ALTIGEN COMMUNICATIONS INC
Form 10-Q
May 14, 2001

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

FORM 10-Q

[x] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITY EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2001

OR

[_] TRANSITION Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the transition period from ____________ to ____________

Commission File Number 000-27427

ALTIGEN COMMUNICATIONS, INC.
(Exact name of Registrant as specified in its charter)

Delaware	94-3204299
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
47427 Fremont Boulevard Fremont, CA	94538
(address of principal executive offices)	(zip code)

Registrant's telephone number, including area code: (510) 252-9712

Securities registered pursuant to Section 12(b) of the Act: None
Securities registered pursuant to Section 12(g) of the Act: Common Stock
(Title of Class)

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 X NO_____

AS OF MAY 11, 2001, 13,768,532 SHARES OF THE REGISTRANT'S COMMON STOCK WERE OUTSTANDING.

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PART I. FINANCIAL INFORMATION

Item 1. Unaudited Condensed Consolidated Financial Statements.

ALTIGEN COMMUNICATIONS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

	March 31, 2001 (unaudited)
ASSETS	
Current assets:	
Cash and cash equivalents	$ 14,313,624
Short-term investments	8,336,826
Accounts receivable, net of allowances of $300,953 and $423,296, respectively	1,634,646
Inventories, net	5,331,213
Prepaid expenses and other current assets	556,253
Promissory note to officer / stockholder	1,000,000
Total current assets	31,172,562
Property and equipment:	
Leasehold improvement	297,922
Furniture and equipment	1,574,452
Computer software	751,040
	2,623,414
Less: Accumulated depreciation	(1,380,220)
Net property and equipment	1,243,194
Long-term investments	397,826
	$ 32,813,582
LIABILITIES AND STOCKHOLDERS' EQUITY	
Current liabilities:	
Accounts payable	$ 886,735
Accrued liabilities:	
Payroll and related benefits	286,598
Warranty	652,814
Marketing	312,279
Other	653,900
Deferred revenue	524,263
Total current liabilities	3,316,589
Commitments and contingencies (Note 2)	
Stockholders' equity:	
Common stock, $.001 par value; Authorized - 50,000,000 Shares; Outstanding - 13,627,454 shares at March 31, 2001 and 13,507,162 shares at September 30, 2000	13,627
Additional paid-in capital	61,480,099
Deferred stock compensation	(771,052)
Accumulated deficit	(31,225,681)
Total stockholders' equity	29,496,993
	$ 32,813,582

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

ALTIGEN COMMUNICATIONS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

	Three Months Ended March 31,		Six Months
	2001	2000	2001
Revenues, net	$ 2,910,209	$ 3,169,636	$ 5,294,719
Cost of revenues	1,703,228	1,424,787	2,894,975
Gross profit	1,206,981	1,744,849	2,399,744
Operating expenses:			
Research and development	1,208,914	975,808	2,367,002
Sales and marketing	2,515,100	2,634,913	4,546,276
General and administrative	729,363	911,698	1,503,264
Deferred stock compensation (Note 3)	352,564	243,240	522,730
Total operating expenses	4,805,941	4,765,659	8,939,272
Loss from operations	(3,598,960)	(3,020,810)	(6,539,528
Interest and other income, net	382,565	545,994	861,489
Net loss	$(3,216,395)	$(2,474,816)	$(5,678,039
Basic and diluted net loss per share	$ (0.24)	$ (0.18)	$ (0.42
Shares used in computing basic and diluted net loss per share	13,613,785	13,430,353	13,584,501

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

ALTIGEN COMMUNICATIONS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	Six Months E
	2001
CASH FLOWS FROM OPERATING ACTIVITIES:	
Net loss	$ (5,678,039)
Adjustments to reconcile net loss to net cash used in operating activities:	
Depreciation	283,217
Amortization of deferred stock compensation	522,730
Provision for accounts receivable allowance	26,406
Provision for excess and obsolete inventories	670,000
Changes in operating assets and liabilities:	
Accounts receivable	380,343

Inventories	(1,733,061)
Prepaid expenses and other current assets	(198,159)
Accounts payable	(218,560)
Accrued liabilities	(532,609)
Deferred revenue	(85,755)
Net cash used in operating activities	(6,563,487)
CASH FLOWS FROM INVESTING ACTIVITIES:	
Purchases of investments	(15,190,738)
Net proceeds from sale of investments	21,443,841
Purchases of property and equipment	(677,772)
Net cash provided by (used in) investing activities	5,575,331
CASH FLOWS FROM FINANCING ACTIVITIES:	
Proceeds from issuances of common stock	160,400
Issuance costs related to initial public offering of common stock	--
Net cash provided by financing activities	160,400
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(827,756)
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	15,141,380
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 14,313,624

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

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION

AltiGen Communications, Inc. ("AltiGen" or the "Company") designs, manufactures and markets integrated, multifunction telecommunications systems that allow businesses to use data networks, such as the Internet, and the traditional telephone network interchangeably and seamlessly to carry voice and data communications.

The accompanying unaudited condensed consolidated financial statements have been prepared in conformity with generally accepted accounting principles for interim financial information and with the instructions for Form 10-Q and Article 10 of Regulation S-X. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed, or omitted, pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). These unaudited condensed consolidated financial statements reflect the operations of the Company and its wholly-owned subsidiary. All significant intercompany transactions and balances have been eliminated. In our opinion, these unaudited condensed consolidated financial statements include all adjustments necessary (which are of a normal and recurring nature) for a fair presentation of the Company's financial position, results of operations and cash flows for the periods presented.

The condensed consolidated balance sheet as of September 30, 2000 has been derived from the audited consolidated financial statements as of that date.

These financial statements should be read in conjunction with our audited consolidated financial statements for the fiscal year ended September 30, 2000, included in the Company's 2000 Annual Report on Form 10-K. Our results of operations for any interim period are not necessarily indicative of the results of operations for any other interim period or for a full fiscal year.

