

3COM CORP
Form 10-Q
April 08, 2008

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q**

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

For the quarterly period ended February 29, 2008

OR

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

For the transition period from to

Commission File No. 0-12867

**3COM CORPORATION
(Exact name of registrant as specified in its charter)**

Delaware

94-2605794

(State or other jurisdiction of
incorporation or organization)

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

**350 Campus Drive
Marlborough, Massachusetts**

01752

(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including area code: **(508) 323-1000**

Former name, former address and former fiscal year, if changed since last report: **N/A**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting
company

(Do not check if a smaller
reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

As of March 28, 2008, 403,179,447 shares of the registrant's common stock were outstanding.

3COM CORPORATION
QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTER ENDED FEBRUARY 28, 2008
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We use a 52 or 53 week fiscal year ending on the Friday nearest to May 31, with each fiscal quarter ending on the Friday generally nearest August 31, November 30 and February 28. For presentation purposes, the periods are shown as ending on August 31, November 30, February 28 and May 31, as applicable. H3C follows a calendar year basis of reporting and therefore results are consolidated on a two-month time lag.

3Com, the 3Com logo, Digital Vaccine, NBX, TippingPoint Technologies, and TippingPoint are registered trademarks and VCX is a trademark of 3Com Corporation or its subsidiaries. H3C is a trademark of H3C Technologies Co., Limited. Other product and brand names may be trademarks or registered trademarks of their respective owners.

This quarterly report on Form 10-Q contains forward-looking statements made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include, without limitation, predictions regarding the following aspects of our future: future growth; future growth of H3C, including strategy, growth, management of growth, dependence, expected benefits, method of consolidation, PRC tax rate and dividend tax, sales from China, and resources needed to comply with Sarbanes-Oxley and manage operations; impact of SFAS No. 123(R) and other accounting regulations; expected annual amortization expense; TippingPoint strategy; environment for enterprise networking equipment; challenges relating to sales growth; supply of components; trend towards Gigabit products; research and development focus; characteristics of IPS and certain H3C products; future sales of connectivity products; re-assessment, development and execution of our go-to-market strategy; strategic product and technology development plans; management of DVBU and Corporate segments to reach sustained profitability; goal of profitability; dependence on China; ability to satisfy cash requirements for at least the next twelve months; restructuring activities and expected charges to be incurred; potential additional restructuring and cost

reduction activities; expected cost savings from restructuring activities and integration; potential acquisitions and strategic relationships including matters relating to our announced proposed acquisition by an entity controlled by affiliates of Bain Capital Partners; future contractual obligations; recovery of deferred tax assets; adjustments to tax benefits; reserves; market risk; outsourcing; competition and pricing pressures; and effect of litigation. You can identify these and other forward-looking statements by the use of words such as may, can, should, expects, plans, anticipates, believes, estimates, predicts, intends, continue, or the negative of such terms, or other comparable terminology. Forward-looking statements also include the assumptions underlying or relating to any forward-looking statements.

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Actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors, including those set forth under Part II Item 1A Risk Factors. All forward-looking statements included in this document are based on our assessment of information available to us at the time this report is filed. We have no intent, and disclaim any obligation, to update any forward-looking statements.

In this Form 10-Q we refer to the People's Republic of China as China or the PRC.

Table of Contents**PART I. FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****3COM CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

(Unaudited)

(In thousands, except per share data)	Three Months Ended		Nine Months Ended	
	February 28,		February 28,	
	2008	2007	2008	2007
Sales	\$ 336,390	\$ 323,441	\$ 973,625	\$ 956,561
Cost of sales	156,716	170,004	492,895	516,544
Gross profit	179,674	153,437	480,730	440,017
Operating expenses:				
Sales and marketing	82,428	77,338	237,617	230,648
Research and development	50,530	48,419	155,039	144,363
General and administrative	26,268	22,466	78,806	65,083
Amortization	25,778	10,228	78,044	34,630
In-process research and development		1,700		1,700
Restructuring charges	736	2,221	4,308	2,776
Total operating expenses	185,740	162,372	553,814	479,200
Operating loss	(6,066)	(8,935)	(73,084)	(39,183)
Gain (loss) on investments, net	23	(582)	351	799
Interest (expense) income, net	(2,879)	11,265	(10,412)	32,802
Other income, net	10,568	9,637	32,994	26,971
Income (loss) before income taxes and minority interest	1,646	11,385	(50,151)	21,389
Income tax provision	(9,486)	(1,374)	(11,967)	(5,047)
Minority interest in income of consolidated joint venture		(14,790)		(38,705)
Net loss	\$ (7,840)	\$ (4,779)	\$ (62,118)	\$ (22,363)
Basic and diluted net loss per share	\$ (0.02)	\$ (0.01)	\$ (0.16)	\$ (0.06)
Shares used in computing per share amounts:				
Basic and diluted	400,142	394,351	398,724	393,196

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

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CONDENSED CONSOLIDATED BALANCE SHEETS**

(Unaudited)

(In thousands, except per share data)	February 28, 2008	May 31, 2007
ASSETS		
Current assets:		
Cash and equivalents	\$ 466,030	\$ 559,217
Notes receivable	106,595	77,368
Accounts receivable, less allowance for doubtful accounts of \$12,788 and \$15,292 respectively	142,309	102,952
Inventories	93,850	107,988
Other current assets	46,601	50,157
Total current assets	855,385	897,682
Property and equipment, less accumulated depreciation and amortization of \$197,947 and \$234,554 respectively	56,766	76,460
Goodwill	767,274	766,444
Intangible assets, net	300,307	371,289
Deposits and other assets	26,757	39,217
Total assets	\$ 2,006,489	\$ 2,151,092
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	\$ 104,489	\$ 110,430
Current portion of long-term debt	48,000	94,000
Accrued liabilities and other	414,693	435,638
Total current liabilities	567,182	640,068
Deferred taxes and long-term obligations	16,839	23,725
Long-term debt	288,000	336,000
Stockholders' equity:		
Preferred stock, \$0.01 par value, 10,000 shares authorized; none outstanding		
Common stock, \$0.01 par value, 990,000 shares authorized; shares issued: 402,913 and 399,064 respectively	2,342,574	2,323,356
Retained earnings (deficit)	(1,238,526)	(1,176,406)
Accumulated other comprehensive income	30,420	4,349
Total stockholders' equity	1,134,468	1,151,299
Total liabilities and stockholders' equity	\$ 2,006,489	\$ 2,151,092

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

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3COM CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

(In thousands)	Nine Months Ended	
	February 28,	
	2008	2007
Cash flows from operating activities:		
Net loss	\$ (62,118)	\$ (22,363)
Adjustments to reconcile net loss to cash used in operating activities:		
Depreciation and amortization	102,731	58,255
Stock-based compensation charges	15,413	15,133
Loss (gain) on property and equipment disposals	2,227	(10,898)
In-process research and development		1,700
Gain on investments, net	(185)	(1,476)
Minority interest in income of consolidated joint venture		38,705
Deferred income taxes	(448)	(8,836)
Changes in assets and liabilities:		
Accounts receivable	(59,344)	(12,392)
Inventories	22,704	23,754
Other assets	7,733	31,689
Accounts payable	(13,447)	(28,098)
Other liabilities	(25,297)	9,682
Net cash (used in) provided by operating activities	(10,031)	94,855
Cash flows from investing activities:		
Purchases of investments		(225,005)
Proceeds from maturities and sales of investments	442	495,941
Purchases of property and equipment	(13,269)	(24,152)
Business acquired in purchase transactions, net of cash acquired		(7,830)
Proceeds from sale of property and equipment	944	33,111
Net cash (used in) provided by investing activities	(11,883)	272,065
Cash flows from financing activities:		
Issuances of common stock	6,124	13,088
Repurchases of common stock	(2,321)	(4,788)
Repayment of long term debt	(94,000)	
Dividend paid to minority interest shareholder		(40,785)
Net cash used in financing activities	(90,197)	(32,485)
Effect of exchange rate changes on cash and equivalents	18,924	7,229
Net change in cash and equivalents during period	(93,187)	341,664

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Cash and equivalents, beginning of period	559,217	501,097
Cash and equivalents, end of period	\$ 466,030	\$ 842,761

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

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(Unaudited)

NOTE 1. BASIS OF PRESENTATION

The unaudited condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. In the opinion of management, these unaudited condensed consolidated financial statements include all adjustments necessary for a fair presentation of our financial position as of February 29, 2008 and June 1, 2007, our results of operations for the three and nine months ended February 29, 2008 and March 2, 2007 and our cash flows for the nine months ended February 29, 2008 and March 2, 2007.

We use a 52 or 53 week fiscal year ending on the Friday nearest to May 31. For convenience, the condensed consolidated financial statements have been shown as ending on the last day of the calendar month. Accordingly, the three months shown as ended February 28, 2008 actually ended on February 29, 2008, the three months shown as ended February 28, 2007 actually ended on March 2, 2007, and the year shown as ended May 31, 2007 actually ended on June 1, 2007. The results of operations for the three and nine months ended February 28, 2008 may not be indicative of the results to be expected for the fiscal year ending May 30, 2008 or any other future periods. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes thereto included in our Annual Report on Form 10-K for the year ended June 1, 2007.

In June 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109* (FIN 48). The interpretation requires companies to recognize the tax benefits of uncertain tax positions only where the position is more likely than not to be sustained upon examination by tax authorities. The amount recognized would be the amount that represents the largest amount of tax benefit that is greater than 50 percent likely of being ultimately realized. A liability would be recognized for any benefit claimed, or expected to be claimed, in a tax return in excess of the benefit recorded in the financial statements, along with any interest and penalty on the excess. FIN 48 requires, among other items, a tabular reconciliation of the change during the reporting period, in the aggregate unrecognized tax benefits claimed or expected to be claimed in tax returns and disclosure relating to accrued interest and penalties for unrecognized tax benefits. Additional disclosure will also be required for those uncertain tax positions where it is reasonably possible that the estimate of the tax benefit will change significantly in the next twelve months. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company adopted FIN 48 as of June 2, 2007. See Note 5 Income Taxes.

Recently issued accounting pronouncements

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements (SFAS No. 157). SFAS No. 157 clarifies the principle that fair value should be based on the assumptions market participants would use when pricing an asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. Under the standard, fair value measurements would be separately disclosed by level within the fair value hierarchy. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007 and is required to be adopted by 3Com in the first quarter of fiscal 2009 but was amended on February 6, 2008 to defer the effective date one year for certain nonfinancial assets and liabilities. We have not yet determined the impact, if any, that the implementation of SFAS No. 157 will have on our results of operations or financial condition.

In September 2006, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin 108

Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements , which expresses the staff's views regarding the process of quantifying financial statement misstatements. The Bulletin is effective at our fiscal year end, May 30, 2008. The Company currently believes the adoption will have no impact on our results of operations, cash flow or financial position.

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In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115 (SFAS 159)*. SFAS 159 expands the use of fair value accounting but does not affect existing standards which require assets or liabilities to be carried at fair value. Under SFAS 159, a company may elect to use fair value to measure accounts and loans receivable, available-for-sale and held-to-maturity securities, equity method investments, accounts payable, guarantees and issued debt. Other eligible items include firm commitments for financial instruments that otherwise would not be recognized at inception and non-cash warranty obligations where a warrantor is permitted to pay a third party to provide the warranty goods or services. If the use of fair value is elected, any upfront costs and fees related to the item must be recognized in earnings and cannot be deferred, e.g., debt issue costs. The fair value election is irrevocable and generally made on an instrument-by-instrument basis, even if a company has similar instruments that it elects not to measure based on fair value. At the adoption date, unrealized gains and losses on existing items for which fair value has been elected are reported as a cumulative adjustment to beginning retained earnings. Subsequent to the adoption of SFAS 159, changes in fair value are recognized in earnings. SFAS 159 is effective for fiscal years beginning after November 15, 2007 and is required to be adopted by 3Com in the first quarter of fiscal 2009. 3Com currently is determining whether fair value accounting is appropriate for any of its eligible items and cannot estimate the impact, if any, which SFAS 159 will have on its consolidated results of operations and financial condition.

