- The increased complexities of storage applications, such as interoperability, storage effectiveness, and business efficiency issues, results in customers requiring storage integration and implementation expertise. We believe our services permit customers to effectively solve these issues, driving demand for our products and services and increasing our revenues.
- Customers require that their business critical applications have effective disaster recovery solutions. The events of September 11, 2001 demonstrate the need for and functionality of our products and services. Our customers had 40 systems located in lower Manhattan that were significantly impacted. In response, our products instantaneously began routing data to remote facilities on behalf of customers located in and around the World Trade Center. We believe all products worked as designed, without material loss of data by any customer.

As a result of the foregoing and other factors, International Data Corporation, or IDC, estimates that the worldwide revenue for network-attached disk storage systems will grow from $25.5 billion in 2001 to $27.8 billion in 2004, a compound annual growth rate of 3.1%. Another indication of demand for our storage networking solutions is the growth of the Fibre Channel market. IDC estimates the revenue for Fibre Channel hubs and switches will grow from $2.0 billion in 2001 to $5.6 billion in 2004, which reflects a compound annual growth rate of 41.7%. IDC estimates the demand for storage consulting and support services will grow from $20.6 billion in 2001 to $23.8 billion in 2004, a compound annual growth rate of 5.0%. IDC estimates that the worldwide revenue for storage management services will grow from $3.6 billion in 2001 to $4.6 billion in 2005, a compound annual growth rate of 6.6%. It is notable however, that we are in the midst of a current economic slowdown affecting most technology sectors and communications in particular. During 2001, IDC estimates worldwide industry sales of disk storage systems declined 18.2% from $31.2 billion in 2000 to $25.5 billion in 2001. We are uncertain of the depth and duration of this slowdown. However, we believe the need for storage networking solutions is significant and will continue to increase over the long term.

Selected Recent Developments

In February 2002, we sold $125 million of 3% convertible subordinated notes due February 2007, raising net proceeds of $121 million. The notes are convertible into our common stock at a price of $19.17 per share. We may redeem the notes upon payment of the outstanding principal balance, accrued interest and a make whole premium if the closing price of our common stock exceeds 175% of the conversion price for at least 20 consecutive trading days within a period of 30 consecutive trading days ending on the trading day prior to the date we mail the redemption notice.

Storage Networking Overview

Storage Networking Industry Background

Growth in Enterprise Data

The volume of enterprise data is increasing due to the proliferation of Web-based content, digital media, e-mail, supply chain management, customer relations management and other data-driven business applications.

Limitations of Traditional Storage Products

The growth of the size and amount of data stored has presented organizations with significant data management challenges and increased storage related costs. As the volume of data stored, and the number of users that require access to the data continue to increase, storage systems and servers are burdened by an increased number of input/output, or I/O, transactions they must perform. However, traditional storage architecture has inherent speed, distance, capacity and performance constraints. For example, depending on the standards and protocols used, the following constraints may exist:

- bandwidth, or the data transmission rate, is generally fixed at 15, 40 or 80 megabytes per second;
- distance between devices is limited to 12 to 150 meters;

- connectivity is limited to 15 storage devices;
- lack of data management capability in SCSI devices places the burden for management tasks on servers, thereby degrading network performance;
- if the server to which the data storage device is connected fails, the data cannot be accessed; and
- local area network, or LAN performance can be significantly degraded while the LAN is being used for storage backup applications.

Advent of Storage Networking Services

Storage networking is necessary for the effective use of large data-intensive applications such as enterprise resource planning, customer relationship management, and digital media. Our current and potential customers have a growing need to access and protect the business critical data created by these types of applications. As a result, we expect increased demand for the purchase and installation of storage networks which will drive demand for our products and demand for our consulting, integration, and managed services for end-to-end storage solutions. As a result of the installation of these solutions, we expect there will also be increased demand for support services.

Complexity and interoperability issues associated with storage networks, coupled with budgetary constraints, cause customers to struggle with the effective implementation of storage networking environments. We believe this will cause many potential customers to look outside their organization for help. Thorough knowledge across a wide variety of proprietary technologies and standards, combining storage expertise and networking knowledge, is not easily found in the marketplace. We anticipate companies such as ours, with comprehensive expertise and skill sets in disaster recovery, business continuity, storage resource management, database, tuning, troubleshooting, switches, networking and storage arrays, will be able to fill in the void for these customers with consulting and integration services. We believe customers may also look to contract out the management of these storage networks as a result of outsourcing the design and implementation of these solutions.

Our Storage Networking Solutions

Our storage networking solutions, consist of products and services that address the limitations of traditional storage architecture in the following ways:

- *Storage networks over unlimited distance* — Our products and services enable organizations to create secure storage networks without any distance limitations. This allows the creation of storage networking over WAN environments in such critical applications as remote data replication, enterprise backup and recovery and remote tape vaulting.
- *Any-to-any connectivity* — Our products are protocol independent — they can connect devices that use Fibre Channel, SCSI, ESCON, and bus and tag protocols. These devices can be connected and extended over telecommunications links including T1/E1, T3/E3 and ATM, or WAN protocols like IP, Fibre Channel and fiber optics. We believe our products connect with substantially all storage vendors.
- *Infrastructure options* — Our products enable the use of IP, ATM, Fibre Channel and fiber optics for expanded use of a storage network infrastructure. This supports the growing amounts of storage created by applications like e-mail and increases due to user demands to access applications in a continuous mode.
- *IP-based networking solutions* — We enable remote data replication over IP-based networks using software provided by EMC, Compaq and Hewlett-Packard. Our solutions allow our customers to capitalize on inexpensive "bandwidth on demand" capabilities of IP-based networks and use existing IP capacity, especially at low traffic times of the day, and rely on existing IP network knowledge. We anticipate expanding storage networking application support with products from other vendors.

- *Consulting and integration services* — Our consulting and integration services help customers evaluate, analyze, design, install and manage storage networks. We strengthened our consulting, integration and managed services capacity with the acquisition of Articulent. We believe these value-added services assist customers in designing, integrating, implementing, and managing storage networks more effectively than they could on their own. Our integration services help customers deal with the complexity of implementing a storage network that is scalable and compatible with customer resources. These services bolster sales of our high margin UltraNet® products and allow us to capture more of our customers' spending. We offer bundled telecommunications access with our products and services to provide customers a complete end-to-end operating solution.

- *Managed services* — We offer outsourced storage management services that complement our current storage networking products on a 24x7x365 basis. Our network management service helps our customers monitor their UltraNet® products and third-party telecommunication lines and allows them to quickly respond to and resolve storage network issues. Our data migration services help our customers migrate large amounts of data from one data center or storage facility to another during consolidation or expansion of data centers. This is a turnkey service including personnel, equipment, software and support. We anticipate adding other outsourced services to monitor and manage complete end-to-end storage solutions for our customers and help drive demand for our storage networking products.

Our storage networking solutions are used for immediate, or real-time, backup and recovery, and support a technology known as remote data replication. Data replication avoids the serious threat to businesses posed by the loss of data between data system backups by simultaneously creating up-to-the-minute images of business-critical data on multiple backup storage disks. Our remote data replication technology permits the backups to be transmitted to a separate geographic location, thereby reducing the risk of natural and site-wide disasters. This technique also permits rapid recovery of data when needed, as it is not necessary to reload tapes.

We also enhance continuous business operations. Traditional LAN-based storage management requires manual handling and transportation of storage to an off-site location. While this ensures a physically-separated copy of valuable corporate data, it requires additional time and expense for handling and transportation. In addition, finding the right tape in a timely manner can be difficult. By bridging the storage network over the WAN, backups can be instantly made to remote locations on disk media, including by data replication, or on tape, known as electronic tape vaulting. This allows for more secure archiving and timely retrieval of the correct business critical data.

Our Storage Networking Strategy

We intend to build upon our position as a leading provider of storage networking solutions. Key elements of this strategy are as follows:

Extend Storage Networking Technology Leadership

We intend to extend our storage networking technology leadership by continuing to broaden our product and service offerings and by expanding our storage networking solutions into new markets. An example of this strategy is our recent introduction of our IP over Fibre Channel and IP over ATM WANs. Currently, our IP-based network solutions enable remote data replication, in conjunction with software products from Compaq, EMC, and Hewlett-Packard and remote tape vaulting over IP-based networks. We are currently developing solutions that will operate in conjunction with storage network applications of other storage networking vendors. In addition our network management service will enable us to use our expertise to assist our customers in keeping the data stored in their storage networks performing efficiently and continuously. We intend to build market share by continuing to focus on areas which make storage networks more useful and accessible, such as WAN applications, any-to-any connectivity, IP-based network and network performance solutions. To achieve leadership, we intend to capitalize on the remote data replication, enterprise backup and recovery, remote tape vaulting and network management capabilities of our products.

Expand Our Consulting and Integration Services

Our consulting and integration services help customers evaluate, analyze, design, install and manage storage networks. We strengthened our consulting, integration and managed services capacity with the acquisition of Articulent. We believe these value-added services assist customers in designing, integrating, implementing, and managing storage networks more effectively than they could on their own. Our integration services eliminate the complexity of implementing a storage network that is scalable and compatible with customer resources. These services bolster sales of our high margin UltraNet® products and allow us to capture more of our customers' spending. We offer bundled telecommunications access with our products and services to provide customers a complete end-to-end operating solution.

Grow Managed Services

We anticipate adding other outsourced services to monitor and manage complete end-to-end storage solutions for our customers and help drive demand for our storage networking products. An example of this is the recent introduction of our network management service that helps our customers monitor their UltraNet® products and third-party telecommunication lines and allows them to quickly respond to and resolve storage network issues. We plan to add management of additional storage resources to the services for problem resolution on the complete storage network.

Further Strengthen Relationships with Storage Networking Industry Leaders

We have established relationships with leaders in the storage networking market, including storage vendors, telecommunications providers, storage management software providers and Fibre Channel switch manufacturers. The parties with whom we have strategic relationships include companies such as Brocade, Compaq, Dynegy Connect, EMC, Hewlett-Packard, Hitachi Data Systems, IBM, McDATA, StorageTek and Veritas. We intend to strengthen our existing relationships and develop new relationships that enable us to offer complementary products and services. We believe our current and future strategic relationships will facilitate the integration of our products, thereby increasing our market share and reducing the length of our sales cycle.

Storage Networking Products

Our storage networking products include the UltraNet® family of storage products, and our channel networking product known as Channelink®.

UltraNet® Storage Director is a high performance switching product that operates at the center of the storage network. It enables storage networks to establish a direct connection between storage elements and servers and share data among diverse servers and storage systems, and networks that are local and geographically dispersed. The switch provides connectivity among SCSI, ESCON, bus and tag, Fibre Channel and WANs.

UltraNet® Edge Storage Router complements the UltraNet® Storage Director by meeting the needs of a broader market. It provides a new price and performance entry point for our core solutions which do not require high port-density and mixed platform support offered by the UltraNet® Storage Director. The UltraNet® Edge Storage Router is designed to reduce the total cost of ownership of enterprise-wide storage networking solutions by leveraging the lower-cost bandwidth offered by IP networks and the performance improvements provided by Fibre Channel.

Channelink® offers connectivity over unlimited distances for mainframes. Applications include remote printing and imaging and data center load balancing, which permits the operation of two or more data centers from one site.

Third party manufactured storage networking products supplied by us, that are designed and manufactured by others, include the following:

- storage systems;
- Fibre Channel switches;
- telecommunications capacity;
- fiber optical multiplexers;
- software; and
- servers.

Storage Networking Services

Our storage networking services help our clients design, deploy, monitor and manage end-to-end storage solutions. We believe these solutions allow our customers to better manage risk and reduce the cost of storage solutions in the enterprise. The acquisition of Articulent strengthened our service offerings and provided us access to Articulent's family of integrated storage services, including consulting, integration and managed services.

Consulting Services

Our consulting services analyze a company's storage needs, determine a storage networking solution to meet those needs, and assist in the development of a business case to justify the storage networking solution. With our consulting, we assist our customers in making their existing networks more flexible and easier to manage. Our consulting expertise is focused on business continuation, disaster recovery, storage infrastructure and network performance to assist information technology managers and corporate executives responsible for planning and funding resources in making sound data management and storage decisions.

Integration Services

Our integration services help companies implement storage networking solutions. These services include project planning, analyzing, designing and documenting a detailed network, installing storage components, integrating storage components, and testing the functionality of the implemented storage solution. Our storage networking products are at the core of our storage architecture implementations, and our long-standing relationships with well-known and successful storage equipment and software manufacturers place us at the forefront of storage management solutions. Our integration services focus on data replication, enterprise back-up and restore, SAN implementation and network management.

Managed Services

Our managed services include a network management service. We monitor our customers' UltraNet® products and telecommunications networks 24x7x365. We believe this service allows our customers to optimize network performance, decreases the chance of downtime and reduces recovery time after failures. Our data migration services help our customers migrate large amounts of data from one data center or storage facility to another during consolidation or expansion of data centers.

Support Services

We offer standard maintenance contracts for our proprietary storage networking products. The contracts generally have a one-year term and provide for advance payment. Our products generally include a one-year limited warranty, and customers generally do not purchase maintenance contracts until the expiration of the warranty period. Customers are offered a variety of contracts to choose from to suit their particular needs. For instance, current options allow a customer to choose support 7 days a week, 24 hours per day, or 5 days per week, 11 hours a day. Other options offer the customer the choice to select air shipment or replacement parts, with the part being installed by the customer's staff, or on site support with spare parts and service being provided by a local parts distributor.

Strategic Storage Networking Relationships

Offering customers effective storage networking solutions requires integrating diverse components, including disk and tape storage devices, storage management software, network management products and Fibre Channel products. Our storage networking relationships include those with key storage vendors, storage management software providers and manufacturers of Fibre Channel and optical networking products. We market our storage networking products directly and through worldwide distributors. We have strategic marketing and supplier relationships with leading storage, telecommunications and fibre switching companies, including Brocade, Compaq, Dynegy Connect, EMC, Hewlett-Packard, Hitachi Data Systems, IBM, McDATA, Pandatel, StorageTek and Veritas. These relationships allow us to provide complete end-to-end storage solutions for our customers. Approximately 20% of our revenues during fiscal year ended January 31, 2002 were represented by products that we supplied on behalf of the parties with whom we have strategic relationships.

Sales and Marketing

We market storage networking products and services in the United States through a direct sales force. We have established representative offices in Canada, the United Kingdom, France, Germany, Australia, Japan, and the Netherlands. We also market these products and services in the United States and throughout the world through systems integrators and independent distributors.

We maintain our own marketing staff and direct sales force. On January 31, 2002, we had approximately 259 persons in our marketing and sales organization.

Customers

Our customers include:

Financial Services	**Telecommunications**	**Information Outsourcing**	**Other**
American Express	AT&T	Computer Sciences Corporation	Best Buy
Bank of America	British Telecommunications	Electronic Data Systems	Wal-Mart
Barclays	Sprint	IBM Global Services	EchoStar
JP Morgan	WorldCom		Boeing
Chase	France Telecom		Lockheed Martin
CitiGroup	Verizon		Mattel
Merrill Lynch			Target
Rabobank International			Merck
Fannie Mae			
Fidelity			
AXA			
Nasdaq			

Research and Development

The markets in which we operate are characterized by rapidly changing technology, new standards and changing customer requirements. Our long term success in these markets depends upon our continuing ability to develop advanced network hardware and software technologies.

To meet the future demands of our customers, we expect to:

- increase the compatibility of our products with the products made by others;
- emphasize the flexible and modular architecture of our products to permit the introduction of new and improved products within existing systems;

- continue to focus on providing sophisticated diagnostic support tools to help deliver high network availability and, in the event of failure, rapid return to service; and
- develop new products based on customer feedback and market trends.

Research and development expenses were 13% of total revenue for the years ended January 31, 2002 and 2001 and 15% of total revenue for the year ended December 31, 1999. We intend to continue to apply a significant portion of resources to product enhancements and new product development for the foreseeable future. We cannot assure you that our research and development activities will be successful.

Manufacturing and Suppliers

In-house manufacturing activities for our products primarily involve quality assurance testing of subassemblies and final system assembly, integration and quality assurance testing. We became ISO 9001 certified in 1999 and have been ISO 9002 certified since 1993.

We manufacture our products based on forecasted orders. Forecasting orders is difficult as most shipments occur at the end of each quarter. Our customers generally place orders for immediate delivery, not in advance of need. Customers may generally cancel or reschedule orders without penalties. Accordingly, we believe that backlog is generally not meaningful for purposes of predicting our revenue for any fiscal period.

We manufacture our UltraNet® and Channelink® products from subassemblies, parts and components, such as integrated circuits, printed circuit boards, power supplies and metal parts, manufactured by others. Some items manufactured by suppliers are made to our specific design criteria.

At January 31, 2002, we held $4.0 million of net inventory for parts that our vendors no longer manufacture. Products in which those parts are included accounted for $85.5 million in revenue during the year ended January 31, 2002. We expect that this inventory will be used in the ordinary course of our business over the next five years. Relevant parts will have to be redesigned after the inventory is used.

We believe that we currently have adequate supply channels. Components and subassemblies used in our products and systems are generally available from a number of different suppliers. However, certain components in our other products are purchased from a limited number of sources. We do not anticipate any difficulty in obtaining an adequate supply of such products and required components. An interruption in our existing supplier relationships or delays by some suppliers, however, could result in production delays and harm our results of operations.

Competition

Our products are sold in markets where other market participants have significantly greater revenues and internationally known brand names. Many of those market participants do not currently sell products similar to ours. However, such market participants may do so in the future, and new products we develop may compete with products sold by well-known market participants. Our competitors in channel networking and storage networking include storage system vendors and others including Crossroads, Gadzoox Networks, Inrange, McDATA, Nishan Systems, QLogic, SAN Valley, SANcastle, StorageTek and Vixel. In addition, Cisco acquired NuSpeed, a developer of an IP-based network product with functionality similar to our product offerings. Our Storage Solutions Division has numerous competitors, including consulting and integration services offered by storage vendors.

The markets in which we operate are characterized by rapidly changing technology and evolving industry standards, resulting in rapid product obsolescence and frequent product and feature introductions and improvements. We compete with several companies that have greater engineering and development resources, marketing resources, financial resources, manufacturing capability, customer support resources and name recognition. As a result, our competitors may have greater credibility with existing and potential customers. They also may be able to adopt more aggressive pricing policies and devote greater resources to the development, promotion and sale of their products than we can to ours, which would allow them to respond more quickly than we can to new or emerging technologies and changes in customer requirements. These competitive pressures may materially harm our business.

The competitive environments of markets in which our storage networking solutions are sold are continuing to develop rapidly. We are not in a position to prepare long range plans in response to unknown competitive pressures. As these markets grow, we anticipate other companies will enter with competing products. In addition, our customers and business relationships may develop and introduce competing products. We anticipate the markets will be highly competitive.

The declining sales of channel networking products present unique competitive pressures. We anticipate pricing pressures may increase in these markets. Consolidation of competing vendors of these products could also have negative consequences.

The principal competitive factors affecting our products include customer service, flexibility, price, performance, reliability, ease of use and functionality. In many situations, the potential customer has an installed base of a competitor's products, which can be difficult to dislodge. IBM, Microsoft and others can significantly influence customers and control technology in our markets. However, we believe our direct sales force, storage networking expert consultants and support services personnel offer us a substantial advantage over new competitors, because these newer competitors do not have the knowledge of storage networking design and support and any-to-any connectivity necessary to sell competing products and services.

Intellectual Property Rights

We rely on a combination of trade secret, copyright, patent and trademark laws, nondisclosure agreements and technical measures to establish and protect our intellectual property rights. That protection may not preclude competitors from developing products with features similar to our products.

We currently own three patents and have nine patent applications filed or in the process of being filed in the United States with respect to our continuing operations. Our pending patent applications, however, may not be issued. We have not applied for patent protection in any foreign countries. Not all of our unique products and technology are patented. Our issued patents may not adequately protect our technology from infringement or prevent others from claiming that our technology infringes that of third parties. Failure to protect our intellectual property could materially harm our business. We believe that patent and copyright protection are less significant to our competitive position because of the rapid pace of technological change in the markets in which our products are sold and because of the effectiveness and quality of our support services, the knowledge, experience and ability of our employees and the frequency of our enhancements.

We rely upon a patent license agreement to manufacture our Channelink® and UltraNet® products that use ESCON. This license expires on December 31, 2004.

We have from time to time received, and may in the future receive, communications from third parties asserting that our products infringe on their patents. We believe that we possess or license all required proprietary rights to the technology included in our products and that our products, trademarks and other intellectual property rights do not infringe upon the proprietary rights of others. However, there can be no assurance that others will not claim a proprietary interest in all or a part of the technology we use or assert claims of infringement. Any such claim, regardless of its merits, could involve us in costly litigation and materially harm our business.

The existence of a large number of patents in the markets in which our products are sold, the rapid rate of issuance of new patents and short product development cycles means it is not economically practical to determine in advance whether a product infringes patent rights of others. We believe that, based upon industry practice, any necessary license or rights under such patents may be obtained on terms that would not materially harm our consolidated financial position or results of operations. However, there can be no assurance in this regard.

Employees

As of January 31, 2002, we had 792 full-time employees for both divisions. On that date, 160 full-time employees provided services to both divisions and are members of our administrative and manufacturing departments. On that date, our Networking Solutions Division had 498 employees and our Storage Solutions Division had 134 employees, which are in addition to those who provide services to both divisions. We consider our ability to attract and retain qualified employees and to motivate such employees to be essential to our future success. Competition for highly skilled personnel is particularly intense in the computer and data communications industry, and we cannot assure that we will continue to attract and retain qualified employees.

Discontinued Operations

Our discontinued operations, which we have historically referred to as our Enterprise Integration Solutions Division, developed and sold our enterprise application integration, or EAI, software that automated the integration of computer software applications and business workflow processes, as well as our traditional server gateways and tools, which enable multiple desktop computers and mainframe terminals to communicate with one another. We changed the name of our Enterprise Integration Solutions Division to Propelis Software, Inc. During 2001, we sold substantially all of the assets of our discontinued operations in a series of transactions. These transactions included the sale of our IntelliFrame subsidiary to webMethods, and the sale of other assets of Propelis subsidiary to Jacada Ltd. All outstanding options to purchase stock of Propelis Software, Inc. have been cancelled or have lapsed. The transactions allow us to focus all of our resources on our storage networking products and services.

Special Note Regarding Forward-Looking Statements

This Form 10-K contains "forward-looking statements" within the meaning of the securities laws. These forward-looking statements are subject to a number of risks and uncertainties, many of which are beyond our control. All statements other than statements of historical facts included or incorporated by reference in this Form 10-K, including the statements under "Business" and elsewhere in this Form 10-K regarding our strategy, future operations, financial position, estimated revenues, projected costs, prospects, plans and objectives of management are forward-looking statements. When used herein, the words "will," "believe," "anticipate," "plan," "intend," "estimate," "expect," "project" and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain these identifying words. Although we believe that our plans, intentions and expectations reflected in or suggested by the forward-looking statements we make in this Form 10-K are reasonable, we can give no assurance that these plans, intentions or expectations will be achieved. Actual results may differ materially from those stated in these forward-looking statements due to a variety of factors, including those described in Exhibit 99 to this Form 10-K and from time to time in our filings with the U.S. Securities and Exchange Commission. All forward-looking statements speak only as of the date of this Form 10-K. Neither we nor any of the initial purchasers undertake any obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. The cautionary statements qualify all forward-looking statements attributable to us or persons acting on our behalf.

Item 2. Properties

Facilities and Properties

Our principal administrative, manufacturing, engineering and development functions are located in leased facilities in the Minneapolis, Minnesota suburb of Plymouth. In addition, we lease office space in England, France, Germany, Australia, Japan, and the Netherlands. We also lease space for sales offices for our direct sales staff and systems consultants in a number of locations throughout the United States and Canada. We believe our facilities are adequate to meet our current needs.

Item 3. Legal Proceedings

From time-to-time we are a party to various legal actions and receive threats of litigation. At this time, management does not believe any such litigation or threats will have a material impact on our financial position.

Item 4. Submission of Matters to a vote of Security Holders

None.

Item 4A. Executive Officers of the Company

Our executive officers are as follows:

Name	Position Served	Age
Thomas G. Hudson	Chairman of the Board, President and Chief Executive Officer	56
Gregory T. Barnum	Chief Financial Officer, Vice President of Finance and Corporate Secretary	47
Jeffrey A. Bertelsen	Corporate Controller and Treasurer	39
William C. Collette	Chief Technology Officer and Vice President of Advanced Technology	58
Nick V. Ganio	Group Vice President of Worldwide Sales, Marketing and Services	42
Mark R. Knittel	Group Vice President of Worldwide Product Operations	47

Thomas G. Hudson has served as President and Chief Executive Officer since June 1996, as a director since August 1996 and Chairman of the Board since May 1999. From 1993 to June 1996, Mr. Hudson served as Senior Vice President of McGraw Hill Companies, a leading information services provider, serving as General Manager of its F.W. Dodge Division, and as Senior Vice President, Corporate Development. From 1968 to 1993, Mr. Hudson served in a number of management positions at IBM Corporation, most recently as Vice President Services Sector Division. Mr. Hudson's IBM career included varied product development, marketing and strategic responsibilities for IBM's financial services customers and extensive international and large systems experience. Mr. Hudson is a graduate of the University of Notre Dame and New York University. Mr. Hudson attended the Harvard Advanced Management Program in 1990. Mr. Hudson also serves on the board of directors of Ciprico, Inc. and Lawson Software, Inc.

Gregory T. Barnum was appointed Vice President of Finance, Chief Financial Officer and Corporate Secretary in July 1997. From September 1992 to July 1997, Mr. Barnum served as Senior Vice President of Finance and Administration, Chief Financial Officer and Corporate Secretary at Tricord Systems, Inc., a manufacturer of enterprise servers. From May 1988 to September 1992, Mr. Barnum served as the Executive Vice President, Finance, Chief Financial Officer, Treasurer and Corporate Secretary for Cray Computer Corporation, a development stage company engaged in the design of supercomputers. Prior to that time, Mr. Barnum served in various accounting and financial management capacities for Cray Research, Inc., a manufacturer of supercomputers. Mr. Barnum is a graduate of the University of St. Thomas.

Jeffrey A. Bertelsen was appointed Corporate Controller and Treasurer in December 1996. Mr. Bertelsen served as our Controller from March 1995 to December 1996. From 1985 to March 1995, Mr. Bertelsen was employed by KPMG LLP, a public accounting firm, most recently as a Senior Audit Manager. Mr. Bertelsen is a graduate of the University of Minnesota.

William C. Collette was appointed Chief Technology Officer in December 1998 and Vice President of Advanced Technology in October 1999. Mr. Collette served as our Vice President of Engineering from December 1995 to October 1999, and as our Director of Future Software Development and as a Software Development Manager from June 1993 to December 1995. From 1990 to 1993, Mr. Collette was employed by SuperComputer Systems, Inc. as a Senior Software Engineer, where he worked with Steve Chen to design the networking for the SS1 Supercomputer. Mr. Collette holds a bachelors degree in business management from Metro State University.

Nick V. Ganio was appointed Group Vice President of Worldwide Sales, Marketing and Services in October 1999. From November 1998 to October 1999, Mr. Ganio served as Vice President of Worldwide Sales and also as Vice President of Direct Sales Worldwide from April 1998 to November 1998. From September 1996 to February 1998, Mr. Ganio served as Vice President of Worldwide Sales and Marketing for Xyplex, Inc. From March 1987 to September 1996, Mr. Ganio held various high-level positions with Digital Equipment Corporation, including Vice President of Operations in Japan, Vice President and General Manager of the Americas Networks Product business and Vice President and Executive Assistant to the Office of President. Mr. Ganio held various sales positions with IBM from May 1981 to February 1987. Mr. Ganio holds a bachelors degree, magna cum laude from Bernard Baruch College.

Mark R. Knittel was appointed Group Vice President of Worldwide Product Operations in October 1999. From May 1997 to October 1999, Mr. Knittel served as our Vice President of Marketing and also as our Vice President of Architecture and Business Development from March 1997 to May 1997. From July 1977 to March 1997, Mr. Knittel was employed with IBM where he held several executive development positions for both hardware and software networking products, as well as multiple strategy positions. Most recently, Mr. Knittel held the position of Director of Campus Product Marketing within the Network Hardware Division of IBM. Mr. Knittel has a masters degree in philosophy from the University of Chicago.

PART II

Item 5. Market for the Registrant's Securities and Related Shareholder Matters

PRICE RANGE OF COMMON STOCK

Our common stock is traded on the Nasdaq National Market under the symbol "CMNT." The following table sets forth for the indicated periods the range of high and low per share sales prices for our common stock as reported on the Nasdaq National Market:

	Price Range of Common Stock	
	High	**Low**
Fiscal Year Ended December 31, 1999		
First Quarter	$17.56	$ 9.75
Second Quarter	30.63	13.00
Third Quarter	23.25	9.19
Fourth Quarter	27.63	7.38
Fiscal Year Ended January 31, 2001		
First Quarter	$27.00	$11.50
Second Quarter	19.88	11.56
Third Quarter	35.25	15.25
Fourth Quarter	40.00	18.69
Fiscal Year Ended January 31, 2002		
First Quarter	$29.88	$ 8.44
Second Quarter	12.59	7.80
Third Quarter	15.73	8.05
Fourth Quarter	24.90	14.10

As of April 1, 2002, there were approximately 1,000 shareholders of record. The Company estimates that approximately an additional 10,500 shareholders own stock held for their accounts at brokerage firms and financial institutions.

DIVIDEND POLICY

We have not paid any cash dividends since our inception, and we do not intend to pay any cash dividends in the future.

Item 6. Selected Consolidated Financial Information

	Years Ended January 31,		Years Ended December 31,		
	2002	2001	1999(1)	1998	1997
	(in thousands, except per share data)				
Consolidated Statements of Operations Data:					
Revenue:					
Product sales	$129,276	$125,432	$ 89,248	$ 74,969	$56,127
Service fees	57,747	50,674	36,741	28,052	24,068
Total revenue	187,023	176,106	125,989	103,021	80,195
Cost of revenue	111,257	83,181	56,795	45,616	36,002
Cost of revenue — special charges	2,325(2)	—	1,414(4)	—	—
Total cost of revenue	113,582	83,181	58,209	45,616	36,002
Gross profit	73,441	92,925	67,780	57,405	44,193
Operating expenses:					
Sales and marketing	52,156	41,019	34,626	32,255	27,504
Engineering and development	23,452	22,572	18,456	14,236	12,384
General and administrative	9,311	8,697	6,922	6,252	4,944
Special charges	996(2)	(287)(3)	1,331(4)	—	—
Total operating expenses	85,915	72,001	61,335	52,743	44,832
Income (loss) from operations	(12,474)	20,924	6,445	4,662	(639)
Loss on sale and write down of webMethods stock	(10,283)(2)	—	—	—	—
Other income, net	5,537	3,152	110	427	1,400
Income (loss) from continuing operations before income taxes	(17,220)	24,076	6,555	5,089	761
Provision (benefit) for income taxes	(5,292)	7,947	2,229	1,730	312
Income (loss) from continuing operations	(11,928)	16,129	4,326	3,359	449
Income (loss) from discontinued operations, net of tax	8,222	(4,135)	329	1,370	(2,763)
Net income (loss)	$ (3,706)	$ 11,994	$ 4,655	$ 4,729	$(2,314)
Diluted income (loss) per share:					
Continuing operations	$ (.40)	$ .58	$ .17	$ .15	$ .02
Discontinued operations	$ .28	$ (.15)	$ .01	$ .06	$ (.12)
Net income (loss)	$ (.12)	$ .43	$ .18	$ .21	$ (.10)
Diluted shares	29,892	27,813	25,818	22,572	22,702
Other Financial Data(5):					
Ratio of earnings to fixed charges	—	12.41x	5.13x	5.55x	1.78x

	As of January 31,		As of December 31,		
	2002	2001	1999	1998	1997
Consolidated Balance Sheet Data:					
Cash, cash equivalents and marketable securities	$118,014	$150,477	$ 26,895	$12,362	$10,824
Working capital	160,271	182,625	50,715	35,587	30,380
Total assets	269,738	268,623	110,654	87,596	78,950
Long-term obligations	708	1,952	1,780	1,816	701
Total shareholders' equity	216,643	213,102	78,472	60,558	55,607

(1) On January 12, 2000, we changed our fiscal year to end on January 31st, rather than December 31st.

(2) Includes special charges and other items recognized in the first quarter of fiscal 2001, including a $2.0 million write-down of inventory, a $325,000 write-off of our FileSpeed product, a $996,000 restructuring charge and a $10.3 million loss on the sale and write-down of webMethods common stock acquired from the disposition of a portion of our discontinued operations.

(3) Includes a reversal of the unused balance of a fiscal 1999 fourth quarter accrual for an abandoned facility of $287,000.

(4) Includes special charges in the fourth quarter of fiscal 1999 of $1.4 million for the write-off of non-SAN-related products and $1.3 million for an abandoned facility.

(5) For the fiscal year 2001, earnings were inadequate to cover fixed charges by $17.2 million. These ratios are calculated by dividing (a) income from continuing operations before income taxes and fixed charges by (b) fixed charges. Fixed charges include interest expense plus a portion of rental expense attributable to interest.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

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

Overview

We are a leading provider of end-to-end storage solutions, including hardware and software products, related consulting and integration services, and managed services in the growing storage networking market. We focus primarily on helping our customers design, develop, deploy and manage storage networks, including storage area networks, or SANs, a high speed network within a business' existing computer system that allows the business to manage its data storage needs with greater efficiency and less disruption to its overall network. We design, manufacture, market and support a wide range of solutions for critical storage networking applications such as remote data replication, or the real-time backup of data to remotely located disks, and remote tape vaulting, or the backup of data to remotely archived tapes. We also supply storage systems, Fibre Channel switches, telecommunications capacity and storage application software.

Our storage networking solutions enable businesses to cost-effectively design, implement, monitor and manage their storage requirements, connect geographically dispersed storage networks, provide continuous availability to greater amounts of data and protect increasing amounts of data more efficiently. We market our storage networking products and services directly to customers through our sales force and worldwide distributors. We also have strategic marketing and supply relationships with leading storage, telecommunications and fibre switching companies, including Brocade, Compaq, Dynegy Connect, EMC, Hewlett-Packard, Hitachi Data Systems, IBM, McDATA, StorageTek and Veritas.

Economic conditions have caused our customers to reevaluate their capital spending plans, and to defer previously planned projects for information technology infrastructure. However, we believe the need for storage networking solutions is significant and will continue to increase.

Due to the slowdown in customer spending for information technology infrastructure, we took cost reduction actions in April 2001 that reduced our quarterly expense run rate, including:

- a 10 percent workforce reduction
- a wage freeze for all employees
- a 10 percent pay cut for executive management
- a 5 percent pay cut for selected other employees; and
- significant reductions in discretionary spending.

The reduction in demand for our products and services also resulted in the following charges in the first quarter of 2001:

- $2.0 million to write-down slow moving inventory
- $325,000 for the write-off of our FileSpeed product; and
- $996,000 for restructuring, principally severance.

During the fourth quarter of 1999, we recorded a $1.3 million charge for the future costs associated with a facility that was abandoned prior to the expiration of the lease term and a $1.4 million charge for the write-off of non-storage networking related products. We reversed the unused portion of the $1.3 million charge for the abandoned facility in the third quarter of 2000. The amount of the reversal was $287,000.

Sale and Write-down of webMethods Stock

During the first quarter of 2001, we sold 232,511 shares of webMethods stock received from the sale of IntelliFrame for approximately $6.2 million, resulting in a pre-tax loss of approximately $8.7 million. We also wrote-down the carrying value of the remaining 41,031 shares of webMethods stock that we still own, resulting in a pre-tax loss of approximately $1.5 million.

