

Edgar Filing: PC TEL INC - Form 10-Q

PC TEL INC  
Form 10-Q  
May 10, 2006

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 20549

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FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2006

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)

77-0364943  
(I.R.S. Employer  
Identification Number)

8725 W. HIGGINS ROAD, SUITE 400,  
CHICAGO IL  
(Address of Principal Executive Office)

60631  
(Zip Code)

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

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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



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ASSETS

|   |           |           |
|---|-----------|-----------|
| CURRENT ASSETS:   |           |           |
| Cash and cash equivalents   | \$ 58,622 | \$ 58,966 |
| Restricted cash   | 208       | 208       |
| Accounts receivable, net of allowance for doubtful<br>accounts of \$321 and \$318, respectively | 13,600    | 13,725    |
| Inventories, net  | 9,827     | 9,547     |
| Prepaid expenses and other assets   | 2,407     | 3,109     |
|   | -----     | -----     |
| Total current assets  | 84,664    | 85,555    |
| PROPERTY AND EQUIPMENT, net   | 11,419    | 11,190    |
| GOODWILL  | 31,406    | 31,020    |
| OTHER INTANGIBLE ASSETS, net  | 15,609    | 16,457    |
| OTHER ASSETS  | 227       | 283       |
|   | -----     | -----     |
| TOTAL ASSETS  | \$143,325 | \$144,505 |
|   | =====     | =====     |

LIABILITIES AND STOCKHOLDERS' EQUITY

|   |           |           |
|---|-----------|-----------|
| CURRENT LIABILITIES:  |           |           |
| Accounts payable  | \$ 2,109  | \$ 2,251  |
| Income taxes payable  | 5,256     | 5,297     |
| Deferred revenue  | 1,893     | 1,944     |
| Other accrued liabilities   | 6,388     | 6,368     |
|   | -----     | -----     |
| Total current liabilities   | 15,646    | 15,860    |
| Pension Liability   | 3,047     | 3,047     |
| Other long-term accrued liabilities   | 1,364     | 1,571     |
|   | -----     | -----     |
| Total liabilities   | \$ 20,057 | \$ 20,478 |
|   | =====     | =====     |
| STOCKHOLDERS' EQUITY:   |           |           |
| Common stock, \$0.001 par value, 100,000,000 shares<br>authorized, 21,855,121 and 20,423,372 shares issued and<br>outstanding at March 31, 2006 and December 31, 2005, respectively | 22        | 22        |
| Additional paid-in capital  | 161,671   | 160,825   |
| Accumulated deficit   | (38,850)  | (36,652)  |
| Accumulated other comprehensive income  | 425       | (168)     |
|   | -----     | -----     |
| Total stockholders' equity  | 123,268   | 124,027   |
|   | -----     | -----     |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY  | \$143,325 | \$144,505 |
|   | =====     | =====     |

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

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|  | THREE MONTHS ENDED<br>MARCH 31, |            |
|--|---------------------------------|------------|
|  | 2006                            | 2005       |
| REVENUES   | \$18,566                        | \$15,008   |
| COST OF REVENUES                                 | 9,844                           | 7,570      |
| GROSS PROFIT                                     | 8,722                           | 7,438      |
| OPERATING EXPENSES:                              |                                 |            |
| Research and development                         | 2,916                           | 2,470      |
| Sales and marketing                              | 3,543                           | 3,115      |
| General and administrative                       | 3,748                           | 4,167      |
| Amortization of intangible assets                | 1,037                           | 883        |
| Restructuring charges, net                       | 553                             | --         |
| Gain on sale of assets and related royalties     | (250)                           | (500)      |
| Total operating expenses                         | 11,547                          | 10,135     |
| LOSS FROM OPERATIONS                             | (2,825)                         | (2,697)    |
| OTHER INCOME, NET                                | 620                             | 541        |
| LOSS BEFORE PROVISION (BENEFIT) FOR INCOME TAXES | (2,205)                         | (2,156)    |
| PROVISION (BENEFIT) FOR INCOME TAXES             | (7)                             | 161        |
| NET LOSS   | \$ (2,198)                      | \$ (2,317) |
| Basic loss per share                             | \$ (0.11)                       | \$ (0.12)  |
| Shares used in computing basic loss per share    | 20,645                          | 20,043     |
| Diluted loss per share                           | \$ (0.11)                       | \$ (0.12)  |
| Shares used in computing diluted loss per share  | 20,645                          | 20,043     |

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

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PCTEL, INC.  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(UNAUDITED, IN THOUSANDS)

|   | THREE MONTHS ENDED<br>MARCH 31, |         |
|---|---------------------------------|---------|
|   | 2006                            | 2005    |
| CASH FLOWS FROM OPERATING ACTIVITIES:   |                                 |         |
| Net loss  | (2,198)                         | (2,317) |
| Adjustments to reconcile net loss to net cash provided by (used in) operating activities: |                                 |         |
| Depreciation and amortization   | 1,527                           | 1,231   |

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|  |         |        |
|--|---------|--------|
| Amortization of stock-based compensation                             | 1,149   | 662    |
| Gain on sale of assets and related royalties                         | (250)   | (500)  |
| Provision for allowance for doubtful accounts                        | 27      | 29     |
| Changes in operating assets and liabilities, net of acquisitions:    |         |        |
| Decrease in accounts receivable                                      | 136     | 77     |
| Increase in inventories  | (223)   | (288)  |
| Decrease in prepaid expenses, other current assets, and other assets | 809     | 43     |
| Increase (decrease) in accounts payable                              | (164)   | 1,162  |
| Increase in income taxes payable                                     | (41)    | (57)   |
| Increase (decrease) in other accrued liabilities                     | 18      | (687)  |
| Increase (decrease) in deferred revenue                              | (310)   | 560    |
|  | -----   | -----  |
| Net cash provided by (used in) operating activities                  | 480     | (85)   |
|  | -----   | -----  |
| CASH FLOWS FROM INVESTING ACTIVITIES:                                |         |        |
| Capital expenditures for property and equipment                      | (792)   | (895)  |
| Proceeds on sale of property and equipment                           | 92      | --     |
| Proceeds on sale of assets and related royalties                     | 250     | 500    |
|  | -----   | -----  |
| Net cash used in investing activities                                | (450)   | (395)  |
|  | -----   | -----  |
| CASH FLOWS FROM FINANCING ACTIVITIES:                                |         |        |
| Payment of withholding tax on stock based compensation               | (1,008) | --     |
| Proceeds from issuance of common stock                               | 666     | 380    |
|  | -----   | -----  |
| Net cash provided by (used in) financing activities                  | (342)   | 380    |
|  | -----   | -----  |
| Net decrease in cash and cash equivalents                            | (312)   | (100)  |
| Effect of exchange rate changes on cash                              | (32)    | (18)   |
| Cash and cash equivalents, beginning of period                       | 58,966  | 83,887 |
|  | -----   | -----  |
| CASH AND CASH EQUIVALENTS, END OF PERIOD                             | 58,622  | 83,769 |
|  | =====   | =====  |

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PCTEL, INC.  
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE THREE MONTHS ENDED MARCH 31, 2006  
(UNAUDITED)

### NOTE 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 ended March 31, 2006 are not necessarily indicative of the results that may be expected for the year ending December 31, 2006. 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, 2005.

### BASIS OF CONSOLIDATION AND FOREIGN CURRENCY TRANSLATION

The company uses the United States dollar as the functional currency for

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the financial statements. The company uses the local currency as the functional currency for its subsidiaries in China (Yuan), Ireland (Euro), and Japan (Yen). 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. At March 31, 2006, the cumulative translation adjustment was positive \$425,000. The company uses the U.S. dollar as the functional currency for its subsidiaries in Israel and for its branch office in Hong Kong. These consolidated financial statements include the accounts of PCTEL and its subsidiaries after eliminating intercompany accounts and transactions.

### NOTE 2. INVENTORIES

Inventories as of March 31, 2006 were composed of raw materials, sub assemblies, finished goods and work-in-process. Sub assemblies are included within raw materials. As of March 31, 2006 and December 31, 2005, the allowance for inventory losses was \$0.9 million.

Inventories consist of the following (in thousands):

|                  | MARCH 31,<br>2006<br>----- | DECEMBER 31,<br>2005<br>----- |
|------------------|----------------------------|-------------------------------|
| Raw materials    | \$6,729                    | \$6,404                       |
| Work in process  | 543                        | 461                           |
| Finished goods   | 2,555                      | 2,682                         |
|                  | -----                      | -----                         |
| Inventories, net | \$9,827                    | \$9,547                       |
|                  | =====                      | =====                         |

### NOTE 3. EARNINGS PER SHARE

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

|   | THREE MONTHS ENDED<br>March 31,<br>----- |               |
|---|--|---------------|
|   | 2006<br>-----                            | 2005<br>----- |
| Net loss  | \$(2,198)                                | \$(2,317)     |
|   | =====                                    | =====         |
| Basic loss per share:                               |  |               |
| Weighted average common shares outstanding          | 21,820                                   | 21,135        |
| Less: Weighted average shares subject to repurchase | (1,175)                                  | (1,092)       |
|   | -----                                    | -----         |

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|  |           |           |
|--|-----------|-----------|
| Weighted average common shares outstanding                                 | 20,645    | 20,043    |
|  | -----     | -----     |
| Basic loss per share   | \$ (0.11) | \$ (0.12) |
|  | =====     | =====     |
| Diluted loss per share:  |           |           |
| Weighted average common shares outstanding                                 | 20,645    | 20,043    |
| Weighted average shares subject to repurchase                              | *         | *         |
| Weighted average common stock option grants                                | *         | *         |
| Weighted average common shares and common stock<br>Equivalents outstanding | 20,645    | 20,043    |
|  | -----     | -----     |
| Diluted loss per share   | \$ (0.11) | \$ (0.12) |
|  | =====     | =====     |

\* 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 491,000 and 337,000 for the three months ended March 31, 2006 and March 31, 2005, respectively.

#### NOTE 4. RECENT ACCOUNTING PRONOUNCEMENTS

In May 2005, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (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. The company does not believe this statement will have a material impact on the company's financial statements.

Effective January 1, 2006, the company adopted Statement of Financial Accounting Standards (SFAS) No. 123(R), "Share Based Payments," as described in Note 5.

#### NOTE 5. STOCK-BASED COMPENSATION

In the first fiscal quarter of fiscal 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 expenses 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 has 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). As required under the modified prospective transition method the company has not

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restated prior period results. As a result, certain components of the company's quarterly financial statements will not be comparable until the first quarter of fiscal 2007, the anniversary of the company's adoption of SFAS No. 123(R). In the quarter ended March 31, 2005, the company accelerated the vesting of all unvested options to purchase shares of common stock of PCTEL that were held by current employees, including executive officers, and which have an exercise price per share equal to or greater than \$10.00. The

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effect of this acceleration resulted in PCTEL not being required to recognize share-based compensation expense of \$3.8 million in the periods after adoption of SFAS No. 123(R).

As part of the adoption of SFAS No. 123(R), the company took the shorthaul approach for the requirement to establish the beginning balance of the additional paid in capital (APIC) pool related to employee compensation. The company determined that it is in a net shortfall position and thus, will start at 0 for the APIC pool in the quarter ending March 31, 2006.

The company uses both stock options and restricted stock as employee incentives. However, the use of stock options is limited to new employee grants and as a component for annual compensation of the company's Chief Executive Officer.

Total stock compensation expense for the three months ended March 31, 2006 was \$1.2 million in the condensed consolidated statements of operations, which included \$0.5 million of restricted stock, \$0.3 million for stock options, \$0.3 million for stock bonuses, and \$0.1 million for our employee stock purchase plan. The company did not realize any tax benefits related to the exercise of stock options or the vesting of restricted stock in the quarter ended March 31, 2006. The impact on net income related to stock-based equity awards was \$1.2 million and \$0.06 per basic and diluted share in the quarter ended March 31, 2006. The following table summarizes the stock based compensation expense by income statement line item:

|                            | THREE MONTHS ENDED<br>MARCH 31,<br>2006<br>----- |
|----------------------------|--|
| Cost of sales              | \$ 77  |
| Research and development   | 145  |
| Sales and marketing        | 224  |
| General and administrative | 703  |
|                            | -----  |
| Total operating expense    | 1,072  |
| Total                      | \$1,149<br>=====                                 |

The company did not capitalize stock-based compensation costs as part of the cost of an asset in the quarter ended March 31, 2006.