INVENTORIES

Inventories (which include costs associated with components assembled by third party assembly manufacturers, as well as internal labor and overhead) are stated at the lower of cost (first-in, first-out) or market. Provisions including $670,000 recorded during the six month period ended March 31, 2001, are made to reduce excess and obsolete inventories to their estimated net realizable values. The components of inventories include:

	March 31, 2001	September 30, 2000
Raw materials....................	$ 3,287,435	$ 1,315,988
Work-in-progress.................	366,537	1,414,121
Finished goods...................	1,677,241	1,538,043
	$ 5,331,213	$ 4,268,152

CASH AND CASH EQUIVALENTS AND SHORT-TERM INVESTMENTS

The Company considers all highly liquid investments with an original maturity of three months or less from the date of purchase to be cash equivalents. Short-term investments are in highly liquid financial

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instruments with original maturities greater than three months but less than one year and are classified as "available-for-sale" investments.

As of March 31, 2001, the Company's cash and cash equivalents consisted of commercial paper and cash deposited in checking and money market accounts. For the second quarter of fiscal years 2001 and 2000, the Company did not make any cash payments for interest or income taxes.

REVENUE RECOGNITION

Revenues consist of sales of hardware, software and peripheral components to end users, including dealers, and to distributors. Revenues from sales to end users are recognized upon shipment. The Company provides for estimated sales returns and allowances and warranty costs related to such sales at the time of shipment. Net revenues consist of product revenues reduced by estimated sales returns and allowances. Sales to distributors are made under terms allowing certain rights of return and protection against subsequent price declines on the Company's products held by the distributors. Upon termination, any unsold products may be returned by the distributor for a full refund. These agreements may be canceled by either party based on a specified notice. As a result of the above provisions, the Company defers recognition of revenues and the proportionate costs of revenues derived from sales to distributors until such distributors resell the Company's products to their customers. The amounts deferred as a

result of this policy are reflected as "deferred revenue" in the accompanying unaudited condensed consolidated balance sheets.

Software components are generally not sold separately from the Company's hardware components. Accordingly, the Company allocates revenues between the hardware and software components of its products based on management's best estimate of their relative fair market values. The Company then accounts for the recognition of software revenues in accordance with Statement of Position (SOP) 97-2, "Software Revenue Recognition". Software revenues consist of license revenues that are recognized upon the delivery of application products. The Company provides limited post-contract customer support (PCS), consisting primarily of technical support and "bug" fixes. In accordance with SOP 97-2, revenue earned on software arrangements involving multiple elements is allocated to each element based upon the relative fair values of the elements. Although the Company provides PCS, the revenue allocated to this element is recognized together with the initial licensing fee on delivery of the software because: (1) the PCS fee is included with the initial licensing fee; (2) the PCS included with the initial license fee is for one year or less; (3) the estimated cost of providing PCS during the arrangement is insignificant; and (4) unspecified upgrades/enhancements offered for minimal or no cost related to PCS arrangements historically have been and are expected to continue to be minimal and infrequent. All estimated costs of providing the services, including upgrades/enhancements are accrued for at the time of delivery.

In December 1999, the SEC issued Staff Accounting Bulletin No. 101 ("SAB 101"), "Revenue Recognition in Financial Statements." SAB 101 provides guidance on applying generally accepted accounting principles to revenue recognition in financial statements. Under current SEC guidance, we will be required to adopt SAB 101 in the fourth quarter of our fiscal 2001. Management has evaluated the effect of the adoption of SAB 101 and has determined that the Company's current revenue recognition policies comply with SAB 101.

BASIC AND DILUTED NET LOSS PER SHARE

Basic and diluted net loss per share has been calculated under SFAS No. 128, "Earnings Per Share." SFAS No. 128 requires companies to compute earnings per share under two methods (basic and diluted). Basic net loss per share is calculated by dividing net loss by the weighted-average shares of common stock outstanding during the period. No separate diluted loss per share information has been presented in the accompanying unaudited condensed consolidated statements of operations since potential common shares from the conversion of dilutive stock options are antidilutive. The Company

evaluated the requirements of the SAB No. 98 and concluded that there are no nominal issuances of common stock or potential common stock which would be required to be shown as outstanding for all periods presented herein as outlined in SAB No. 98.

COMPREHENSIVE INCOME

In June 1997, the Financial Accounting Standards Board ("FASB") issued SFAS No. 130, "Reporting Comprehensive Income," which establishes standards for reporting and presentation of comprehensive income. SFAS No. 130, which was adopted by the Company in the first quarter of fiscal year 1998, requires companies to report a new measurement of income. "Comprehensive Income (Loss)" is to include as other comprehensive income, foreign currency translation gains and losses and other unrealized gains and losses that have historically been excluded from net income (loss) and reflected instead in equity. The Company's other comprehensive income is immaterial for all periods presented.

SEGMENT REPORTING

In June 1997, the FASB also issued SFAS No. 131, "Disclosures About Segments of an Enterprise and Related Information." SFAS No. 131 was adopted by the Company beginning on October 1, 1997. This statement establishes standards for disclosures about operating segments, products and services, geographic areas and major customers. The Company is organized and operates as one operating segment. The Company operates primarily in one geographic area, the United States.

Net revenue by geographic region based on customer location for the three month and six month periods ended March 31, 2001 and 2000 were as follows:

	Three Months Ended March 31,		Six Months Ended March 31,	
	2001	2000	2001	2000
Net Revenue				
United States	100%	94%	99%	95%
International	-	6%	1%	5%
	100%	100%	100%	100%

Net revenue by certain customers individually that account for more than 10% of revenue for the three month and six month periods ended March 31, 2001 and 2000 were as follows:

	Three Months Ended March 31,		Six Months Ended March 31,	
	2001	2000	2001	2000
Customer A	38%	14%	33%	--
Customer B	28%	14%	27%	15%
Customer C	22%	16%	20%	16%
Customer D	--	21%	--	25%
Customer E	--	11%	--	--
Others	12%	24%	20%	44%
	100%	100%	100%	100%

Nearly all long-lived assets are located in the United States for all periods presented.

ACCOUNTING FOR DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

In June 1998, the FASB issued SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities,"which requires companies to record derivative financial instruments on the balance sheet as assets or liabilities, measured at fair value. Gains or losses resulting from changes in the values of

those derivatives would be accounted for depending on the use of the derivative and whether it qualifies for hedging accounting. The key criterion for hedge accounting is that the hedging relationship must be highly effective in achieving offsetting changes in fair value or cash flows. In June 1999, the FASB issued SFAS No. 137, "Accounting for Derivative Instruments and Hedging Activities - Deferral of the Effective Date of FASB Statement No. 133," which amend SFAS No. 133 to be effective for all fiscal quarters of all fiscal years beginning after June 15, 2000 (or October 1, 2000 for AltiGen). Management does not believe this statement will have a material impact on the financial position or results of operations as the Company does not currently hold any derivative instruments and does not engage in hedging activities.

