

PC TEL INC  
Form 10-Q  
August 08, 2007

**Table of Contents**

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

**Form 10-Q**

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

**For the quarterly period ended June 30, 2007**

**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 000-27115  
PCTEL, Inc.**

*(Exact Name of Business Issuer as Specified in Its Charter)*

**Delaware**  
*(State or Other Jurisdiction of  
Incorporation or Organization)*  
**8725 W. Higgins Road, Suite 400,**  
**Chicago IL**  
*(Address of Principal Executive Office)*

**77-0364943**  
*(I.R.S. Employer  
Identification Number)*  
**60631**  
*(Zip Code)*

**(773) 243-3000**  
*(Registrant's Telephone Number, Including Area Code)*

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act:

Large accelerated filer       Accelerated filer       Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes  No

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date.

<b>Title</b>	<b>Outstanding</b>
Common Stock, par value \$.001 per share	22,496,137 as of August 1, 2007

**PCTEL, Inc.**  
**Form 10-Q**  
**For the Quarterly Period Ended June 30, 2007**  
**TABLE OF CONTENTS**

	<b>Page</b>
<b>PART I</b>	
Item 1	Financial Statements
	<u>Condensed Consolidated Balance Sheets</u> 3
	<u>Condensed Consolidated Statements of Operations</u> 4
	<u>Condensed Consolidated Statements of Cash Flows</u> 5
	<u>Notes to the Condensed Consolidated Financial Statements</u> 6
Item 2	<u>Management's Discussion and Analysis of Financial Condition And Results of Operations</u> 17
Item 3	<u>Quantitative and Qualitative Disclosures about Market Risk</u> 24
Item 4	<u>Controls and Procedures</u> 24
<b>PART II</b>	
Item 1	<u>Legal Proceedings</u> 24
Item 1A	<u>Risk Factors</u> 24
Item 2	<u>Changes in Securities, Use of Proceeds, and Issuer of Purchases of Equity Securities</u> 24
Item 4	<u>Submission of Matters to a Vote of Security Holders</u> 25
Item 6	<u>Exhibits</u> 26
	<u>Signature</u> 26
	<u>Offer Letter</u>
	<u>Section 302 Certification of Principal Executive Officer</u>
	<u>Section 302 Certification of Principal Financial Officer</u>
	<u>Section 906 Certification</u>

**Table of Contents**

**PCTEL, INC.**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
**(UNAUDITED, in thousands except per share amounts)**

	<b>June 30, 2007</b>	<b>December 31, 2006</b>
<b>ASSETS</b>		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 68,644	\$ 59,148
Short-term investments		11,623
Accounts receivable, net of allowance for doubtful accounts of \$275 and \$333, respectively	15,887	14,034
Inventories, net	9,350	7,258
Prepaid expenses and other current assets	1,936	2,059
Total current assets	95,817	94,122
PROPERTY AND EQUIPMENT, net	12,488	12,357
GOODWILL	17,641	17,569
OTHER INTANGIBLE ASSETS, net	5,182	7,451
OTHER ASSETS	1,183	1,221
<b>TOTAL ASSETS</b>	<b>\$ 132,311</b>	<b>\$ 132,720</b>
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
CURRENT LIABILITIES:		
Accounts payable	\$ 4,774	\$ 885
Deferred revenue	1,399	1,025
Other accrued liabilities	6,941	6,964
Short-term debt	770	869
Total current liabilities	13,884	9,743
Other long-term accrued liabilities	2,355	2,284
Total liabilities	\$ 16,239	\$ 12,027
COMMITMENTS and CONTINGENCIES (Note 9)		
STOCKHOLDERS EQUITY:		
Common stock, \$0.001 par value, 100,000,000 shares authorized, 22,500,019 and 22,065,145 shares issued and outstanding at June 30, 2007 and December 31, 2006, respectively	22	22
Additional paid-in capital	166,654	165,556
Accumulated deficit	(50,636)	(46,671)
Accumulated other comprehensive income	32	1,786

Total stockholders' equity	116,072	120,693
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>\$ 132,311</b>	<b>\$ 132,720</b>

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

3

---

Table of Contents

**PCTEL, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
**(UNAUDITED, in thousands except per share amounts)**

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
<b>REVENUES</b>	\$ 18,962	\$ 26,758	\$ 37,913	\$ 45,324
<b>COST OF REVENUES</b>	9,169	9,702	18,368	19,546
<b>GROSS PROFIT</b>	9,793	17,056	19,545	25,778
<b>OPERATING EXPENSES:</b>				
Research and development	4,031	3,336	8,006	6,253
Sales and marketing	3,412	3,196	6,879	6,738
General and administrative	3,373	3,725	7,121	7,473
Amortization of intangible assets	476	1,056	1,172	2,093
Restructuring charges, net	2,074	(1,269)	2,074	(716)
Gain on sale of assets and related royalties	(250)	(250)	(500)	(500)
Total operating expenses	13,116	9,794	24,752	21,341
<b>INCOME (LOSS) FROM OPERATIONS</b>	(3,323)	7,262	(5,207)	4,437
<b>OTHER INCOME, NET</b>	847	747	1,800	1,368
<b>INCOME (LOSS) BEFORE INCOME TAXES</b>	(2,476)	8,009	(3,407)	5,805
<b>PROVISION FOR INCOME TAXES</b>	731	1,683	558	1,676
<b>NET INCOME (LOSS)</b>	\$ (3,207)	\$ 6,326	\$ (3,965)	\$ 4,129
Basic income (loss) per share	\$ (0.15)	\$ 0.30	\$ (0.19)	\$ 0.20
Shares used in computing basic income (loss) per share	21,092	20,837	21,078	20,656
Diluted income (loss) per share	\$ (0.15)	\$ 0.29	\$ (0.19)	\$ 0.19
Shares used in computing diluted income (loss) per share	21,092	21,586	21,078	21,371

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

**Table of Contents**

**PCTEL, INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(UNAUDITED, in thousands except per share amounts)**

	<b>Six Months Ended</b>	
	<b>June 30,</b>	
	<b>2007</b>	<b>2006</b>
<b>Operating Activities:</b>		
Net income (loss)	\$ (3,965)	\$ 4,129
Adjustments to reconcile net loss to net cash used:		
Depreciation and amortization	2,195	3,084
Stock-based compensation	2,535	2,214
Gain on sale of assets and related royalties	(500)	(500)
(Gain) loss on disposal/sale of property and equipment	(32)	66
Restructuring costs	1,807	
Payment of withholding tax on stock-based compensation	(785)	(1,020)
Changes in operating assets and liabilities:		
Accounts receivable, net	(1,852)	(5,592)
Inventories, net	(2,853)	626
Prepaid expenses and other assets	56	743
Accounts payable	3,884	(438)
Income taxes payable	459	425
Other accrued liabilities	(1,518)	(1,320)
Deferred revenue	373	(682)
Net cash (used in) provided by operating activities	(196)	1,735
<b>Investing Activities:</b>		
Capital expenditures	(1,741)	(1,481)
Proceeds from disposal of property and equipment	28	97
Purchase of short-term investments	(19,977)	
Proceeds from maturities of short-term investments	31,600	
Proceeds on sale of assets and related royalties	500	500
Net cash provided by (used in) investing activities	10,410	(884)
<b>Financing Activities:</b>		
Proceeds from issuance of common stock	798	2,330
Payments for repurchase of common stock	(1,448)	
Tax benefit from stock option exercises		1,205
Short-term borrowings, net	(99)	959
Net cash (used in) provided by financing activities	(749)	4,494
Net increase in cash and cash equivalents	9,465	5,345
Effect of exchange rate changes on cash	31	(41)

Cash and cash equivalents, beginning of year	59,148	58,307
<b>Cash and Cash Equivalents, End of Period</b>	<b>\$ 68,644</b>	<b>\$ 63,611</b>

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

5

---



**Table of Contents**

**PCTEL, Inc.**  
**NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**For the Three Months Ended June 30, 2007**  
**(UNAUDITED)**

**1. Basis of Presentation**

The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three months and six months ended June 30, 2007 are not necessarily indicative of the results that may be expected for the year ending December 31, 2007. For further information, refer to the consolidated financial statements and footnotes thereto included in the company's annual report on Form 10-K for the year ended December 31, 2006.

