing of the acquisition and for which we had no alternative future use.

A portion of the purchase price in a business combination is allocated to goodwill and intangibles. Prior to May 1, 2002, goodwill and purchased intangibles were amortized over their estimated useful lives. Subsequent to May 1, 2002, goodwill and intangible assets with indefinite lives are no longer amortized but subject to annual impairment testing.

Impairment charges consist of write downs to the carrying value of intangible assets and goodwill arising from various business combinations to their implied fair value.

Restructuring costs generally include termination costs for employees associated with a formal restructuring plan and the cost of facilities or other unusable assets abandoned or sold.

Other acquisition costs primarily consist of incentive payments for employee retention included in certain of the purchase agreements of companies we acquired and costs incurred in connection with transactions that were not completed.

Other income and expenses generally consist of bank fees, gains or losses as a result of the periodic sale of assets and other-than-temporary decline in the value of investments.

Recent Acquisitions

Acquisition of Honeywell VCSEL Optical Products Business

On March 1, 2004, we completed the acquisition of Honeywell International Inc. s VCSEL Optical Products business unit for a purchase price and transaction expenses totaling approximately $80.9 million in cash and $1.2 million in our common stock. The acquisition was accounted for under the purchase method of accounting. The acquisition was undertaken to lower our cost of goods sold as a result of being more vertically integrated, to gain access to intellectual property and know-how associated with making short wavelength VCSELs for both data communications and other market applications in the future and the additional revenue and earnings growth associated with new product opportunities. The amount of goodwill recorded in this acquisition reflected the value to be realized associated with these incremental cost savings and future revenue opportunities. The results of operations of this business unit, which we now refer to as our Advanced Optical Components, or AOC, Division are included in our consolidated financial statements beginning on March 1, 2004.

Acquisition of Assets of Data Transit Corp.

On August 6, 2004, we completed the purchase of substantially all of the assets of Data Transit Corp. in exchange for a cash payment of $500,000 and the issuance of a convertible promissory note in the original principal amount of $16.3 million. Transaction costs totaled $682,000. The acquisition of Data Transit expanded our product offering for testing and monitoring systems, particularly those systems based on the SAS and SATA protocols used in the disk drive industry. The amount of goodwill recorded with this acquisition reflected the incremental earnings associated with selling this new test and monitoring capability, the underlying know-how for making these products which we plan to incorporate into our XGig product platform and cost synergies associated with integrating the operations of Data Transit with our Network Tools Division. The principal balance of the note issued in this acquisition bears interest at 8% per annum and is due and payable, if not sooner converted, on the second anniversary of its issuance. Generally, the terms of the convertible promissory note provide for automatic conversion of the outstanding principal and interest into shares of our common stock on a biweekly basis, commencing on the later of the effectiveness of a registration statement covering the resale of the shares or one year after the closing date. The conversion price is the average closing bid price of the stock for the three days preceding the date of conversion. The amount of principal and interest to be converted on each conversion date is based on the average trading volume of our common stock over the preceding 14 days. The acquisition was accounted for as a purchase and, accordingly, the results of operations of the acquired assets (beginning with the closing date of the acquisition) and the estimated fair value of assets acquired were included in our consolidated financial statements beginning in the second quarter of fiscal 2005.

Acquisition of Transceiver and Transponder Product Line From Infineon Technologies AG

On April 29, 2004, we entered into an agreement with Infineon Technologies AG to acquire Infineon s fiber optics business unit. On October 11, 2004, we entered into an amended purchase agreement under which the terms of the acquisition were modified. On January 25, 2005, we and Infineon terminated the amended purchase agreement and entered into a new agreement under which we acquired certain assets of Infineon s fiber optics business unit associated with the design, development and manufacture of optical transceiver and transponder products in exchange for 34 million shares of our common stock. The closing of the acquisition took place on January 31, 2005, the first day of our fourth quarter of fiscal 2005. The acquisition expanded our product offering and customer base for optical transceivers and transponders and expanded our portfolio of intellectual property used in designing and manufacturing these products as well as those to be developed in the future. The amount of goodwill recorded in this acquisition reflected the value to be realized associated with cost savings resulting from integrating these products with our Optical Subsystems and Components Division as well as the incremental growth in revenue and earnings from the sale of future products. We did not acquire any employees or assume any liabilities as part of the acquisition, except for obligations under customer contracts. The 34 million shares of our common stock issued to Infineon were valued at approximately $59.5 million based on the closing price of our common stock on January 31, 2005. The acquisition was accounted for as a purchase and, accordingly, the results of operations of the acquired assets (beginning with the closing date of the acquisition) and the estimated fair value of assets acquired were included in our consolidated financial statements beginning in the fourth quarter of fiscal 2005.

Acquisition of I-TECH CORP.

On April 8, 2005, we completed our acquisition of I-TECH CORP., a privately-held network test and monitoring company based in Eden Prairie, Minnesota. The acquisition expanded our product offering for testing and monitoring systems, particularly for systems relying on the Fibre Channel protocol, and expanded our portfolio of intellectual property used in designing and manufacturing these products as well as those to be developed in the future. The amount of goodwill recorded with this acquisition reflected the underlying patents and know-how used in manufacturing future products and cost synergies associated with integrating the operations of I-TECH with our Network Tools Division. The acquisition agreement provided for the merger of I-TECH with a wholly-owned subsidiary of Finisar and the issuance by Finisar to the sole holder of I-TECH s common stock of promissory notes in the aggregate principal amount of approximately $12.1 million. The

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notes are convertible into shares of Finisar common stock over a period of one year following the closing of the acquisition. The exact number of shares of Finisar common stock to be issued pursuant to the promissory notes is dependent on the trading price of Finisar s common stock on the dates of conversion of the notes. The results of operations of I-TECH (beginning with the closing date of the acquisition) and the estimated fair value of assets acquired were included in our consolidated financial statements beginning in the fourth quarter of fiscal 2005.

Acquisition of InterSAN, Inc.

On May 12, 2005, we completed the acquisition of InterSAN, Inc., a privately-held company located in Scotts Valley, California. Under the terms of the acquisition agreement, InterSAN merged with a wholly-owned subsidiary of Finisar and the holders of InterSAN s securities will be entitled to receive up to 7,132,186 shares of Finisar common stock having a value of approximately $8.8 million. Approximately 10% of the shares of Finisar common stock that would otherwise be distributed to the holders of InterSAN s securities at the closing of the acquisition were deposited into an escrow account for 12 months following the closing for the purpose of providing a fund against which Finisar may assert claims for damages, if any, based on breaches of the representations and warranties made by InterSAN in the agreement. The results of operations of InterSAN (beginning with the closing date of the acquisition) and the estimated fair value of assets acquired will be included in our consolidated financial statements beginning in the first quarter of fiscal 2006 ending July 31, 2005.