Note 2. COMMITMENTS AND CONTINGENCIES

The Company has settled its litigation with Sonoma Systems, Inc. ("SSI"), formerly NetPhone, Inc. ("NetPhone"). On June 30, 1999, the Company had filed a complaint for declaratory judgment against NetPhone seeking a judgement that the Company does not infringe any valid claims of U.S. Patent No. 5,875,234 patent ("the `234 patent"), a patent allegedly owned by NetPhone. NetPhone answered the complaint on July 13, 1999 and asserted a counterclaim, alleging infringement and seeking injunctive relief against what NetPhone refers to as the Quantum Device. On August 11, 1999, the Company received NetPhone's motion for preliminary injunction. On February 11, 2000, the district court issued an order denying NetPhone's motion for preliminary injunction, finding that "AltiGen has raised substantial questions as to whether the `234 patent will survive attacks on its validity at trial." NetPhone was subsequently acquired by Sonoma Systems, Inc. and SSI was added as a party to the lawsuit.

On February 6, 2001, SSI and the Company entered into a Patent Cross-License Agreement pursuant to which the Company and SSI will have the right to use certain intellectual property rights of the other in their respective businesses. The terms of the Cross-License Agreement are confidential. This agreement finally settles all outstanding disputes between the parties, including the lawsuit that was pending in the U.S. District Court for the Northern District of California.

Note 3. DEFERRED STOCK COMPENSATION

The amortization of deferred stock compensation relates to the following items in the accompanying unaudited condensed consolidated statements of operations:

	Three Months Ended March 31,		Six Months En[...] March 31,	
	2001	2000	2001	2
Research and development	$ 151,334	$ 105,806	$ 222,948	$ 2
Sales and marketing	110,162	88,190	164,514	1
General and administrative	91,068	49,244	135,268	
	$ 352,564	$ 243,240	$ 522,730	$ 4

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

FORWARD-LOOKING INFORMATION

Certain statements in this Form 10-Q contain "forward-looking" information (as defined in Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act of 1934, as amended) that involve risks and uncertainties which may cause actual results to differ materially from those predicted in the forward-looking statements. Forward-looking statements can be identified by their use of such verbs as "expects," "anticipates," and "believes" or similar verbs or conjugations of such verbs. If any of our assumptions on which the statements are based prove incorrect or should unanticipated circumstances arise, our actual results could materially differ from those anticipated by such forward-looking statements. The differences could be caused by a number of factors or combination of factors, including, but not limited to, the "Certain Factors Affecting Business, Operating Results and Financial Conditions " described herein and the Risk Factors described in our Securities and Exchange Commission filings, including the Registration Statement on Form S-1, as amended (Registration No. 333-79509), effective October 4, 1999.

OVERVIEW

We are a leading provider of integrated, multi-function telecommunications systems. We were incorporated in May 1994 and began operations in July 1994. From inception through July 1996, we were a development-stage company and had no revenues. During this period, our operating activities consisted primarily of developing our initial product, recruiting personnel, raising capital and building our corporate infrastructure. We first recognized revenues from product sales of our Quantum board and AltiWare software in July 1996. We generated net revenues of $2.9 million and $5.3 million for the second quarter and the first six months of fiscal 2001, respectively, compared to net revenues of $3.2 million and $5.7 million for the second quarter and the first six months of fiscal 2000. As of March 31, 2001, we had an accumulated deficit of $31.2 million.

We derive our revenues from sales of our AltiServ system, which includes Quantum boards, Triton boards and AltiWare software. Software sales were $531,000 and $1.0 million for the second quarter and the first six months of fiscal 2001, respectively, compared to software sales of $304,000 and $587,000 for the second quarter and the first six months of fiscal 2000, respectively. We generally do not sell software separately from our hardware products. We believe software sales will comprise a greater portion of our net revenues in the future. Product revenues consist of sales to end users (including dealers) and to distributors. Revenues from product sales to end users are recognized upon shipment. We defer recognition of sales to distributors until they resell our products to their customers. Under our distribution contracts, a distributor has the right in certain circumstances to return products the distributor determines are overstocked, so long as they provide an offsetting purchase order for products in an amount equal to or greater than the dollar value of the returned products. In addition, we provide distributors protection from subsequent price reductions.

Our cost of revenues consists of component and material costs, direct labor costs, provisions for excess and obsolete inventory, warranty costs and overhead related to manufacturing our products. Software sales typically carry a higher gross margin than hardware sales.

We have experienced operating losses and negative cash flows from operations in each quarterly and annual period since our inception and we currently expect to continue to incur losses for the foreseeable future. We have not recognized any future tax benefits of our cumulative net operating losses due to uncertainty as to future realizability.

Results of Operations

The following table sets forth consolidated statements of operations data for the periods indicated as a percentage of net revenues.

	Three Months Ended March 31,		Six Mon Marc
	2001	2000	2001
	(unaudited)		(unau
Revenues,net............................	100.0%	100.0%	100.0%
Cost of revenues	58.5	45.0	54.7
Gross profit...........................	41.5	55.0	45.3
Operating expenses :			
Research and development	41.5	30.8	44.7
Sales and marketing	86.4	83.0	85.8
General and administrative	25.1	28.8	28.4
Deferred stock compensation.............	12.1	7.7	9.9
Total operating expenses................	165.1	150.3	168.8
Loss from operations	(123.6)	(95.3)	(123.5)
Interest and other income, net	13.1	17.2	16.3
Net loss................................	(110.5)%	(78.1)%	(107.2)%

Revenues, net. Revenues consist of sales to end users (including dealers) and to distributors. Net revenues were $2.9 million and $5.3 million for the second quarter and the first six months of fiscal 2001, a decrease of 8% and 6% from net revenues of $3.2 million and $5.7 million for the same periods of fiscal 2000, respectively. The decrease in revenues was a result of decreased or delayed capital spending by existing and prospective customers and the recent slowdown of the U.S. economy. Sales through our main distributors, AltiSys, Synnex, Ingram Micro, and Tech Data (now terminated) accounted for approximately 28.2%, 38.2%, 21.7%, and 4.0%, respectively, of our revenues for the second quarter of fiscal 2001 compared to 14.5%, 14.2%, 16.1%, and 20.8%, respectively, of our revenues for the same period of fiscal 2000.

