ARRIS GROUP INC
Form 10-Q
May 07, 2012
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

For the quarter ended March 31, 2012

of

ARRIS GROUP, INC.

A Delaware Corporation

IRS Employer Identification No. 58-2588724

SEC File Number 000-31254

3871 Lakefield Drive

Suwanee, GA 30024

(678) 473-2000

ARRIS Group, Inc. (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, and (2) has been subject to such filing requirements for the past 90 days.

ARRIS Group, Inc. is a large accelerated filer and is not a shell company.

ARRIS is required to submit electronically and post on its corporate web site Interactive Data Files required to be submitted and posted pursuant to Rule 405 of regulation S-T.

As of April 30, 2012, 113,041,028 shares of the registrant s Common Stock, $0.01 par value, were outstanding.

ARRIS GROUP, INC.

FORM 10-Q

For the Three Months Ended March 31, 2012

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PART I. CONDENSED FINANCIAL INFORMATION

Item 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

ARRIS GROUP, INC.

CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share data) (unaudited)

	March 31, 2012	December 31, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	$ 215,808	$ 235,875
Short-term investments, at fair value	298,539	282,904
Total cash, cash equivalents and short-term investments	514,347	518,779
Restricted cash	3,943	4,101
Accounts receivable (net of allowances for doubtful accounts of $1,398 in 2012 and $1,443 in 2011)	183,427	152,437
Other receivables	5,071	8,789
Inventories (net of reserves of $11,550 in 2012 and $12,243 in 2011)	105,114	115,912
Prepaids	12,436	10,408
Current deferred income tax assets	22,068	22,048
Other current assets	16,792	27,071
Total current assets	863,198	859,545
Property, plant and equipment (net of accumulated depreciation of $136,143 in 2012 and $130,331 in 2011)	57,810	61,375
Goodwill	195,268	194,542
Intangible assets (net of accumulated amortization of $216,753 in 2012 and $209,374 in 2011)	117,444	124,823
Investments	82,968	71,095
Noncurrent deferred income tax assets	42,106	38,433
Other assets	11,699	10,997
	$ 1,370,493	$ 1,360,810
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 54,576	$ 40,671
Accrued compensation, benefits and related taxes	31,081	36,764
Accrued warranty	3,094	3,350
Deferred revenue	60,129	43,746
Other accrued liabilities	31,054	33,325
Total current liabilities	179,934	157,856
Long-term debt, net of current portion	212,765	209,766
Accrued pension	25,739	25,260
Noncurrent income tax liability	26,676	24,450
Noncurrent deferred income tax liabilities	352	337
Other noncurrent liabilities	26,256	26,936
Total liabilities	471,722	444,605

Stockholders equity:		
Preferred stock, par value $1.00 per share, 5.0 million shares authorized; none issued and outstanding	-	-
Common stock, par value $0.01 per share, 320.0 million shares authorized; 113.7 million and 114.8 million shares issued and outstanding in 2012 and 2011, respectively	1,467	1,449
Capital in excess of par value	1,247,763	1,245,115
Treasury stock at cost, 32.1 million and 29.8 million shares in 2012 and 2011	(280,724)	(254,409)
Accumulated deficit	(59,469)	(65,268)
Unrealized gain on marketable securities (net of accumulated tax benefit (expense) of $108 in 2012 and ($119) in 2011)	149	(267)
Unfunded pension liability (net of accumulated tax effect of $3,257 in 2012 and 2011)	(10,231)	(10,231)
Cumulative translation adjustments	(184)	(184)
Total stockholders equity	898,771	916,205
	$ 1,370,493	$ 1,360,810

See accompanying notes to the condensed consolidated financial statements.