**Basis of Consolidation and Foreign Currency Translation**

The company uses the United States dollar as the functional currency for the financial statements. The company uses the local currency as the functional currency for its subsidiaries in China (Yuan), Ireland (Euro), United Kingdom (Pounds Sterling), Serbia (Euro), Japan (Yen), and Malaysia (Ringgit). Assets and liabilities of these operations are translated to U.S. dollars at the exchange rate in effect at the applicable balance sheet date, and revenues and expenses are translated using average exchange rates prevailing during that period. Translation gains (losses) are recorded in accumulated other comprehensive income as a component of stockholders' equity. All gains and losses resulting from other transactions originally in foreign currencies and then translated into U.S. dollars are included in net income in other income (expense). The company recorded net foreign exchange losses of \$76,000 and \$102,000 for the three months and six months ended June 30, 2007, respectively. The company recorded net foreign exchange gains of \$56,000 and \$27,000 for the three months and six months ended June 30, 2006, respectively.

**Recent Accounting Pronouncements**

In February 2007, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS No. 159) provides the option to report certain financial assets and liabilities at fair value, with the intent to mitigate volatility in financial reporting that can occur when related assets and liabilities are recorded on different bases. This statement is effective for us beginning January 1, 2008. We do not expect SFAS 159 to have a material impact on our consolidated financial statements.

Effective January 2007, the company adopted provisions of FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48). See Note 10 on Income Taxes for discussion of FIN 48.

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 157, *Fair Value Measurements*, which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS No. 157 does not require any new fair value measurements, but provides guidance on how to measure fair value by providing a fair value hierarchy used to classify the source of the information. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. We will adopt SFAS 157 on its effective date. The company is in the process of determining any potential impact that the adoption of SFAS No. 157 will have on our financial statements.

In May 2005, FASB issued SFAS No. 154, *Accounting Changes and Error Corrections*, a replacement of APB Opinion No. 20 and FASB Statement No. 3. This statement applies to all voluntary changes in accounting principle, and requires retrospective application to prior periods' financial statements for changes in accounting principle. SFAS No. 154 will be effective for the company beginning in fiscal year 2007. This statement does not have a material impact on the company's consolidated financial statements.

**2. Cash Equivalents and Short-Term Investments**

At June 30, 2007, cash equivalents were invested in money market funds as well as certificates of deposit and commercial paper with original maturities of less than 90 days. There were no short-term investments at June 30, 2007. At December 31, 2006, cash and cash equivalents were invested in money market funds as well as certificates of deposit, commercial paper, and municipal bonds with original maturities of less than 90 days. At December 31, 2006, short-term investments were invested in commercial paper and municipal bonds with original maturities of greater than 90 days.

**Table of Contents****3. Inventories**

Inventories as of June 30, 2007 and December 31, 2006 were composed of raw materials, sub assemblies, finished goods and work-in-process. Sub assemblies are included within raw materials. As of June 30, 2007 and December 31, 2006, the allowance for inventory losses was \$1.1 million and \$0.9 million, respectively.

Inventories consist of the following (in thousands):

	<b>June 30, 2007</b>	<b>December 31, 2006</b>
Raw materials	\$ 8,347	\$ 6,089
Work in process	440	417
Finished goods	1,615	1,635
Excess & Obsolescence reserves	(1,052)	(883)
Inventories, net	\$ 9,350	\$ 7,258

**4. Earnings per Share**

The following table set forth the computation of basic and diluted earnings per share (in thousands, except per share data):

	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Net earnings (loss)	\$ (3,207)	\$ 6,326	\$ (3,965)	\$ 4,129
Basic loss per share:				
Weighted average common shares outstanding	22,573	22,122	22,559	21,941
Less: Weighted average shares subject to repurchase	(1,481)	(1,285)	(1,481)	(1,285)
Weighted average common shares outstanding	21,092	20,837	21,078	20,656
Basic earnings (loss) per share	\$ (0.15)	\$ 0.30	\$ (0.19)	\$ 0.20
Diluted loss per share:				
Weighted average common shares outstanding	21,092	20,837	21,078	20,656
Weighted average shares subject to repurchase	*	411	*	436
Weighted average common stock option grants	*	338	*	279
Weighted average common shares and common stock Equivalents outstanding	21,092	21,586	21,078	21,371
Diluted earnings (loss) per share	\$ (0.15)	\$ 0.29	\$ (0.19)	\$ 0.19

\* These amounts have been excluded since the effect is anti-dilutive.

Common stock equivalents consist of stock options and restricted shares using the treasury stock method. Common stock options and restricted shares are excluded from the computation of diluted earnings per share if their effect is anti-dilutive. The weighted average common stock option grants excluded from the calculations of diluted net loss per share were 731,000 and 848,000 for the three and six months ended June 30, 2007.

**5. Stock-Based Compensation**

**Table of Contents**

In the first fiscal quarter of 2006, the company adopted SFAS No. 123(R), Share Based Payments, which revises SFAS No. 123, Accounting for Stock Based Compensation. SFAS No. 123(R) requires the company to record compensation expense for share-based payments, including employee stock options, at fair value. Prior to fiscal 2006, the company had accounted for its stock-based compensation awards pursuant to Accounting Principles Opinion (APB) No. 25, Accounting for Stock Issued to Employees, and its related interpretations, which allowed use of the intrinsic value method. Under the intrinsic value method, compensation expense for stock option based employee compensation was not recognized in the income statement as all stock options granted by the company had an exercise price equal to the market value of the underlying common stock on the option grant date.

The company elected to use the modified prospective transition method to adopt SFAS No. 123(R). Under this transition method, compensation expense includes expense for all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS No. 123, and the expense for all share-based payments granted subsequent to January 1, 2006 based on the grant date fair value estimated in accordance with the provisions of SFAS No. 123(R).

In the three months ended June 30, 2007, the company recognized stock-based compensation expense of \$1.1 million in the condensed consolidated statements of operations, which included \$0.9 million of restricted stock amortization and \$0.2 million for stock option expense. In the six months ended June 30, 2007, the company recognized stock-based compensation expense of \$2.5 million, which included \$1.7 million for restricted stock amortization, \$0.5 million for stock option expense \$0.2 million of stock bonuses, and \$0.1 million for stock compensation expense for the ESPP. Total stock compensation expense for the three months ended June 30, 2006 was \$1.1 million, which included \$0.7 million for restricted stock amortization, \$0.3 million for stock option expense, and \$0.1 million for stock bonuses. Total stock compensation expense for the six months ended June 30, 2006 was \$2.2 million, which included \$1.2 million of restricted stock amortization, and \$0.6 million for stock option expense, and \$0.4 million for stock bonuses.

**Stock Options**

The fair value of each unvested option was estimated on the date of grant using the Black-Scholes option valuation model with the following assumptions during the six months ended June 30, 2007 and 2006:

	<b>June 30, 2007</b>	<b>June 30, 2006</b>
Weighted average fair value of options granted	\$3.03	\$2.97
Dividend yield	None	None
Risk-free interest rate	4.8%	4.5%
Expected volatility	45%	50%
Expected life (in years)	2.5	2.2

The company granted 154,650 options for the three months ended June 30, 2007 and 221,910 options in the six months ended June 30, 2007. The company granted 117,149 options in the three months ended June 30, 2006 and 251,739 options in the six months ended June 30, 2006. The company received \$0.1 million in proceeds from the exercise of 11,949 options during the three months ended June 30, 2007, and received \$0.5 million in proceeds from the exercise of 66,057 options during the six months ended June 30, 2007. The company received \$1.7 million in proceeds from the exercise of 215,593 options during the three months ended June 30, 2006, and received proceeds of \$2.1 million from the exercise of 274,191 options during the six months ended June 30, 2006. As of June 30, 2007, the unrecognized compensation expense related to the unvested portion of the company's stock options was approximately \$1.1 million, net of estimated forfeitures to be recognized through 2009 over a weighted average period of 1.3 years. A summary of the company's stock option activity and related information follows for the three months ended June 30, 2007 (in thousands except share amounts):

**Table of Contents**

	<b>Options Outstanding</b>	<b>Weighted Average Exercise Price</b>	<b>Weighted Average Contractual Life (Yrs)</b>	<b>Aggregate Intrinsic Value</b>
<b>Outstanding at December 31, 2006</b>	3,965,627	\$ 9.63		
Granted	221,910	9.71		
Exercised	(66,057)	7.47		
Cancelled	(26,752)	11.10		
Forfeited	(82,037)	9.39		
<b>Outstanding at June 30, 2007</b>	4,012,691	\$ 9.67	6.62	\$1,630
<b>Exercisable at June 30, 2007</b>	3,249,342	\$ 9.76	6.08	\$1,521

The following table summarizes information about stock options outstanding under all Stock Plans at June 30, 2007:

<b>Range of Exercise Prices</b>	<b>Options Outstanding</b>			<b>Options Exercisable</b>	
	<b>Number Outstanding</b>	<b>Weighted Average Remaining Contractual Life</b>	<b>Weighted- Average Exercise Price</b>	<b>Number Exercisable</b>	<b>Weighted Average Exercise Price</b>
\$ 6.00 \$ 7.20	443,213	4.92	\$ 6.88	443,213	\$ 6.88
\$ 7.26 \$ 7.83	423,412	6.14	7.52	358,844	7.52
\$ 7.84 \$ 8.62	441,636	6.25	8.12	358,256	8.04
\$ 8.63 \$ 9.16	485,425	7.44	9.02	254,220	8.93
\$ 9.17 \$ 10.10	416,210	8.69	9.69	97,470	9.80
\$ 10.20 \$ 10.70	623,854	6.46	10.54	603,544	10.54
\$ 10.72 \$ 11.55	432,941	6.73	11.21	387,795	11.24
\$ 11.56 \$ 11.84	705,100	6.56	11.72	705,100	11.72
\$ 12.16 \$ 13.30	33,400	6.14	12.82	33,400	12.82
\$ 59.00 \$ 59.00	7,500	2.59	59.00	7,500	59.00
\$ 6.00 \$ 59.00	4,012,691	6.62	\$ 9.67	3,249,342	\$ 9.76

**Employee Stock Purchase Plan (ESPP)**

Eligible employees are able to purchase common stock at the lower of 85% of the fair market value of the common stock on the first or last day of each offering period under the company's Employee Stock Purchase Plan (ESPP). Each offering period is six months. The company received proceeds of \$0.3 million from the issuance of 39,069 shares under the ESPP in February 2007.

Based on the 15% discount and the fair value of the option feature of this plan, this plan is considered compensatory under SFAS 123(R). Compensation expense is calculated using the fair value of the employees' purchase rights under the Black-Scholes model.

The key assumptions used in the valuation model during the six months ended June 30, 2007 and 2006 are provided below:

	<b>June 30, 2007</b>	<b>June 30, 2006</b>
Dividend yield	None	None
Risk-free interest rate	5.0%	4.3%

Expected volatility	45%	50%
Expected life (in years)	0.5	0.5

The ESPP was amended and restated effective at the company's annual meeting of stockholders on June 5, 2007. The plan was extended by 10 years and the shares reserved for issuance was reduced from 850,000 to 750,000.

**Table of Contents****Restricted Stock**

Restricted stock is amortized ratably over the vesting period of the applicable shares. The company grants restricted awards that generally vest over service periods. Grants to new employees vest over five years. In prior years, the annual grants to employees vested over five years. For the 2007 annual grants, the company issued restricted stock to employees with a four-year vesting period. The company has granted certain executives with performance based restricted stock awards. Each quarter, the company determines compensation expense for these awards based on estimated achievement compared to the targets for each grant.

The company issued 211,722 restricted awards in the three months ended June 30, 2007 and 512,852 restricted stock awards for the six months ended June 30, 2007. The company issued 118,174 restricted stock awards in the three months ended June 30, 2006 and 393,174 restricted stock awards for the six months ended June 30, 2007. For the three months ended June 30, 2007, 2,345 shares vested with a value of \$23,000 and for the six months ended June 30, 2007, 177,765 shares vested with a value of \$1.7 million. During the three months ended June 30, 2006, 2,500 shares vested with a value of \$18,000, and for the six months ended June 30, 2006, 168,860 shares vested with a value of \$1.6 million. Total unrecognized compensation expense related to restricted stock was approximately \$10.4 million, net of forfeitures to be recognized through 2012 over a weighted average period of 2.8 years.

A summary of the company's restricted stock activity and related information follows for the three months ended June 30, 2007:

	<b>Restricted Shares</b>	<b>Weighted Average Grant Date Fair Value</b>
Balance at December 31, 2006	1,164,748	8.56
Restricted stock awards	512,852	10.25
Restricted shares vested	(177,765)	9.46
Restricted shares cancelled	(19,200)	8.68
Balance at June 30, 2007	1,480,635	9.12

**Short Term Incentive Plan**

The bonuses for the company's Short Term Incentive Plan are paid in shares of the company's common stock. The shares earned under the plan are issued in the first quarter following the end of the fiscal year. In February 2007, the company issued 42,923 shares, net of shares withheld for payment of withholding tax, for the 2006 Short Term Incentive Plan. In February 2006, the company issued 140,290 shares, net of shares withheld for payment of withholding tax, for the 2005 Short Term Incentive plan and 14,796 shares, net of shares withheld for payment of withholding tax, for the 2005 CEO Stretch Bonus Plan. The CEO Stretch Bonus Plan was discontinued in 2006.

**Employee Withholding Taxes on Stock Awards**

Effective January 1, 2006, for ease in administering the issuance of stock awards, the company holds back shares of vested restricted stock awards and short-term incentive plan stock awards for the value of the statutory withholding taxes. During the six months ended June 30, 2007 and June 30, 2006, the company paid \$0.8 million and \$1.0 million, respectively, for withholding taxes related to stock awards.

**Stock Repurchases**

On May 16, 2007, the Board of Directors authorized the buyback of an additional 500,000 shares of common stock. The company repurchased 146,084 shares for \$1.5 million during the three months ended June 30, 2007. As of June 30, 2007, the company is authorized to purchase 539,916 additional shares under repurchase programs.

**6. Comprehensive Income**

The following table provides the calculation of other comprehensive income for the three and six months ended June 30, 2007 and June 30, 2006 (in thousands):



**Table of Contents**

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
	<b>(Unaudited)</b>		<b>(Unaudited)</b>	
Net income (loss)	\$ (3,207)	\$ 6,326	\$ (3,965)	\$ 4,129
Other comprehensive income:				
Foreign currency translation adjustments	29	1,372	63	1965
Realized foreign currency translation adjustments	(1,817)		(1,817)	
Comprehensive income (loss)	\$ (4,995)	\$ 7,698	\$ (5,719)	\$ 6,094

The reclassification adjustment of \$1.8 million for the three and six months ended June 30, 2007 represents the realization of foreign exchange translation adjustments due to the substantially complete liquidation of PCTEL Ltd. Ireland.

**7. Restructuring****UMTS Restructuring**

On June 14, 2007, the company announced to its customers and certain affected employees that it was exiting operations related to its UMTS iVET antenna product line, effective immediately. The company closed its research and development facility in Dublin, Ireland as well as a related engineering satellite office in the United Kingdom, and discontinued the UMTS portion of its contract manufacturing, which was located in St. Petersburg, Russia. These actions terminated 12 redundant employee positions in Ireland and three redundant employee positions in the United Kingdom. The facilities and employees affected by the company's closure decision were originally part of the company's acquisition of Sigma Wireless Ltd. in July 2005. In September 2006, the company discontinued the manufacturing of UMTS, PMR, and DPMR lines of the antenna products in Dublin, Ireland as announced in April 2006.

The company recorded \$2.1 million of restructuring costs in its consolidated statements of operations in the three months ended June 30, 2007 related to the exit of its UMTS iVET antenna product line. The major components of the expense are \$1.9 million of gross cash-based restructuring charges plus \$0.2 million of net asset impairments.

The cost categories of the \$1.9 million of cash-based restructuring costs are \$0.3 million of employee severance; \$0.1 million of future lease payments; \$0.1 million of office clean up costs; and up to \$1.4 million in potential contract manufacturing obligations, primarily related to inventory in the supply chain.

The company will be selling off fixed assets, which will offset the restructuring costs and asset impairments described above. No estimate of proceeds can be made at this time.

The company incurred \$0.7 million of non-cash asset impairments in connection with the exiting of the UMTS iVET antenna product line. The categories of asset impairment are: \$0.8 million of inventory; \$0.5 million of fixed assets; \$0.1 million of prepaid assets; \$1.1 million of intangible assets related to purchase accounting of the Sigma Wireless acquisition in 2005; offset by a \$1.8 million realization of comprehensive income related to foreign currency translation of the Irish entity that was substantially liquidated in the three months ended June 30, 2007.