Critical Accounting Policies

The preparation of our financial statements and related disclosures require that we make estimates, assumptions and judgments that can have a significant impact on our net revenue and operating results, as well as on the value of certain assets, contingent assets and liabilities on our balance sheet. We believe that the estimates, assumptions and judgments involved in the accounting policies described below have the greatest potential impact on our financial statements and, therefore, consider these to be our critical accounting policies. See Note 1 to our consolidated financial statements included elsewhere in this prospectus for more information about these critical accounting policies, as well as a description of other significant accounting policies.

Revenue Recognition, Warranty and Sales Returns

Our revenue recognition policy follows SEC Staff Accounting Bulletin (SAB) No. 104, Revenue Recognition. Specifically, we recognize revenue when persuasive evidence of an arrangement exists, title and risk of loss have passed to the customer, generally upon shipment, the price is fixed or determinable and collectability is reasonably assured. For those arrangements with multiple elements, or in related arrangements with the same customer, we invoice and charge for each separate element and allocate revenue to the separate elements based upon each element s fair value as determined by the list price for each element.

At the time revenue is recognized, we establish an accrual for estimated warranty expenses associated with our sales, recorded as a component of cost of revenues. Our warranty period usually extends 12 months from the date of sale and our warranty accrual represents our best estimate of the amounts necessary to settle future and existing claims on products sold as of the balance sheet date. While we believe that our warranty accrual is adequate and that the judgment applied is appropriate, such amounts estimated to be due and payable could differ materially from what actually transpire in the future. If our actual warranty costs are greater than the accrual, costs of revenue will increase in the future. We also provide an allowance for estimated customer returns, which is netted against revenue. This provision is based on our historical returns, analysis of credit memo data and our return policies. If the historical data used by us to calculate the estimated sales returns does not properly reflect future returns, revenue could be overstated.

Allowance for Doubtful Accounts

We evaluate the collectability of our accounts receivable based on a combination of factors. In circumstances where, subsequent to delivery, we become aware of a customer s potential inability to meet its obligations, we record a specific allowance for the doubtful account to reduce the net recognized receivable to the amount we reasonably believe will be collected. For all other customers, we recognize an allowance for doubtful accounts based on the length of time the receivables are past due. A material adverse change in a major customer s ability to meet its financial obligations to us could result in a material reduction in the estimated amount of accounts receivable that can ultimately be collected and an increase in our general and administrative expenses for the shortfall.

Slow Moving and Obsolete Inventories

We make inventory commitment and purchase decisions based upon sales forecasts. To mitigate the component supply constraints that have existed in the past and to fill orders with non-standard configurations, we build inventory levels for certain items with long lead times and enter into certain longer-term commitments for certain items. We permanently write off 100% of the cost of inventory that we specifically identify and consider obsolete or excessive to fulfill future sales estimates. We define obsolete inventory as inventory that will no longer be used in the manufacturing process. We periodically discard obsolete inventory. Excess inventory is generally defined as inventory in excess of projected usage, and is determined using our best estimate of future demand at the time, based upon information then available to us. In making these assessments, we are required to make judgments as to the future demand for current or committed inventory levels. We use a 12-month demand forecast, and in addition to the demand forecast, we also consider:

- parts and subassemblies that can be used in alternative finished products;
- parts and subassemblies that are unlikely to be engineered out of our products; and
- known design changes which would reduce our ability to use the inventory as planned.

Significant differences between our estimates and judgments regarding future timing of product transitions, volume and mix of customer demand for our products and actual timing, volume and demand mix may result in additional write-offs in the future, or additional usage of previously written-off inventory in future periods for which we would benefit by a reduced cost of revenues in those future periods.

Investment in Equity Securities

For strategic reasons, we may make minority investments in private or public companies or extend loans or receive equity or debt from these companies for services rendered or assets sold. Our minority investments in private companies are primarily motivated by our desire to gain early access to new technology. Our investments in these companies are passive in nature in that we generally do not obtain representation on the boards of directors. Our investments have generally been part of a larger financing in which the terms were negotiated by other investors, typically venture capital investors. These investments are generally made in exchange for preferred stock with a liquidation preference that helps protect the underlying value of our investment. At the time we made our investments, in most cases the companies had not completed development of their products and we did not enter into any significant supply agreements with the companies in which we invested. In determining if and when a decline in the market value of these investments below their carrying value is other-than-temporary, we evaluate the market conditions, offering prices, trends of earnings and cash flows, price multiples, prospects for liquidity and other key measures of performance. Our policy is to recognize an impairment in the value of its minority equity investments when clear evidence of an impairment exists, such as (a) the completion of a new equity financing that may indicate a new value for the investment, (b) the failure to complete a new equity financing arrangement after seeking to raise additional funds or (c) the commencement of proceedings under which the assets of the business may be placed in receivership or liquidated to satisfy the claims of debt and equity stakeholders. As of April 30, 2005, the carrying value of these investments totaled $21.4 million. Future adverse changes in market conditions or poor operating results at any of the companies in which we hold a minority position could result in losses or an inability to recover the carrying value of these investments.

Restructuring Accrual

During the fiscal year ended April 30, 2003, we initiated actions to reduce our cost structure due to sustained negative economic conditions that had impacted our operations and resulted in lower than anticipated revenues. In May and October 2002, we reduced its workforce in the United States. The restructuring actions in fiscal 2003 resulted in a reduction in the U.S. workforce of approximately 255 employees, or 36% of our U.S. workforce measured as of the beginning of fiscal 2003, and affected all areas of our U.S. operations. During fiscal 2003, we sold certain assets and transferred certain liabilities of our subsidiary, Sensors Unlimited, Inc, closed our Hayward facility, and began the process of closing the facilities occupied by our subsidiary, Demeter Technologies, Inc. As facilities in the United States were consolidated, related leasehold improvement and equipment were written off. As a result of these restructuring activities, we incurred a charge of $9.4 million in fiscal 2003. The restructuring charge included approximately $5.4 million for the write-off of leasehold improvements and equipment in the vacated buildings, approximately $1.8 million of severance-related charges, approximately $1.5 million of excess committed facilities payments and approximately $700,000 of miscellaneous costs required to effect the closures.