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ARRIS GROUP, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data and percentages) (unaudited)

	Three Months Ended March 31, 2012	2011
Net sales:		
Products	$ 265,270	$ 234,946
Services	37,631	32,490
Total net sales	302,901	267,436
Cost of sales:		
Products	175,123	152,755
Services	18,870	17,735
Total cost of sales	193,993	170,490
Gross margin	108,908	96,946
Operating expenses:		
Selling, general, and administrative expenses	39,544	36,838
Research and development expenses	44,147	36,040
Restructuring charges	5,203	
Acquisition costs	607	
Loss on sale of product line	337	
Amortization of intangible assets	7,379	8,944
Total operating expenses	97,217	81,822
Operating income	11,691	15,124
Other expense (income):		
Interest expense	4,350	4,225
Gain on investments	(961)	(423)
Loss on foreign currency	808	888
Interest income	(755)	(778)
Other income, net	(436)	(113)
Income from continuing operations before income taxes	8,685	11,325
Income tax expense (benefit)	2,886	(239)
Net income	$ 5,799	$ 11,564
Net income per common share:		
Basic	$ 0.05	$ 0.09
Diluted	$ 0.05	$ 0.09
Weighted average common shares:		
Basic	115,075	122,297

Diluted	117,597	125,732

See accompanying notes to the condensed consolidated financial statements.

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ARRIS GROUP, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(in thousands) (unaudited)

	00000000	00000000
	Three Months Ended March 31,	
	2012	2011
Net income	$ 5,799	$ 11,564
Unrealized gain on marketable securities, net of tax effect of $227 in 2012 and $0 in 2011, respectively	416	852
Comprehensive income, net of tax	$ 6,215	$ 12,416

See accompanying notes to the condensed consolidated financial statements.

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ARRIS GROUP, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands) (unaudited)

	Three Months Ended March 31,	
	2012	**2011**
Operating activities:		
Net income	$ 5,799	$ 11,564
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation	7,195	5,855
Amortization of intangible assets	7,379	8,944
Stock compensation expense	6,649	5,284
Deferred income tax benefit	(4,635)	(7,844)
Amortization of deferred finance fees	160	163
Provision for doubtful accounts	54	
Gain on investments	(961)	(423)
Loss on disposal of product line	337	
Loss on disposal of fixed assets	3	34
Excess income tax benefits from stock-based compensation plans	(1,654)	(3,700)
Non-cash interest expense	2,999	2,832
Changes in operating assets and liabilities, net of effect of acquisitions and dispositions:		
Accounts receivable	(31,799)	(24,043)
Other receivables	3,693	534
Inventories	7,243	(4,024)
Income taxes payable and recoverable	6,365	2,270
Accounts payable and accrued liabilities	22,398	(7,048)
Prepaids and other, net	4,048	6,031
Net cash provided by (used in) operating activities	35,273	(3,571)
Investing activities:		
Purchases of property, plant and equipment	(3,762)	(6,251)
Cash proceeds from sale of property, plant and equipment		42
Purchases of investments	(77,766)	(99,361)
Sales of investments	51,908	105,949
Cash proceeds from sale of product line	3,249	
Net cash provided by (used in) investing activities	(26,371)	379
Financing activities:		
Repurchase of common stock	(26,315)	
Excess income tax benefits from stock-based compensation plans	1,654	3,700
Repurchase of shares to satisfy employee tax withholdings	(8,033)	(8,245)
Proceeds from issuance of common stock	3,725	13,363
Net cash provided by (used in) financing activities	(28,969)	8,818
Net increase (decrease) in cash and cash equivalents	(20,067)	5,626
Cash and cash equivalents at beginning of period	235,875	353,121
Cash and cash equivalents at end of period	$ 215,808	$ 358,747

See accompanying notes to the condensed consolidated financial statements.

ARRIS GROUP, INC.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

Note 1. Organization and Basis of Presentation

ARRIS Group, Inc. (together with its consolidated subsidiaries, except as the context otherwise indicates, ARRIS or the Company), is a global communications technology company, headquartered in Suwanee, Georgia. ARRIS operates in three business segments, Broadband Communications Systems, Access, Transport & Supplies, and Media & Communications Systems, specializing in integrated broadband network solutions that include products, systems and software for content and operations management (including video on demand, or VOD), and professional services. ARRIS is a leading developer, manufacturer and supplier of telephony, data, video, construction, rebuild and maintenance equipment for the broadband communications industry. In addition, ARRIS is a leading supplier of infrastructure products used by cable system operators to build-out and maintain hybrid fiber-coaxial (HFC) networks. The Company provides its customers with products and services that enable reliable, high speed, two-way broadband transmission of video, telephony, and data.