**Dublin, Ireland Restructuring**

On April 7, 2006, the company reached an agreement in principle with the labor union responsible for the company's manufacturing and certain other personnel in its Dublin, Ireland factory to discontinue the manufacture of the iVET, PMR and DPMR lines of the company's antenna products at that location. The agreement was formally signed on April 20, 2006. This agreement enabled the company to wind down its manufacturing operations at the Dublin facility, terminate 65 redundant employee positions, downsize its space under the current lease at this location, and reduce its pension obligations to terminated and remaining employees. Manufacturing of the lines of antenna products was relocated either to a contract manufacturer in St. Petersburg, Russia, or to the company's BTG facility in Bloomingdale, Illinois. The process of winding down manufacturing operations in Dublin and relocating the products to their new manufacturing locations was completed in September 2006 and the general and administrative support

functions were eliminated in December 2006. During the three months ended June 30, 2007, the company made lease payments related to the facility space no longer in use. For three months ended June 30, 2006, the company recorded a restructuring benefit of \$1.3 million, which included a net benefit related to the termination of the pension plan \$2.6 million, offsetting employee severance costs of \$0.9 million and inventory write-offs of \$0.4 million. For six months ended June 30, 2006,

**Table of Contents**

the company recorded a restructuring benefit of \$0.7 million, which included a net benefit related to the termination of the pension plan of \$2.6 million, offsetting employee severance costs of \$1.4 million and inventory write-offs of \$0.4 million.

The following table shows the cash-based restructuring activity during the six months ended June 30, 2007 (in thousands):

	<b>Accrual Balance at December 31, 2006</b>	<b>Restructuring Expense</b>	<b>Cash Payments</b>	<b>Accrual Balance at June 30, 2007</b>
<b>2006 Dublin Restructuring</b>				
Facility lease	52		(52)	
	<b>\$ 52</b>		<b>\$ (52)</b>	<b>\$ 0</b>
<b>2007 UMTS Restructuring</b>				
Purchase commitments		931		931
Employee related		347	(241)	106
Facility & Office		167	(34)	133
	<b>\$ 0</b>	<b>\$ 1,445</b>	<b>\$ (275)</b>	<b>\$ 1,170</b>
<b>Total</b>	<b>\$ 52</b>	<b>\$ 1,445</b>	<b>\$ (327)</b>	<b>\$ 1,170</b>

**8. Short Term Debt**

The short-term borrowings consist of the following (in thousands):

	<b>June 30, 2007</b>	<b>December 31, 2006</b>
Maxrad Tianjin	\$ 102	\$ 100
PCTEL Limited (Ireland)	668	769
<b>Total</b>	<b>\$ 770</b>	<b>\$ 869</b>

The borrowings for Maxrad Tianjin are denominated in Chinese Yuan and the weighted average interest rate on these borrowings was 6.8% during the six months ended June 30, 2007. The borrowings for PCTEL Limited are denominated in Euros and the weighted average interest rate on these borrowings was 5.4% during the six months ended June 30, 2007.

**9. Commitments and Contingencies****Warranties and Sales Returns**

The company's BTG segment allows its major distributors and certain other customers to return unused product under specified terms and conditions. In accordance with FAS 48, the company accrues for product returns at the time of original sale based on historical sales and return trends. The company's allowance for sales returns was \$231,000 and

\$242,000 at June 30, 2007 and December 31, 2006, respectively.

The company offers repair and replacement warranties of on average two years for antennas products and one year for scanner products. The company's warranty reserve for these products based on historical sales and costs of repair and replacement trends. The company reports warranty reserves as a current liability included in accrued liabilities. The warranty reserve was \$133,000 and \$184,000 at June 30, 2007 and December 31, 2006, respectively.

**Legal Proceedings**

**Table of Contents****Ronald H. Fraser v. PC-Tel, Inc., Wells Fargo Shareowner Services, Wells Fargo Bank Minnesota, N.A.**

In March 2002, plaintiff Ronald H. Fraser ( Fraser ) filed a complaint in the California Superior Court for breach of contract and declaratory relief against us and for breach of contract, conversion, negligence and declaratory relief against the company s transfer agent, Wells Fargo Bank Minnesota, N.A. The complaint seeks compensatory damages allegedly suffered by Fraser as a result of the sale of certain stock by Fraser during a secondary offering in April 2000. At a mandatory settlement conference held in September 2004, Fraser stipulated to judgment in favor of the company. In November 2004 Fraser appealed the judgment entered against him. On February 6, 2007, the Court of Appeal for the Sixth Appellate District issued an opinion affirming the trial court s order granting PCTEL s motion for summary judgment. On March 2, 2007, Fraser submitted an appeal of this decision and on March 7, 2007, the Court of Appeal for the Sixth Appellate District denied his appeal. In March 2007, Fraser appealed to the Supreme Court of California. In May 2007, Fraser was denied his appeal.

**10. Income Taxes**

The company recorded income tax expense of \$0.6 million for the six months ended June 30, 2007. This tax expense represents a projected effective rate of -16%. The tax rate for the six months ended June 30, 2007 differs from the statutory tax rate because the company has a valuation allowance on its deferred tax assets. Provision for deferred tax liabilities related to goodwill amortization also impacted the effective rate.

Significant management judgment is required to assess the likelihood that the company s deferred tax assets will be recovered from future taxable income. The company maintains a valuation allowance against deferred tax assets, as a result of uncertainties regarding whether they will be realized.

The company adopted the provisions of FIN 48 on January 1, 2007. FIN 48 prescribes the recognition threshold and measurement attribute for the financial statement recognition and measurement of uncertain tax positions taken or expected to be taken in a tax return. Upon adoption, the company decreased deferred tax assets and the associated valuation allowances by \$0.9 million. There was no net balance sheet impact as a result of adoption of FIN 48.

The company files a consolidated federal income tax return, income tax returns with various states, and foreign income tax returns in various foreign jurisdictions. Our federal and our state income tax years, with limited exceptions, are closed through 2001. The company does not believe that any of its tax positions will significantly change within the next twelve months. Future changes in the unrecognized tax benefit will have no impact on the effective tax rate due to the existence of the valuation allowance.

The company classifies interest and penalties associated with our uncertain tax positions as a component of income tax expense. There were no interest or penalties related to income taxes recorded in the consolidated financial statements.

**11. Industry Segment, Customer and Geographic Information**

The company principally operates in three business segments. They are Broadband Technology Group (BTG), Mobility Solutions Group (MSG), and Licensing. The segment information for the three and six months ended June 30, 2006 has been restated to reflect the company s current segment reporting structure.

PCTEL s chief operating decision maker (CEO) uses only the below measures in deciding how to allocate resources and assess performance among the segments.

The results of operations by segment are as follows (in thousands):

**Table of Contents**

<b>(unaudited)</b>	<b>BTG</b>	<b>MSG</b>	<b>LICENSING</b>	<b>TOTAL</b>
<b>Three months ended June 30, 2007</b>				
Revenue	\$ 16,175	\$ 2,463	\$ 324	\$ 18,962
Gross Profit	\$ 7,056	\$ 2,417	\$ 320	\$ 9,793
Operating Expenses				\$ 13,116
Operating Loss				\$ (3,323)

<b>(unaudited)</b>	<b>BTG</b>	<b>MSG</b>	<b>LICENSING</b>	<b>TOTAL</b>
<b>Three months ended June 30, 2006</b>				
Revenue	\$ 16,708	\$ 2,668	\$ 7,382	\$ 26,758
Gross Profit	\$ 7,024	\$ 2,653	\$ 7,379	\$ 17,056
Operating Expenses				\$ 9,794
Operating Income				\$ 7,262

<b>(unaudited)</b>	<b>BTG</b>	<b>MSG</b>	<b>LICENSING</b>	<b>TOTAL</b>
<b>Six months ended June 30, 2007</b>				
Revenue	\$ 32,516	\$ 4,798	\$ 599	\$ 37,913
Gross Profit	\$ 14,248	\$ 4,705	\$ 592	\$ 19,545
Operating Expenses				\$ 24,752
Operating Loss				\$ (5,207)

<b>(unaudited)</b>	<b>BTG</b>	<b>MSG</b>	<b>LICENSING</b>	<b>TOTAL</b>
<b>Six months ended June 30, 2006</b>				
Revenue	\$ 32,768	\$ 4,784	\$ 7,772	\$ 45,324
Gross Profit	\$ 13,259	\$ 4,755	\$ 7,764	\$ 25,778
Operating Expenses				\$ 21,341
Operating Income				\$ 4,437

The company's revenues to customers outside of the United States, as a percent of total revenues for the three and six months ended June 30, 2007 and June 30, 2006, are as follows:

<b>(unaudited)</b>	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Europe	19%	17%	21%	19%
Asia Pacific	6%	7%	6%	6%
Latin America	4%	2%	4%	2%
North America	3%	2%	2%	3%
	32%	28%	33%	30%

Revenue from the company's major customers representing 10% or more of total revenues for the three and six months ended June 30, 2007 and June 30, 2006 are as follows:

<b>(Unaudited)</b>	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
<b>Customer</b>	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Agere Systems	0%	26%	0%	15%

Agere was a customer in the licensing segment. The company recorded \$7.0 million from licensing settlement from Agere during the three months ended June 2006. There are no customers that represent 10% or greater of the company's revenues in the three or six months ended June 30, 2007.