In June 2007, the FASB ratified EITF 07-3, *Accounting for NonRefundable Advance Payments for Goods or Services Received for Use in Future Research and Development Activities (EITF 07-3)*. EITF 07-3 requires that nonrefundable advance payments for goods or services that will be used or rendered for future research and development activities be deferred and capitalized and recognized as an expense as the goods are delivered or the related services are performed. EITF 07-3 is effective, on a prospective basis, for fiscal years beginning after December 15, 2007 and will be adopted in the first quarter of fiscal 2009. The Company is currently evaluating the impact, if any, of the pending adoption of EITF 07-3 on its consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141R, *Business Combinations* to improve reporting and to create greater consistency in the accounting and financial reporting of business combinations. The standard requires the acquiring entity in a business combination to recognize all (and only) the assets acquired and liabilities assumed in the transaction; establishes the acquisition-date fair value as the measurement objective for all assets acquired and liabilities assumed; and requires the acquirer to disclose to investors and other users all of the information they need to evaluate and understand the nature and financial effect of the business combination. SFAS No. 141R applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008, with the exception of the accounting for valuation allowances on deferred taxes and acquired tax contingencies. SFAS 141R amends SFAS 109, such that adjustments made to valuation allowances on deferred income taxes and acquired income tax contingencies associated with acquisitions that closed prior to the effective date of SFAS 141R would apply the provisions of SFAS 141R. An entity may not apply SFAS 141R before that date. Given SFAS 141R relates to prospective business combinations, the Company has currently not determined the potential effects on the consolidated financial statements.

In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements* to improve the relevance, comparability, and transparency of financial information provided to investors by requiring all entities to report noncontrolling (minority) interests in subsidiaries in the same way as required in the consolidated financial statements. Moreover, SFAS No. 160 eliminates the diversity that currently exists in accounting for transactions between an entity and noncontrolling interests by requiring that they be treated as equity transactions. SFAS No. 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. Earlier adoption is prohibited. The Company is currently evaluating whether the adoption of SFAS No. 160 will have a significant effect on its consolidated financial position, results of operations or cash flows.

On March 19, 2008, the FASB issued FASB Statement No. 161, *Disclosures about Derivative Instruments and Hedging Activities* an Amendment of FASB Statement 133. Statement 161 enhances required disclosures regarding derivatives and hedging activities, including enhanced disclosures regarding how: (a) an entity uses derivative instruments; (b) derivative instruments and related hedged items are accounted for under FASB Statement No.133,

Accounting for Derivative Instruments and Hedging Activities; and (c) derivative instruments and related hedged

items affect an entity's financial position, financial performance, and cash flows. Statement 161 is effective for fiscal years and interim periods beginning after November 15, 2008. The Company has currently not determined the potential effects on the consolidated financial statements.

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In order to determine the fair value of stock options and employee stock purchase plan shares, we use the Black-Scholes option pricing model and apply the single-option valuation approach to the stock option valuation. In order to determine the fair value of restricted stock awards and restricted stock units we use the closing market price of 3Com common stock on the date of grant. We recognize stock-based compensation expense on a straight-line basis over the requisite service period of the awards for options granted following the adoption of SFAS No. 123(R) for time vested awards. We recognize compensation expense for performance based restricted stock in the fiscal quarter when an event makes it probable that performance will more than likely be achieved. For unvested stock options outstanding as of May 31, 2006, we will continue to recognize stock-based compensation expense using the accelerated amortization method prescribed in FASB Interpretation No. 28, Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans .

As of February 28, 2008, total unrecognized stock-based compensation expense relating to unvested employee stock options, restricted stock and employee stock purchase plan, adjusted for estimated forfeitures, was \$15.1 million, \$18.3 million and \$0.2 million, respectively. These amounts are expected to be recognized over a weighted-average period of 2.3 years for stock options, 1.9 years for restricted stock and .08 years for employee stock purchase plan. If actual forfeitures differ from current estimates, total unrecognized stock-based compensation expense will be adjusted for future changes in estimated forfeitures.

Stock-based compensation recognized and disclosed uses the Black-Scholes option pricing model for estimating the fair value of options granted under the company's equity incentive plans. The Black-Scholes option pricing model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. Option valuation models require the input of highly subjective assumptions, including the expected stock price volatility. The underlying weighted-average assumptions used in the Black-Scholes model and the resulting estimates of fair value per share were as follows for options granted during the nine months ended February 28, 2008 and the three and nine months ended February 28, 2007 (There were no option grants, restricted stock awards, restricted stock units or employee stock purchase plan grants in the three months ended February 28, 2008):

	Three Months Ended February 28, 2007	Nine Months Ended February 28, 2008	Nine Months Ended February 28, 2007
<i>Employee stock options:</i>			
Volatility	41.8%	40.5%	41.8%
Risk-free interest rate	4.7%	4.7%	4.7%
Dividend yield	0.0%	0.0%	0.0%
Expected life (years)	4.0	3.8	4.0
Weighted average fair value per grant	\$ 1.59	\$ 1.49	\$ 1.67
<i>Employee Stock Purchase Plan:</i>			
Volatility	49.2%	61.1%	49.2%
Risk-free interest rate	5.1%	4.0%	5.1%
Dividend yield	0.0%	0.0%	0.0%
Expected life (years)	0.5	0.5	0.5
Weighted average fair value per grant	\$ 1.27	\$ 1.60	\$ 1.27

Restricted Stock Awards:

Weighted average fair value per grant	*	\$ 3.90	\$ 4.45
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Restricted Stock Units:

Weighted average fair value per grant	\$ 4.12	\$ 3.72	\$ 4.43
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* *No grants
during the
period.*

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The following table presents stock-based compensation expenses included in the accompanying consolidated statements of operations (in thousands):

	Three Months Ended February 28, 2008	Three Months Ended February 28, 2007	Nine Months Ended February 28, 2008	Nine Months Ended February 28, 2007
Cost of sales	\$ 496	\$ 418	\$ 1,403	\$ 1,119
Sales and marketing	1,753	1,553	4,146	4,358
Research and development	1,100	1,060	2,794	3,774
General and administrative	2,195	1,865	7,070	5,882
Stock-based compensation expense before tax	\$5,544	\$ 4,896	\$ 15,413	\$ 15,133

Stock Options. As of February 28, 2008, our outstanding stock options as a percentage of outstanding shares were approximately 12 percent. Stock option detail as of February 28, 2008, was as follows (shares in thousands):

	Number of shares	Weighted average exercise price
Outstanding May 31, 2007	52,280	\$ 5.23
Granted	1,455	4.08
Exercised	(1,800)	2.12
Cancelled	(5,639)	5.97
Outstanding February 28, 2008	46,296	\$ 5.23
Exercisable	25,307	\$ 5.76
Weighted average grant-date fair value of options granted		\$ 1.49

During the nine months ended February 28, 2008 approximately 1.8 million options were exercised with an aggregate intrinsic value of \$4.6 million. The intrinsic value is calculated as the difference between the exercise date market value and the exercise price of the options. The aggregate intrinsic value of in-the-money options outstanding and options exercisable as of February 28, 2008 was \$4.9 million and \$4.7 million, respectively. The intrinsic value is calculated as the difference between the market value as of February 29, 2008 and the exercise price of the options. The closing market value as of February 29, 2008 was \$3.29 per share as reported by the NASDAQ Global Select Market.

Options outstanding that are vested and expected to vest as of February 28, 2008 are as follows:

Number of Shares (in thousands)	Weighted average Grant-Date Fair Value	Weighted Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value (in thousands)
36,307	\$ 5.40	4.2	\$ 4,873

Vested and expected to vest at February 28,
2008

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Restricted Stock Awards. Restricted stock award activity during the nine months ended February 28, 2008 and restricted stock award detail as of February 28, 2008, were as follows (shares in thousands):

	Number of Shares (unvested)	Weighted average Grant-Date Fair Value
Outstanding May 31, 2007	2,403	\$ 4.33
Granted	790	3.90
Vested	(586)	4.36
Forfeited	(281)	4.14
Outstanding February 28, 2008	2,326	\$ 4.20

During the nine months ended February 28, 2008 approximately 0.6 million restricted shares with an aggregate fair value of \$2.4 million became vested. Total aggregate intrinsic value of unvested restricted stock awards at February 28, 2008 was \$7.7 million with a weighted-average remaining contractual term of 1.9 years.

Restricted Stock Units. Restricted stock unit activity during the nine months ended February 28, 2008 and restricted stock units outstanding as of February 28, 2008, were as follows (shares in thousands):

	Number of Shares (unvested)
Outstanding May 31, 2007	3,111
Granted	4,427
Vested	(1,449)
Forfeited	(553)
Outstanding February 28, 2008	5,536

During the nine months ended February 28, 2008 approximately 1.4 million restricted share units with an aggregate fair value of \$5.4 million became vested. Total aggregate intrinsic value of restricted stock units at February 28, 2008 was \$18.2 million with a weighted-average remaining contractual term of 1.9 years.

Employee Stock Purchase Plan. We have an employee stock purchase plan (ESPP) under which eligible employees may authorize payroll deductions of up to ten percent of their compensation, as defined, to purchase common stock at a price of 85 percent of the lower of the fair market value as of the beginning or the end of the six-month offering period. We recognized \$1.2 million of stock-based compensation expense related to the ESPP in the nine months ended February 28, 2008.

NOTE 3. ACQUISITIONS

On November 17, 2003, we formed H3C, formerly known as the Huawei-3Com joint venture, with a subsidiary of Huawei Technologies, Ltd. (Huawei). H3C is domiciled in Hong Kong, and has its principal operating center in Hangzhou, China. Two years after formation of H3C, we had the one-time option to purchase an additional two percent ownership interest from Huawei. We exercised this right and entered into an agreement to purchase an additional two percent ownership interest in H3C from Huawei for an aggregate purchase price of \$28.0 million. The acquisition occurred on January 27, 2006 at which time we owned a majority interest in the joint venture and, therefore, consolidated H3C's financial statements (beginning February 1, 2006). Three years after formation of H3C, we and Huawei each had the right to initiate a bid process to purchase the equity interest in H3C held by the other. 3Com initiated the bidding process on November 15, 2006 to buy Huawei's 49 percent stake in H3C. Huawei

ultimately accepted our bid and the transaction closed on March 29, 2007, at which time 3Com paid the \$882 million purchase price in full. As such, H3C is now a wholly owned subsidiary in the nine months ended February 28, 2008 as compared to the same period of the previous year when we owned 51 percent and Huawei had a minority ownership.

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In recent fiscal years, we have undertaken several initiatives involving significant changes in our business strategy and cost structure.

In fiscal 2001, we began a broad restructuring of our business to enhance the focus and cost effectiveness of our businesses in serving their respective markets. These restructuring efforts continued through fiscal 2008. As of February 28, 2008, accrued liabilities related to actions initiated in fiscal 2001, 2002, 2003, 2004, 2005, 2006, 2007, and 2008 (the Fiscal 2001 Actions, Fiscal 2002 Actions, Fiscal 2003 Actions, Fiscal 2004 Actions, Fiscal 2005 Actions, Fiscal 2006 Actions, Fiscal 2007 Actions, and Fiscal 2008 Actions) mainly consist of lease obligations associated with vacated facilities and employee separation costs.

Restructuring charges related to these various initiatives resulted in a net charge of \$0.7 million in the third quarter of fiscal 2008 and a net charge of \$2.2 million in the third quarter of fiscal 2007. Net restructuring charges in the third quarter of fiscal 2008 consisted of \$0.8 million for severance and outplacement costs and a net benefit of \$0.1 million for adjustments to facilities-related charges. Included in the \$0.8 million of severance and outplacement costs was a \$0.6 million charge related to the termination of the unvested stock options, restricted stock and restricted stock units, of terminated employees, who were let go as part of the Fiscal 2008 Actions. The severance agreements contain a provision for the payout of the intrinsic value of the share-based compensation held by these employees at termination based on the consideration such instruments would receive under the proposed acquisition by affiliates of Bain Capital Partners if such transaction actually was consummated by a specified date. The net restructuring charge in the third quarter of fiscal 2007 resulted from severance, outplacement and other costs of \$2.1 and \$0.1 million in facility related charges. Restructuring charges for the first nine months of fiscal 2008 were \$4.3 million, and net restructuring charges for the first nine months of fiscal 2007 were \$2.8 million.

Accrued liabilities associated with restructuring charges totaled \$2.8 million as of February 28, 2008 and are included in the caption *Accrued liabilities and other* in the accompanying consolidated balance sheets. These liabilities are classified as current because we expect to satisfy such liabilities in cash within the next 12 months.