Stock Options



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The company issues stock options with exercise prices no less than 100% of the fair value of the company's stock on the grant date. The options contain gradual vesting provisions, whereby 25% vest one year from the date of grant and thereafter in monthly increments over the remaining three years. All unexercised options expire ten years after the date of grant. Prior to 2006, the company used the intrinsic value method to value all stock options issued under these plans, and therefore recorded no compensation expense for these stock options. At January 1, 2006, the company had 0.9 million in unvested stock options outstanding. Beginning in fiscal 2006, the company is recognizing compensation expense on a graded vesting basis. The fair value of each unvested option was estimated based on the date of grant using the Black-Scholes valuation model.

In the quarter ended March 31, 2006, the company issued 134,590 options with a weighted average fair value of \$2.59. Based on this valuation, the company recognized \$45,000 of expense in the quarter ended March 31, 2006 and anticipates that it will recognize \$0.2 million of expense for these options in fiscal year 2006. Total cost recognized in the quarter ended March 31, 2006 for all stock options was \$0.3 million. The company estimates that it will recognize expense of \$0.9 million for stock options in fiscal 2006, net of estimated forfeitures. As of March 31, 2006, the unrecognized compensation expense related to the unvested portion of the company's stock options was approximately \$1.2 million, net of estimated forfeitures to be recognized through 2009 over a weighted average period of 1.6 years.

During the quarter ended March 31, 2006, 58,604 options were exercised. The company received \$0.4 million in proceeds from the exercise of options during the quarter ended March 31, 2006. The company did not realize any tax benefits related to the exercise of stock options in the quarter ended March 31, 2006.

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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 three months ended March 31, 2006 and 2005 are provided below:

|                          | 2006 | 2005 |
|--------------------------|------|------|
|                          | ---- | ---- |
| Dividend yield           | None | None |
| Expected volatility      | 50%  | 36%  |
| Risk-free interest rate  | 4.3% | 3.6% |
| Expected life (in years) | 2.00 | 2.23 |

The risk free interest rate was based on the U.S. Treasury yields with remaining term that approximates the expected life of the options granted. The expected life used for options granted in 2006 was based on historical data of employee exercise performance. Prior to fiscal 2006, the expected life was based on the average life of outstanding options. The estimated volatility for fiscal 2006 was based on the company's historical stock price volatility for the period January 1, 2001 through December 31, 2005. The company believes five years accurately matches the expected term of the options. The company used an expected dividend yield of 0% for all periods because the company has never paid and does not anticipate paying dividends in the foreseeable future. Starting in fiscal 2006, the company used an estimated forfeiture rate based on historical forfeiture data. Prior to fiscal 2006, the company used the actual forfeiture

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method allowed under SFAS No. 123, which assumed that all options vest and pro forma expense was adjusted when options were forfeited. Based on the Black-Scholes option-pricing model, the weighted average estimated fair value of employee stock option grants was \$3.03 for 2005, \$3.63 for 2004, and \$2.79 for 2003.

A summary of the company's stock option activity and related information follows for the quarter ended March 31, 2006:

|                                  | SUMMARY OF<br>OPTION<br>ACTIVITY | WEIGHTED<br>AVERAGE<br>EXERCISE<br>PRICE | WEIGHTED<br>AVERAGE<br>CONTRACTUAL<br>LIFE (YRS) | AGGREGATE<br>INTRINSIC<br>VALUE |
|----------------------------------|----------------------------------|--|--|---------------------------------|
|                                  | -----                            | -----                                    | -----  | -----                           |
| Outstanding at December 31, 2005 | 4,112,881                        | \$ 9.54                                  |  |                                 |
| Granted                          | 134,590                          | 8.56                                     |  |                                 |
| Expired or cancelled             | (70,000)                         | 14.58                                    |  |                                 |
| Forfeited                        | (64,730)                         | 7.95                                     |  |                                 |
| Exercised                        | (58,604)                         | 7.57                                     |  |                                 |
|                                  | -----                            | -----                                    |  |                                 |
| Outstanding at March 31, 2006    | 4,054,137                        | \$ 9.47                                  | 7.40   | \$3,716                         |
| Exercisable at March 31, 2006    | 3,267,372                        | \$ 9.76                                  | 7.07   | \$2,718                         |

The following table summarizes information about stock options outstanding under the 1995 Plan, 1997 Plan, 2001 Plan, Directors Plan and Executive Options at March 31, 2006:

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| RANGE OF<br>EXERCISABLE<br>PRICES | NUMBER OF<br>OUTSTANDING<br>SHARES AT<br>MARCH 31, 2006 | OPTIONS OUTSTANDING                                     |  | OPTIONS EXERCISABLE                        |                                    |
|-----------------------------------|---|---|--|--|------------------------------------|
|                                   |   | WEIGHTED<br>AVERAGE<br>REMAINING<br>CONTRACTUAL<br>LIFE | WEIGHTED<br>AVERAGE<br>EXERCISE<br>PRICE | NUMBER<br>EXERCISABLE AT<br>MARCH 31, 2006 | WEIGHTED AVERAGE<br>EXERCISE PRICE |
| -----                             | -----   | -----   | -----                                    | -----                                      | -----                              |
| \$5.96-\$7.04                     | 421,183   | 6.26  | \$ 6.68                                  | 352,819                                    | \$ 6.69                            |
| \$7.07-\$7.53                     | 483,130   | 7.12  | \$ 7.37                                  | 325,640                                    | \$ 7.38                            |
| \$7.55-\$7.95                     | 543,355   | 6.90  | \$ 7.78                                  | 445,178                                    | \$ 7.78                            |
| \$8.00-\$8.91                     | 399,142   | 8.01  | \$ 8.46                                  | 154,983                                    | \$ 8.27                            |
| \$9.00-\$10.25                    | 607,007   | 7.63  | \$ 9.67                                  | 394,721                                    | \$ 9.87                            |
| \$10.33-\$10.75                   | 452,880   | 7.75  | \$10.70                                  | 450,348                                    | \$10.70                            |
| \$10.80-\$11.56                   | 432,350   | 7.65  | \$11.38                                  | 428,683                                    | \$11.38                            |
| \$11.60-\$13.30                   | 707,500   | 7.78  | \$11.80                                  | 707,500                                    | \$11.80                            |
| \$59.00                           | 7,500   | 3.84  | \$59.00                                  | 7,500                                      | \$59.00                            |
|                                   | -----   |   |  | -----                                      |                                    |
|                                   | 4,054,047   | 7.40  | \$ 9.47                                  | 3,267,372                                  | \$ 9.76                            |

Employee Stock Purchase Plan (ESPP)

Eligible employees are able to purchase common stock at the lower of 85% of

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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. 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 company recognized compensation expense of \$43,000 in the quarter ended March 31, 2006.

The key assumptions used in the valuation model during the three months ended March 31, 2006 and 2005 are provided below:

|                          | EMPLOYEE STOCK<br>PURCHASE PLAN |       |
|--------------------------|---------------------------------|-------|
|                          | 2006                            | 2005  |
| Dividend yield           | None                            | None  |
| Expected volatility      | 50%                             | 36%   |
| Risk-free interest rate  | 4.30%                           | 3.40% |
| Expected life (in years) | 0.5                             | 0.5   |

### Restricted Stock

As part of the company's long-term incentive plans for employees, the company issues restricted stock to officers, key employees, and directors. Each restricted share entitles the participant to one share of the company's common stock on the vesting date. In connection with the grant of restricted stock to employees, the company records deferred stock compensation representing the fair value of the common stock on the date the restricted stock is granted. Compensation expense for restricted stock is recognized on a straight-line basis over the vesting period and is based on the market price of the company's common stock on the grant date. Restricted stock vests based on a service period, typically five years. Starting in the quarter ended March 31, 2006, the company estimated forfeitures based on historical forfeiture data. Prior to 2006, the company used the actual forfeiture method allowed under SFAS No. 123, which assumed that all awards vest and expense was adjusted when restricted stock awards were forfeited. The company recognized stock based compensation expense of \$0.6 million and \$0.4 million in the quarters ended March 31, 2006 and March 31, 2005, respectively.

The company issued 275,000 restricted awards in the quarter ended March 31, 2006 with a value of \$2.3 million. During the quarter ended March 31, 2006, 166,360 shares vested with a value of \$1.5 million. At March 31, 2006, the total unrecognized compensation expense related to restricted stock was approximately \$6.1 million, net of forfeitures to be recognized through 2011 over a weighted average period of 2.5 years. The company did not realize any tax benefits related to the vesting of restricted stock in the quarter ended March 31, 2006.

A summary of the company's restricted stock activity and related information follows for the quarter ended March 31, 2006:

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|                               | RESTRICTED<br>SHARES | WEIGHTED<br>AVERAGE<br>GRANT DATE<br>FAIR VALUE |
|-------------------------------|----------------------|---|
|                               | -----                | -----   |
| Unvested at December 31, 2005 | 1,103,800            | 8.51  |
| Granted                       | 275,000              | 8.48  |
| Vested                        | (166,360)            | 9.37  |
| Cancelled                     | (37,000)             | 8.22  |
|                               | -----                | ----  |
| Unvested at March 31, 2006    | 1,175,440            | 8.39  |

### Short Term Incentive

The bonuses for the company's Short Term Bonus Incentive Plan are paid in shares of the company's common stock. The shares are issued in the first quarter following the end of the fiscal year. The company recorded stock-based compensation expense of \$0.3 million and \$0.2 million for the Short Term Bonus Incentive Plan for the quarters ended March 31, 2006 and March 31, 2005 respectively. In the quarter ended March 31, 2006, the company issued 140,290 shares, net of shares withheld for payment of withholding taxes, for the 2005 Short Term Bonus Incentive Plan and 14,796 shares, net of shares withheld for payment of withholding tax, for the 2005 CEO Stretch Bonus Plan.

### Pro-forma Information

The company applied the provisions of APB 25 to determine our stock-based compensation expense for all periods prior to January 1, 2006. The following table illustrates the effect on net income and net income per share if we had applied the fair value recognition provision of SFAS 123 to our stock-based compensation plans during the three months ended March 31, 2005 (in thousands, except per share data):

|  | THREE MONTHS ENDED<br>MARCH 31, 2005 |
|--|--------------------------------------|
|  | -----                                |
|  | (UNAUDITED)                          |
| Net loss -- as reported  | \$ (2,317)                           |
| Add: Stock-based employee compensation<br>expense included in net loss                                     | \$ 662                               |
| Less: Stock-based employee compensation expense<br>determined under fair value based method for all awards | (4,433)                              |
|  | -----                                |
| Net loss -- proforma   | \$ (6,088)                           |
|  | =====                                |
| Net loss per share -- basic as reported  | \$ (0.12)                            |
| Net loss per share -- basic proforma   | \$ (0.30)                            |
| Net loss per share -- diluted as reported  | \$ (0.12)                            |
| Net loss per share -- diluted proforma   | \$ (0.30)                            |

The pro-forma net loss and pro-forma net loss per share for the quarter ended March 31, 2005 includes the \$3.8 million impact of the acceleration of the underwater options.

### Employee Withholding Taxes on Stock Awards

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Effective 2006, for ease in administering the issuance of stock awards, the company holds back shares to satisfy minimum withholding tax requirements. The company holds back shares of vested restricted stock awards and short-term incentive plan stock awards for the value of the withholding taxes. During the quarter ended March 31, 2006, the company paid \$1.0 million for withholding taxes related to stock awards.

### NOTE 6. STOCK REPURCHASES

In August 2002, the Board of Directors authorized the repurchase of up to 1,000,000 shares of the common stock. In February and November 2003, the company extended the stock repurchase program to repurchase up to 1,000,000 and 500,000 additional

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shares, respectively, on the open market from time to time. During 2005, the company repurchased 86,900 shares for approximately \$0.8 million and during 2004 the company repurchased 461,400 shares of the common stock for approximately \$4.3 million. Since the inception of the stock repurchase program the company has repurchased 2,086,900 shares of the outstanding common stock for approximately \$16.6 million. The company did not repurchase any shares in the quarter ended March 31, 2006. The company is authorized to purchase 413,100 additional shares under the repurchase program.