Acquisition of Articulent

On April 3, 2001 we acquired all of the outstanding stock of Articulent Inc., a privately held, leading provider of storage solutions and services for $12.4 million in cash, plus the assumption of approximately $24.4 million of liabilities and the acquisition of approximately $19.3 million of tangible assets. The agreement includes a $10.0 million incentive payout based upon meeting certain revenue and earnings milestones over the twelve-month period beginning May 1, 2001. At the present time, we do not anticipate that the revenue and earnings milestones required for the incentive payout will be achieved.

Discontinued Operations — Divestiture of Propelis Software, Inc.

Propelis Software, Inc., formerly known as our Enterprise Integration Solutions Division, developed and sold our enterprise application integration, or EAI, software that automates the integration of computer software applications and business workflow processes. In August 2000, we determined to divest Propelis Software, Inc. and focus on our core storage networking business. As a result, Propelis Software, Inc. has been accounted for as discontinued operations in the accompanying financial statements, meaning that the division's revenues and expenses are not shown and its net income (loss) for all periods are included under the "Discontinued Operations" caption in our statement of operations. During 2001, we sold substantially all of the assets of our discontinued operations in a series of transactions. These included the sale of our IntelliFrame subsidiary to webMethods and the sale of other assets to Jacada Ltd. All outstanding options to purchase stock of Propelis Software have been cancelled or have lapsed.

On February 2, 2001 we sold all of the outstanding stock of IntelliFrame Corporation, including the technology underlying our Propelis BPm™ product, to webMethods, Inc. for $8.8 million in cash and 273,542 shares of webMethods common stock. The stock received from webMethods, Inc. was valued at $17.1 million, which reflects a discount from its publicly reported trading price due to the initial restrictions placed on our ability to freely sell the stock. In connection with this transaction, we paid $3.0 million to two employees, who were former shareholders of IntelliFrame, to satisfy all obligations to make further bonus payments under their employment agreements. The sale resulted in an after tax gain of $12.6 million in the first quarter of 2001.

In the first quarter of 2001, we accrued $9.3 million for the estimated future operating losses of Propelis Software, Inc. through the potential date of divestiture, resulting in an after tax loss of $6.2 million.

On August 23, 2001 the Company sold substantially all of the remaining assets and liabilities of Propelis Software, Inc. to Jacada Ltd. for $6.0 million in cash, plus a warrant to purchase 350,000 ordinary shares of Jacada Ltd. stock at a price of $3.26 per share. The transaction resulted in an after tax gain of $1.8 million in the third quarter of 2001.

Convertible Debt Offering

In February 2002, we sold $125 million of 3% convertible subordinated notes due February 2007, raising net proceeds of $121 million. The notes are convertible into our common stock at a price of $19.17 per share. We may redeem the notes upon payment of the outstanding principal balance, accrued interest and a make whole premium if the closing price of our common stock exceeds 175% of the conversion price for at least 20 consecutive trading days within a period of 30 consecutive trading days ending on the trading day prior to the date we mail the redemption notice. We are required and intend to register 6.5 million shares within 180 days of the original issuance of the notes.

Change in Year End

On January 12, 2000, we changed our fiscal year end to January 31st, from December 31st. We believe the twelve months ended December 31, 1999 provide a meaningful comparison to the twelve months ended January 31, 2002 and 2001. There are no factors, seasonal or otherwise, that would impact the comparability of information or trends, if results for the twelve months ended January 31, 2000 were presented in lieu of results for the twelve months ended December 31, 1999. References in this Form 10-K to fiscal 2001 and 2000 represent the twelve months ended January 31, 2002 and 2001, respectively. References to fiscal year 1999 represent the twelve months ended December 31, 1999.

Accounting Policies

In preparing the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, management must make decisions which impact the reported amounts and the related disclosures. Such decisions include the selection of the appropriate accounting principles to be applied and the assumptions on which to base accounting estimates. In reaching such decisions, management applies judgment based on its understanding and analysis of the relevant circumstances. Note 1 to the consolidated financial statements provides a summary of the significant accounting policies followed in the preparation of the financial statements.

The Company's critical accounting policies include the following:

Revenue Recognition

Revenue is recognized upon shipment for product sales with standard configurations and product sales with other than standard configurations which have demonstrated performance in accordance with its customer's specifications prior to shipment provided that (a) evidence of an arrangement exists, (b) delivery has occurred, (c) the price to the customer is fixed and determinable, and (d) collectibility is assured. All other product sales are recognized when customer acceptance is received or the passage of the customer acceptance period. We accrue for warranty costs and sales returns at the time of shipment based on experience. In transactions that include multiple products and/or services, we allocate the sales value among each of the deliverables based on their relative fair values.

Service fees are recognized as revenue when earned, which is generally on a straight-line basis over the contracted service period or as the services are rendered. Deferred revenue primarily consists of the unearned portion of service agreements billed in advance to customers.

Valuation of Accounts Receivable

We review accounts receivable to determine which are doubtful of collection. In addition, we also make estimates of potential future product returns. In making the determination of the appropriate allowance for doubtful accounts and product returns, we consider specific accounts, changes in customer payment terms, historical write-offs and returns, changes in customer demand and relationships, concentrations of credit risk and customer credit worthiness. Changes in the credit worthiness of customers, general economic conditions and other factors may impact the level of future write-offs and product returns.

Valuation of Inventory

We review obsolescence to determine that inventory items deemed obsolete are appropriately reserved. In making the determination we consider our history of inventory write-offs, future sales of related products, and quantity of inventory at the balance sheet date assessed against our past usage rates and future expected usage rates. Changes in factors such as technology, customers demand, competitor product introductions and other matters could affect the level of inventory obsolescence in the future.

Valuation of Deferred Taxes

Significant management judgment is required in determining the provision for incomes taxes, deferred tax assets and liabilities and any valuation allowance recorded against net deferred tax assets. We are required to estimate our income taxes in each jurisdiction where we operate. This process involves estimating our actual current tax exposure together with assessing temporary differences resulting from differing treatment of items, such as the depreciable life of fixed assets for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included in our consolidated balance sheet. We then assess the likelihood that our deferred tax assets will be recovered from future taxable income, and to the extent we believe recovery is unlikely, we must establish a valuation allowance. To the extent we establish a valuation allowance or increase the valuation allowance in a given period, we must increase tax expense within our statement of operations.

We have recorded a valuation allowance of $1.2 million at January 31, 2002 due to uncertainties related to our ability to utilize certain state and foreign tax credits and loss carryforwards. The valuation allowance is based on our estimates of taxable income by jurisdiction and the period over which our deferred tax assets are recoverable. In the event actual results differ from these estimates or we adjust these estimates in future periods, we may need to establish an additional valuation allowance which could materially impact our financial position and results of operations.

Valuation of Long-Lived and Intangible Assets and Goodwill

We assess the impairment of long-lived and intangible assets and goodwill whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Factors we consider important which could trigger an impairment review include significant under performance relative to expected operating results, changes in the manner of use of the acquired assets or the strategy of our overall business, negative industry or economic trends, significant decline in our stock price for a sustained period, and our market capitalization relative to our net book value.

When we determine that the carrying value of long-lived and intangibles assets and goodwill may not be recoverable based upon the existence of one or more of the above indicators of impairment, we measure any impairment based on the projected discounted cash flow method using a discount rate commensurate with the risk inherent in our current business model. Net long-lived and intangible assets, and goodwill amounted to $44.7 million at January 31, 2002, and no asset impairments were identified as of that date.

We adopted Statement of Financial Accounting Standards ("SFAS") No. 142 "Goodwill and Other Intangible Assets" effective February 1, 2002. As a result, we have ceased amortizing goodwill at February 1, 2002 of $15.0 million. In 2001, we recorded amortization expense related to this goodwill of $624,000 which will no longer be required in 2002. In lieu of amortization, we are required to perform an initial impairment review of our goodwill in 2002 and an annual impairment review thereafter.

Upon completion of any impairment review, there can no be assurance that a material charge will not be required.

Results of Continuing Operations

The following table sets forth financial data for our continuing operations for the periods indicated as a percentage of total revenue except for gross profit, which is expressed as a percentage of the related revenue.

The segment operating information presented below is for illustrative purposes only and has been adjusted to eliminate the effects of special items and other charges recognized by our Networking Solutions Division during the first quarter of 2001, including a $2.0 million write-down of inventory, a $325,000 write-off of our FileSpeed product and a $996,000 restructuring charge. The segment operating information eliminates special charges recognized by our Networking Solutions Division in the fourth quarter of 1999, including $1.4 million for the write-off of non-SAN-related products and $1.3 million for an abandoned facility. It also eliminates the effect in the third quarter of 2000 of a $287,000 reversal of the unused portion of the accrual for the abandoned facility.

	Networking Solutions Division			Storage Solutions Division		
	2001	2000	1999	2001	2000	1999
Revenue:						
Product sales	67.2%	74.1%	73.5%	74.3%	34.0%	—%
Service fees	32.8	25.9	26.5	25.7	66.0	100.0
Total revenue	100.0	100.0	100.0	100.0	100.0	100.0
Gross profit:						
Product sales	53.1	58.0	58.5	17.3	53.4	—
Service fees	48.9	45.5	45.0	(11.5)	13.5	54.2
Total gross profit	51.8	54.7	54.9	9.9	27.1	54.2
Operating expenses:						
Sales and marketing	32.4	22.8	28.5	15.7	29.3	—
Engineering and development	16.8	13.8	15.2	.9	—	—
General and administrative	6.1	5.3	5.7	2.0	—	—
Total operating expenses	55.3	41.9	49.4	18.6	29.3	—
Income (loss) from operations	(3.5)%	12.8%	5.5%	(8.7)%	(2.2)%	54.2%

Revenue

Years Ended January 31, 2002 and 2001

Networking Solutions

Our Networking Solutions Division generated revenue of $136.9 million in 2001, a decrease of 16%, from $163.5 million in 2000. Storage networking related product revenue decreased 16% in 2001 to $69.8 million from $83.5 million in 2000. Approximately $3.2 million of storage networking product revenue in 2001 resulted from the sale of our new UltraNet® Edge product, which started to ship in our third quarter ended October 31, 2001. Sales of channel extension product applications decreased 41% in 2001 to $22.2 million from $37.7 million in 2000. Our older channel extension products continue to be a profitable part of our business and a key application for many of our storage networking customers. We expect sales of channel extension products to continue for the foreseeable future but do not expect revenues to grow substantially. Revenue for our Networking Solutions Division was negatively impacted in 2001 as economic conditions caused our customers to reevaluate their capital spending plans, and to defer previously planned projects for information technology infrastructure.

During 2000, partner relationships with STK and Compaq generated significant product revenue. Sales of the DXE product to STK contributed $9.3 million of product revenue in 2000, compared to $1.5 million of product revenue in 2001. We discontinued the DXE/RDE product line in March 2001, and are transitioning the customer base to our UltraNet® products. An OEM agreement with Compaq contributed $5.7 million of product revenue in 2000. No revenue was generated from this OEM agreement in 2001.

Maintenance revenue increased 6% in 2001 to $44.8 million from $42.3 million in 2000. The increase in revenue is due to the growing installed base of customers using our networking products. The maintenance revenue growth rate slowed in 2001 compared to 2000 due to the decline in Networking product revenue in 2001. In addition, some customers elected not to re-new maintenance agreements in 2001 for our older Channelink® products.

Storage Solutions

Prior to our acquisition of Articulent in April 2001, our Storage Solutions Division consisted of our SAN products and storage networking design and implementation services. Revenue from our Storage Solutions Division increased in 2001 to $50.2 million, an increase of 297% from $12.6 million in 2000. The acquisition of Articulent in April 2001 significantly expanded our solution offerings and accounted for most of the increase.

Years Ended January 31, 2001 and December 31, 1999

Networking Solutions

Our Networking Solutions Division generated revenue of $163.5 million in 2000, an increase of 35%, from $121.4 million in 1999. Storage networking applications for both open systems and mainframes continued to drive new product revenue. Storage networking-related product revenue increased 56% in 2000 to $83.5 million from $53.6 million in 1999. Sales of channel extension product applications increased 6% in 2000 to $37.7 million from $35.6 million in 1999.

During 2000, partner relationships with STK and Compaq generated significant product revenue. Sales of the DXE product to STK contributed $9.3 million of product revenue in 2000, while our OEM relationship with Compaq contributed $5.7 million of product revenue.

Maintenance revenue increased 32% in 2000 to $42.3 million from $32.2 million in 1999. The increase in revenue is due to the growing installed base of customers using our networking products.

Storage Solutions

Revenue from our SAN products and storage networking design and implementation services increased 176% in 2000 to $12.6 million from $4.6 million in 1999. The increase is due to greater customer demand for storage area networks and storage networking. These applications tend to be highly complex, and for these reasons, businesses often outsource their design and implementation to third parties. In addition, we were just starting to increase our investment in these service areas in 1999, resulting in additional revenue in 2000.

General

Revenue from the sale of products and services outside the United States decreased by 12% or $6.0 million in 2001 when compared to 2000, and increased by 20% or $8.9 million in 2000 when compared to 1999. We derived 25%, 30% and 35% of our revenue outside the United States in 2001, 2000 and 1999, respectively. The decrease in revenue generated outside the United States in 2001 is primarily attributable to the global economic slow-down and reduced spending on information technology by our customers. In addition, the Articulent business acquired in April 2001 is primarily focused in the United States and does not have a significant presence in international markets.

No single customer accounted for more than 10% of our revenue in 2001, 2000 or 1999. Price discounting had a small impact on revenue generated by our Networking Solutions business in 2001.

In 2001, approximately 30%, 7% and 17% of our product revenue was derived from businesses in the financial services, telecommunications and information outsourcing industries, respectively.

We primarily sell our storage networking products directly to end-user customers in connection with joint marketing activities with our business partners. For a new customer, the initial sales and design cycle, from first contact through shipment, can vary from 90 days to 12 months or more. We expect that this cycle will continue.

We expect continued quarter-to-quarter fluctuations in revenue in both domestic and international markets. The timing of sizable orders, because of their relative impact on total quarterly sales for both our Networking and Storage Solutions Divisions, may contribute to such fluctuations. The level of product sales reported by us in any given period will continue to be affected by the receipt and fulfillment of sizable new orders in both domestic and international markets.

Gross Profit Margin

Years Ended January 31, 2002 and January 31, 2001

Networking Solutions

Excluding the $2.0 million write-down of slow moving inventory and the $325,000 write-off of our FileSpeed product in the first quarter of 2001, gross profit margins from the sale of networking products were 53% in 2001 compared to 58% in 2000. The decline in gross margin percentage was due to the continued movement in sales mix toward our UltraNet® products which carry a lower margin than our older Channelink® products, and higher levels of sales discounts.

Gross service margins for our networking maintenance business improved in 2001 to 49% from 46% in 2000. The improvement was due to the steadily increasing base of customers contracting for maintenance services, the cost reduction actions that were taken in April 2001, and a change in third party maintenance and logistic suppliers in 2001 that also reduced our costs.

Storage Solutions

Gross profit margins from the sale of storage solutions products were 17% in 2001 compared to 53% in 2000. The decline in gross margin percentage was primarily due to an increase in the sale of lower margin third party products resulting from the acquisition of Articulent in April 2001. Historically, the product solutions offered by Articulent have generated gross margins in the 15% to 25% range.

Gross profit margins from storage solutions services were a negative 12% in 2001 compared to a positive 13% in 2000. The decline in gross margin percentage and negative gross margin in 2001 is due to the fixed cost structure of the services business and low levels of service revenue in 2001. The service costs for the solutions business, mainly people, tend to be fixed in nature. We expect to generate a gross profit from services in the future as business volumes pick up.

Years Ended January 31, 2001 and December 31, 1999

Networking Solutions

Gross profit margins from the sale of networking products were 58% in 2000, compared to 57% in 1999. Excluding a $1.4 million charge for the write-off of non-storage networking-related products, gross profit margins from the sale of products would have been 59% in 1999. The decrease in gross profit margins to 58% from 59% in 1999 was due to an increase in sales of our DXE product to STK, and our UltraNet® Gateway product to Compaq, both of which carry lower gross margins, but comparable operating margins, than our Channelink® and UltraNet® products sold through direct channels.

Gross profit margins for our networking maintenance business were 46% and 45% in 2000 and 1999, respectively. The improvement was due to the steadily increasing base of customers contracting for maintenance services.

Storage Solutions

Gross profit margins from the sale of storage solutions products were 53% in 2000. There were no storage solutions product sales in 1999, as we were just starting to invest in our storage solutions business and were not offering storage solution products.

Gross profit margins from our storage solution services were 13% in 2000 compared to 54% in 1999. The decline in gross profit margin in 2000 was due to our hiring additional technical and consulting personnel to expand our storage solutions service offerings and capabilities.

Operating Expenses

Years Ended January 31, 2002 and 2001

Networking Solutions

Sales and marketing expense increased 19% in 2001 to $44.3 million from $37.3 million in 2000. Since the beginning of 2001, we have increased our sales force by over 25% and have added additional sales management to increase revenue and grow our business.

Engineering and development expense increased 2% in 2001 to $23.0 million from $22.6 million in 2000. The increase was primarily due to continued development of our UltraNet® family of products, particularly the UltraNet® Edge product, which generated over $3.0 million of revenue since its introduction in the third quarter of 2001. This increase was partially offset by the cost reduction actions take in April 2001, including the workforce reduction, wage cuts and reductions in discretionary spending.

Storage Solutions

Sales, marketing, engineering and development expense increased 125% in 2001 to $8.3 million from $3.7 million in 2000. The increase was primarily due to the incremental costs associated with the acquisition of Articulent in April 2001, including wages for approximately 125 new employees and related costs such as travel, training and facilities.

General and Administrative

General and administrative expenses increased 7% in 2001 to $9.3 million from $8.7 million in 2000. The increase in expense is primarily due to the acquisition of Articulent, including additional costs for insurance and professional fees. In 2001, goodwill and intangible amortization associated with the Articulent acquisition totaled $594,000. In 2001, we had total goodwill amortization of $624,000 which we will not have in 2002 due to our adoption of the new accounting pronouncement related to goodwill.

Years Ending January 31, 2001 and December 31, 1999

Networking Solutions

Sales and marketing expense increased 8% in 2000 to $37.3 million from $34.6 million in 1999. The increase in expense resulted from higher commissions, wages, fringe benefits and travel associated with additional headcount required to generate the 36% increase in product revenue for 2000.

Engineering and development expense increased 22% in 2000 to $22.6 million from $18.5 million in 1999. The increase was primarily due to continued development of our UltraNet® family of products that provide customers with additional applications to satisfy their growing storage networking capabilities. During 2000, we announced storage networking over standard IP solutions, including tape, SCSI and Fibre Channel over IP to strengthen our presence in the IP solutions market. We made investments in additional employees to develop these new applications.

Storage Solutions

Sales and marketing expense associated with our Storage Solutions Division increased to $3.7 million in 2000 from nothing in 1999 when we were just starting to invest in our storage solutions business.

General and administrative

General and administrative expense increased 26% in 2000 to $8.7 million from $6.9 million in 1999. The increase was due to higher costs for wages, insurance and professional fees required to support the growth in our business.

Other

Years Ending January 31, 2002 and 2001 and December 31, 1999

Excluding the loss from the sale and write-down of webMethods stock, other income in 2001 and 2000 increased by $2.4 million and $3.0 million, respectively, when compared to the prior year due to an increase in interest income resulting from higher balances of cash and marketable securities available for investment partially offset by lower-yields. In October of 2000, we raised $110 million from a secondary stock offering. Pending use of the offering proceeds for general corporate purposes or complementary acquisitions, the funds have been invested in investment grade, interest-bearing securities. The proceeds from our recently completed convertible debt offering will be similarly invested until used for general working capital purposes including potential acquisitions.

Changes in interest expense in 2001, 2000 and 1999 are due to fluctuations in the balance of capital lease obligations. Interest expense is expected to increase by $1.1 million per quarter as a result of our recent sale of $125 million of 3% convertible subordinated notes due February 2007.

We recorded a provision for income taxes at an effective tax rate of 31% in 2001, and at an effective tax rate of 33% and 34% in 2000 and 1999, respectively. The fluctuations in our effective tax rate are primarily due to the large special charges recorded in 2001 and 1999, the amount of nondeductible foreign losses and fluctuations in the level of benefit from our foreign sales corporation. We also recorded an $830,000 valuation allowance in 2001 for certain state and foreign tax credits and loss carryforwards. Utilization of these benefits in future periods was determined to be unlikely. Based on an assessment of our taxable earnings history and prospective future taxable income, we have determined it to be more likely than not that our remaining net deferred tax asset will be realized in future periods. We may be required to provide a valuation allowance for this asset in the future if we do not generate sufficient taxable income as planned.

Liquidity and Capital Resources

We have historically financed our operations through the public and private sale of equity securities, bank borrowings under lines of credit, capital and operating equipment leases and cash generated by operations.

Cash, cash equivalents and marketable securities at January 31, 2002 totaled $118.0 million, a decrease of $32.5 million since January 31, 2001. Operations utilized $33.8 million of cash in 2001, primarily to fund our operating loss and discontinued operations in the first half of the year, and a $9.0 million increase in inventory resulting from lower than anticipated demand for our networking products and introduction of our new UltraNet® Edge product. Proceeds from the exercise of stock options and purchases of stock through our employee stock purchase plan provided cash in 2001 of $6.4 million. Uses of cash in 2001 included $12.4 million for the purchase of Articulent and purchases of property and equipment and field support spares totaling $11.0 million. We also used $787,000 of cash in 2001 to repurchase 90,000 shares of our common stock.

In February 2002, we sold $125 million of 3% convertible subordinated notes, raising net proceeds of $121 million. The proceeds from the offering will be used for general working capital purposes, including potential acquisitions.

Expenditures for capital equipment and field support spares have been, and will likely continue to be, a significant capital requirement. We believe that our current balances of cash, cash equivalents and marketable securities, when combined with anticipated cash flows from operations and proceeds from our recently completed convertible debenture offering will be adequate to fund our operating plans and meet our current anticipated aggregate capital requirements, at least through fiscal 2002.

In April 2001, our board of directors authorized the repurchase of up to $50.0 million of our common stock. As of January 31, 2002 we had repurchased 90,000 shares of our common stock for $787,000.

In March of 2001, our board of directors adopted an amendment to our 1999 Non-Qualified Stock Award Plan increasing the number of shares authorized for issuance from 1,730,000 to 3,230,000.

We believe that inflation has not had a material impact on our operations or liquidity to date.

Our future minimum contractual cash obligations at January 31, 2002, including open purchase orders incurred in the ordinary course of business, are as follows:

Cash Obligation	Total	Less Than One Year	One to Three Years	Four to Five Years	After Five Years
Capital leases	$ 2.4 million	$ 1.7 million	$ 742,000	None	None
Operating leases	$27.1 million	$ 5.4 million	$9.2 million	$2.5 million	$10.0 million
Purchase orders	$13.8 million	$12.9 million	861,000	72,000	None

On February 20, 2002, we sold $125 million in aggregate principal amount of 3% convertible subordinated notes due February 2007. Holders of the notes may, in whole or part, convert the notes into shares of our common stock at a conversion price of approximately $19.17 per share (aggregate of approximately 6.5 million shares) at any time prior to maturity on February 15, 2007. We may redeem the notes in whole or part at any time if the closing price of our common stock has exceeded 175% of the conversion price then in effect for at least 20 trading days within a period of 30 consecutive trading days ending on the trading day prior to the date we mail the redemption notice. We are required to pay interest on February 15 and August 15 of each year, beginning on August 15, 2002. Debt issuance costs of $3.2 million are being amortized over a five year term using the straight line method, which approximates the effective interest rate method. The amortization of these debt issuance costs will accelerate upon early redemption of the notes. The net proceeds remain available for general working capital purposes, including potential acquisitions. Cash obligations related to this debt include annual interest payments of $3.8 million for the next five fiscal years starting 2002 and a principal payment of $125 million due February 2007.

Related Party Transactions

During 2001, we purchased $491,000 of bandwidth from Dynegy Connect, an entity wholly owned by Dynegy Global Communications. At January 31, 2002 we have commitments to purchase $1.2 million of additional bandwidth from Dynegy Connect through fiscal 2006. All of the bandwidth purchases were for re-sale at a profit. The bandwidth was purchased from Dynegy Connect because they offered us the best pricing. We have purchased bandwidth from competitors of Dynegy Connect when their pricing has been more attractive. Our board member, Lawrence McLernon, is chief executive officer of Dynegy Global Communications.

New Accounting Pronouncements

In July 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standard No. ("SFAS") 141, "Business Combinations," and SFAS 142, "Goodwill and Other Intangible Assets." SFAS 141 requires that the purchase method of accounting be used for all business combinations initiated after June 30, 2001 as well as all purchase method business combinations completed after June 30, 2001. SFAS 141 also specifies criteria that intangible assets must meet to be recognized and reported apart from goodwill. SFAS 142 requires that goodwill and intangible assets with indefinite useful lives, arising from acquisitions occurring after June 30, 2001, no longer be amortized, but instead be tested for impairment at least annually in accordance with the provisions of SFAS 142. Goodwill and intangible assets acquired in business combinations completed before July 1, 2001 continued to be amortized in accordance with appropriate pre-SFAS 142 and 144 requirements until February 1, 2002. SFAS 142 also requires that intangible assets with definite useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment in accordance with SFAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets."

SFAS 144, issued in October 2001, supercedes SFAS 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of," removing from its scope any reference to goodwill impairment and offering guidance on using cash flows to value long-lived assets. In addition, SFAS 144 supercedes the accounting and reporting provisions for the disposal of a business presented in Accounting Principles Board Opinion No. 30, "Reporting the Results of Unusual and Infrequently Occurring Events and Transactions," primarily by broadening the definition of a "discontinued operation" to include business components not considered business segments.

The Company adopted the provisions of SFAS 141 as of July 1, 2001 and SFAS 142, and SFAS 144 as of February 1, 2002.

Under transition provisions of SFAS 141 and SFAS 142, as of February 1, 2002, the Company must evaluate its existing intangible assets and goodwill that were acquired in a purchase business combination occurring before July 1, 2001, make any necessary reclassifications of intangible assets and goodwill to conform with the new criteria in SFAS 141 for recognition apart from goodwill, and conduct an impairment review of the carrying values of intangible assets and goodwill at that date. Also as of February 1, 2002, the Company will be required to reassess the useful lives and residual values of all intangible assets acquired in purchase business combinations, and make any necessary amortization period adjustments by April 30, 2002. Also by April 30, 2002, any intangible asset identified as having an indefinite useful life must be tested for impairment in accordance with the provisions of SFAS 142, and any impairment loss as of February 1, 2002 recognized as the cumulative effect of a change in accounting principle in the first quarter of 2002.

In connection with the transitional goodwill impairment evaluation, SFAS 142 requires the Company to perform an assessment by July 31, 2002 to determine whether goodwill was impaired as of the date of adoption. Any transitional impairment loss will be measured as of February 1, 2002 and reflected as a first quarter 2002 cumulative effect of a change in accounting principle in the Company's statement of earnings as soon as practicable but not later than January 31, 2003.

The pro forma effect of cessation of goodwill amortization prescribed by SFAS 142 would have increased earnings from continuing operations by $624,000, or $0.02 per diluted common share for fiscal year 2001.

Because of the extensive effort needed to implement SFAS 141, SFAS 142 and SFAS 144, it is not practicable to reasonably estimate the impact of their implementation on the Company's financial statements at the date of this report, including whether any transitional impairment losses will be required to be recognized as the cumulative effect of a change in accounting principle.

Change in Fiscal Year

On January 12, 2000, we changed our fiscal year end to January 31st, rather than December 31st. Our summary January 2000 results are as follows: revenues $4.3 million; gross profit $1.3 million; operating expenses $5.3 million; net loss from continuing operations $2.6 million; net loss from discontinued operations $1.0 million; and net loss $3.6 million. We typically incur significant losses in the first month following the completion of a quarter because our revenue is significantly less than the average monthly revenues we generate in any quarterly or annual period.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

We have no derivative financial instruments in our cash, cash equivalents and marketable securities. We mainly invest our cash and cash equivalents in investment grade, highly liquid investments, consisting of money market instruments, bank certificates of deposits and investments in commercial paper.

At January 31, 2002, our marketable securities include a $258,000 investment in a Standard & Poors 500 stock price index fund and a $290,000 investment in a NASDAQ 100 index tracking stock. These investments were purchased to directly offset any investment gains or losses owed to participants under our executive deferred compensation plan which has been established for selected key employees. We also own 41,031 shares of webMethods stock received from the sale of IntelliFrame.

We are exposed to market risks related to fluctuations in foreign exchange rates because some sales transactions, and the assets and liabilities of our foreign subsidiaries, are denominated in foreign currencies, primarily French francs, the euro and British pounds sterling. As of January 31, 2002, we have hedged a portion of our risk by purchasing a forward exchange contract for 450,000 British pounds sterling that settles in February 2002.

Item 8. Consolidated Financial Statements and Supplementary Data

COMPUTER NETWORK TECHNOLOGY CORPORATION

CONSOLIDATED BALANCE SHEETS
(in thousands, except per share data)

	January 31, 2002	January 31, 2001
Assets		
Current assets:		
Cash and cash equivalents	$ 34,402	$ 39,444
Marketable securities	83,612	111,033
Receivables, net	53,962	43,613
Inventories	31,410	22,447
Net current assets of discontinued operations	—	5,430
Deferred tax asset	5,134	11,415
Other current assets	4,138	2,226
Total current assets	212,658	235,608
Property and equipment, net	25,604	25,215
Field support spares, net	4,562	4,446
Deferred tax asset	11,048	—
Goodwill and other intangibles, net	14,533	1,200
Other assets	1,333	2,154
	$269,738	$268,623
Liabilities and shareholders' equity		
Current liabilities:		
Accounts payable	$ 17,240	$ 20,293
Accrued liabilities	20,158	15,780
Deferred revenue	13,466	15,489
Current installments of obligations under capital lease	1,523	1,421
Total current liabilities	52,387	52,983
Deferred tax liability	—	586
Obligations under capital lease, less current installments	708	1,952
Total liabilities	53,095	55,521
Shareholders' equity:		
Undesignated preferred stock, authorized 965 shares; none issued and outstanding	—	—
Series A junior participating preferred stock, authorized 40 shares; none issued and outstanding	—	—
Common stock, $.01 par value; authorized 100,000 shares; issued and outstanding 30,383 at January 31, 2002, and 29,656 at January 31, 2001	304	297
Additional paid-in capital	202,996	195,910
Unearned compensation	(1,232)	(1,304)
Retained earnings	15,459	19,165
Accumulated other comprehensive income (loss)	(884)	(966)
Total shareholders' equity	216,643	213,102
	$269,738	$268,623

See accompanying notes to consolidated financial statements

COMPUTER NETWORK TECHNOLOGY CORPORATION

CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data)

	Years Ended January 31, 2002	Years Ended January 31, 2001	Year Ended December 31, 1999	Month Ended January 31, 2000
Revenue:				
Product sales	$129,276	$125,432	$ 89,248	$ 1,237
Service fees	57,747	50,674	36,741	3,105
Total revenue	187,023	176,106	125,989	4,342
Cost of revenue:				
Cost of product sales	76,254	52,873	38,411	894
Cost of service fees	37,328	30,308	19,798	2,148
Total cost of revenue	113,582	83,181	58,209	3,042
Gross profit	73,441	92,925	67,780	1,300
Operating expenses:				
Sales and marketing	52,156	41,019	34,626	2,643
Engineering and development	23,452	22,572	18,456	1,814
General and administrative	9,311	8,697	6,922	836
Abandoned facility	—	(287)	1,331	—
Restructuring charge	996	—	—	—
Total operating expenses	85,915	72,001	61,335	5,293
Income (loss) from operations	(12,474)	20,924	6,445	(3,993)
Other income (expense):				
Loss on sale and write-down of webMethods stock	(10,283)	—	—	—
Interest income	6,166	3,802	744	95
Interest expense	(285)	(338)	(264)	(6)
Other, net	(344)	(312)	(370)	4
Other income (expense), net	(4,746)	3,152	110	93
Income (loss) from continuing operations before income taxes	(17,220)	24,076	6,555	(3,900)
Provision (benefit) for income taxes	(5,292)	7,947	2,229	(1,287)
Income (loss) from continuing operations	(11,928)	16,129	4,326	(2,613)
Discontinued operations:				
Gain on disposition of discontinued operations, net of tax	8,222	—	—	—
Income (loss) from discontinued operations, net of tax	—	(4,135)	329	(1,012)
	8,222	(4,135)	329	(1,012)
Net income (loss)	$ (3,706)	$ 11,994	$ 4,655	$(3,625)
Basic income (loss) per share:				
Continuing operations	$ (.40)	$ .64	$ .19	$ (.11)
Discontinued operations	$ .28	$ (.16)	$ .01	$ (.04)
Net income (loss)	$ (.12)	$ .47	$ .20	$ (.15)
Shares	29,892	25,383	23,137	23,815
Diluted income (loss) per share:				
Continuing operations	$ (.40)	$ .58	$ .17	$ (.11)
Discontinued operations	$ .28	$ (.15)	$ .01	$ (.04)
Net income (loss)	$ (.12)	$ .43	$ .18	$ (.15)
Shares	29,892	27,813	25,818	23,815

See accompanying notes to consolidated financial statements

COMPUTER NETWORK TECHNOLOGY CORPORATION

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY AND COMPREHENSIVE INCOME (LOSS)

(in thousands)

	Common Stock		Additional Paid-in Capital	Unearned Compensation	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
	Shares	Amount					
Balance, December 31, 1998	22,254	$223	$ 54,921	$ (355)	$ 6,141	$(372)	$ 60,558
Shares issued pursuant to the employee stock purchase plan, restricted stock plan and exercise of stock options	1,538	15	9,354	(799)	—	—	8,570
Tax benefits from employee stock transactions	—	—	4,652	—	—	—	4,652
Compensation expense	—	—	—	316	—	—	316
Comprehensive income:							
Net income	—	—	—	—	4,655	—	4,655
Translation adjustment, net of tax effect of $0	—	—	—	—	—	(279)	(279)
Total comprehensive income	—	—	—	—	—	—	4,376
Balance, December 31, 1999	23,792	$238	$ 68,927	$ (838)	$10,796	$(651)	$ 78,472
Shares issued pursuant to the employee stock purchase plan, restricted stock plan and exercise of stock options	49	—	507	(341)	—	—	166
Tax benefits from employee stock transactions	—	—	—	—	—	—	—
Compensation expense	—	—	—	49	—	—	49
Comprehensive income:							
Net loss	—	—	—	—	(3,625)	—	(3,625)
Translation adjustment, net of tax effect of $0	—	—	—	—	—	49	49
Total comprehensive loss	—	—	—	—	—	—	(3,576)
Balance, January 31, 2000	23,841	$238	$ 69,434	$(1,130)	$ 7,171	$(602)	$ 75,111
Shares issued pursuant to the employee stock purchase plan, restricted stock plan and exercise of stock options	1,215	13	8,181	(675)	—	—	7,519
Shares issued pursuant to a secondary stock offering, net of offering costs	4,600	46	110,189	—	—	—	110,235
Tax benefits from employee stock transactions	—	—	8,106	—	—	—	8,106
Compensation expense	—	—	—	501	—	—	501
Comprehensive income:							
Net income	—	—	—	—	11,994	—	11,994
Translation adjustment, net of tax effect of $0	—	—	—	—	—	(364)	(364)
Total comprehensive income	—	—	—	—	—	—	11,630
Balance, January 31, 2001	29,656	$297	$195,910	$(1,304)	$19,165	$(966)	$213,102
Shares issued pursuant to the employee stock purchase plan, restricted stock plan and exercise of stock options	817	8	6,894	(496)	—	—	6,406
Tax benefits from employee stock transactions	—	—	978	—	—	—	978
Repurchase of common stock	(90)	(1)	(786)	—	—	—	(787)
Compensation expense	—	—	—	568	—	—	568
Comprehensive income:							
Net loss	—	—	—	—	(3,706)	—	(3,706)
Unrealized gain on marketable securities, net of tax effect of $299						510	510
Translation adjustment, net of tax effect of $0	—	—	—	—	—	(428)	(428)
Total comprehensive loss	—	—	—	—	—	—	(3,624)
Balance, January 31, 2002	30,383	$304	$202,996	$(1,232)	$15,459	$(884)	$216,643

See accompanying notes to consolidated financial statements

COMPUTER NETWORK TECHNOLOGY CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	Years Ended January 31, 2002	Years Ended January 31, 2001	Year Ended December 31, 1999	Month Ended January 31, 2000
Operating Activities:				
Net income (loss)	$ (3,706)	$ 11,994	$ 4,655	$(3,625)
Discontinued operations	(8,222)	4,135	(329)	1,012
Depreciation and amortization	15,127	11,812	9,083	652
Compensation expense	568	346	219	49
Loss on sale and write-down of webMethods stock	10,283	—	—	—
Change in deferred taxes	(1,268)	(5,344)	(1,936)	—
Changes in operating assets and liabilities, net of acquisition:				
Receivables	(40)	(14,833)	(5,872)	608
Inventories	(4,517)	(3,717)	3,489	(4,305)
Other current assets	(1,575)	(445)	(804)	(4)
Accounts payable	(21,879)	11,036	4,272	(2,151)
Accrued liabilities	(7,606)	17,754	2,563	(3,878)
Deferred revenue	(2,091)	5,569	2,636	2,045
Net cash provided by (used in) continuing operations	(24,926)	38,307	17,976	(9,597)
Net cash provided by (used in) discontinued operations	(8,830)	(1,490)	789	1,051
Cash provided by (used in) operating activities	(33,756)	36,817	18,765	(8,546)
Investing Activities:				
Additions to property and equipment	(8,198)	(14,329)	(8,262)	(542)
Additions to field support spares	(2,770)	(2,520)	(2,727)	(271)
Additions to purchased technology	—	(375)	—	—
Acquisition of Articulent, net of cash acquired	(11,145)	—	—	—
Net proceeds from the sale of IntelliFrame	5,800	—	—	—
Net proceeds from the sale of Propelis Software	6,000	—	—	—
Proceeds from the sale of webMethods stock	6,281	—	—	—
Purchase of marketable securities	(87,786)	(148,389)	(15,421)	—
Proceeds from marketable securities	115,717	45,998	5,286	2,070
Other assets	876	(1,967)	327	3
Discontinued operations — additions to long-term assets	—	(158)	(507)	(12)
Cash provided by (used in) investing activities	24,775	(121,740)	(21,304)	1,248
Financing Activities:				
Payments for repurchases of common stock	(787)	—	—	—
Proceeds from issuance of common stock	6,406	117,754	8,570	166
Repayments of obligations under capital leases	(1,421)	(1,187)	(327)	(65)
Discontinued operations — repayment of debt	—	—	(1,000)	(1,000)
Cash provided by (used in) financing activities	4,198	116,567	7,243	(899)
Effects of exchange rate changes	(259)	(174)	(306)	(13)
Net increase (decrease) in cash and cash equivalents	(5,042)	31,470	4,398	(8,210)
Cash and cash equivalents — beginning of period	39,444	7,974	11,786	16,184
Cash and cash equivalents — end of period	$ 34,402	$ 39,444	$ 16,184	$ 7,974

See accompanying notes to consolidated financial statements

(1) Summary of Significant Accounting Policies

Description Of Business

Computer Network Technology Corporation is a leading provider of end-to-end storage solutions, related consulting and integration services, and managed services in the high-performance storage networking market.