Fiscal 2008 Actions

Activity and liability balances related to the fiscal 2008 restructuring actions are as follows (in thousands):

	Employee Separation Expense	Total
Balance as of May 31, 2007	\$	\$
Provisions	4,214	4,214
Payments and non-cash charges	(2,462)	(2,462)
Balance as of February 28, 2008	\$ 1,752	\$ 1,752

Employee separation expenses include severance pay, outplacement services, medical and other related benefits. During the nine months ended February 28, 2008, the total reduction in workforce associated with actions initiated during fiscal 2008 included approximately 68 employees who had been separated or were currently in the separation process and approximately 9 additional employees who had been notified but had not yet worked their last day. We expect to complete any remaining activities related to actions initiated in fiscal 2008 in the next 12 months.

Table of Contents***Fiscal 2007 Actions***

Activity and liability balances related to the fiscal 2007 restructuring actions are as follows (in thousands):

	Employee Separation Expense	Facilities- related Charges	Other Restructuring Costs	Total
Balance as of May 31, 2007	\$ 1,330	\$ 264	\$	\$ 1,594
Provisions (benefits)	(93)	59	53	19
Payments and non-cash charges	(1,237)	(174)	(53)	(1,464)
Balance as of February 28, 2008	\$	\$ 149	\$	\$ 149

Employee separation expenses include severance pay, outplacement services, medical and other related benefits. The reduction in workforce affected employees involved in research and development, sales and marketing, customer support, and general and administrative functions. In the nine months ended February 28, 2008, the total reduction in workforce associated with actions initiated during fiscal 2007 included approximately 5 employees who had been separated or were currently in the separation process.

We expect to complete any remaining activities related to actions initiated in fiscal 2007 in the next 12 months.

Fiscal 2001 through 2006 Actions

Activity and liability balances related to the fiscal 2001 through 2006 restructuring actions are as follows (in thousands):

	Employee Separation Expense	Facilities- related Charges	Other Restructuring Costs	Total
Balance as of May 31, 2007	\$ 303	\$ 1,479	\$	\$ 1,782
Provisions (benefits)	17	55	3	75
Payments and non-cash charges		(976)	(3)	(979)
Balance as of February 28, 2008	\$ 320	\$ 558	\$	\$ 878

Facilities related provisions in the nine months ended were related to revised lease obligation terms.

We expect to complete any remaining activities related to these actions in the next 12 months.

NOTE 5. INCOME TAXES

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109 (FIN 48), that clarifies the accounting and recognition for income tax positions taken or expected to be taken in our tax returns. FIN 48 provides guidance on derecognition of tax benefits, classification on the balance sheet, interest and penalties, accounting in interim periods, disclosure, and transition. The Company adopted the provisions of FIN 48 on June 2, 2007 which resulted in no adjustment to the beginning of the year retained earnings balance. As of the adoption date, the Company had unrecognized tax benefits of \$24.8 million and valuation allowances of \$937.1 million, for a total of \$961.9 million in unrecognized tax benefits. The valuation allowance of \$937.1 million includes \$143.5 million attributable to the tax benefit of stock option deductions, which, if recognized, will be allocated directly to paid-in-capital. In addition, the valuation allowance includes approximately \$59.3 million for acquired net operating loss carryforwards which, if

realized, would result in a decrease in goodwill. The remaining tax benefits, if recognized, would affect our effective tax rate. As of the end of the third quarter of fiscal 2008 the balance of unrecognized tax benefits excluding the valuation allowance was \$28.3 million, representing an increase over the fiscal year to date of \$3.5 million. All of this increase, if recognized, would affect our effective tax rate. The amount of the increase in the third quarter was \$0.9 million. Substantially all of these increases relate to tax positions taken in the current fiscal period. Since adoption there has been a reduction of \$0.6 million in the amount of unrecognized benefits as a result of the expiration of applicable statutes. Substantially all of this increase occurred in the current quarter.

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The Company files a consolidated U.S. income tax return and tax returns in various state and local jurisdictions, and our subsidiaries file tax returns in various foreign jurisdictions. In the normal course of business, the Company is subject to examination by taxing authorities throughout the world, including such major jurisdictions as China, the United Kingdom and Singapore, as well as the U.S. With some exceptions, the Company is no longer subject to U.S. federal, state and local, or non-U.S., income tax examinations for years before 2004.

The significant exceptions are as follows. In Singapore we are subject to examination in relation to transfer pricing and other issues for fiscal years 1999 to 2004. Subsequent to the end of the third quarter we have made substantial progress in settling this examination, and we expect that there will be a favorable change in our balance of unrecognized tax benefits as a result. We are currently finalizing our calculations and we expect to make the necessary entries in the fourth quarter. In the Netherlands we are under examination for fiscal year 1997 in relation to the taxable status of income from an interest in a foreign partnership. In Hong Kong we are under examination for fiscal years 2000 to 2002 in relation to an offshore claim in respect of income from our Asia Pacific Region customer service business. It is possible that these examinations will be settled within the next twelve months and therefore it is reasonably possible that, as a result of settlement, there could be a material change in the balance of unrecognized tax benefits. However it is not possible to estimate the amount of the potential change.

We estimate that the balance of unrecognized tax benefits will decrease by approximately \$0.9 million over the next twelve months as a result of the expiration of various statutes.

The Company recognizes interest and penalties related to uncertain tax positions in income tax expense. As of June 2, 2007, the combined amount of accrued interest and penalties related to uncertain tax positions was \$2.1 million, which was recorded within the balance of unrecognized tax benefits. As of the end of the third quarter of fiscal 2008 the balance of interest and penalties included in unrecognized tax benefits was \$2.6 million, representing an increase over the fiscal year to date of \$0.5 million. The amount of the increase in tax expense related to interest and penalties in the current quarter was \$0.1 million.

NOTE 6. COMPREHENSIVE INCOME (LOSS)

The components of comprehensive income (loss), net of tax, are as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	February 28,		February 28,	
	2008	2007	2008	2007
Net income (loss)	\$ (7,840)	\$ (4,779)	\$ (62,118)	\$ (22,363)
Other comprehensive income:				
Net unrealized gain (loss) on investments		248	(210)	2,252
Change in accumulated translation adjustments	11,822	2,947	26,071	6,614
Total comprehensive income (loss)	\$ 3,982	\$ (1,584)	\$ (36,257)	\$ (13,497)

NOTE 7. NET LOSS PER SHARE

Employee stock options of 46.3 million, restricted stock awards of 2.3 million and restricted stock units of 5.5 million shares for both the three and nine months ended February 28, 2008 and stock options of 54.7 million, restricted stock awards of 3.0 million and restricted stock units of 3.5 million shares for both the three and nine months ended February 28, 2007 were not included in the computation of diluted earnings per share as the net loss for these periods would have made their effect antidilutive.

Table of Contents**NOTE 8. INVENTORIES**

The components of inventories are as follows (in thousands):

	February 28, 2008	May 31, 2007
Finished goods	\$ 67,794	\$ 61,857
Work-in-process	4,587	7,143
Raw materials	21,469	38,988
Total	\$ 93,850	\$ 107,988

NOTE 9. INTANGIBLE ASSETS, NET

The following table details our purchased intangible assets (in thousands):

	February 28, 2008			May 31, 2007		
	Gross	Accumulated Amortization	Net	Gross	Accumulated Amortization	Net
Existing technology	\$ 377,170	\$ (182,282)	\$ 194,888	\$ 387,233	\$ (148,641)	\$ 238,592
Trademark	55,502		55,502	55,500		55,500
Huawei non-compete agreement	33,633	(16,569)	17,064	33,000	(61)	32,939
OEM agreement	24,496	(5,966)	18,530	23,800	(22)	23,778
Maintenance contracts	19,000	(9,764)	9,236	19,000	(7,389)	11,611
Other	22,089	(17,002)	5,087	21,924	(13,055)	8,869
Total	\$ 531,890	\$ (231,583)	\$ 300,307	\$ 540,457	\$ (169,168)	\$ 371,289

In the first quarter of fiscal 2008 we wrote off a \$15.6 million fully amortized existing technology intangible asset related to our connectivity business. Since the products associated with the connectivity business are near the end of the product life cycle, we have concluded that the asset does not provide any future benefit. Additionally, in the first nine months of fiscal 2008 our gross intangible assets increased by \$7.0 million for the appreciation on the Renminbi affecting the value of certain intangible assets tied to our Chinese business. These intangible assets have a weighted-average useful life of approximately four years.

We have completed our annual tests for impairment of the carrying value of goodwill, which are conducted as of the end of the third fiscal quarter each year. These tests involve the comparison of the estimated fair value of our reporting units in which goodwill resides to their carrying value. As a result of these tests, we have concluded that no impairment exists as of February 28, 2008.

NOTE 10. ACCRUED WARRANTY

Most products are sold with varying lengths of warranty ranging from 90 days to limited lifetime. Allowances for estimated warranty obligations are recorded in the period of sale, based on historical experience related to product failure rates and actual warranty costs incurred during the applicable warranty period and are recorded as part of cost of goods sold. Also, on an ongoing basis, we assess the adequacy of our allowances related to warranty obligations recorded in previous periods and may adjust the balances to reflect actual experience or changes in future expectations.

The following table summarizes the activity in the allowance for estimated warranty costs for the nine months ended February 28, 2008 and 2007 (in thousands):

Nine Months Ended

	February 28,	
	2008	2007
Accrued warranty, beginning of period	\$ 40,596	\$ 41,791
Cost of warranty claims processed during the period	(31,040)	(37,851)
Provision for warranties related to products sold during the period	29,122	35,817
Accrued warranty, end of period	\$ 38,678	\$ 39,757

Table of Contents**NOTE 11. LONG-TERM DEBT**

On March 22, 2007, H3C Holdings Limited (the Borrower), an indirect wholly-owned subsidiary of 3Com Corporation, entered into the Credit and Guaranty Agreement dated as of March 22, 2007 among H3C Holdings Limited, as Borrower, 3Com Corporation, 3Com Holdings Limited and 3Com Technologies, as Holdco Guarantors, various Lenders, Goldman Sachs Credit Partners L.P., as Mandated Lead Arranger, Bookrunner, Administrative Agent and Syndication Agent (GSCP), and Industrial and Commercial Bank of China (Asia) Limited, as Collateral Agent (the Credit Agreement). On March 28, 2007, the Borrower borrowed \$430 million under the Credit Agreement in the form of a senior secured term loan to finance a portion of the purchase price for 3Com's acquisition of 49 percent of H3C Technologies Co., Limited, or H3C.

On May 25, 2007, the parties amended and restated the Credit Agreement in order to, among other things, convert the facility into two tranches with different principal amortization schedules and different interest rates, as further described below (the A&R Loans). The parties closed the A&R Loans on May 31, 2007.

Interest on borrowings is payable semi-annually on March 28 and September 28, and commenced on September 28, 2007. The applicable LIBOR rate at September 30, 2007 was 5.1% and, based on the credit spread mandated by the agreement, the effective interest rate for Tranche A was 7.1% and the effective interest rate for Tranche B was 8.1%. Remaining payments of principal on the A&R Loans are due as follows on September 28, for fiscal years ending May 31 (in thousands):

	Tranche A	Tranche B
2009	46,000	2,000
2010	46,000	2,000
2011	46,000	2,000
2012		20,000
2013		172,000

In the second quarter of fiscal 2008, we made principal and interest payments of \$94.0 million and \$11.2 million, respectively. Accrued interest as of February 28, 2008 related to the long-term debt was \$6.8 million.

During the fourth quarter of fiscal 2008 we plan to make a voluntary prepayment of \$35 million applied to the final principal payment on Tranche B.

As of February 28, 2008, we were in compliance with all of our debt covenants under the A&R Loans.

NOTE 12. SEGMENT INFORMATION

Based on the information provided to our chief operating decision-maker (CODM) for purposes of making decisions about allocating resources and assessing performance, we review the operations of the business by looking at four reporting segments. In prior fiscal years we reported two segments, SCN and H3C. In fiscal 2008, we have realigned our internal reporting and, as a result, we have changed our segment reporting to be in line with the way we are now internally managing our business. This change breaks-out the SCN segment into the Data and Voice business unit (DVBU), our TippingPoint security division (TippingPoint) and corporate expenses (Corp). We do not use any allocation methods to distribute these corporate expenses to our operating business units.