The following table is a history of the share repurchases by year (\$'s in thousands):

| FISCAL YEAR | SHARES    | AMOUNT   |
|-------------|-----------|----------|
| -----       | -----     | -----    |
| 2002        | 775,800   | \$ 5,282 |
| 2003        | 762,800   | 6,224    |
| 2004        | 461,400   | 4,310    |
| 2005        | 86,900    | 783      |
| Q1 2006     | 0         | 0        |
|             | -----     | -----    |
|             | 2,086,900 | \$16,599 |

### NOTE 7. COMPREHENSIVE INCOME

The following table provides the calculation of other comprehensive income for the three months ended March 31, 2006 and March 31, 2005 (in thousands):

|                                   | THREE MONTHS ENDED |           |
|-----------------------------------|--------------------|-----------|
|                                   | March 31,          |           |
|                                   | -----              | -----     |
|                                   | 2006               | 2005      |
|                                   | -----              | -----     |
|                                   | (UNAUDITED)        |           |
| Net loss                          | \$(2,198)          | \$(2,317) |
| Other comprehensive income:       |                    |           |
| Cumulative translation adjustment | 593                | (18)      |

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|                    |            |            |
|--------------------|------------|------------|
|                    | -----      | -----      |
| Comprehensive loss | \$ (1,605) | \$ (2,335) |
|                    | =====      | =====      |

### NOTE 8. RESTRUCTURING CHARGES

#### 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. This agreement will enable the company to wind down its manufacturing operations at the Dublin facility, terminate 65 redundant employee positions, terminate its facility lease at this location, and reduce its pension obligations to terminated employees. Manufacturing of the discontinued lines of antenna products will be substantially relocated either to a contract manufacturer in St. Petersburg, Russia, or to the company's Antenna Products Group facility in Bloomingdale, Illinois. The process of winding down manufacturing operations in Dublin and relocating the products to their new manufacturing locations is expected to be complete by mid-2006, and the related general and administrative support functions are expected to be eliminated by the end of 2006.

The company will continue to maintain antenna research and development as well as sales and marketing activities in a smaller facility in Dublin to be established during the last quarter of 2006. The company believes that its restructuring activities in Dublin will enable it to improve the gross profit margins of the antenna product lines that were included with the company's acquisition of Sigma Wireless Technologies in July 2005.

The company expects to incur restructuring costs related to the discontinuation of its Dublin manufacturing operations. The categories of costs are: severance pay for employees whose jobs are being made redundant; future minimum lease payments through June 2007 on the existing Dublin facility which will be vacated; and, termination of the employee pension defined benefit plan. The severance, future lease payments, and a portion of the termination of the employee pension defined benefit plan will result in future cash expenditures.

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The company will incur severance costs of approximately \$1.4 million. Approximately \$0.6 million is statutory and is recorded in the first quarter 2006. It is comprised of a gross cost of \$1.4 million less a government rebate of \$0.8 million. The \$1.4 million gross cost is recorded in the balance sheet in Other Accrued Liabilities. The \$0.8 million government rebate is recorded in the balance sheet in Prepaid Expenses and Other Assets. The remaining \$0.8 million will be recorded over the service period of the affected employees. It is anticipated that the future minimum lease payments between the time the facility is vacated and the end of the minimum lease period will be between \$0.1 and \$0.2 million. The company is evaluating the potential credit, if any, which will result in the termination of the pension plan and related payout to the pension members. The estimated pension liability at March 31, 2006 is \$3.1 million. When those costs or credits are known, the company will make additional disclosure.

In connection with the discontinuance of manufacturing operations in the Dublin facility, the company will dispose of certain fixed assets. We currently estimate the net book value of such assets to be in a range between \$0.3 and \$0.5 million. The impairment is non-cash in nature.

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The following table shows the restructuring activity during the three months ended March 31, 2006:

|  | ACCRUAL<br>BALANCE AT<br>DECEMBER 31,<br>2005<br>----- | RESTRUCTURING<br>CHARGES, NET<br>----- | PAYMENTS<br>----- | RECEIPTS<br>----- | A<br>BAL<br>MA<br>----- |
|--|--|--|-------------------|-------------------|-------------------------|
| Severance and employment related costs | \$--   | \$1,381                                | \$--              | \$--              | \$                      |
| Government Rebate                      |  | \$ (828)                               |                   |                   |                         |
|  | ---  | -----                                  | ---               | ---               | -                       |
|  | \$--   | \$ 553                                 | \$--              | \$--              | \$                      |
|  | ===  | =====                                  | ===               | ===               | =                       |

### NOTE 9. CONTINGENCIES

#### WARRANTIES AND SALES RETURNS

The company's APG 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. At March 31, 2006, the company's allowance for sales returns was \$284,000.

The company offers repair and replacement warranties of on average two years for APG products and one year for RFSG products. At March 31, 2006, the company has carried a warranty reserve of \$139,000 for these products based on historical sales and costs of repair and replacement trends.

#### 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 the company, 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. Fraser filed his opening brief in October 2005. The appellant's reply brief was filed in March 2006. We expect the court to schedule an oral argument later this year. The company believes that this appeal is without merit and intends to defend the appeal vigorously. However, the company cannot predict or determine the outcome or resolution of this proceeding or the potential range of loss if any.

#### Litigation with Agere and Lucent

In May 2003, the company filed in the U.S. District Court for the Northern District of California a patent infringement lawsuit against Agere Systems and Lucent Technologies claiming that Agere has infringed four of the company's patents and that Lucent has infringed three of the company's patents. Agere counterclaimed asking for a declaratory judgment that the claims of the four patents are invalid, unenforceable and not infringed by Agere.

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Because of a then-pending reexamination proceeding for PCTEL's U.S. Patent No. 5,787,305 (the '305 patent), the claims against Agere and Lucent relating to the '305 patent were stayed by stipulation of the parties. Claims construction discovery under the Patent Local Rules was taken with respect to the three patents as to which the litigation was not stayed, and the claims construction issues relating to those patents have been briefed to the Court. A hearing on the construction of the claims of those patents was held in May 2005, and the court issued its claim construction ruling in September 2005.

The stay regarding the '305 patent was lifted by stipulation of the parties after the company received the Reexamination Certified from the U.S. Patent Office. Claims construction discovery was taken with respect to the '305 patent. A hearing on the construction of the claims of the '305 patent was held in January 2006 and the court issued its claim construction ruling in March 2006 and scheduled a status conference for late May 2006. The parties have agreed to engage in non-binding mediation. No trial date has been set. Although the company believes that it has meritorious claims and defenses, the company cannot predict or determine the outcome or resolution of this proceeding or the potential range of gain if any.

NOTE 10. INCOME TAXES

For the three months ended March 31, 2006, the company recorded a tax benefit of approximately \$7,000. The company provides a full valuation reserve on its deferred tax assets, provides for deferred tax liabilities related to goodwill that is deductible for tax purposes, and is expected to utilize NOL carryforwards to offset a portion of the expected full year tax liability.

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 has maintained a full valuation allowance against all the deferred tax assets since 2001, as a result of uncertainties regarding whether they will be realized.

NOTE 11. INDUSTRY SEGMENT, CUSTOMER AND GEOGRAPHIC INFORMATION

PCTEL operates in four distinct reportable segments: Antenna Product (antenna), RF Solutions (test), Mobility Solutions (software), and the Licensing segment. Intercompany sales and profits from Antenna Products to RF Solutions are eliminated. The APG segment includes the results of, Sigma Wireless Technologies ("Sigma"), which was acquired in July 2005, for the three months ended March 31, 2006.

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

The results of operations by segment are as follows:

|                                   | APG      | RFSG    | MSG     | LICENSING | ELIMINATION | CONSOLIDATED |
|-----------------------------------|----------|---------|---------|-----------|-------------|--------------|
|                                   | -----    | -----   | -----   | -----     | -----       | -----        |
| (UNAUDITED)                       |          |         |         |           |             |              |
| THREE MONTHS ENDED MARCH 31, 2006 |          |         |         |           |             |              |
| Revenue                           | \$12,388 | \$3,706 | \$2,117 | \$390     | \$(35)      | \$18,566     |
| Gross Profit                      | \$ 3,681 | \$2,578 | \$2,082 | \$385     | \$(4)       | \$ 8,722     |



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|                    |  |  |  |  |  |  |         |
|--------------------|--|--|--|--|--|--|---------|
| Operating Expenses |  |  |  |  |  |  | \$11,5  |
| Operating Loss     |  |  |  |  |  |  | \$ (2,8 |

|                                   | APG      | RFGS    | MSG     | LICENSING | ELIMINATION | CONSOLIDATED |
|-----------------------------------|----------|---------|---------|-----------|-------------|--------------|
|                                   | -----    | -----   | -----   | -----     | -----       | -----        |
| (UNAUDITED)                       |          |         |         |           |             |              |
| THREE MONTHS ENDED MARCH 31, 2005 |          |         |         |           |             |              |
| Revenue                           | \$10,321 | \$3,083 | \$1,122 | \$492     | \$ (10)     | \$15,0       |
| Gross Profit                      | \$ 3,546 | \$2,328 | \$1,080 | \$487     | \$ (3)      | \$ 7,4       |
| Operating Expenses                |          |         |         |           |             | \$10,1       |
| Operating Loss                    |          |         |         |           |             | \$ (2,6      |

The company's revenues to customers outside of the United States, as a percent of total revenues for the three months ended March 31, 2006, are as follows:

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|                         | THREE MONTHS ENDED<br>MARCH 31, |       |
|-------------------------|---------------------------------|-------|
|                         | -----                           | ----- |
| (UNAUDITED)             | 2006                            | 2005  |
|                         | ----                            | ----  |
| Europe                  | 20%                             | 9%    |
| Canada                  | 4%                              | 4%    |
| China & Hong Kong       | 4%                              | 2%    |
| South & Central America | 1%                              | 2%    |
| Taiwan                  | 0%                              | 1%    |
| Other                   | 2%                              | 3%    |
|                         | ----                            | ----  |
|                         | 31%                             | 21%   |
|                         | ====                            | ====  |

The increase in Europe during the quarter ended March 31, 2006 is primarily the result of the product lines acquired from Sigma in July 2005.

Revenue to the company's major customers representing 10% or more of total revenues for the three months ended March 31, 2006:

|                     | THREE MONTHS ENDED<br>MARCH 31, |       |
|---------------------|---------------------------------|-------|
|                     | -----                           | ----- |
| (UNAUDITED)         | 2006                            | 2005  |
| CUSTOMER            | ----                            | ----  |
| -----               | ----                            | ----  |
| Tessco Technologies | 11%                             | 13%   |

Tessco is a customer of the company's APG segment.

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### NOTE 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 of their employment. Under this plan, employees may elect to contribute up to 15% 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 \$151,000 and \$145,000 in employer contributions to the 401(k) plan for the three months ended March 31, 2006 and 2005, respectively.

#### Post-retirement health insurance

In July 2003, the company started a plan to cover post-retirement health insurance for Martin H. Singer, Chairman of the Board and Chief Executive Officer. On January 6, 2006, upon authorization of the Compensation Committee 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 March 31, 2006.

#### Personal Retirement Savings Account

The Personal Retirement Savings Account (PRSA) covers all current Sigma employees. 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 \$3,000 and \$0 for the three months ended March 31, 2006 and 2005, respectively.

#### Pension Plan

Certain Sigma employees participate in the Sigma Communications Group Retirement and Death Benefit Plan ("old plan"). This plan was closed to new employees in December 2003. As part of the acquisition of Sigma in July 2005, the company assumed the liability for the Sigma employee participants in that defined benefit plan. 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

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related to the Sigma participants in the old plan. As part of the restructuring of the Dublin operation, the company intends to terminate the pension plan and make a payout to the pension members. The termination of the pension plan is scheduled to occur in the second half of 2006, but the company is not able at this time to estimate costs or credits for the pension termination. See footnote 8 on restructuring.

The effect on operations of the pension plan for the three months ended March 31, 2006 and 2005, respectively was as follows:

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### PENSION BENEFITS THREE MONTHS ENDED MARCH 31

|                                | 2006  | 2005  |
|--------------------------------|-------|-------|
|                                | ----- | ----- |
| Service costs                  | \$ 55 | --    |
| Interest costs                 | 61    | --    |
| Expected return on plan assets | (46)  | --    |
|                                | ----- | ----- |
| Net periodic expense           | \$ 70 | --    |
|                                | ===== | ====  |

The company made pension contributions of \$38,000 in the quarter ending March 31, 2006.

#### NOTE 13. SIGMA ACQUISITION

On July 4, 2005, the company purchased all of the outstanding shares of Sigma Wireless Technology Limited ("Sigma"). Sigma is based in Dublin, Ireland and develops, manufactures and distributes antenna products designed for public safety and for the UMTS cellular networks. The Sigma acquisition expands the company's product lines within its APG segment. With the acquisition of Sigma, the company gains entry into the growing cellular base station antenna market and also gains a geographic footprint in Europe.