During the first quarter of fiscal 2004, we completed the closure of our subsidiary, Demeter Technologies, Inc. In addition, we began closing our German operations and reducing the German workforce of approximately 10 employees engaged in research and development in the optical subsystems and components reporting segment. As a result of these restructuring activities, a charge of $2.2 million was incurred in the first quarter. The restructuring charge included $800,000 of severance-related charges, approximately $600,000 of fees associated with the early termination of our facilities lease in Germany, approximately $450,000 for remaining payments for excess leased equipment and approximately $300,000 of miscellaneous costs incurred to effect the closures.

During the second quarter of fiscal 2004, we completed the closure of our German facility. The intellectual property, technical know-how and certain assets related to our German operations were consolidated with our operations in Sunnyvale, California, during the second quarter. We incurred an additional $317,000 of net restructuring expenses in the second quarter. This amount included an additional $273,000 of restructuring expenses related to the closure of German operations, consisting of $373,000 for legal and exit fees associated with the closure, additional severance-related payments and the write-off of abandoned assets, partially offset by lower than anticipated fees associated with the termination of the German facilities lease of $100,000. The expenses related to the closure of the German facility were partially offset by an $85,000 reduction in restructuring expenses associated with the closure of our subsidiary, Demeter Technologies, Inc. offset by additional severance-related expenses.

During the third quarter of fiscal 2004, we realized a benefit of $1.2 million related to restructuring expenses due to lower than anticipated fees and the consequent reversal of an associated accrual from the termination of a purchasing agreement related to the closure of our subsidiary, Demeter Technologies, Inc.

During the fourth quarter of fiscal 2004, we realized a benefit of $791,000 related to restructuring expenses due to lower than anticipated lease and facility clean-up costs related to the closure of the Demeter facility.

The facilities consolidation charges were calculated using estimates and were based upon the remaining future lease commitments for vacated facilities from the date of facility consolidation, net of estimated future sublease income. The estimated costs of vacating these leased facilities were based on market information and trend analyses, including information obtained from third party real estate sources. We have engaged brokers to locate tenants to sublease the Hayward facility. As of April 30, 2005, $509,000 of committed facilities payments, net of anticipated sublease income, remains accrued and is expected to be fully utilized by fiscal 2006.

Goodwill, Purchased Intangibles and Other Long-Lived Assets

Our long-lived assets include significant investments in goodwill and other intangible assets. Under accounting standards in effect through April 30, 2002, we were required to make judgments about the recoverability of these assets whenever events or changes in circumstances indicated that the carrying value of these assets may be impaired or not recoverable. In order to make such judgments, we were required to make assumptions about the value of these assets in the future including future prospects for earnings and cash flows of the businesses underlying these investments. While we determined that no impairment was recorded or necessary during fiscal 2001 and 2002 under then applicable accounting standards, the judgments and assumptions we made about the future were complex, subjective and can be affected by a variety of factors including industry and economic trends, our market position and the competitive environment of the businesses in which we operate.

In June 2001, the Financial Accounting Standards Board, or FASB, issued Statement of Financial Accounting Standards, or SFAS 141 Business Combinations and SFAS 142 Goodwill and Other Intangible Assets. SFAS 141 requires business combinations initiated after June 30, 2001 to be accounted for using the purchase method of accounting. SFAS 141 also included guidance on the initial recognition and measurement of goodwill and other intangible assets arising from business combinations completed after June 30, 2001. SFAS 142 prohibits the amortization of goodwill and intangible assets with indefinite useful lives. SFAS 142 requires that these assets be reviewed for impairment at least annually. Intangible assets with finite lives will continue to be amortized over their estimated useful lives.

We applied SFAS 142 beginning in the first quarter of fiscal 2003. Application of the non-amortization provisions of SFAS 142 significantly reduced amortization expense, which included $123.7 million and $51.5 million of goodwill amortization for the fiscal years ended April 30, 2002 and 2001, respectively. We reclassified assembled workforce and customer base of $6.1 million to goodwill as required by SFAS 142 at the date of adoption. SFAS 142 also requires that goodwill be tested for impairment at the reporting unit level at adoption and at least annually thereafter, utilizing a two-step methodology. The initial step requires us to determine the fair value of each reporting unit and compare it to the carrying value, including goodwill, of such unit. We believe that we operate two reporting units, optical subsystems and components and network test and monitoring systems. If the fair value of the reporting unit exceeds the carrying value, no impairment loss would be recognized. However, if the carrying value of the reporting unit exceeds its fair value, the goodwill of the unit may be impaired. The amount, if any, of the impairment would then be measured in the second step.

In July 2002, we performed the required impairment testing of goodwill and indefinite-lived intangible assets. As a result of that testing, we incurred a transitional impairment charge of $460.6 million in the first quarter of fiscal 2003, representing substantially all of our goodwill attributable to our optical subsystems and components reporting unit as of April 30, 2002. The resulting impairment charge was reflected as the cumulative effect of a change in accounting principles in the first quarter of fiscal 2003. The largest portion of the transitional impairment charge arose from the acquisition of a number of companies designed to strengthen our capabilities within our optical subsystems and components business. The goodwill resulted from our acquisition of these companies when valuations were generally much higher than current levels. However, we made such acquisitions principally in exchange for shares of our common stock which were also more highly valued at the time the acquisitions were made. As a result, none of the transactions associated with the creation of a significant amount of goodwill resulted from a corresponding outlay of our cash. Had these transactions taken place when valuations were lower, and at the same share exchange ratios, the goodwill amounts would have been considerably smaller.

During the fourth quarters of fiscal 2003, 2004 and 2005, we performed the required annual impairment testing of goodwill and indefinite-lived intangible assets and determined that no impairment charge was required. At April 30, 2005 our investment in goodwill and intangible assets was $119.7 and $37.5 million, respectively.

We are required to make judgments about the recoverability of our long-lived assets, other than goodwill, whenever events or changes in circumstances indicate that the carrying value of these assets may be impaired or not recoverable. In order to make such judgments, we are required to make assumptions about the value of these assets in the future including future prospects for earnings and cash flows. If impairment is indicated, we write those assets down to their fair value which is generally determined based on discounted cash flows. Judgments and assumptions about the future are complex, subjective and can be affected by a variety of factors including industry and economic trends, our market position and the competitive environment of the businesses in which we operate.