Cost of revenues. Cost of revenues were $1.7 million and $2.9 million for the second quarter and the first six months of fiscal 2001, an increase of 20% and 12% from cost of revenues of $1.4 million and $2.6 million for the same periods of fiscal 2000, respectively. Cost of revenues consists primarily of component and material costs, direct labor costs, provisions for excess and obsolete inventory, warranty costs and overhead related to manufacturing our products. Cost of revenues as a percentage of net revenues increased from 45.0% and 45.7% for the second quarter and the first six months of fiscal 2000, respectively, to 58.5% and 54.7% for the same periods of fiscal 2000, respectively. This increase was primarily due to an increase in provision for excess and obsolete inventory as a result of our higher inventory balance as of March 31, 2001 reflecting the slowdown in telecom capital spending and the general downturn in the U.S. economy. Management continues to closely monitor the company's inventory levels. Further declines in demand, although not currently anticipated, would result in

reduced sales, increased operating losses and reductions in inventory valuation.

Gross profit. Gross profit decreased to $1.2 million and $2.4 million for the second quarter and the first six months of fiscal 2001, respectively, from $1.4 million and $3.1 million for the same periods of fiscal 2000, respectively. As a percentage of revenue, gross profit decreased from 55.0% and 54.3% for the

second quarter and the first six months of fiscal 2000, respectively, to 41.5% and 45.3% for the same periods of fiscal 2001, respectively. The decrease in gross profit as a percentage of net revenues was primarily due to an increase in provision for excess and obsolete inventory as well as the decrease in revenues.

Research and development expenses. Research and development expenses increased to $1.2 million and $2.4 million for the second quarter and the first six months of fiscal 2001, respectively, from $976,000 and $1.8 million for the same periods of fiscal 2000, respectively. The increase was primarily due to hiring of additional engineers, and increased resources dedicated to release of new products. Additionally, the Company expanded research and development facilities in China, resulting in increased depreciation and spending on design and development of new products. We currently intend to increase research and development expenses in absolute dollars in the foreseeable future to allow us to develop new products, features, and expand into new markets in Asia Pacific.

Sales and marketing expenses. Sales and marketing expenses remained relatively flat at $2.5 million and $4.5 million for the second quarter and the first six months of fiscal 2001, respectively, from $2.6 million and $4.3 million for the same periods of fiscal 2000, respectively. Sales and marketing expenses consist of compensation, commissions and related cost for personnel engaged in sales and marketing functions, trade show expenses, promotional and marketing programs and related expenses. The reduction in expenditures for the second quarter of fiscal 2001 was the result of management's desire to conserve capital during the current economic downturn. In the near term, sales and marketing expenses are expected to be maintained at the same level as in the previous quarter. Long term, it may be necessary to increase sales and marketing expenses to introduce our new products and continue to pursue new channels and markets and to promote customer and end user awareness of the features and benefits of our products.

General and administrative expenses. General and administrative expenses decreased to $729,000 and $1.5 million for the second quarter and the first six months of fiscal 2001 from $912,000 and $1.6 million for the same period of fiscal 2000, respectively. The decrease was primarily due to reduction in legal fees as a result of the settlement of litigation with Sonoma Systems, Inc. and management's desire to conserve capital during the current economic downturn. In the near term, general and administrative expenses are expected to be maintained at the same level as in the previous quarter. Long term, it may be necessary to increase general and administrative expenses while we continue to build our infrastructure to support the growth of our business.

Deferred stock compensation expense. Deferred stock compensation expense was $353,000 and $523,000 for the second quarter and the first six months of fiscal 2001, respectively, as compared to $243,000 and $486,000 for the same period of fiscal 2000, respectively. Deferred stock compensation expense reflects the amortization of stock compensation charges resulting from granting stock options at exercise prices below the deemed fair value of our common stock on the dates the options were granted. We are amortizing these amounts using the straight-line method over the vesting period of the related stock options. We expect to amortize approximately $279,000 of the remaining balance of this deferred stock compensation in fiscal year 2001, $401,000 in fiscal year 2002, and $91,000 in fiscal year 2003 and doing so will increase our loss (or reduce any profits that

we may have).

Interest and other income, net. Net interest and other income decreased to $383,000 and $861,000 for the second quarter and the first six months of fiscal 2001, respectively, from $546,000 and $1.0 million for the same period of fiscal 2000, respectively. The Company invested the proceeds from our initial public offering in October 1999 in highly liquid, short-term and long-term investments. The decrease was due to decreases in invested principal and interest rates.

Liquidity and Capital Resources

Since inception, we have financed our operations primarily through the sale of equity securities. We

have raised an aggregate of $24.7 million, net of offering expenses, through the sale of preferred stock. On October 8, 1999, AltiGen received cash proceeds, net of underwriters' discounts and commissions, and expenses previously paid of $1.5 million, totaling approximately $33.3 million upon the closing of its initial public offering. As of March 31, 2001, we had cash and cash equivalents of $14.3 million, which consist of cash deposited in checking and money market accounts with original maturities of less than three months and $8.3 million of short-term investments.

Net cash used in our operating activities was $6.6 million and $4.5 million for the six months ended March 31, 2001 and 2000, respectively. Net cash used in operating activities primarily reflected the impact of the net loss for each of the periods, as well as working capital required to fund our growth in operations.

Net cash provided by investing activities was $5.6 million for the six months ended March 31, 2001, which was primarily a result of redemption of short-term investments. Cash used in investing activities for the six months ended March 31, 2000 was $23.4 million, which was primarily a result of purchases of short and long-term investments.

Net cash provided by financing activities was $160,000 for the six months ended March 2001, consisting primarily of proceeds from the exercise of stock options and investments in our employee stock purchase plan. Cash provided by financing activities was $34.7 million for the six months ended March 31, 2000, which was primarily due to $33.3 million in net proceeds from the initial public offering of 3,737,500 shares of common stock on October 9, 1999.