**Table of Contents****12. Benefit Plans****401(k) Plan**

The 401(k) plan covers all of the domestic employees beginning the first of the month following the month they begin their employment. Under this plan, employees may elect to contribute a portion of their current compensation to the 401(k) plan up to the statutorily prescribed annual limit. The company may make discretionary contributions to the 401(k) plan. The company made \$162,000 and \$156,000 in employer contributions to the 401(k) plan for the three months ended June 30, 2007 and June 30, 2006, respectively. The company made \$342,000 and \$307,000 in employer contributions to the 401(k) plan for the six months ended June 30, 2007 and 2006, respectively.

**Personal Retirement Savings Account**

The Personal Retirement Savings Account (PRSA) covers all current employees of PCTEL Limited in Ireland and the United Kingdom. Under this plan, there is no limit for employee contributions of their current compensation to the PRSA plan. The company may make discretionary contributions to this plan. The company made contributions of approximately \$35,000 and \$6,000 for the six months ended June 30, 2007 and June 30, 2006, respectively.

**Executive Deferred Compensation Plan**

The company provides an Executive Deferred Compensation Plan for executive officers and senior managers. Under this plan, our executives may defer up to 50% of salary and 100% of cash bonuses with a minimum of \$1,500. In addition, the company provides a 4% matching cash contribution which vests over three years subject to the executive's continued service. The executive has a choice of investment alternatives from a menu of mutual funds. The plan is administered by the Compensation Committee and an outside party tracks investments and provides our executives with quarterly statements showing relevant contribution and investment data. Upon termination of employment, death, disability or retirement, the executive will receive the value of his account in accordance with the provisions of the plan. Upon retirement, the executive may request to receive either a lump sum payment, or payments in annual installments over 15 years or over the lifetime of the participant with 20 annual payments guaranteed. As of June 30, 2007, the deferred compensation obligation of \$1.0 million was included in Other Long-Term Accrued Liabilities. The company funds the obligation related to the Executive Deferred Compensation Plan with corporate-owned life insurance policies. The cash surrender value of such policies is included in Other Assets.

**Post-retirement health insurance**

On January 6, 2006, upon authorization of the Board of Directors, the company and Mr. Singer entered into an amended and restated employment agreement which eliminated the post-retirement healthcare benefits for Mr. Singer and his family that were previously included in his original employment agreement. Mr. Singer requested the elimination of these benefits for reasons related to future corporate expense, the company's commitment to defined contribution plans rather than defined benefit plans, and parity of benefits with other executives of the company. The company reversed the liability of \$141,000 in the quarter ended June 30, 2006.

**Pension Plan - Ireland**

As part of the acquisition of Sigma in July 2005, the company assumed the liability for the Sigma employee participants in Sigma Communications Group Retirement and Death Benefit Plan (old plan). This old plan was closed to new employees in December 2003. At July 4, 2005 and December 31, 2005, a third party actuary determined the company's pension assets, accumulated pension obligation, and the projected benefit obligation related to the Sigma participants in the old plan. In the first quarter of 2006, the company set up a new plan - the PCTEL Europe Pension Plan (the Plan) for the 56 employees of Sigma that were participants in the old plan.

As part of the restructuring of the Dublin operation, the company terminated the Plan on June 16, 2006. The company negotiated the terms of the pension termination with the Sigma labor union since the Sigma labor union represents the majority of the people in the Plan. Under the terms of the settlement, the company funded 50% of the cash shortfall in the Plan as calculated by the third party actuary less any severance amounts given to employees that exceeded 3 weeks severance for every year of service. The funding shortfall was based on pension requirements in accordance with Irish regulations. The company incurred approximately \$0.6 million in cash expense to fund the pension shortfall and for related expenses. The result was a non-cash net gain on the termination of the pension plan of \$2.6 million, which was recorded as an offset to restructuring cost.





**Table of Contents**

Prior to the termination of the Plan, the effect on operations of the pension plan for the three and six months ended June 30, 2007 and June 30, 2006, respectively, was as follows (in thousands):

	<b>Pension Benefits Three Months Ended June 30,</b>		<b>Pension Benefits Three Months Ended June 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Service costs		\$ 78		\$ 133
Interest costs		89		150
Expected return on plan assets		(66)		(112)
Net periodic expense		101		171

The company made pension contributions of \$183,000 during the three months ended June 30, 2006.

**Table of Contents****Item 2: Management's Discussion and Analysis of Financial Condition and Results of Operations**

The following information should be read in conjunction with the condensed interim financial statements and the notes thereto included in Item 1 of this Quarterly Report and in conjunction with the financial statements for the year ended December 31, 2006 contained in our Form 10-K filed on March 16, 2007. Except for historical information, the following discussion contains forward looking statements that involve risks and uncertainties, including statements regarding our anticipated revenues, profits, costs and expenses and revenue mix. These forward-looking statements include, among others, those statements including the words, may, will, plans, seeks, expects, anticipates, believes and words of similar import. Such statements constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. You should not place undue reliance on these forward-looking statements. Our actual results could differ materially from those anticipated in these forward-looking statements.

**Introduction**

PCTEL focuses on wireless broadband mobility. We design and develop innovative antennas that extend the reach of broadband and other wireless networks and that simplify the implementation of those networks. We provide highly specialized software-defined radios that facilitate the design and optimization of broadband wireless networks and we develop software that simplifies and secures wireless access to the network. We provide our products, both software and RF products, to wireless and private carriers, wireless infrastructure and handset providers, wireless equipment distributors, VARs and other OEMs. Additionally, we license our intellectual property, principally related to a discontinued modem business, to semiconductor, PC manufacturers, modem suppliers, and others.

We operate in three separate product segments: our Broadband Technology Group (BTG), Mobility Solutions Group (MSG), and Licensing. PCTEL maintains expertise in several technology areas. These include DSP chipset programming, Radio Frequency, software engineering, mobile device operating systems, antenna design and manufacture, mechanical engineering, wireless connectivity, authentication, security, specialized communication devices, advanced algorithm development, and cellular engineering. We report revenue and gross profit for BTG, MSG, and Licensing as separate product segments. In 2006, we reorganized from four segments to three segments. The revenues and gross profit by segment have been restated to reflect our current segment reporting structure. Growth in product revenue is dependent both on gaining further revenue traction in the existing product profile as well as further acquisitions to support the wireless initiatives. Revenue growth for antenna products is correlated to emerging wireless applications in broadband wireless, in-building wireless, wireless Internet service providers, GPS and Mobile SATCOM. The LMR, PMR, DPMR and on-glass mobile antenna applications represent mature markets. Revenue for scanning receivers is tied to the deployment of new wireless technology, such as 2.5G and 3G, and the need for existing wireless networks to be tuned and reconfigured on a regular basis. Revenue growth in the MSG segment is correlated to the success of data services offered by the customer base. The roll out of such data services is in the early stage of market development.

Licensing revenue is dependent on the signing of new license agreements and the success of the licensees in the marketplace. New licenses often contain up front payments pertaining to past royalty liability, or one time payments if the license is perpetual. This can make licensing revenue uneven. During 2006, we were successful in licensing our modem technology to what we believe is the last of the significant users of its modem technology that are not already under license. We anticipate that licensing revenue will decline in 2007 to approximately \$1.0 million or less and will continue to decline significantly in future periods.

**Table of Contents****Results of Operations****Three and Six months Ended June 30, 2007 and 2006***(All amounts in tables, other than percentages, are in thousands)***Revenues**

	<b>BTG</b>	<b>MSG</b>	<b>LICENSING</b>	<b>TOTAL</b>
<b>Three months ended June 30, 2007</b>				
Revenue	\$16,175	\$2,463	\$ 324	\$18,962
% change from year ago period	(3.2%)	(7.7%)	(95.6%)	(29.1%)
<b>Three months ended June 30, 2006</b>				
Revenue	\$16,708	\$2,668	\$ 7,382	\$26,758
% change from year ago period	0.2%	103.5%	2130.2%	46.1%
<b>Six months ended June 30, 2007</b>				
Revenue	\$32,516	\$4,798	\$ 599	\$37,913
% change from year ago period	(0.8%)	0.3%	(92.3%)	(16.4%)
<b>Six months ended June 30, 2006</b>				
Revenue	\$32,768	\$4,784	\$ 7,772	\$45,324
% change from year ago period	9.0%	96.6%	844.3%	36.0%

**BTG** revenues were approximately \$16.2 million for the three months ended June 30, 2007, a decrease of 3% from the prior year period. BTG revenues were approximately \$32.5 million for the six months ended June 30, 2007, a decrease of 1% from the prior year period. Year over year declines in antenna product revenue were offset by growth in scanning receiver sales. The decline in antenna product revenue reflects our decision to exit the UMTS antenna market and the continued elimination of lower margin product lines.