During fiscal 2003, we discontinued a product line at our Demeter Technologies subsidiary that was not making a significant contribution to our operating results and was no longer considered a key part of our product strategy. The discontinued product line had been included in the optical subsystems and components segment. Certain assets of Demeter Technologies were sold to an unaffiliated party in conjunction with the product line discontinuation. As a result of the discontinuation of the product line, we determined that we would no longer utilize certain intangible assets obtained in the Demeter Technologies acquisition that were associated with that product line. We wrote off those intangible assets, with a net book value of $10.1 million and, the resulting charge was reported as an impairment of goodwill and intangible assets in fiscal 2003. During the second fiscal quarter of fiscal 2005, we determined that the remaining intangible assets related to certain purchased passive optical technology, acquired from New Focus, Inc., was obsolete, and had a fair value of zero. Accordingly an impairment charge of $3.7 million was recorded against the remaining net book value of these assets during the second quarter of fiscal 2005.

Results of Operations

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

	Fiscal Years Ended April 30,		
	2005	**2004**	**2003**
Revenues:			
Optical subsystems and components	86.0%	86.2%	82.2%
Network test and monitoring systems	14.0	13.8	17.8
Total revenues	100.0	100.0	100.0
Cost of revenues	73.2	77.4	78.4
Amortization of acquired developed technology	7.9	10.4	13.2
Impairment of acquired developed technology	1.4		
Gross profit	17.5	12.3	8.4
Operating expenses:			
Research and development	22.4	33.5	36.2
Sales and marketing	10.6	10.8	12.2
General and administrative	8.3	9.0	9.1
Amortization of (benefit from) deferred stock compensation	0.1	(0.1)	(1.0)
Acquired in-process research and development	0.6	3.3	
Amortization of purchased intangibles	0.4	0.3	0.5
Impairment of tangible assets	6.7		
Impairment of goodwill and intangible assets			6.4
Restructuring costs	0.1	0.2	5.6
Other acquisition costs		0.1	0.1
Total operating expenses	49.1	57.2	69.0

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	Fiscal Years Ended April 30,		
	2005	2004	2003
Loss from operations	(31.5)	(45.0)	(60.6)
Interest income, net	0.9	1.7	2.8
Interest expense, net	(5.2)	(15.6)	(6.8)
Other income (expense), net	(4.5)	(2.3)	(30.8)
Loss before income taxes and cumulative effect of an accounting change	(40.3)	(61.1)	(95.5)
Provision for income taxes	0.3	0.2	0.1
Loss before cumulative effect of an accounting change	(40.6)	(61.3)	(95.6)
Cumulative effect of an accounting change			(276.7)
Net loss	(40.6)%	(61.3)%	(372.3)%

Comparison of Fiscal Years Ended April 30, 2005 and 2004

Revenues. Revenues increased $95.2 million, or 51.3%, to $280.8 million in fiscal 2005 compared to $185.6 million in fiscal 2004. Sales of optical subsystems and components and network test and monitoring systems represented 86.0% and 14.0%, respectively, of total revenues in fiscal 2005, compared to 86.2% and 13.8%, respectively, in fiscal 2004.

Optical subsystems and components revenues increased $81.6 million, or 51.0%, to $241.6 million in fiscal 2005 compared to $160.0 million in fiscal 2004. Our Advanced Optical Components, or AOC, division, acquired on March 1, 2004 from Honeywell International Inc., contributed $30.9 million for the full 2005 fiscal year compared to $6.7 million in fiscal 2004. Our acquisition on January 31, 2005, of certain assets of Infineon s fiber optics business unit contributed $4.9 million in the fourth quarter of 2005. Excluding the effect of acquisitions, sales of optical subsystems and components increased $52.5 million, or 29%, in fiscal 2005. Of this increase, $36.1 million was related to sales of products for MAN and telecom applications and $19.3 million was related to sales of products for short distance LAN/ SAN applications. Increased sales in these product lines were partially offset by a $2.9 million decline in sales of other products. The increase in revenues from the sale of these products was primarily the result of an increase in the volume of units sold to new and existing customers, partially offset by a decrease in average selling prices.

Network test and monitoring systems revenues increased $13.6 million, or 53.3%, to $39.2 million in fiscal 2005 compared to $25.6 million in fiscal 2004. Approximately $7.8 million of the increase was related to product lines acquired from Data Transit in August 2004 with the remainder due to increased sales of new test and monitoring products used in the development of Fibre Channel SANs operating at 2 and 4 Gbps.

Sales to Cisco Systems, our largest customer, represented 27.8% of total revenues, or $78.1 million, in fiscal 2005 compared to 22.2% of total revenues, or $41.3 million, in fiscal 2004.

Amortization and Impairment of Acquired Developed Technology. Amortization of acquired developed technology, a component of cost of revenues, increased $6.7 million, or 34.7%, in fiscal 2005 to $25.9 million compared to $19.2 million in fiscal 2004. The increase was due to the acquisition of Honeywell s VCSEL Optical Products business in March 2004 which contributed an additional $3.0 million in fiscal 2005 compared to fiscal 2004, and the fiscal 2005 acquisitions of Data Transit, I-TECH and certain product lines from Infineon which contributed $1.0 million, $25,000 and $424,000, respectively in fiscal 2005. Additionally, in the second quarter of fiscal 2005 we recorded an impairment charge of $3.7 million to write-off the remaining net book value of certain passive optical technology associated with our acquisition of assets of New Focus, Inc in May 2002.

Gross Profit. Gross profit increased $26.5 million, or 116.1%, to $49.3 million in fiscal 2005 compared to $22.8 million in fiscal 2004. Gross profit as a percentage of total revenue was 17.5% in fiscal 2005 compared to 12.3% in fiscal 2004. We recorded charges of $11.3 million for obsolete and excess inventory in fiscal 2005 and $22.3 million in fiscal 2004. We sold inventory that was written-off in previous periods resulting in a benefit of $9.3 million in fiscal 2005 and $17.9 million in fiscal 2004. As a result, we recognized a net charge of $2.0 million in fiscal 2005 compared to $4.4 million in fiscal 2004. Excluding the amortization of acquired developed technology and the impairments thereon and the net impact of excess and obsolete inventory charges, gross profit would have been $77.2 million, or 27.5% of revenue, in fiscal 2005, compared to $46.4 million, or 25.0% of revenue in fiscal 2004. The increase in gross profit was primarily due to an increase in unit sales across most of our product lines, which spread our fixed overhead costs over a higher production volume, reduced material costs, and a favorable shift of product mix to an increased percentage of sales of products for longer distance MAN and telecom applications that typically have higher margins than our products for shorter distance LAN/ SAN applications, as well as increased sales of network test and monitoring systems that have higher margins than optical subsystems and components.

Research and Development Expenses. Research and development expenses increased $606,000, or 1.0%, to $62.8 million in fiscal 2005 compared to $62.2 million in fiscal 2004. The increase in research and development expenses was primarily due to a $3.8 million increase in spending as a result of our acquisition of Honeywell s VCSEL optical products business unit, partially offset by lower depreciation costs which were the result of accelerated depreciation recorded in conjunction with the shutdown of our operations at Demeter in the first quarter of 2004. Research and development expenses as a percent of revenues decreased to 22.4% in fiscal 2005 compared to 33.5% in fiscal 2004 as a result of increased revenues.