Discontinued Operations

In 2001, the Company divested Propelis Software, Inc. formerly known as the Enterprise Integration Solutions Division. Accordingly, Propelis Software, Inc. has been accounted for as discontinued operation in the accompanying financial statements.

Change in Year End

On January 12, 2000, the Company changed its fiscal year end to January 31st, from December 31st. The Company believes that the twelve months ended December 31, 1999 provide a meaningful comparison to the twelve months ended January 31, 2002 and 2001. There are no factors, of which the Company is aware, seasonal or otherwise, that would impact the comparability of information or trends, if results for the twelve months ended January 31, 1999 were presented in lieu of results for the twelve months ended December 31, 1999. References in these footnotes to fiscal 2001 and 2000 represent the twelve months ended January 31, 2002 and 2001, respectively. References to fiscal 1999 represent the twelve months ended December 31, 1999.

Principles Of Consolidation

The accompanying consolidated financial statements include the accounts of Computer Network Technology Corporation and its subsidiaries (together, the Company). All significant intercompany balances and transactions are eliminated in consolidation.

Revenue Recognition

Revenue is recognized upon shipment for product sales with standard configurations and product sales with other than standard configurations which have demonstrated performance in accordance with customer specifications prior to shipment provided that (a) evidence of an arrangement exists, (b) delivery has occurred, (c) the price to the customer is fixed and determinable, and (d) collectibility is assured. All other product sales are recognized as revenue when customer acceptance is received or upon passage of the customer acceptance period. Warranty costs and sales returns are accrued at the time of shipment based on experience. In transactions that include multiple products and/or services, the sales value is allocated among each of the deliverables based on their relative fair values.

Service fees are recognized as revenue when earned, which is generally on a straight-line basis over the contracted service period or as the services are rendered. Deferred revenue primarily consists of the unearned portion of service agreements billed in advance to customers.

Valuation of Accounts Receivable

Accounts receivable are reviewed to determine which are doubtful of collection. Estimates are also made of potential future product returns. In making the determination of the appropriate allowance for doubtful accounts and product returns, the Company considers specific accounts, changes in customer payment terms, historical write-offs and returns, changes in customer demand and relationships, concentrations of credit risk and customer credit worthiness. The provision for doubtful accounts and product returns was $898,000, $1,600,000 and $519,000 in 2001, 2000 and 1999, respectively. The accounts receivable balances at January 31, 2002 and 2001 were $53,962,000 and $43,613,000, respectively, net of an allowance for doubtful accounts and sales returns of $1,848,000 and $2,383,000, respectively.

Valuation of Inventory

Inventories are stated at the lower of cost (determined on a first in, first out basis) or market. The Company reviews obsolescence to determine that inventory items deemed obsolete are appropriately reserved. In making the determination, consideration is given to the history of inventory write-offs, future sales of related products, and quantity of inventory at the balance sheet date assessed against past usage rates and future expected usage rates.

Valuation of Deferred Taxes

Significant management judgment is required in determining the provision for incomes taxes, deferred tax assets and liabilities and any valuation allowance recorded against net deferred tax assets. The Company is required to estimate income taxes in each jurisdiction where it operates. This process involves estimating actual current tax exposure together with assessing temporary differences resulting from differing treatment of items, such as the depreciable life of fixed assets for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included in the consolidated balance sheet. The Company assesses the likelihood that its deferred tax assets will be recovered from future taxable income and to the extent recovery is believed unlikely, establishes a valuation allowance. The Company must increase tax expense within its statements of operations when a valuation allowance is established or increased in a given period.

The Company has recorded a valuation allowance of $1,240,000 at January 31, 2002 due to uncertainties related to its ability to utilize certain state and foreign tax credits and loss carryforwards. The valuation allowance is based on estimates of taxable income by jurisdiction and the period over which deferred tax assets are recoverable. The Company may need to establish an additional valuation allowance in future periods, which could materially impact its financial position and results of operations, should actual results differ from estimates or should estimates be adjusted in future periods.

Goodwill And Other Intangibles

Goodwill represents the excess of purchase price over the fair value of net assets acquired. In 2001, goodwill was amortized using the straight-line method over periods ranging from seventeen to twenty years. Other intangibles represent amounts assigned to intangible assets at the time of a purchase acquisition and includes purchased technology and customer lists. Such costs are amortized using the straight-line method over periods ranging from two to ten years.

Recorded amounts are regularly reviewed and recoverability assessed. The review considered factors such as whether the amortization of the goodwill and other intangible assets over its remaining life can be recovered through forecasted undiscounted cash flows.

Cash Equivalents

The Company considers investments in highly liquid debt securities having an initial maturity of three months or less to be cash equivalents.

Marketable Securities

Unrealized gains and losses on available-for-sale securities are excluded from earnings and are reflected as a separate component of shareholders' equity. Unrealized gains and losses on trading securities are included in earnings.

Property And Equipment

Property and equipment owned by the Company is carried at cost and depreciated using the straight-line method over three to eight years. Leasehold improvements are amortized using the straight-line method over the terms of the respective leases. Expenditures for repairs and maintenance are charged to expense as incurred. Capital lease equipment is amortized over the life of the lease.

The carrying value of long-lived assets is reviewed whenever events or changes in circumstances such as market value, asset utilization, physical change, legal factors or other matters indicate that the carrying value may not be recoverable. When the review indicates that the carrying value of the asset or group of assets representing the lowest level of identifiable cash flows exceeds the sum of the expected future cash flows (undiscounted and without interest charges), an impairment loss is recognized. The amount of the impairment loss is the amount by which the carrying value exceeds the fair value of the impaired asset or group of assets.

Field Support Spares

Field support spares are carried at cost and depreciated using the straight-line method over three years.

Engineering And Development

The Company has expensed all engineering and development costs to date.

Foreign Currency

The financial statements of the Company's international subsidiaries have been translated into U.S. dollars. Assets and liabilities are translated into U.S. dollars at year-end exchange rates, while equity accounts are translated at historical rates. Income and expenses are translated at the average exchange rates during the year. The resulting translation adjustments are recorded as a separate component of shareholders' equity.

The Company is exposed to market risks related to fluctuations in foreign exchange rates because some sales transactions, and the assets and liabilities of its foreign subsidiaries, are denominated in foreign currencies. As of January 31, 2002, the Company has hedged a portion of its risk by purchasing a forward exchange contract for 450,000 British pounds sterling that settles in February 2002. Gains and losses from transactions denominated in foreign currencies and forward exchange contracts are included in net income (loss).

The Company recognized foreign currency transaction gains in fiscal 2000 of $7,000. The Company recognized a foreign currency transaction loss in fiscal 2001 and 1999 of $106,000 and $196,000, respectively. Foreign currency transaction gains and losses in the one month transition period ended January 31, 2000 were not significant.

Stock Compensation Plans

The Company accounts for its stock based compensation awards in accordance with Accounting Principles Board Opinion No. 25 "Accounting for Stock Issued to Employees" (APB No. 25) and provides the footnote disclosures required by Statement of Financial Accounting Standards No. 123 "Accounting for Stock Based Compensation" (SFAS No. 123).

Reclassifications

Certain prior year amounts have been reclassified to conform to the current year presentation.

Use Of Estimates

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

Estimates that could significantly affect the results of operations or financial condition of the Company include the determination of the deferred tax asset, recoverability of goodwill, determination of deferred revenue, valuation of accounts receivable and valuation of inventory. Further discussion on these estimates can be found in related disclosures elsewhere in these notes to the consolidated financial statements.

Net Income (Loss) Per Share

Basic net income per share is computed based on the weighted average number of common shares outstanding, while diluted net income per share is computed based on the weighted average number of common shares outstanding plus potential dilutive shares of common stock. Potential dilutive shares of common stock include stock options which have been granted to employees and directors and awards under the employee stock purchase plan. Net loss per basic and diluted share is based on the weighted average number of common shares outstanding. Potential dilutive shares of common stock have been excluded from the computation of net loss per share due to their anti-dilutive effect.

Comprehensive Income (loss)

Comprehensive income (loss) consists of the Company's net income (loss), foreign currency translation adjustment and unrealized gains and losses from available-for-sale securities and is presented in the consolidated statement of shareholders' equity and comprehensive income (loss).

New Accounting Pronouncements

In July 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standard No. ("SFAS") 141, "Business Combinations," and SFAS 142, "Goodwill and Other Intangible Assets." SFAS 141 requires that the purchase method of accounting be used for all business combinations initiated after June 30, 2001 as well as all purchase method business combinations completed after June 30, 2001. SFAS 141 also specifies criteria that intangible assets must meet to be recognized and reported apart from goodwill. SFAS 142 requires that goodwill and intangible assets with indefinite useful lives, arising from acquisitions occurring after June 30, 2001, no longer be amortized, but instead be tested for impairment at least annually in accordance with the provisions of SFAS 142. Goodwill and intangible assets acquired in business combinations completed before July 1, 2001 continued to be amortized in accordance with appropriate pre-SFAS 142 and 144 requirements until February 1, 2002. SFAS 142 also requires that intangible assets with definite useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment in accordance with SFAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets."

SFAS 144, issued in October 2001, supercedes SFAS 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of," removing from its scope any reference to goodwill impairment and offering guidance on using cash flows to value long-lived assets. In addition, SFAS 144 supercedes the accounting and reporting provisions for the disposal of a business presented in Accounting Principles Board Opinion No. 30, "Reporting the Results of Unusual and Infrequently Occurring Events and Transactions," primarily by broadening the definition of a "discontinued operation" to include business components not considered business segments.

The Company adopted the provisions of SFAS 141 as of July 1, 2001 and SFAS 142, and SFAS 144 as of February 1, 2002.

Under transition provisions of SFAS 141 and SFAS 142, as of February 1, 2002, the Company must evaluate its existing intangible assets and goodwill that were acquired in a purchase business combination occurring before July 1, 2001, make any necessary reclassifications of intangible assets and goodwill to conform with the new criteria in SFAS 141 for recognition apart from goodwill, and conduct an impairment review of the carrying values of intangible assets and goodwill at that date. Also as of February 1, 2002, the Company will be required to reassess the useful lives and residual values of all intangible assets acquired in purchase business combinations, and make any necessary amortization period adjustments by April 30, 2002. Also by April 30, 2002, any intangible asset identified as having an indefinite useful life must be tested for impairment in accordance with the provisions of SFAS 142, and any impairment loss as of February 1, 2002 recognized as the cumulative effect of a change in accounting principle in the first quarter of 2002.

In connection with the transitional goodwill impairment evaluation, SFAS 142 requires the Company to perform an assessment by July 31, 2002 to determine whether goodwill was impaired as of the date of adoption. Any transitional impairment loss will be measured as of February 1, 2002 and reflected as a first quarter 2002 cumulative effect of a change in accounting principle in the Company's statement of earnings as soon as practicable but not later than January 31, 2003.

The pro forma effect of cessation of goodwill amortization prescribed by SFAS 142 would have increased earnings from continuing operations by $624,000, or $0.02 per diluted common share for fiscal year 2001.

Because of the extensive effort needed to implement SFAS 141, SFAS 142 and SFAS 144, it is not practicable to reasonably estimate the impact of their implementation on the Company's financial statements at the date of this report, including whether any transitional impairment losses will be required to be recognized as the cumulative effect of a change in accounting principle.

(2) Components of Selected Balance Sheet Accounts

	January 31, 2002	January 31, 2001
Inventories:		
Components and subassemblies	$22,391	$15,218
Work in process	3,834	2,813
Finished goods	5,185	4,416
	$31,410	$22,447
Property and equipment:		
Land	$ 1,186	$ —
Machinery and equipment	43,161	35,567
Office and data processing equipment	21,388	22,764
Furniture and fixtures	3,895	3,197
Leasehold improvements	2,183	1,856
	71,813	63,384
Less accumulated depreciation and amortization	46,209	38,169
	$25,604	$25,215
Field support spares:		
Field support spares	$22,704	$19,934
Less accumulated depreciation	18,142	15,488
	$ 4,562	$ 4,446
Goodwill and other intangibles:		
Purchased technology	$ —	$ 2,040
Customer list	505	—
Goodwill	15,042	866
	15,547	2,906
Less accumulated amortization	1,014	1,706
	$14,533	$ 1,200
Accrued liabilities:		
Compensation	$10,323	$ 8,986
Income taxes	3,084	2,450
Product warranty	1,935	1,629
Other	4,816	2,715
	$20,158	$15,780

(3) Marketable Securities

The Company's investments in marketable securities are summarized as follows:

	January 31, 2002	January 31, 2001
Available-for-Sale:		
Bank certificates of deposit	$35,096	$ 29,519
U.S. government and agency securities	10,362	10,866
Corporate debt securities	36,538	69,732
Corporate equity securities	1,068	—
	83,064	110,117
Trading:		
Standard & Poors 500 stock price index fund	258	514
NASDAQ 100 tracking stock	290	402
	$83,612	$111,033

The amount of gross unrealized gains with respect to investments in available-for-sale securities at January 31, 2002 was $809,000. The amount of gross unrealized gains and losses with respect to investments in available-for-sale securities at January 31, 2001 and December 31, 1999 was not significant. The Company realized a loss of $8,747,000 in 2001 from the sale of 232,511 shares of webMethods stock received in connection with the sale of IntelliFrame in 2001 (see note 5 to the consolidated financial statements). Proceeds from the sale of available-for-sale securities in fiscal 2001, 2000 and 1999 were $47,723,000, $1,204,000 and $984,000, respectively. There were no sales of available-for-sale securities during the one month transition period ended January 31, 2000. At January 31, 2002, the Company's investments in available-for-sale securities have contractual maturities of three years or less.

An additional loss of $1,536,000 was realized in 2001 when the remaining 41,031 shares of webMethods stock received in connection with the sale of IntelliFrame experienced a decline in value that was determined to be other than temporary, resulting in a write-down of the shares. The Company realized no other significant gains or losses with respect to available-for-sale securities during fiscal 2001, 2000, 1999 or the one-month transition period ended January 31, 2000.

The Company's trading securities consist of a mutual fund investment that seeks to provide a return corresponding to the Standard & Poors 500 stock price index and a NASDAQ 100 tracking stock. The Company intends to use any gain or loss from these investments to fund the investment gains or losses allocated to participants under the Company's executive deferred compensation plan. The amount of unrealized holding gains (losses) with respect to trading securities included in net income (loss) for fiscal 2001, 2000, 1999 and the one month transition period ended January 31, 2000 was $(266,000), $(168,000), $112,000, and $(11,995), respectively.

(4) Acquisitions

On April 3, 2001 the Company acquired all of the outstanding stock of Articulent Inc., a privately held, leading provider of storage solutions and services for $12,360,000 in cash, plus the assumption of approximately $24,394,000 of liabilities and the acquisition of approximately $19,333,000 of tangible assets. The agreement includes a potential $10,000,000 incentive payout based upon meeting certain revenue and earnings milestones over the twelve months beginning May 1, 2001. The Company does not anticipate that the revenue and earnings milestones required for the incentive payout will be achieved. The acquisition was accounted for as a purchase and the consolidated financial statements of the Company include the results of Articulent since April 3, 2001. The purchase price was allocated to the fair value of the assets and liabilities acquired as follows:

Purchase Price:	
Cash paid	$12,360
Fair Value of Assets Acquired and Liabilities Assumed:	
Cash	$ 624
Accounts receivable	10,287
Inventory	4,446
Fixed assets	3,393
Customer list	505
Goodwill	13,809
Deferred taxes	3,107
Other assets	583
Accounts payable	(18,302)
Accrued expenses	(2,324)
Note payable	(3,768)
Total purchase consideration	$12,360

The following table presents the unaudited pro forma consolidated results of operations of the Company for the year ended January 31, 2002 and 2001 as if the acquisition of Articulent took place on February 1, 2001 and 2000, respectively:

	Pro Forma Year Ended January 31,	
	2002	2001
Total revenue	$194,740	$245,030
Net income (loss)	$ (5,772)	$ 2,454
Net income (loss) per share	$ (.19)	$ .09

The pro-forma results include amortization of the customer list and goodwill presented above. The unaudited pro-forma results are for comparative purposes only and do not necessarily reflect the results that would have been recorded had the acquisition occurred at the beginning of the period presented or the results which might occur in the future.

(5) Discontinued Operations

Propelis Software, Inc. formerly known as the Enterprise Integration Solutions Division, including IntelliFrame, developed and sold EAI software that automates the integration of computer software applications, and business workflow processes. In August 2000, the Company determined to divest Propelis Software, Inc. and focus on its core storage networking business. As a result, Propelis Software, Inc. has been accounted for as a discontinued operation in the accompanying financial statements.

On February 2, 2001 the Company sold all of the outstanding stock of IntelliFrame Corporation, including the technology underlying the Propelis BPm™ product, to webMethods, Inc. for $8,800,000 in cash and 273,542 shares of webMethods common stock. The stock received from webMethods, Inc. was valued at $17,058,000, which reflects a discount from its publicly reported trading price due to the initial restrictions placed on the Company's ability to freely sell the stock. In connection with this transaction, the Company paid $3,000,000 to two employees, who were former shareholders of IntelliFrame, to satisfy all obligations to make further bonus payments under their employment agreements. The sale resulted in an after tax gain of $12,620,000 in the first quarter of 2001.

In the first quarter of 2001, the Company accrued $9,250,000 for the estimated future operating losses of Propelis Software, Inc. through the potential date of divestiture, resulting in an after tax loss of $6,197,000.

In August 2001, the Company sold substantially all of the remaining assets and liabilities of Propelis Software, Inc. to Jacada Ltd. for $6,000,000 in cash, plus a warrant to purchase 350,000 ordinary shares of Jacada Ltd. stock at a price of $3.26 per share. The final sales price was subject to adjustment based on the closing balance sheet of Propelis. The transaction resulted in an after tax gain of $1,799,000 in the third quarter of 2001.

(6) Leases

The Company leases all office and manufacturing space and certain equipment under noncancelable capital and operating leases. At January 31, 2002 and 2001, leased capital assets included in property and equipment were as follows:

	January 31, 2002	January 31, 2001
Property and equipment:		
Office and data processing equipment	$4,836	$4,557
Less accumulated amortization	2,605	842
	$2,231	$3,715

Future minimum lease payments, excluding executory costs such as real estate taxes, insurance and maintenance expense, by year and in the aggregate are as follows:

	Minimum Lease Commitments Capital	Minimum Lease Commitments Operating
Year Ending January 31,		
2003	$1,667	$ 5,408
2004	742	3,775
2005	—	2,826
2006	—	2,572
2007	—	2,543
Thereafter	—	10,010
Total minimum lease payments	2,409	27,134
Less minimum sublease income	—	272
Net minimum lease payments	2,409	$26,862
Less amounts representing interest at rates ranging from 8.89% to 11.29%	178	
Present value of minimum capital lease payments	2,231	
Less current installments	1,523	
Obligations under capital lease, less current installments	$ 708	

Rent expense under noncancelable operating leases, exclusive of executory costs, for fiscal 2001, 2000, 1999 and the one month transition period ended January 31, 2000 was $5,857,000, $5,315,000, $3,970,000 and $430,888, respectively. During the year ended December 31, 1999, the Company recognized a $1,331,000 charge for the future costs associated with a facility that was abandoned prior to expiration of the lease term. During the year ended January 31, 2001, the Company reversed $287,000 representing the unused portion of the accrual for the abandoned facility.

(7) Shareholders' Equity

Common Stock Repurchase

In April 2001, the Company's board of directors authorized the repurchase of up to $50,000,000 of the Company's common stock. During 2001, the Company repurchased 90,000 shares of its common stock for $787,000 pursuant to this authorization.

Rights Plan

On July 24, 1998 the Company's board of directors adopted a shareholders rights plan pursuant to which rights were distributed as a dividend at the rate of one preferred share purchase right for each outstanding share of common stock of the Company. The rights will expire on July 23, 2008 unless extended, earlier redeemed or exchanged by the Company.

Stock Options And Restricted Stock

The Company maintains stock option and restricted stock plans (the Plans) which provide for the grant of stock options, restricted stock and stock based awards to officers, other employees, consultants, and independent contractors as determined by the compensation committee of the board of directors. A maximum of 11,780,000 shares of common stock were issuable under the terms of the Plans as of January 31, 2002, of which no more than 3,830,000 shares may be issued as restricted stock or other stock based awards. As of January 31, 2002, there were 2,299,000 shares of common stock available for future grants under these plans.

Restricted stock issued under the Plans is recorded at fair market value on the date of grant and generally vests over a two to four year period. Vesting for some grants may be accelerated if certain performance criteria are achieved. Compensation expense is recognized over the applicable vesting period. During fiscal 2001, 2000, 1999 and the one month transition period ended January 31, 2000, the Company issued 106,000, 61,100, 90,250 and 3,000 restricted shares, respectively, having an aggregate weighted fair market value per share of $10.63, $17.43, $16.25 and $17.44, respectively. Compensation expense recognized for restricted shares in fiscal 2001, 2000, 1999 and the one month transition period ended January 31, 2000 was $568,000, $346,000, $219,000 and $49,000, respectively.

All stock options granted under the Plans have an exercise price equal to fair market value on the date of grant, vest and become exercisable over individually defined periods, generally four years, and expire ten years from the date of grant. During fiscal 1999, stock options for 800,000 shares were granted at an exercise price of $21.88 and vest after six years. The options did provide for acceleration of vesting upon certain increases in the Company's stock price. In March of 2001, the vesting for these options was changed to ratably over a four-year period from the original date of grant. As of January 31, 2002, 50% of these options were vested.

A summary of the status of the Company's outstanding stock options and related changes for fiscal 2001, 2000, 1999 and the one month transition period ended January 31, 2000 is presented below:

	Years Ended January 31,				Year Ended December 31,		Month Ended January 31,	
	2002		2001		1999		2000	
Options	Shares	Weighted-Average Exercise Price	Shares	Weighted Average Exercise Price	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Outstanding at beginning of period	4,655	$13.45	4,798	$10.02	4,972	$ 5.63	4,678	$ 9.78
Granted	2,666	9.71	1,552	18.77	1,689	18.40	165	15.29
Exercised	(549)	7.61	(1,123)	5.93	(1,540)	5.54	(21)	4.89
Canceled	(1,019)	15.30	(572)	13.92	(443)	10.79	(24)	8.69
Outstanding at end of period	5,753	$11.99	4,655	$13.45	4,678	$ 9.78	4,798	$10.02
Exercisable at end of period	2,107	$11.01	1,633	$ 8.08	1,901	$ 6.31	1,870	$ 6.39
Weighted-average fair value of grants during the period		$ 7.26		$13.56		$12.68		$12.82

The following table summarizes information about stock options outstanding at January 31, 2002:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted-Average Remaining Contractual Life (in years)	Weighted-Average Exercise Price	Number Exercisable	Weighted-Average Exercise Price
$ 3.50 - $ 4.99	598	5.4	$ 4.42	500	$ 4.37
$ 5.00 - $ 7.99	523	4.2	$ 6.05	499	$ 6.03
$ 8.00 - $14.99	3,020	8.7	$10.01	530	$11.22
$15.00 - $19.99	697	8.0	$17.64	171	$17.51
$20.00 - $32.75	915	7.6	$22.56	407	$22.24
	5,753			2,107	

Employee Stock Purchase Plan

The 1992 Employee Stock Purchase Plan (the Purchase Plan) allows eligible employees an opportunity to purchase an aggregate of 1,100,000 shares of the Company's common stock at a price per share equal to 85% of the lesser of the fair market value of the Company's common stock at the beginning or the end of each six-month purchase period. Under the terms of the Purchase Plan, no participant may acquire more than 5,000 shares of the Company's common stock or more than $5,000 in aggregate fair market value of common stock (as defined) during any six-month purchase period. Common shares sold to employees under the Purchase Plan in fiscal 2001, 2000 and 1999 were 163,705, 102,920 and 86,972, respectively. No shares were sold to employees under the Purchase Plan in the one month transition period ended January 31, 2000.

The fair value of each purchase right granted in fiscal 2001, 2000 and 1999 was $7.34, $3 72 and $6.38, respectively.

Stock Compensation

The Company has elected to continue to account for its plans in accordance with APB No. 25. Accordingly, no compensation cost related to stock option grants or shares sold to employees under the Employee Stock Purchase Plan has been recognized in the Company's financial statements. Had compensation cost for the Company's stock-based compensation plans been recognized consistent with the fair value method of SFAS No. 123, the Company's net income (loss) and net income (loss) per basic and diluted share would have been reduced to the pro forma amounts indicated below:

	Years Ended January 31, 2002	Years Ended January 31, 2001	Year Ended December 31, 1999	Month Ended January 31, 2000
Net income (loss):				
As reported	$ (3,706)	$11,994	$4,655	$(3,625)
Pro forma	$(10,815)	$ 5,626	$ (795)	$(4,032)
Net income (loss) per share:				
As reported				
Basic	$ (.12)	$ .47	$ .20	$ (.15)
Diluted	$ (.12)	$ .43	$ .18	$ (.15)
Pro forma				
Basic	$ (.36)	$ .22	$ (.03)	$ (.17)
Diluted	$ (.36)	$ .20	$ (.03)	$ (.17)

In determining the compensation cost of stock option grants and shares sold to employees under the employee stock purchase plan, as specified by SFAS No. 123, the fair value of each award has been estimated on the date of grant using the Black-Scholes option pricing model. The weighted average assumptions used in these calculations are summarized below:

	Years Ended January 31, 2002	Years Ended January 31, 2001	Year Ended December 31, 1999	Month Ended January 31, 2000
Risk free interest rate	4.51%	5.90%	5.64%	6.66%
Expected life	5.73	5.33	5.23	4.22
Expected volatility	86.88%	85.06%	79.66%	80.61%

(8) Net Income (Loss) Per Share

The components of net income (loss) per basic and diluted share are as follows:

	Net Income (loss)	Weighted Average Shares Outstanding	Per Share Amount
Years Ended January 31,			
2002:			
Basic	$(3,706)	29,892	$(.12)
Dilutive effect of employee stock purchase awards and options	—	—	—
Diluted	$(3,706)	29,892	$(.12)
2001:			
Basic	$11,994	25,383	$ .47
Dilutive effect of employee stock purchase awards and options	—	2,430	(.04)
Diluted	$11,994	27,813	$ .43
Year Ended December 31, 1999			
Basic	$ 4,655	23,137	$ .20
Dilutive effect of employee stock purchase awards and options	—	2,681	(.02)
Diluted	$ 4,655	25,818	$ .18
Month Ended January 31, 2000			
Basic	$(3,625)	23,815	$(.15)
Dilutive effect of employee stock purchase awards and options	—	—	—
Diluted	$(3,625)	23,815	$(.15)

The total weighted average number of common stock equivalents excluded from the calculation of potentially dilutive securities due to the inclusion of such securities in a calculation of net loss per share would have been anti-dilutive for the year ended January 31, 2002 and the one month transition period ended January 31, 2000 were 1,292,016 and 2,029,084, respectively.

(9) Income Taxes

The components of income from continuing operations before income taxes and income tax expense (benefit) for each of the years in the three-year period ended January 31, 2002 and the one month transition period ended January 31, 2000 consists of the following:

	Years Ended January 31, 2002	Years Ended January 31, 2001	Year Ended December 31, 1999	Month Ended January 31, 2000
Income (loss) from continuing operations before income taxes:				
U.S	$(17,756)	$19,595	$ 6,356	$(3,511)
Foreign	536	4,481	199	(389)
Total	$(17,220)	$24,076	$ 6,555	$(3,900)
Income tax provision:				
Current:				
U.S	$ —	$ 5,180	$ 3,356	$ 52
Foreign	284	1,348	60	—
State	—	1,027	749	11
Total current	284	7,555	4,165	63
Deferred:				
U.S	(5,198)	458	(1,525)	(1,133)
State	(378)	(66)	(411)	(217)
Total deferred	(5,576)	392	(1,936)	(1,350)
Total income tax expense (benefit)	$ (5,292)	$ 7,947	$ 2,229	$(1,287)

The reconciliation of the statutory federal tax rate and the effective tax rate for each of the years in the three-year period ended January 31, 2002 and the one-month transition ended January 31, 2000 is as follows:

	Years Ended January 31, 2002	Years Ended January 31, 2001	Year Ended December 31, 1999	Month Ended January 31, 2000
Statutory tax rate	34.0%	34.0%	34.0%	34.0%
Increase (decrease) in taxes resulting from:				
State taxes, net of federal tax benefit	3.3	2.6	3.4	3.3
Extraterritorial income and foreign sales corporation	.5	(1.9)	(5.3)	—
Meals and entertainment	(.6)	.4	1.1	(.1)
Valuation allowance	(4.8)	—	—	—
Other	(1.7)	(2.1)	.8	(4.2)
Total	30.7%	33.0%	34.0%	33.0%

The tax effects of temporary differences that give rise to significant portions of the Company's deferred tax assets and (liabilities) as of January 31, 2002 and 2001 were as follows:

	Years Ended January 31,	
	2002	2001
Deferred tax assets:		
Inventory	$ 4,658	$ 2,725
Accrued compensation	1,145	1,026
Reserves for bad debts and sales returns	636	694
Foreign net operating loss carryforwards	410	410
Federal and state tax credits	1,265	2,130
Federal and state net operating loss carryforwards	7,895	4,268
Write down of webMethods stock	1,071	—
Other	900	714
Total gross deferred tax assets	17,980	11,967
Valuation allowance	(1,240)	(410)
Net deferred tax assets	16,740	11,557
Deferred tax liabilities:		
Property and equipment	(109)	(343)
Other	(449)	(385)
Total gross deferred tax liabilities	(558)	(728)
Net deferred tax assets	$16,182	$10,829

The Company recorded a valuation allowance at January 31, 2002 and 2001 of $1,240,000 and $410,000, respectively. The valuation allowance at January 31, 2001 was related to certain foreign net operating loss carryforwards. The valuation allowance was increased by $830,000 in 2001 for the tax benefits associated with certain foreign and state tax credits and state net operating loss carryforwards. Utilization of these tax benefits in future periods was determined to be unlikely. At January 31, 2002, the Company had net operating loss and credit carryforwards available for federal tax purposes of approximately $19,986,000 and $909,000, respectively, which will expire between the years 2019 and 2022.

The Company has assessed its taxable earnings history and prospective future taxable income. Based on this assessment, management has determined that it is more likely than not that its remaining net deferred tax assets will be realized in future periods. The Company may be required to provide a valuation allowance for this asset in the future if it does not generate sufficient taxable income as planned.

(10) Annual Bonus Plan

The Company's Annual Bonus Plan provides a formula for determination of cash bonus payments to eligible employees based on a defined percentage of a participant's qualifying base compensation multiplied by the Company's annual bonus plan factor. The annual bonus plan factor is based on a chart which outlines payout percentages for achievement of defined levels of revenue and operating profit as a percentage of revenue.

The annual bonus expense for fiscal 2001, 2000, and 1999 was $1,134,000, $2,035,000 and $420,000, respectively. There was no bonus for the one month transition period ended January 31, 2000.

(11) 401(k) and Deferred Compensation Plans

The Company has a 401(k) salary savings plan which covers substantially all of its employees. The Company matches 100% of a participant's annual plan contributions up to an annual maximum per participant of $2,500 which vests over a four year period from the participant's date of hire.

The Company has also established an executive deferred compensation plan for selected key employees which allows participants to defer a substantial portion of their compensation each year. The Company matches 20% of a participant's annual plan contributions up to an annual maximum per participant of $10,000. Matching contributions vest over a four year period from the later of July 1, 1997 or the participant's date of hire. In addition, the Company provides participants with an annual earnings credit based on the investment indexes selected by the participant prior to the start of each plan year.

The Company's expense under the 401(k) and deferred compensation plans for fiscal 2001, 2000, 1999 and the one month transition period ended January 31, 2000 was $1,969,000, $1,132,000, $470,000 and $329,000, respectively.

(12) Segment Information

The Company has two reportable segments consisting of its Networking Solutions business unit and Storage Solutions business unit. The Networking Solutions business unit consists of our storage and channel networking products and related services. The Storage Solutions business consists of our storage networking design and implementation services and the storage management business we acquired from Articulent in April of 2001. The Company's two reportable segments are strategic business units that offer different products and services. They are managed separately because each business requires different market strategies. The Company evaluates performance based on operating profit or loss before special charges and income taxes.