In exchange for all of the outstanding shares of Sigma, the company paid cash consideration of 19.4 million Euro (approximately \$23.1 million), plus assumed an unfunded pension obligation of approximately 2.5 million Euro (approximately \$3.0 million), and incurred approximately 1.7 million Euro (approximately \$2.0 million) in transaction costs. In addition to the cash consideration at closing, the selling stockholders of Sigma may earn up to an additional 7.5 million Euro (approximately \$9.1 million) in cash based on Sigma's revenue performance over the 18-month period ending December 31, 2006. In April 2006, the company outlined a plan to restructure Dublin manufacturing. See footnote 8 related to Dublin restructuring.

The unaudited pro forma affect on the financial results of PCTEL for the three months ended March 31, 2005 as if the acquisition had taken place on January 1, 2005 are as follows:

|   | THREE MONTHS ENDED<br>MARCH 31,<br>2005 |
|---|---|
|   | -----                                   |
| Revenues  | \$17,738                                |
| Loss from Operations                            | \$(3,488)                               |
| Net Loss  | \$(3,253)                               |
| Basic loss per share                            | \$ (0.16)                               |
| Shares used in computing basic loss per share   | 20,043                                  |
| Diluted earnings per share                      | \$ (0.16)                               |
| Shares used in computing diluted loss per share | 20,043                                  |

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### 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. 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," "intends," "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 for many reasons, including the risks faced by us described below and elsewhere in this Quarterly Report, and in other documents we file with the SEC. Factors that might cause future results to differ materially from those discussed in the forward looking statements include, but are not limited to, those discussed in "Factors Affecting Operating Results" and elsewhere in this Quarterly Report.

#### INTRODUCTION

PCTEL is focused on growing wireless revenue and maximizing the monetary value of its intellectual property. The company reports revenue and gross profit for the Antenna Products Group (APG), RF Solutions Group (RFSG), Mobility Solutions Group (MSG), and Licensing as separate product segments.

Growth in wireless product revenue is dependent both on gaining further revenue traction in the existing product profile as well as further acquisitions to support the company's wireless initiatives.

Revenue growth in the APG segment is tied to emerging wireless applications in broadband wireless, in-building wireless, wireless Internet service providers, GPS and Mobile SATCOM. The LMR and on-glass mobile antenna applications represent mature markets. A critical factor for revenue growth is the successful absorption of Sigma Wireless Technologies Limited ("Sigma") acquired in July 2005.

Revenue in the RFSG segment 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. The company has found it necessary to enter into litigation from time to time as a means to bring companies under license. The company is currently in litigation with Agere and Lucent over the use of PCTEL's intellectual property. The company believes this litigation is the single largest opportunity to maximize the monetary value of the company's intellectual property. Licensing revenue is expected to continue to decline due to the expiration of existing licensing arrangements.

#### RESULTS OF OPERATIONS

THREE MONTHS ENDED MARCH 31, 2006

(ALL AMOUNTS IN TABLES, OTHER THAN PERCENTAGES, ARE IN THOUSANDS)

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REVENUES

|                                   | APG      | RFSG    | MSG     | LICENSING | ELIMINATION | CONSOLIDATED |
|-----------------------------------|----------|---------|---------|-----------|-------------|--------------|
| THREE MONTHS ENDED MARCH 31, 2006 |          |         |         |           |             |              |
| Revenue                           | \$12,388 | \$3,706 | \$2,117 | \$ 390    | \$ (35)     | \$18,556     |
| % change from year ago period     | 20.0%    | 20.2%   | 88.7%   | (20.7%)   | NA          | 23%          |

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|                                   |          |         |         |         |         |          |
|-----------------------------------|----------|---------|---------|---------|---------|----------|
| THREE MONTHS ENDED MARCH 31, 2005 |          |         |         |         |         |          |
| Revenue                           | \$10,321 | \$3,083 | \$1,122 | \$ 492  | \$ (10) | \$15,008 |
| % change from year ago period     | 101.9%   | 30.2%   | 0.4%    | (76.6%) | NA      | 40%      |

APG began operations with the purchase of MAXRAD in January 2004. Revenues were supplemented in the fourth quarter of fiscal 2004 with the acquisition of several product lines from Andrew Corporation in October 2004 and in the third quarter of fiscal 2005 with the acquisition of Sigma in July 2005. For the three months ended March 31, 2006, revenue growth excluding the product lines acquired from Sigma was approximately 3% higher than the comparable period of last year. The company experienced softness in some of its mobile antenna product line that adversely affected the organic growth comparison. Approximately 17% of the revenue growth in the quarter-to-quarter comparison was attributable to the product lines acquired from Sigma (iVET and PMR).

RFSG revenues were approximately \$3.7 million in the three months ended March 31, 2006, up approximately 20% from the comparable period in fiscal 2005. The company continued to benefit from the roll out of UMTS networks and the related need for 3G scanners. The segment also benefits when carrier capital spending slows down, and the carriers need greater capacity with their existing infrastructure. The RFSG scanning products enable cellular network engineers to optimize the performance of the current networks.

MSG revenues increased approximately 89% in the three months ended March 31, 2006 compared to the same period in fiscal 2005. The increase in revenues is from growth in established wireless data products and from IMS (IP multimedia subsystem) revenue.

Licensing revenues declined approximately \$0.1 million in the three months ended March 31, 2006 compared to the comparable period in fiscal 2005. This segment continues to be affected by the expiration of older licensing agreements related to modem technology. Absent resolution to the litigations with Agere or Lucent, licensing revenue is expected to be approximately \$0.4 million in the second quarter 2006.

Intercompany sales from APG to RFSG are eliminated in consolidation.

GROSS PROFIT

| APG | RFSG | MSG | LICENSING | ELIMINATION | CONSOLIDATED |
|-----|------|-----|-----------|-------------|--------------|
|-----|------|-----|-----------|-------------|--------------|

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|                                   | -----   | -----   | -----   | -----   | ----- | -----  |
|-----------------------------------|---------|---------|---------|---------|-------|--------|
| THREE MONTHS ENDED MARCH 31, 2006 |         |         |         |         |       |        |
| Gross Profit                      | \$3,681 | \$2,578 | \$2,082 | \$ 385  | \$(4) | \$8,72 |
| Percentage of revenue             | 29.7%   | 69.6%   | 98.3%   | 98.7%   | NA    | 47.    |
| % change from year ago period     | 3.8%    | 10.7%   | 92.8%   | (20.9%) | NA    | 17.    |
| THREE MONTHS ENDED MARCH 31, 2005 |         |         |         |         |       |        |
| Gross Profit                      | \$3,546 | \$2,328 | \$1,080 | \$ 487  | \$(3) | \$7,43 |
| Percentage of revenue             | 34.4%   | 75.5%   | 96.3%   | 99.0%   | NA    | 49.    |
| % change from year ago period     | 65.9%   | 44.1%   | 0.5%    | 76.7%   | NA    | 7.     |

The company's product segments vary significantly in gross profit percent. The decline in overall gross profit as a percentage of revenues compared to the prior year is due primarily to the decline in gross profit percentage of APG products.

Gross profit as a percentage of revenue for APG was 29.7% in the three months ended March 31, 2006, approximately 4.7% lower than the comparable period in fiscal 2005. The addition of product lines from Sigma impacted the gross profit percentage unfavorably by 6.1% in the three months ended March 31, 2006. The discontinuation of Dublin manufacturing and outsourcing to contract manufactures is expected to yield gross margins comparable with the core APG product lines by the fourth quarter of fiscal 2006.

Gross profit as a percentage of revenue for RFSG was 69.6% in the three months ended March 31, 2006, approximately 5.9% lower than the comparable period in fiscal 2005. There was a heavier mix of software in the first quarter of 2005, which produces

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higher margins than the traditional RFS products. The company expects long-term gross profit in this segment to be between 70% and 75%.

Gross profit as a percentage of revenue for MSG was approximately 98.3% and 96.3% for the three months ended March 31, 2006 and March 31, 2005 respectively. The cost of goods sold in the segment relates primarily to third party licenses included in the Roaming Client product. The company expects long-term gross profit in this segment to be in the upper 90% range.

Gross profit as a percentage of revenue for Licensing was 98.7% and 99.0% for the three and nine months ended March 31, 2006 and March 31, 2005, respectively.

RESEARCH AND DEVELOPMENT

|                               | THREE MONTHS ENDED<br>MARCH 31, 2006 | THREE MONTHS ENDED<br>MARCH 31, 2005 |
|-------------------------------|--------------------------------------|--------------------------------------|
|                               | -----                                | -----                                |
| Research and development      | \$2,916                              | \$2,470                              |
| Percentage of revenues        | 15.7%                                | 16.5%                                |
| % change from year ago period | 18.1%                                | 20.1%                                |

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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 \$0.4 million for the three months ended March 31, 2006 compared to the comparable period in 2005. The increase is due to the costs associated with the addition of the Sigma product lines (\$0.3 million) and higher stock compensation expenses (\$0.1 million).

### SALES AND MARKETING

|                               | THREE MONTHS ENDED<br>MARCH 31, 2006<br>----- | THREE MONTHS ENDED<br>MARCH 31, 2005<br>----- |
|-------------------------------|---|---|
| Sales and Marketing           | \$3,543                                       | \$3,115                                       |
| Percentage of revenues        | 19.1%   | 20.8%   |
| % change from year ago period | 13.7%   | 3.8%  |

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 \$0.4 million for the three months ended March 31, 2006 compared to the same period in fiscal 2005. The increase is due to the costs associated with the addition of the Sigma product lines (\$0.4 million).

### GENERAL AND ADMINISTRATIVE

|                               | THREE MONTHS ENDED<br>MARCH 31, 2006<br>----- | THREE MONTHS ENDED<br>MARCH 31, 2005<br>----- |
|-------------------------------|---|---|
| General and Administrative    | \$3,748                                       | \$4,167                                       |
| Percentage of revenues        | 20.2%   | 27.8%   |
| % change from year ago period | (10.1%)                                       | 22.8%   |

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 decreased approximately \$0.4 million for the three months ended March 31, 2006 compared to the same period in fiscal 2005 due to lower legal expenses, professional service fees, and reversal of CEO retirement benefits, offset by higher stock compensation expenses and the costs associated with the addition of the product lines from Sigma.

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### AMORTIZATION OF OTHER INTANGIBLE ASSETS

|   | THREE MONTHS ENDED<br>MARCH 31, 2006 | THREE MONTHS ENDED<br>MARCH 31, 2005 |
|---|--------------------------------------|--------------------------------------|
|   | -----                                | -----                                |
| Amortization of other intangible assets | \$1,037                              | \$883                                |
| Percentage of revenues                  | 5.6%                                 | 5.9%                                 |

The amortization of intangible assets relates to DTI in 2003, MAXRAD in January 2004, the antenna product lines from Andrew Corporation in October 2004, and Sigma in July 2005. The \$0.2 million increase for amortization in the three months ended March 31, 2006 is due to the impact of the third quarter fiscal 2005 acquisition of Sigma.

### RESTRUCTURING CHARGES

|                        | THREE MONTHS ENDED<br>MARCH 31, 2006 | THREE MONTHS ENDED<br>MARCH 31, 2005 |
|------------------------|--------------------------------------|--------------------------------------|
|                        | -----                                | -----                                |
| Restructuring Charges  | \$553                                | \$ --                                |
| Percentage of revenues | 3.0%                                 | 0.0%                                 |

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. This agreement will enable the company to wind down its manufacturing operations at the Dublin facility, terminate 65 redundant employee positions, terminate its facilities lease at this location, and reduce its pension obligations to terminated employees. Manufacturing of the discontinued lines of antenna products will be substantially relocated either to a contract manufacturer in St. Petersburg, Russia, or to the company's Antenna Products Group facility in Bloomingdale, Illinois. The process of winding down manufacturing operations in Dublin and relocating the products to their new manufacturing locations is expected to be complete by mid- 2006, and the related general and administrative support functions are expected to be eliminated by the end of 2006.

The company will continue to maintain antenna research and development as well as sales and marketing activities in a smaller facility in Dublin to be established during the last quarter of 2006. The company believes that its restructuring activities in Dublin will enable it to improve the gross profit margins of the antenna product lines that were included with the company's acquisition of Sigma Wireless Technologies in July 2005.

The company expects to incur restructuring costs related to the discontinuation of its Dublin manufacturing operations. The categories of costs are: severance pay for employees whose jobs are being made redundant; future minimum lease payments through June 2007 on the existing Dublin facility which will be vacated; and, termination of the employee pension defined benefit plan. The severance, future lease payments, and a portion of the termination of the employee pension defined benefit plan will result in future cash expenditures.