Sales and Marketing Expenses. Sales and marketing expenses increased $9.7 million, or 48.4%, to $29.8 million in fiscal 2005 compared to $20.1 million in fiscal 2004. The increase in sales and marketing expenses was primarily due to a $5.0 million increase in personnel-related costs, a $1.6 million increase in commission expense and a $1.3 million increase in advertising and marketing costs, all associated with our increase in revenue. Sales and marketing expenses as a percent of revenues decreased to 10.6% in fiscal 2005 compared to 10.8% in fiscal 2004.

General and Administrative Expenses. General and administrative expenses increased $6.6 million, or 39.6%, to $23.4 million in fiscal 2005 compared to $16.7 million in fiscal 2004. The increase was primarily due to additional costs associated with the evaluation and testing of internal control systems required under Section 404 of the Sarbanes-Oxley Act of 2002, a $2.2 million increase in audit fees, a $1.8 million increase in legal expense and a $554,000 increase in personnel-related costs primarily related to the acquisition of Honeywell s VCSEL Optical Products business unit. General and administrative expenses as a percent of revenues decreased to 8.3% in fiscal 2005 compared to 9.0% in fiscal 2004.

Amortization of (Benefit from) Deferred Stock Compensation. Amortization of deferred stock compensation costs increased by $267,000 to $162,000 in fiscal 2005, compared to a credit of $105,000 in fiscal 2004. The benefit from deferred stock compensation is related to the termination of employees during a period with deferred compensation associated with their stock options and the effects of the graded vested method of amortization which accelerates the amortization of deferred compensation.

Acquired In-process Research and Development. In-process research and development, or IPR&D, expenses decreased $4.6 million, or 74.8%, to $1.6 million in fiscal 2005 compared to $6.2 million recorded in fiscal 2004. In fiscal 2005, $318,000 was related to the acquisition of Data Transit, $1.1 million was related to the acquisition of Infineon s optical transceiver products, and $114,000 was related to the acquisition of I-TECH. The amount recorded in fiscal 2004 was related to the acquisition of Honeywell s VCSEL Optical Products business unit.

Amortization of Purchased Intangibles. Amortization of purchased intangibles increased $532,000, or 93.0%, to $1.1 million in fiscal 2005 compared to $572,000 in fiscal 2004. The increase was due to purchased intangibles related to our acquisition of Data Transit.

Impairment of Tangible Assets. During the quarter ended January 31, 2005, we recorded an impairment charge if $18.8 million to write down the carrying value of one of our corporate office facilities located in Sunnyvale, California upon entering into a sale-leaseback agreement. The property was written down to its appraised value, which was based on the work of an independent appraiser in conjunction with the sale-

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leaseback agreement. Due to retention by the Company of an option to acquire the leased properties at fair value at the end of the fifth year of the lease, the sale-leaseback transaction was recorded in the Company s fourth quarter ending April 30, 2005 as a financing transaction under which the sale will not be recorded until the option expires or is otherwise terminated. At April 30, 2005, the carrying value of the financing liability, included in Other Long-Term Liabilities, was $12.3 million and the current portion of the financing liability, included in Current Portion of Long-term Liabilities, was $200,000.

Restructuring Costs. We recorded a restructuring charge of $287,000 in fiscal 2005 to adjust the operating lease liability for our Hayward facility that was closed in fiscal 2003. During 2004, we recorded $382,000 in restructuring charges.

Interest Income. Interest income decreased $775,000, or 24.4%, to $2.4 million in fiscal 2005 compared to $3.2 million in fiscal 2004. The decrease was primarily the result of decreasing investment balances during fiscal 2005.

Interest Expense. Interest expense is primarily related to our convertible subordinated notes due in 2008 and 2010. Interest expense decreased $14.4 million, or 49.9%, to $14.5 million in fiscal 2005 compared to $28.9 million in fiscal 2004. The decrease was primarily due to the conversion and repurchase in fiscal 2004 of $24.8 million in principal amount of convertible notes due in 2008. In connection with the conversion, we recorded non-cash interest expense of $10.8 million representing the fair value of the incremental shares issued to induce the exchange and $5.8 million representing the remaining unamortized discount for the beneficial conversion feature. Of our total interest expense, $4.3 million and $10.2 million was the amortization of the beneficial conversion feature of these notes in fiscal 2005 and 2004, respectively.

Other Income (Expense), Net. Other income (expense), net, increased $8.2 million, or 189.4%, to an expense of $12.6 million in fiscal 2005 compared to an expense of $4.3 million in fiscal 2004. In the fourth quarter of fiscal 2005, we recorded an impairment charge of $10.0 million to write-off a minority equity investment in a company. The remaining expense in fiscal 2005 and 2004 primarily consisted of our proportional share of losses associated with a minority investment and amortization of subordinated loan costs.

Provision for Income Taxes. We recorded an income tax provision of $856,000 for fiscal 2005 compared to $334,000 for fiscal 2004. A deferred tax liability has been established to reflect tax amortization of goodwill for which no book amortization has occurred. Due to the uncertainty regarding the timing and extent of our future profitability, we have recorded a valuation allowance to offset potential income tax benefits associated with our operating losses. As a result, we did not record any income tax benefit in either fiscal 2005 or 2004. There can be no assurance that deferred tax assets subject to the valuation allowance will ever be realized.

Comparison of Fiscal Years Ended April 30, 2004 and 2003

Revenues. Revenues increased $19.1 million, or 11.5%, to $185.6 million in fiscal 2004 compared to $166.5 million in fiscal 2003. This increase reflected a $23.2 million, or 16.9%, increase in sales of optical subsystems and components, to $160.0 million in fiscal 2004 compared to $136.8 million in fiscal 2003, partially offset by a $4.0 million, or 13.6%, decrease in sales of network test and monitoring systems, to $25.6 million in fiscal 2004 compared to $29.6 million in fiscal 2003. Sales of optical subsystems and components and network test and monitoring systems represented 86.2% and 13.8%, respectively, of total revenues in fiscal 2004, compared to 82.2% and 17.8%, respectively, in fiscal 2003. The increase in revenues from the sale of optical subsystems and components in fiscal 2004 was primarily the result of an increase in volume of units sold to new and existing customers, as well as contributions of $6.7 million from sales by our Advanced Optical Components division, the former Honeywell VCSEL Optical Products business unit, that we acquired on March 2, 2004 from Honeywell International Inc., partially offset by a decrease in average selling prices. The decrease in revenues from the sale of network test and monitoring systems was due to decreased demand for new test equipment used in the development of Fibre Channel SANs operating at 2 Gbps and a continued reduction in global IT spending which affected the demand for equipment used in monitoring Gigabit Ethernet networks.