Reportable Segment Information:

	Years Ending January 31, 2002	Years Ending January 31, 2001	Year Ended December 31, 1999	Month Ended January 31, 2000
Revenue:				
Networking Solutions	$136,866	$163,468	$121,410	$ 4,278
Storage Solutions	50,157	12,638	4,579	64
Total	$187,023	$176,106	$125,989	$ 4,342
Income (Loss) from Operations:				
Networking Solutions	$ (4,773)	$ 20,914	$ 6,706	$ (3,804)
Storage Solutions	(4,380)	(277)	2,484	(189)
Special charges	(3,321)	287	(2,745)	—
Total	$(12,474)	$ 20,924	$ 6,445	$ (3,993)
Depreciation and amortization:				
Networking Solutions	$ 13,246	$ 11,755	$ 9,070	$ 645
Storage Solutions	1,881	57	13	7
Total	$ 15,127	$ 11,812	$ 9,083	$ 652

	Years Ending January 31, 2002	Years Ending January 31, 2001	Year Ended December 31, 1999	Month Ended January 31, 2000
Expenditures for long-lived assets:				
Networking Solutions	$ 9,865	$ 17,023	$ 10,930	$ 798
Storage Solutions	1,103	201	59	15
Total	$ 10,968	$ 17,224	$ 10,989	$ 813
Total assets (end of period):				
Networking Solutions	$235,776	$264,868	$109,444	$105,301
Storage Solutions	33,962	3,755	1,210	1,212
Total	$269,738	$268,623	$110,654	$106,513
Foreign Operations Information:				
Revenue:				
United States	$140,667	$123,717	$ 82,494	$ 3,620
United Kingdom	17,245	16,554	13,402	490
France	6,327	5,213	4,348	86
Other	22,784	30,622	25,745	146
Total	$187,023	$176,106	$125,989	$ 4,342
Long-lived assets (end of period):				
United States	$ 43,897	$ 29,678	$ 21,464	$ 21,497
United Kingdom	693	856	901	918
Other	109	327	265	268
Total	$ 44,699	$ 30,861	$ 22,630	$ 22,683

Revenue has been attributed to the country where the end-user customer is located.

No single customer accounted for more than 10% of the Company's total revenue in fiscal 2001, 2000 or 1999. For the one month transition period ended January 31, 2000, sales of DXE product and service to StorageTek for our Networking Solutions segment accounted for 22% of total revenue.

(13) Noncash Financing and Investing Activities and Supplemental Cash Flow Information

Cash payments for interest expense in fiscal 2001, 2000, 1999 and the one month transition period ended January 31, 2000 were $285,000, $338,000, $222,000 and $6,000, respectively.

Cash payments for income taxes, net of refunds received, in fiscal 2001, 2000 and 1999 were $17,000, $3,286,000 and $2,116,000, respectively. There were no cash payments for income taxes or refunds received during the one month transition period ended January 31, 2000.

During fiscal 2001, 2000, 1999 and the one month transition period ending January 31, 2000, the Company entered into capital lease obligations for equipment valued at $279,000, $1,849,000, $653,000 and $307,000, respectively.

During fiscal 2001 and 2000, deferred tax assets increased by $994,000 and $5,736,000, respectively, as a result of the tax benefit from employee stock transactions which could not be currently utilized.

(14) Disclosures about Fair Value of Financial Instruments

The carrying amount for cash and cash equivalents, accounts receivable and long-term obligations approximates fair value because of the short maturity of those instruments. Marketable securities are recorded at market value at January 31, 2002.

(15) Related Party Transactions

During 2001, the Company purchased $491,000 of bandwidth from Dynegy Connect, an entity wholly owned by Dynegy Global Communications. At January 31, 2002 the Company has commitments to purchase $1.2 million of additional bandwidth from Dynegy Connect through fiscal 2006. All of the bandwidth purchases were for re-sale under specific agreements to customers at a profit. The bandwidth was purchased from Dynegy Connect because they offered the best pricing. The Company has purchased bandwidth from competitors of Dynegy Connect when their pricing has been more attractive. The Company's board member, Lawrence McLernon, is chief executive officer of Dynegy Global Communications.

(16) Subsequent Event

In February 2002, the Company sold $125 million of 3% convertible subordinated notes due February 2007, raising net proceeds of $121 million. The notes are convertible into our common stock at a price of $19.17 per share. The Company may redeem the notes upon payment of the outstanding principal balance, accrued interest and a make whole premium if the closing price of the Company common stock exceeds 175% of the conversion price for at least 20 consecutive trading days within a period of 30 consecutive trading days ending on the trading day prior to the date we mail the redemption notice.

INDEPENDENT AUDITORS' REPORT

The Board of Directors and Shareholders
Computer Network Technology Corporation:

We have audited the accompanying consolidated balance sheets of Computer Network Technology Corporation and subsidiaries as of January 31, 2002 and 2001, and the related consolidated statements of operations, shareholders' equity and comprehensive income (loss), and cash flows for the years ended January 31, 2002 and 2001, the year ended December 31, 1999, and the one month transition period ended January 31, 2000. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Computer Network Technology Corporation and subsidiaries as of January 31, 2002 and 2001, and the results of their operations and their cash flows for the years ended January 31, 2002 and 2001, the year ended December 31, 1999, and the one month transition period ended January 31, 2000, in conformity with accounting principles generally accepted in the United States of America.

/s/ KPMG LLP

Minneapolis, Minnesota
February 25, 2002

QUARTERLY FINANCIAL DATA
(unaudited)

	Years Ended January 31, 2002 and 2001			
	First Quarter(2)	Second Quarter	Third Quarter(3)	Fourth Quarter
	(in thousands, except per share data)			
2001(1)				
Revenue	$ 29,413	$41,583	$55,362	$60,665
Gross profit	10,465	16,560	22,027	24,389
Income (loss) from operations	(10,478)	(2,597)	(326)	927
Income from discontinued operations, net of tax	6,423	—	1,799	—
Net income (loss)	(6,555)	(821)	2,398	1,272
Net income (loss) per share:				
Basic	(.22)	(.03)	.08	.04
Diluted	(.22)	(.03)	.08	.04
2000(1)				
Revenue	$ 38,607	$44,341	$46,198	$46,960
Gross profit	20,332	24,091	24,206	24,296
Income from operations	2,887	5,701	6,516	5,820
Loss from discontinued operations, net of tax	(116)	(1,903)	(1,150)	(966)
Net income	1,830	2,053	3,705	4,406
Net income per share:				
Basic	.08	.09	.15	.15
Diluted	.07	.08	.13	.14

(1) We divested Propelis Software, Inc. formerly known as our Enterprise Integration Solutions Division to focus all of our resources on our core storage networking business. Accordingly, the financial information for Propelis Software, Inc. has been accounted for as discontinued operations.

(2) Continuing operations for the first quarter of fiscal 2001 includes a $2.0 million write down of inventory, a $325,000 write-off of our FileSpeed product and a $1.0 million restructuring charge. Continuing operations also includes a loss on the sale and write-down of webMethods stock of $10.3 million. Discontinued operations for the first quarter of fiscal 2001 includes a provision of $6.2 million, net of tax, to accrue for the estimated future operating losses of Propelis Software, Inc. through the expected date of divestiture. Discontinued operations for the first quarter of 2001 includes an after tax gain of $12.6 million resulting from the sale of IntelliFrame.

(3) Continuing operations for the third quarter of fiscal 2000 includes a reversal of the unused balance of a 1999 fourth quarter accrual for an abandoned facility. The amount of the reversal was $287,000. Discontinued operations for the third quarter of fiscal 2001 includes an after tax gain of $1.8 million from the sale of substantially all of the remaining assets and liabilities of Propelis Software, Inc. to Jacada Ltd.

Item 9. Changes in and Disagreements with Accountants and Financial Disclosure

None.

PART III

Item 10. Directors and Executive Officers

The information set forth under the captions "Election of Directors" and "Section 16(a) Beneficial Ownership Reporting Compliance" in the definitive Proxy Statement for the Annual Meeting of Shareholders to be held on June 25, 2002, to be filed with the Securities and Exchange Commission (the "Commission") on or before May 26, 2002, is incorporated herein by reference. For information concerning the executives officers, see Item 4A of this Annual Report on Form 10K.

Item 11. Executive Compensation

The information set forth under the captions "Summary Compensation Table," "Option Tables," "Employment Agreements," "Election of Directors — Compensation of Directors," "Internal Revenue Code Section 162(m)" and "Comparative Stock Price Performance" in the definitive Proxy Statement for the Annual Meeting of Shareholders to be held on June 25, 2002, to be filed with the Commission on or before May 26, 2002, is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management

The information set forth under the captions "Security Ownership of Certain Beneficial Owners and Management" in the definitive Proxy Statement for the Annual Meeting of Shareholders to be held on June 25, 2002, to be filed with the Commission on or before May 26, 2002, is incorporated herein by reference.

Item 13. Certain Relationships and Related Transactions

During 2001, we purchased $491,000 of bandwidth from Dynegy Connect, an entity wholly owned by Dynegy Global Communications. At January 31, 2002 we have commitments to purchase $1.2 million of additional bandwidth from Dynegy Connect through fiscal 2006. All of the bandwidth purchases were for re-sale under specific agreements to customers at a profit. The bandwidth was purchased from Dynegy Connect because they offered us the best pricing. We have purchased bandwidth from competitors of Dynegy Connect when their pricing has been more attractive. Our board member, Lawrence McLernon, is chief executive officer of Dynegy Global Communications.

PART IV

Item 14. Exhibits, Consolidated Financial Statement Schedules, and Reports on Form 8-K.

(a) 1. Consolidated Financial Statements and Schedules of Registrant

Consolidated Statements of Operations for the Years Ended January 31, 2002 and 2001, December 31, 1999, and the one month transition period ended January 31, 2000.

Consolidated Balance Sheets as of January 31, 2002 and 2001.

Consolidated Statements of Shareholders' Equity and Comprehensive Income (Loss) for the Years Ended January 31, 2002 and 2001, December 31, 1999, and the one month transition period ended January 31, 2000.

Consolidated Statements of Cash Flows for the Years Ended January 31, 2002 and 2001, December 31, 1999, and the one month transition period ended January 31, 2000.

Notes to Consolidated Financial Statements

Independent Auditors' Report

(a) 2. Consolidated Financial Statement Schedule of Registrant

Independent Auditors' Report on Consolidated Financial Statement Schedule

Schedule II: Valuation and Qualifying Accounts for the Years Ended January 31, 2002 and 2001, December 31, 1999 and the one month transition period ended January 31, 2000.

All other schedules are omitted as the required information is inapplicable or is presented in the consolidated financial statements or related notes thereto.

Schedule II

COMPUTER NETWORK TECHNOLOGY CORPORATION

Valuation and Qualifying Accounts

Years ended January 31, 2002, 2001 and December 31, 1999 and the One Month Transition period ended January 31, 2000 (in thousands)

Description	Balance at beginning of period	Additions: Charged to costs & expenses	Additions: Charged to other account	Deductions	Balance at end of period
Year ended January 31, 2002					
Allowance for doubtful accounts and sales returns	$2,383	898	—	(1,433)	$1,848
Year ended January 31, 2001					
Allowance for doubtful accounts and sales returns	$1,128	1,600	—	(345)	$2,383
One month period ended January 31, 2000					
Allowance for doubtful accounts and sales returns	$ 959	169	—	—	$1,128
Year ended December 31, 1999					
Allowance for doubtful accounts and sales returns	$1,225	519	—	(785)	$ 959

INDEPENDENT AUDITORS' REPORT ON FINANCIAL STATEMENT SCHEDULE

The Board of Directors and Shareholders
Computer Network Technology Corporation:

Under the date of February 25, 2002, we reported on the consolidated balance sheets of Computer Network Technology Corporation and subsidiaries as of January 31, 2002 and 2001, and the related consolidated statements of operations, shareholders' equity and comprehensive income (loss), and cash flows for the years ended January 31, 2002 and 2001, the year ended December 31, 1999, and the one month transition period ended January 31, 2000 as contained in the fiscal 2001 annual report on Form 10-K. These consolidated financial statements and our report thereon are included in the annual report on Form 10-K for fiscal 2001. In connection with our audits of the aforementioned consolidated financial statements, we also have audited the related financial statement schedule as listed in the accompanying index. This financial statement schedule is the responsibility of the Company's management. Our responsibility is to express an opinion on the financial statement schedule based on our audits.

In our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

/s/ KPMG LLP

Minneapolis, Minnesota
February 25, 2002

(a) 3. Exhibits

The Company undertakes to furnish to any shareholder so requesting a copy of any of the following exhibits upon payment to the Company of the reasonable costs incurred by the Company in furnishing any such exhibit.

Exhibit	Description
2.	Purchase Agreement as of April 3, 2001 between Computer Network Technology Corporation and Ernest J. Parsons (Articulent, Inc.).(2)
3.1	Second Restated Articles of Incorporation of the Company. (Incorporated by reference to Exhibits 3(i)-1 and 3(i)-2 to current report on Form 8-K dated May 25, 1999.)
3.2	Articles of Amendment of the Second Restated Articles of the Company. (Incorporated by reference to Exhibit 3(i)-1 to current report on Form 8-K dated May 25, 1999.)
3.3	By-laws of the Company. (Incorporated by reference to Exhibit 3(ii)-1 to current report on Form 8-K dated May 25, 1999.)
4.1	Rights Agreement between the Company and Chase Mellon Shareholder Services, L.L.C., as Rights Agent including the form of Rights Certificate and the Summary of Rights to Purchase Preferred Shares. (Incorporated by reference to Exhibit 1 to Form 8-A dated July 29, 1998 and Exhibit 1 to Form 8-A/A dated November 27, 2000.)
4.2	First Amendment of Rights Agreement dated November 21, 2000. (Incorporated by Reference to Exhibit 1 to Form 8-A/A dated November 27, 2000.)
4.3	First Amendment of Certificate of Designations, Preferences and Rights of Series A Junior Participating Preferred Stock. ($.01 Par Value Per Share) of Computer Network Technology Corporation (Incorporated by reference to Exhibit 2 to Form 8-A/A dated November 27, 2000.)
4.4	Form of Common Stock Certificate. (Incorporated by reference to Exhibit 4.2 to Form S-3 Registration Statement No. 333-80841.)
4.5	Registration Rights Agreement, dated as of February 20, 2002, among Bear, Sterns & Co. Inc., SG Cowan Securities Corporation and Soundview Technology Corporation(2)
4.6	Indenture, dated as of February 20, 2002, between the Company and U.S. Bank National Association, as Trustee(2)
4.7	Form of Note (included in Exhibit 4.6)(2)
10.1	Amended 1992 Stock Award Plan.(1)(2)
10.2	Amended and Restated 1999 Non-Qualified Stock Award Plan.(2)
10.3	March 10, 1994 Incentive Stock Option Agreements. (Incorporated by reference to Exhibit 28.2 Form S-8 Registration Statement No. 33-83266.)(1)
10.4	March 10, 1994 Non-Qualified Stock Option Agreements. (Incorporated by reference to Exhibit 28.3 Form S-8 Registration Statement No. 33-83266.)(1)
10.5	Building Lease by and between Opus Northwest, L.L.C., and Computer Network Technology Corporation. (Incorporated by reference to Exhibit 10A Form 10Q for the quarterly period ended September 30, 1998.)
10.6	Employment Agreement by and between the Company and Thomas G. Hudson as amended. (Incorporated by reference to Exhibit 10Z Form 10-Q for the quarterly period ended June 30, 1996.)(1)
10.7	CNT's 2002 Annual Bonus Plan.(1)(2)
10.8	Employment Agreement by and between the Company and Mark Knittel. (Incorporated by reference to Exhibit 10AA Form 10-K for the year ended December 31, 1997.)(1)

Exhibit	Description
10.9	Amendment to CNT Executive Deferred Compensation Plan. (Incorporated by reference to Exhibit 10I Form 10-K for the year ended January 31, 2001.)(1)
10.10	Employment/Non-Compete Agreement by and between the Company and Nick V. Ganio. (Incorporated by reference to Exhibit 10Q to Form 10-K for the Year Ended December 31, 1998.)(1)
10.11	1997 Restricted Stock Plan.(1)(2)
10.12	Articulent One-Time Bonus Plan (Incorporated by reference to Exhibit 99.2 to Form 8-K dated April 3, 2001.)(1)
10.13	Amended and Restated 1992 Employee Stock Purchase Plan(1)(2)
10.14	2002 Stock Award Plan(1)(2)
12.	Ratio of Earnings to Fixed Charges(2)
21.	Subsidiaries of the Registrant.(2)
23.	Independent Auditors' Consent.(2)
99.1	Cautionary Statements.(2)
99.2	Calculation of Additional Purchase Price to be Paid in Connection with Acquisition of Articulent, Inc. (Incorporated by reference to Exhibit 99.1 to Form 8-K dated April 3, 2001).

(1) Management contracts or compensatory plans or arrangements with the Company.

(2) Filed herewith.

(b) Reports on Form 8-K

No filings were made on Form 8-K during the quarterly period ended January 31, 2002.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

COMPUTER NETWORK TECHNOLOGY CORPORATION

Dated: April 12, 2002

By: /s/ THOMAS G. HUDSON

Thomas G. Hudson, President and Chief Executive Officer (Principal Executive Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

/s/ THOMAS G. HUDSON Thomas G. Hudson	President and Chief Executive Officer (Principal Executive Officer) and Director	April 24, 2002
/s/ GREGORY T. BARNUM Gregory T. Barnum	Vice President of Finance, Chief Financial Officer and Secretary (Principal Financial Officer)	April 24, 2002
/s/ JEFFREY A. BERTELSEN Jeffrey A. Bertelsen	Corporate Controller and Treasurer (Principal Accounting Officer)	April 24, 2002
/s/ PATRICK W. GROSS Patrick W. Gross	Director	April 24, 2002
/s/ ERWIN A. KELEN Erwin A. Kelen	Director	April 24, 2002
/s/ LAWRENCE MCLERNON Lawrence McLernon	Director	April 24, 2002
/s/ JOHN A. ROLLWAGEN John A. Rollwagen	Director	April 24, 2002

INDEX TO EXHIBITS

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(1) Management contracts or compensatory plans or arrangements with the Company.

(2) Filed herewith.

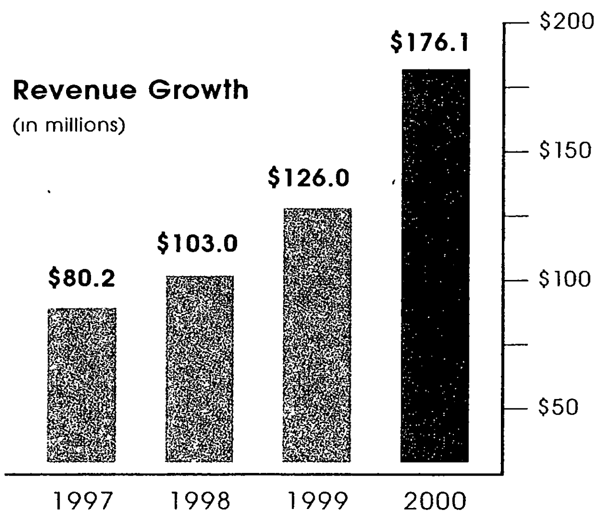
About CNT

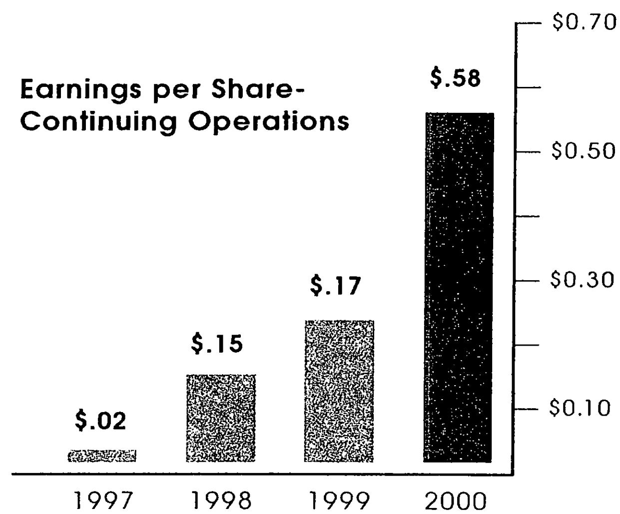
CNT is the global specialist in storage networking, delivering innovative solutions that drive superior business results for its customers. CNT solutions are relied on by organizations around the world to integrate business-critical applications and storage environments so their information is safe and accessible to all that need it—anytime, anywhere.

Through an intelligent combination of innovative technology and professional services, CNT's storage networking solutions provide organizations with the confidence and enthusiasm to use technology to connect and manage information, the most important corporate asset.

CNT provides storage networking products and services for all types of organizations, from Fortune 500 corporations to Global 2000 businesses. More than half of the Fortune 100 companies are CNT customers. Our strategic partnerships include the world's leading enterprise storage, software and platform vendors.

A global company based in Minneapolis, Minnesota, CNT has more than 790 employees, five international operating subsidiaries, over 20 international distributors and customers in 30 countries. CNT is listed on the Nasdaq National Market System under the symbol CMNT.





(in thousands, except per share data)	**2000**	1999	1998	1997
Total revenue	**$176,106**	$125,989	$103,021	$80,195
Earnings from continuing operations	**16,129**	4,326	3,359	449
Diluted earnings per share from continuing operations	**$0.58**	$0.17	$0.15	$0.02
Total assets	**268,623**	110,654	87,596	78,950
Shareholders' equity	**213,102**	78,472	60,558	55,607
Operating margin	**11.9%**	5.1%	4.5%	(0.8%)

To Our Shareholders:

Storage networking is complex. It is about data. The way that it is accessed. How it is protected and made available throughout an enterprise. The distances across which it is moved and shared. How cost-effectively it is managed. And most important, it is about turning data into information—mission-critical information that serves as the foundation of business. Across every industry, companies are entrusting CNT with their valuable data to create and manage storage infrastructure solutions that transform data into information.

In 2000, CNT continued to build its business upon one simple truth: we have the products, services and experience to access, move, store and manage information throughout any enterprise and across any distance—providing organizations with the confidence and enthusiasm to use information technology to drive superior business results. We accomplish this through continuous technical innovation and an unwavering passion for customer service.

At the end of calendar 1999, we announced our intention to focus exclusively on storage networking and divest our Enterprise Integration Solutions (EIS) business. In fiscal 2000, we took an important step in that direction by first selling IntelliFrame, and recently renaming EIS as Propelis™, in anticipation of its separation from CNT later this year.

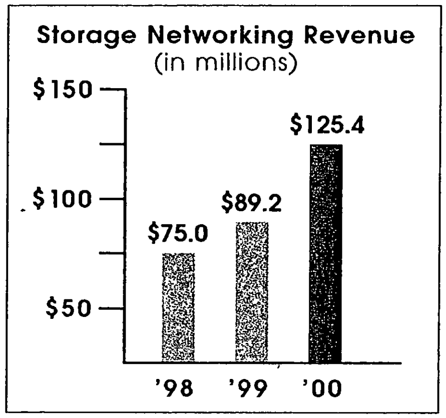
Our steadfast commitment to the rapidly expanding storage networking market drove record revenue growth in 2000, despite the weakening economy, which caused a slower than anticipated fourth quarter. We delivered two industry-first storage-networking technologies that utilize low-cost and infinite distance Internet Protocol (IP), allowing customers to leverage their existing infrastructures for cost-effective storage networks. In addition, we formally launched our professional services organization, which enables companies to further benefit from our proven expertise in storage networking.

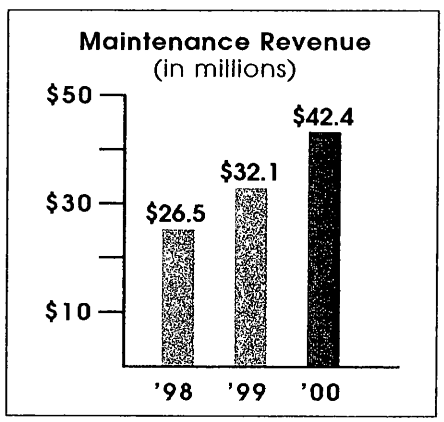
Financial Results

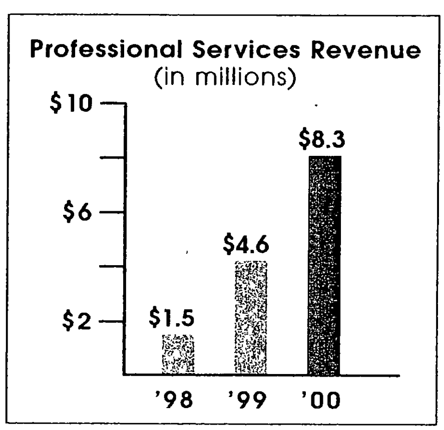
For fiscal 2000, CNT reported record revenues of $176.1 million, an increase of 40 percent from $126.0 million in 1999. Net income from continuing operations, excluding a one-time gain of $287,000 from the reversal of a restructuring accrual, totaled $15.9 million, or $.57 per share, up 160 percent compared to net income from continuing operations, before special charges, of $6.1 million, or $.24 per share, in 1999. Including discontinued operations and the one-time gain of $287,000, net income totaled $12.0 million, or $.43 per share, a 158 percent rise from 1999.

CNT raised $110 million during the third quarter from the sale of 4.6 million shares of CNT common stock. Proceeds from the offering will allow the company to invest in key storage networking and professional services markets, and pursue complementary product and business acquisitions.

In the first quarter of fiscal 2001, CNT sold its IntelliFrame business to webMethods, Inc. (Nasdaq: WEBM) for $8.8 million in cash and 273,542 shares of newly issued webMethods common stock.







Storage Networking— The UltraNet® Products

Networking product revenues rose substantially in 2000, to $125.4 million, up 41 percent from 1999. Storage networking-related products sales were exceptionally strong, up 64 percent from 1999 to a record $87.8 million

Driving demand for storage, and particularly storage networking, is the proliferation and increasingly critical nature of information. Our customers need 24x7 availability, greater storage capacity, protection and disaster recovery, and guaranteed data integrity.

During 2000, CNT delivered two industry-first technologies: data mirroring over IP in partnership with EMC Corporation; and IP Storage capabilities for tape, fibre channel and Small Computer Systems Interface (SCSI), enabling companies to build storage infrastructures over IP networks, such as intranets and Virtual Private Networks (VPNs). These key technologies demonstrate our ongoing commitment to leadership and innovation.

I want to emphasize that we did not simply announce these solutions, as did our industry competitors; we are delivering, installing and supporting them in production at customer sites today. We continue to be the only company providing such capability over IP networks.

Our customers face the increasing, and often overwhelming, complexity of storage networking. They need a single source to bring together the diverse technologies from multiple vendors that are necessary for a comprehensive storage solution. CNT is the leading specialist in all types of storage networks, across any distance. Through trusted and established relationships with leaders in the storage industry, we are able to combine our own hardware, software and services with products from every major storage player to deliver complete solutions directly to our global 1000 customers.

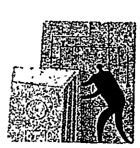
Storage Networking—Services

CNT's professional services group grew substantially in both size and revenue during fiscal 2000. Professional services revenue rose to $8.3 million, up 82 percent from 1999. Our services group grew by 31 employees during the year, bringing its year-end total to 57. Recently, we more than doubled the services group by gaining 120 professionals with our acquisition of leading storage management services provider, Articulent. The transaction was a stock purchase for $12 million in cash, plus the assumption of approximately $24 million of liabilities and included the acquisition of approximately $19 million of tangible assets.

In October we announced the availability of our field-proven Storage Networking Services organization, formed to help customers design and implement storage networks quickly and cost-effectively using the industry's best SAN technologies. We have professionally trained and certified storage networking services personnel—service consultants who are certified in dozens of technologies, and have field-proven experience.

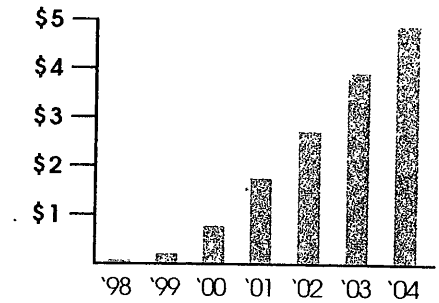
According to Steve Duplessie, Senior Analyst and Founder, Enterprise Storage Group, "CNT is one of the few large SAN assessment and professional services companies we've found that has multi-platform, multi-vendor, real-life experience designing storage networks."

A testament to our real-world storage networking experience can be found in EchoStar/DISH Networks, a direct broadcast satellite television products and services company. CNT's Storage Networking Services organization provided satellite broadcaster EchoStar/DISH Networks with a detailed, comprehensive plan for storage network design, implementation and proof-of-concept testing that enabled improved data protection and operating efficiency.

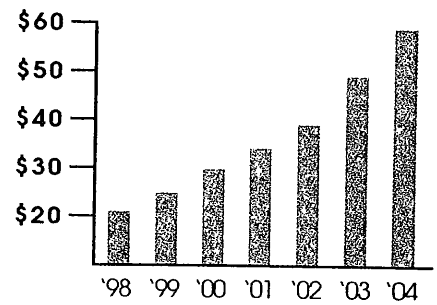


Industry Trends

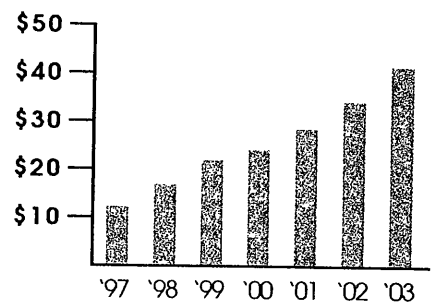
(in billions)



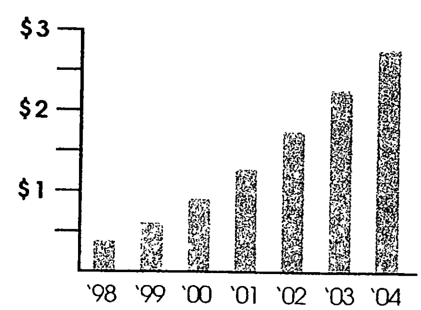
Fibre Channel Market*



Storage Market**



Managed Services Market***



Data Mirroring Market****

* Source Dataquest December 2000
** Source IDC April 2000
*** Source IDC May 2000
**** Source Dataquest May 2000

Outlook

CNT's story is one of success. Four years ago we were in a small, declining market with an aging product line. Today CNT is a growth company positioned in a market that is large and fast growing: storage networking.

As an acknowledged leader and technical innovator, we're helping to meet and drive the demand for cost-effective, comprehensive storage networking solutions—serving as a trusted partner to efficiently manage and protect information for some of the world's largest corporations.

Our steadfast commitment to technology leadership and long-term growth is delivering record financial performance. While there are short-term economic uncertainties, and quarter to quarter lumpiness, we measure ourselves on delivering annual growth and sustained improvement. We remain confident of storage networking's growth prospects.

We move into fiscal 2001 with a strong balance sheet — debt-free and with a positive cash flow—delivering real profits and growth to our shareholders and employees, and innovative products and services to our customers.

In the coming months we will continue to focus on storage networking, specifically:

- continuing our industry leadership in IP storage solutions and standards;
- further developing our professional services organization;
- pursuing opportunities to add to our growing family of storage services including consulting, implementation and managed services;
- continuing to explore innovative technological solutions in metropolitan area network (MAN), optical networking, network operations and storage resource management.

On behalf of CNT's board I want to extend a special thanks to long time board member Larry Pearlman, who will be retiring from CNT's board after twelve years of service. Larry's contributions have helped CNT grow from $3 million to more than $170 million in revenues. Everyone at CNT sincerely appreciates the guidance, insight and inspiration he has brought to the company.

I also would like to thank you for your continued support and extend a special thanks to our 790 forward-thinking employees who continue to go the extra mile to keep CNT at the forefront of the storage networking industry.

Sincerely,

Thomas G. Hudson

Thomas G. Hudson

President, Chief Executive Officer and
Chairman of the Board

April 12, 2001

Principal Outside Counsel

Leonard, Street and Deinard Professional Association
Minneapolis, Minnesota

Independent Auditors

KPMG LLP
Minneapolis, Minnesota

Transfer Agent

Shareholder inquiries relating to shareholder records, stock transfer, change of ownership or change of address should be directed to the company's transfer agent:

Mellon Investor Services LLC
85 Challenger Road
Ridgefield Park, NJ 07660
(888) 213-0965
www.mellon-investor.com

Form 10-K

A copy of our annual report on Form 10-K, filed with the Securities and Exchange Commission, will be furnished free of charge to any CNT shareholder upon request to:

Investor Relations
CNT
6000 Nathan Lane North
Minneapolis, Minnesota 55442
(763) 268-6111
investor_relations@cnt.com

Investor Inquiries

Shareholders, securities analysts, portfolio managers and others in the investment community seeking information about CNT should contact Investor Relations at (763) 268-6111 or by e-mail at investor_relations@cnt.com.

Annual Meeting

Shareholders, employees and friends are invited to attend CNT's annual meeting on Thursday, June 28, at 10:00 a.m. at CNT's corporate headquarters in the Minneapolis suburb of Plymouth, Minnesota.

Corporate Location

CNT
6000 Nathan Lane North
Minneapolis, Minnesota, USA
Tel. 763-268-6000
Fax: 763-268-6800

Board of Directors

Thomas G. Hudson
Chairman of the Board

Patrick W. Gross
Founder and Chairman, Executive Committee
American Management Systems, Inc.

Erwin A. Kelen
President, Kelen Ventures

Lawrence Perlman
Retired Chairman and Chief Executive Officer, Ceridian Corporation
Retiring from CNT Board as of June 28, 2001

John A. Rollwagen
Investor/Business Advisor

Management

Thomas G. Hudson
President, Chief Executive Officer and Chairman of the Board

Gregory T. Barnum
Chief Financial Officer, Vice President of Finance and Corporate Secretary

Jeffrey A. Bertelsen
Corporate Controller and Treasurer

Robert R. Beyer
Vice President of Worldwide Customer Support Services

William C. Collette
Chief Technology Officer and Vice President of Advanced Technology

Nick V. Ganio
Group Vice President of Worldwide Sales, Marketing and Services

Kevin J. Hansen
Senior Director of Human Resources

Gary M. Johnson
Vice President of Storage Networking Services

Mark R. Knittel
Group Vice President of Worldwide Product Operations

Paul J. Martin
Vice President of Engineering Operations

James I. Morin
Vice President of Strategic Planning

Ernest J. Parsons
General Manager of Systems Integration and Consulting Services

Julie C. Quintal
Vice President of Quality and Business Process

Barbara L. Schmit
Chief Information Officer

CNT® www.cnt.com

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended January 31, 2001
Commission file number: 0-13994

COMPUTER NETWORK TECHNOLOGY CORPORATION

(Exact Name of Registrant as Specified in its Charter)

Minnesota	**41-1356476**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
6000 Nathan Lane North, Plymouth, Minnesota	**55442**
(Address of Principal Executive Offices)	(Zip Code)

(763) 268-6000
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act: Common Stock $.01 par value

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 if disclosure of delinquent filers pursuant to item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

The aggregate market value of Common Stock held by non-affiliates of the Registrant as of April 1, 2001 was approximately $316,904,000 based on a closing price of $10.81 per share as reported by the Nasdaq National Market on such date.

As of April 1, 2001 Registrant had 29,722,581 shares of Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of Computer Network Technology Corporation's definitive Proxy Statement for the Annual Meeting of Shareholders to be held on June 28, 2001 are incorporated by reference into Part III of this Form 10-K.

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PART I

Item 1. Business

BUSINESS

Overview

We are a leading provider of hardware and software products, related professional services, and managed services in the rapidly growing storage networking market. We focus primarily on helping our customers design, develop, deploy and manage storage networks, a high speed network within a business' existing computer system that allows the business to manage its expanding data storage needs with greater efficiency and less disruption to its overall network. We design, manufacture, market and support a wide range of products for critical storage networking applications such as remote disk mirroring, or the real-time backup of data to remotely located disks, and remote tape vaulting, or the backup of data to remotely archived tapes. Revenue from our storage networking products were $87.8 million, $53.6 million and $31.9 million for the years ended January 31, 2001, December 31, 1999 and 1998, respectively.