The condensed consolidated financial statements reflect all adjustments (consisting of normal recurring accruals) that are, in the opinion of management, necessary for a fair presentation of the consolidated financial statements for the periods shown. Interim results of operations are not necessarily indicative of results to be expected from a twelve-month period. These financial statements should be read in conjunction with the Company s most recently audited consolidated financial statements and notes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2011, as filed with the United States Securities and Exchange Commission (SEC).

Note 2. Impact of Recently Adopted Accounting Standards

In September 2011, the Financial Accounting Standards Board (FASB) issued new accounting guidance intended to simplify goodwill impairment testing. Entities will be allowed to perform a qualitative assessment on goodwill impairment to determine whether a quantitative assessment is necessary. This new guidance is effective for the Company beginning January 1, 2012. The Company does not expect the adoption of this guidance to have any impact on its consolidated financial statements.

In June 2011, FASB issued guidance regarding the presentation of comprehensive income. This guidance requires presentation of total comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The guidance is effective on a retrospective basis for the interim and annual periods ending on or after December 15, 2011. ARRIS adopted the accounting standard in the first quarter of 2012 and elected to present the information in two separate but consecutive statements. The adoption of this guidance did not have a significant impact on the Company s consolidated financial statements.

In May 2011, FASB issued amendments to some fair value measurement principles and disclosure requirements for fair value measurements. The provisions of this guidance are effective for the interim and annual periods ending on or after December 15, 2011. ARRIS adopted the accounting standard in the first quarter of 2012. The adoption of this guidance did not have a significant impact on the Company s consolidated financial statements.

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Note 3. Investments

ARRIS investments as of March 31, 2012 and December 31, 2011 consisted of the following (in thousands):

	As of March 31, 2012	As of December 31, 2011
Current Assets:		
Available-for-sale securities	$ 298,539	$ 282,904
Noncurrent Assets:		
Available-for-sale securities	81,968	70,095
Cost method investments	1,000	1,000
	82,968	71,095
Total	$ 381,507	$ 353,999

ARRIS investments in debt and marketable equity securities are categorized as available-for-sale. The Company currently does not hold any held-to-maturity securities. Realized gains and losses on trading securities and available-for-sale securities are included in net income. Unrealized gains and losses on available-for-sale securities are included in our consolidated balance sheet as a component of accumulated other comprehensive income (loss). The total (gains) losses included in the accumulated other comprehensive income related to available-for-sale securities were ($0.1) million and $0.3 million, net of tax, as of March 31, 2012 and December 31, 2011, respectively. Realized and unrealized gains and losses in total and by individual investment as of March 31, 2012 and December 31, 2011 were not material. The amortized cost basis of the Company s investments approximates fair value.

As of March 31, 2012 and December 31, 2011, ARRIS cost method investment is an investment in a private company. Due to the fact the investment is in a private company, ARRIS is exempt from estimating the fair value. However, ARRIS is required to estimate the fair value if there has been an identifiable event or change in circumstance that may have a significant adverse effect on the fair value of the investment. Each quarter ARRIS evaluates its investment for any other-than-temporary impairment, by reviewing any capital transactions, the current revenues, bookings and long-term plan of the private company. During the evaluation performed as of December 31, 2011, ARRIS concluded that the private company would be depleting cash balances in early 2012. Further, ARRIS was notified that the private company intends to raise capital by offering a new round of financing to its existing and new investors. During the fourth quarter of 2011, ARRIS concluded that the investee s need to raise additional funds was an indicator of impairment and therefore, performed steps to determine the fair value of its investment in the private company. ARRIS was unable to apply traditional valuation techniques as the required inputs to these techniques are unavailable. ARRIS determined that the best estimate of the fair value of its investment was to calculate it based upon the preliminary indication of value related to the new round of financing. As a result of these considerations, ARRIS recorded an other-than-temporary impairment on its investment of $3.0 million in the fourth quarter of 2011. As of March 31, 2012, ARRIS believes there has been no further other-than-temporary impairment but will continue to evaluate the investment for impairment.