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Sales to Cisco Systems represented 22.2%, or $41.3 million, and 10.4%, or $17.2 million, of our total revenues during fiscal 2004 and fiscal 2003, respectively.

Amortization and Impairment of Acquired Developed Technology. Amortization of acquired developed technology decreased $2.7 million, or 12.5% in 2004 to $19.2 million compared to $22.0 million in 2003 as a result of a $10.1 million impairment charge for acquired developed technology that was recorded in 2003 related to a discontinued product line at our Demeter subsidiary.

Gross Profit. Gross profit increased $8.8 million, or 62.8%, to $22.8 million in fiscal 2004 compared to $14.0 million in fiscal 2003. Gross profit as a percentage of total revenue was 12.3% in 2004 compared to 8.4% in 2003. The increase in gross profit was primarily the result of a decline in the charge for excess and obsolete inventory, which was $22.3 million in 2004 compared to $24.3 million in 2003, which was offset by sales of previously written off inventory, with associated costs of zero, of $17.9 million in fiscal 2004 and $15.1 million in fiscal 2003. Gross profit also improved due to reductions in material costs, and an increase in unit sales which spread our fixed overhead costs over a higher production volume. Additionally, amortization of acquired developed technology, a component of cost of revenues, decreased $2.7 million, or 12.5%, in 2004 to $19.2 million compared to $22.0 million in 2003 as a result of a $10.1 million impairment charge for acquired developed technology that was recorded in 2003 related to a discontinued product line at our Demeter subsidiary.

Research and Development Expenses. Research and development expenses increased $1.9 million, or 3.1%, to $62.2 million in fiscal 2004 compared to $60.3 million in fiscal 2003. The increase was primarily due to the full-year effect of the operations of our Genoa Corporation subsidiary, acquired on April 3, 2003, offset by a 10% decline in personnel. Research and development expenses as a percent of revenues decreased to 33.5% in fiscal 2004 compared to 36.2% in fiscal 2003 as a result of increased revenues.

Sales and Marketing Expenses. Sales and marketing expenses decreased $169,000, or 0.8%, to $20.1 million in fiscal 2004 compared to $20.2 million in fiscal 2003. Sales and marketing expenses as a percent of revenues decreased to 10.8% in fiscal 2004 compared to 12.2% in fiscal 2003.

General and Administrative Expenses. General and administrative expenses increased $1.5 million, or 9.9%, to $16.7 million in fiscal 2004 compared to $15.2 million in fiscal 2003. The increase was primarily due to a $996,000 increase in bad debt expense and a $529,000 increase in legal expenses compared to those in fiscal 2003 as a result of increased efforts to obtain patents for and license our technology. The increase in bad debt expense was primarily due to the application of our existing reserve policy, which we periodically evaluate based on our actual experience, against a larger accounts receivable balance at the end of fiscal 2004. General and administrative expenses as a percent of revenues decreased to 9.0% in fiscal 2004 compared to 9.1% in fiscal 2003.

Amortization of (Benefit from) Deferred Stock Compensation. Amortization of deferred stock compensation costs decreased by $1.6 million, or 93.9%, to a credit of $105,000 in fiscal 2004 compared to a credit of $1.7 million in fiscal 2003. This decrease was related to the termination of employees with deferred compensation associated with their stock options and the effects of the graded vested method of amortization which accelerates the amortization of deferred compensation.

Acquired In-process Research and Development. In-process research and development, or IPR&D, expenses of $6.2 million recorded in fiscal 2004 related to the acquisition of the VCSEL Optical Products business unit from Honeywell in March 2004. There was no IPR&D expense in fiscal 2003 related to the acquisition of Genoa.

Amortization of Goodwill and Other Purchased Intangibles. Amortization of goodwill and other purchased intangibles decreased $186,000 or 24.5%, to $572,000 in fiscal 2004 compared to $758,000 in fiscal 2003.

Impairment of Goodwill and Intangible Assets. No impairment of goodwill or intangible assets was recorded during fiscal 2004. In fiscal 2003, we discontinued a product line at our Demeter subsidiary resulting in an impairment of acquired developed technology totaling $10.1 million and a goodwill impairment of $485,000 related to our Transwave acquisition.

Restructuring Costs. Restructuring costs decreased $9.0 million, or 95.9%, to $382,000 in fiscal 2004 compared to $9.4 million in fiscal 2003. During fiscal 2003, we recorded charges of $1.2 million for severance costs associated with a reduction in our U.S.-based workforce, $3.1 million to consolidate our facilities and operations located in Hayward, California into our facilities in Sunnyvale, California, and $5.2 million to close our El Monte, California, facilities. These restructuring activities were completed during fiscal 2004.

Other Acquisition Costs. Other acquisition costs increased $24,000, or 12.1%, to $222,000 in fiscal 2004 compared to $198,000 in fiscal 2003.

Interest Income. Interest income decreased $1.5 million, or 31.9%, to $3.2 million in fiscal 2004 compared to $4.7 million in fiscal 2003. The decrease in interest income was primarily the result of decreasing investment balances during fiscal 2004.

Interest Expense. Interest expense increased $17.5 million, or 153.5%, to $28.9 million in fiscal 2004 compared to $11.4 million in fiscal 2003. The increase in interest expense was primarily due to the conversion and repurchase of $24.8 million in principal amount of convertible notes due 2008. In connection with the conversion, we recorded non-cash interest expense of $10.8 million representing the fair value of the incremental shares issued to induce the exchange and $5.8 million representing the remaining unamortized discount for the beneficial conversion feature. Additionally, we issued an additional $150 million of convertible debt in October 2003. Of the total interest expense, $10.2 million and $4.8 million was related to the amortization of the beneficial conversion feature of these notes in fiscal 2004 and 2003, respectively.

Other Income (Expense), Net. Other income (expense), net, decreased $47.0 million, or 91.6%, to an expense of $4.3 million in fiscal 2004 compared to an expense of $51.3 million in fiscal 2003. In fiscal 2003, we incurred costs of $36.8 million associated with the sale of assets of our Sensors Unlimited subsidiary, which was primarily due to the write off of certain intangible assets associated with the original acquisition of Sensors Unlimited, which we had no plans to utilize and had abandoned, as well as the payment of contingent consideration related to the original acquisition of Sensors Unlimited. In fiscal 2003, we also recorded an impairment charge of $12.0 million on our minority equity investments in two companies. During fiscal 2003, these two companies raised additional funds in financings in which we declined to participate. As a result of the financings, our investments in the two companies was diluted to an immaterial interest and we determined that an impairment event had occurred and wrote off these investments in full.