We currently believe that existing cash and cash equivalents balances and short-term investments, will provide us with sufficient funds to finance our operations for at least the next 12 months. Our management intends to invest our cash in excess of current operating requirements in short-term, interest-bearing investment-grade securities. Subsequently, we may need to raise additional funds, and additional financing may not be available on favorable terms, if at all. We may also require additional capital to acquire or invest in complementary businesses or products, or obtain the right to use complementary technologies. If we can not raise funds, if needed, on acceptable terms, we may not be able to develop or enhance our products, take advantage of future opportunities, or respond to competitive pressures or unanticipated requirements, which could seriously harm our business, financial condition, and results of operations. If additional funds are raised through the issuance of equity securities, the net tangible book value per share may decrease, the percentage ownership of then current stockholders may be diluted, and such equity securities may have rights, preferences or privileges senior to those of the holders of our common stock.

CERTAIN FACTORS AFFECTING BUSINESS, OPERATING RESULTS, AND FINANCIAL CONDITION

Risks Related to AltiGen

We have a history of losses and expect to incur future losses, which may prevent us from becoming profitable.

We have experienced operating losses since our inception. As of March 31, 2001, we had an accumulated deficit of $31.2 million. We expect to incur operating losses for the foreseeable future, and these losses may be substantial. Further, we expect our operating cash flows to be negative for the foreseeable future. Because we expect increased expenditures for product development and general and administrative expenses, and substantial increases in sales and marketing expenses, we will need to increase revenues significantly to achieve profitability and positive operating cash flows. Even if we do achieve profitability and positive operating cash flows, we may not be able to sustain or increase profitability or positive operating cash flows on a quarterly or annual basis.

We have a limited operating history, which makes it difficult to evaluate our business and our future prospects.

We shipped our first products in July 1996. As a result of our limited operating history, we have limited financial data that you can use to evaluate our business. You must consider our prospects in light of the risks, expenses and challenges we might encounter because we are at an early stage of development in a new and rapidly evolving market. To address these risks and achieve profitability and increased sales levels, we must:

- establish and increase market acceptance of our technology, products and systems;
- expand our network of distributors, dealers and companies that buy our products in bulk, customize them for particular applications or customers, and resell them under their own names;
- introduce products and systems incorporating our technology and enhancements to our product applications on a timely basis;
- respond effectively to competitive pressures; and
- successfully market and support our products and systems.

We may not successfully meet any of these challenges, and our failure to do so will seriously harm our business and results of operations. In addition, because of our limited operating history, we have limited insight into trends that may emerge and harm our business.

Our operating results vary, making future operating results difficult to predict.

Our quarterly and annual operating results have varied significantly in the past and will likely vary significantly in the future. A number of factors, many of which are beyond our control, may cause our operating results to vary, including:

- our sales cycle, which may vary substantially from customer to customer;

. unfavorable changes in the prices and delivery of the components we purchase;

. the size and timing of orders for our products, which may vary depending on the season, and the contractual terms of those orders;

. the size and timing of our expenses, including operating expenses and expenses of developing new products and product enhancements;

. deferrals of customer orders in anticipation of new products, services or product enhancements introduced by us or by our competitors; and

. our ability to attain and maintain production volumes and quality levels for our products.

Our budgets and commitments that we have made for the future are based in part on our expectations of future sales. If our sales do not meet expectations, it will be difficult for us to reduce our expenses quickly, and consequently our operating results may suffer.

Our dealers often require immediate shipment and installation of our products. As a result, we have historically operated with limited backlog, and our sales and operating results in any quarter depend primarily on orders booked and shipped during that quarter.

Any of the above factors could harm our business, financial condition and results of operations. We believe that period-to-period comparisons of our results of operations are not meaningful, and you should not rely upon them as indicators of our future performance.

Our market is highly competitive, and we may not have the resources to compete adequately.

The market for our integrated, multifunction telecommunications systems is new, rapidly evolving and highly competitive. We expect competition to intensify in the future as existing competitors develop new products and new competitors enter the market. We believe that a critical component to success in this market is the ability to establish and maintain strong partner and customer relationships with a wide variety of domestic and international providers. If we fail to establish or maintain these relationships, we will be at a serious competitive disadvantage.

We face competition from companies providing traditional private telephone systems. Our principal competitors that produce traditional private telephone systems are Lucent Technologies and Nortel Networks. We also compete against providers of multifunction telecommunications systems, including Picasso Communications, Inc. and Artisoft, Inc. We potentially face competition from companies such as Shoreline Teleworks, Inc., NBX Corporation, acquired by 3Com Corporation, Selsius Systems, acquired by Cisco Systems, Inc., as well as any number of future competitors. Many of our competitors are substantially larger than we are and have significantly greater name recognition, financial, sales and marketing, technical, customer support, manufacturing and other resources. These competitors may also have more established distribution channels and stronger relationships with service providers. These competitors may be able to respond more rapidly to new or emerging technologies and changes in customer requirements or devote greater resources to the development, promotion and sale of their products. These competitors may enter our existing or future markets with solutions that may be less expensive, provide higher performance or additional features or be introduced earlier than our solutions. We also expect that other companies may enter our market with better products and technologies.

If any technology that is competing with ours is more reliable, faster, less expensive or has other advantages over our technology, then the demand for our products and services could decrease and harm our business.

We expect our competitors to continue to improve the performance of their current products and introduce new products or new technologies. If our competitors successfully introduce new products or enhance their existing products, this could reduce the sales or market acceptance of our products and services, increase price competition or make our products obsolete. To be competitive, we must

continue to invest significant resources in research and development, sales and marketing and customer support. We may not have sufficient resources to make these investments or to make the technological advances necessary to be competitive, which in turn will cause our business to suffer. A description of our principal competitors and the competitive nature of our market are discussed in greater detail in "Business--Competition."

Losing any of our key distributors would harm our business. We also need to establish and maintain relationships with additional distributors and original equipment manufacturers.