Classification of available-for-sale securities as current or non-current is dependent upon management s intended holding period, the security s maturity date and liquidity consideration based on market conditions. If management intends to hold the securities for longer than one year as of the balance sheet date, they are classified as non-current.

Note 4. Fair Value Measurement

Fair value is based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The authoritative guidance establishes a fair value hierarchy that is based on the extent and level of judgment used to estimate the fair value of assets and liabilities. In order to increase consistency and comparability in fair value measurements, the FASB has established a fair value hierarchy that prioritizes observable and unobservable inputs used to measure fair value into three broad levels. An asset or liability s categorization within the fair value hierarchy is based upon the lowest level of input that is significant to the measurement of its fair value. The three levels of input defined by the authoritative guidance are as follows:

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Level 1: Quoted prices (unadjusted) in active markets that are accessible at the measurement date for assets or liabilities. The fair value hierarchy gives the highest priority to Level 1 inputs.

Level 2: Observable prices that are based on inputs not quoted on active markets, but corroborated by market data.

Level 3: Unobservable inputs are used when little or no market data is available. The fair value hierarchy gives the lowest priority to Level 3 inputs.

The following table presents the Company s investment assets and foreign currency contract positions measured at fair value on a recurring basis as of March 31, 2012 (in thousands):

	Level 1	Level 2	Level 3	Total
Current investments	$ 102,797	$ 195,742	$	$ 298,539
Noncurrent investments	15,795	66,173		81,968
Foreign currency contracts asset position	1,423			1,423
Foreign currency contracts liability position	320			320

In addition to the amounts disclosed in the above table, the fair value of the Company s Israeli severance pay assets, which were almost fully comprised of Level 2 assets, was $3.7 million as of March 31, 2012 and December 31, 2011.

All of the Company s short-term investments and long-term investments instruments are classified within Level 1 or Level 2 of the fair value hierarchy as they are valued using quoted market prices, market prices for similar securities, or alternative pricing sources with reasonable levels of price transparency. The types of instruments valued based on quoted market prices in active markets include the Company s investment in money market funds, mutual funds, U.S. government bonds and investments in public companies. Such instruments are generally classified within Level 1 of the fair value hierarchy. The types of instruments valued based on other observable inputs include the Company s cash surrender value of company owned life insurance, corporate obligations and bonds, commercial paper and certificates of deposit. Such instruments are classified within Level 2 of the fair value hierarchy.

In determining the value of certain Level 2 instruments, ARRIS has performed steps to verify the accuracy of the valuations provided by ARRIS brokerage firms. ARRIS has reviewed the most recent Statement on Standards for Attestation Engagements No. 16 (SSAE report) for each brokerage firm holding investments for ARRIS. The SSAE report for each did not identify any control weakness in the brokerages policies and procedures, in particular as they relate to the pricing and valuation of financial instruments. ARRIS has determined the third party pricing source used by each firm to be a reliable recognized source of financial valuations. In addition ARRIS has performed further testing on a large sample of its corporate obligations and commercial paper investments. These tests did not show any material discrepancies in the valuations provided by the brokerage firms. It is the Company s intent to continue to verify valuations on a quarterly basis, using one or more reliable recognized third party pricing providers. See Note 3 and Note 5 for further information on the Company s investments and derivative instruments.

All of the Company s foreign currency contracts are over-the-counter instruments. There is an active market for these instruments, and therefore, they are classified as Level 1 in the fair value hierarchy. ARRIS does not enter into currency contracts for trading purposes. The Company has a master netting agreement with the primary counterparty to the derivative instruments. This agreement allows for the net settlement of assets and liabilities arising from different transactions with the same counterparty.