Provision for Income Taxes. We recorded an income tax provision of $334,000 in fiscal 2004 compared to $229,000 in fiscal 2003. The tax provision consists of state and foreign taxes. Due to the uncertainty regarding the timing and extent of our future profitability, we have recorded a valuation allowance to offset potential income tax benefits associated with our operating losses. As a result, we had no income tax benefit in fiscal 2004 or 2003.

Liquidity and Capital Resources

At April 30, 2005, cash, cash equivalents and short-term investments were $102.4 million compared to $143.4 million at April 30, 2004. Restricted securities, used to secure future interest payments on our convertible debt were $9.1 million at April 30, 2005 compared to $15.2 million at April 30, 2004. At April 30, 2005, total short and long term debt was $267.8 million, compared to $233.7 million at April 30, 2004. Of the $34.1 million increase in debt, $32.1 million was related to the issuance of convertible notes in connection with the acquisitions of Data Transit and I-TECH and a minority investment in a private company.

Net cash used by operating activities totaled $28.0 million in fiscal 2005, compared to $32.8 million in fiscal 2004 and $18.9 million in fiscal 2003. The use of cash in operating activities in fiscal 2005 was primarily a result of operating losses adjusted for non-cash related items. Working capital uses of cash in fiscal 2005 included cash inflows of $10.9 million offset by outflows of $18.6 million. Cash inflows were primarily due to a $5.3 million increase in deferred revenue and a $1.9 million increase in accrued liabilities. The increase in deferred revenue was the result of increased sales through distributor channels. The increase in accrued

liabilities was primarily due to an increase in our warranty reserve as a result of increased revenues. Cash outflows were primarily due to a $13.3 million increase in accounts receivable as a result of increased revenue and an increase in other assets of $5.3 million, which consisted primarily of investments in our patent portfolio.

Net cash used in investing activities totaled $27.9 million in fiscal 2005 compared to $88.3 million in fiscal 2004, and $17.6 million in fiscal 2003. The use of cash for investing activities in fiscal 2005 was primarily related to facility improvements and purchases of equipment at our new AOC Division manufacturing facility in Texas as well as purchases of equipment for our facility in Malaysia to support increased production volume. The use of cash for investing activities in fiscal 2004 consisted primarily of our purchase of the assets of Honeywell s VCSEL Optical Products business unit and purchases of equipment to support increased production volume in our Malaysian manufacturing facility. The use of cash for investing activities in fiscal 2003 primarily consisted of purchases of plant, property and equipment totaling $18.8 million, offset in part by $5.6 million of proceeds from the sale of product lines.

Net cash provided by financing activities was $15.5 million in fiscal 2005 compared to $150.0 million in fiscal 2004 and $1.5 million in fiscal 2003. Cash provided by financing activities in fiscal 2005 included $12.9 million in proceeds from the sale-leaseback of one of our corporate offices and proceeds of $2.5 million from the exercise of stock options. Cash provided by financing activities in fiscal 2004 primarily represented the net proceeds of $145.1 million from issuance of convertible debt, and proceeds of $6.1 million from the exercise of employee stock options, offset by repayments of $1.9 million on our convertible notes. Cash provided by financing activities in fiscal 2003 was primarily due to proceeds from the exercise of employee stock options.

On April 29, 2005, we entered into a letter of credit reimbursement agreement with Silicon Valley Bank for a period of one year. Under the terms of the agreement, Silicon Valley Bank is providing a $7 million letter of credit facility to house existing letters of credit issued by Silicon Valley Bank and any other letters of credit that may be required by the Company. Cost related to the credit facility consisted of a loan fee of 0.50% of the credit facility amount, or $35,000, plus the bank s out of pocket expenses associated with the credit facility. The credit facility is unsecured with a negative pledge on all assets, including intellectual property. The agreement requires us to maintain our primary banking and cash management relationships with Silicon Valley Bank or SVB Securities and to maintain a minimum unrestricted cash and cash equivalents balance, net of any outstanding debt and letters of credit exposure, of $40 million at all times. At April 30, 2005 outstanding letters of credit secured by this facility totaled $2,950,510.

We believe that our existing balances of cash, cash equivalents and short-term investments, together with the cash expected to be generated from our future operations, will be sufficient to meet our cash needs for working capital and capital expenditures for at least the next 12 months. We may however require additional financing to fund our operations in the future. The significant contraction in the capital markets, particularly in the technology sector, may make it difficult for us to raise additional capital if and when it is required, especially if we experience disappointing operating results. If adequate capital is not available to us as required, or is not available on favorable terms, our business, financial condition and results of operations will be adversely affected.

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At April 30, 2005, we had contractual obligations of $350.1 million as shown in the following table (in thousands):

			Payments Due by Period		
Contractual Obligations	Total	Less Than 1 Year	1-3 Years	4-5 Years	After 5 Years
Short-term debt	$ 15,811	$ 15,811	$	$	$
Long-term debt	266,520		16,270	100,250	150,000
Lease commitment under sale-leaseback agreement	51,464	2,962	6,124	6,403	35,975
Operating leases	7,865	4,814	2,420	631	
Purchase obligations	6,449	6,449			
Minimum royalty obligation	2,000	2,000			
Total contractual obligations	$ 350,109	$ 32,036	$ 24,814	$ 107,284	$ 185,975

Short-term debt consists of a convertible promissory note for $12.1 million due in fiscal 2006, related to our fiscal 2005 acquisition of I-TECH, and a convertible promissory note for $3.75 million to CyOptics, issued in conjunction with our purchase of CyOptics preferred stock in the fourth quarter of fiscal 2005. (See note 13 to the consolidated financial statements included elsewhere in this prospectus.)

Long-term debt consists of a convertible promissory note in the principal amount of $16.3 million due on August 6, 2006, if not sooner converted, and two series of convertible subordinated notes in the aggregate principal amount of $100.3 million due October 15, 2008, and $150.0 million due October 15, 2010. The two series of notes are convertible by the holders of the notes at any time prior to maturity into shares of Finisar common stock at specified conversion prices. The two series of notes are redeemable by us, in whole or in part, after October 15, 2004 and October 15, 2007, respectively. Holders of the notes due in 2010 have the right to require us to repurchase some or all of their notes on October 15, 2007. We may choose to pay the repurchase price in cash, shares of Finisar common stock, or a combination thereof.