Our storage networking products enable businesses to cost-effectively manage their increasing storage requirements, connect geographically dispersed storage networks, provide continuous availability to greater amounts of data and protect increasing amounts of data more efficiently. We market our storage networking products and services directly to customers through our sales force, worldwide distributors and original equipment manufacturers, or OEMs. Our distribution and OEM relationships include Hewlett Packard and StorageTek. We also have strategic marketing partnerships with leading storage industry and fibre switching companies, including Brocade, Compaq, EMC, Hitachi Data Systems, IBM, Legato and SCH Technologies.

We were the first to develop, and remain a leader in, the following storage networking applications:

- *Storage networking over wide area networks, or WANs.* Our storage networking over WAN products enable businesses to manage and protect data across remote locations, in real time if necessary, through applications such as remote disk mirroring and remote tape vaulting. Wide area networks, or WANs, are networks dispersed over long distances that communicate by traditional or fiber optic third-party telecommunication lines.
- *Fibre Channel-based storage networking over WANs.* In October 1999, we introduced our first Fibre Channel-based storage networking over WAN product. Fibre Channel is a recently developed technology that dramatically improves the speed of data input and output, or I/O, between existing storage networking storage devices and the ability to connect additional devices to storage networking. We believe our Fibre Channel-based storage networking over WAN products offer significant growth prospects. These products uniquely address constraints in distance, connectivity and data transmission speeds inherent in the Fibre Channel standard. We believe Fibre Channel technology combined with our products will enable businesses to efficiently consolidate, cluster and share data from multiple storage devices on storage networks.
- *Storage networks over IP-based networks.* In February 2000, we introduced the first products to allow storage networking applications, such as remote disk mirroring, to be deployed over private networks that are based on Internet protocol, or IP, the standard method for data transmission over the Internet. Our products were the first to extend the Fibre Channel, SCSI and ESCON standards to IP-based networks, and we are the only company currently providing such products. SCSI and ESCON are older, widely used standards for communicating between computers. These products uniquely enable businesses that use virtual private IP-based networks, including many Web-based businesses, to build storage networking over WAN applications.

Our storage networking solutions operate across most business computing environments, including open systems, servers and mainframes. Open systems and servers are newer systems that are easy to scale, or expand, and that use hardware and software standards not proprietary to any vendor. Mainframes are computer systems with high processing power that have historically been used by large businesses for storing and processing large amounts of data. Compared to available alternatives, we believe our storage networking products offer greater ability to connect various applications and heterogeneous environments using different interfaces, protocols and standards, and to connect and link devices in storage networks transparently, meaning with little or no alteration of other vendors' hardware or software products.

We believe the recent introduction of our products that enable storage networking applications over IP-based networks will benefit existing customers and expand our reach into the rapidly growing Internet market. This product extends the "bandwidth on demand" advantages of IP-based networks into storage applications and allows customers to access telecommunications capacity only as needed through a general connection, as opposed to leasing expensive dedicated lines. By deploying storage networks over IP-based networks, companies can leverage their existing under-utilized bandwidth, and can rely on their existing IP network knowledge. We believe that these cost savings, along with the generally expected decreasing costs of telecommunications capacity, will create high-growth opportunities for us in remote disk mirroring, remote tape vaulting and future storage networking applications we enable.

Historically, we have operated through two vertically integrated divisions. We have and continue to market our storage networking products through our continuing operations, which we have historically referred to as our Networking Solutions Division, which represent our core business. Our storage networking products consist primarily of our UltraNet® and Channelink® families of products. Our continuing operations also market our established channel networking products, which enable computers to transmit data over unlimited distances. Our discontinued operations, which we have historically referred to as our Enterprise Integration Solutions Division, develop and sell our enterprise application integration, or EAI, software that automates the integration of computer software applications and business workflow processes, as well as our traditional server gateways and tools, which enable multiple desktop computers and mainframe terminals to communicate with one another. We recently changed the name of our Enterprise Integration Solutions Division to Propelis Software, Inc. We have announced our intention to divest Propelis Software, Inc. in order to focus all of our resources on our storage networking products and related services.

Our Market Opportunities

We believe several forces will continue to drive the demand for our storage networking products:

- The volume of enterprise data is increasing significantly due to the proliferation of Internet and Web-based content, digital media, e-mail, e-commerce and data warehousing. As a result, the demand for storage capacity is growing rapidly.
- Actual and expected declines in telecommunications costs and the introduction of new, cost-effective technologies such as Fibre Channel switching and fiber optic transmission capabilities will make remote disk mirroring and remote tape backup applications more cost effective for our customers. We also believe the total cost of ownership for storage may be increasing, due to labor, management and other costs required to implement shared storage across the enterprise. The decrease in telecommunications costs, coupled with an overall increase in the cost of ownership, contributes to a trend of consolidating and connecting storage across many servers and many locations, which drives demand for our products.
- Storage networking applications over IP-based networks will further expand the type and amount of data our customers will backup and disk mirror to remote locations, and also bring Web-based and storage service provider companies into our customer base.

As a result of the foregoing and other factors, International Data Corporation, or IDC, estimates that the worldwide revenue for storage network-attached disk storage systems will grow from $1.4 billion in 1999 to $10.9 billion in 2003, a compound annual growth rate of 66%. Another indication of a strong demand for our storage networking products is the growth of the Fibre Channel market. IDC estimates the revenue for Fibre Channel hubs and switches will grow from $0.4 billion in 1999 to $4.2 billion in 2003, which reflects a compound annual growth rate of 76%. It is notable however, that we are in the midst of a current economic slowdown affecting most technology sectors and communications in particular. We are uncertain of the depth and duration of this slowdown. However, we believe the need for storage networking solutions is significant and will continue to increase.

Selected Recent Developments

On April 24, 2001 we announced that our anticipated revenues for our first quarter ending April 30, 2001 will be 30%-40% lower than the fourth quarter of fiscal 2000. As a result, we announced a one-time charge for our first quarter consisting of $700,000, or $.02 per share after tax, for an approximate 10% reduction in workforce; $300,000, or $.01 per share after tax, for a write-off of non-strategic product lines; and $2.0 million, or $.04 per share after tax, for an increase in reserves for slow-moving inventory. We also announced other cost control measures including elimination of most outside contract and temporary employees; a freeze on all wage increases; a 10% pay reduction for executive management; a 5% pay reduction for all other employees; a consolidation of facilities; and cuts in discretionary spending company wide. In addition, our board of directors authorized the repurchase of up to $50 million of our common stock to be effected from time to time.

Acquisition of Articulent Inc. On April 3, 2001 we acquired all of the outstanding stock of Articulent Inc., a privately held, leading provider of storage management services for $12 million in cash, plus the assumption of approximately $24 million of liabilities and the acquisition of approximately $19 million of tangible assets. The agreement includes a $10 million incentive payout based upon meeting certain revenue and earnings milestones over the next twelve months. The acquisition further strengthens our storage services organization, which provides companies with the expertise to manage information enterprise-wide.

Divestiture of Propelis Software, Inc. Our board of directors has determined to divest Propelis Software, Inc. formerly known as our Enterprise Integration Solutions Division in order to focus all of our resources on our storage networking products. Accordingly, the financial information for this wholly owned subsidiary has been accounted for as discontinued operations. In the first quarter of fiscal 2001, we expect to accrue for the estimated future losses to be generated by Propelis Software, Inc. through the potential date of divestiture, resulting in a one-time after tax loss of approximately $3.5 million.

Sale of IntelliFrame. On February 2, 2001, we completed the sale of our IntelliFrame subsidiary, which was part of Propelis Software, Inc., including the technology underlying our Propelis BPm™ product to WebMethods for $8.8 million in cash and 273,542 shares of WebMethods stock. Propelis Software, Inc. retains a license, subject to certain restrictions, to the Propelis BPm™ product, its name, the customers and the prospects. We expect that Propelis Software, Inc. will continue to sell the Propelis BPm™ product in the future. In the first quarter of fiscal 2001, we expect to recognize a one-time after tax gain of approximately $12.5 million from the sale of IntelliFrame in the discontinued operations section of our statement of operations. The stock we received from WebMethods has experienced a significant decline in value since February 2, 2001. We will not record a loss in our statement of operations for the decline in value of the WebMethods stock until such time as the stock is sold, or the decline in value is determined to be other than temporary. As a result of the divestiture of Propelis Software, Inc. and the sale of Intelliframe, we expect to report a net one-time after tax gain of approximately $9.0 million in the first quarter of fiscal 2001.

Secondary Stock Offering. On October 11, 2000, we completed a secondary stock offering, raising approximately $110 million from the sale of 4.6 million shares of our common stock.

Storage Networking Applications Over IP-Based Networks. In February 2000, we introduced the first products to allow storage networking applications, such as remote disk mirroring using EMC's SRDF software, and remote tape vaulting to be deployed over standard IP-based networks. We anticipate expanding our product offerings to support additional storage networking applications from other vendors. The recent expansion of support of IP includes what we believe is the only working capability to extend Fibre Channel technology and the SCSI interface over IP-based networks.

Storage Networking Overview

Storage Networking Industry Background

Growth in Enterprise Data

The volume of enterprise data is increasing significantly due to the proliferation of Internet and Web-based content distribution, digital media, e-commerce, e-mail and data warehousing. Furthermore, the proliferation of the Internet has created new industries in Web hosting and data caching, which has led to an increase in the volume of enterprise data needed to be tracked and stored.

Limitations of Traditional Storage Solutions

The rapid escalation of the size and amount of data stored has presented organizations with significant data management challenges and increased storage related costs. As the volume of data stored, and the number of users that require access to the data continue to increase, storage systems and servers are burdened by an increased number of input/output, or I/O, transactions they must perform. However, traditional storage architecture has inherent speed, distance, capacity and performance constraints. For example, depending on the standards and protocols used, the following constraints may exist:

- bandwidth, or the data transmission rate, is generally fixed at 15, 40 or 80 megabytes per second;
- distance between devices is limited to 12 to 150 meters;
- connectivity is limited to 15 storage devices;
- the lack of data management capability in SCSI devices places the burden for management tasks on servers, thereby degrading network performance;
- if the server to which the data storage device is connected fails, the data cannot be accessed; and
- LAN performance can be significantly degraded while the LAN is being used for storage backup applications.

Advent of Fibre Channel

In response to the speed, distance, capacity and performance limitations of traditional storage architectures, the Fibre Channel interface was developed in the mid-1990s as an open standard technology specifically for high performance, data intensive environments. Fibre Channel products offer over one gigabit per second of bandwidth and enable the inter-connectivity of millions of storage devices and servers. Fibre Channel also offers distance connectivity of up to 10 kilometers, a single interface for networking and I/O applications, technology that supports a variety of traditional I/O and LAN protocols and interfaces and the ability to support simultaneous two-way communications, which effectively doubles bandwidth. The introduction of the Fibre Channel interface means that storage networks are becoming a viable alternative to traditional data storage architecture.

However, Fibre Channel-based storage networks do not provide complete solutions for managing large amounts of data in a distributed environment. Consequently, solutions are required that address the following Fibre Channel limitations:

- *Distance* — Customers require products that support transfers over unlimited distances. Fibre Channel supports a maximum connection distance of 10 kilometers. Transmission across third-party telecommunications lines is not supported by Fibre Channel.
- *Connectivity* — Customers want their existing computing systems to communicate with one another and share data. Mainframe systems have interface channels using the ESCON or bus and tag protocols, and open systems use SCSI or LAN standards known as TCP/IP, or Transmission Control Protocol/Internet Protocol. Fibre Channel switches cannot communicate with non-Fibre Channel switches, requiring further connectivity solutions. Protocols are a set of rules for communicating between computers. Standards are specifications for hardware or software that are

widely used and accepted. An interface is the connection and interaction between hardware, software and the user.

- *Application availability* — Customers need to keep applications online and running during infrastructure changes, backup, testing and unplanned outages to remain competitive in today's business economy. Fibre Channel by itself does not provide continuous application availability.

- *Bandwidth on demand* — Dedicated high capacity telecommunications lines that have traditionally been used with storage networks, namely T1, T3 and ATM lines, are expensive and permit remote backup of only the most mission critical data. Customers require storage networking solutions that utilize less expensive IP-based networks in order to remotely backup greater amounts of information and make greater use of storage networking advantages. Fibre Channel does not provide the inherent ability to transmit data over IP-based networks.

Our Storage Networking Solutions

Our storage networking products address the limitations of traditional storage architecture and Fibre Channel technology in the following ways:

- *Storage networks over unlimited distance* — Our products enable organizations to create secure storage networks without any distance limitations. This allows the creation of storage networking over WAN environments in such critical applications as remote disk mirroring and remote tape vaulting.

- *Any-to-any connectivity* — Our products are protocol independent — they can connect devices that use Fibre Channel, SCSI, ESCON, and bus and tag protocols. These devices can be connected and extended over telecommunications links including T1/E1, T3/E3 and ATM, or WAN protocols like IP, Fibre Channel and fiber optics. We believe our products connect with substantially all storage vendors.

- *Infrastructure options* — Our products enable the use of IP, ATM, Fibre Channel and fiber optics for expanded use of a storage network infrastructure. This supports the growing amounts of storage created by applications like e-commerce and increases due to user demands to access applications in a continuous mode.

- *IP-based networking solutions* — We enable remote disk mirroring using EMC's SRDF software and tape vaulting over standard IP-based networks. Our solutions allow our customers to capitalize on inexpensive bandwidth on demand capabilities of IP-based networks and use under-utilized, existing IP bandwidth, especially at low traffic times of the day, and rely on existing IP network knowledge. We anticipate expanding storage networking application support with products from other vendors.

Our storage networking solutions are used for immediate, or real-time, backup and recovery, and support a technology known as remote disk mirroring. Disk mirroring avoids the serious threat to businesses posed by the loss of data between data system backups by simultaneously creating up-to-the-minute images of business-critical data on multiple backup storage disks. Our remote disk mirroring technology permits the backups to be transmitted to a geographically separated location, thereby reducing the risk of natural and site-wide disasters. This technique also permits rapid recovery of data when needed, as it is not necessary to reload tapes.

We also enhance continuous business operations. Traditional LAN-based storage management requires manual handling and transportation of storage to an off-site location. While this ensures a physically-separated copy of valuable corporate data, it requires additional time and expense for handling and transportation. In addition, finding the right tape in a timely manner can be difficult. By bridging the storage network over the WAN, backups can be instantly made to remote locations on disk media, including by disk mirroring, or on tape, known as electronic tape vaulting. The benefit is secure archiving and timely retrieval of the correct business-critical data.

Our Storage Networking Strategy

We intend to build upon our position as a leading provider of storage networking solutions. Key elements of this strategy are as follows:

Extend Storage Networking Leadership

We intend to extend our storage networking leadership by continuing to broaden our product and service offerings and by expanding our storage networking solutions into new markets. An example of this strategy is our recent introduction of Fibre Channel over ATM WANs. We intend to build market share by continuing to focus on areas which make storage networks more useful and accessible, such as WAN applications, any-to-any connectivity, and IP-based network solutions. To achieve leadership, we intend to capitalize on the remote disk mirroring and remote tape vaulting capabilities of our products.

Expand IP-Based Network Solutions

Currently, our IP-based network solutions enable remote disk mirroring, in conjunction with EMC's SRDF software products, and remote tape vaulting over IP-based networks. We are currently developing solutions which will operate in conjunction with storage network applications of other storage networking vendors.

Partner with Storage Networking Industry Leaders

We have established relationships with leaders in the storage networking market, including storage vendors, storage management software providers and Fibre Channel switch manufacturers. Our strategic partners include companies such as Brocade, Compaq, EMC, Hewlett Packard, Hitachi Data Systems, IBM, Legato, Nortel, SCH Technologies and StorageTek. We intend to strengthen our relationships with existing strategic partners and develop relationships with new strategic partners that offer complementary products and services. We believe that current and future strategic relationships will facilitate the integration of our products with our strategic partners, thereby increasing our market share and reducing the length of our sales cycle.

Focus on Professional Services

Our professional services help customers evaluate, analyze, design, install and manage storage networks. We believe this value-added professional service assists customers in designing SANs, integrating SAN components and implementing SANs better than they could on their own. Our integration services eliminate the complexity of implementing a SAN that is scalable and compatible with customer resources. These services bolster sales of our products and allow us to generate high margin revenues.

Explore Additional Managed Services

We offer outsourced storage management services that complement our current storage networking products. Our data migration service helps our customers migrate large amounts of data from one data center or storage facility to another during consolidation or expansion of data centers. This is a turnkey service including personnel, equipment, software and support. We provide an outsourced electronic tape vaulting service in conjunction with Iron Mountain. We anticipate adding other outsourced services that help drive demand for our storage networking products.

Our Storage Networking Products

Our storage networking products include the UltraNet® family of storage products, and our channel networking product known as Channelink®.

UltraNet® Storage Director is a high performance switching product that operates at the center of the storage network. It enables storage networks to establish a direct connection between storage elements and servers and share data among diverse servers and storage systems, and networks that are local and geographically dispersed. The switch provides connectivity among SCSI, ESCON, Fibre Channel and WANs. Two sizes are offered — with 6 or 12 expansion slots.

UltraNet® Storage Gateway provides much of the same functionality and performance of the UltraNet® Storage Director at a lower entry price. The product is targeted at small storage networking applications.

UltraNet® Fibre Channel Switch enhances our ability to provide open systems solutions for Fibre Channel only configurations as well as mixed environments. Mixed environments can include SCSI server and storage systems that require access to Fibre Channel solutions. Brocade manufactures this switch and we resell it alone or with our storage network system solutions. This switch is available in 8 and 16 expansion slot models.

UltraNet® Wave Optimizer and UltraNet® Wave Multiplexer increase the bandwidth available from fiber optic lines by carrying multiple signals over a single cable using different wave lengths (colors of light) or time slots. Pandatel manufactures these DWDM, or dense wave division multiplexing, and TDM, or time dimension multiplexing products.

Channelink® offers connectivity over unlimited distances and is used for remote disk mirroring and remote tape vaulting in environments using older protocols.

Our Storage Networking Partners

Offering customers effective storage networking solutions requires integrating diverse components, including disk and tape storage devices, storage management software, network management products and Fibre Channel products. The optimal package of goods and services allows a customer to reduce storage management costs by consolidating data centers and centralizing data management. We work with our business partners to provide customers with those benefits. Our storage networking alliances include those with key storage vendors, storage management software providers and manufacturers of Fibre Channel and optical networking products. We market our storage networking products directly and through worldwide distributors and OEMs, including Hewlett Packard and StorageTek. We also have strategic marketing partnerships with leading storage industry and fibre switching companies, including Brocade, Compaq, EMC, Hewlett Packard, Hitachi Data Systems, IBM, Legato and SCH Technologies. Benefits of our alliances include:

- The working relationship provides us with visibility regarding market trends and technology requirements and allows us to contact customers earlier in the sales cycle and ascertain their needs.
- Sales of storage systems for disk mirroring provides a ready market for our remote disk mirroring applications.
- A platform to demonstrate our interoperability with various platforms and integrate heterogeneous components allowing us to gain preferred provider status with key vendors.
- The resulting customer base provides us with strong reference accounts to further increase market penetration.

EMC

We have established a relationship with EMC for remote disk mirroring applications. This existing relationship includes an agreement to provide an exclusive package of remote disk mirroring hardware, software and implementation service. Together with EMC, we offer complementary professional services and linked customer support organizations. We work with EMC to provide our mutual customers with timely, effective service. In fiscal 2000, sales of our storage networking products to customers using EMC's disk mirroring systems accounted for 28% of our total product revenue. We also market our remote disk mirroring applications with other vendors, including Hitachi Data Systems and IBM.

IBM

IBM is one of our oldest strategic partners. We coordinate local market activities with IBM, provide mutual assistance and prepare combined proposals. We also partner with IBM to provide customers with outsourced disaster avoidance and recovery capability and remote disk mirroring applications.

StorageTek

In November 1999, we entered into a three-year agreement with StorageTek under which it resells our storage networking over WAN products. In addition, we purchased StorageTek's DXE/RDE product line for $2.5 million in cash and assumed ongoing manufacturing and engineering responsibilities for this product line. This acquisition will provide us with access to StorageTek's large installed base of customers for cross-selling our storage networking products. We discontinued the DXE/RDE product line in March 2001, and plan to transition the customer base to our UltraNet® and Channelink® products. We have certified StorageTek's tape drives with our UltraNet® product and work closely with them to ensure interoperability.

Compaq

Our UltraNet® Open Systems Gateway product supports Compaq's StorageWorks Data Replication Manager over long distances. The relationship with Compaq is significant because we believe Compaq is the largest provider of storage today. In 1999, Compaq entered into a multi-million dollar commitment to resell our storage networking products. In fiscal 2000, Compaq purchased $5.7 million of product under their commitment. We have released them from any further commitment, and will be working with them on a co-sell basis in the future. We believe this type of arrangement will be more beneficial to both companies going forward.

Brocade

Our UltraNet® Fibre Channel Switch, which is manufactured by Brocade, became generally available in June 1999. We believe the combination of our UltraNet® storage networking solutions and UltraNet® family of Fibre Channel switches offers customers an attractive architecture for developing storage networking solutions. The industry expects complete interoperability for Fibre Channel devices, and we believe our storage networking solutions are a step in that direction.

Other Storage Networking Products

We also offer channel extension products, which are certified for use with over 250 different devices. These products offer connectivity over unlimited distances, free of limitations imposed by traditional standards and protocols. These products are used for the following applications:

- *Data Center Consolidation:* The consolidation of data centers in different locations to one location; often useful after mergers or acquisitions.
- *Remote Printing/Imaging:* High-speed digital printing or imaging at remote locations.
- *Data Center Load Balancing:* Operating two or more data centers from one site. The application is transparent to the systems and servers that are interconnected as well as to data users, meaning users do not know that the data is not located centrally.

Under our agreement with StorageTek, we have also assumed ongoing manufacturing and continuing engineering responsibility for StorageTek's DXE/RDE product line. This product line is used for similar applications as our Channelink® product line and substantially all sales of such products are to StorageTek. We discontinued the DXE/RDE product line in March 2001 and plan to transition the customer base to our UltraNet® and Channelink® products.

Professional Services

SAN Services

Our SAN assessment analyzes a company's storage needs, determines a SAN solution to meet those needs, and assists in development of a business case to justify the SAN solution. With a SAN assessment, we assist our customers in making their existing networks more flexible and easier to manage. This thorough assessment assists information technology managers and corporate executives responsible for planning and funding computer resources in making sound data management and storage decisions.

Our reliable, repeatable SAN assessment process includes the following phases. These phases are designed for efficient evaluation and recommendation of an appropriate storage networking infrastructure for storage.

- *SAN audit:* the audit contains a summary of business needs and an inventory of a customer's network components and storage capability.
- *SAN analysis:* the analysis includes a profile of a customer's current environment compared to its competitors, capacity planning, and a projection of a customer's future needs.
- *SAN recommendation:* this phase develops a detailed summary report containing one to three recommended SAN solutions.
- *SAN implementation:* this phase implements the recommended solution, including deployment of SAN components, testing and documentation.

Storage Architecture Services

Our professional services help companies implement storage networking and business continuance solutions. Our consulting and implementation services include strategic planning, project planning, analyzing, designing and documenting a detailed network, installing storage components, integrating storage components, and testing the functionality of the implemented storage solution. Our storage networking products are at the heart of our storage architecture implementations, and our long-standing partnerships with well-known and successful storage equipment and software manufacturers place us at the forefront of storage management solutions.

Product Support

We offer standard maintenance contracts for our storage networking products. The contracts generally have a one-year term and provide for advance payment. Customers are offered a variety of contracts to choose from to suit their particular needs. For instance, current options allow a customer to choose support seven days a week, 24 hours per day, or five days per week, 11 hours a day. Other options offer the customer the choice to select air shipment or replacement parts, with the part being installed by the customer's staff, or on site support with spare parts and service being provided by a local parts distributor.

Sales and Marketing

We market our storage networking products in the United States through a direct sales force. We have established representative offices in Canada, the United Kingdom, France, Germany, Australia, Japan, and The Netherlands. We also market the products in the United States and throughout the world through OEMs, systems integrators and independent distributors.

We maintain our own marketing staff and direct sales force. On January 31, 2001, we had approximately 200 persons in our marketing and sales organization for continuing operations.

Customers

Our customers include:

Financial Services	Telecommunications	Information Outsourcing
American Express	AT&T Technologies	Comdisco Disaster Recovery Services
Bank of America	British Telecom	Computer Sciences Company Ltd
Barclays	Sprint	Electronic Data Systems
Chase	Worldcom	IBM Global Services
Citibank		Integrated Systems Solutions Corp.
Merrill Lynch		
Rabo Bank		

Research and Development

The markets in which we operate are characterized by rapidly changing technology, new standards and changing customer requirements. Our long term success in these markets depends upon our continuing ability to develop advanced network hardware and software technologies.

To meet the future demands of our customers, we expect to:

- increase the compatibility of our products with the products made by others;
- emphasize the flexible and modular architecture of our products to permit the introduction of new and improved products within existing systems;
- continue to focus on providing sophisticated diagnostic support tools to help deliver high network availability and, in the event of failure, rapid return to service; and
- develop new products based on customer feedback and market trends.

Research and development expenses were equal to 13% of our total revenue in 2000, compared to 15% and 14% of total revenue in 1999 and 1998, respectively. We intend to continue to apply a significant portion of resources to product enhancements and new product development for the foreseeable future. We cannot assure you that our research and development activities will be successful.

Manufacturing and Suppliers

In-house manufacturing activities for our products primarily involve quality assurance testing of subassemblies and final system assembly, integration and quality assurance testing. We became ISO 9001 certified in 1999 and have been ISO 9002 certified since 1993.

We manufacture our products based on forecasted orders. Forecasting orders is difficult as most shipments occur at the end of each quarter. Our customers generally place orders for immediate delivery, not in advance of need. Customers may generally cancel or reschedule orders without penalties. Accordingly, we believe that backlog is generally not meaningful for purposes of predicting our revenue for any fiscal period.

Some of our products, including Fibre Channel switches, time division multiplexers and wave division multiplexers, are manufactured by OEMs for sale by us. We manufacture our other products from subassemblies, parts and components, such as integrated circuits, printed circuit boards, power supplies and metal parts, each manufactured by others. Some items manufactured by suppliers are made to our specific design criteria.

At January 31, 2001, we held $4.4 million of inventory for parts that our vendors no longer manufacture. Products in which those parts are included accounted for approximately $112.5 million of sales in 2000. We expect that this inventory will be used in the ordinary course of our business over the next five years. Relevant parts will have to be redesigned after the inventory is used.

We believe that we currently have adequate supply channels. Components and subassemblies used in our products and systems are generally available from a number of different suppliers. However, certain OEM products, such as Fibre Channel switches, time division multiplexers and wave division multiplexers, and components in our other products are purchased from a limited number of sources. We do not anticipate any difficulty in obtaining an adequate supply of purchased OEM products and required components. An interruption in our existing supplier relationships or delays by some suppliers, however, could result in production delays and harm our results of operations.

Competition

Our products are sold in markets where other market participants have significantly greater revenues and internationally known brand names. Many of those market participants do not currently sell products similar to ours. However, such market participants may do so in the future, and new products we develop may compete with products sold by well-known market participants. Our competitors in channel networking and storage networking include storage system vendors and others including Crossroads, Gadzoox, InRange, McData, Network Systems, QLogic, StorageTek and Vixel. In addition, Cisco Systems recently acquired a company which is developing IP-based network solutions which may have functionality similar to our product offerings.

The markets in which we operate are characterized by rapidly changing technology and evolving industry standards, resulting in rapid product obsolescence and frequent product and feature introductions and improvements. We compete with several companies that have greater engineering and development resources, marketing resources, financial resources, manufacturing capability, customer support resources and name recognition. As a result, our competitors may have greater credibility with existing and potential customers. They also may be able to adopt more aggressive pricing policies and devote greater resources to the development, promotion and sale of their products than we can to ours, which would allow them to respond more quickly than we can to new or emerging technologies and changes in customer requirements. These competitive pressures may materially harm our business.

The competitive environments of markets in which our storage networking products are sold are continuing to develop rapidly. We are not in a position to prepare long range plans in response to unknown competitive pressures. As these markets grow, we anticipate other companies will enter with competing products. In addition, customers and business partners could possibly develop and introduce competing products. We anticipate the markets will be highly competitive.

The declining sales of channel networking products present unique competitive pressures. We anticipate pricing pressures may increase in these markets. Consolidation of competing vendors of these products could also have negative consequences.

The principal competitive factors affecting our products include customer service, flexibility, price, performance, reliability, ease of use and functionality. In many situations, the potential customer has an installed base of a competitor's products, which can be difficult to dislodge. IBM, Microsoft and others can significantly influence customers and control technology in our markets.

Intellectual Property Rights

We rely on a combination of trade secret, copyright, patent and trademark laws, nondisclosure agreements and technical measures to establish and protect our intellectual property rights. That protection may not preclude competitors from developing products with features similar to our products.

We currently own three patents and have eight patent applications filed or in the process of being filed in the United States with respect to our continuing operations. Our pending patent applications, however, may not be issued. We have not applied for patent protection in any foreign countries. Not all of our unique products are patented. Our issued patents may not adequately protect our technology from infringement or prevent others from claiming that our technology infringes that of third parties. Failure to protect our intellectual property could materially harm our business. We believe that patent and copyright protection are less significant to our competitive position because of the rapid pace of technological change in the markets in which our products are sold and because of the effectiveness and quality of our support services, the knowledge, experience and ability of our employees and the frequency of our enhancements.

We rely upon a patent license agreement to manufacture our Channelink® and UltraNet® products that use ESCON. This license expires on December 31, 2004.

We have from time to time received, and may in the future receive, communications from third parties asserting that our products infringe on their patents. We believe that we possess or license all required proprietary rights to the technology involved in our products and that our products, trademarks and other intellectual property rights do not infringe upon the proprietary rights of others. However, there can be no assurance that others will not claim a proprietary interest in all or a part of the technology we use or assert claims of infringement. Any such claim, regardless of its merits, could involve us in costly litigation and materially harm our business.

The existence of a large number of patents in the markets in which our products are sold, the rapid rate of issuance of new patents and short product development cycles means it is not economically practical to determine in advance whether a product infringes patent rights of others. We believe that, based upon industry practice, any necessary license or rights under such patents may be obtained on terms that would not materially harm our consolidated financial position or results of operations. However, there can be no assurance in this regard.

Employees

As of January 31, 2001, we had 769 full-time employees for both divisions. On that date, 148 full-time employees provided services to both divisions and are members of our administrative and manufacturing departments. On that date, our continuing operations had 525 employees in addition to those who provide services to both divisions. We consider our ability to attract and retain qualified employees and to motivate such employees to be essential to our future success. Competition for highly skilled personnel is particularly intense in the computer and data communications industry, and we cannot assure that we will continue to attract and retain qualified employees.

Discontinued Operations — Propelis Software, Inc.

Our board of directors has determined to divest Propelis Software, Inc., formerly known as our Enterprise Integration Solutions Division, in order to focus all of our resources on our storage networking products. Accordingly, the financial information for this wholly owned subsidiary has been accounted for as discontinued operations. In the first quarter of fiscal 2001, we expect to accrue for the estimated future losses to be generated by Propelis Software, Inc. through the potential date of divestiture, resulting in a one-time after tax loss of approximately $3.5 million.

On February 2, 2001, we completed the sale of our IntelliFrame subsidiary including the technology underlying our Propelis BPm™ product to WebMethods for $8.8 million in cash and 273,542 shares of WebMethods stock. Propelis Software, Inc. retains a license, subject to certain restrictions, to the Propelis BPm™ product, its name, the customers and the prospects. We expect that Propelis Software, Inc. will continue to sell the Propelis BPm™ product in the future. In the first quarter of fiscal 2001, we expect to recognize a one-time after tax gain of approximately $12.5 million from the sale of IntelliFrame in the discontinued operations section of our statement of operations.

Our Enterprise Integration Solution

Our EAI solutions help organizations integrate legacy applications with powerful new business applications that improve customer productivity and customer satisfaction. Our EAI solutions preserve our customers' investment in their computer systems, allow enterprise-wide real-time access to data, are flexible and highly scalable. In addition to integrating existing systems, our EAI solutions are particularly suited for developing new applications, such as:

- *CRM applications:* CRM applications facilitate integration of information collected in different areas of a company that affect customer relations. CRM applications can instantly pull together customer information from multiple databases.

- *E-commerce applications:* Customer data integrated from a variety of legacy environments can enhance a company's ability to interact with suppliers and partners, sell products and provide customer service over the Internet. Our solutions filter legacy data, translate and format it so that it can be used with Sun Microsystem's NetDynamics and Lotus' Domino products and other Internet tools to build effective Internet-based sales and service applications in less time.

Further, Propelis BPm™ includes new tools that provide business logic, rules and process workflow management for improved development and deployment of large e-commerce and CRM applications. With Propelis BPm™, our EAI solution is able to do more than just display information — it is able to suggest alternative courses of action. For instance, Propelis BPm™ can recommend whether a customer should use funds in an account to pay a credit card bill, or transfer funds to a more favorable interest bearing account. A beta version of our Propelis BPm™ product became available during the second quarter of 2000, and we recorded our first revenue from the sale of Propelis BPm™ in the third quarter of 2000. The product will be sold both on a standalone basis and with Propelis EAi subject to certain restrictions in a license agreement with WebMethods.

Our EAI products are marketed through a direct sales staff and through our business partner program. An alliance with Siebel provides a comprehensive solution to established call centers and for sales force applications. Alliances with Cap Gemini, Deloitte Consulting and PricewaterhouseCoopers provide a platform for each business partner to introduce our EAI products to customers by trained specialists.

Our Enterprise Integration Solutions Products

Propelis EAi is a development tool that permits legacy applications to be linked real-time with new business applications. The product is used with our Propelis BPm™ offering. Propelis EAi uses a "zero coding" approach, i.e., it captures application screens, analyzes the interaction between the legacy system and the user, builds a model of the legacy application, and establishes all of the necessary data paths, transformations and logic for integrating the legacy application with the new front-end application. As a result of "zero coding," Propelis EAi provides one of the fastest ways to e-commerce by enabling the easy reuse of existing legacy application programs. Key features of Propelis EAi include:

- no changes to our customers' existing applications software environment;

- a graphical user interface, which promotes rapid implementation;

- three-tier architecture for mainframe, server and client workstations, which enhance scalability and transparency; and

- centralized management to administer, monitor and troubleshoot large-scale deployments.

Propelis BPm™ is a business process management tool that enables creation of new business processes quickly and seamlessly. With Propelis BPm™, organizations can integrate mission-critical business processes, applications, data and people, online and in real time. Propelis BPm™ features a five step process including:

- business process modeling, including built-in workflow, integrated project management and dynamic process change capabilities;

- tasks are developed graphically with reusable components, including both graphical user interface (GUI) and non-GUI task options, and support for standard Web and Java interfaces;

- graphical incorporation of required data and open architecture, including built-in legacy integration for mainframe and AS/400 applications, graphical drill-down to industry standard adapters, database integration and optional integration of existing or newly developed custom code;
- automated single point deployment that generates the entire run-time environment from the solution model, including updating all clients and servers eliminating consistency/compatibility issues and dynamic deployment that allows for automatic change processes at run time with no stop/recompile/start, and;
- run time that allows for user-based definition of views and GUI options, flexibility to deploy Java or HTML clients, or integration with a preferred desktop environment.