Note 5. Derivative Instruments and Hedging Activities

ARRIS has certain international customers who are billed in their local currency. Changes in the monetary exchange rates may adversely affect the Company s results of operations and financial condition. When appropriate, ARRIS enters into various derivative transactions to enhance its ability to manage the volatility relating to these typical business exposures. The Company does not hold or issue derivative instruments for trading or other speculative purposes. The Company s derivative instruments are recorded in the Consolidated

Balance Sheets at their fair values. The Company s derivative instruments are not designated as hedges, and accordingly, all changes in the fair value of the instruments are recognized as a loss (gain) on foreign currency in the Consolidated Statements of Operations. The maximum time frame for ARRIS derivatives is currently less than twelve months. Derivative instruments which are subject to master netting arrangements are not offset in the Consolidated Balance Sheets.

The fair values of ARRIS derivative instruments recorded in the Consolidated Balance Sheet as of March 31, 2012 and December 31, 2011 were as follows (in thousands):

	As of March 31, 2012		**As of December 31, 2011**	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Derivatives Not Designated as Hedging Instruments:				
Foreign exchange contracts asset derivatives	Other current assets	$ 1,423	Other current assets	$ 3,295
Foreign exchange contracts liability derivatives	Other accrued liabilities	$ 320	Other accrued liabilities	$ 546

The change in the fair values of ARRIS derivative instruments recorded in the Consolidated Statements of Operations during the three months ended March 31, 2012 and 2011 were as follows (in thousands):

		Three Months Ended March 31,	
	Statement of Operations Location	2012	2011
Derivatives Not Designated as Hedging Instruments:			
Foreign exchange contracts	(Gain) loss on foreign currency	$ (1,161)	$ 2,133

Note 6. Business Acquisitions

Acquisition of BigBand Networks, Inc.

On November 21, 2011, ARRIS completed its tender offer for all outstanding shares of common stock of BigBand Networks, Inc. Pursuant to the Agreement and Plan of Merger, all outstanding shares of common stock of BigBand were canceled and converted into the right to receive cash equal to $2.24 per share, without interest and net of applicable withholding taxes. This transaction was accounted for as a business combination. The acquisition supports ARRIS strategy of expanding its video product suite and investing in the evolution towards network convergence on an all IP platform. This expanded portfolio and access to new market channels is expected to provide greater opportunities to grow ARRIS customer base worldwide. The goodwill and intangible assets resulting from this acquisition are recorded in the BCS segment.

Purchase Price and Preliminary Allocation

The purchase price was allocated to the tangible assets and identifiable intangible assets acquired and liabilities assumed based on their relative fair values. The excess of the purchase price over the net tangible and identifiable intangible assets and liabilities assumed was recorded as goodwill. While the Company uses its best estimates and assumptions as a part of the purchase price allocation process to accurately value assets acquired and liabilities assumed at the acquisition date, the estimates are inherently uncertain and subject to refinement. As a result, during the measurement period, which may be up to one year from the acquisition date, ARRIS records adjustments to the assets acquired and liabilities assumed, with the corresponding offset to goodwill. Upon the conclusion of the measurement period, any subsequent adjustments are recorded to the consolidated statements of operations.

Accounting for business combinations requires management to make significant estimates and assumptions, especially at the acquisition date with respect to intangible assets, obligations assumed and pre-acquisition contingencies. Although the Company believes the assumptions and estimates made in the past have been reasonable and appropriate, they are based in part on historical experience and information obtained from the management of the acquired companies and are inherently uncertain.

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In addition, uncertain tax positions and tax related valuation allowances assumed in connection with a business combination are initially estimated as of the acquisition date and the Company reevaluates these items quarterly with certain adjustments to the preliminary estimates being recorded to goodwill provided that it is within the measurement period and the Company continues to collect information in order to determine their estimated values. Subsequent to the measurement period or the final determination of the uncertain tax positions estimated value or tax related valuation allowances, changes to these uncertain tax positions and tax related valuation allowances will affect the provision for income taxes in the consolidated statement of operations and could have a material impact on the results of operations and financial position.