Sales through our four key distributors, Altisys, Synnex, Ingram Micro, and Tech Data accounted for 92.0% of our net revenues in the second quarter of fiscal 2001. Our business and operating results will suffer if either of these distributors does not continue distributing our products, fails to distribute the volume of our products that it currently distributes or fails to expand our customer base. We also need to establish and maintain relationships with additional distributors and original equipment manufacturers. We may not be able to establish, or successfully manage, relationships with additional distribution partners. In addition, our agreements with distributors typically provide for termination by either party upon written notice to the other party. For example, our agreement with Synnex provides for termination, with or without cause, by either party upon 30 days' written notice to the other party, or upon insolvency or bankruptcy. Generally, these agreements are non-exclusive and distributors sell products that compete with ours. If we fail to establish or maintain relationships with distributors and original equipment manufacturers, our ability to increase or maintain our sales and our customer base will be substantially harmed. In the second quarter of fiscal 2001, we cancelled our agreement with Tech Data and Avnet/Hallmark.

We sell our products through dealers and distributors, which limits our ability to control the timing of our sales, and this makes it more difficult to predict our revenues.

We do not recognize revenue from the sale of our products to our distributors until these products are sold to either dealers or end users. We have little control over the timing of product sales to dealers and end users. Our lack of control over the revenue which we recognize from our distributors' sales to dealers and end users limits our ability to predict revenue for any given period. Our budgets and commitments that we have made for the future are based in part on our expectations of future sales. If our sales do not meet expectations, it will be difficult for us to reduce our expenses quickly, and consequently our operating results may suffer.

We rely on sole-sourced components and third-party technology and products; if these components are not available, our business may suffer.

We purchase technology from third parties that is incorporated into our

products, including virtually all of our hardware products. We order sole-sourced components using purchase orders and do not have supply contracts for them. One sole-sourced component, a Mitel Corporation chip, is particularly important to our business because it is included in virtually all of our hardware products. If we were unable to purchase an adequate supply of these sole-sourced components on a timely basis, we would be required to develop alternative solutions. This could entail qualifying an alternative source or redesigning our products based on different components. Our inability to obtain these sole-sourced components, especially the Mitel Corporation chip, could significantly delay shipment of our products, which could have a negative effect on our business, financial condition and results of operations.

We rely on dealers to promote, sell, install and support our products, and their failure to do so may substantially reduce our sales and thus seriously harm our business.

We rely on dealers who can provide high quality sales and support services. As with our distributors, we compete with other telecommunications systems providers for our dealers' business, as our dealers generally market competing products. If a dealer promotes a competitor's products to the detriment of

our products or otherwise fails to market our products and services effectively, we could lose market share. In addition, the loss of a key dealer or the failure of dealers to provide adequate customer service could cause our business to suffer. If we do not properly train our dealers to sell, install and service our products, our business will suffer.

Software or hardware errors may seriously harm our business and damage our reputation, causing loss of customers and revenues.

Users expect telephone systems to provide a high level of reliability. Our products are inherently complex and may have undetected software or hardware errors. We have detected and may continue to detect errors and product defects in our installed base of products, new product releases and product upgrades. For example, a small number of our boards failed and were returned. We have replaced these boards and made certain design changes. We cannot be sure that the problem has been fully addressed and that similar or different problems may not occur in existing or new boards in the future. In addition, end users may install, maintain and use our products improperly or for purposes for which they were not designed. These problems may degrade or terminate the operation of our products, which could cause end users to lose telephone service, cause us to incur significant warranty and repair costs, damage our reputation and cause significant customer relations problems. Any significant delay in the commercial introduction of our products due to errors or defects, any design modifications required to correct these errors or defects or any negative effect on customer satisfaction as a result of errors or defects could seriously harm our business, financial condition and results of operations.

Any claims brought because of problems with our products or services could seriously harm our business, financial condition and results of operations. We currently offer a one-year hardware guarantee to end users. If our products fail within the first year, we face replacement costs. Our insurance policies may not provide sufficient or any coverage should a claim be asserted. In addition, our introduction of products and systems with reliability, quality or compatibility problems could result in reduced revenues, uncollectible accounts receivable, delays in collecting accounts receivable, warranties and additional costs. Our customers, end users or employees could find errors in our products and systems after we have begun to sell them, resulting in product redevelopment costs and loss of, or delay in, their acceptance by the markets in which we compete.

Further, we may experience significant product returns in the future. Any of these events could have a material adverse effect on our business, financial condition and results of operations.

We may face infringement issues that could harm our business by requiring us to license technology on unfavorable terms or temporarily or permanently cease sales of key products.

Generally, litigation, which can be costly and time consuming, may be necessary to determine the scope and validity of others' proprietary rights, or to enforce any patent issued to us, in either case, in judicial or administrative proceedings. For example, we have settled a litigation with Sonoma Systems, Inc. ("SSI"), formerly NetPhone, Inc. On June 30, 1999, the Company had filed a complaint for declaratory judgment against NetPhone seeking a judgement that the Company does not infringe any valid claims of U.S. Patent No. 5,875,234 patent ("the `234 patent"), a patent allegedly owned by NetPhone. NetPhone answered the complaint on July 13, 1999 and asserted a counterclaim, alleging infringement and seeking injunctive relief against what NetPhone refers to as the Quantum Device. On August 11, 1999, the Company received NetPhone's motion for preliminary injunction. On February 11, 2000, the district court issued an order denying NetPhone's motion for preliminary injunction, finding that "AltiGen has raised substantial questions as to whether the `234 patent will survive attacks on its validity at trial." NetPhone was subsequently acquired by Sonoma Systems, Inc. and SSI was added as a party to the lawsuit.

On February 6, 2001, SSI and the Company entered into a Patent Cross-License Agreement pursuant to which the Company and SSI will have the right to use certain intellectual property rights of the other in their respective businesses. The terms of the Cross-License Agreement are confidential. This

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agreement finally settles all outstanding disputes between the parties, including the lawsuit that was pending in the U.S. District Court for the Northern District of California.

More generally, litigation related to these types of claims may require us to acquire licenses under third-party patents which may not be available on acceptable terms, if at all. We believe that an increasing portion of our revenues in the future will come from sales of software applications for our hardware products. The software market has traditionally experienced widespread unauthorized reproduction of products in violation of developers' intellectual property rights. This activity is difficult to detect, and legal proceedings to enforce developers' intellectual property rights are often burdensome and involve a high degree of uncertainty and substantial costs.