Management evaluates segment performance based on segment revenue, gross profit, operating expense and operating income (loss).

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Summarized financial information of our results of operations by segment for the three and nine months ended February 28, 2008 and 2007 is as follows.

Three Months Ended February 28, 2008

(in thousands)	H3C	DVBU	Tipping Point	Corp	Eliminations/ Other	Total
Revenue	\$212,558	\$134,603	\$23,639		\$(34,410) <i>a</i>	\$336,390
Gross profit	120,230	43,362	16,578		(496) <i>c</i>	179,674
Operating expense	73,413	49,445	17,337	10,995 <i>b</i>	34,550 <i>d</i>	185,740
Operating income (loss)	\$ 46,817	\$ (6,083)	\$ (759)	\$(10,995)	\$ (35,046)	\$ (6,066)

Three Months Ended February 28, 2007

(in thousands)	H3C	DVBU	Tipping Point	Corp	Eliminations/ Other	Total
Revenue	\$195,144	\$132,882	\$24,503		\$(29,088) <i>a</i>	\$323,441
Gross profit	89,640	47,672	16,807	(264) <i>b</i>	(418) <i>c</i>	153,437
Operating expense	64,066	47,509	18,626	13,544 <i>b</i>	18,627 <i>d</i>	162,372
Operating income (loss)	\$ 25,574	\$ 163	\$ (1,819)	\$(13,808)	\$(19,045)	\$ (8,935)

Nine Months Ended February 28, 2008

(in thousands)	H3C	DVBU	Tipping Point	Corp	Eliminations/ Other	Total
Revenue	\$582,309	\$414,058	\$74,892		\$(97,634) <i>a</i>	\$973,625
Gross profit	315,693	127,029	50,740	(210) <i>b</i>	(12,522) <i>c</i>	480,730
Operating expense	214,150	147,257	51,505	33,952 <i>b</i>	106,950 <i>d</i>	553,814
Operating income (loss)	\$101,543	\$ (20,228)	\$ (765)	\$(34,162)	\$ (119,472)	\$ (73,084)

Nine Months Ended February 28, 2007

(in thousands)	H3C	DVBU	Tipping Point	Corp	Eliminations/ Other	Total
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Revenue	\$555,403	\$414,218	\$65,515		\$(78,575) <i>a</i>	\$956,561
Gross profit	260,439	137,593	44,059	(954) <i>b</i>	(1,120) <i>c</i>	440,017
Operating expense	184,905	155,013	52,018	34,775 <i>b</i>	52,489 <i>d</i>	479,200
Operating income (loss)	\$ 75,534	\$ (17,420)	\$ (7,959)	\$(35,729)	\$ (53,609)	\$ (39,183)

a Represents eliminations for inter-company revenue during the respective periods.

b Represents costs not directly attributable to any operating business segment.

c Includes stock based compensation in all periods plus purchase accounting inventory related adjustments as applicable.

d Includes stock-based compensation, amortization and restructuring in all periods and acquisition related expenses as applicable.

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Certain product groups accounted for a significant portion of our sales. Sales from these product groups as a percentage of total sales for the respective periods are as follows (in thousands except percentages):

	Three Months Ended February 28,				Nine Months Ended February 28,			
	2008		2007		2008		2007	
Networking	\$ 279,771	83%	\$ 259,196	80%	\$ 797,280	82%	\$ 776,081	81%
Security	30,459	9%	30,647	9%	97,004	10%	87,691	9%
Voice	15,093	5%	18,700	6%	48,071	5%	51,198	5%
Services	10,309	3%	9,805	3%	29,292	3%	26,724	3%
Legacy connectivity products	758	%	5,093	2%	1,978	%	14,867	2%
Total	\$ 336,390		\$ 323,441		\$ 973,625		\$ 956,561	

NOTE 13. GEOGRAPHIC INFORMATION

Sales by geographic region are as follows (in thousands):

	Three Months Ended February 28,		Nine Months Ended February 28,	
	2008	2007	2008	2007
China	\$ 169,864	\$ 154,291	\$ 459,725	\$ 445,076
Europe, Middle East, and Africa	75,368	65,736	218,239	206,203
North America	42,871	58,538	155,478	172,120
Asia Pacific (except China)	27,059	26,906	76,306	79,577
Latin and South America	21,228	17,970	63,877	53,585
Total	\$ 336,390	\$ 323,441	\$ 973,625	\$ 956,561

Sales information by geography to the extent available is reported based on the customer's designated delivery point, except in the case of H3C's original equipment manufacturer, or OEM, sales which are based on the hub locations of H3C's OEM partners.

NOTE 14. LITIGATION

We are a party to lawsuits in the normal course of our business. Litigation can be expensive and disruptive to normal business operations. Moreover, the results of complex legal proceedings are difficult to predict. We believe that we have meritorious defenses in the matter set forth below in which we are named as a defendant. An unfavorable resolution of the lawsuits described below could adversely affect our business, financial position, results of operations, or cash flows. We cannot estimate the loss or range of loss that may be reasonably possible as a result of this litigation and, accordingly, we have not recorded any associated liability in our consolidated balance sheets.

On December 5, 2001, TippingPoint and two of its current and former officers and directors, as well as the managing underwriters in TippingPoint's initial public offering, were named as defendants in a purported class action lawsuit filed in the United States District Court for the Southern District of New York. The lawsuit, which is part of a consolidated action that includes over 300 similar actions, is captioned *In re Initial Public Offering Securities Litigation, Brian Levey vs. TippingPoint Technologies, Inc., et al.* (Civil Action Number 01-CV-10976). The principal allegation in the lawsuit is that the defendants participated in a scheme to manipulate the initial public offering and subsequent market price of TippingPoint's stock (and the stock of other public companies) by knowingly assisting the underwriters' requirement that certain of their customers had to purchase stock in a specific initial public offering as a condition to being allocated shares in the initial public offerings of other companies. In relation to TippingPoint, the purported plaintiff class for the lawsuit comprises all persons who purchased TippingPoint stock from March 17, 2000

through December 6, 2000. The suit seeks rescission of the purchase prices paid by purchasers of shares of TippingPoint common stock. On September 10, 2002, TippingPoint's counsel and counsel for the plaintiffs entered into an agreement pursuant to which the plaintiffs dismissed, without prejudice, TippingPoint's former and current officers and directors from the lawsuit. In May 2003, a memorandum of understanding was executed by counsel for the plaintiffs, the issuer-defendants and their insurers setting forth the terms of a settlement that would result in the termination of all claims brought by the plaintiffs against the issuer-defendants and the individual defendants named in the lawsuit. In August 2003, TippingPoint's Board of Directors approved the settlement

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terms described in the memorandum of understanding. In May 2004, TippingPoint signed a settlement agreement on behalf of itself and its current and former directors and officers with the plaintiffs. This settlement agreement formalizes the previously approved terms of the memorandum of understanding and, subject to certain conditions, provides for the complete dismissal, with prejudice, of all claims against TippingPoint and its current and former directors and officers. Any direct financial impact of the settlement is expected to be borne by TippingPoint's insurers. On August 31, 2005, the District Court issued its preliminary approval of the settlement terms. The settlement remains subject to numerous conditions, including final approval by the District Court. There can be no assurance that such conditions will be met. If the District Court rejects the settlement agreement, in whole or in part, or the settlement does not occur for any other reason and the litigation against TippingPoint continues, we intend to defend this action vigorously, and to the extent necessary, to seek indemnification and/or contribution from the underwriters in TippingPoint's initial public offering pursuant to its underwriting agreement with the underwriters. However, there can be no assurance that indemnification or contribution will be available to TippingPoint or enforceable against the underwriters.

On December 22, 2006, Australia's Commonwealth Scientific and Research Organization (CSIRO) filed suit in the United States District Court for the Eastern District of Texas (Tyler Division) against several manufacturers and suppliers of wireless products, including 3Com, seeking money damages and injunctive relief. The complaint alleges that the manufacture, use, and sale of wireless products compliant with the IEEE 802.11(a) or 802.11(g) wireless standards infringes on CSIRO's patent, U.S. Patent No. 5,487,069. On March 9, 2007, 3Com filed its Answer, denying infringement and claiming invalidity and unenforceability of the CSIRO patent, among other defenses. The case is in the discovery phase of litigation. The majority of 3Com's wireless products are supplied to the Company under OEM Purchase and Development Agreements that impose substantial intellectual property indemnification obligations upon 3Com's suppliers. We cannot make any predictions as to the outcome of this litigation and intend to vigorously defend the matter.

Between September 28, 2007 and October 10, 2007, five putative class action complaints were filed in the Court of Chancery of the State of Delaware in connection with the announcement of the proposed acquisition of the Company by affiliates of Bain Capital Partners: Fisk v. 3Com Corporation, et al., Civil Action No. 3256-VCL; Bendit v. 3Com Corporation, et al., Civil Action No. 3258-VCL; Litvintchouk v. Robert Y.L. Mao, et al., Civil Action No. 3264-VCL; Kadlec v. 3Com Corporation, et al., Civil Action No. 3268-VCL; and Kahn v. 3Com Corporation, et al., Civil Action No. 3286-VCL. On October 12, 2007, the above-referenced actions were consolidated for all purposes and captioned: IN RE: 3COM SHAREHOLDERS LITIGATION, Civil Action No. 3256-VCL. An additional two putative class action complaints were filed in the Superior Court of Middlesex County, Massachusetts: Tansey v. 3Com Corporation, et al., Civil Action No. 07-3768, and Davenport v. Benhamou, et al., Civil Action No. 07-3973F. All of the complaints name 3Com and the current members of our board of directors as defendants. All of the complaints except the Tansey and Kahn petitions also name Paul G. Yovovich, a former member of our board of directors, as a defendant. Excepting the Tansey and Davenport petitions, all of the complaints also name Bain Capital Partners as a defendant. The Tansey complaint names Bain Capital, LLC as a defendant. The Davenport complaint also names Diamond II Acquisition Corp. and Diamond II Holdings, Inc. as defendants. Diamond II Acquisition Corp. was also named as a defendant in the Kahn complaint. The Bendit complaint also names Huawei Technologies Company as a defendant, and the Tansey complaint also names Huawei Technology Co. Ltd. as a defendant. Plaintiffs purport to represent stockholders of 3Com who are similarly situated to them. Among other things, the seven complaints allege that the proposed purchase price of \$5.30 per share is inadequate and that our directors, in approving the proposed Merger, breached fiduciary duties owed to 3Com's shareholders because they allegedly failed to take steps to maximize the value to our public stockholders. The complaints further allege that Bain Capital Partners and, in some cases, 3Com and Huawei, aided and abetted these alleged breaches of fiduciary duty. The complaints seek class certification, damages and certain forms of equitable relief, including enjoining the consummation of the Merger and a direction to our board of directors to obtain a transaction in the best interests of 3Com's shareholders. On November 2 and 13, 2007, the defendants filed motions to dismiss or, in the alternative, stay the two Massachusetts proceedings. On December 20, 2007 and January 23, 2008, the Massachusetts proceedings were stayed pending the resolution of class certification in the consolidated Delaware action captioned IN RE: 3COM SHAREHOLDERS LITIGATION. In the consolidated

Delaware action the parties have reached an agreement in principle to settle, which has been embodied in a Memorandum of Understanding filed with the court for its consideration. If the Merger is not consummated for any reason, we expect the courts to dismiss the actions in their entirety without consideration of any settlement.

Table of Contents**NOTE 15. PROPOSED ACQUISITION BY AFFILIATES OF BAIN CAPITAL PARTNERS LLC**

On September 28, 2007, the Company, entered into an Agreement and Plan of Merger (the Merger Agreement) by and among the Company, Diamond II Holdings, Inc., a corporation organized under the laws of the Cayman Islands, (Newco), and Diamond II Acquisition Corp., a Delaware corporation and a wholly owned subsidiary of Newco (Merger Sub). Pursuant to the terms of the Merger Agreement, Merger Sub would be merged with and into the Company, and as a result the Company would continue as the surviving corporation and a wholly owned subsidiary of Newco (the Merger). Newco is controlled by Bain Capital Fund IX, L.P. and Shenzhen Huawei Investment & Holding Co. Ltd. The Board of Directors of the Company unanimously approved this transaction.