Special Note Regarding Forward-Looking Statements

This Form 10-K and other documents we have filed with the Securities and Exchange Commission contain forward-looking statements, which may include statements about our:

- anticipated receipt of orders and demand for our products;
- business strategy;
- timing of and plan for the introduction or phase-out of products or services;
- enhancements of existing products or services;
- the divestiture of Propelis Software, Inc. formerly known as our Enterprise Integration Solutions Division;
- ability to integrate Articulent Inc. with our existing businesses;
- entering into strategic partnerships; and
- other plans, objectives, expectations and intentions contained in the Form 10-K that are not historical facts.

When used in this Form 10-K, the words "may," "should," "expect," "plan," "anticipate," "believe," "estimate," "predict," "intend," "potential" or "continue" and similar expressions are generally intended to identify forward-looking statements. These forward-looking statements involve risks and uncertainties. Actual results could differ materially from those expressed or implied by these forward-looking statements as a result of certain risk factors, including but not limited to (i) competitive factors, including pricing pressures; (ii) variability in quarterly sales; (iii) economic trends generally and in various geographic markets; (iv) relationships with our strategic partners; (v) unanticipated risks associated with introducing new products and features, including Propelis BPm™; (vi) technological change affecting our products; (vii) the financial performance of Propelis Software, Inc. prior to the proposed divestiture ; (viii) our ability to integrate Articulent Inc. with our existing businesses and (viii) other events and other important factors disclosed previously and from time to time in our filings with the U.S. Securities and Exchange Commission and in Exhibit 99 to this 10-K. In addition, there can be no assurance that the divestiture of Propelis Software, Inc. can be completed on acceptable terms and conditions. In addition, there can be no assurance the stock of WebMethods received in the IntelliFrame transaction can be liquidated within any time frame or at a gain. We assume no obligation to update any forward-looking statements. These statements are only predictions. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements.

Item 2. Properties

Facilities and Properties

Our principal administrative, manufacturing, engineering and development functions are located in leased facilities in the Minneapolis, Minnesota suburb of Plymouth. In addition, we lease office space in

England, France, Germany, Australia, Japan, and The Netherlands. We also lease space for sales offices for our direct sales staff and systems consultants in a number of locations throughout the United States and Canada. We believe our facilities are adequate to meet our current needs.

Item 3. Legal Proceedings

We are currently not a party to any legal proceedings that could materially harm our business.

Item 4. Submission of Matters to a vote of Security Holders

None.

Item 4A. Executive Officers of the Company

Our executive officers are as follows:

Name	Position Served	Age
Thomas G. Hudson	Chairman of the Board, President and Chief Executive Officer	54
Gregory T. Barnum	Chief Financial Officer, Vice President of Finance and Corporate Secretary	46
Jeffrey A. Bertelsen	Corporate Controller and Treasurer	38
William C. Collette	Chief Technology Officer and Vice President of Advanced Technology	57
Nick V. Ganio	Group Vice President of Worldwide Sales, Marketing and Services	41
Mark R. Knittel	Group Vice President of Worldwide Product Operations	46

Thomas G. Hudson has served as President and Chief Executive Officer since June 1996, as a director since August 1996 and Chairman of the Board since May 1999. Mr. Hudson has also served as acting general manager of Propelis Software, Inc. since November 1999. From 1993 to June 1996, Mr. Hudson served as Senior Vice President of McGraw Hill Companies, a leading information services provider, serving as General Manager of its F.W. Dodge Division, and as Senior Vice President, Corporate Development. From 1968 to 1993, Mr. Hudson served in a number of management positions at IBM Corporation, most recently as Vice President Services Sector Division. Mr. Hudson's IBM career included varied product development, marketing and strategic responsibilities for IBM's financial services customers and extensive international and large systems experience. Mr. Hudson is a graduate of the University of Notre Dame and New York University. Mr. Hudson attended the Harvard Advanced Management Program in 1990.

Gregory T. Barnum was appointed Vice President of Finance, Chief Financial Officer and Corporate Secretary in July 1997. From September 1992 to July 1997, Mr. Barnum served as Senior Vice President of Finance and Administration, Chief Financial Officer and Corporate Secretary at Tricord Systems, Inc., a manufacturer of enterprise servers. From May 1988 to September 1992, Mr. Barnum served as the Executive Vice President, Finance, Chief Financial Officer, Treasurer and Corporate Secretary for Cray Computer Corporation, a development stage company engaged in the design of supercomputers. Prior to that time, Mr. Barnum served in various accounting and financial management capacities for Cray Research, Inc., a manufacturer of supercomputers. Mr. Barnum is a graduate of the University of St. Thomas.

Jeffrey A. Bertelsen was appointed Corporate Controller and Treasurer in December 1996. Mr. Bertelsen served as our Controller from March 1995 to December 1996. From 1985 to March 1995, Mr. Bertelsen was employed by KPMG LLP, a public accounting firm, most recently as a Senior Audit Manager. Mr. Bertelsen is a graduate of the University of Minnesota.

William C. Collette was appointed Chief Technology Officer in December 1998 and Vice President of Advanced Technology in October 1999. Mr. Collette served as our Vice President of Engineering from

December 1995 to October 1999, and as our Director of Future Software Development and as a Software Development Manager from June 1993 to December 1995. From 1990 to 1993, Mr. Collette was employed by SuperComputer Systems, Inc. as a Senior Software Engineer, where he worked with Steve Chen to design the networking for the SS1 Supercomputer. Mr. Collette holds a bachelors degree in business management from Metro State University.

Nick V. Ganio was appointed Group Vice President of Worldwide Sales, Marketing and Services in October 1999. From November 1998 to October 1999, Mr. Ganio served as Vice President of Worldwide Sales and also as Vice President of Direct Sales Worldwide from April 1998 to November 1998. From September 1996 to February 1998, Mr. Ganio served as Vice President of Worldwide Sales and Marketing for Xyplex, Inc. From March 1987 to September 1996, Mr. Ganio held various high-level positions with Digital Equipment Corporation, including Vice President of Operations in Japan, Vice President and General Manager of the Americas Networks Product business and Vice President and Executive Assistant to the Office of President. Mr. Ganio held various sales positions with IBM from May 1981 to February 1987. Mr. Ganio holds a bachelors degree, magna cum laude from Bernard Baruch College.

Mark R. Knittel was appointed Group Vice President of Worldwide Product Operations in October 1999. From May 1997 to October 1999, Mr. Knittel served as our Vice-President of Marketing and also as our Vice President of Architecture and Business Development from March 1997 to May 1997. From July 1977 to March 1997, Mr. Knittel was employed with IBM where he held several executive development positions for both hardware and software networking products, as well as multiple strategy positions. Most recently, Mr. Knittel held the position of Director of Campus Product Marketing within the Network Hardware Division of IBM. Mr. Knittel has a masters degree in philosophy from the University of Chicago.

PART II

Item 5. Market for the Registrant's Securities and Related Shareholder Matters

PRICE RANGE OF COMMON STOCK

Our common stock is traded on the Nasdaq National Market under the symbol "CMNT." The following table sets forth for the indicated periods the range of high and low per share sales prices for our common stock as reported on the Nasdaq National Market:

	Price Range of Common Stock	
	High	**Low**
2000		
First Quarter	$27.00	$11.50
Second Quarter	19.88	11.56
Third Quarter	35.25	15.25
Fourth Quarter	40.00	18.69
1999		
First Quarter	$17.56	$ 9.75
Second Quarter	30.63	13.00
Third Quarter	23.25	9.19
Fourth Quarter	27.63	7.38
1998		
First Quarter	$ 5.00	$ 3.69
Second Quarter	5.88	3.88
Third Quarter	6.50	3.50
Fourth Quarter	14.25	3.75

As of April 1, 2001, there were 1,000 shareholders of record. The Company estimates that approximately an additional 6,000 shareholders own stock held for their accounts at brokerage firms and financial institutions.

DIVIDEND POLICY

We have not paid any cash dividends since our inception, and we do not intend to pay any cash dividends in the future.

Item 6. Selected Consolidated Financial Information

	Year Ended January 31, 2001	Years Ended December 31, 1999	1998	1997	1996
		(in thousands, except per share data)			
Consolidated Statements of Operations Data:					
Revenue:					
Product sales	$125,432	$ 89,248	$ 74,969	$56,127	$61,412
Service fees	50,674	36,741	28,052	24,068	20,667
Total revenue	176,106	125,989	103,021	80,195	82,079
Cost of revenue	83,181	56,795	45,616	36,002	38,111
Cost of revenue — special charges	—	1,414 (2)	—	—	—
Total cost of revenue	83,181	58,209	45,616	36,002	38,111
Gross profit	92,925	67,780	57,405	44,193	43,968
Operating expenses:					
Sales and marketing	41,019	34,626	32,255	27,504	22,370
Engineering and development	22,572	18,456	14,236	12,384	10,963
General and administrative	8,697	6,922	6,252	4,944	5,137
Special charges	(287) (1)	1,331 (2)	—	—	(779) (3)
Total operating expenses	72,001	61,335	52,743	44,832	37,691
Income (loss) from operations	20,924	6,445	4,662	(639)	6,277
Other income, net	3,152	110	427	1,400	2,072
Income from continuing operations before income taxes	24,076	6,555	5,089	761	8,349
Provision for income taxes	7,947	2,229	1,730	312	3,173
Income from continuing operations	16,129	4,326	3,359	449	5,176
Income (loss) from discontinued operations, net of tax	(4,135)	329	1,370	(2,763)	(3,816)
Net income (loss)	$ 11,994	$ 4,655	$ 4,729	$(2,314)	$ 1,360
Diluted income (loss) per share:					
Continuing operations	$ .58	$ .17	$ .15	$ .02	$ .22
Discontinued operations	$ (.15)	$ .01	$ .06	$ (.12)	$ (.16)
Net income (loss)	$ .43	$ .18	$ .21	$ (.10)	$ .06
Diluted shares	27,813	25,818	22,572	22,702	23,557

	As of January 31, 2001	As of December 31, 1999	1998	1997	1996
Consolidated Balance Sheet Data:					
Cash, cash equivalents and marketable securities	$150,477	$ 26,895	$ 12,362	$10,824	$35,065
Working capital	182,625	50,715	35,587	30,380	48,192
Total assets	268,623	110,654	87,596	78,950	81,561
Long-term obligations	1,952	1,780	1,816	701	—
Total shareholders' equity	213,102	78,472	60,558	55,607	64,161

(1) Reflects a reversal of the unused balance of a 1999 fourth quarter accrual for an abandoned facility of $287,000.

(2) Reflects special charges in the fourth quarter of 1999 of $1.4 million for the write-off of non-storage network-related products and $1.3 million for an abandoned facility.

(3) Reflects a $779,000 reversal of a portion of a 1995 management reorganization charge.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

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

Overview

We are a leading provider of hardware and software products and related professional services in the rapidly growing storage networking market. We focus primarily on helping our clients design, develop, deploy and manage storage networks. Our storage networking products represent our core business and account for a substantial majority of our revenue and profit. Our storage networking products consist primarily of our UltraNet® and Channelink® families of products. We also market our established channel networking products, which enable computers to transmit data over unlimited distances.

The current global economic slowdown makes it difficult to predict the demand for our products as we cannot forecast the length, duration and impact of the slowdown. Slower growth throughout the economy has caused our customers to reevaluate their capital spending plans, and to defer previously planned projects for information technology infrastructure. However, we believe the need for storage networking solutions is significant and will continue to increase.

On April 24, 2001 we announced that our anticipated revenues for our first quarter ending April 30, 2001 will be 30%-40% lower than the fourth quarter of fiscal 2000. As a result, we announced a one-time charge for our first quarter consisting of $700,000, or $.02 per share after tax, for an approximate 10% reduction in workforce; $300,000, or $.01 per share after tax, for a write-off of non-strategic product lines; and $2.0 million, or $.04 per share after tax, for an increase in reserves for slow-moving inventory. We also announced other cost control measures including elimination of most outside contract and temporary employees; a freeze on all wage increases; a 10% pay reduction for executive management; a 5% pay reduction for all other employees; a consolidation of facilities; and cuts in discretionary spending company wide. In addition, our board of directors authorized the repurchase of up to $50 million of our common stock to be effected from time to time.

On April 3, 2001 we acquired all of the outstanding stock of Articulent Inc., a privately held, leading provider of storage management services for $12 million in cash, plus the assumption of approximately $24 million of liabilities and the acquisition of approximately $19 million of tangible assets. The agreement includes a $10 million incentive payout based upon meeting certain revenue and earnings milestones over the next twelve months. The acquisition further strengthens our storage services organization, which provides companies with the expertise to manage information enterprise-wide.

On January 12, 2000, we changed our fiscal year end to January 31, from December 31. References in this Form 10-K to fiscal year 2000 represent the twelve months ended January 31, 2001. References in this Form 10-K to fiscal years 1999 and 1998 represent the twelve months ended December 31, 1999 and 1998. We have not submitted financial information for the twelve months ended January 31, 2000 and 1999 in this Form 10-K because the information is not practical or cost beneficial to prepare. We believe that the twelve months ended December 31, 1999 and 1998 provide a meaningful comparison to the twelve months ended January 31, 2001. There are no factors, of which we are aware, seasonal or otherwise, that would impact the comparability of information or trends, if results for the twelve months ended January, 31, 2000 and 1999 were presented in lieu of results for the twelve months ended December 31, 1999 and 1998.

Discontinued Operation — Divestiture of Propelis Software, Inc.

Our discontinued operations, which we have historically referred to as our Enterprise Integration Solutions Division, develops and sells our EAI software that automates the integration of computer applications and business workflow processes, as well as our traditional server gateways and tools which enable multiple desktop computers and mainframe terminals to communicate with one another. We recently changed the name of our Enterprise Integration Solutions Division to Propelis Software, Inc. Our board of directors has determined to divest Propelis Software, Inc. in order to focus all of our resources on our other storage networking products. As a result of this decision, Propelis Software, Inc. is shown as a discontinued operation in our consolidated statements of operations, meaning that the division's revenues, costs and expenses are not shown and its net income (loss), net of tax for all periods are included under the "Discontinued Operations" caption.

In the first quarter of fiscal 2001, we expect to accrue for the estimated future losses to be generated by Propelis Software, Inc. through the potential date of divestiture, resulting in a one-time after tax loss of approximately $3.5 million.

On February 2, 2001, we completed the sale of our IntelliFrame subsidiary, which was part of Propelis Software, Inc., including the technology underlying our Propelis BPm™ product to WebMethods for $8.8 million in cash and 273,542 shares of WebMethods stock. Propelis Software, Inc. retains a license, subject to certain restrictions, to the BPm™ product, its name, the customers and the prospects. We expect that Propelis Software, Inc. will continue to sell the BPm™product in the future. In the first quarter of fiscal 2001, we expect to recognize a one-time after tax gain of approximately $12.5 million from the sale of Intelliframe in the discontinued operations section of our statement of operations.

For additional information regarding the results of operations of Propelis Software, Inc., see note 4, "Discontinued Operations" to the consolidated financial statements. Certain general and administrative, facility and information technology infrastructure costs that had previously been allocated to and reported in the operating results of Propelis Software, Inc. have been reallocated and reported in the results for continuing operations.

Results of Continuing Operations

The following table sets forth financial data for our continuing operations for the periods indicated as a percentage of total revenue except for gross profit, which is expressed as a percentage of the related revenue.

	Year Ended January 31,	Years Ended December 31,	
	2001	1999	1998
Revenue:			
Product sales	71.2%	70.8%	72.8%
Service fees	28.8	29.2	27.2
Total revenue	100.0	100.0	100.0
Gross profit:			
Product sales	57.9	57.0	63.4
Service fees	40.2	46.1	35.2
Total gross profit	52.8	53.8	55.7
Operating expenses:			
Sales and marketing	23.3	27.5	31.3
Engineering and development	12.8	14.6	13.8
General and administrative	4.9	5.5	6.1
Abandoned facility	(.2)	1.1	—
Total operating expenses	40.8	48.7	51.2
Income from operations	12.0	5.1	4.5
Other income, net	1.7	.1	.4
Income from continuing operations before income taxes	13.7	5.2	4.9
Provision for income taxes	4.5	1.8	1.7
Income from continuing operations	9.2	3.4	3.2
Income (loss) from discontinued operations, net of tax	(2.4)	.3	1.4
Net income	6.8%	3.7%	4.6%

Revenue

Years Ended January 31, 2001 and December 31, 1999

Revenue from products increased 41% in 2000 to $125.4 million from $89.2 million in 1999. Storage networking applications for both open systems and mainframes continued to drive our new product revenue. Storage networking related product revenue increased 64% in 2000 to $87.8 million from $53.6 million in 1999. Revenue in the fourth quarter was negatively impacted because slower growth throughout the economy caused our customers to reevaluate their capital spending plans, and to defer previously planned projects for information technology infrastructure. Sales of channel extension product applications increased 6% in 2000 to $37.7 million from $35.6 million in 1999. Although we expect sales of channel extension products to decline in the future, it continues to be a profitable part of our business and a key application for many of our storage networking customers.

During 2000, partner relationships with STK and Compaq generated significant product revenue. Sales of the DXE product to STK contributed $9.3 million of product revenue, while our OEM relationship with Compaq contributed $5.7 million of product revenue. We discontinued the DXE/RDE product line in March 2001, and plan to transition the customer base to our UltraNet® and Channelink® products. In 1999, Compaq entered into a multi-million dollar commitment to resell our storage networking products. We have released them from any further commitment, and will be working with them on a co-sell basis in the future. We believe this type of arrangement will be more beneficial to both companies going forward.

Service revenue increased 38% in 2000 to $50.7 million from $36.7 million in 1999. Professional service revenue in 2000 totaled $8.3 million, an increase of 82%, from $4.6 million in 1999 as a result of increased demand for our new professional service offerings. Traditional maintenance services accounted for the remaining increase in revenue due to the growing installed base of customers using our networking products.

Years Ended December 31, 1999 and 1998

Revenue from products increased 19% in 1999 to $89.2 million from $75.0 million in 1998. Storage networking applications for both open systems and mainframes continued to drive new product revenue during 1999. Storage networking product sales increased 68% in 1999 to $53.6 million from $31.9 million in 1998. Channel extension product applications declined 17% in 1999 to $35.6 million from $43.1 million in 1998.

Service revenue increased 31% in 1999 to $36.7 million, due to the growing installed base of customers using our products. In addition, the sale of professional services increased 203% in 1999 to $4.6 million from $1.5 million in 1998.

General

Revenue from the sale of products and services outside the United States increased in 2000 and 1999 by $8.9 million, or 20%, and $10.1 million, or 30%, respectively, when compared to the prior year. We derived 30%, 35% and 32% of our revenue outside the United States in 2000, 1999 and 1998, respectively. The increase in revenue generated outside the United States is primarily attributable to growing customer demand for storage networking-related product applications.

No single customer accounted for more than 10% of our revenue in 2000, 1999 or 1998. Revenue increases in 2000 and 1999 were attributable to increases in sales of storage networking products and additional services. Price increases for our products and services did not have a significant impact on revenue in 2000, 1999 or 1998.

During the year ended January 31, 2001, approximately 21%, 5% and 10% of our product revenue was derived from businesses in the financial services, telecommunications and information outsourcing industries, respectively.

We derive an increasingly significant portion of our revenue from sales of our storage networking products. We expect that revenue from traditional channel networking products will decline in the future as we continue to focus more of our resources on our storage networking products and service offerings.

We primarily sell our storage networking products directly to end-user customers in connection with joint marketing activities with our business partners and OEMs. OEMs combine our products with their own products and sell the combined products to their customers. For a new customer, the initial sales and design cycle, from first contact through shipment, can vary from 90 days to 12 months or more. We expect that this cycle will continue.

We expect continued quarter-to-quarter fluctuations in revenue in both domestic and international markets. The timing of sizable orders, because of their relative impact on total quarterly sales, may contribute to such fluctuations. The level of product sales reported by us in any given period will continue to be affected by the receipt and fulfillment of sizable new orders in both domestic and international markets.

Gross Profit Margin

Years Ended January 31, 2001 and December 31, 1999

Gross profit margin from the sale of products was 58% in 2000, compared to 57% in 1999. Excluding a $1.4 million charge for the write-off of non-storage networking-related products, gross profit margin from the sale of products would have been 59% in 1999. The decrease in gross profit margin to 58% from 59% in 1999 was due to an increase in sales of our DXE product to STK, and our UltraNet® Gateway product to Compaq, both of which carry lower gross margin, but comparable operating margin, than our Channelink® and UltraNet® products sold through direct channels.

Gross profit margin from services revenues in 2000 and 1999 was 40% and 46%, respectively. The decrease in gross margin was due to new professional services employees who have been added in 2000 in anticipation of future growth in professional services.

Years Ended December 31, 1999 and 1998

Gross profit margin from the sale of products was 57% in 1999, compared to 63% in 1998. The decrease in gross profit margin in 1999 compared to 1998 is attributable to the write-off of non-storage networking-related products totaling $1.4 million. Excluding this charge, gross profit margin from the sale of products would have been 59% in 1999. The remaining decrease in gross profit margin in 1999 was due to an increase in UltraNet® product sales, which have a slightly lower gross margin than our traditional Channelink® products.

Gross profit margin from service revenues in 1999 and 1998 was 46% and 35%, respectively. The improvement in gross profit margin in 1999 compared to 1998 is attributable to economies of scale resulting from the steadily increasing base of our customers contracting for services and new incremental revenue from professional services, which offers a higher gross margin than our traditional service business.

Operating Expenses

Years Ending January 31, 2001 and December 31, 1999

Sales and marketing expense increased 18% in 2000 to $41.0 million from $34.6 million in 1999. The increase in expense resulted from higher commissions and additional headcount required to generate the 41% increase in product revenue for 2000.

Engineering and development expense increased 22% in 2000 to $22.6 million from $18.5 million in 1999. The increase was primarily due to continued development of our UltraNet® family of products that provide customers with additional applications to satisfy their growing storage networking capabilities. During 2000, we announced storage networking over standard IP solutions, including tape, SCSI and Fibre Channel over IP to strengthen our presence in the IP solutions market.

General and administrative expense increased 26% in 2000 to $8.7 million from $6.9 million in 1999. The increase was due to higher costs for wages, insurance and professional fees.

Years Ended December 31, 1999 and 1998

Sales and marketing expense increased 7% in 1999 to $34.6 million from $32.3 million in 1998. The increase in expense resulted from higher commissions and additional headcount required to generate the 19% increase in product revenue for 1999.

Engineering and development expense increased 30% in 1999 to $18.5 million from $14.2 million in 1998. The increase was due to the continued development of our UltraNet® family of products that provide customers with additional applications to satisfy their growing need for storage networking capabilities. Revenue related to shipments of UltraNet® products increased 111% to $37.5 million in 1999 from $17.7 million in 1998.

General and administrative expense increased 11% in 1999 to $6.9 million from $6.3 million in 1998 due to increases in insurance costs and professional fees.

Special Charges

Years Ended January 31, 2001, December 31, 1999 and 1998

During the fourth quarter of 1999, we recorded a $1.3 million charge for the future costs associated with a facility that was abandoned prior to the expiration of the lease term and a $1.4 million charge for the write-off of non-storage networking related products. We reversed the unused portion of the $1.3 million charge for the abandoned facility in the third quarter of 2000. The amount of the reversal was $287,000.

Other

Years Ending January 31, 2001, December 31, 1999 and 1998

Other income increased in 2000 and 1999 by $3.0 million and $351,000, respectively, when compared to the prior year due to an increase in interest income resulting from higher balances of cash and marketable securities available for investment. In October of 2000, we raised $110 million from a secondary stock offering. Pending use of the offering proceeds for general corporate purposes or complementary acquisitions, the funds have been invested in investment grade, interest-bearing securities.

Interest expense increased to $338,000 in 2000 from $264,000 in 1999 due to an increase in capital lease obligations.

We recorded a provision for income taxes at an effective tax rate of 33% in 2000, and at an effective tax rate of 34% in both 1999 and 1998. The fluctuations in our effective tax rate are primarily due to the large special charges that have been recorded each year, the amount of nondeductible foreign losses and fluctuations in the level of benefit from our foreign sales corporation. Based on an assessment of our taxable earnings history and prospective future taxable income, we have determined it to be more likely than not that our net deferred tax asset will be realized in future periods. We may be required to provide a valuation allowance for this asset in the future if we do not generate sufficient taxable income as planned.

Discontinued Operations

Years Ending January 31, 2001 and December 31, 1999

Discontinued operations consisting of Propelis Software, Inc. formerly known as our Enterprise Integration Solutions Division generated a loss after income taxes in 2000 of $4.1 million, compared to income after income taxes of $329,000 in 1999. The decrease in profitability can be attributed to a 64% decline in revenue from sales of our server gateways and tools products in 2000 to $3.5 million from $9.7 million in 1999. In addition, lower margin hardware sales accounted for a larger percentage of server gateways and tools product revenue in 2000 when compared to the same periods of 1999. Maintenance revenue from our traditional server gateways and tools products declined in 2000 to $2.5 million, from $5.0 million in 1999, due to a drop off in the installed base of customers using our traditional server gateways and tools products.

Years Ended December 31, 1999 and 1998

Discontinued operations generated income after income taxes of $329,000 in 1999 compared to income after income taxes of $1.4 million in 1998. The decrease in profitability can be attributed to a 40% decline in revenue from sales of our server gateways and tools products in 1999 to $9.7 million from $16.1 million in 1998. In addition, total maintenance revenue declined to $6.3 million in 1999 from $7.6 million in 1998 due to a drop off in the installed base of customers using our traditional server gateways and tools products.

Acquisition and Sale of Intelliframe

On December 3, 1998, we acquired, for $2.0 million, all of the outstanding stock of IntelliFrame, a start-up software and services company that develops technology for integrating legacy systems with client/server systems and the Internet. On February 2, 2001, we sold IntelliFrame to WebMethods, Inc. for $8.8 million in cash and 273,542 shares of WebMethods stock. In the first quarter of fiscal 2001, we expect to recognize a one-time after tax gain of approximately $12.5 million from the sale of Intelliframe in the discontinued operations section of our statement of operations. Since February 2, 2001, WebMethods stock has experienced a significant decline in market value. We will not record a loss in our statement of operations for this decline in market value until such time as the stock is sold, or the decline in value is determined to be other than temporary.

Options

We have issued options for the purchase of approximately 2.9 million shares of common stock in Propelis Software, Inc. (formerly RealLegacy.com, Inc.) our wholly owned subsidiary including our EAI business, to our directors and the employees and officers of Propelis Software, Inc. The options have an exercise price of $2.00 per share, equal to their estimated fair market value on the date of grant, and have individually defined terms and vesting periods.

Liquidity and Capital Resources

We have historically financed our operations through the public and private sale of equity securities, bank borrowings under lines of credit, capital and operating equipment leases and cash generated by operations.

Cash, cash equivalents and marketable securities at January 31, 2001 totaled $150.5 million, an increase of $133.9 million since January 31, 2000. During the third quarter of 2000, we raised $110 million from a secondary stock offering. Operations and proceeds from the exercise of stock options provided cash in 2000 of $36.8 million and $7.5 million, respectively. Uses of cash in 2000 included the purchase of property and equipment, field support spares and purchased technology totaling $17.2 million.

Expenditures for capital equipment and field support spares have been, and will likely continue to be, a significant capital requirement. We believe that our current balances of cash, cash equivalents and marketable securities, when combined with anticipated cash flows from operations, will be adequate to fund our operating plans and meet our current anticipated aggregate capital requirements, at least through fiscal 2001.

In March of 2001, our board of directors adopted an amendment to our 1999 Non-Qualified Stock Award Plan increasing the number of shares authorized for issuance from 1,730,000 to 3,230,000.

We believe that inflation has not had a material impact on our operations or liquidity to date.

New Accounting Pronouncements

Statement of Financial Accounting Standard No. 133, "Accounting for Derivative Instruments and Hedging Activities" (SFAS No. 133), effective for us on February 1, 2001, establishes new standards for recognizing all derivatives as either assets or liabilities and measuring those instruments at fair value. SFAS No. 133 did not have a material impact on our financial position or results of operations.

Change in Fiscal Year

On January 12, 2000, we changed our fiscal year end to January 31, rather than December 31. Our summary January 2000 results are as follows: revenues $4.3 million; gross profit $1.3 million; operating expenses $5.3 million; net loss from continuing operations $2.6 million; net loss from discontinued operations $1.0 million; and net loss $3.6 million. We typically incur significant losses in the first month following the completion of a quarter because our revenue is significantly less than the average monthly revenues we generate in any quarterly or annual period.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

We have no derivative financial instruments in our cash, cash equivalents and marketable securities. We mainly invest our cash and cash equivalents in investment grade, highly liquid investments, consisting of money market instruments, bank certificates of deposits and investments in commercial paper. On February 2, 2001, we received 273,542 shares of WebMethods stock in connection with the sale of IntelliFrame. For purposes of recognizing our gain on sale, the stock was value at $17.0 million, or $62 per share. Since February 2, 2001, WebMethods stock has experienced a significant decline in market value. We will not record a loss in our statement of operations for this decline in market value until such time as the stock is sold, or the decline in value is determined to be other than temporary.

At January 31, 2001, our marketable securities include a $514,000 investment in a Standard and Poors 500 stock price index fund and a $402,000 investment in a NASDAQ 100 index tracking stock. These investments were purchased to directly offset any investment gains or losses owed to participants under our executive deferred compensation plan which has been established for selected key employees.

We are exposed to market risks related to fluctuations in foreign exchange rates because some sales transactions, and the assets and liabilities of our foreign subsidiaries, are denominated in foreign currencies, primarily French francs, the euro and British pounds sterling. As of January 31, 2001, we have hedged a portion of our risk by purchasing forward exchange contracts for 900,000 British pounds sterling that settle at various times through April 2001.

Item 8. Consolidated Financial Statements and Supplementary Data

COMPUTER NETWORK TECHNOLOGY CORPORATION

CONSOLIDATED BALANCE SHEETS
(in thousands, except per share data)

	January 31, 2001	December 31, 1999
Assets		
Current assets:		
Cash and cash equivalents	$ 39,444	$ 16,184
Marketable securities	111,033	10,711
Receivables, net	43,613	29,517
Inventories	22,447	14,425
Net current assets of discontinued operations	5,430	5,089
Deferred tax asset	11,415	3,415
Other current assets	2,226	1,776
Total current assets	235,608	81,117
Property and equipment, net	25,215	17,529
Field support spares, net	4,446	3,879
Deferred tax asset	—	2,070
Goodwill and other intangibles, net	1,200	1,222
Net non-current assets of discontinued operations	—	4,645
Other assets	2,154	192
	$268,623	$110,654
Liabilities and shareholders' equity		
Current liabilities:		
Accounts payable	$ 20,293	$ 11,408
Accrued liabilities	15,780	10,010
Deferred revenue	15,489	8,296
Current installments of obligations under capital lease	1,421	688
Total current liabilities	52,983	30,402
Deferred tax liability	586	—
Obligations under capital lease, less current installments	1,952	1,780
Total liabilities	55,521	32,182
Shareholders' equity:		
Undesignated preferred stock, authorized 965 shares; none issued and outstanding	—	—
Series A Junior Participating Preferred Stock, authorized 40 shares; none issued and outstanding	—	—
Common stock, $.01 par value; authorized 100,000 shares; issued and outstanding 29,656 at January 31, 2001, and 23,792 at December 31, 1999	297	238
Additional paid-in capital	195,910	68,927
Unearned compensation	(1,304)	(838)
Retained earnings	19,165	10,796
Accumulated other comprehensive income-foreign currency translation adjustment	(966)	(651)
Total shareholders' equity	213,102	78,472
	$268,623	$110,654

See accompanying notes to consolidated financial statements

COMPUTER NETWORK TECHNOLOGY CORPORATION

CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data)

	Year Ended January 31, 2001	Years Ended December 31, 1999	Years Ended December 31, 1998	Month Ended January 31, 2000
Revenue:				
Product sales	$125,432	$89,248	$74,969	$ 1,237
Service fees	50,674	36,741	28,052	3,105
Total revenue	176,106	125,989	103,021	4,342
Cost of revenue:				
Cost of product sales	52,873	38,411	27,441	894
Cost of service fees	30,308	19,798	18,175	2,148
Total cost of revenue	83,181	58,209	45,616	3,042
Gross profit	92,925	67,780	57,405	1,300
Operating expenses:				
Sales and marketing	41,019	34,626	32,255	2,643
Engineering and development	22,572	18,456	14,236	1,814
General and administrative	8,697	6,922	6,252	836
Abandoned facility	(287)	1,331	—	—
Total operating expenses	72,001	61,335	52,743	5,293
Income (loss) from operations	20,924	6,445	4,662	(3,993)
Other income (expense):				
Interest income	3,802	744	393	95
Interest expense	(338)	(264)	(79)	(6)
Other, net	(312)	(370)	113	4
Other income, net	3,152	110	427	93
Income (loss) from continuing operations before income taxes	24,076	6,555	5,089	(3,900)
Provision (benefit) for income taxes	7,947	2,229	1,730	(1,287)
Income (loss) from continuing operations	16,129	4,326	3,359	(2,613)
Income (loss) from discontinued operations, net of tax	(4,135)	329	1,370	(1,012)
Net income (loss)	$ 11,994	$ 4,655	$ 4,729	$(3,625)
Basic income (loss) per share:				
Continuing operations	$ .64	$ .19	$ .15	$ (.11)
Discontinued operations	$ (.16)	$ .01	$ .06	$ (.04)
Net income (loss)	$ .47	$ .20	$ .21	$ (.15)
Shares	25,383	23,137	22,095	23,815
Diluted income (loss) per share:				
Continuing operations	$ .58	$ .17	$ .15	$ (.11)
Discontinued operations	$ (.15)	$ .01	$ .06	$ (.04)
Net income (loss)	$ .43	$ .18	$ .21	$ (.15)
Shares	27,813	25,818	22,572	23,815

See accompanying notes to consolidated financial statements

COMPUTER NETWORK TECHNOLOGY CORPORATION

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY AND COMPREHENSIVE INCOME

(in thousands)

	Common Stock		Additional Paid-in Capital	Unearned Compensation	Retained Earnings	Accumulated Other Comprehensive Income	Total
	Shares	Amount					
Balance, December 31, 1997	22,195	$222	$ 54,439	$ (35)	$ 1,412	$(431)	$ 55,607
Shares issued pursuant to the employee stock purchase plan, restricted stock plan and exercise of stock options	454	5	2,041	(401)	—	—	1,645
Tax benefits from employee stock transactions	—	—	195	—	—	—	195
Repurchase of common stock	(395)	(4)	(1,754)	—	—	—	(1,758)
Compensation expense	—	—	—	81	—	—	81
Comprehensive income:							
Net income	—	—	—	—	4,729	—	4,729
Translation adjustment, net of tax effect of $0	—	—	—	—	—	59	59
Total comprehensive income	—	—	—	—	—	—	4,788
Balance, December 31, 1998	22,254	$223	$ 54,921	$ (355)	$ 6,141	$(372)	$ 60,558
Shares issued pursuant to the employee stock purchase plan, restricted stock plan and exercise of stock options	1,538	15	9,354	(799)	—	—	8,570
Tax benefits from employee stock transactions	—	—	4,652	—	—	—	4,652
Compensation expense	—	—	—	316	—	—	316
Comprehensive income:							
Net loss	—	—	—	—	4,655	—	4,655
Translation adjustment, net of tax effect of $0	—	—	—	—	—	(279)	(279)
Total comprehensive income	—	—	—	—	—	—	4,376
Balance, December 31, 1999	23,792	$238	$ 68,927	$ (838)	$10,796	$(651)	$ 78,472
Shares issued pursuant to the employee stock purchase plan, restricted stock plan and exercise of stock options	49	—	507	(341)	—	—	166
Tax benefits from employee stock transactions	—	—	—	—	—	—	—
Compensation expense	—	—	—	49	—	—	49
Comprehensive income:							
Net loss	—	—	—	—	(3,625)	—	(3,625)
Translation adjustment, net of tax effect of $0	—	—	—	—	—	49	49
Total comprehensive loss	—	—	—	—	—	—	(3,576)
Balance, January 31, 2000	23,841	$238	$ 69,434	$(1,130)	$ 7,171	$(602)	$ 75,111
Shares issued pursuant to the employee stock purchase plan, restricted stock plan and exercise of stock options	1,215	13	8,181	(675)	—	—	7,519
Shares issued pursuant to a secondary stock offering, net of offering costs	4,600	46	110,189	—	—	—	110,235
Tax benefits from employee stock transactions	—	—	8,106	—	—	—	8,106
Compensation expense	—	—	—	501	—	—	501
Comprehensive income:							
Net income	—	—	—	—	11,994	—	11,994
Translation adjustment, net of tax effect of $0	—	—	—	—	—	(364)	(364)
Total comprehensive income	—	—	—	—	—	—	11,630
Balance, January 31, 2001	29,656	$297	$195,910	$(1,304)	$19,165	$(966)	$213,102

See accompanying notes to consolidated financial statements

COMPUTER NETWORK TECHNOLOGY CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	Year Ended January 31, 2001	Years Ended December 31, 1999	Years Ended December 31, 1998	Month Ended January 31, 2000
Operating Activities:				
Net income (loss)	$ 11,994	$ 4,655	$ 4,729	$(3,625)
Discontinued operations	4,135	(329)	(1,370)	1,012
Depreciation and amortization	11,812	9,083	7,414	652
Compensation expense	346	219	58	49
Change in deferred taxes	(5,344)	(1,936)	506	—
Changes in operating assets and liabilities:				
Receivables	(14,833)	(5,872)	872	608
Inventories	(3,717)	3,489	(6,815)	(4,305)
Other current assets	(445)	(804)	127	(4)
Accounts payable	11,036	4,272	(78)	(2,151)
Accrued liabilities	17,754	2,563	4,179	(3,878)
Deferred revenue	5,569	2,636	(1,528)	2,045
Net cash provided by (used in) continuing operations	38,307	17,976	8,094	(9,597)
Net cash provided by (used in) discontinued operations	(1,490)	789	2,829	1,051
Cash provided by (used in) operating activities	36,817	18,765	10,923	(8,546)
Investing Activities:				
Additions to property and equipment	(14,329)	(8,262)	(6,345)	(542)
Additions to field support spares	(2,520)	(2,727)	(2,198)	(271)
Additions to purchased technology	(375)	—	(185)	—
Purchase of marketable securities	(148,389)	(15,421)	(18,054)	—
Redemption of marketable securities	45,998	5,286	23,512	2,070
Other assets	(1,967)	327	6	3
Discontinued operations — acquisition of business	—	—	169	—
Discontinued operations — additions to long-term assets	(158)	(507)	(547)	(12)
Cash provided by (used in) investing activities	(121,740)	(21,304)	(3,642)	(1,248)
Financing Activities:				
Payments for repurchases of common stock	—	—	(1,758)	—
Proceeds from issuance of common stock	117,754	8,570	1,645	166
Repayments of obligations under capital leases	(1,187)	(327)	(181)	(65)
Discontinued operations — repayment of debt	—	(1,000)	—	(1,000)
Cash provided by (used in) financing activities	116,567	7,243	(294)	(899)
Effects of exchange rate changes	(174)	(306)	9	(13)
Net increase (decrease) in cash and cash equivalents	31,470	4,398	6,996	(8,210)
Cash and cash equivalents — beginning of period	7,974	11,786	4,790	16,184
Cash and cash equivalents — end of period	$ 39,444	$ 16,184	$ 11,786	$ 7,974

See accompanying notes to consolidated financial statements

COMPUTER NETWORK TECHNOLOGY CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
January 31, 2001, December 31, 1999 and 1998
(tabular amounts in thousands except per share data)

(1) Summary of Significant Accounting Policies

Description Of Business

Computer Network Technology Corporation is a leading worldwide provider of high-performance storage networking solutions and world class services.