Lease commitment under the sale-leaseback agreement for our corporate office building, which we entered into in the fourth quarter of 2005 and includes $12.6 million recorded on our balance sheet as of April 30, 2005 as other long-term liabilities and current portion of long-term liabilities. (See Note 9 to the consolidated financial statements included elsewhere in this prospectus.)

Operating lease obligations consist primarily of base rents for facilities we occupy at various locations.

Purchase obligations consist of standby repurchase obligations and are related to materials purchased and held by subcontractors on our behalf to fulfill the subcontractors purchase order obligations at their facilities. Our repurchase obligations of $6.5 million has been expensed and recorded on the balance sheet as non-cancelable purchase obligations as of April 30, 2005.

The minimum commitment for royalty payments is related to the purchase of certain assets of New Focus and has been recorded on our balance sheet as of April 30, 2005 as current portion of long-term liabilities.

Off-Balance-Sheet Arrangements

At April 30, 2005 and April 30, 2004, we did not have any off-balance sheet arrangements or relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which are typically established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

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Effect of New Accounting Standards

In December 2004, the Financial Accounting Standards Board (FASB) issued Statement of Accounting Standards (SFAS) 123R, which replaces SFAS 123 and supersedes Accounting Principles Board (APB) 25. As permitted by SFAS 123, the Company currently accounts for share-based payments to employees using APB 25 s intrinsic value method. Under APB 25 the Company generally recognizes no compensation expense for employee stock options, as the exercise prices of the options granted are usually equal to the quoted market price of our common stock on the day of the grant. SFAS 123R requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values. The pro forma disclosures previously permitted under SFAS 123 will no longer be an alternative to financial statement recognition. In April 2005, the Securities and Exchange Commission (SEC) issued a rule delaying the required adoption date for SFAS 123R to the first interim period of the first fiscal year beginning on or after June 15, 2005. The Company will adopt SFAS 123R as of May 1, 2006.

Under SFAS 123R, we must determine the appropriate fair value model to be used for valuing share-based payments, the amortization method of compensation cost and the transition method to be used at date of adoption. The transition methods include retroactive and prospective adoption options. The prospective method requires that compensation expense be recorded for all unvested stock options and restricted stock at the beginning of the first quarter of adoption. The retroactive method requires that compensation expense for all unvested stock options and restricted stock begins with the first period restated. Under the retroactive option, prior periods may be restated either as of the beginning of the year of adoption or for all periods presented. We expect to adopt SFAS 123R under the prospective method. We are evaluating the requirements of SFAS 123R and have not yet determined the effect of adopting SFAS 123R or whether the adoption will result in amounts that are similar to the current pro forma disclosures under SFAS 123, although we expect that the adoption of SFAS 123R will result in significant stock-based compensation expense.

In December 2004, the FASB issued SFAS 153, Exchanges of Nonmonetary Assets, as an amendment of APB 29, Accounting for Nonmonetary Transactions. SFAS 153 addresses the measurement of exchanges of nonmonetary assets and eliminates the exception from fair value measurement for nonmonetary exchanges of similar productive assets in APB 29 and replaces it with an exception for exchanges that do not have commercial substance. This Statement specifies that a nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. The provisions of this Statement are effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005 and must be applied prospectively. The Company do not expect that the adoption of SFAS 153 will have a material effect on our results of operations.

In November 2004, the FASB issued SFAS No. 151, Inventory Costs an Amendment of APB No. 43, Chapter 4, or SFAS 151, which is the result of the FASB s efforts to converge U.S. accounting standards for inventory with International Accounting Standards. SFAS 151 requires abnormal amounts of idle facility expense, freight, handling costs, and wasted material to be recognized as current-period charges. It also requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. SFAS 151 is effective for inventory costs incurred during fiscal years beginning after June 15, 2005. The Company does not expect the adoption of SFAS 151 to have a material impact on our results of operations.

Quantitative and Qualitative Disclosures About Market Risk

Our exposure to market risk for changes in interest rates relates primarily to our investment portfolio. The primary objective of our investment activities is to preserve principal while maximizing yields without significantly increasing risk. We place our investments with high credit issuers in short-term securities with maturities ranging from overnight up to 36 months or have characteristics of such short-term investments. The average maturity of the portfolio will not exceed 18 months. The portfolio includes only marketable securities with active secondary or resale markets to ensure portfolio liquidity. We have no investments denominated in foreign country currencies and therefore our investments are not subject to foreign exchange risk.

We invest in equity instruments of privately-held companies for business and strategic purposes. These investments are included in other long-term assets and are accounted for under the cost method when our ownership interest is less than 20% and we do not have the ability to exercise significant influence. For entities in which we hold greater than a 20% ownership interest, or where we have the ability to exercise significant influence, we use the equity method. We recorded losses of $1.8 million in fiscal 2005, $1.3 million in fiscal 2004 and $764,000 in fiscal 2003 for investments accounted for under the equity method. For these non-quoted investments, our policy is to regularly review the assumptions underlying the operating performance and cash flow forecasts in assessing the carrying values. We identify and record impairment losses when events and circumstances indicate that such assets are impaired. We recognized impairment on these assets of $10.0 million in fiscal 2005, $1.6 million in fiscal 2004 and $12.0 million in fiscal 2003. If our investment in a privately-held company becomes marketable equity securities upon the company s completion of an initial public offering or its acquisition by another company, our investment would be subject to significant fluctuations in fair market value due to the volatility of the stock market.

The following table summarizes the expected maturity, average interest rate and fair market value of the short-term debt securities held by us (and related receivables) and debt securities issued by us as of April 30, 2005 (in thousands):

	Fiscal Years Ended April 30,				
	2006	**2007**	**2008 and Thereafter**	**Total Cost**	**Fair Market Value**
Assets					
Available for sale debt securities	$ 51,364	$ 18,312	$ 10,517	$ 80,193	$ 79,697
Average interest rate	2.90%	4.01%	4.24%		
Restricted securities	$ 3,717	$ 5,393	$	$ 9,110	$ 8,967
Average interest rate	1.59%	2.36%			
Loan receivable from I-TECH	$ 2,004	$	$	$ 2,004	$ 2,004
Average interest rate	3.35%				
Loan receivable from Data Transit	$ 1,000	$	$	$ 1,000	$ 1,000
Average interest rate	8.00%				
Liabilities					
Long-term debt:					
Fixed rate	$	$	$ 100,250	$ 100,250	$ 89,974
Average interest rate			5.25%		