Any failure by us to protect our intellectual property could harm our business and competitive position.

Our success depends, to a certain extent, upon our proprietary technology. We currently rely on a combination of patent, trade secret, copyright and trademark law, together with non-disclosure and invention assignment agreements, to establish and protect the proprietary rights in the technology used in our products.

Although we have filed patent applications, we are not certain that our patent applications will result in the issuance of patents, or that any patents issued will provide commercially significant protection to our technology. In addition, others may independently develop substantially equivalent proprietary information not covered by patents to which we own rights, may obtain access to our know-how or may claim to have issued patents that prevent the sale of one or

more of our products. Also, it may be possible for third parties to obtain and use our proprietary information without our authorization. Further, the laws of some countries, such as those in Japan, one of our target markets, may not adequately protect our intellectual property or may be uncertain. Our success also depends on trade secrets that cannot be patented and are difficult to protect. If we fail to protect our proprietary information effectively, or if third parties use our proprietary technology without authorization, our competitive position and business will suffer.

Our products may not meet the legal standards required for their sale in some countries; if we cannot sell our products in these countries, our results of operations may be seriously harmed.

The United States and other countries in which we intend to sell our products have standards for safety and other certifications that must be met for our products to be legally sold in those countries. We have tried to design our products to meet the requirements of the countries in which we sell or plan to sell them. We have also obtained or are trying to obtain the certifications that we believe are required to sell our products in these countries. However, we cannot guarantee that our products meet all of these standards or that we will be able to obtain any certifications required. In addition, there is, and will likely continue to be, an increasing number of laws and regulations pertaining to the products we offer and may offer in the future. These laws or regulations may include, for example, more stringent safety standards, requirements for additional or more burdensome certifications or more stringent consumer protection laws.

If our products do not meet a country's standards or we do not receive the certifications required by a country's laws or regulations, then we may not be able to sell those products in that country. This may seriously harm our results of operation by reducing our sales or requiring us to invest significant resources to conform our products to these standards.

Our market is subject to changing preferences; failure to keep up with these changes would result in our losing market share, thus seriously harming our business, financial condition and results of operations.

Our customers and end users expect frequent product introductions and have changing requirements for new products and features. Therefore, to be competitive, we will need to develop and market new products and product enhancements that respond to these changing requirements on a timely and cost-effective basis. Our failure to do so promptly and cost-effectively would seriously harm our business, financial condition and results of operations. Also, introducing new products could require us to write off existing inventory as obsolete, which could harm our results of operations.

If we do not manage our growth effectively, our business will suffer.

We may not be successful in managing any future growth. We have expanded our operations rapidly since our inception. In order to manage this expansion and to grow in the future, we will need to expand or enhance our management, manufacturing, research and development and sales and marketing capabilities. We may not be able to hire the management, staff or other personnel required to do so.

We may not be able to install adequate control systems in an efficient and timely manner, and our current or planned operational systems, procedures and controls may not be adequate to support our future operations. Difficulties in installing and implementing new systems, procedures and controls may

significantly burden our management and our internal resources. Delays in the implementation of new systems or operational disruptions when we transition to new systems would impair our ability to accurately forecast sales demand, manage our product inventory and record and report financial and management information on a timely and accurate basis.

Lead times for materials and components used in the assembly of our products vary significantly, and depend on factors such as the supplier, contract terms and demand for a component at a given time. If orders do not match forecasts, we may have excess or inadequate inventory of certain materials and components, which may seriously harm our business, financial condition and results of operations.

Our planned expansion in international markets will involve new risks that our previous domestic operations have not prepared us to address; our failure to address these risks could harm our business, financial condition and results of operations.

We intend to expand our international sales and marketing efforts. Our efforts are subject to a variety of risks associated with conducting business internationally, any of which could seriously harm our business, financial condition and results of operations. These risks include:

- tariffs, duties, price controls or other restrictions on foreign currencies or trade barriers, such as import or export licensing imposed by foreign countries, especially on technology;

- potential adverse tax consequences, including restrictions on repatriation of earnings;

- fluctuations in foreign currency exchange rates, which could make our products relatively more expensive in foreign markets; and

- conflicting regulatory requirements in different countries that may require us to invest significant resources customizing our products for each country.

We need additional qualified personnel to maintain and expand our business; our failure to promptly attract and retain qualified personnel may seriously harm our business, financial condition and results of operations.

We depend, in large part, on our ability to attract and retain highly skilled personnel, particularly engineers and sales and marketing personnel. We need highly trained technical personnel to design and support our server-based telecommunications systems. In addition, we need highly trained sales and marketing personnel to expand our marketing and sales operations in order to increase market awareness of our products and generate increased revenues. Competition for highly trained personnel is intense, especially in the San Francisco Bay Area where most of our operations are located. We cannot be certain that we will be successful in our recruitment and retention efforts. If we fail to attract or retain qualified personnel or suffer from delays in hiring required personnel, our business, financial condition and results of operations may be seriously harmed.

Our facility is vulnerable to damage from earthquakes and other natural disasters; any such damage could seriously or completely impair our business.

We perform final assembly, software installation and testing of our products at our facility in Fremont, California. Our facility is located on or near known earthquake fault zones and is vulnerable to damage from fire, floods,

earthquakes, power loss, telecommunications failures and similar events. If such a disaster occurs, our ability to perform final assembly, software installation and testing of our products at our facility would be seriously, if not completely, impaired. If we were unable to obtain an alternative place or way to perform these functions, our business, financial condition and results of operations would suffer. The insurance we maintain may not be adequate to cover our losses against fires, floods, earthquakes and general business interruptions.

Our strategy to outsource assembly and test functions in the future could delay delivery of products, decrease quality or increase costs.

Based on volume or customer requirements, we may begin outsourcing some assembly and test functions. In addition, we may determine that we need to establish assembly and test operations overseas to better serve our international customers. Establishing overseas assembly and test operations may be more difficult or take longer than we anticipate. This outsourcing strategy involves certain risks, including the potential lack of adequate capacity and reduced control over delivery schedules, manufacturing yield, quality and costs. In the event that any significant subcontractor were to become unable or unwilling to continue to manufacture or test our products in the required volumes, we would have to identify and qualify acceptable replacements. Finding replacements could take time, and we cannot be sure that additional sources would be available to us on a timely basis. Any delay or increase in costs in the assembly and testing of products by third-party subcontractors could seriously harm our business, financial condition and results of operations. Our manufacturing and assembly operations are discussed in greater detail in "Business--Manufacturing and Assembly."