**MSG** revenues decreased approximately 8% to \$2.5 million for the three months ended June 30, 2007, compared to the same period in fiscal 2006. The second quarter of 2006 included a heavy concentration of software customization fees. MSG revenues of approximately \$4.8 million for the six months ended June 30, 2007 were flat compared to the prior year period. The principle products in this segment are our Data Roaming Client software and associated Central Configuration Server as well as our IMS (IP multimedia subsystem) client software. Data client revenues dominate MSG revenues as IMS technology is currently in its pre-commercial deployment trial stage throughout the world.

**Licensing** revenues were approximately \$0.3 million in the three months ended June 30, 2007 compared to \$7.4 million in the three months ended June 30, 2006. Licensing revenues were approximately \$0.6 million in six months ended June 30, 2007 compared to \$7.8 million in the six months ended June 30, 2006. The second quarter of 2006 included a \$7.0 million IP licensing settlement from Agere. With the completion of the modem patent litigation last year, we only have several relatively small licensing agreements that will run to completion in 2007.

**Table of Contents****Gross Profit**

	<b>BTG</b>	<b>MSG</b>	<b>LICENSING</b>	<b>TOTAL</b>
<b>Three Months Ended June 30, 2007</b>				
Gross profit	\$ 7,056	\$2,417	\$ 320	\$ 9,793
Percentage of revenue	43.6%	98.1%	98.8%	51.6%
% of revenue change from year ago period	1.6%	-1.3%	-1.2%	-12.1%
<b>Three Months Ended June 30, 2006</b>				
Gross profit	\$ 7,024	\$2,653	\$ 7,379	\$17,056
Percentage of revenue	42.0%	99.4%	100.0%	63.7%
% of revenue change from year ago period	-0.6%	2.3%	0.6%	16.2%
<b>Six Months Ended June 30, 2007</b>				
Gross profit	\$14,248	\$4,705	\$ 592	\$19,545
Percentage of revenue	43.8%	98.1%	98.8%	51.6%
% of revenue change from year ago period	3.4%	-1.3%	-1.1%	-5.3%
<b>Six Months Ended June 30, 2006</b>				
Gross profit	\$13,259	\$4,755	\$ 7,764	\$25,778
Percentage of revenue	40.5%	99.4%	99.9%	56.9%
% of revenue change from year ago period	-2.7%	2.6%	0.7%	8.4%

Our product segments vary significantly in gross profit percent. The decrease in overall gross profit as a percentage of revenues for the three and six months ended June 30, 2007 compared to the prior year periods is due to the one time \$7.0 million license settlement from Agere in the second quarter of 2006. Excluding this one-time settlement, gross profit as a percentage of sales increased approximately 1 percentage point for the three months ended June 30, 2007 and increased approximately 3 percentage points for the six months ended June 30, 2007, compared to the same periods in fiscal 2006. Excluding the Agere settlement, the increase in gross profit is due to a higher mix of MSG products and scanning receivers, as well margin improvements within the antenna product line.

**BTG** margin was approximately 43.6% in the three months ended June 30, 2007, 1.6 percentage points better than the comparable period in fiscal 2006. BTG margin was approximately 43.8% in the six months ended June 30, 2007, 3.4 percentage points better than the comparable period in fiscal 2006. The margin improvement in the three and six months ended June 30, 2007 reflects growth in our higher margin scanning receiver products and the elimination of lower margin antenna products from the portfolio. Margin improvements also include the positive impact of the outsourcing of the products manufactured in Dublin, Ireland to lower manufacturing sources in 2006. We expect long-term gross profit in this segment to be in the mid 40% range.

**MSG** margin was approximately 98.1% for the three and six months ended June 30, 2007. The cost of goods sold in the segment relates primarily to third party licenses included in the Roaming Client product. Compared to 2006, gross profit as a percentage of revenue was 1.3 percentage points lower than the three and six months ended June 30, 2006. We expect long-term gross profit in this segment to be in the upper 90% range.

**Licensing** margin was approximately 98.8% for the three and six months ended June 30, 2007. Compared to 2006, gross profit as a percentage of revenue was 1.2 percentage points worse than the three months ended June 30, 2006 and 1.1 percentage points worse than the six months ended June 30, 2006.

**Research and Development**

	<b>Three Months Ended June 30, 2007</b>	<b>Three Months Ended June 30, 2006</b>	<b>Six Months Ended June 30, 2007</b>	<b>Six Months Ended June 30, 2006</b>
Research and development	\$ 4,031	\$ 3,336	\$ 8,006	\$ 6,253

Edgar Filing: PC TEL INC - Form 10-Q

Percentage of revenues	21.3%	12.5%	21.1%	13.8%
% change from year ago period	20.8%	37.1%	28%	27.5%

---

19

**Table of Contents**

Research and development expenses include costs for software and hardware development, prototyping, certification and pre-production costs. All costs incurred prior to establishing the technological feasibility of computer software products to be sold are research and development costs and expensed as incurred in accordance with FAS 86. No significant costs have been incurred subsequent to determining the technological feasibility.

Research and development expenses increased approximately \$0.7 million for the three months ended June 30, 2007 compared to the comparable period in 2006 and \$1.8 million for the six months ended June 30, 2007 compared to the comparable period in 2006. The increase is due to incremental investments in headcount and expenses across all products.

**Sales and Marketing**

	<b>Three Months Ended June 30, 2007</b>	<b>Three Months Ended June 30, 2006</b>	<b>Six Months Ended June 30, 2007</b>	<b>Six Months Ended June 30, 2006</b>
Sales and marketing	\$ 3,412	\$ 3,196	\$ 6,879	\$ 6,738
Percentage of revenues	18.0%	11.9%	18.1%	14.9%
% change from year ago period	6.8%	8.9%	2.1%	11.4%

Sales and marketing expenses include costs associated with the sales and marketing employees, sales representatives, product line management, and trade show expenses.

Sales and marketing expenses increased approximately \$0.2 million for the three months ended June 30, 2007 compared to the same period in fiscal 2006 and approximately \$0.1 million for the six months ended June 30, 2007 compared to the same period in fiscal 2006 reflecting additional investments in distribution.

**General and Administrative**

	<b>Three Months Ended June 30, 2007</b>	<b>Three Months Ended June 30, 2006</b>	<b>Six Months Ended June 30, 2007</b>	<b>Six Months Ended June 30, 2006</b>
General and administrative	\$ 3,373	\$ 3,725	\$ 7,121	\$ 7,473
Percentage of revenues	17.8%	13.9%	18.8%	16.5%
% change from year ago period	(9.4%)	(3.6%)	(4.7%)	-6.9%

General and administrative expenses include costs associated with the general management, finance, human resources, information technology, legal, insurance, public company costs, and other operating expenses to the extent not otherwise allocated to other functions.

General and administrative expenses were approximately \$0.4 million lower for the three and six months ended June 30, 2007 compared to the same periods in fiscal 2006 as higher stock-based compensation expense offset reduction of costs associated with the Dublin facility. In the three months ended March 31, 2006, we also reversed a liability of \$141,000 for CEO retirement benefits.

**Amortization of Intangible Assets**

	<b>Three Months Ended June 30, 2007</b>	<b>Three Months Ended June 30, 2006</b>	<b>Six Months Ended June 30, 2007</b>	<b>Six Months Ended June 30, 2006</b>
Amortization of intangible assets	\$ 476	\$ 1,056	\$ 1,172	\$ 2,093
Percentage of revenues	2.5%	3.9%	3.1%	4.6%

Amortization expense declined \$0.6 million in the three months ended June 30, 2007 compared to the same period in fiscal 2006, and declined \$0.9 million in the six months ended June 30, 2007 compared to the same period in fiscal 2006. Of the \$0.6 million decrease in amortization for the three months ended June 30, 2007, \$0.3 million is due to lower amortization for the intangible assets that were impaired during the three months ended September 30, 2006 and \$0.3 million is because the intangible assets related to the DTI acquisition were fully amortized as of March 2007. Of the \$0.9 million decrease in amortization expense in the six months ended June 30, 2007, \$0.6 million is due to lower

amortization for the intangible assets that were impaired in September 2006, and \$0.3 million is due to lower amortization for the



**Table of Contents**

reevaluated the carrying value of the technology and customer relationships intangible assets and goodwill from the Sigma acquisition, as required by Statement of Financial Accounting Standards No. 121 Accounting for the Impairment of Long Lived Assets and for Long Lived Assets to be Disposed Of and Statement of Accounting Standards No. 142 Goodwill and Intangible Assets. The company concluded that the carrying value of intangible assets was impaired by \$6.0 million and the carrying value of the goodwill was impaired by \$14.3 million.