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The company will incur severance costs of approximately \$1.4 million. Approximately \$0.6 million is statutory and is recorded in the first quarter 2006. It is comprised of a gross cost of \$1.4 million less a government rebate of \$0.8 million. The \$1.4 million gross cost is recorded in the balance sheet in Other Accrued Liabilities. The \$0.8 million government rebate is recorded in the balance sheet in Prepaid Expenses And Other Assets. The remaining \$0.8 million will be recorded over the service period of the affected employees. It is anticipated that the future minimum lease payments between the time the facility is vacated and the end of the minimum lease period will be between \$0.1 and \$0.2 million. The company is still evaluating the potential credit, if any, which would be incurred with the termination of the pension plan and related payout to the pension members. It is not in a position at this time to estimate costs or credits for the pension termination. When those costs or credits are known, the company will make additional disclosure.

In conjunction with the discontinuance of manufacturing operations in the Dublin facility, the company will dispose of fixed assets no longer required. It anticipates the net book value of such assets to be in a range between \$0.3 and \$0.5 million. The impairment is non-cash in nature.

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### GAIN ON SALE OF ASSETS AND RELATED ROYALTIES

|  | THREE MONTHS ENDED<br>MARCH 31, 2006 | THREE MONTHS ENDED<br>MARCH 31, 2005 |
|--|--------------------------------------|--------------------------------------|
|  | -----                                | -----                                |
| Gain on sale of assets and related royalties | \$250                                | \$500                                |
| Percentage of revenues                       | 1.3%                                 | 3.3%                                 |

For the three months ended March 31, 2006, the gain on sale of assets and related royalties consists of \$0.3 million for Conexant royalties. The company recorded royalties of \$0.5 million from Conexant in the first quarter of fiscal 2005. The company renegotiated the royalty agreement with Conexant in the third quarter of 2005 whereby the cap on the quarterly payments was lowered but the term of the agreement was extended.

### OTHER INCOME, NET

|                        | THREE MONTHS ENDED<br>MARCH 31, 2006 | THREE MONTHS ENDED<br>MARCH 31, 2005 |
|------------------------|--------------------------------------|--------------------------------------|
|                        | -----                                | -----                                |
| Other income, net      | \$620                                | \$541                                |
| Percentage of revenues | 3.3%                                 | 3.6%                                 |

Other income, net, consists primarily of interest income, and also foreign exchange gains and losses. Interest income increased for the three months ended March 31, 2006 compared to the same periods in fiscal 2005 due to higher interest rates.

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### PROVISION (BENEFIT) FOR INCOME TAXES

|                         | THREE MONTHS ENDED<br>MARCH 31, 2006 | THREE MONTHS ENDED<br>MARCH 31, 2005 |
|-------------------------|--------------------------------------|--------------------------------------|
| Provision (benefit) for |                                      |                                      |
| income taxes            | \$ (7)                               | \$ 161                               |
| Effective Tax Rate      | 0.3%                                 | (7.5%)                               |

The tax rate for the three months ended March 31, 2006 and March 31, 2005, respectively differs from the statutory rate of 35% because the company provides a full valuation reserve on its deferred tax assets, provides for deferred tax liabilities related to goodwill that is deductible for tax purposes, and is expected to utilize NOL carryforwards to offset a portion of the expected full year tax liability.

The Company regularly evaluates its estimates and judgments related to uncertain tax positions and, when necessary, establishes contingency reserves to account for its 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

On January 1, 2006, the company adopted SFAS No. 123(R), which requires the measurement and recognition of compensation expense for all share-based awards based on estimated fair values. In the three months ended March 31, 2006, the company recognized stock-based compensation expense of \$1.2 million in the condensed consolidated statements of operations, which included \$0.5 million of restricted stock, \$0.3 million for stock options, \$0.3 million for stock bonuses, and \$0.1 million for our employee stock purchase plan. Prior to the adoption of SFAS No. 123(R), the company accounted for stock-based awards using the intrinsic value method in accordance with APB 25 as allowed under SFAS No. 123. As a result, stock options had no intrinsic value on their grant dates, and the company did not record any compensation expense for stock options. Prior to the adoption of SFAS No. 123(R), the company did not record any compensation expense for the employee stock purchase plan, which was deemed non-compensatory.

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The company estimates compensation expense of \$0.9 million, net of forfeitures in 2006 related to stock options and \$0.2 million compensation expense in 2006 related to the employee stock purchase plan. The company will continue to use both stock options as a long-term employee incentive. However, the use of stock options is currently limited to new employee grants and as a component for annual compensation of the company's Chief Executive Officer. The company will emphasize restricted stock for employee incentives.

In the three months ended March 31, 2005, the company recorded stock-based compensation expense of \$0.7 million, including \$0.4 million for restricted stock and \$0.2 million for stock bonuses. The following table summarizes the stock based compensation expense by income statement line item for the three

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months ended March 31, 2006 and March 31, 2005, respectively:

|                            | THREE MONTHS ENDED<br>MARCH 31, 2006<br>----- | THREE MONTHS ENDED<br>MARCH 31, 2005<br>----- |
|----------------------------|---|---|
| Cost of sales              | \$ 77   | \$ 2  |
| Research and development   | 145   | 50  |
| Sales and marketing        | 224   | 133   |
| General and administrative | 703   | 477   |
|                            | -----   | -----   |
| Total operating expense    | 1,072   | 660   |
| Total                      | \$1,149<br>=====                              | \$662<br>=====                                |

### LIQUIDITY AND CAPITAL RESOURCES

|   | THREE MONTHS ENDED<br>MARCH 31, 2006<br>----- | THREE MONTHS ENDED<br>MARCH 31, 2005<br>----- |
|---|---|---|
| Net cash provided by (used in) operating activities | \$ 480  | \$ (85)                                       |
| Net cash used in investing activities               | (450)   | (395)   |
| Net cash (used in) provided by financing activities | (342)   | 380   |
| Cash, cash equivalents at the end of period         | 58,622  | 83,769  |
| Working capital at the end of period                | 69,018  | 87,003  |

The company's operating activities provided approximately \$0.5 million of net cash for the three months ended March 31, 2006. The increase in cash from operating activities for the three months ended March 31, 2006 compared to the three months ended March 31, 2005 is due to positive cash flow changes in both prepaid expenses and other assets, and accrued liabilities. The positive cash flow from prepaid expenses and other assets is primarily due to a federal income tax refund received in the three months ended March 31, 2006. Cash flow related to accrued liabilities was negative in the three months ended March 31, 2005 due to the payout of retention bonuses related to the DTI acquisition. The company used approximately \$0.5 million for investing activities during the three months ended March 31, 2006. The company used approximately \$0.8 million for capital expenditures, offsetting proceeds from royalties of \$0.2 and sale of fixed assets of \$0.1 million. For the three months ended March 31, 2006, financing activities included \$1.0 million for the payment of withholding tax on stock-based compensation offsetting approximately \$0.7 million of proceeds for the issuance of common stock related to stock option exercises and shares purchased through the Employee Stock Purchase Plan.

As of March 31, 2006, the company had approximately \$58.6 million in cash and cash equivalents and working capital of approximately \$69.0 million. The decline in the cash balance and working capital compared to the three months ended March 31, 2005 is due primarily to the acquisition of Sigma.

The company believes that the existing sources of liquidity, consisting of cash and cash from operations, will be sufficient to meet the working capital needs for the foreseeable future. The company will continue to evaluate opportunities for development of new products and potential acquisitions of

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technologies or businesses that could complement the business. The company may use

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available cash or other sources of funding for such purposes.

### CONTRACTUAL OBLIGATIONS AND COMMERCIAL COMMITMENTS

The following summarizes the contractual lease obligations for office and product assembly facilities, motor vehicles, and equipment and the effect such obligations are expected to have on the liquidity and cash flows in future periods (in thousands):

|                      | Total   | Less than<br>1 year | 1-3 years | 4-5 years | After<br>5 years |
|----------------------|---------|---------------------|-----------|-----------|------------------|
|                      | -----   | -----               | -----     | -----     | -----            |
| Leases               | \$5,084 | \$1,210             | \$2,500   | \$956     | \$418            |
| Purchase commitments | 135     | 135                 |           |           |                  |
|                      | -----   | -----               | -----     | -----     | -----            |
| Total obligations    | 5,219   | 1,345               | 2,500     | 956       | 418              |

These obligations for leases include \$116,000 related to capital leases for motor vehicles and manufacturing equipment in Dublin, Ireland.

In the quarter ended March 31, 2006, the company relocated its RFSG operations to a new leased facility in Germantown, Maryland. The company is still obligated for the operating lease on Wisteria Drive in Germantown, Maryland through July 2007. The company recorded an expense of \$0.2 million in the quarter ended March 31, 2006 for the remaining net lease obligation.

The company has a remaining firm purchase contract for \$135,000 with an RFSG software supplier. The quantity committed represents the lifetime requirements for this software. The company has no other firm inventory purchase contract commitments with major suppliers beyond near term needs.

As part of the acquisition of Sigma, the selling stockholders of Sigma may earn up to an additional 7.5 million Euro (approximately \$9.1 million) in cash based on Sigma's revenue performance over the 18-month period ending December 31, 2006. The company believes that such a payout for Sigma's revenue performance is unlikely.

In April 2006, the company announced a restructuring plan for Dublin manufacturing. As part of the restructuring, the company will terminate the pension plan related to its Dublin employees in the quarter ending June 30, 2006. The financial obligation from this pension termination and financial statement impact are not known at this time. See footnote 8 related to the company's restructuring plan.

### CHANGE IN CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The company uses 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 its Annual Report on Form 10-K filed with the Securities and Exchange Commission for the year ended December

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31, 2005.

### Accounting policies

The company adopted SFAS No. 123(R), "Share Based Payments," during the three months ended March 31, 2006. SFAS No. 123(R), which requires the measurement and recognition of compensation expense for all share-based awards based on estimated fair values. Our share-based awards include stock options, restricted stock awards, stock bonuses, and the company's Employee Stock Purchase Plan. Prior to the adoption of SFAS No. 123(R), the company accounted for stock-based awards using the intrinsic value method in accordance with APB 25 as allowed under SFAS No. 123. As a result, stock options had no intrinsic value on their grant dates, and the company did not record any compensation expense for stock options. The company has elected to use the modified prospective transition method to adopt SFAS No. 123(R). Under this transition method starting in 2006, compensation expense will include 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).

The company uses the Black-Scholes model to estimate the fair value of our options awards and employee stock purchase rights issued under our Employee Stock Purchase Plan. Based on this valuation, the company is recognizing compensation expense for stock options on a graded vesting basis. The Black-Scholes model requires estimates of the expected term of the option, future

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volatility, and the risk-free interest rate. See footnote 5 related to stock-based compensation. In addition to the assumptions used to calculate the fair value of our options, the company is required to estimate the expected forfeiture rate of all share-based award and only recognize expense for those awards we expect to vest. The stock-based compensation expense recognized in our condensed consolidated statements of operations has been reduced for estimated forfeitures.

### Estimates

This discussion and analysis of financial condition and results of operations is based on the company's condensed consolidated financial statements, which have been prepared in conformity with accounting principles generally accepted in the United States. The preparation of these financial statements requires the use of estimates and assumptions related to the reporting of assets, liabilities, revenues, expenses and related disclosures. In preparing these financial statements, the company has made its best estimates and judgments of certain amounts included in the financial statements. Estimates are revised periodically. Actual results could differ from these estimates.

### ITEM 3: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The company is exposed to market risk from changes in interest rates and foreign exchange rates.

#### INTEREST RATE RISK

We manage the sensitivity of our results of operations to credit risks and interest rate risk by maintaining a conservative investment portfolio. The

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primary objective of our investment activities is to preserve principal without significantly increasing risk. To achieve this objective, we maintain our portfolio of cash equivalents in money market funds, which are fixed at \$1 per share and for which only the yield fluctuates. Due to changes in interest rates, our future investment income may fall short of expectations. Since the company invests in money market funds, we have no unrealized holding gains or losses as of March 31, 2006 and 2005, respectively. A hypothetical increase or decrease of 10% in market interest rates would not result in a material change in interest income earned through maturity on investments held at March 31, 2006. We do not hold or issue derivative, derivative commodity instruments or other financial instruments for trading purposes.

### FOREIGN CURRENCY RISK

We are exposed to currency fluctuations, as we sell our products internationally. We manage the sensitivity of our international sales by denominating the majority of transactions in U.S. dollars. Beginning in July 2005, our results include commercial activity by Sigma. Sigma transactions are denominated primarily in pounds sterling and Euro. If the United States dollar uniformly increased or decreased in strength by 10% relative to the currencies in which our sales were denominated, our net loss would not have changed by a material amount for the three months ended March 31, 2006. For purposes of this calculation, we have assumed that the exchange rates would change in the same direction relative to the United States dollar. Our exposure to foreign exchange rate fluctuations, however, arises in part from translation of the financial statements of foreign subsidiaries into U.S. dollars in consolidation. As exchange rates vary, these results, when translated, may vary from expectations and adversely impact overall expected profitability. The effect of foreign exchange rate fluctuation gains for the three months ended March 31, 2006 and 2005 was positive \$593,000 and negative 18,000, respectively.