Risks Related to the Industry

Integrated, multifunction telecommunications systems may not achieve widespread acceptance, and our fixed costs in the short run could cause our operating results and business to suffer.

The market for integrated, multifunction telecommunications systems is relatively new and rapidly evolving. Businesses have invested substantial resources in the existing telecommunications infrastructure, including traditional private telephone systems, and may be unwilling to replace these systems in the near term or at all. Businesses may also be reluctant to adopt integrated, multifunction telecommunications systems because of their concern about the current limitations of data networks, including the Internet. For example, end users sometimes experience delays in receiving calls and reduced voice quality during calls when routing calls over data networks. Moreover, businesses that

begin to route calls over the same networks that currently carry only their data may also experience these problems if the networks do not have sufficient capacity to carry all of these communications at the same time. We incur many fixed costs in anticipation of a certain level of revenues. If businesses defer purchasing or decide not to purchase integrated, multifunction telecommunications systems and the market for our products does not grow or grows substantially more slowly than we anticipate, our operating results will suffer and our business will be harmed because we will be unable to reduce fixed costs in the short term to offset the reduced revenues.

Future regulation or legislation could harm our business or increase our cost of doing business.

In April 1998, the Federal Communications Commission submitted a report to Congress stating that it may regulate certain Internet services if it determines that such Internet services are functionally equivalent to conventional telecommunications services. The increasing growth of the voice over data network market and the popularity of supporting products and services, however, heighten the risk that national governments will seek to regulate the transmission of voice communications over networks such as the Internet. In addition, large telecommunications companies may devote substantial lobbying efforts to influence the regulation of this market so as to benefit their interests, which may be contrary to our interests. These regulations may include, for example, assessing access or settlement charges, imposing tariffs or imposing regulations based on encryption concerns or the characteristics and quality of products and services. Future laws, legal decisions or regulations, as well as changes in interpretations of existing laws and regulations, could require us to expend significant resources to comply with them. In addition, these future events or changes may create uncertainty in our market that could reduce demand for our products.

Evolving standards may delay our product introductions, increase our product development costs or cause end users to defer or cancel plans to purchase our products, any of which could adversely affect our business.

The standards in our market are still evolving. These standards are designed to ensure that integrated, multifunction telecommunications products from different manufacturers can operate together. Some of these standards are proposed by other participants in our market, including some of our competitors, and include proprietary technology. In recent years, these standards have changed, and new standards have been proposed, in response to developments in our market. Our failure to conform our products to existing or future standards may limit their acceptance by market participants. We may not anticipate which standards will achieve the broadest acceptance in our market in the future, and we may take a significant amount of time and expense to adapt our products to these standards. We may also have to pay additional royalties to developers of proprietary technologies that become standards in our market. These delays and expenses may seriously harm our results of operations. In addition, customers and users may defer or cancel plans to purchase our products due to concerns about the ability of our products to conform to existing standards or to adapt to new or changed standards, and this could seriously harm our results of operations.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Market Risk. Our interest income is sensitive to changes in the general level of U.S. interest rates, particularly since the majority of our investments are in cash equivalents and short-term instruments. Due to the short-term nature of our cash equivalents and investments, we have concluded that there is no material market risk exposure. Therefore, no quantitative tabular disclosures are required.

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PART II

Item1. Legal Proceedings

Generally, litigation, which can be costly and time consuming, may be necessary to determine the scope and validity of others' proprietary rights, or to enforce any patent issued to us, in either case, in judicial or administrative proceedings. For example, we have settled a litigation with Sonoma Systems, Inc. ("SSI"), formerly NetPhone, Inc. On June 30, 1999, the Company had filed a complaint for declaratory judgment against NetPhone seeking a judgement that the Company does not infringe any valid claims of U.S. Patent No. 5,875,234 patent

("the `234 patent"), a patent allegedly owned by NetPhone. NetPhone answered the complaint on July 13, 1999 and asserted a counterclaim, alleging infringement and seeking injunctive relief against what NetPhone refers to as the Quantum Device. On August 11, 1999, the Company received NetPhone's motion for preliminary injunction. On February 11, 2000, the district court issued an order denying NetPhone's motion for preliminary injunction, finding that "AltiGen has raised substantial questions as to whether the `234 patent will survive attacks on its validity at trial." NetPhone was subsequently acquired by Sonoma Systems, Inc. and SSI was added as a party to the lawsuit.

On February 6, 2001, SSI and the Company entered into a Patent Cross-License Agreement pursuant to which the Company and SSI will have the right to use certain intellectual property rights of the other in their respective businesses. The terms of the Cross-License Agreement are confidential. This agreement finally settles all outstanding disputes between the parties, including the lawsuit that was pending in the U.S. District Court for the Northern District of California.

Item 2. Changes in Securities and Use of Proceeds

For the three months ended March 31, 2001, we issued 44,917 shares of common stock pursuant to the exercise of stock options at exercise prices ranging from $0.17 to $0.83. All of the stock options were granted under our 1994 Stock Option Plan prior to our initial public offering. Our issuance of shares of our common stock upon the exercise of these options was exempt from registrant pursuant to rule 701 promulgated under the Securities Act of 1933, as amended.

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

At the Company's annual meeting of stockholders on February 9, the stockholders approved the following items:

1. The election of the following individuals as directors of the Company: Wen-Huang (Simon) Chang and Richard Black.

2. The appointment of Arthur Andersen LLP as the independent public accountants of the Company for the fiscal year ending September 30, 2001.

Item 6. Exhibits and Report on Form 8-K

(a) Exhibits:

None

(b) Report on Form 8-K

None

Item 3. and Item 5. not applicable

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, in the city of Fremont, State of California, on the 14th day of May, 2001.

ALTIGEN COMMUNICATIONS, INC.

Dated: May 14, 2001

By: /s/ Philip M. McDermott

Philip M. McDermott,
Chief Financial Officer
(Principal Financial and Accounting Officer)