Pursuant to the Merger Agreement, at the effective time of the Merger, each issued and outstanding share of common stock of the Company would be canceled and will be automatically converted into the right to receive \$5.30 in cash, without interest. Vesting of all outstanding 3Com equity based awards would continue until the closing of the merger, in accordance with their respective terms. At the closing of the Merger, all outstanding shares of restricted stock and restricted stock units would fully vest and such outstanding shares of restricted stock and restricted stock unit awards would be purchased for \$5.30 per share less applicable withholdings. Immediately prior to the closing of the Merger, outstanding options would become fully vested and exercisable. To the extent unexercised as of the closing of the Merger, options with an exercise price below \$5.30 per share would be cashed out at the difference between \$5.30 and the exercise price of the option, less applicable withholdings. All other options would terminate as of the closing of the Merger.

The Merger Agreement contains a non-solicitation or no shop provision restricting the Company from soliciting alternative acquisition proposals from third parties and from providing information to and engaging in discussions with third parties regarding alternative acquisition proposals. The no-shop provision is subject to a customary fiduciary-out provision which allows the Company under certain circumstances to participate in discussions with third parties with respect to bona fide written unsolicited alternative acquisition proposals and to terminate the Merger Agreement under certain circumstances after paying a termination fee of \$66.0 million. The Merger Agreement further provides that, upon its termination under specified circumstances, the buyers would be required to pay the Company a termination fee of either \$66.0 million or \$110.0 million as applicable.

The buyers have obtained equity and debt financing commitments for the transactions contemplated by the Merger Agreement. The aggregate proceeds of the commitments, together with the available cash of the Company, will be sufficient for the buyers to pay the aggregate merger consideration and all related fees and expenses in the event the transaction is consummated. Consummation of the Merger is subject to customary conditions to closing.

On March 20, 2008, an affiliate of Bain Capital Partners, LLC sent a letter to the Company purporting to terminate the Merger Agreement. The Company publicly announced later that day that it does not believe Bain Capital Partners, LLC's attempt to terminate the Merger Agreement is valid and on March 24, 2008 the Company delivered a letter to affiliates of Bain Capital Partners, LLC that, among other things, confirmed this position. 3Com intends to continue to fulfill its obligations under the terms of the existing Merger Agreement and intends to pursue the \$66.0 million termination fee payable under the Merger Agreement under certain circumstances. On March 21, 2008, 3Com held its scheduled shareholder meeting to enable 3Com shareholders to vote on the company's existing Merger Agreement. Obtaining shareholder approval of the Merger Agreement is a condition to seeking the termination fee. At the shareholders' meeting approximately 70% of the outstanding shares of the Company's common stock voted to adopt the Merger Agreement.

The parties had made a joint voluntary filing with the Committee on Foreign Investment in the United States (CFIUS) in connection with the proposed merger transaction. The parties withdrew their joint filing after they were unable to reach a mitigation agreement with CFIUS to address concerns raised by CFIUS, and no application has been re-submitted to date. At the time they withdrew their joint application, the parties notified CFIUS that they would not go forward with the proposed transaction in the form presented to CFIUS, which included a minority investment by affiliates of Huawei Technologies in 3Com.

In light of the foregoing, there can be no assurance that the parties will be able to close the merger transaction contemplated by the existing Merger Agreement. There can be no assurance that the Company will be able to collect the termination fee.

Several purported class action lawsuits have been filed since September 28, 2007 by 3Com shareholders against the Company, its current directors, a former director, Bain Capital Partners, and in some cases, Huawei Technologies. See note 14 Litigation for a further discussion of these actions.

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

INTRODUCTION

The following discussion should be read in conjunction with the condensed consolidated financial statements and the related notes that appear elsewhere in this document.

BUSINESS OVERVIEW

We are incorporated in Delaware. A pioneer in the computer networking industry, we provide secure, converged networking solutions, as well as maintenance and support services, for enterprises and public sector organizations of all sizes. Headquartered in Marlborough, Massachusetts, we have worldwide operations, including sales, marketing, research and development, and customer service and support capabilities.

Our products and services can generally be classified in the following categories:

§ Networking;

§ Security;

§ Voice;

§ Services; and

§ Legacy Connectivity Products.

We have undergone significant changes in recent years, including:

§ The proposed acquisition of the Company by affiliates of Bain Capital Partners;

§ the formation and subsequent 100 percent acquisition of our Chinese joint venture H3C;

§ financing a portion of the purchase price for our acquisition of H3C by entering into a \$430 million senior secured credit agreement;

§ restructuring activities, which included outsourcing of information technology, all manufacturing activity in our DVBU segment, significant headcount reductions in other functions, and selling excess facilities;

§ significant changes to our executive leadership;

§ acquiring TippingPoint Technologies, Inc.; and

§ realigning our DVBU sales and marketing channels and expenditures.

We believe an overview of these significant recent events is helpful to gain a clearer understanding of our operating results.

Significant Events

Proposed Acquisition of the Company

On September 28, 2007 the Company entered into an Agreement and Plan of Merger to be acquired by an entity controlled by affiliates of Bain Capital Partners. Affiliates of Huawei Investment & Holding Co. Ltd would be minority investors in the acquiring entity in the event the transaction is consummated. On March 20, 2008, an affiliate of Bain Capital Partners, LLC sent a letter to the Company purporting to terminate the Merger Agreement. The Company publicly announced later that day that it does not believe Bain Capital Partners, LLC's attempt to terminate the Merger Agreement is valid and on March 24, 2008 the Company delivered a letter to affiliates of Bain Capital Partners, LLC that, among other things, confirmed this position. 3Com intends to continue to fulfill its obligations under the terms of the existing Merger Agreement and intends to pursue the \$66 million termination fee payable under the Merger Agreement under certain circumstances. On March 21, 2008, 3Com held its scheduled shareholder

meeting to enable 3Com shareholders to vote on the company's existing Merger Agreement. Obtaining shareholder approval of the Merger Agreement is a condition to seeking the termination fee. At the shareholders' meeting approximately 70% of the outstanding shares of the Company's common stock voted to adopt the Merger Agreement.

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The parties had made a joint voluntary filing with the Committee on Foreign Investment in the United States (CFIUS) in connection with the proposed merger transaction. The parties withdrew their joint filing after they were unable to reach a mitigation agreement with CFIUS to address concerns raised by CFIUS, and no application has been re-submitted to date. At the time they withdrew their joint application, the parties notified CFIUS that they would not go forward with the proposed transaction in the form presented to CFIUS, which included a minority investment by affiliates of Huawei Technologies in 3Com.

In light of the foregoing, there can be no assurance that the parties will be able to close the merger transaction contemplated by the existing Merger Agreement. There can be no assurance that the Company will be able to collect the termination fee.. For a further discussion of risks associated with the proposed acquisition, please refer to Risk Factors in Part II, Item 1A in this Form 10-Q.

H3C

On November 17, 2003, we formed H3C, formerly known as the Huawei-3Com joint venture, with a subsidiary of Huawei Technologies, Ltd. (Huawei). H3C is domiciled in Hong Kong, and has its principal operating center in Hangzhou, China. Two years after formation of H3C, we had the one-time option to purchase an additional two percent ownership interest from Huawei. We exercised this right and entered into an agreement to purchase an additional two percent ownership interest in H3C from Huawei for an aggregate purchase price of \$28.0 million. The acquisition occurred on January 27, 2006 at which time we owned a majority interest in the joint venture and, therefore, consolidated H3C's financial statements (beginning February 1, 2006). Three years after formation of H3C, we and Huawei each had the right to initiate a bid process to purchase the equity interest in H3C held by the other. 3Com initiated the bidding process on November 15, 2006 to buy Huawei's 49 percent stake in H3C. Huawei ultimately accepted our bid and the transaction closed on March 29, 2007, at which time 3Com paid the \$882 million purchase price in full. As such, H3C is a wholly owned subsidiary for the three and nine months ended February 28, 2008 as compared to the same period of the previous year when we owned 51 percent and Huawei had a minority ownership.

We financed a portion of the purchase price for the acquisition of Huawei's 49 percent ownership in H3C through a \$430 million senior secured credit agreement with several lenders.

New Products

We have introduced multiple new products targeted at the small, medium and large enterprise markets, including modular switches and routers, as well as voice over IP, or VoIP, security, wireless, storage, surveillance and unified switching solutions. We also announced our Open Services Networking, or OSN, strategy as well as launched OSN products.

Business Environment and Future Trends

Networking industry analysts and participants differ widely in their assessments concerning the prospects for near-term industry growth. Industry factors and trends also present significant challenges in the medium-term with respect to our goals for sales growth, gross margin improvement and profitability. Such factors and trends include:

- § Intense competition in the market for higher-end, enterprise core routing and switching products;
- § Aggressive product pricing by competitors targeted at gaining share in market segments where we have had a strong position historically, such as the small to medium-sized enterprise market; and
- § The advanced nature and ready availability of merchant silicon, which allows low-end competitors to deliver competitive products and makes it increasingly difficult for us to differentiate our products.

We believe that long-term success in this environment requires us to be a global technology leader and to continue to invest in the development of key technologies. Our key focus for the near future will be to continue to manage each of our operating segments toward sustainable growth, to make targeted investments in the integration of sales efforts and back office functions between H3C and both DVBU and Corporate, to maintain investment in key technologies, and to manage our TippingPoint and DVBU segments towards profitability. In the remainder of fiscal 2008, we also intend to continue investing in our H3C segment, in which we expect continued growth year over year, but at a slower rate than in the past. This is expected to involve continued investment in research and development, increased focus

on growth both inside and outside of China, and growing the dedicated H3C infrastructure in concert with a global 3Com consolidated plan. In addition we may make certain targeted investments in the integration of the H3C with both the DVBU and Corporate operating segments designed to drive more profitable near and long-term growth of the business.

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We continue to face significant challenges in the DVBU segment with respect to sales growth, gross margin and profitability. We believe future sales growth for the DVBU segment depends to a substantial degree on increased sales of our H3C-sourced and H3C branded networking products. An important goal is for the DVBU segment to represent a growing percentage of H3C's channel sales outside of China. We also believe our growth opportunities can be best achieved if we expand our product lines targeting small and medium businesses, or SMB, customers as well as selected medium-enterprise customers. These product enhancements are expected to be based in part upon leveraging open source and open architecture platforms to differentiate our networking offerings. These are also expected to be complemented by expanded security offerings such as the development of attack, access and application controls. Finally, we intend to look to improve our channels to market on these products. In order to achieve our sales goals in the DVBU segment for the remainder of fiscal 2008, it is important that we continue to enhance the features and capabilities of our products in a timely manner in order to expand our addressable market opportunities, distribution channels and market competitiveness. Also, we expect a very competitive pricing environment for the foreseeable future; this will likely continue to exert downward pressure on our DVBU sales, gross margin and profitability. Other important factors in the continued success of our H3C business are expected to include: retaining key management and employees, continuing sales through Huawei as an OEM partner of H3C in the near-to-medium term, expanded channel sales through the DVBU segment outside of China, and continuing the year-over-year growth in H3C.

Our goals for our TippingPoint segment include launching new leading-edge technology products and achieving sustainable profitability while growing sales.

Summary of Three Months Ended February 29, 2008 Financial Performance

- § Our sales in the three months ended February 28, 2008 were \$336.4 million, compared to sales of \$323.4 million in the three months ended February 28, 2007, an increase of \$13.0 million, or 4.0 percent.
- § Our gross margin improved to 53.4 percent in the three months ended February 28, 2008 from 47.4 percent in the three months ended February 28, 2007.
- § Our operating expenses in the three months ended February 28, 2008 were \$185.7 million, compared to \$162.4 million in the three months ended February 28, 2007, a net increase of \$23.3 million, or 14.3 percent.
- § Our net loss in the three months ended February 28, 2008 was \$7.8 million, compared to a net loss of \$4.8 million in the three months ended February 28, 2007.
- § Our balance sheet contains cash and equivalents of \$466.0 million as of February 28, 2008, compared to cash and equivalents of \$559.2 million at June 1, 2007 (the end of fiscal 2007). The balance sheet also includes debt of \$336 million with \$48 million classified as a current liability as of February 28, 2008 compared with debt of \$430 million with \$94 million classified as a current liability at the end of fiscal 2007.