The total purchase price includes the aggregate cash consideration which was paid out at the closing date of acquisition. The following is a summary of the total purchase price of the transaction and preliminary allocation of the preliminary purchase price (in thousands):

Cash paid at $2.24 per common share	$ 162,417
Converted restricted shares for which service was performed pre-acquisition	280
Total preliminary purchase price	$ 162,697
Tangible assets and liabilities acquired:	
Cash, short-term and long-term investments	$ 109,263
Account receivable	4,612
Inventory	7,005
Other assets	9,670
Property, plant and equipment	6,010
Deferred tax assets	21,960
Deferred revenue	(9,967)
Accrued compensation, including change of control and Israeli severance liabilities	(19,427)
Accrued legal settlement	(495)
Other liabilities	(6,342)
Net tangible assets acquired	122,289
Identifiable intangible assets:	
Acquired in-process research and development	7,800
Other identifiable intangible assets:	
Existing technology	16,400
Order backlog	700
Customer relationships	12,400
Identifiable intangible assets	37,300
Goodwill	3,108
Preliminary allocation of purchase price	$ 162,697

Note 7. Disposal of Product Line

In March of 2012, the Company completed the sale of certain assets of its ECCO electronic connector product line to Eclipse Embedded Technologies, Inc. for approximately $3.9 million, which included $3.2 million paid as of closing and delivery of a promissory note in the principal amount of $0.7 million together with interest. The sale included inventory, accounts receivable, property, plant and equipment, as well as accounts payable and certain accrued liabilities. The Company recorded a net loss of $(0.3) million on the sale, which included approximately $0.3 million of transaction related costs.

The ECCO electronic connector product line disposal group, represented a component of the entity that was comprised of operations and cash flows that were clearly distinguished operationally and for financial reporting purposes and although meeting the criteria for reporting in discontinued operations, the Company has determined the results of the ECCO product line are immaterial to the overall financial results of the

Company and presentation as discontinued operations would not result in a material change to our consolidated financial results.

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The Company s assessment took into account the results of the ECCO product line and its impact on consolidated assets, revenues and expenses for each of the three years ended December 31, 2011, of which the impact for each category was less than 1.0% for each of the years. In addition, the net loss on the sale is also deemed to be immaterial to the consolidated financial results of the Company.

Note 8. Pension Benefits

Components of Net Periodic Pension Cost (in thousands):

	Three Months Ended March 31,	
	2012	2011
Service cost	$ 84	$ 78
Interest cost	521	536
Expected return on plan assets	(315)	(406)
Amortization of net loss	210	72
Net periodic pension cost	$ 500	$ 280

Employer Contributions

No minimum funding contributions are required in 2012 under the Company s defined benefit plan. However, the Company made voluntary contributions to the plan of approximately $22 thousand for the three months ended March 31, 2012. Additionally, the Company made a voluntary contribution to the plan of $0.5 million in April 2012. The Company has established two rabbi trusts to fund the Company s pension obligations under the non-qualified plan of the Chief Executive Officer and certain executive officers. The balance of these rabbi trust assets as of March 31, 2012 was approximately $14.6 million and is included in Investments on the Consolidated Balance Sheets.

Note 9. Guarantees

Warranty

ARRIS provides warranties of various lengths to customers based on the specific product and the terms of individual agreements. The Company provides for the estimated cost of product warranties based on historical trends, the embedded base of product in the field, failure rates, and repair costs at the time revenue is recognized. Expenses related to product defects and unusual product warranty problems are recorded in the period that the problem is identified. While the Company engages in extensive product quality programs and processes, including actively monitoring and evaluating the quality of its suppliers, the estimated warranty obligation could be affected by changes in ongoing product failure rates, material usage and service delivery costs incurred in correcting a product failure, as well as specific product failures outside of ARRIS baseline experience. If actual product failure rates, material usage or service delivery costs differ from estimates, revisions (which could be material) would be recorded to the warranty liability.