### ITEM 4: CONTROLS AND PROCEDURES

#### (A) EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES

As of the end of the period covered by this report, under the supervision and with the participation of PCTEL management, including the company's Chief Executive Officer and its Chief Financial Officer, management evaluated the effectiveness of the company's disclosure controls and procedures, as such term is defined under Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended. Based on that evaluation, the company's Chief Executive Officer and its Chief Financial Officer concluded that the company's disclosure controls and procedures were ineffective as of March 31, 2006 because of the material weakness originally identified in the fourth quarter of 2004 (discussed below). In light of the material weakness described below, the company performed additional analysis and other post-closing procedures to ensure our financial statements are prepared in accordance with generally accepted accounting principles. Accordingly, management believes that the financial statements included in this report fairly present in all material respects our financial condition, results of operations and cash flows for the periods presented.

A material weakness is a control deficiency, or combination of control deficiencies, that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. As of December 31, 2004 and December 31, 2005, the company did not maintain effective controls over the accounting for income taxes, including the determination of income taxes payable, deferred income tax assets and

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liabilities and the related income tax provision. Specifically, the company did not have effective controls over determining net operating loss carrybacks, applicable state tax rates applied, and the tax effect of stock option exercises. In addition, the company did not have effective controls to monitor the difference between the income tax basis and the financial reporting basis of assets and liabilities and reconcile the difference to deferred income tax assets and liabilities. This control deficiency resulted in audit adjustments to the financial statements for the fourth quarter 2004, to the 2005 annual consolidated financial statements with respect to income tax disclosures, and the 2005 second quarter consolidated financial statements with respect to the provision for income taxes. Additionally, this control deficiency could result in a misstatement of income taxes payable, deferred income tax assets and liabilities and the related income tax provision, that would result in a material misstatement to annual or interim financial statements that would not be prevented or detected. Accordingly, management has determined that this control deficiency constituted a material weakness. The remediation plan for the material weakness identified at December 31, 2004 and December 31, 2005 is described below. Because the remediation of this material weakness is still in process, the company's Chief Executive Officer and its Chief Financial Officer has concluded that the company did not maintain effective internal control over financial reporting as of March 31, 2006, based on criteria in "Internal Control-Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Management has excluded Sigma from its assessment of the effectiveness of internal control over financial reporting as of December 31, 2005 because Sigma was acquired by the company through a purchase business combination in July 2005. Sigma is a wholly owned subsidiary of the company that represents 21% of consolidated total assets and 9% of consolidated revenues, respectively, as of and for the three months ended March 31, 2006.

### (B) CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING

The company made significant progress during the year ended December 31, 2005 in executing the remediation plans that were established to address the material weakness in its internal control surrounding the accounting for income taxes. This resulted in certain improvements in the company's internal control over financial reporting. With the help of external advisors (other than the company's independent registered public accounting firm), the following remedial actions have been undertaken:

- Engaged an outside tax consultant to prepare the tax provision, provide tax expertise and expertise in the application of Statement of Financial Accounting Standards No. 109 "Accounting for Income Taxes".
- Implemented an internal training program to enhance the capabilities of its internal tax personnel.
- Acquired software to automate and better control the tax provision preparation process.
- Improved its system of internal controls over the review of the consolidated income tax provision.

Specifically, the Company's changes in controls over income taxes were successful in the remediation of the deficiencies related to the determination of income tax payable and deferred income tax assets and liabilities.

As demonstrated by the above, the company has made significant progress in its efforts to remediate this material weakness during 2005 and the first quarter ended March 31, 2006. This is evidenced by the company's overall positive results from its 2005 internal control compliance testing required by

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Section 404 of the Sarbanes-Oxley Act of 2002, which was carried out by the Company in the third and fourth quarters of 2005. In making its determination as to the status of the remediation of this material weakness, the company has considered all of the factors outlined above and has concluded that the internal controls surrounding the accounting for income taxes are effectively designed, however, as a result of the audit adjustments in 2004 and 2005, the company has not demonstrated operating effectiveness with respect to controls over the completeness and accuracy of its income tax provision and the presentation and disclosures related to income taxes. The remediation efforts are in process, but have not been completed as of March 31, 2006.

In order to remediate this deficiency in internal controls, the company will continue its training and education efforts in this area so that operating effectiveness can be demonstrated over a period of time that is sufficient to support the conclusion that the material weakness has been remediated. In addition, to further enhance the controls surrounding the accounting for income taxes, the Company will continue its efforts with respect to 1) its oversight over the quarterly and annual preparation of its tax provision and related disclosures by its outside tax consultant, and 2) the need to consider additional resources to help execute its internal controls over the accounting for income taxes.

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Except as otherwise discussed above, there have been no changes in the company's internal control over financial reporting during the most recently completed fiscal quarter that have materially affected, or are 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 the company, 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. Fraser filed his opening brief in October 2005. The appellant's reply brief was filed in March 2006. We expect the court to schedule an oral argument later this year. The company believes that this appeal is without merit and intends to defend the appeal vigorously. However, the company cannot predict or determine the outcome or resolution of this proceeding or the potential range of loss if any.

#### Litigation with Agere and Lucent

In May 2003, the company filed in the U.S. District Court for the Northern District of California a patent infringement lawsuit against Agere Systems and Lucent Technologies claiming that Agere has infringed four of the company's patents and that Lucent has infringed three of the company's patents. Agere counterclaimed asking for a declaratory judgment that the claims of the four patents are invalid, unenforceable and not infringed by Agere.



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Because of a then-pending reexamination proceeding for PCTEL's U.S. Patent No. 5,787,305 (the '305 patent), the claims against Agere and Lucent relating to the '305 patent were stayed by stipulation of the parties. Claims construction discovery under the Patent Local Rules was taken with respect to the three patents as to which the litigation was not stayed, and the claims construction issues relating to those patents have been briefed to the Court. A hearing on the construction of the claims of those patents was held in May 2005, and the court issued its claim construction ruling in September 2005.

The stay regarding the '305 patent was lifted by stipulation of the parties after the company received the Reexamination Certified from the U.S. Patent Office. Claims construction discovery was taken with respect to the '305 patent. A hearing on the construction of the claims of the '305 patent was held in January 2006 and the court issued its claim construction ruling in March 2006 and scheduled a status conference for late May 2006. The parties have agreed to engage in non-binding mediation. No trial date has been set. Although the company believes that it has meritorious claims and defenses, the company cannot predict or determine the outcome or resolution of this proceeding or the potential range of gain if any.

### ITEM 1A: RISK FACTORS

This quarterly report on Form 10-Q, including this Management's Discussion and Analysis, contains forward-looking statements. These forward-looking statements are subject to substantial risks and uncertainties that could cause our future business, financial condition or results of operations to differ materially from our historical results or currently anticipated results, including those set forth below.

#### RISKS RELATED TO OUR BUSINESS

COMPETITION WITHIN THE WIRELESS CONNECTIVITY PRODUCTS INDUSTRIES IS INTENSE AND IS EXPECTED TO INCREASE SIGNIFICANTLY. OUR FAILURE TO COMPETE SUCCESSFULLY COULD MATERIALLY HARM OUR PROSPECTS AND FINANCIAL RESULTS.

The wireless products connectivity markets are intensely competitive. We may not be able to compete successfully against current or potential competitors. We expect competition to increase in the future as current competitors enhance their product offerings, new suppliers enter the wireless connectivity products markets, new communication technologies are introduced and additional networks are deployed. Our client software competes with software developed internally by Network Interface Card (NIC) vendors, service providers for 802.11 networks, and with software developed by large systems integrators. Increased competition could materially and adversely affect our business and operating results through pricing pressures, the loss of market

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share and other factors.

The antenna market is highly fragmented and is served by many local product providers. We may not be able to displace established competitors from their customer base with our products. We may not achieve the design wins necessary to participate in WCDMA network deployments where our products compete. Where we have design wins, we may not be the sole source supplier or may receive only a small portion of the business from each customer.

Many of our present and potential competitors have substantially greater

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financial, marketing, technical and other resources with which to pursue engineering, manufacturing, marketing, and distribution of their products. These competitors may succeed in establishing technology standards or strategic alliances in the connectivity products markets, obtain more rapid market acceptance for their products, or otherwise gain a competitive advantage. We can offer no assurance that we will succeed in developing products or technologies that are more effective than those developed by our competitors. We can offer no assurance that we will be able to compete successfully against existing and new competitors as the connectivity wireless markets evolve and the level of competition increases.

OUR ABILITY TO GROW OUR BUSINESS MAY BE THREATENED IF THE DEMAND FOR WIRELESS DATA SERVICES DOES NOT CONTINUE TO GROW.

Our ability to compete successfully in the wireless market is dependent on the continued trend toward wireless telecommunications and data communications services. If the rate of growth slows and service providers reduce their capital investments in wireless infrastructure or fail to expand into new geographic markets, our revenue may decline. Wireless data solutions are relatively unproven in the marketplace and some of the wireless technologies have only been commercially introduced in the last few years. We began offering wireless products in the second quarter of fiscal 2002. If wireless data access technology turns out to be unsuitable for widespread commercial deployment, we may not be able to generate enough sales to achieve and grow our business. We have listed below some of the factors that we believe are key to the success or failure of wireless access technology:

- reliability and security of wireless access technology and the perception by end-users of its reliability and security,
- capacity to handle growing demands for faster transmission of increasing amounts of data, voice and video,
- the availability of sufficient frequencies for network service providers to deploy products at commercially reasonable rates,
- cost-effectiveness and performance compared to wire line or other high speed access solutions, whose prices and performance continue to improve,
- suitability for a sufficient number of geographic regions, and
- availability of sufficient site locations for wireless access.

The factors listed above influence our customers' purchase decisions when selecting wireless versus other high-speed data access technology. Future legislation, legal decisions and regulation relating to the wireless telecommunications industry may slow or delay the deployment of wireless networks.

Wireless access solutions compete with other high-speed access solutions such as digital subscriber lines, cable modem technology, fiber optic cable and other high-speed wire line and satellite technologies. If the market for our wireless solutions fails to develop or develops more slowly than we expect due to this competition, our sales opportunities will be harmed. Many of these alternative technologies can take advantage of existing installed infrastructure and are generally perceived to be reliable and secure. As a result, they have already achieved significantly greater market acceptance and penetration than wireless data access technologies. Moreover, current wireless data access technologies have inherent technical limitations that may inhibit their widespread adoption in many areas.

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We expect wireless data access technologies to face increasing competitive pressures from both current and future alternative technologies. In light of these factors, many service providers may be reluctant to invest heavily in wireless data access solutions, including Wi-Fi. If service providers do not continue to establish Wi-Fi "hot spots," we may not be able to generate sales for our Wi-Fi products and our revenue may decline.

OUR WIRELESS BUSINESS IS DEPENDENT UPON THE CONTINUED GROWTH OF EVOLVING TELECOMMUNICATIONS AND INTERNET INDUSTRIES.

Our future success is dependent upon the continued growth of the data communications and wireless industries, particularly

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with regard to Internet usage. The global data communications and Internet industries are relatively new and evolving rapidly and it is difficult to predict potential growth rates or future trends in technology development for this industry. The deregulation, privatization and economic globalization of the worldwide telecommunications market that have resulted in increased competition and escalating demand for new technologies and services may not continue in a manner favorable to us or our business strategies. In addition, the growth in demand for wireless and Internet services, and the resulting need for high speed or enhanced data communications products and wireless systems, may not continue at its current rate or at all.

OUR FUTURE SUCCESS DEPENDS ON OUR ABILITY TO DEVELOP AND SUCCESSFULLY INTRODUCE NEW AND ENHANCED PRODUCTS FOR THE WIRELESS MARKET, WHICH MEET THE NEEDS OF CUSTOMERS.

Our revenue depends on our ability to anticipate our existing and prospective customers' needs and develop products that address those needs. Our future success will depend on our ability to introduce new products for the wireless market, anticipate improvements and enhancements in wireless technology and wireless standards, and to develop products that are competitive in the rapidly changing wireless industry. Introduction of new products and product enhancements will require coordination of our efforts with those of our customers, suppliers, and manufacturers to rapidly achieve volume production. If we fail to coordinate these efforts, develop product enhancements or introduce new products that meet the needs of our customers as scheduled, our operating results will be materially and adversely affected and our business and prospects will be harmed. We cannot assure you that product introductions will meet the anticipated release schedules or that our wireless products will be competitive in the market. Furthermore, given the emerging nature of the wireless market, there can be no assurance our products and technology will not be rendered obsolete by alternative or competing technologies.