Discontinued Operations

The Company has determined to divest Propelis Software, Inc. formerly known as the Enterprise Integration Solutions Division. Accordingly, Propelis Software, Inc. has been accounted for as discontinued operations in the accompanying financial statements.

Change in Year End

On January 12, 2000, the Company changed its fiscal year end to January 31, from December 31. The Company believes that the twelve months ended December 31, 1999 and 1998 provide a meaningful comparison to the twelve months ended January 31, 2001. There are no factors, of which the Company is aware, seasonal or otherwise, that would impact the comparability of information or trends, if results for the twelve months ended January 31, 1999 and 1998 were presented in lieu of results for the twelve months ended December 31, 1999 and 1998. References in these footnotes to fiscal 2000 represent the twelve months ended January 31, 2001. References to fiscal 1999 and 1998 represent the twelve months ended December 31, 1999 and 1998.

Principles Of Consolidation

The accompanying consolidated financial statements include the accounts of Computer Network Technology Corporation and its subsidiaries (together, the Company). All significant intercompany balances and transactions are eliminated in consolidation.

Revenue Recognition

Revenue from product sales is generally recognized by the Company upon shipment or signed customer acceptance depending on the terms of the contract or purchase order. Service fees are recognized as revenue when earned, which is generally on a straight-line basis over the contracted service period. Deferred revenue primarily consists of the unearned portion of service agreements billed in advance to customers.

In December of 1999, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements," (SAB 101), which provides guidance on the recognition, presentation, and disclosure of revenue in financial statements filed with the SEC. SAB 101 outlines the basic criteria that must be met to recognize revenue and provides guidance for disclosures related to revenue recognition polices. Adoption of SAB 101 during the fourth quarter of 2000 did not have a material impact on the Company's financial position or results of operations.

Cash Equivalents

The Company considers investments in highly liquid debt securities having an initial maturity of three months or less to be cash equivalents.

Marketable Securities

If significant, unrealized gains and losses on available-for-sale securities are excluded from earnings and are reflected as a separate component of shareholders' equity. Unrealized gains and losses on trading securities are included in earnings.

Inventories

Inventories are stated at the lower of cost (determined on a first in, first out basis) or market.

Property And Equipment

Property and equipment owned by the Company is carried at cost and depreciated using the straight-line method over three to eight years. Leasehold improvements are amortized using the straight-line method over the terms of the respective leases. Expenditures for repairs and maintenance are charged to expense as incurred. Capital lease equipment is amortized over the life of the lease.

Field Support Spares

Field support spares are carried at cost and depreciated using the straight-line method over three years.

Goodwill And Other Intangibles

Goodwill represents the excess of purchase price over the fair value of net assets acquired and is amortized using the straight-line method over periods ranging from five to twenty years. Purchased technology and other identifiable intangible assets are carried at cost and amortized using the straight-line method over periods ranging from two to seven years.

Impairment of Long-Lived Assets

The recoverability of long-lived assets is assessed whenever events or changes in circumstances indicate the carrying value of the asset may not be recoverable through future undiscounted cash flow.

Allowance For Returns And Credit Losses

An allowance is made for potential returns and uncollectible accounts based on current and historical experience. The allowance for returns and credit losses at January 31, 2001, December 31, 1999 and 1998 was $2,383,000, $959,000 and $1,225,000, respectively.

Engineering And Development

The Company has expensed all engineering and development costs to date.

Foreign Currency

The financial statements of the Company's international subsidiaries have been translated into U.S. dollars. Assets and liabilities are translated into U.S. dollars at year-end exchange rates, while equity accounts are translated at historical rates. Income and expenses are translated at the average exchange rates during the year. The resulting translation adjustments are recorded as a separate component of shareholders' equity.

The Company is exposed to market risks related to fluctuations in foreign exchange rates because some sales transactions, and the assets and liabilities of its foreign subsidiaries, are denominated in foreign currencies. As of January 31, 2001, the Company has hedged a portion of its risk by purchasing forward exchange contracts for 900,000 British pounds sterling that settle at various times through April 2001. Gains and losses from transactions denominated in foreign currencies and forward exchange contracts are included in net income (loss).

The Company recognized foreign currency transaction gains in fiscal 2000 and 1998 of $7,000 and $110,000, respectively. The Company recognized a foreign currency transaction loss in fiscal 1999 of $196,000. Foreign currency transaction gains and losses in the one month transition period ended January 31, 2000 were not significant.

Income Taxes

Deferred tax assets and liabilities are recognized for the expected future tax consequences of temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases.

Stock Compensation Plans

The Company accounts for its stock based compensation awards in accordance with Accounting Principles Board Opinion No. 25 "Accounting for Stock Issued to Employees" (APB No. 25) and provides the footnote disclosures required by Statement of Financial Accounting Standards No. 123 "Accounting for Stock Based Compensation" (SFAS No. 123).

Reclassifications

Certain prior year amounts have been reclassified to conform to the current year presentation.

Use Of Estimates

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

Net Income (Loss) Per Share

Basic net income per share is computed based on the weighted average number of common shares outstanding, while diluted net income per share is computed based on the weighted average number of common shares outstanding plus potential dilutive shares of common stock. Potential dilutive shares of common stock include stock options which have been granted to employees and directors and awards under the employee stock purchase plan. Net loss per basic and diluted share is based on the weighted average number of common shares outstanding. Potential dilutive shares of common stock have been excluded from the computation of net loss per share due to their anti-dilutive effect.

Comprehensive Income

Comprehensive income consists of the Company's net income (loss) and foreign currency translation adjustment and is presented in the consolidated statement of shareholders' equity and comprehensive income.

New Accounting Pronouncements

Statement of Financial Accounting Standard No. 133, "Accounting for Derivative Instruments and Hedging Activities" (SFAS No. 133), effective for us on February 1, 2001, establishes new standards for recognizing all derivatives as either assets or liabilities and measuring those instruments at fair value. SFAS No. 133 did not have a material impact on our financial position or results of operations.

(2) Components of Selected Balance Sheet Accounts

	January 31, 2001	December 31, 1999
Inventories:		
Components and subassemblies	$15,218	$ 8,661
Work in process	2,813	3,109
Finished goods	4,416	2,655
	$22,447	$14,425
Property and equipment:		
Machinery and equipment	$35,567	$25,415
Office and data processing equipment	22,764	18,761
Furniture and fixtures	3,197	2,221
Leasehold improvements	1,856	2,264
	63,384	48,661
Less accumulated depreciation and amortization	38,169	31,132
	$25,215	$17,529
Field support spares:		
Field support spares	$19,934	$16,311
Less accumulated depreciation	15,488	12,432
	$ 4,446	$ 3,879
Goodwill and other intangibles:		
Purchased technology	$ 2,040	$ 1,665
Goodwill	866	866
	2,906	2,531
Less accumulated amortization	1,706	1,309
	$ 1,200	$ 1,222
Accrued liabilities:		
Compensation	$ 8,986	$ 5,949
Income taxes	2,450	1,049
Abandoned facility	—	1,331
Product warranty	1,629	740
Other	2,715	941
	$15,780	$10,010

(3) Marketable Securities

The Company's investments in marketable securities are summarized as follows:

	January 31, 2001	December 31, 1999
Available-for-Sale:		
Bank certificates of deposit	$ 29,519	$ 971
U.S. government and agency securities	10,866	—
Corporate debt securities	69,732	9,348
	110,117	10,319
Trading:		
Standard & Poors 500 stock price index fund	514	392
NASDAQ 100 tracking stock	402	—
	$111,033	$10,711

The amount of gross unrealized gains and losses with respect to investments in available-for-sale securities at January 31, 2001 and December 31, 1999 was not significant. The Company realized no significant gains or losses with respect to available-for-sale securities during fiscal 2000, 1999, 1998 or the one month transition period ended January 31, 2000. Proceeds from the sale of available-for-sale securities in fiscal 2000, 1999 and 1998 were $1,204,000, $984,000 and $8,093,000, respectively. There were no sales of available-for-sale securities during the one month transition period ended January 31, 2000. At January 31, 2001, the Company's investments in available-for-sale securities have contractual maturities of three years or less.

The Company's trading securities consist of a mutual fund investment that seeks to provide a return corresponding to the Standard & Poors 500 stock price index and a NASDAQ 100 tracking stock. The Company intends to use any gain or loss from these investments to fund the investment gains or losses owed to participants under the Company's executive deferred compensation plan. The amount of unrealized holding gains (losses) with respect to trading securities included in net income (loss) for fiscal 2000, 1999, 1998 and the one month transition period ended January 31, 2000 was $(168,000), $112,000, $0 and $(11,995), respectively.

On February 2, 2001, the Company received 273,542 shares of WebMethods, Inc. common stock in connection with the sale of Intelliframe (see note 4 to the consolidated financial statements). The common stock of WebMethods, Inc. has experienced a significant decline in value since February 2, 2001. We will not record a loss in our statement of operations for the decline in value of the WebMethods stock until such time as the stock is sold, or the decline in value is determined to be other than temporary.

(4) Discontinued Operations

The Company has determined that it will divest its wholly owned subsidiary Propelis Software, Inc. formerly known as the Enterprise Integration Solutions Division. Accordingly, Propelis Software, Inc. has been accounted for as a discontinued operation in the accompanying financial statements. Propelis Software, Inc. develops and sells EAI software that automates the integration of computer software applications, and business workflow processes, as well as our traditional server gateways and tools, which enable multiple desktop computers and mainframe terminals to communicate with one another. Summary financial information for the discontinued operations was as follows:

Condensed Consolidated Statements of Operations of Discontinued Operations:

	Year Ended January 31, 2001	Years Ended December 31, 1999	1998	Month Ended January 31, 2000
Revenue	$16,132	$25,704	$30,514	$ 472
Income (loss) before income taxes	$(6,174)	$ 498	$ 2,550	$(1,510)
Provision (benefit) for income taxes	(2,039)	169	1,180	(498)
Net income (loss) from discontinued operations	$(4,135)	$ 329	$ 1,370	$(1,012)

Certain general and administrative, facility and information technology infrastructure costs that had previously been allocated to and reported in the operating results of Propelis Software, Inc. have been reallocated to continuing operations.

Condensed Consolidated Statements of Net Assets of Discontinued Operations:

	January 31, 2001	December 31, 1999
Receivables, net	$4,419	$7,330
Other current assets	631	1,775
Goodwill and other intangibles, net	1,497	2,205
Other long-term assets	1,303	2,440
Total assets	7,850	13,750
Debt	—	1,000
All other liabilities	2,420	3,016
Net assets of discontinued operations	$5,430	$9,734

IntelliFrame — Discontinued Operations

Effective December 3, 1998, the Company acquired all of the outstanding stock of IntelliFrame Corporation (IntelliFrame), a start-up software and services company which develops technology for legacy systems integration with client/server and Internet technologies. The purchase price of $2,000,000 was paid in two installments of $1,000,000 each in January 1999 and 2000. The acquisition was accounted for as a purchase and the consolidated financial statements of the Company include, as part of discontinued operations, the results of IntelliFrame since December 3, 1998. The purchase price was allocated to the fair value of the assets and liabilities acquired as follows:

Net tangible assets	$ 148
Identifiable intangibles and goodwill	1,295
In-process research and development	927
Deferred tax liability	(370)
Cash paid	$2,000

On February 2, 2001 the Company sold all of the outstanding stock of IntelliFame Corporation, including the technology underlying the Company's Propelis BPm™ product, to WebMethods, Inc. for

$8.8 million in cash and 273,542 shares of WebMethods common stock. The stock received from WebMethods, Inc. was valued at $17.0 million, which reflects a discount from its publicly reported trading price due to the restrictions on when the stock can be sold. The Company retained a license, subject to certain restrictions, to the Propelis BPm™ product, its name and the customers. In connection with this transaction, the Company paid $3.0 million to two employees, who were former shareholders of IntelliFrame, to satisfy all obligations to make further bonus payments under their employment agreements. In the first quarter of fiscal 2001, the Company expects to recognize an after tax gain of approximately $12.5 million from the sale of Intelliframe in the discontinued operations section of its statement of operations. Since February 2, 2001, WebMethods stock has experienced a significant decline in market value. We will not record a loss in our statement of operations for this decline in market value until such time as the stock is sold, or the decline in value is determined to be other than temporary.

Integration Activities — Discontinued Operations

In October of 1997, the Company acquired substantially all of the assets and assumed certain liabilities of the Internet Solutions Division of Apertus Technologies Incorporated (Apertus), a provider of Internet-to-Mainframe connectivity products and web access to legacy applications. Subsequent to the acquisition of Apertus, the Company decided to consolidate certain operations and recorded a charge of $2,184,000 for costs incurred to integrate existing businesses, including accruals for severance, facility closures and infrastructure integration. During the three months ended December 31, 1999, the Company determined that it would not complete a previously planned consolidation of facilities in the United Kingdom. As a result, the remaining accrual for integration activities of $430,000 was reversed and included in results from discontinued operations in the accompanying 1999 consolidated statement of operations.

In December 1997, the Company sold the assets and technologies relating to the vision line of products acquired from Apertus for $2,000,000 in cash, plus additional payments ranging from $1,500,000 to $2,000,000, depending upon the vision product line achieving a defined future revenue target. The Company did not recognize any gain or loss upon receipt of the initial $2,000,000 cash payment. During the years ended January 31, 2001 and December 31, 1999, the Company received additional payments from the sale of the vision product line of $1,210,000 and $667,000, respectively, which were recognized as income and included in results from discontinued operations. There are no additional payments to be received from the sale of the vision product line.

(5) Leases

The Company leases all office and manufacturing space and certain equipment under noncancelable capital and operating leases. At January 31, 2001 and December 31, 1999, leased capital assets included in property and equipment were as follows:

	January 31, 2001	December 31, 1999
Property and equipment:		
Office and data processing equipment	$4,388	$3,027
Less accumulated amortization	842	1,098
	$3,546	$1,929

Future minimum lease payments, excluding executory costs such as real estate taxes, insurance and maintenance expense, by year and in the aggregate are as follows:

	Minimum Lease Commitments	
	Capital	Operating
Year Ending January 31		
2002	$1,682	$ 4,879
2003	1,479	3,295
2004	629	2,680
2005	—	2,345
2006	—	2,345
Thereafter	—	9,621
Total minimum lease payments	3,790	25,165
Less minimum sublease income	—	826
Net minimum lease payments	3,790	$24,339
Less amounts representing interest at rates ranging from 8.89% to 10.69%	417	
Present value of minimum capital lease payments	3,373	
Less current installments	1,421	
Obligations under capital lease, less current installments	$1,952	

Rent expense under noncancelable operating leases, exclusive of executory costs, for fiscal 2000, 1999, 1998 and the one month transition period ended January 31, 2000 was $5,315,000, $3,970,000, $3,122,000 and $430,888, respectively. The Company recently moved into a new leased facility for its principal office and manufacturing operations. During the year ended December 31, 1999, the Company recognized a $1,331,000 charge for the future costs associated with a facility that was abandoned prior to expiration of the lease term. During the year ended January 31, 2001, the Company reversed $287,000 representing the unused portion of the accrual for the abandoned facility.

(6) Shareholders' Equity

Common Stock Repurchase

On March 10, 1997 the Company's board of directors authorized the repurchase of up to 2,000,000 shares of the Company's common stock. During fiscal 1997 and 1998, the Company repurchased 1,799,900 shares of its common stock for $8,446,000 pursuant to this authorization. No shares have been repurchased since fiscal 1998.

Rights Plan

On July 24, 1998 the Company's board of directors adopted a shareholders rights plan pursuant to which rights were distributed as a dividend at the rate of one preferred share purchase right for each outstanding share of common stock of the Company. The rights will expire on July 23, 2008 unless extended, earlier redeemed or exchanged by the Company.

Stock Options And Restricted Stock

The Company maintains stock option and restricted stock plans (the Plans) which provide for the grant of stock options, restricted stock and stock based awards to officers, other employees, consultants, and independent contractors as determined by the compensation committee of the board of directors. A maximum of 8,830,000 shares of common stock were issuable under the terms of the Plans as of January 31, 2001, of which no more than 930,000 shares may be issued as restricted stock or other stock based awards. As of January 31, 2001, there were 906,000 shares of common stock available for future grants under these plans.

Restricted stock issued under the Plans is recorded at fair market value on the date of grant and generally vests over a two to four year period. Vesting for some grants may be accelerated if certain performance criteria are achieved. Compensation expense is recognized over the applicable vesting period. During fiscal 2000, 1999, 1998 and the one month transition period ended January 31, 2000, the Company issued 61,100, 90,250, 81,000 and 3,000, restricted shares, respectively, having an aggregate weighted fair market value per share of $17.43, $16.25, $4.81, and $17.44, respectively. Compensation expense recognized for restricted shares in fiscal 2000, 1999, 1998 and the one month transition period ended January 31, 2000 was $501,000, $316,000, $81,000 and $49,000, respectively.

All stock options granted under the Plans have an exercise price equal to fair market value on the date of grant, vest and become exercisable over individually defined periods, generally four years, and expire ten years from the date of grant. During fiscal 1999, stock options for 800,000 shares were granted at an exercise price of $21.88 and vest after six years. The options did provide for acceleration of vesting upon certain increases in the Company's stock price. In March of 2001, the vesting for these options was changed to ratably over a four-year period from the original date of grant. As of January 31, 2001, 25% of these options were vested.

A summary of the status of the Company's outstanding stock options and related changes for fiscal 2000, 1999, 1998 and the one month transition period ended January 31, 2000 is presented below:

	Year Ended January 31,		Years Ended December 31,				Month Ended January 31,	
	2001		1999		1998		2000	
Options	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Outstanding at beginning of period	4,798	$10.02	4,972	$ 5.63	4,321	$5.42	4,678	$ 9.78
Granted	1,552	18.77	1,689	18.40	1,269	6.08	165	15.29
Exercised	(1,123)	5.93	(1,540)	5.54	(219)	4.66	(21)	4.89
Canceled	(572)	13.92	(443)	10.79	(399)	5.33	(24)	8.69
Outstanding at end of period	4,655	$13.45	4,678	$ 9.78	4,972	$5.63	4,798	$10.02
Exercisable at end of period	1,633	$ 8.08	1,901	$ 6.31	2,388	$5.71	1,870	$ 6.39
Weighted-average fair value of grants during the period		$13.56		$12.68		$4.48		$12.82

The following table summarizes information about stock options outstanding at January 31, 2001:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted-Average Remaining Contractual Life (in years)	Weighted-Average Exercise Price	Number Exercisable	Weighted-Average Exercise Price
\$ 3.50 – \$ 4.99	746	6.4	\$ 4.45	424	\$ 4.36
\$ 5.00 – \$ 7.99	912	5.1	\$ 6.01	743	\$ 6.00
\$ 8.00 – \$14.99	857	7.9	\$12.69	316	\$12.07
\$15.00 – \$19.99	1,032	8.4	\$17.53	32	\$15.98
\$20.00 – \$33.88	1,108	8.6	\$22.41	118	\$21.65
	4,655			1,633	

Propelis Software, Inc. (formerly RealLegacy.com, Inc.) Stock Options

We have issued options for the purchase of approximately 2.9 million shares of common stock in Propelis Software, Inc., our wholly owned subsidiary including our EAI business, to our directors and the employees and officers of Propelis Software, Inc. The options have an exercise price of $2.00 per share equal to their estimated fair market value on the date of grant, and have individually defined terms and vesting periods.

Employee Stock Purchase Plan

The 1992 Employee Stock Purchase Plan (the Purchase Plan) allows eligible employees an opportunity to purchase an aggregate of 1,100,000 shares of the Company's common stock at a price per share equal to 85% of the lesser of the fair market value of the Company's common stock at the beginning or the end of each six-month purchase period. Under the terms of the Purchase Plan, no participant may acquire more than 5,000 shares of the Company's common stock or more than $5,000 in aggregate fair market value of common stock (as defined) during any six-month purchase period. Common shares sold to employees under the Purchase Plan in fiscal 2000, 1999 and 1998 were 102,920, 86,972 and 153,163, respectively. No shares were sold to employees under the Purchase Plan in the one month transition period ended January 31, 2000.

The fair value of each purchase right granted in fiscal 2000, 1999 and 1998 was $3.72, $6.38 and $1.57, respectively.

Stock Compensation

The Company has elected to continue to account for its plans in accordance with APB No. 25. Accordingly, no compensation cost related to stock option grants or shares sold to employees under the Employee Stock Purchase Plan has been recognized in the Company's financial statements. Had compensation cost for the Company's stock-based compensation plans been recognized consistent with the fair value method of SFAS No. 123, the Company's net income (loss) and net income (loss) per basic and diluted share would have been reduced to the pro forma amounts indicated below:

	Year Ended January 31, 2001	Years Ended December 31, 1999	Years Ended December 31, 1998	Month Ended January 31, 2000
Net income (loss):				
As reported	$11,994	$4,655	$4,729	$(3,625)
Pro forma	$ 5,626	$ (795)	$2,580	$(4,032)
Net income (loss) per share:				
As reported				
Basic	$ .47	$ .20	$ .21	$ (.15)
Diluted	$ .43	$ .18	$ .21	$ (.15)
Pro forma				
Basic	$ .22	$ (.03)	$ .12	$ (.17)
Diluted	$ .20	$ (.03)	$ .11	$ (.17)

In determining the compensation cost of stock option grants and shares sold to employees under the employee stock purchase plan, as specified by SFAS No. 123, the fair value of each award has been estimated on the date of grant using the Black-Scholes option pricing model. The weighted average assumptions used in these calculations are summarized below:

	Year Ended January 31, 2001	Years Ended December 31, 1999	Years Ended December 31, 1998	Month Ended January 31, 2000
Risk free interest rate	5.90%	5.64%	5.26%	6.66%
Expected life	5.33	5.23	8.41	4.22
Expected volatility	85.06%	79.66%	67.50%	80.61%

(7) Net Income (Loss) Per Share

The components of net income (loss) per basic and diluted share are as follows:

	Net Income (loss)	Weighted Average Shares Outstanding	Per Share Amount
Year Ended January 31, 2001			
Basic	$11,994	25,383	$ .47
Dilutive effect of employee stock purchase awards and options	—	2,430	(.04)
Diluted	$11,994	27,813	$ .43
Years Ended December 31,			
1999:			
Basic	$ 4,655	23,137	$ .20
Dilutive effect of employee stock purchase awards and options	—	2,681	(.02)
Diluted	$ 4,655	25,818	$ .18
1998:			
Basic	$ 4,729	22,095	$ .21
Dilutive effect of employee stock purchase awards and options	—	477	—
Diluted	$ 4,729	22,572	$ .21
Month Ended January 31, 2000			
Basic	$(3,625)	23,815	$(.15)
Dilutive effect of employee stock purchase awards and options	—	—	—
Diluted	$(3,625)	23,815	$(.15)

(8) Income Taxes

The components of income from continuing operations before income taxes and income tax expense (benefit) for each of the years in the three-year period ended January 31, 2001 and the one month transition period ended January 31, 2000 consists of the following:

	Year Ended January 31, 2001	Years Ended December 31, 1999	Years Ended December 31, 1998	Month Ended January 31, 2000
Income (loss) from continuing operations before Income taxes:				
U.S.	$19,595	$ 6,356	$4,251	$(3,511)
Foreign	4,481	199	838	(389)
Total	$24,076	$ 6,555	$5,089	$(3,900)
Income tax provision:				
Current:				
U.S.	$ 5,180	$ 3,356	$ 693	$ 52
Foreign	1,348	60	277	—
State	1,027	749	254	11
Total current	7,555	4,165	1,224	63
Deferred:				
U.S.	458	(1,525)	453	(1,133)
State	(66)	(411)	53	(217)
Total deferred	392	(1,936)	506	(1,350)
Total income tax expense (benefit)	$ 7,947	$ 2,229	$1,730	$(1,287)

The reconciliation of the statutory federal tax rate and the effective tax rate for each of the years in the three-year period ended January 31, 2001 and the one-month transition ended January 31, 2000 is as follows:

	Year Ended January 31, 2001	Years Ended December 31, 1999	Years Ended December 31, 1998	Month Ended January 31, 2000
Statutory tax rate	34.0%	34.0%	34.0%	34.0%
Increase (decrease) in taxes resulting from:				
State taxes, net of federal tax benefit	2.6	3.4	4.0	3.3
Foreign sales corporation	(1.9)	(5.3)	(6.3)	—
Meals and entertainment	.4	1.1	1.2	(.1)
Other	(2.1)	.8	1.1	(4.2)
Total	33.0%	34.0%	34.0%	33.0%

The tax effects of temporary differences that give rise to significant portions of the Company's deferred tax assets and (liabilities) as of January 31, 2001 and December 31, 1999 was as follows:

	January 31, 2001	December 31, 1999
Deferred tax assets:		
Inventory	$ 2,725	$1,556
Accrued compensation	1,026	847
Property and equipment	—	869
Reserves for bad debts and sales returns	694	135
Foreign net operating loss carryforwards	410	410
Federal and state tax credits	2,130	1,083
Federal and state net operating loss carryforwards	4,268	118
Abandoned facility	—	512
Other	714	648
Total gross deferred tax assets	11,967	6,178
Valuation allowance	(410)	(410)
Net deferred tax assets	11,557	5,768
Deferred tax liabilities:		
Property and equipment	(343)	—
Other	(385)	(283)
Total gross deferred tax liabilities	(728)	(283)
Net deferred tax assets	$10,829	$5,485

The Company recorded a valuation allowance at January 31, 2001 and December 31, 1999 of $410,000 for the tax benefits associated with certain losses incurred from foreign operations. At January 31, 2001, the Company had net operating loss and credit carryforwards available for federal tax purposes of approximately $10,618,000 and $1,138,000, respectively, which will expire during the years 2001 through 2019.

The Company has assessed its taxable earnings history and prospective future taxable income. Based on this assessment, management has determined that it is more likely than not that its net deferred tax assets will be realized in future periods. The Company may be required to provide a valuation allowance for this asset in the future if it does not generate sufficient taxable income as planned.

(9) Annual Bonus Plan

The Company's Annual Bonus Plan provides a formula for determination of cash bonus payments to eligible employees based on a defined percentage of a participant's qualifying base compensation multiplied by the Company's annual bonus plan factor. The annual bonus plan factor is based on a chart which outlines payout percentages for achievement of defined levels of revenue and operating profit as a percentage of revenue.

The annual bonus expense for fiscal 2000, 1999, and 1998 was $2,035,000, $420,000 and $1,673,000, respectively. There was no bonus for the one month transition period ended January 31, 2000.

(10) 401(k) and Deferred Compensation Plans

The Company has a 401(k) salary savings plan which covers substantially all of its employees. The Company matches 100% of a participant's annual plan contributions up to an annual maximum per participant of $1,500 which vests over a four year period.

The Company has also established an executive deferred compensation plan for selected key employees which allows participants to defer a substantial portion of their compensation each year. The Company matches 20% of a participant's annual plan contributions up to an annual maximum per participant of $10,000. Matching contributions vest over a four year period from the later of July 1, 1997 or the participant's date of hire. In addition, the Company provides participants with an annual earnings credit based on the investment indexes selected by the participant prior to the start of each plan year.

The Company's expense under the 401(k) and deferred compensation plans for fiscal 2000, 1999, 1998 and the one month transition period ended January 31, 2000 was $1,132,000, $470,000, $570,000, and $329,000, respectively.

(11) Segment Information

The Company operates in one reportable segment, which provides high-performance storage networking solutions and services. The Company previously accounted for Propelis Software, Inc. as a reportable segment. The Company no longer provides segment information for this business because it has been accounted for as a discontinued operation.

Information with respect to the Company's foreign operations is summarized as follows:

	Year Ended January 31, 2001	Years Ending December 31, 1999	Years Ending December 31, 1998	Month Ended January 31, 2000
Revenue:				
United States	$123,717	$ 82,494	$ 69,655	$ 3,620
United Kingdom	16,554	13,402	9,596	490
France	5,213	4,348	5,479	86
Other	30,622	25,745	18,291	146
Total	$176,106	$125,989	$103,021	$ 4,342
Long-Lived Assets (end of period):				
United States	$ 29,678	$ 21,464	$ 18,454	$21,497
United Kingdom	856	901	1,049	918
Other	327	265	570	268
Total	$ 30,861	$ 22,630	$ 20,073	$22,683

Revenue has been attributed to the country where the end-user customer is located.

No single customer accounted for more than 10% of the Company's total revenue in fiscal 2000, 1999 or 1998. For the one month transition period ended January 31, 2000, sales of DXE product and service to StorageTek accounted for 22% of total revenue.

(12) Noncash Financing and Investing Activities and Supplemental Cash Flow Information

Cash payments for interest expense in fiscal 2000, 1999, 1998 and the one-month transition period ended January 31, 2000 were $338,000, $222,000, $79,000 and $6,000, respectively.

Cash payments for income taxes, net of refunds received, in fiscal 2000, 1999 and 1998 were $3,286,000, $2,116,000 and $331,000, respectively. There were no cash payments for income taxes or refunds received during the one month transition period ended January 31, 2000.

During fiscal 2000, 1999, 1998 and the one-month transition period ending January 31, 2000, the Company entered into capital lease obligations for equipment valued at $1,849,000, $653,000, $1,441,000 and $307,000, respectively.

During fiscal 2000, deferred tax assets increased by $5,736,000 as a result of the tax benefit from employee stock transactions which could not be currently utilized.

(13) Disclosures about Fair Value of Financial Instruments

The carrying amount for cash and cash equivalents, marketable securities, accounts receivable and long-term obligations approximates fair value because of the short maturity of those instruments.

(14) Subsequent Event (Unaudited)

On April 3, 2001 the Company acquired all of the outstanding stock of Articulent Inc., a privately held, leading provider of Storage Management Services for $12 million in cash, plus assumption of approximately $24 million of liabilities and the acquisition of approximately $19 million of tangible assets. The agreement includes a $10 million incentive payout based upon meeting certain revenue and earnings milestones over the next twelve months.

INDEPENDENT AUDITORS' REPORT

The Board of Directors and Shareholders
Computer Network Technology Corporation:

We have audited the accompanying consolidated balance sheets of Computer Network Technology Corporation and subsidiaries as of January 31, 2001 and December 31, 1999, and the related consolidated statements of operations, shareholders' equity and comprehensive income, and cash flows for the year ended January 31, 2001, each of the years in the two-year period ended December 31, 1999, and the one month transition period ended January 31, 2000. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Computer Network Technology Corporation and subsidiaries as of January 31, 2001 and December 31, 1999, and the results of their operations and their cash flows for the year ended January 31, 2001, each of the years in the two-year period ended December 31, 1999, and the one month transition period ended January 31, 2000, in conformity with accounting principles generally accepted in the United States of America.

/s/ KPMG LLP

Minneapolis, Minnesota
February 20, 2001, except
for note 14, as to which
the date is April 3, 2001

QUARTERLY FINANCIAL DATA
(unaudited)

	Years Ended January 31, 2001 and December 31, 1999			
	First Quarter(3)	Second Quarter	Third Quarter(4)	Fourth Quarter(5)
	(in thousands, except per share data)			
2000(1)(2)				
Revenue	$38,607	$44,341	$46,198	$46,960
Gross profit	20,332	24,091	24,206	24,296
Income from operations	2,887	5,701	6,516	5,820
Loss from discontinued operations, net of tax	(116)	(1,903)	(1,150)	(966)
Net income	1,830	2,053	3,705	4,406
Net income per share:				
Basic	.08	.09	.15	.15
Diluted	.07	.08	.13	.14
1999(2)				
Revenue	$29,245	$30,492	$34,079	$32,173
Gross profit	16,255	17,254	19,321	14,950
Income (loss) from operations	1,999	1,967	3,820	(1,341)
Income (loss) from discontinued operations, net of tax	1,405	532	162	(1,770)
Net income (loss)	2,697	1,786	2,749	(2,577)
Net income (loss) per share:				
Basic	.12	.08	.12	(.11)
Diluted	.11	.07	.11	(.11)

(1) On January 12, 2000, we changed our fiscal year end to January 31, rather than December 31.