The Company offers extended warranties and support service agreements on certain products. Revenue from these agreements is deferred at the time of the sale and recognized on a straight-line basis over the contract period. Costs of services performed under these types of contracts are charged to expense as incurred, which approximates the timing of the revenue stream.

Information regarding the changes in ARRIS aggregate product warranty liabilities for the three months ended March 31, 2012 was as follows (in thousands):

Balance at December 31, 2011	$ 6,387
Accruals related to warranties (including changes in estimates)	636
Settlements made (in cash or in kind)	(960)
Balance at March 31, 2012	$ 6,063

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Note 10. Restructuring Charges

ARRIS has restructuring accruals representing contractual obligations that related to excess leased facilities and equipment in ARRIS ATS segment. Payments will be made over their remaining lease terms through 2014, unless terminated earlier (in thousands):

Balance as of December 31, 2011	$	1,144
Payments		(95)
Balance as of March 31, 2012	$	1,049

In the fourth quarter of 2011, the Company initiated a restructuring plan as a result of its acquisition of BigBand Networks. The plan focuses on the rationalization of personnel, facilities and systems across multiple segments in the ARRIS organization. During the fourth quarter of 2011, ARRIS recorded a restructuring charge of $3.4 million, of which $3.3 million was related to severance and termination benefits and $0.1 million was related to facilities. In the first quarter of 2012, ARRIS recorded additional restructuring charge of $5.2 million, of which $4.4 million was related to severance and termination benefits and $0.8 million was related to facilities. As of March 31, 2012, the total liability remaining for this restructuring plan was approximately $3.6 million, the majority of which is expected to be paid during the first half of 2012 (in thousands):

Balance as of December 31, 2011	$	2,824
Restructuring charges		5,203
Payments		(4,405)
Balance as March 31, 2012	$	3,622

Additionally, ARRIS acquired remaining restructuring accruals of approximately $0.4 million representing BigBand contractual obligations that related to excess leased facilities and equipment. The balance of this restructuring accrual as of December 31, 2011 and March 31, 2012 was $0.2 million and $0, respectively. The restructuring accruals were in ARRIS BCS segment.

Note 11. Inventories

Inventories are stated at the lower of average cost, approximating first-in, first-out, or market. The components of inventory were as follows, net of reserves (in thousands):

		December 31, March 31, 2012		December 31, December 31, 2011
Raw material	$	18,251	$	22,759
Work in process		3,785		3,551
Finished goods		83,078		89,602
Total inventories, net	$	105,114	$	115,912

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Note 12. Property, Plant and Equipment

Property, plant and equipment, at cost, consisted of the following (in thousands):

	March 31, 2012	December 31, 2011
Land	$ 2,562	$ 2,612
Building and leasehold improvements	24,556	25,243
Machinery and equipment	166,835	163,851
	193,953	191,706
Less: Accumulated depreciation	(136,143)	(130,331)
Total property, plant and equipment, net	$ 57,810	$ 61,375

Note 13. Convertible Senior Notes

In 2006, the Company issued $276.0 million of 2% convertible senior notes due 2026. The notes are convertible, at the option of the holder, based on an initial conversion rate, subject to adjustment, of 62.1504 shares per $1,000 principal amount (which represents an initial conversion price of approximately $16.09 per share of our common stock), into cash up to the principal amount and, if applicable, shares of the Company s common stock, cash or a combination thereof. The notes are unsecured senior obligations, and are effectively subordinated to all liabilities, including trade payables and lease obligations of the Company s subsidiaries. The notes may be converted during any calendar quarter in which the closing price of ARRIS common stock for 20 or more trading days in a period of 30 consecutive trading days ending on the last trading day of the immediately preceding calendar quarter exceeds 120% of the conversion price in effect at that time (which, based on the current conversion price, would be $19.31) and upon the occurrence of certain other events. Upon conversion, the holder will receive the principal amount in cash and an additional payment, in either cash or stock at the option of the Company. The additional payment will be based on a formula which calculates the difference between the initial conversion rate ($16.09) and the market price at the date of the conversion. As of May 4, 2012, the notes could not be converted by the holders thereof. Interest is payable on May 15 and November 15 of each year. The Company may redeem the notes at any time on or after November 15, 2013, subject to certain conditions. In addition, the holders may require the Company to purchase all or a portion of their convertible notes on or after November 13, 2013. There are no significant financial covenants related to the notes.