**Restructuring charges (benefit)**

	<b>Three Months Ended June 30, 2007</b>	<b>Three Months Ended June 30, 2006</b>	<b>Six Months Ended June 30, 2007</b>	<b>Six Months Ended June 30, 2006</b>
Restructuring charges (benefit)	\$ 2,074	\$ (1,269)	\$ 2,074	\$ (716)
Percentage of revenues	10.9%	(4.7%)	5.5%	(1.6%)

On June 14, 2007 we announced that we are exiting operations related to our UMTS iVET antenna product line. The restructuring expense of \$2.1 million for the three and six months ended June 30, 2007 represents the costs associated closing our research and development facility in Dublin, Ireland as well as a related engineering satellite office in the United Kingdom, and discontinuing the UMTS portion of our contract manufacturing, which was located in St. Petersburg, Russia. These actions terminated twelve redundant employee positions in Ireland and three redundant employee positions in the United Kingdom. The facilities and employees affected by our closure decision were originally part of our acquisition of Sigma Wireless Ltd. in July 2005. The major components of the restructuring expense are \$1.9 million of gross cash-based restructuring charges plus \$0.2 million of net asset impairments. Net impairments include a \$1.8 million benefit related to recognition of other comprehensive income related to foreign translation adjustments. We realized the benefit due to the substantially complete liquidation of PCTEL Ltd. Ireland. The company believes that our restructuring activities will positively impact operating costs in a range of \$0.3 to \$0.4 million per quarter, starting in the third quarter 2007.

The benefit recorded in 2006 relates to the restructuring for the discontinuation of manufacturing in Dublin, Ireland. On April 7, 2006, we reached an agreement in principle with the labor union responsible for our manufacturing and certain other personnel in our Dublin, Ireland factory to discontinue the manufacture of the iVET, PMR and DPMR lines of our antenna products at that location. The agreement was formally signed on April 20, 2006. This agreement enabled us to wind down our manufacturing operations at the Dublin facility, terminate 65 redundant employee positions, downsize our space under the current lease at this location, and reduce our pension obligations to terminated and remaining employees. The process of winding down manufacturing operations in Dublin and relocating the products to their new manufacturing locations was completed in September 2006 and the general and administrative support functions were eliminated in December 2006. For the three months ended June 30, 2006 we recorded a restructuring benefit of \$1.3 million, which included a net benefit related to the termination of the pension plan of \$2.6 million offsetting employee severance costs of \$0.9 million and inventory write-offs of \$0.4 million. For the six months ended June 30, 2006, we recorded a restructuring benefit of \$0.7 million, which included the net benefit related to the termination of the pension plan of \$2.6 million, offsetting employee severance of \$1.4 million and inventory write-offs of \$0.4 million.

**Gain on sale of assets and related royalties**

	<b>Three Months Ended June 30, 2007</b>	<b>Three Months Ended June 30, 2006</b>	<b>Six Months Ended June 30, 2007</b>	<b>Six Months Ended June 30, 2006</b>
Gain on sale of assets and related royalties	\$ (250)	\$ (250)	\$ (500)	\$ (500)
Percentage of revenues	1.3%	0.9%	1.3%	1.1%

All royalty amounts represent royalties from Conexant. The royalty agreement with Conexant runs through June 30, 2009.

**Other Income, Net**

	<b>Three Months Ended June 30, 2007</b>	<b>Three Months Ended June 30, 2006</b>	<b>Six Months Ended June 30, 2007</b>	<b>Six Months Ended June 30, 2006</b>
Other income, net	\$ 847	\$ 747	\$ 1,800	\$ 1,368
Percentage of revenues	4.5%	2.8%	4.7%	3.0%

21

---

**Table of Contents**

Other income, net, consists primarily of interest income, and also interest expense and foreign exchange gains and losses. Interest income increased for the three and six months ended June 30, 2007 compared to the same periods in fiscal 2006 due primarily to higher interest rates, higher yielding cash investments, and higher average cash balances. Starting in the quarter ended June 30, 2006, we invested in commercial paper, certificates of deposit, and municipal bonds in addition to money market funds. We expect to continue to invest our cash in money market funds, commercial paper, and certificates of deposit.

**Provision for Income Taxes**

	<b>Three Months Ended June 30, 2007</b>	<b>Three Months Ended June 30, 2006</b>	<b>Six Months Ended June 30, 2007</b>	<b>Six Months Ended June 30, 2006</b>
Provision for income taxes	\$ 731	\$ 1,683	\$ 558	\$ 1,676
Effective tax rate	(29.5%)	21.0%	(16.4%)	28.9%

The tax rate for the three months ended June 30, 2007 differs from the statutory rate of 35% because we provide a valuation allowance on our deferred tax assets, and also due to provisions for deferred tax liabilities related to goodwill amortization that is deductible for tax purposes.

The tax rate for the three months ended June 30, 2006 differs from the statutory rate of 35% because of the valuation allowance on our deferred tax assets, the provision for deferred tax liabilities related to goodwill that is deductible for tax purposes, and the utilization of NOL carryforwards.

We regularly evaluate our estimates and judgments related to uncertain tax positions and, when necessary, establish contingency reserves to account for our uncertain tax positions. As we obtain more information via the settlement of tax audits and through other pertinent information, these projections and estimates are reassessed and may be adjusted accordingly. These adjustments may result in significant income tax provisions or provision reversals.

**Stock-based compensation expense**

In the three months ended June 30, 2007, we recognized stock-based compensation expense of \$1.1 million in the condensed consolidated statements of operations, which included \$0.9 million of restricted stock amortization and \$0.2 million for stock option expense. In the six months ended June 30, 2007, we recognized stock-based compensation expense of \$2.5 million, which included \$1.7 million for restricted stock amortization, \$0.5 million for stock option expense \$0.2 million of stock bonuses, and \$0.1 million for stock compensation expense for the ESPP. Total stock compensation expense for the three months ended June 31, 2006 was \$1.1 million, which included \$0.7 million for restricted stock amortization, \$0.3 million for stock option expense, and \$0.1 million for stock bonuses. Total stock compensation expense for the six months ended June 30, 2006 was \$2.2 million, which included \$1.2 million of restricted stock amortization, and \$0.6 million for stock option expense, and \$0.4 million for stock bonuses.

The following table summarizes the stock-based compensation expense by income statement line item:

	<b>Three Months Ended June 30, 2007</b>	<b>Three Months Ended June 30, 2006</b>	<b>Six Months Ended June 30, 2007</b>	<b>Six Months Ended June 30, 2006</b>
Cost of sales	\$ 88	\$ 86	\$ 187	\$ 163
Research and development	153	161	387	306
Sales and marketing	183	215	363	439
General and administrative	714	603	1,598	1,306
Total operating expense	1,050	979	2,348	2,051
Total	\$ 1,138	\$ 1,065	\$ 2,535	\$ 2,214



**Table of Contents****Liquidity and Capital Resources**

	<b>Six Months Ended June 30, 2007</b>	<b>Six Months Ended June 30, 2006</b>
Net income (loss)	\$ (3,207)	\$ 4,129
Charges for depreciation, amortization, stock-based compensation, and other non-cash items	5,168	3,844
Changes in operating assets and liabilities	(1,399)	(6,238)
Net cash provided by (used in) operating activities	\$ (196)	\$ 1,735
Net cash provided by (used in) investing activities	10,410	(884)
Net cash provided by (used in) financing activities	(749)	4,494
Cash and cash equivalents at the end of period	68,644	63,611
Short-term borrowings at end of period	770	959

Our cash and short-term investments, net of short-term borrowings were approximately \$67.9 million and \$62.7 million as of June 30, 2007 and June 30, 2006, respectively. Our working capital was \$81.9 million and \$76.7 million as of June 30, 2007 and 2006, respectively. The increase in cash and working capital at June 30, 2007 compared to June 30, 2006 is due to cash from operations, including the \$7.0 million license settlement received in July 2006.