WE MAY EXPERIENCE INTEGRATION OR OTHER PROBLEMS WITH POTENTIAL ACQUISITIONS, WHICH COULD HAVE AN ADVERSE EFFECT ON OUR BUSINESS OR RESULTS OF OPERATIONS. NEW ACQUISITIONS COULD DILUTE THE INTERESTS OF EXISTING STOCKHOLDERS, AND THE ANNOUNCEMENT OF NEW ACQUISITIONS COULD RESULT IN A DECLINE IN THE PRICE OF OUR COMMON STOCK.

We may in the future make acquisitions of, or large investments in, businesses that offer products, services, and technologies that we believe would complement our products or services, including wireless products and technology. We may also make acquisitions of, or investments in, businesses that we believe could expand our distribution channels. Even if we were to announce an acquisition, we may not be able to complete it. Additionally, any future

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acquisition or substantial investment would present numerous risks, including:

- difficulty in integrating the technology, operations, internal accounting controls or work force of the acquired business with our existing business,
- disruption of our on-going business,
- difficulty in realizing the potential financial or strategic benefits of the transaction,
- difficulty in maintaining uniform standards, controls, procedures and policies,
- dealing with tax, employment, logistics, and other related issues unique to international organizations and assets we acquire,
- possible impairment of relationships with employees and customers as a result of integration of new businesses and management personnel, and
- impairment of assets related to resulting goodwill, and reductions in our future operating results from amortization of intangible assets.

We expect that future acquisitions could provide for consideration to be paid in cash, shares of our common stock, or a combination of cash and our common stock. If consideration for a transaction is paid in common stock, this would further dilute our existing stockholders.

WE MAY NEVER ACHIEVE THE ANTICIPATED BENEFITS FROM OUR RECENT ACQUISITION OF SIGMA WIRELESS TECHNOLOGIES.

We acquired Sigma Wireless Technologies in July 2005 as part of our continuing efforts to expand our wireless line and product offerings. We may experience difficulties in achieving the anticipated benefits of this acquisition. This acquisition represents an expansion for our Antenna Products Group. Potential risks with this acquisitions includes:

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- the loss or decrease in orders of one or more of the major customers,
- delay in 3G network deployments utilizing acquired products,
- decrease in demand for wireless devices that use the acquired products,
- lack of acceptance for electrical tilt antenna products in general
- the ability to realize gross and operating margins necessary to achieve targeted results
- difficulties in assimilation of related personnel, operations, technologies or products, and
- challenges in integrating internal accounting and financial controls for financial reporting purposes.

OUR GROSS PROFIT MAY VARY BASED ON THE MIX OF SALES OF OUR PRODUCTS AND LICENSES OF OUR INTELLECTUAL PROPERTY, AND THESE VARIATIONS MAY CAUSE OUR NET INCOME TO

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DECLINE.

We derive a portion of our sales from our software-based connectivity products. Due in part to the competitive pricing pressures that affect our products and in part to increasing component and manufacturing costs, we expect gross profit from both existing and future products to decrease over time. In addition, licensing revenues from our intellectual property historically have provided higher margins than our product sales. Changes in the mix of products sold and the percentage of our sales in any quarter attributable to products as compared to licensing revenues could cause our quarterly results to vary and could result in a decrease in gross profit and net income.

ANY DELAYS IN OUR NORMALLY LENGTHY SALES CYCLES COULD RESULT IN CUSTOMERS CANCELING PURCHASES OF OUR PRODUCTS.

Sales cycles for our products with major customers are lengthy, often lasting nine months or longer. In addition, it can take an additional nine months or more before a customer commences volume production of equipment that incorporates our products. Sales cycles with our major customers are lengthy for a number of reasons, including:

- our original equipment manufacturer customers and carriers usually complete a lengthy technical evaluation of our products, over which we have no control, before placing a purchase order,
- the commercial introduction of our products by an original equipment manufacturer and carriers is typically limited during the initial release to evaluate product performance, and
- the development and commercial introduction of products incorporating new technologies frequently are delayed.

A significant portion of our operating expenses is relatively fixed and is based in large part on our forecasts of volume and timing of orders. The lengthy sales cycles make forecasting the volume and timing of product orders difficult. In addition, the delays inherent in lengthy sales cycles raise additional risks of customer decisions to cancel or change product phases. If customer cancellations or product changes were to occur, this could result in the loss of anticipated sales without sufficient time for us to reduce our operating expenses.

OUR REVENUES MAY FLUCTUATE EACH QUARTER DUE TO BOTH DOMESTIC AND INTERNATIONAL SEASONAL TRENDS.

The connectivity products market is too new for us to be able to predict seasonal revenue patterns. Such patterns are also true for wireless test and measurements products, such as those produced by our RF Solutions Group, where capital spending is involved.

We are currently expanding our sales in international markets, particularly in Europe and Asia. To the extent that our revenues in Europe and Asia or other parts of the world increase in future periods, we expect our period-to-period revenues to reflect seasonal buying patterns in these markets.

WE RELY ON INDEPENDENT COMPANIES TO MANUFACTURE, ASSEMBLE AND TEST OUR PRODUCTS. IF THESE COMPANIES DO NOT MEET THEIR COMMITMENTS TO US, OUR ABILITY TO SELL PRODUCTS TO OUR CUSTOMERS WOULD BE IMPAIRED.

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We have limited manufacturing capability. For some product lines we outsource the manufacturing, assembly, and testing of printed circuit board subsystems. For other product lines, we purchase completed hardware platforms and add our proprietary software. While there is no unique capability with these suppliers, any failure by these suppliers to meet delivery commitments would cause us to delay shipments and potentially be unable to accept new orders for product.

In addition, in the event that these suppliers discontinued the manufacture of materials used in our products, we would be forced to incur the time and expense of finding a new supplier or to modify our products in such a way that such materials were not necessary. Either of these alternatives could result in increased manufacturing costs and increased prices of our products.

We assemble our APG products in our APG facilities located in Illinois and China. We may experience delays, disruptions, capacity constraints or quality control problems at our assembly facilities, which could result in lower yields or delays of product shipments to our customers. In addition, we are having an increasing number of our APG products manufactured in China via contract manufacturers. Any disruption of our own or contract manufacturers' operations could cause us to delay product shipments, which would negatively impact our sales, competitive reputation and position. In addition, if we do not accurately forecast demand for our products, we will have excess or insufficient parts to build our product, either of which could seriously affect our operating results.

IN ORDER FOR US TO OPERATE AT A PROFITABLE LEVEL AND CONTINUE TO INTRODUCE AND DEVELOP NEW PRODUCTS FOR EMERGING MARKETS, WE MUST ATTRACT AND RETAIN OUR EXECUTIVE OFFICERS AND QUALIFIED TECHNICAL, SALES, SUPPORT AND OTHER ADMINISTRATIVE PERSONNEL.

Our performance is substantially dependent on the performance of our current executive officers and certain key engineering, sales, marketing, financial, technical and customer support personnel. If we lose the services of our executives or key employees, replacements could be difficult to recruit and, as a result, we may not be able to grow our business.

Competition for personnel, especially qualified engineering personnel, is intense. We are particularly dependent on our ability to identify, attract, motivate and retain qualified engineers with the requisite education, background and industry experience. As of March 31, 2006, we employed a total of 74 people in our engineering department. If we lose the services of one or more of our key engineering personnel, our ability to continue to develop products and technologies responsive to our markets may be impaired. FAILURE TO MANAGE OUR TECHNOLOGICAL AND PRODUCT GROWTH COULD STRAIN OUR MANAGEMENT, FINANCIAL AND ADMINISTRATIVE RESOURCES.

Our ability to successfully sell our products and implement our business plan in rapidly evolving markets requires an effective management planning process. Future product expansion efforts could be expensive and put a strain on our management by significantly increasing the scope of their responsibilities and by increasing the demands on their management abilities. To effectively manage our growth in these new technologies, we must enhance our marketing, sales, research and development areas.

WE MAY BE SUBJECT TO LITIGATION REGARDING INTELLECTUAL PROPERTY ASSOCIATED WITH OUR WIRELESS BUSINESS AND THIS COULD BE COSTLY TO DEFEND AND COULD PREVENT US FROM USING OR SELLING THE CHALLENGED TECHNOLOGY.

In recent years, there has been significant litigation in the United States involving intellectual property rights. We have from time to time in the past received correspondence from third parties alleging that we infringe the

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third party's intellectual property rights. We expect potential claims to increase in the future, including with respect to our wireless business. Intellectual property claims against us, and any resulting lawsuit, may result in our incurring significant expenses and could subject us to significant liability for damages and invalidate what we currently believe are our proprietary rights. These lawsuits, regardless of their merits or success, would likely be time-consuming and expensive to resolve and could divert management's time and attention. This could have a material and adverse effect on our business, results of operation, financial condition and prospects. Any potential intellectual property litigation against us related to our wireless business could also force us to do one or more of the following:

- cease selling, incorporating or using technology, products or services that incorporate the infringed intellectual property,
- obtain from the holder of the infringed intellectual property a license to sell or use the relevant technology, which license may not be available on acceptable terms, if at all, or
- redesign those products or services that incorporate the disputed intellectual property, which could result in substantial unanticipated development expenses.

If we are subject to a successful claim of infringement related to our wireless intellectual property and we fail to develop non-infringing intellectual property or license the infringed intellectual property on acceptable terms and on a timely basis, operating

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results could decline and our ability to grow and sustain our wireless business could be materially and adversely affected. As a result, our business, financial condition, results of operation and prospects could be impaired.

We may in the future initiate claims or litigation against third parties for infringement of our intellectual property rights or to determine the scope and validity of our proprietary rights or the proprietary rights of our competitors. These claims could also result in significant expense and the diversion of technical and management personnel's attention.

UNDETECTED SOFTWARE ERRORS OR FAILURES FOUND IN NEW PRODUCTS MAY RESULT IN A LOSS OF CUSTOMERS OR A DELAY IN MARKET ACCEPTANCE OF OUR PRODUCTS.

Our products may contain undetected software errors or failures when first introduced or as new versions are released. To date, we have not been made aware of any significant software errors or failures in our products. However, despite testing by us and by current and potential customers, errors may be found in new products after commencement of commercial shipments, resulting in loss of customers or delay in market acceptance.

OUR FINANCIAL POSITION AND RESULTS OF OPERATIONS MAY BE ADVERSELY AFFECTED IF TAX AUTHORITIES CHALLENGE US AND THE TAX CHALLENGES RESULT IN UNFAVORABLE OUTCOMES.

We currently have international subsidiaries located in Japan, China, Ireland, United Kingdom, and Israel as well as international branch offices located in Hong Kong and Taiwan. Our branch office in Taiwan is presently in the liquidation process. The complexities resulting from operating in several different tax jurisdictions increase our exposure to worldwide tax challenges.

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CONDUCTING BUSINESS IN INTERNATIONAL MARKETS INVOLVES FOREIGN EXCHANGE RATE EXPOSURE THAT MAY LEAD TO REDUCED PROFITABILITY.

With the recent acquisition of Sigma, we have increased risk from foreign currency exposure. Sigma's functional currency is the Euro, and Sigma conducts business in both the Euro and pounds sterling. We believe that foreign exchange exposures may lead to reduced profitability.

### RISKS RELATED TO OUR INDUSTRY

OUR INDUSTRY IS CHARACTERIZED BY RAPIDLY CHANGING TECHNOLOGIES. IF WE ARE NOT SUCCESSFUL IN RESPONSE TO RAPIDLY CHANGING TECHNOLOGIES, OUR PRODUCTS MAY BECOME OBSOLETE AND WE MAY NOT BE ABLE TO COMPETE EFFECTIVELY.

The wireless data access business is characterized by rapidly changing technologies, short product life cycles and frequent new product introductions. To remain competitive, we have successfully introduced several new products.

Both the cellular (2.5G and 3G) and Wi-Fi (802.11) spaces are rapidly changing and prone to standardization. We will continue to evaluate, develop and introduce technologically advanced products that will position us for possible growth in the wireless data access market. If we are not successful in response to rapidly changing technologies, our products may become obsolete and we may not be able to compete effectively.