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Summary of Nine Months Ended February 28, 2008 Financial Performance

- § Our sales in the nine months ended February 28, 2008 were \$973.6 million, compared to sales of \$956.6 million in the nine months ended February 28, 2007, an increase of \$17.0 million, or 1.8 percent.
- § Our gross margin improved to 49.4 percent in the nine months ended February 28, 2008 from 46.0 percent in the nine months ended February 28, 2007.
- § Our operating expenses in the nine months ended February 28, 2008 were \$553.8 million, compared to \$479.2 million in the nine months ended February 28, 2007, a net increase of \$74.6 million, or 15.6 percent.
- § Our net loss in the nine months ended February 28, 2008 was \$62.1 million, compared to a net loss of \$22.4 million in the nine months ended February 28, 2007.

CRITICAL ACCOUNTING POLICIES

Our critical accounting policies are described in Note 2 to our Consolidated Financial Statements contained in our Annual Report on Form 10-K for the fiscal year ended June 1, 2007. These policies continue to be those that we feel are most important to a reader's ability to understand our financial results.

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109 (FIN 48), that clarifies the accounting and recognition for income tax positions taken or expected to be taken in our tax returns. FIN 48 provides guidance on derecognition of tax benefits, classification on the balance sheet, interest and penalties, accounting in interim periods, disclosure, and transition. The Company adopted the provisions of FIN 48 on June 2, 2007 which resulted in no adjustment to the beginning of the year retained earnings balance. As of the adoption date, the Company has unrecognized tax benefits of \$24.8 million and valuation allowances of \$937.1 million, for a total of \$961.9 million in tax benefits. The valuation allowance of \$937.1 million includes \$143.5 million attributable to the tax benefit of stock option deductions, which, if recognized, will be allocated directly to paid-in-capital. In addition, the valuation allowance includes approximately \$59.3 million for acquired net operating loss carryforwards which, if realized, would result in a decrease in goodwill. The remaining tax benefits, if recognized would affect our effective tax rate. As of the end of the third quarter of fiscal 2008 the balance of unrecognized tax benefits excluding the valuation allowance was \$28.3 million, representing an increase over the fiscal year to date of \$3.5 million. All of this increase, if recognized, would affect our effective tax rate. The amount of the increase in the second quarter was \$0.9 million. Substantially all of these increases relate to tax positions taken in the current fiscal period.

The Company files a consolidated U.S. income tax return and tax returns in various state and local jurisdictions, and our subsidiaries file tax returns in various foreign jurisdictions. In addition to the U.S., our major taxing jurisdictions include China, the United Kingdom and Singapore. For each of the major taxing jurisdictions, the tax years fiscal 1999 through fiscal 2007 remain open to examination by the respective taxing authorities.

We are currently subject to examination in certain foreign jurisdictions in relation to transfer pricing and other issues. It is possible that certain of these examinations will be settled within the next twelve months. As a result it is reasonably possible that there could be a material change in the balance of unrecognized tax benefits. However it is not possible to estimate the amount of the potential change.

The Company recognizes interest and penalties related to uncertain tax positions in income tax expense. As of June 2, 2007, the combined amount of accrued interest and penalties related to uncertain tax positions was \$2.1 million, which was recorded within the balance of unrecognized tax benefits. As of the end of the third quarter of fiscal 2008 the balance of interest and penalties included in unrecognized tax benefits was \$2.6 million, representing an increase over the fiscal year to date of \$0.5 million. The amount of the increase in the current quarter was \$0.1 million.

Table of Contents**RESULTS OF OPERATIONS****THREE AND NINE MONTHS ENDED FEBRUARY 28, 2008 AND 2007**

The following table sets forth, for the periods indicated, the percentage of total sales represented by the line items reflected in our condensed consolidated statements of operations:

	Three Months Ended February 28,		Nine Months Ended February 28,	
	2008	2007	2008	2007
Sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	46.6	52.6	50.6	54.0
Gross profit margin	53.4	47.4	49.4	46.0
Operating expenses:				
Sales and marketing	24.5	23.9	24.5	24.1
Research and development	15.0	15.0	15.9	15.1
General and administrative	7.8	6.9	8.1	6.8
Amortization and write-down of intangible assets	7.7	3.2	8.0	3.6
In-process research and development		0.5		0.2
Restructuring charges	0.2	0.7	0.4	0.3
Total operating expenses	55.2	50.2	56.9	50.1
Operating loss	(1.8)	(2.8)	(7.5)	(4.1)
(Loss) gain on investments, net	0.0	(0.2)	0.0	0.1
Interest (expense) income, net	(0.9)	3.5	(1.1)	3.4
Other income, net	3.2	3.0	3.4	2.8
Income (loss) before income taxes and minority interest	0.5	3.5	(5.2)	2.2
Income tax provision	(2.8)	(0.4)	(1.2)	(0.5)
Minority interest in income of consolidated joint venture		(4.6)		(4.0)
Net loss	(2.3)%	(1.5)%	(6.4)%	(2.3)%

Sales

Consolidated sales for the three and nine months ended February 28, 2008 and 2007 by segment were as follows (dollars in millions):

	Three Months Ended February 28,		Nine Months Ended February 28,	
	2008	2007	2008	2007
H3C	\$212.6	\$195.1	\$582.3	\$555.4
DVBU	134.6	132.9	414.0	414.2
TippingPoint	23.6	24.5	74.9	65.5
Intercompany eliminations and other	(34.4)	(29.1)	(97.6)	(78.5)
Consolidated sales	\$336.4	\$323.4	\$973.6	\$956.6

Sales in our H3C segment increased \$17.5 million, or 9.0 percent, in the three months ended February 28, 2008 and increased \$26.9 million, or 4.8 percent in the nine months ended February 28, 2008 compared to the same period in the previous fiscal year. The increase in sales in the three months ended February 28, 2008 is primarily attributable to increased direct sales in China as well as appreciation of the Renminbi of about 5.5 percent related to our sales in China, partially offset by reduced OEM sales to Huawei. The growth for the nine months ended February 28, 2008 is primarily attributable to the appreciation on the Renminbi related to our sales in China as well as increased sales to our DVBU segment and increased direct sales in China, offset in-part by reduced sales to Huawei.

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Sales in our DVBU segment increased \$1.7 million, or 1.3 percent, in the three months ended February 28, 2008 and remained flat in the nine months ended February 28, 2008 compared to the same periods in the previous fiscal year. The increase in sales in the three months ended February 28, 2008 is primarily attributable to increased sales in our EMEA, and LAT regions, mostly offset by decreased sales in our connectivity products and decreased sales in our North America region. The decrease in our North America region was primarily attributable to uncertainty surrounding our proposed acquisition by affiliates of Bain Capital Partners as well as execution challenges. The decrease in sales in the nine months ended February 28, 2008 is primarily attributable to decreased sales in our connectivity business which resulted from our exit of that business and reductions in North America region mostly offset by increased demand for DVBU's Gigabit products in both our EMEA region and our Latin America region. Sales in our TippingPoint segment decreased \$0.9 million, or 3.7 percent, in the three months ended February 28, 2008 and increased \$9.4 million, or 14.4 percent in the nine months ended February 28, 2008 compared to the same periods in the previous fiscal year. The decrease in sales in the three months ended February 28, 2008 are primarily attributable to recording a one-time \$3.2 million revenue adjustment primarily associated with the deferral of certain Federal Government sales. The increase in sales in the nine months ended February 28, 2008 is primarily attributable to an increase in large account sales and related service revenue partially offset by the recording of a \$3.2 million revenue adjustment described above.

Intercompany eliminations and other increased by \$5.3 million or 18.2 percent, in the three months ended February 28, 2008 and increased \$19.1 million, or 24.3 percent in the nine months ended February 28, 2008 compared to the same periods in the previous fiscal year. This increase in both periods is primarily due to increased sales from our H3C segment to our DVBU segment.

Consolidated revenues increased by \$13.0 million or 4.0 percent in the three months ended February 28, 2008 and increased by \$17.0 million, or 1.8 percent in the nine months ended February 28, 2008 compared to the same period in the previous fiscal year.

Sales by major product categories are as follows (dollars in millions):

	Three Months Ended February 28,				Nine Months Ended February 28,			
	2008		2007		2008		2007	
Networking	\$ 279.8	83%	\$ 259.2	80%	\$ 797.3	82%	\$ 776.1	81%
Security	30.5	9%	30.6	9%	97.0	10%	87.7	9%
Voice	15.1	5%	18.7	6%	48.0	5%	51.2	5%
Services	10.3	3%	9.8	3%	29.3	3%	26.7	3%
Connectivity Products	0.7	%	5.1	2%	2.0	%	14.9	2%
Total	\$ 336.4	100%	\$ 323.4	100%	\$ 973.6	100%	\$ 956.6	100%

Networking revenue includes sales of our Layer 2 and Layer 3 stackable 10/100/1000 managed switching lines, our modular switching lines, routers, wireless switching offerings and our small to medium-sized enterprise market products. Sales of our networking products increased \$20.6 million or 7.9 percent in the three months ended February 28, 2008 and increased \$21.2 million or 2.7 percent in the nine months ended February 28, 2008 compared to the same period in the previous fiscal year. The increase in the three and nine months ended February 28, 2008 is primarily attributable to expansion in our global sales of H3C-developed products, appreciation on the Renminbi related to our sales in China partially offset by reduced sales to Huawei and slower than expected sales in our North American region.

Security revenue includes our TippingPoint® products and services, as well as other security products, such as H3C's security offerings, and our virtual private network, or VPN, and network access control, or NAC, offerings. Sales of our security products remained relatively flat in the three months ended February 28, 2008 and increased \$9.3 million, or 10.6 percent for the nine months ended February 28, 2008 compared to the same period in the previous fiscal year. The increase is primarily driven by increased sales of our TippingPoint products in our North American region due to

a couple of large deals and slightly increased sales on a global basis partially offset by recording a \$3.2 million revenue adjustment primarily associated with the deferral of certain Federal Government sales.

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Voice revenue includes our NBX® and VCX voice-over-internet protocol, or VoIP, product lines, as well as voice gateway offerings. Sales of our Voice products decreased \$3.6 million or 19.3 percent in the three months ended February 28, 2008 and \$3.2 million, or 6.3 percent in the nine months ended February 28, 2008 compared to the same period in the previous fiscal year due to decreased demand in North America.

Services revenue includes professional services and maintenance contracts, excluding TippingPoint maintenance which is included in security revenue. Services revenue increased \$0.5 million or 0.5 percent in the three months ended February 28, 2008 and \$2.6 million, or 9.7 percent in the nine months ended February 28, 2008 compared to the same period in the previous fiscal year. The increase was driven primarily by increased service offerings tied to expanded H3C networking sales.

Connectivity Products revenue in the three and nine months ended February 28, 2008 was minimal compared to prior periods with continued future revenue only expected to be from royalty arrangements. The decrease resulted from our exit of this product line as well as a royalty payment in the three and nine months ended February 28, 2007 of \$4.5 million absent in the current fiscal period.

Gross Margin

Gross margin for the three and nine months ended February 28, 2008 and 2007 by segment were as follows (dollars in millions):

	Three Months Ended		Nine Months Ended	
	February 28,		February 28,	
	2008	2007	2008	2007
H3C	56.6%	45.9%	54.2%	46.9%
DVBU	32.2%	35.9%	30.7%	33.2%
TippingPoint	70.1%	68.6%	67.8%	67.3%
Intercompany eliminations and other	1.4%	1.4%	12.8%	1.4%
Gross Margin	53.4%	47.4%	49.4%	46.0%

Gross margin in our H3C segment improved 10.7 points to 56.6 percent in the three months ended February 28, 2008 from 45.9 percent, and 7.3 points to 54.2 percent in the nine months ended February 28, 2008 from 46.9 percent in the same periods in the previous fiscal year. The improvement in gross profit margin is explained by reduced cost of products, and improved pricing of products, including inter-company pricing as well as healthy growth of new products with higher margins as well as appreciation on the Renminbi related to our direct sales in China.

Gross margin in our DVBU segment decreased 3.7 points to 32.2 percent in the three months ended February 28, 2008 from 35.9 percent in the same period of the previous fiscal year, and 2.5 points to 30.7 percent in the nine months ended February 28, 2008 from 33.2 percent in the same period of the previous fiscal year. The decline for the three months ended February 28, 2008 is explained by inter-company pricing and the lack of connectivity product revenue which had 100 percent margin. The decline is explained by costs associated with our change in service providers and reduced pricing, primarily in the mid-range switching product-offerings and inter-company pricing, offset in part by product cost reductions.