We consumed \$0.2 million of net cash from operating activities during the six months ended June 30, 2007 substantially due to unfavorable changes in operating assets and liabilities of \$1.4 million. The primary change was an increase in inventories of \$2.9 million for the six months ended June 30, 2007. During the six months ended June 30, 2006, cash from operating activities provided \$1.7 million as net income changes in operating assets and liabilities was \$0.8 million excluding the \$7.0 million receivable related to the Agere settlement.

We received proceeds of \$11.6 million related to the maturity of short-term investments and used \$1.7 million for capital expenditures during the six months ended June 30, 2007. For the six months ended June 30, 2006, we had capital expenditures of \$1.5 million offset by \$0.5 million in proceeds from the sale of assets and related royalties. We used \$0.7 million from financing activities during the six months ended June 30, 2007 as we repurchased common stock for \$1.4 million, but received \$0.8 million in proceeds from the sale of common stock related to stock option exercises and shares purchased through the ESPP. During the six months ended June 30, 2006, we received proceeds of \$2.3 million related to stock option exercises and shares purchased through the ESPP, and also received proceeds from net borrowings of \$1.0 million. We borrowed funds in Ireland for the Dublin operations in June 2006.

We believe that the existing sources of liquidity, consisting of cash, short-term investments and cash from operations, will be sufficient to meet the working capital needs for the foreseeable future. We continue to evaluate opportunities for development of new products and potential acquisitions of technologies or businesses that could complement the business. We may use available cash or other sources of funding for such purposes.

**Contractual Obligations and Commercial Commitments**

As of June 30, 2007, we had operating lease obligations of approximately \$4.7 million through 2013. As of June 30, 2007, we had purchase obligations of \$5.9 million for the purchase of inventory, as well as for other goods and services, in the ordinary course of business, and exclude the balances for purchases currently recognized as liabilities on the balance sheet.

In June 2007, we closed our research and development facility in Dublin, Ireland as well as a related engineering satellite office in the United Kingdom (UK), and discontinued the UMTS portion of our contract manufacturing, which was located in St. Petersburg Russia. We negotiated a termination of the UK lease and our Ireland lease terminates effective December 31, 2007.

As part of the UMTS restructuring announced in June 2007, we had obligations of \$1.2 million at June 30, 2007, consisting of purchase commitments, employee related costs, and facility costs.



**Table of Contents****Critical Accounting Policies and Estimates**

We use certain critical accounting policies as described in Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations - Critical Accounting Policies of our Annual Report on Form 10-K filed with the Securities and Exchange Commission for the year ended December 31, 2006. There have been no material changes in any of our critical accounting policies since December 31, 2006, except for the adoption of Financial Accounting Standards Board Interpretation No. 48 - Accounting for Uncertainty in Income Taxes (FIN 48). See Note 10 of Notes to Financial Statements on Income Taxes, including discussion of the impact of adopting FIN 48: Uncertain Tax Positions on January 1, 2007.

**Item 3: Quantitative and Qualitative Disclosures about Market Risk**

See our 2006 Annual Report on Form 10-K (Item 7A). As of June 30, 2007, there have been no material changes in this information.

**Item 4: Controls and Procedures**

The company's management evaluated, with the participation of the Chief Executive Officer and Chief Financial Officer, the effectiveness of the company's disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that the company's disclosure controls and procedures are effective to ensure that information we are required to disclose in reports that we file or submit under the Securities Exchange Act of 1934 is accumulated and communicated to the company's management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure, and that such information is recorded, processed, summarized, and reported within time periods specified in the Securities and Exchange Commission rules and forms. There has been no change in the company's internal control over financial reporting that occurred during the period covered by this Quarterly Report on Form 10-Q that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting.

**PART II Other Information****Item 1: Legal Proceedings****Ronald H. Fraser v. PC-Tel, Inc., Wells Fargo Shareowner Services, Wells Fargo Bank Minnesota, N.A.**

In March 2002, plaintiff Ronald H. Fraser (Fraser) filed a complaint in the California Superior Court for breach of contract and declaratory relief against us and for breach of contract, conversion, negligence and declaratory relief against our transfer agent, Wells Fargo Bank Minnesota, N.A. The complaint seeks compensatory damages allegedly suffered by Fraser as a result of the sale of certain stock by Fraser during a secondary offering in April 2000. At a mandatory settlement conference held in September 2004, Fraser stipulated to judgment in favor of us. In November 2004 Fraser appealed the judgment entered against him. On February 6, 2007, the Court of Appeal for the Sixth Appellate District issued an opinion affirming the trial court's order granting PCTEL's motion for summary judgment. On March 2, 2007, Fraser submitted an appeal of this decision and on March 7, 2007, the Court of Appeal for the Sixth Appellate District denied his appeal. In March 2007, Fraser appealed to the Supreme Court of California. In May 2007, Fraser was denied his appeal.

**Item 1A: Risk Factors****Factors That May Affect Our Business, Financial Condition and Future Operating Results**

There have been no material changes with respect to risk factors as previously disclosed in our Annual Report on Form 10-K for our fiscal year ended December 31, 2006.

**Item 2: Changes in Securities, use of proceeds, and issuer purchases of equity securities**

**Table of Contents**

<b>Total Number of Shares Repurchased</b>	<b>Average Price Paid Per Share</b>	<b>Number of Shares Authorized to Repurchase</b>	<b>Total Number of Shares Purchased as Part of Publicly Announced Programs</b>	<b>Maximum Number of Shares That May Yet Be Purchased Under the Programs</b>
146,084	9.91	500,000	2,314,000	186,000
			2,460,084	539,916
			2,460,084	539,916

In 2002 and 2003, the Board of Directors authorized the repurchase of up to 2,500,000 shares of common stock. Through December 31, 2006 we had repurchased 2,314,000 shares from this total authorized. In May, company repurchased 146,084 shares of common stock at an average price of \$9.91. Also in May 2007, the Board of Directors authorized the repurchase up to 500,000 additional shares of common stock. As of June 30, 2007, we were authorized to repurchase 539,916 shares of common stock.

**Item 4: Submission of Matters to a Vote of Security Holders**

We held our 2007 Annual Meeting of Stockholders on June 5, 2007 in Chicago, Illinois. We solicited votes by proxy pursuant to proxy solicitation materials delivered to our stockholders on or about April 27, 2007. The following is a brief description of matters voted on at the meeting and a statement of the number of votes cast for, against or withheld and the number of abstains:

1. Election of Richard C. Alberding and Carl A. Thomsen as Class III directors until the Annual Meeting of Stockholders in 2010:

	<b>FOR</b>	<b>WITHHELD</b>
Richard C. Alberding	17,142,099	2,573,453
Carl A. Thomsen	17,459,696	2,255,856

The terms of office of John Sheehan, Brian Jackman, Steven D. Levy, and Giacomo Marini continued after the meeting.

2. Approval of the amended and restated 1998 Employee Stock Purchase Plan:

<b>VOTES FOR</b>	<b>VOTES AGAINST</b>	<b>ABSTAIN</b>
11,735,252	1,894,976	11,457

3. Approval of the Executive Compensation Plan:

<b>VOTES FOR</b>	<b>VOTES AGAINST</b>	<b>ABSTAIN</b>
11,447,661	2,183,617	10,407

4. Ratification of the appointment of Grant Thornton LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2007:

<b>VOTES FOR</b>	<b>VOTES AGAINST</b>	<b>ABSTAIN</b>
19,670,358	37,386	7,808



**Table of Contents****Item 6: Exhibits**

<b>Exhibit No.</b>	<b>Description</b>	<b>Reference</b>
10.59	1998 Employee Stock Purchase Plan	Incorporated by reference to the same number filed with the Registrant's Current Report on Form 8-K filed on June 5, 2007
10.60	Executive Compensation Plan	Incorporated by reference to the same number filed with the Registrant's Current Report on Form 8-K filed on June 5, 2007
10.61	Offer letter between PCTEL, Inc. and Robert Suastegui, Vice President and General Manager, Global Sales and Marketing, dated May 16, 2007	Filed herewith
31.1	Certification of Principal Executive Officer pursuant to Section 302 of Sarbanes-Oxley Act of 2002	Filed herewith
31.2	Certification of Principal Financial Officer pursuant to Section 302 of Sarbanes-Oxley Act of 2002.	Filed herewith
32.1	Certification of Principal Executive Officer and Principal Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of Sarbanes-Oxley Act of 2002.	Filed herewith

**Table of Contents**

SIGNATURE

Pursuant to the requirements 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:

PCTEL, Inc.  
A Delaware Corporation  
(Registrant)

/s/ Martin H. Singer

Martin H. Singer  
Chairman of the Board and Chief Executive Officer  
Date: August 8, 2007

27