CHANGES IN LAWS OR REGULATIONS, IN PARTICULAR, FUTURE FCC REGULATIONS AFFECTING THE BROADBAND MARKET, INTERNET SERVICE PROVIDERS, OR THE COMMUNICATIONS INDUSTRY, COULD NEGATIVELY AFFECT OUR ABILITY TO DEVELOP NEW TECHNOLOGIES OR SELL NEW PRODUCTS AND THEREFORE, REDUCE OUR PROFITABILITY.

The jurisdiction of the Federal Communications Commission, or FCC, extends to the entire communications industry, including our customers and their products and services that incorporate our products. Future FCC regulations affecting the broadband access services industry, our customers or our products may harm our business. For example, future FCC regulatory policies that affect the availability of data and Internet services may impede our customers' penetration into their markets or affect the prices that they are able to charge. In addition, FCC regulatory policies that affect the specifications of wireless data devices may impede certain of our customers' ability to manufacture their products profitably, which could, in turn, reduce demand for our products. Furthermore, international regulatory bodies are beginning to adopt standards for the communications industry. Although our business has not been hurt by any regulations to date, in the future, delays caused by our compliance with regulatory requirements may result in order cancellations or postponements of product purchases by our customers, which would reduce our profitability.

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### RISKS RELATED TO OUR LICENSING PROGRAM

OUR ABILITY TO SUSTAIN REVENUE FROM THE LICENSING OF OUR INTELLECTUAL PROPERTY IS SUBJECT TO MANY RISKS, AND ANY INABILITY TO SUCCESSFULLY LICENSE OUR INTELLECTUAL PROPERTY COULD MATERIALLY AND ADVERSELY AFFECT OUR BUSINESS, FINANCIAL CONDITION AND OPERATING RESULTS.

In addition to our wireless product lines, we offer our intellectual property through licensing and product royalty arrangements. We have over 100



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U.S. patents granted or pending addressing both essential International Telecommunications Union and non-essential technologies. In connection with our intellectual property licensing efforts, we have filed several patent infringement lawsuits and are aggressively pursuing unlicensed companies to license their unauthorized use of our intellectual property. We have pending patent infringement litigation claims with Agere and Lucent. We expect litigation to continue to be necessary to enforce our intellectual property rights and to determine the validity and scope of the proprietary rights of others. Because of the high degree of complexity of the intellectual property at issue, the inherent uncertainties of litigation in general and the preliminary nature of these litigation matters, we cannot assure you that we will ultimately prevail or receive the judgments that we seek. We may not be able to obtain licensing agreements from these companies on terms favorable to us, if at all. In addition, we may be required to pay substantial monetary damages as a result of claims these companies have brought against us which could materially and adversely affect our business, financial condition and operating results.

LITIGATION EFFORTS RELATED TO OUR LICENSING PROGRAM ARE EXPECTED TO BE COSTLY AND MAY NOT ACHIEVE OUR OBJECTIVES.

Litigation such as our suits with Agere and Lucent can take years to resolve and can be expensive to pursue or defend. In addition, the allegations and claims involved in these lawsuits, even if ultimately resolved in our favor, could be time consuming to litigate and divert management attention. We may not ultimately prevail in these matters or receive the judgments that we seek. We could also face substantial monetary damages as a result of claims others bring against us. In addition, courts' decisions on current pending and future motions could have the effect of determining the ultimate outcome of the litigation prior to a trial on the merits, or strengthen or weaken our ability to assert claims and defenses in the future. Accordingly, an adverse judgment could seriously harm our business, financial position and operating results and cause our stock price to decline substantially.

WE EXPECT TO CONTINUE TO BE SUBJECT TO LITIGATION REGARDING INTELLECTUAL PROPERTY CLAIMS RELATED TO OUR LICENSING PROGRAM WHICH COULD IMPAIR OUR ABILITY TO GROW OR SUSTAIN REVENUES FROM OUR LICENSING EFFORTS.

As we continue to aggressively pursue licensing arrangements with companies that are using our intellectual property without our authorization, we expect to continue to be subject to lawsuits that challenge the validity of our intellectual property or that allege that we have infringed third party intellectual property rights. Any of these claims could result in substantial damages against us and could impair our ability to grow and sustain our licensing business. This could materially and adversely affect our business, financial condition, operating results and prospects. As a result, at least in part, of our licensing efforts to date, we are currently subject to claims from Agere and Lucent regarding patent infringement matters of the nature described above. We have also been subject to claims from others in the past regarding similar matters. In addition, in recent years, there has been significant litigation in the United States involving intellectual property rights. We expect these claims to increase as our intellectual property portfolio becomes larger. Intellectual property claims against us, and any resulting lawsuit, may result in our incurring significant expenses and could subject us to significant liability for damages and invalidate what we currently believe are our proprietary rights. These lawsuits, regardless of their merits or success, would likely be time-consuming and expensive to resolve and could divert management's time and attention.

OUR ABILITY TO ENFORCE OUR INTELLECTUAL PROPERTY RIGHTS MAY BE LIMITED, AND ANY LIMITATION COULD ADVERSELY AFFECT OUR ABILITY TO SUSTAIN OR INCREASE REVENUE FROM OUR LICENSING PROGRAM.

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Our ability to sustain and grow revenue from the licensing of our intellectual property is dependent on our ability to enforce our intellectual property rights. Our ability to enforce these rights is subject to many challenges and may be limited. For example, one or more of our pending patents may never be issued. In addition, our patents, both issued and pending, may not prove enforceable in actions against alleged infringers Agere and Lucent have currently pending claims seeking to invalidate one or more of our patents. If a court were to invalidate one or more of our patents, this could materially and adversely affect our licensing program. Furthermore, some foreign laws, including those of various countries in Asia, do not protect our proprietary rights to the same extent as United States laws.

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### RISKS RELATED TO OUR COMMON STOCK

THE TRADING PRICE OF OUR STOCK PRICE MAY BE VOLATILE BASED ON A NUMBER OF FACTORS, SOME OF WHICH ARE NOT IN OUR CONTROL.

The trading price of our common stock has been highly volatile. The common stock price has fluctuated from a low of \$6.70 to a high of \$10.16 during the past twelve months. Our stock price could be subject to wide fluctuations in response to a variety of factors, many of which are out of our control, including:

- announcements of technological innovations,
- new products or services offered by us or our competitors,
- actual or anticipated variations in quarterly operating results,
- outcome of ongoing intellectual property related litigations,
- changes in financial estimates by securities analysts,
- conditions or trends in our industry,
- our announcement of significant acquisitions, strategic partnerships, joint ventures or capital commitments,
- additions or departures of key personnel,
- mergers and acquisitions, and
- sales of common stock by our stockholders or us.

In addition, the NASDAQ National Market, where many publicly held telecommunications companies, including PCTEL, are traded, often experiences extreme price and volume fluctuations. These fluctuations often have been unrelated or disproportionate to the operating performance of these companies. In the past, following periods of volatility in the market price of an individual company's securities, securities class action litigation often has been instituted against that company. This type of litigation, if instituted, could result in substantial costs and a diversion of management's attention and resources.

PROVISIONS IN OUR CHARTER DOCUMENTS MAY INHIBIT A CHANGE OF CONTROL OR A CHANGE OF MANAGEMENT, WHICH MAY CAUSE THE MARKET PRICE FOR OUR COMMON STOCK TO FALL AND MAY INHIBIT A TAKEOVER OR CHANGE IN OUR CONTROL THAT A STOCKHOLDER MAY CONSIDER

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FAVORABLE.

Provisions in our charter documents could discourage potential acquisition proposals and could delay or prevent a change in control transaction that our stockholders may favor. These provisions could have the effect of discouraging others from making tender offers for our shares, and as a result, these provisions may prevent the market price of our common stock from reflecting the effects of actual or rumored takeover attempts and may prevent stockholders from reselling their shares at or above the price at which they purchased their shares. These provisions may also prevent changes in our management that our stockholders may favor. Our charter documents do not permit stockholders to act by written consent, do not permit stockholders to call a stockholders meeting, and provide for a classified board of directors, which means stockholders can only elect, or remove, a limited number of our directors in any given year.

Our board of directors has the authority to issue up to 5,000,000 shares of preferred stock in one or more series. The board of directors can fix the price, rights, preferences, privileges and restrictions of this preferred stock without any further vote or action by our stockholders. The rights of the holders of our common stock will be affected by, and may be adversely affected by, the rights of the holders of any preferred stock that may be issued in the future. Further, the issuance of shares of preferred stock may delay or prevent a change in control transaction without further action by our stockholders. As a result, the market price of our common stock may drop.

UNDER REGULATIONS REQUIRED BY THE SARBANES-OXLEY ACT OF 2002, IF WE ARE UNABLE TO SUCCESSFULLY IMPLEMENT PROCESSES AND PROCEDURES TO ACHIEVE AND MAINTAIN EFFECTIVE INTERNAL CONTROL OVER OUR FINANCIAL REPORTING, OUR ABILITY TO PROVIDE RELIABLE AND TIMELY FINANCIAL REPORTS COULD BE HARMED.

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We must comply with the rules promulgated under section 404 of the Sarbanes-Oxley Act of 2002. Section 404 requires an annual management report assessing the effectiveness of our internal control over financial reporting, a report by our independent registered public accountants addressing this assessment, and a report by our independent auditors addressing the effectiveness of our internal control.

In connection with reporting our financial results for the year ended December 31, 2004 and 2005, we identified and described a "material weakness" (as defined by the relevant accounting standards) in our internal control related to our accounting for income taxes. Specifically, we did not have effective controls over determining net operating loss carrybacks, applicable state tax rates applied, and the tax effect of stock option exercises. In addition, we did not have effective controls to monitor the difference between the income tax basis and the financial reporting basis of assets and liabilities and reconcile the difference to deferred income tax assets and liabilities. This control deficiency resulted in audit adjustments to the fourth quarter 2004 financial statements. To address the material weakness described above, PCTEL has engaged an outside tax consultant and has implemented an internal training program to enhance the capabilities of its internal tax personnel. The remediation program to address the previously identified material weakness and remediation testing for other internal control deficiencies identified in 2004 is still in process. The occurrence of control deficiencies in our internal control, and material weaknesses in particular, adversely affect our ability to report our financial results on a timely and accurate basis.

While we have expended significant resources in developing the necessary

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documentation and testing procedures required by Section 404, we cannot be certain that the actions we are taking to improve, achieve and maintain our internal control over financial reporting will be adequate or that we will be able to implement our planned processes and procedures. If we do not comply with our requirements under Section 404 in a timely manner, or the processes and procedures that we implement for our internal control over financial reporting are inadequate, our ability to provide reliable and timely financial reports, and consequently our business and operating results, could be harmed. This in turn could result in an adverse reaction in the financial markets due to a loss of confidence in the reliability of our financial reports, which could cause the market price of our Common Stock to decline. See also Item 4 for discussion on Controls and Procedures.

### ITEM 2: UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

There were no share repurchases under the company's repurchase program during the three months ended March 31, 2006:

In August 2002, the Board of Directors authorized the repurchase of up to 1,000,000 shares of our common stock, which was completed in February 2003. We announced this stock repurchase program in our Quarterly Report Form 10-Q for the quarterly period ended March 31, 2002. In February and November 2003, we extended our stock repurchase program to repurchase up to 1,000,000 and 500,000 additional shares, respectively, on the open market from time to time. We announced the extensions of our stock repurchase program in our stock repurchase program in our Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2003 and in our Annual Report on Form 10-K for the period ended December 31, 2003, respectively.

### ITEM 6: EXHIBITS

| EXHIBIT<br>NUMBER<br>----- | DESCRIPTION<br>-----   |
|----------------------------|--|
| 10.52 (a)                  | Amended and Restated Employment Agreement, dated as of January 6, 2006, by and between PCTEL, Inc. and Martin H. Singer  |
| 10.53 (a)                  | Amended and Restated Retention Agreement, dated as of January 6, 2006, by and between PCTEL, Inc. and Martin H. Singer   |
| 31.1                       | Certification of Principal Executive Officer pursuant to Section 302 of Sarbanes-Oxley Act of 2002   |
| 31.2                       | Certification of Principal Financial Officer pursuant to Section 302 of Sarbanes-Oxley Act of 2002   |
| 32                         | 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 |
| (a)                        | Incorporated by reference to the exhibit bearing the same number filed with the Registrant's Current Report on Form 8-K filed on January 10, 2006.                               |

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SIGNATURE

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, this Report has been signed below by the following person on behalf of the Registrant and in the capacity and on the date indicated:

PCTEL, Inc.  
A Delaware Corporation  
(Registrant)

/s/ MARTIN H. SINGER

-----  
Martin H. Singer  
Chairman of the Board and  
Chief Executive Officer

Date: May 10, 2006