Gross margin in our TippingPoint segment improved 1.5 points to 70.1 percent in the three months ended February 28, 2008 from 68.6 percent and 0.5 points to 67.8 percent in the nine months ended February 28, 2008 from 67.3 percent in the same period in the previous fiscal year. These increases are primarily due to more favorable product mix of sales in the current quarter and to a lesser extent certain cost decreases.

Gross margin related to intercompany eliminations and other remained flat at 1.4 percent in the three months ended February 28, 2008 and increased 11.4 points to 12.8 percent in the nine months ended February 28, 2008 from 1.4 percent in the same period in the previous fiscal year. This category contains our intercompany eliminations and other items, which in the case of periods presented includes mainly the amortization of the purchase accounting step-up in inventory from our acquisition of the remaining 49 percent of H3C. The effect of the purchase accounting amortization was included in the first six months of our fiscal 2008, but was not present in the current quarter or any

of the prior-year periods presented.

Table of Contents**Operating Expenses**

(dollars in millions)	Three Months Ended				Nine Months Ended			
	February 28,		Change		February 28,		Change	
	2008	2007	\$	%	2008	2007	\$	%
Sales and marketing	\$ 82.4	\$ 77.4	\$ 5.0	6%	\$ 237.6	\$ 230.6	\$ 7.0	3%
Research and development	50.5	48.4	2.1	4%	155.0	144.4	10.6	7%
General and administrative	26.3	22.5	3.8	17%	78.8	65.1	13.7	21%
Amortization	25.8	10.2	15.6	153%	78.1	34.6	43.5	126%
In-process research and development		1.7	(1.7)	-100%		1.7	(1.7)	-100%
Restructuring	0.7	2.2	(1.5)	-68%	4.3	2.8	1.5	54%
Total	\$ 185.7	\$ 162.4	\$ 23.3	14%	\$ 553.8	\$ 479.2	\$ 74.6	16%

Sales and Marketing. The most significant factors in the increase in the three and nine months ended February 28, 2008 compared to the same periods in fiscal 2007 was the increased China related sales and marketing costs of \$3.0 million due to increased compensation related charges.

Research and Development. The most significant factor contributing to the increase in the three and nine months ended February 28, 2008 compared to the same period in fiscal 2007 was continued investment in our China-based development efforts and increased headcount of 37 Chinese employees partially offset by a decline in DVBU research and development costs.

General and Administrative. The most significant factor in the increase in the three and nine months ended February 28, 2008 compared to the same periods in fiscal 2007 was \$3.0 and \$10.6 million of acquisition related costs from the proposed acquisition by affiliates of Bain Capital Partners in the three and nine months ended February 28, 2008 respectively.

Amortization. Amortization increased \$15.6 million and \$43.5 million in the three and nine months ended February 28, 2008, respectively, when compared to the previous fiscal year due to a significant increase in amortization charges related to our acquisition of the remaining 49% of H3C in March 2007.

Restructuring Charges

Restructuring charges resulted in a net charge of \$0.7 million in the third quarter of fiscal 2008 and a net charge of \$2.2 million in the third quarter of fiscal 2007. Net restructuring charges in the third quarter of fiscal 2008 consisted of \$0.8 million for severance and outplacement costs and a net benefit of \$0.1 million for facilities-related charges. Included in the \$0.8 million of severance and outplacement costs was a \$0.6 million charge related to the termination of the unvested stock options, restricted stock and restricted stock units, of employees who were terminated as part of the Fiscal 2008 Actions. The severance agreements contain a provision for the payout of the intrinsic value of the share-based compensation held by these employees at termination based on the consideration such instruments would receive under the proposed acquisition by affiliates of Bain Capital Partners if such transaction actually was consummated by a specified date. The net restructuring charge in the third quarter of fiscal 2007 resulted from severance, outplacement and other costs of \$2.1 and \$0.1 million in facility related charges. Restructuring charges for the first nine months of fiscal 2008 were \$4.3 million, and net restructuring charges for the first nine months of fiscal 2007 were \$2.8 million.

See Note 4 to Condensed Consolidated Financial Statements for a more detailed discussion of restructuring charges.

Gain (loss) on Investments, Net

Net gains on investments were zero million and \$0.4 million in the three and nine months ended February 28, 2008, respectively, which resulted from gains on our remaining investment portfolios. Net losses on investments were

\$0.6 million in the three months ended February 28, 2007 primarily reflecting losses from sales of most of our remaining investment portfolios. Net gains on investments were \$0.8 million in the first nine months of fiscal 2007, primarily reflecting a \$1.4 million gain from the sale of certain investment portfolios partially offset by \$0.6 million of losses from the sales of our investment portfolio in the third quarter.

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In the three and nine months ended February 28, 2008, the Company incurred \$2.9 million and \$10.4 million, respectively, in net interest expense, versus net interest income of \$11.3 million and \$32.8 million in same periods of the prior fiscal year. The change was directly attributable to the reduced cash balance and incurrence of debt, both resulting from the use of funds and borrowings for the acquisition of the final 49 percent of H3C in March 2007.

Other Income, Net

Other income, net was \$10.6 million in the three months ended February 28, 2008, an increase of \$1.0 million compared to the three months ended February 28, 2007. The increase was primarily related to a gain of \$1.2 million related to the sale of a patent no longer used in our business. Other income, net was \$33.0 million in the nine months ended February 28, 2008, an increase of \$6.0 million compared to the nine months ended February 28, 2007. The increase was primarily due to \$6.2 million of gains from the sale of two patents no longer used in our business and larger software subsidy amounts in our H3C segment in the nine month period, offset in part by the absence of the Hemel facility insurance gain.

Income Tax Provision

Our income tax provision was \$9.5 million for the three months ended February 28, 2008, an increase of \$8.1 million when compared to the corresponding period in the previous fiscal year. The primary reason for the increase over the corresponding period and recent periods is that we have revalued the deferred tax assets and liabilities relating to our H3C subsidiary in China. The net effect of these revaluations is an increase in our tax provision for the current quarter of \$6.1 million. Under the new PRC tax law, effective January 1, 2008, companies which qualify as new and high technology companies will pay corporate income tax at a reduced rate of 15% instead of the higher default rate. We believe that our H3C subsidiary in China will qualify for this reduced rate, although obtaining this status is subject to approval of tax authorities and the detailed application process has not yet been announced. Even though we expect our long-term income tax rate in China will be 15%, accounting rules require us to revalue our deferred tax balances to the normal default rates until such time as we qualify for the reduced rate. This is discussed further in Risk Factors below. The remainder of the income tax provision for the current quarter and all of the provision for the corresponding period was the result of providing for taxes in certain foreign jurisdictions at various statutory rates. Notwithstanding the issue discussed above, our H3C subsidiary in China is currently entitled to tax concessions which began in 2004 and exempted it from the PRC income tax for its initial two years and entitle it to a 50 percent reduction in income tax in the following three years. 2008 will be the final year of those tax concessions. Consequently, until such time as we receive approval for the reduced long-term rate of 15 percent, we currently expect the H3C statutory rate in China to be 9 percent for the calendar year 2008, and, on the expectation that we qualify for the reduced rate, 15 percent thereafter.

The company has US Federal net operating loss carryforwards in the amount of \$2.6 billion as of May 31, 2007.

Minority Interest of Huawei in the Income of Consolidated Huawei-3Com Joint Venture

There is no minority interest in the three or nine months ended February 28, 2008 as H3C is now a wholly-owned subsidiary. In the three and nine months ended February 28, 2007 we recorded an allocation to minority interest of \$14.8 million and \$38.7 million, respectively, representing Huawei's 49 percent interest in the net income reported by the H3C joint venture for the three and nine months ended February 28, 2007.

Net Loss

Our net loss in the three months ended February 28, 2008 was \$7.8 million, a \$3.0 million increase in net loss when compared to the same period of the previous fiscal year. The increase was primarily driven by increased amortization expenses of \$15.6 million due to the acquisition of the remaining 49 percent of H3C, increased income taxes of \$8.1 million related to a change in tax filing status in China, acquisition costs of \$3.0 million related to the proposed acquisition by affiliates of Bain Capital Partners, increased sales and marketing related costs of \$5.0 million, increased R&D expenses of \$2.1 million, partially offset by increased gross profits during the quarter, decreased restructuring costs of \$1.5 million and a \$1.2 million gain from the sales of a patent during the period. Our net loss in the nine months ended February 28, 2008 was \$62.1 million, a \$39.7 million increase in net loss when compared to the same period of the previous fiscal year. The increase was primarily driven by increased amortization expenses of \$43.5 million due to the acquisition of the remaining 49 percent of H3C, increased income taxes of \$6.9 million

related to a change in tax filing status in China, acquisition costs of \$10.6 million related to the proposed acquisition by affiliates of Bain Capital Partners, increased sales and marketing related costs of \$7.0 million, increased R&D expenses of \$10.6 million and increased restructuring charges of \$1.5 million, partially offset by increased gross profits and \$6.2 million of gains from the sale of two patents during the period.

Table of Contents**LIQUIDITY AND CAPITAL RESOURCES**

Cash and equivalents as of February 28, 2008 were \$466.0 million, a decrease of \$93.2 million compared to the balance of \$559.2 million as of May 31, 2007. The following table shows the major components of our condensed consolidated statements of cash flows for the nine months ended February 28, 2008 and 2007:

(In millions)	Nine Months Ended	
	February 28,	
	2008	2007
Cash and equivalents, beginning of period	\$ 559.2	\$ 501.1
Net cash (used in) provided by operating activities	(10.0)	94.9
Net cash (used in) provided by investing activities	(11.9)	272.1
Net cash used in financing activities	(90.2)	(32.5)
Other	18.9	7.2
Cash and equivalents, end of period	\$ 466.0	\$ 842.8

Net cash used in operating activities was \$10.0 million in the nine months ended February 28, 2008, primarily reflecting our net loss of \$62.1 million and increased deferred income taxes of \$0.4 million, more than offset by \$102.7 million of depreciation and amortization, \$15.4 million of stock-based compensation, and \$2.2 million of loss on disposal of assets. Changes in assets and liabilities resulted in a net use of cash of \$67.7 million, with other liabilities decreasing \$25.3 million primarily due to a \$95 million previously accrued compensation charge related to the change-in-control portion of H3C's Equity Appreciation Rights Plan (which was triggered by the acquisition of the remaining 49% of H3C). Additionally accounts receivable and notes receivable increased \$59.3 million, partially offset by a decrease in inventory of \$22.7 million.

Net cash used in investing activities was \$11.9 million for the nine months ended February 28, 2008, consisting primarily of \$13.3 million of net outflows related to purchases of property and equipment.

Net cash used in financing activities was \$90.2 million in the nine months ended February 28, 2008. During the nine months ended February 28, 2008, we made a principal payment of \$94.0 million related to our long term debt and we acquired \$2.3 million of shares of restricted stock awards upon vesting from employees including those shares tendered to us to satisfy the tax withholding obligations that arise in connection with such vesting. This was offset by proceeds of \$6.1 million from issuances of our common stock upon exercise of stock options.

As of February 28, 2008, bank-issued standby letters of credit and guarantees totaled \$7.3 million, including \$6.9 million relating to potential foreign tax, custom, and duty assessments.

We currently have no material capital expenditure purchase commitments other than ordinary course purchases of computer hardware, software and leasehold improvements. We believe that our future cash requirements will likely include an aggregate of \$5 million to \$7 million for professional fees related to our proposed acquisition by affiliates of Bain Capital Partners that are not contingent on the closing of the deal.

Cash requirements relating to our senior secured debt for the next twelve months include a March 2008 interest payment of approximately \$13.1 million and a September 2008 interest and principal payment of approximately \$61.1 million. We also voluntarily prepaid \$35 million of principal on our debt in March 2008. We made this prepayment because H3C's cash flows enabled us to do so, and we expect our mandatory prepayment requirement for a percentage of H3C's excess cash flow would result in us prepaying approximately \$35 million in principal in September 2008. Voluntary pre-payments count dollar-for-dollar against any mandatory pre-payment requirement under the excess cash flow provision. Prepaying in March enables us to allocate the pre-payment to the final principal payment on our more expensive tranche of debt (instead of pro rata between the two tranches), thereby saving some interest expense.

We expect to have continued significant cash outflows as part of the continued vesting under our H3C Equity Appreciation Rights Plan; including \$39 million, \$30 million and \$17 million respectively, in our fiscal years 2009, 2010, and 2011.