(2) Our board of directors has determined to divest Propelis Software, Inc. formerly known as our Enterprise Integration Solutions Division to focus all of our resources on our storage networking products and services. Accordingly, the financial information for Propelis Software, Inc. has been accounted for as discontinued operations.

(3) Discontinued operations in the first quarter of 2000 and 1999 include other nonrecurring income of $1.2 million and $667,000, or $.03 and $.02 per share after tax, due to recognition of payments received in connection with the sale of our vision product line.

(4) Continuing operations for the third quarter of 2000 includes a reversal of the unused balance of a 1999 fourth quarter accrual for an abandoned facility. The amount of the reversal was $287,000.

(5) Continuing operations for the 1999 fourth quarter includes special charges of $1.4 million for the write-off of non-storage networking related products and $1.3 million for an abandoned facility. Discontinued operations includes the reversal of the remaining integration accrual of $430,000 relating to the acquisition of the Internet Solutions Division of Apertus Technologies, Inc.

Item 9. Changes in and Disagreements with Accountants and Financial Disclosure

None.

PART III

Item 10. Directors and Executive Officers

The information set forth under the captions "Election of Directors" and "Section 16(a) Beneficial Ownership Reporting Compliance" in the definitive Proxy Statement for the Annual Meeting of Shareholders to be held on June 28, 2001, to be filed with the Securities and Exchange Commission (the "Commission") on or before May 29, 2001, is incorporated herein by reference. For information concerning the executives officers, see Item 4A of this Annual Report on Form 10K.

Item 11. Executive Compensation

The information set forth under the captions "Summary Compensation Table," "Option Tables," "Employment Agreements," "Election of Directors — Compensation of Directors," "Internal Revenue Code Section 162(m)" and "Comparative Stock Price Performance" in the definitive Proxy Statement for the Annual Meeting of Shareholders to be held on June 28, 2001, to be filed with the Commission on or before May 29, 2001, is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management

The information set forth under the captions "Security Ownership of Certain Beneficial Owners and Management" in the definitive Proxy Statement for the Annual Meeting of Shareholders to be held on June 28, 2001, to be filed with the Commission on or before May 29, 2001, is incorporated herein by reference.

Item 13. Certain Relationships and Related Transactions

None.

PART IV

Item 14. Exhibits, Consolidated Financial Statement Schedules, and Reports on Form 8-K.

(a) 1. Consolidated Financial Statements and Schedules of Registrant

Consolidated Statements of Operations for the Years Ended January 31, 2001, December 31, 1999 and 1998, and the one month transition period ended January 31, 2000.

Consolidated Balance Sheets as of January 31, 2001 and December 31, 1999

Consolidated Statements of Shareholders' Equity and Comprehensive Income for the Years Ended January 31, 2001, December 31, 1999 and 1998, and the one month transition period ended January 31, 2000.

Consolidated Statements of Cash Flows for the Years Ended January 31, 2001, December 31, 1999 and 1998, and the one month transition period ended January 31, 2000.

Notes to Consolidated Financial Statements

Independent Auditors' Report

(a) 2. Consolidated Financial Statement Schedule of Registrant

Independent Auditors' Report on Consolidated Financial Statement Schedule

Schedule II: Valuation and Qualifying Accounts for the Years Ended January 31, 2001, December 31, 1999 and 1998, and the one month transition period ended January 31, 2000.

All other schedules are omitted as the required information is inapplicable or is presented in the consolidated financial statements or related notes thereto.

Schedule II

COMPUTER NETWORK TECHNOLOGY CORPORATION

Valuation and Qualifying Accounts

Years ended January 31, 2001, December 31, 1999 and 1998
and the One Month Transition period ended January 31, 2000
(in thousands)

Description	Balance at Beginning of period	Additions: Charged to costs & expenses	Additions: Charged to other account	Deductions	Balance at end of period
Year ended January 31, 2001					
Allowance for doubtful accounts and sales returns	$1,128	1,600	—	(345)	$2,383
One month period ended January 31, 2000					
Allowance for doubtful accounts and sales returns	$ 959	169	—	—	$1,128
Year ended December 31, 1999					
Allowance for doubtful accounts and sales returns	$1,225	519	—	(785)	$ 959
Year ended December 31, 1998					
Allowance for doubtful accounts and sales returns	$2,979	690	—	(2,444)	$1,225

INDEPENDENT AUDITORS' REPORT ON FINANCIAL STATEMENT SCHEDULE

The Board of Directors and Shareholders
Computer Network Technology Corporation:

Under the date of February 20, 2001, except for note 14, as to which the date is April 3, 2001 we reported on the consolidated balance sheets of Computer Network Technology Corporation and subsidiaries as of January 31, 2001 and December 31, 1999, and the related consolidated statements of operations, shareholders' equity and comprehensive income, and cash flows for the year ended January 31, 2001, each of the years in the two-year period ended December 31, 1999, and the one month transition period ended January 31, 2000 as contained in the fiscal 2000 annual report on Form 10-K. These consolidated financial statements and our report thereon are included in the annual report on Form 10-K fiscal 2000. In connection with our audits of the aforementioned consolidated financial statements, we also have audited the related financial statement schedule as listed in the accompanying index. This financial statement schedule is the responsibility of the Company's management. Our responsibility is to express an opinion on the financial statement schedule based on our audits.

In our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

/s/ KPMG LLP

Minneapolis, Minnesota
February 20, 2001

(a) 3. Exhibits

The Company undertakes to furnish to any shareholder so requesting a copy of any of the following exhibits upon payment to the Company of the reasonable costs incurred by the Company in furnishing any such exhibit.

Exhibit	Description
3A.	Second Restated Articles of Incorporation of the Company. (Incorporated by reference to Exhibits 3(i)-1 and 3(i)-2 to current report on Form 8-K dated May 25, 1999.)
3B.	Articles of Amendment of the Second Restated Articles of the Company. (Incorporated by reference to Exhibit 3(i)-1 to current report on Form 8-K dated May 25, 1999.)
3C.	By-laws of the Company. (Incorporated by reference to Exhibit 3(ii)-1 to current report on Form 8-K dated May 25, 1999.)
4.1	Rights Agreement between the Company and Chase Mellon Shareholder Services, L.L.C., as Rights Agent including the form of Rights Certificate and the Summary of Rights to Purchase Preferred Shares. (Incorporated by reference to Exhibit 1 to Form 8-A dated July 29, 1998 and Exhibit 1 to Form 8-A/A dated November 27, 2000.)
4.2	First Amendment of Rights Agreement dated November 21, 2000. (Incorporated by Reference to Exhibit 1 to Form 8/8 dated November 27, 2000.)
4.3	First Amendment of Certificate of Designations, Preferences and Rights of Series A Junior Participating Preferred Stock. ($.01 Par Value Per Share) of Computer Network Technology Corporation (Incorporated by reference to Exhibit 2 to Form 8-A/A dated November 27, 2000.)
4.4	Form of Common Stock Certificate. (Incorporated by reference to Exhibit 4.2 to Form S-3 Registration Statement No. 333-80841.)
10A.	Amended 1992 Stock Award Plan. (Incorporated by reference to Exhibit 99 Form S-8 Registration Statement No. 333-80791.) (1)
10B.	Amended and Restated 1999 Non-Qualified Stock Award Plan. (2)
10C.	March 10, 1994 Incentive Stock Option Agreements. (Incorporated by reference to Exhibit 28.2 Form S-8 Registration Statement No. 33-83266.) (1)
10D.	March 10, 1994 Non-Qualified Stock Option Agreements. (Incorporated by reference to Exhibit 28.3 Form S-8 Registration Statement No. 33-83266.) (1)
10E.	Building Lease by and between Opus Northwest, L.L.C., and Computer Network Technology Corporation. (Incorporated by reference to Exhibit 10A Form 10Q for the quarterly period ended September 30, 1998.)
10F.	Employment Agreement by and between the Company and Thomas G. Hudson as amended. (Incorporated by reference to Exhibit 10Z Form 10-Q for the quarterly period ended June 30, 1996.) (1)
10G.	Description of CNT Annual Bonus Plan. (2)
10H.	Employment Agreement by and between the Company and Mark Knittel. (Incorporated by reference to Exhibit 10AA Form 10-K for the year ended December 31, 1997.) (1)
10I.	Amendment to CNT Executive Deferred Compensation Plan. (2)
10J.	Employment/Non-Compete Agreement by and between the Company and Nick V. Ganio. (Incorporated by reference to Exhibit 10Q to Form 10-K for the Year Ended December 31, 1998.) (1)
10K.	1997 Restricted Stock Plan. (Incorporated by reference to Exhibit 99 to Form S-8 Registration Statement No. 333-59951.) (1)
10L.	Form of Non-Qualified Stock Option Agreement for Propelis Software, Inc. (formerly RealLegacy.com, Inc.) 2000 Key Employee Stock Award Plan (Incorporated by reference to Form 10-Q for the quarterly period ended April 30, 2000.) (1)

Exhibit	Description
10M.	Form of Non-Qualified Stock Option Agreement for Propelis Software, Inc. (formerly RealLegacy.com, Inc.) 2000 Director and Officer Stock Award Plan (Incorporated by reference to Exhibit 10B to Form 10-Q for the quarterly period ended April 30, 2000.)(1)
10N.	Propelis Software, Inc. (formerly RealLegacy.com, Inc.) 2000 Key Employee Stock Award Plan (Incorporated by reference to Exhibit 10C to Form 10-Q for the quarterly period ended April 30, 2000).(1)
10O.	Propelis Software, Inc. (formerly RealLegacy.com, Inc.) Director And Officer Stock Award Plan (Incorporated by reference to Appendix A to definitive proxy statement dated April 13, 2000.)(1)
10P.	Articulent One-Time Bonus Plan (Incorporated by reference to Exhibit 99.2 to Form 8-K dated April 3, 2001.)(1)
10Q	Amended 1992 Employee Stock Purchase Plan. (Incorporated by reference to Exhibit 99 Form S-8 Registration Statement No. 333-80793.)(1)
10R.	Amendment to Amended 1992 Employee Stock Purchase Plan.(1)(2)
21.	Subsidiaries of the Registrant.(2)
23.	Independent Auditors' Consent.(2)
99A.	Cautionary Statements.(2)
99B.	Calculation of Additional Purchase Price to be Paid in Connection with Acquisition of Articulent, Inc. (Incorporated by reference to Exhibit 99.1 to Form 8-K dated April 3, 2001).

(1) Management contracts or compensatory plans or arrangements with the Company.

(2) Filed herewith.

(b) Reports on Form 8-K

Form 8K regarding change in rights plan during November was filed during the quarterly period ended January 31, 2001.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

COMPUTER NETWORK TECHNOLOGY CORPORATION

Dated: April 25, 2001

By: /s/ THOMAS G. HUDSON

Thomas G. Hudson, President and Chief Executive Officer (Principal Executive Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

/s/ THOMAS G. HUDSON Thomas G. Hudson	President and Chief Executive Officer (Principal Executive Officer) and Director	April 25, 2001
/s/ GREGORY T. BARNUM Gregory T. Barnum	Vice President of Finance, Chief Financial Officer and Secretary (Principal Financial Officer)	April 25, 2001
/s/ JEFFREY A. BERTELSEN Jeffrey A. Bertelsen	Corporate Controller and Treasurer (Principal Accounting Officer)	April 25, 2001
/s/ PATRICK W. GROSS Patrick W. Gross	Director	April 25, 2001
/s/ ERWIN A. KELEN Erwin A. Kelen	Director	April 25, 2001
/s/ LAWRENCE PERLMAN Lawrence Perlman	Director	April 25, 2001
/s/ JOHN A. ROLLWAGEN John A. Rollwagen	Director	April 25, 2001

INDEX TO EXHIBITS

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4.3	First Amendment of Certificate of Designations, Preferences and Rights of Series A Junior Participating Preferred Stock. ($.01 Par Value Per Share) of Computer Network Technology Corporation (Incorporated by reference to Exhibit 2 to Form 8-A/A dated November 27, 2000.)
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10O.	Propelis Software, Inc. (formerly RealLegacy.com, Inc.) Director And Officer Stock Award Plan (Incorporated by reference to Appendix A to definitive proxy statement dated April 13, 2000.) (1)
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23.	Independent Auditors' Consent. (2)
99A	Cautionary Statements. (2)
99B	Calculation of Additional Purchase Price to be Paid in Connection with Acquisition of Aritculent, Inc. (Incorporated by reference to Exhibit 99.1 to Form 8-K dated April 3, 2001).

(1) Management contracts or compensatory plans or arrangements with the Company.

(2) Filed herewith.

Computer Netwo
Subsidiaries of th

Done

Articulent Inc.
- Incorporated under the

Articulent LLC
- Organized under the la

Business Impact Technol
- Incorporated under the
- d/b/a CNT BI-TECH

Business Impact Technol
- Incorporated under the
- d/b/a BI-TECH Swede

CNT International Ltd.
- Incorporated under the
- d/b/a CNT Internationa

CNT France S.A.
- Incorporated under French law
- d/b/a CNT France S.A. and CNTF

Computer Network Technology GmbH
- Incorporated under German law

CNTFS Corporation
- Incorporated under Barbados law

CNT Deutschland GmbH
- Incorporated under German law

Computer Network Technology (Asia Pacific) Pty. Ltd.
- Incorporated under Australian law
- d/b/a CNT A/P

CNT Japan K.K.
- Incorporated under Japanese law

CNT Acquisition I Corporation (formerly known as RealLegacy.com, Inc. and also formerly known as Propelis Software, Inc.)
- Incorporated under Minnesota law

Computer Network Technology do Brasil Ltda.
- Incorporated under Brazillian law

CNT Telecom Services, Inc.
- Incorporated under Minnesota law

Basketball Corporation
- Incorporated under Delaware law

EXHIBIT G

Small and Minority-Owned Telecommunications Business Participation Plan

ANNUAL COMPANY WIDE COMMERCIAL PRODUCTS
SMALL BUSINESS AND SMALL DISADVANTAGED BUSINESS SUBCONTRACTING PLAN

FOR

Computer Network Technology Corporation
6000 Nathan Lane North
Minneapolis, MN 55442

ISSUED TO:

Computer Network Technology Corporation PROCUREMENT & SOURCING
Computer Network Technology Corporation LEGAL DEPARTMENT
Computer Network Technology Corporation OPERATIONS MANAGEMENT
Computer Network Technology Corporation QUALITY MANAGEMENT

PERIOD COVERED: FEBRUARY 1, 2003 TO JANUARY 31, 2004

2003 COMMERCIAL SUBCONTRACTING PLAN FOR
SMALL BUSINESS, AND SMALL DISADVANTAGED BUSINESS CONCERNS

SUBMITTED FOR THE CONSIDERATION OF N/A

BY Computer Network Technology Corporation
Minneapolis, Minnesota

Pursuant to Section 211 of public law 95-507,
Federal Acquisition Regulation Part 19

Computer Network Technology Corporation manufactures and markets commercially a complete line of data communications equipment and other computer related equipment Computer Network Technology Corporation has implemented a Subcontracting Plan, designed to enhance the utilization of Small Businesses, Small Disadvantaged Businesses, and Women Owned Business concerns (hereinafter referred to as S/SDBC/WOB) in subcontracting opportunities

This Company Wide Subcontracting Plan for Commercial Products is an Annual Plan, effective for Computer Network Technology Corporation fiscal year 2003, which shall begin on February 1, 2003 and ends on January 31, 2004

A Percentage Goals for the Utilization as Subcontractors of Small Business Concerns and Small Business Concerns Owned and Controlled by Socially and Economically Disadvantaged Individuals

1 Statement of total dollars contracted.

For fiscal year of 2003, Computer Network Technology Corporation anticipates a total dollar volume of purchases or subcontracts with all suppliers of approximately $85,000,000 Foreign purchases or subcontracts are included in the total dollar amount of $85,000,000 Of the total amount Computer Network Technology Corporation estimates that approximately $64,000,000 of the purchases or subcontracts are regarded as special purchases for which alternative sources other than large business concerns are not available. The remaining purchases or subcontracts of approximately $21,000,000 would be placed with all categories of suppliers including S/SDBC/WOB concerns.

Computer Network Technology Corporation has established in this Subcontracting Plan the following goals for fiscal year 2003

SUBCONTRACT CATEGORY	TYPE OF SUPPLIES	DOLLAR AMOUNT	% OF SUB-CONTRACT TOTAL
a) Large Business	Items 10, 17, 22,24,26,28 below	$64,000,000	75%
b) Small Business	All items but 22 & 24 below	$21, 000,000	25%
c) Small Disadvantaged Business	All Items but 22,24,26 below	$3,400,000	4 0 % *

d) Women-Owned Business	All Items but 22,24,26 below	$3,400,000	4 0 %	*
TOTAL SUBCONTRACTS		$85,000,000	100.0 %	

* The 4 0 percent goals for Small Disadvantaged Businesses and Women-Owned Businesses are included in the total Small Business Subcontract percentage of 25% stated in Item A.1 b above, and represents 32%. percent of the $21, 000,000 of planned subcontracts to small business concerns

2 Description of principal product and service areas presently, and projected for 2003 to be, purchased or subcontracted by Computer Network Technology Corporation are as follows

1 Semiconductors
2 Capacitors
3 Resistors
4 P C. Boards
5 Transformers/inductors
6. Relays
7. Connectors
8 Switches
9 Chemicals
10 Computers
11 Wire
12. Cable
13 Perishable Tools
14 Office Supplies
15 Packing Material
16 Hardware
17 Disk Drives
18 Power Supplies
19 Fabricated Metal Parts & Machined Parts
20. Fans
21 Plastic Injection Molded Parts
22. Contract Manufacturers
23 Fuses
24 Cabinets
25 Consulting Services
26 Subcontracted Labor
27 Telecommunications Services
28 Computer Software

3 Statement of Method used in Developing Goals

Computer Network Technology Corporation has an ongoing program of identifying S/SDBC/WOB concerns as potential sources of supply. This program is summarized within the context of this Plan and described in detail in Computer Network Technology Corporation's Policy No 750-10-02 The formalized program provides the necessary guidance to our procurement personnel Our records are reviewed annually by the President of Computer Network Technology Corporation and are available for review by the Defense Logistics Agency and Defense Contract Management Area Operations (DCMAO) Philadelphia, as well as the Small Business Administration

In developing and achieving the subcontracting goals for S/SDBC/WOB concerns, Computer Network Technology Corporation has compiled a list of those concerns from which Computer Network Technology Corporation presently purchases or subcontracts, and from which Computer Network Technology Corporation will continue to draw for future purchases and subcontracts To develop additional source lists of small business concerns and small disadvantaged business concerns from which Computer Network Technology Corporation can additionally draw for future purchases and subcontracts toward the goals, Computer Network Technology Corporation will obtain and use source identification systems that are reasonable and readily available, including those that may be obtained from the Small Business Administration's Procurement Automated Source System, the National Minority Supplier Development Council's Minority Business Enterprise Network and the Minority Business Development Agency.

Furthermore, efforts are being made through our Purchasing Dept to identify local and state S/SDBC/WOB concerns that can supply products and services that Computer Network Technology Corporation procures

Based upon Computer Network Technology Corporation's past performance in subcontracting with S/SDBC/WOB concerns, and on the Company's current and future commitment to SocioEconomic programs, this plan serves to reaffirm that commitment and provides a system which will afford the maximum, practicable opportunity for S/SDBC/WOB concerns to participate in Computer Network Technology Corporation subcontracts

4 Method for Determining Indirect and Overhead Costs.

Computer Network Technology Corporation has not included indirect and overhead costs as an element in establishing the subcontracting goals for S/SDBC/WOB concerns.

B Plan Administrator

As the Program Manager, Director of Supply Chain Management, Computer Network Technology Corporation, 100 Mount Holly By-Pass, Lumberton, NJ 08048-0440, Phone 609/518-4000, Fax 609 518-4385, will administer Computer Network Technology Corporation's Subcontracting Plan for the utilization of S/SDBC/WOB concerns

In this regard, the duties of the Program Manager shall consist of, but not be limited to, the following

1. Oversee compliance with the content of the Subcontracting Plan,
2. Maintain a program designed to locate qualified or qualifiable S/SDBC/WOB sources for current and future purchases and subcontracting;
3 If needed, provide technical assistance to S/SDBC/WOB concerns in the form of advice and/or documents.
4 Coordinate inquiries and requests for advice from S/SDBC/WOB concerns on purchasing and subcontracting matters,
5 Participate in Government/Industry conferences to assist S/SDBC/WOB concerns,
6 Maintain records and prepare or obtain reports of compliance with this Subcontracting Plan as required by the contracting agency or the Small Business Administration
7 Act as the focal point for studies or surveys as may be required to determine the extent of compliance with this Subcontracting Plan,
8 Make available to the management of Computer Network Technology Corporation information on the status of S/SDBC/WOB programs with relation to goals and objectives established,
9 Assist as Computer Network Technology Corporation determines to be necessary, to brief, train and motivate Computer Network Technology Corporation personnel to ensure support of S/SDBC/WOB concerns and this Subcontracting Plan, and
10 Coordinate the availability of S/SDBC/WOB source lists for buyers and other concerned Computer Network Technology Corporation personnel.

C Description of Efforts to Assure Equitable Subcontracting Opportunity.
Computer Network Technology Corporation typically manufacturers standard commercial, off-the-shelf products purchased by commercial and government

customers S/SDBC/WOB concerns will be given the same opportunity to bid for subcontracts as is given all other concerns S/SDBC/WOB concerns will be afforded the same opportunities, even in those cases in which Computer Network Technology Corporation' subcontracting needs are significantly in excess of the capacity and capability of those concerns However, in such cases, the S/SDBC/WOB concern will be required to perform at acceptable levels of cost, delivery and quality

D Utilization of Small Business Concerns and Small Disadvantaged Business Concerns, Flow Down Requirements, and Second Tier Subcontracting.

Computer Network Technology Corporation will include, where contractually required, the FAR clause 52 219-8, "Utilization of Small Business Concerns and Small Disadvantaged Business Concerns" in all future subcontracts in excess of $10,000 Additionally, where contractually required, except for Small Business Concerns, Computer Network Technology Corporation will include the flow-down requirements of FAR 52 219 9, "Subcontracting Plan for Small Business and Small Disadvantaged Business Concerns," in all subcontracts in excess of $500,000, or in the case of a contract for the construction of any public facility, $1,000,000, and require them to adopt and comply with a plan substantially similar to the plan agreed to by Computer Network Technology Corporation as required by Public Law 95-507

E Assurances of Reports and Cooperation

Computer Network Technology Corporation will submit SF 294 and/or SF 295, as applicable, and cooperate in studies or surveys as may be required by the contracting agency or the Small Business Administration in order to determine the extent of compliance by Computer Network Technology Corporation with this Subcontracting Plan Additionally, Computer Network Technology Corporation will ensure that its subcontractors agree to submit Standard Forms 294 and/or 295, as applicable

F Recitation of Records Maintained and Efforts to Identify and Award Subcontracts

Computer Network Technology Corporation will undertake every reasonable effort to solicit S/SDBC/WOB concerns for subcontracting. As part of that effort, Computer Network Technology Corporation will require each of its Buyers who are responsible for awarding subcontracts, to seek out and identify S/SDBC/WOB concerns Upon learning of such business concerns, each buyer shall be required by Computer Network Technology Corporation to have that information entered into its Supplier database for archival record maintenance. Each buyer shall use that information when soliciting future subcontract business.

Included among the records that will be maintained to demonstrate procedures for compliance with the requirements and goals set forth in the plan are the following

1. Source lists, guides and other data for identifying S/SDBC/WOB concerns are being compiled as described above The Program Manager will maintain these source lists and guides for use by Buyers in the Purchasing Departments and other departments

2 The Program Manager will maintain records of organization contacted for S/SDBC/WOB sources.

3. All subcontract solicitations in excess of $100,000 will be recorded with an indication of whether or not a S/SDBC/WOB concern was solicited Failure of S/SDBC/WOB concerns to receive a subcontract award will be documented as to cause

4 Records of outreach efforts made with trade associations, business development organizations, procurement conferences and trade fairs to further Computer Network Technology Corporation' plan for the utilization of S/SDBC/WOB concerns will be maintained by the Program Manager

5 The Program Manager will record all internal activities in the nature of workshops, seminars, training programs and monitoring activities to evaluate compliance, which are used to guide and encourage buyers in complying with Computer Network Technology Corporation' plan for the utilization of S/SDBC/WOB concerns

6. Company Wide records will also be maintained to support award data for each subcontract to each S/SDBC/WOB concern These records shall be available in Computer Network Technology Corporation database, as outlined in "G" below

G Policies and Procedures

Computer Network Technology Corporation maintains a comprehensive set of policy and procedure manuals, which define, Company standard business practices These manuals describe management responsibility and provide Company guidance and intent relative to the implementation of Government contracting policy Computer Network Technology Corporation Policy Manual 750-10-02 covers company subcontracting policy relative to S/SDBC/WOB

H Management Interest and Involvement

Computer Network Technology Corporation, Corporate, project, line, and administrative managers at all levels, have a strong commitment to the success of our subcontracting efforts with S, SDBC's, and WOB's. Their interest and involvement are demonstrated by active participation in developing and implementing plans for achieving quantitative and qualitative subcontracting goals. The ,Director of Supply Chain Management, a senior Computer Network Technology Corporation manager, is responsible for mobilizing Company resources to meet contractual and corporate commitments with regard to promoting contract opportunities for S/SDBC/WOB concerns. He continuously reviews project performance against corporate subcontracting goals

Computer Network Technology Corporation 6000 Nathan Lane North Minneapolis, MN 55442	COMPANY
SIGNATURE	SIGNATURE
Greg Barnum TYPED NAME	TYPED NAME
Vice President, Finance, PLAN ADMINISTRATOR TITLE	TITLE/POSITION
November 5, 2003 DATE	DATE

Phone: 763 268-6000
Fax 763 268-6810

EXHIBIT H
Incumbent Local Exchange Service Providers

LISTING
Incumbent Local Exchange Service Providers
Certificated In Tennessee
(Facilities-Based)

1) **Ardmore Telephone Company, Inc.**
P O Box 549
517 Ardmore Avenue
Ardmore, TN 38449
(205) 423-2131
(205) 423-2208 (Fax)

2) **BellSouth**
333 Commerce Street
Nashville, TN 37201-3300
(615) 214-3800
(615) 214-8820 (Fax)

3) **Century Telephone of Adamsville**
P O Box 405
116 N Oak Street
Adamsville, TN 38310
(901) 632-3311
(901) 632-0232 (Fax)

4) **Century Telephone of Claiborne**
P O Box 100
507 Main Street
New Tazewell, TN 37825
(423) 626-4242
(423) 626-5224 (Fax)

5) **Century Telephone of Ooltewah-Collegedale, Inc.**
P O Box 782
5616 Main Street
Ooltewah, TN 37363
(423) 238-4102
(423) 238-5699 (Fax)

6) **Citizens Communications Company of Tennessee**
P O Box 770
300 Bland Street
Bluefield, WV 24701

LISTING

INCUMBENT LOCAL EXCHANGE SERVICE PROVIDERS

CERTIFICATED IN TENNESSEE

(FACILITIES-BASED)

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7) **CITIZENS COMMUNICATIONS COMPANY OF THE VOLUNTEER STATE**
P O Box 770
300 Bland Street
Bluefield, WV 24701

8) **LORETTO TELEPHONE COMPANY, INC.**
P O Box 130
Loretto, TN 38469
(931) 853-4351
(931) 853-4329 (Fax)

9) **MILLINGTON TELEPHONE COMPANY, INC.**
P.O. Box 429
4880 Navy Road
Millington, TN 38083-0429
(901) 872-3311
(901) 873-0022 (Fax)

10) **SPRINT-UNITED**
112 Sixth Street
Bristol, TN 37620
(423) 968-8161
(423) 968-3148 (Fax)

11) **TDS TELECOM-CONCORD TELEPHONE EXCHANGE, INC.**
P O Box 22610
701 Concord Road
Knoxville, TN 37933-0610
(423) 966-5828
(423) 966-9000 (Fax)

12) **TDS TELECOM-HUMPHREYS COUNTY TELEPHONE COMPANY**
P O Box 552
203 Long Street
New Johnsonville, TN 37134-0552
(931) 535-2200
(931) 535-3309 (Fax)

13) **TDS TELECOM-TELLICO TELEPHONE COMPANY, INC.**
P O Box 9

102 Spence Street
Tellico Plains, TN 37385-0009
(423) 671-4600
(423) 253-7080 (Fax)

14) **TDS TELECOM-TENNESSEE TELEPHONE COMPANY**
P.O Box 18139
Knoxville, TN 37928-2139
(423) 922-3535
(423) 922-9515 (Fax)

15) **TEC-CROCKETT TELEPHONE COMPANY, INC.**
P O Box 7
Friendship, TN 38034
(901) 677-8181

16) **TEC-PEOPLE'S TELEPHONE COMPANY, INC.**
P.O Box 310
Erin, TN 37061
(931) 289-4221
(931) 289-4220 (Fax)

17) **TEC-WEST TENNESSEE TELEPHONE COMPANY, INC.**
P.O Box 10
244 E Main Street
Bradford, TN 38316
(901) 742-2211
(901) 742-2212 (Fax)

18) **UNITED TELEPHONE COMPANY**
P O Box 38
120 Taylor Street
Chapel Hill, TN 37034
(931) 364-2289
(931) 364-7202 (Fax)

EXHIBIT I
Sworn Pre-filed testimony

BEFORE THE
TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE

APPLICATION OF COMPUTER NETWORK TECHNOLOGY CORPORATION FOR A CERTIFICATE TO PROVIDE COMPETING PRIVATE LINE SPECIAL ACCESS SERVICES

PRE-FILED TESTIMONY OF GREGORY BARNUM

I, Gregory Barnum, do hereby testify as follows in support of the application of Computer Network Technology Corporation (CNT) for a Certificate of convenience and necessity as a competing telecommunications services provider to provide telecommunication services throughout the State of Tennessee

Q Please state your full name, business address, and position
Gregory Barnum, 6000 Nathan Lane, Minneapolis, MN 55442, Corporate Secretary, Vice President of Finance and Chief Financial Officer

Q Please briefly describe your duties
Directly responsible for Accounting, Treasury, Credit and Collections, Contracts, Facilities, Financial Reporting, Investor Relations, Information Technology, Mergers and Acquisitions, Operations Planning, Order Entry, Supply Chain Management, Taxation, and the duties of the Secretary to the Board

Q Please describe your business experience and educational background
Vice President of Finance, CFO and Corporate Secretary of CNTC since July 1997 Previous to that, I have served as either CFO or VP of Finance for various companies since 1980 BA in Accounting from College of St Thomas, St Paul, MN, CPA Minnesota in 1979 CPA Colorado, 1990 For more information, see attached resume

Q Are all statements in CNT's application true and correct to the best of your knowledge, information and belief?
Yes

Q Please describe the current corporate structure of CNT
See attached organizational chart

Q Does CNT possess the requisite managerial, financial, and technical abilities to provide the services for which it has applied for authority?

Yes

Q Please describe CNT's financial qualifications

As of April 20, 2003, CNT had approximately $220 million in cash and cash equivalents without our current assets This cash position, coupled with the ongoing income stream received from customers for whom we provide connectivity, will ensure that our financial capability is sufficient to meet our needs

Q Please describe CNT's managerial and technical qualifications

Please see attached resumes

Q What services will CNT offer?

CNT will be providing End to End Data Storage services via private line special access lines, specifically dedicated point to point and point to multi point data access

Q Will CNT offer service to all consumers within its service area?

No, CNT will primarily be serving Commercial customers

Q Does CNT plan to offer local exchange telecommunications services in areas served by any incumbent local exchange telephone company with fewer than 100,000 total access lines?

Yes

Q Will the granting of a certificate of convenience and necessity to CNT serve the public interest?

Yes

Q Does CNT intend to comply with all TRA rules, statues, and orders pertaining to the provision of telecommunications services in Tennessee, including those for disconnection and reconnection of service?

Yes

Q Has any state ever denied CNT or one of its affiliates authorization to provide intrastate service?

No

Q Has any state ever revoked the certification of CNT or one of its affiliates?

No

Q Has CNT or one of its affiliates ever been investigated or sanctioned by any regulatory authority for service or billing irregularities?

No

Q Who is knowledgeable about CNT's operations and will serve as CNT's regulatory and customer service contact?

Gregory Barnum, 6000 Nathan Lane, Minneapolis MN, 55442 (763)268-6000

Q Please explain in detail CNT's proposed procedures for responding to information requests from the TRA and its staff

All relevant information will be provided upon request to the commission or upon reasonable notice of request, CNT will bear all reasonable costs of travel for the commission to examine information located outside the state of Tennessee

Q Does this conclude your testimony?

Yes

I swear that the foregoing testimony is true and correct to the best of my knowledge

Gregory Barnum
Vice President
Computer Network Technology Corporation

Subscribed and sworn to me this 11TH day of SEPTEMBER, 2003

Notary Public

STEVAN J. EIDE
NOTARY PUBLIC-MINNESOTA
MY COMMISSION EXPIRES 1-31-2005

State of Minnesota

County of WRIGHT

My commission expires 1/31/05

Certificate of Service

I hereby certify that on 11/14/03 I served the foregoing, by first class mail upon the following

Ardmore Telephone Company, Inc
P O Box 549
517 Ardmore Avenue
Ardmore, TN 38449
205 423 2131
205 423 2208 (fax)

Century Telephone of Claiborne
P O Box 100
507 Main Street
New Tazewell, TN 37825
423 626 4242
423 626 5224 (fax)

Citizens Communications
Company of the Volunteer State
P O Box 770
300 Bland Street
Bluefield, WV24701

Sprint-United
112 Sixth Street
Bristol, TN 37620
423 968 8161
423 968 3148 (fax)

BellSouth
333 Commerce Street
Nashville, TN 37201-3300
615 214 3800
615 214 8820 (fax)

Century Telephone of Ooltewah
Collegedale, Inc
P O Box 782
5616 Main Street
Ooltewah, TN 37363
423 238.4102
423 238 5699 (fax)

Loretto Telephone Company, Inc
P O. Box 130
Loretto, TN 38469
931.853 4351
931853 4329 (fax)

TDS Telecom-Concord
Telephone Exchange, Inc
P.O. Box 22610
701 Concord Road
Knoxville, TN 37933-0610
423 966.5828
423 966 9000 (fax)

Century Telephone of Adamsville
P.O Box 405
115 N Oak Street
Adamsville, TN 38310
901 632 3311
901 632 0232 (fax)

Citizen Communication Company of
Tennessee
P O Box 770
300 Bland Street
Bluefield, WV 24701

Millington Telephone Company, Inc
4880 Navy Road
Millington, TN 38053
901.872 3311
901 873 0022 (fax)

TDS Telecom- Humphreys
County Telephone Company
P O Box 552
203 Long Street
New Johnsonville, TN 37134-0552

931 535 2200
931 535.3309 (fax)

TDS Telecom-Tellico Telephone
Company, Inc
P O Box 9
102 Spence Street
Tellico Plains, TN 37385-0009
423 671 4600
423 253 7080 (fax)

TEC-People's Telephone Company, Inc
P O. Box 310
Erin, TN 37061
931 289 4221
931 289 4220 (fax)

TDS Telecom-Tennessee Telephone
Company
P O Box 18139
Knoxville, TN 37928-2139
423.922 3535
423.922.9515 (fax)

TEC-West Tennessee Telephone
Company, Inc
P O. Box 10
244 E Main Street
Bradford, TN 38316
901 742 2211
901 742 2212 (fax)

TEC-Crockett Telephone Company, Inc
P O Box 7
Friendship, TN 38034
901 677 8181

United Telephone Company
P.O Box 38
120 Taylor Street
Chapel Hill, TN 37034
931.364.2289
931 364.7202 (fax)

Paulette Bannack
Signature

PAULETTE BANNACK
Name of Individual

Operations Director
Title Windfall Resources International, LLC