During 2011, the Company acquired $5.0 million face value of the notes for approximately $5.0 million. The Company allocated $2 thousand to the reacquisition of the equity component of the notes. The Company also wrote off approximately $33 thousand of deferred finance fees associated with the portion of the notes acquired. As a result, the Company realized a loss of approximately $19 thousand on the retirement of the notes.

During 2010, ARRIS acquired $24.0 million principal amount of the notes, which had a book value, net of debt discount, of $20.0 million for approximately $23.3 million. The Company allocated $0.1 million to the reacquisition of the equity component of the notes. The Company also wrote off approximately $0.2 million of deferred finance fees associated with the portion of the notes acquired. As a result, the Company realized a gain of approximately $0.4 million on the retirement of the notes.

ARRIS accounts for the liability and equity components of the notes separately. The Company is accreting the debt discount related to the equity component to non-cash interest expense over the estimated seven year life of the convertible notes, which represents the first redemption date of November 15, 2013 when the Company may redeem the notes at its election or the note holders may require their redemption. The equity and liability components related to the notes were as follows (in thousands):

	March 31, 2012	December 31, 2011
Carrying amount of the equity component	$ 48,209	$ 48,209

Principal amount of the liability component	$ 232,050	$ 232,050
Unamortized discount	(19,285)	(22,284)
Net carrying amount of the liability component	$ 212,765	$ 209,766

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The following table presents the contractual interest coupon and the amortization of the discount on the equity component related to the notes during the three months ended March 31, 2012 and 2011 (in thousands):

	Three Months Ended March 31,	
	2012	2011
Contractual interest recognized	$ 1,160	$ 1,185
Amortization of discount	2,999	2,832

The effective annual interest rate on the debt component is 7.93%.

The Company paid approximately $7.8 million of finance fees related to the issuance of the notes. Of the $7.8 million, approximately $5.3 million was attributed to the debt component and $2.5 million was attributed to the equity component of the convertible debt instrument. The portion related to the debt component is being amortized over seven years. The remaining balance of unamortized financing costs from these notes as of March 31, 2012 and December 31, 2011 was $1.0 million and $1.2 million, respectively.

The Company has not paid cash dividends on its common stock since its inception.

Note 14. Segment Information

The management approach has been used to present the following segment information. This approach is based upon the way the management of the Company organizes segments within an enterprise for making operating decisions and assessing performance. Financial information is reported on the basis that it is used internally by the chief operating decision maker (CODM) for evaluating segment performance and deciding how to allocate resources to segments. The Company s chief executive officer has been identified as the CODM.

The *Broadband Communications Systems (BCS)* segment s product solutions include Headend and Subscriber Premises equipment that enable cable operators to provide Voice over IP, Video over IP and high-speed data services to residential and business subscribers.

The *Access, Transport & Supplies (ATS)* segment s product lines cover all components of a hybrid fiber coax network, including managed and scalable headend and hub equipment, optical nodes, radio frequency products, transport products and supplies.

The *Media & Communications Systems (MCS)* segment provides content and operations management systems, including products for Video on Demand, Ad Insertion, Digital Advertising, Service Assurance, Service Fulfillment and Mobile Workforce Management.

These operating segments were determined based on the nature of the products and services offered.

The Company evaluates performance based on several factors, of which the primary financial measures are revenues and gross margins. A measure of assets is not applicable, as segment assets are not regularly reviewed by the CODM for evaluating performance and allocating resources to the segment. The accounting policies of the operating segments are the same as those disclosed in Form 10-K for the year ended December 31, 2011.

The table below represents information about the Company s reporting segments for the three months ended March 31, 2012 and 2011 (in thousands):