We currently believe that our existing cash and equivalents and future cash from operations will be sufficient to satisfy our anticipated cash requirements for at least the next 12 months.

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Table of Contents**EFFECTS OF RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS**

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109 (FIN 48), that clarifies the accounting and recognition for income tax positions taken or expected to be taken in our tax returns. FIN 48 provides guidance on derecognition of tax benefits, classification on the balance sheet, interest and penalties, accounting in interim periods, disclosure, and transition. The Company adopted the provisions of FIN 48 on June 2, 2007 which resulted in no adjustment to the beginning of the year retained earnings balance. As of the adoption date, the Company has unrecognized tax benefits of \$24.8 million and valuation allowances of \$937.1 million, for a total of \$961.9 million in tax benefits. The valuation allowance of \$937.1 million includes \$143.5 million attributable to the tax benefit of stock option deductions, which, if recognized, will be allocated directly to paid-in-capital. In addition, the valuation allowance includes approximately \$59.3 million for acquired net operating loss carryforwards which, if realized, would result in a decrease in goodwill. The remaining tax benefits, if recognized would affect our effective tax rate. As of the end of the third quarter of fiscal 2008 the balance of unrecognized tax benefits excluding the valuation allowance was \$28.3 million, representing an increase over the fiscal year to date of \$3.5 million. All of this increase, if recognized, would affect our effective tax rate.

The Company files a consolidated U.S. income tax return and tax returns in various state and local jurisdictions, and our subsidiaries file tax returns in various foreign jurisdictions. In addition to the U.S., our major taxing jurisdictions include China, the United Kingdom and Singapore. For each of the major taxing jurisdictions, the tax years fiscal 1999 through fiscal 2007 remain open to examination by the respective taxing authorities.

We are currently subject to examination in certain foreign jurisdictions in relation to transfer pricing and other issues. It is possible that certain of these examinations will be settled within the next twelve months. As a result it is reasonably possible that there could be a material change in the balance of unrecognized tax benefits, however it is not possible to estimate the amount of the potential change.

The Company recognizes interest and penalties related to uncertain tax positions in income tax expense. As of the end of the third quarter of fiscal 2008 the balance of accrued interest and penalties related to uncertain tax positions was \$2.6 million, representing an increase over the fiscal year to date of \$0.5 million.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements (SFAS No. 157). SFAS No. 157 clarifies the principle that fair value should be based on the assumptions market participants would use when pricing an asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. Under the standard, fair value measurements would be separately disclosed by level within the fair value hierarchy. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007 and is required to be adopted by 3Com in the first quarter of fiscal 2009. We have not yet determined the impact, if any, that the implementation of SFAS No. 157 will have on our results of operations or financial condition.

In September 2006, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin 108

Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements , which expresses the staff's views regarding the process of quantifying financial statement misstatements. The Bulletin is effective at our fiscal year end 2008. The Company intends to comply with SAB 108 as applicable.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115 (SFAS 159). SFAS 159 expands the use of fair value accounting but does not affect existing standards which require assets or liabilities to be carried at fair value. Under SFAS 159, a company may elect to use fair value to measure accounts and loans receivable, available-for-sale and held-to-maturity securities, equity method investments, accounts payable, guarantees and issued debt. Other eligible items include firm commitments for financial instruments that otherwise would not be recognized at inception and non-cash warranty obligations where a warrantor is permitted to pay a third party to provide the warranty goods or services. If the use of fair value is elected, any upfront costs and fees related to the item must be recognized in earnings and cannot be deferred, e.g., debt issue costs. The fair value election is irrevocable and generally made on an instrument-by-instrument basis, even if a company has similar instruments that it elects not to measure based on fair value. At the adoption date, unrealized gains and losses on existing items for which fair value has been elected are

reported as a cumulative adjustment to beginning retained earnings. Subsequent to the adoption of SFAS 159, changes in fair value are recognized in earnings. SFAS 159 is effective for fiscal years beginning after November 15, 2007 and is required to be adopted by 3Com in the first quarter of fiscal 2009. 3Com currently is determining whether fair value accounting is appropriate for any of its eligible items and cannot estimate

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the impact, if any, which SFAS 159 will have on its consolidated results of operations and financial condition. In June 2007, the FASB ratified EITF 07-3, *Accounting for NonRefundable Advance Payments for Goods or Services Received for Use in Future Research and Development Activities* (EITF 07-3). EITF 07-3 requires that nonrefundable advance payments for goods or services that will be used or rendered for future research and development activities be deferred and capitalized and recognized as an expense as the goods are delivered or the related services are performed. EITF 07-3 is effective, on a prospective basis, for fiscal years beginning after December 15, 2007 and will be adopted in the first quarter of fiscal 2009. The Company is currently evaluating the impact, if any, of the pending adoption of EITF 07-3 on its consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141R, *Business Combinations* to improve reporting and to create greater consistency in the accounting and financial reporting of business combinations. The standard requires the acquiring entity in a business combination to recognize all (and only) the assets acquired and liabilities assumed in the transaction; establishes the acquisition-date fair value as the measurement objective for all assets acquired and liabilities assumed; and requires the acquirer to disclose to investors and other users all of the information they need to evaluate and understand the nature and financial effect of the business combination. SFAS No. 141R applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008, with the exception of the accounting for valuation allowances on deferred taxes and acquired tax contingencies. SFAS 141R amends SFAS 109, such that adjustments made to valuation allowances on deferred income taxes and acquired income tax contingencies associated with acquisitions that closed prior to the effective date of SFAS 141R would apply the provisions of SFAS 141R. An entity may not apply SFAS 141R before that date. Given SFAS 141R relates to prospective business combinations, the Company has currently not determined the potential effects on the consolidated financial statements.

In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements* to improve the relevance, comparability, and transparency of financial information provided to investors by requiring all entities to report noncontrolling (minority) interests in subsidiaries in the same way as required in the consolidated financial statements. Moreover, SFAS No. 160 eliminates the diversity that currently exists in accounting for transactions between an entity and noncontrolling interests by requiring that they be treated as equity transactions. SFAS No. 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. Earlier adoption is prohibited. The Company is currently evaluating whether the adoption of SFAS No. 160 will have a significant effect on its consolidated financial position, results of operations or cash flows.

On March 19, 2008, the FASB issued FASB Statement No. 161, *Disclosures about Derivative Instruments and Hedging Activities* an Amendment of FASB Statement 133. Statement 161 enhances required disclosures regarding derivatives and hedging activities, including enhanced disclosures regarding how: (a) an entity uses derivative instruments; (b) derivative instruments and related hedged items are accounted for under FASB Statement No.133,

Accounting for Derivative Instruments and Hedging Activities; and (c) derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. Statement 161 is effective for fiscal years and interim periods beginning after November 15, 2008. The Company has currently not determined the potential effects on the consolidated financial statements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We no longer hold any marketable equity traded securities as of February 28, 2008.

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ITEM 4. CONTROLS AND PROCEDURES

Our management carried out an evaluation, under the supervision and with the participation of our President and Chief Executive Officer and our Chief Financial Officer, of the effectiveness of our disclosure controls and procedures as of the end of our quarter ended February 29, 2008 pursuant to Exchange Act Rule 13a-15(b). The term "disclosure controls and procedures," as defined under the Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. Based upon that evaluation, our President and Chief Executive Officer and our Chief Financial Officer concluded that, as of the end of our quarter ended February 29, 2008, our disclosure controls and procedures were effective.

There have been no changes in our internal control over financial reporting that occurred during the three months ended February 29, 2008 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The information set forth in Note 14 to the Notes to the Condensed Consolidated Financial Statements is incorporated by reference herein.

ITEM 1A. RISK FACTORS

Risk factors may affect our future business and results. The matters discussed below could cause our future results to materially differ from past results or those described in forward-looking statements and could have a material adverse effect on our business, financial condition, results of operations and stock price.

Risk Related to Announced Acquisition by an entity controlled by affiliates of Bain Capital Partners

On September 28, 2007, we announced an agreement to be acquired by an entity controlled by affiliates of Bain Capital Partners. We cannot provide any assurance that the proposed acquisition will be consummated. If the transaction closes, we cannot assure you of the timing of the closing.

Consummation of the proposed acquisition is subject to the satisfaction of various conditions described in the Merger Agreement. We cannot guarantee that these closing conditions will be satisfied, that we will receive the required approvals or that the proposed acquisition will be successfully completed. Many of these conditions are out of our control. In the event that the proposed acquisition is not completed or is delayed:

management's and our employees' attention from our day-to-day business may be diverted because matters related to the proposed acquisition may require substantial commitments of their time and resources;

we may lose key employees;

our relationships with customers and vendors may be substantially disrupted as a result of uncertainties with regard to our business and prospects;

certain costs related to the proposed acquisition, such as legal and accounting fees and reimbursement of certain expenses, are payable by us whether or not the proposed acquisition is completed;

under certain circumstances, if the proposed acquisition is not completed, we may be required to pay a termination (break-up) fee of up to \$66 million; and

the market price of shares of our common stock may decline to the extent that the current market price of those shares reflects a market assumption that the proposed acquisition will be completed.

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On March 20, 2008, an affiliate of Bain Capital Partners, LLC sent a letter to the Company purporting to terminate the Merger Agreement. The Company publicly announced later that day that it does not believe Bain Capital Partners, LLC's attempt to terminate the Merger Agreement is valid and on March 24, 2008 the Company delivered a letter to affiliates of Bain Capital Partners, LLC that, among other things, confirmed this position. 3Com intends to continue to fulfill its obligations under the terms of the existing Merger Agreement and intends to pursue the \$66 million termination fee payable under the Merger Agreement under certain circumstances. On March 21, 2008, 3Com held its scheduled shareholder meeting to enable 3Com shareholders to vote on the company's existing Merger Agreement. Obtaining shareholder approval of the Merger Agreement is a condition to seeking the termination fee. At the shareholders' meeting approximately 70% of the outstanding shares of the Company's common stock voted to adopt the Merger Agreement.

The parties had made a joint voluntary filing with the Committee on Foreign Investment in the United States (CFIUS) in connection with the proposed merger transaction. The parties withdrew their joint filing after they were unable to reach a mitigation agreement with CFIUS to address concerns raised by CFIUS, and no application has been re-submitted to date. At the time they withdrew their joint application, the parties notified CFIUS that they would not go forward with the proposed transaction in the form presented to CFIUS, which included a minority investment by affiliates of Huawei Technologies in 3Com.

In light of the foregoing, there can be no assurance that the parties will be able to close the merger transaction contemplated by the existing Merger Agreement. There can be no assurance that the Company will be able to collect the termination fee.

Any of these events could have a material negative impact on our results of operations and financial condition and could adversely affect the price of our common stock. In fact, due to some of the recent announcements described above, we believe our stock price has already been negatively impacted.

Risks Related to Historical Losses, Financial Condition and Substantial Indebtedness

We have incurred significant net losses in recent fiscal periods, including \$7.8 million for the quarter ended February 28, 2008 and \$4.8 million for the quarter ended February 28, 2007 and we may not be able to return to profitability.

We cannot provide assurance that we will return to profitability. While we continue to take steps designed to improve our results of operations, we have incurred significant net losses in recent periods. We face a number of challenges that have affected our operating results during the current and past several fiscal years. Specifically, we have experienced, and may continue to experience, the following:

- declining sales due to price competition and reduced incoming order rate;

- operating expenses that, as a percentage of sales, have exceeded our desired financial model;

- management changes;

- disruptions and expenses resulting from our workforce reductions, management changes and employee attrition;

- risk of increased excess and obsolete inventories; and

- interest expense resulting from our senior secured loan.

If we cannot overcome these challenges, reduce our expenses and/or increase our revenue, we may not become profitable.

We may not be able to compensate for lower sales or unexpected cash outlays with cost reductions sufficient to generate positive net income or cash flow.

If we do not increase our sales, we may need to further reduce costs in order to achieve profitability. As we have implemented significant cost reduction programs over the last several years, it may be difficult to make significant further cost reductions without in turn reducing our sales. If we are not able to effectively reduce our costs and expenses, particularly in our DVBU and Corporate segments, we may not be able to generate positive net income. If

we continue to experience negative cash flow from operations from our DVBU and Corporate segments over a prolonged period of time or if we suffer unexpected cash outflows, our