NETLOGIC MICROSYSTEMS INC
Form DEF 14A
April 20, 2007

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

SCHEDULE 14A

Proxy Statement Pursuant to Section 14(a)

of the Securities Exchange Act of 1934

Filed by the Registrant x   Filed by a Party other than the Registrant ¨

Check the appropriate box:

¨ Preliminary proxy statement

¨ **Confidential, for use of the Commission only**

x Definitive proxy statement

¨ Definitive additional materials

¨ Soliciting material pursuant to §240.14a-12

NETLOGIC MICROSYSTEMS, INC.

(Name of Registrant as Specified in its Charter)

(Name of Person(s) Filing Proxy Statement, if other than Registrant)

Payment of filing fee (Check the appropriate box):

x No fee required.

¨ Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

(1) Title of each class of securities to which transaction applies:

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(2) Aggregate number of securities to which transaction applies:

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(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

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(4) Proposed maximum aggregate value of transaction:

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¨ Fee paid previously with preliminary materials

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(1) Amount Previously Paid:

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(2) Form, Schedule or Registration Statement No.:

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(3) Filing Party:

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(4) Date Filed:

NETLOGIC MICROSYSTEMS, INC.

1875 Charleston Road

Mountain View, CA 94043

Dear Stockholder,

You are cordially invited to attend the 2007 Annual Meeting of Stockholders (the Annual Meeting) of NetLogic Microsystems, Inc. (the Company), to be held on May 18, 2007, 8:00 a.m., local time, at the offices of Bingham McCutchen LLP, 1900 University Avenue, East Palo Alto, California 94303.

It is important that your shares be represented and voted at the meeting. Whether you plan to attend the Annual Meeting or not, it is important that you promptly register your vote in accordance with the instructions set forth on the enclosed proxy card. A return addressed envelope is enclosed for your convenience. This will ensure your proper representation at the Annual Meeting. Returning the proxy does not deprive you of your right to attend the Annual Meeting. If you decide to attend the Annual Meeting and wish to change your proxy vote, you may do so automatically by voting in person at the meeting.

The matters expected to be acted upon at the meeting are described in detail in the following Notice of the 2007 Annual Meeting of Stockholders and Proxy Statement.

On behalf of our board of directors, I would like to express our appreciation for your continued interest in the affairs of the Company. We look forward to seeing you at the Annual Meeting.

Sincerely,

Ronald S. Jankov
President and Chief Executive Officer

First mailed to stockholders on

or about April 20, 2007

YOUR VOTE IS IMPORTANT.

PLEASE REMEMBER TO PROMPTLY RETURN YOUR PROXY.

NETLOGIC MICROSYSTEMS, INC.

NOTICE OF 2007 ANNUAL MEETING OF STOCKHOLDERS

To be held on May 18, 2007

To the Stockholders of NetLogic Microsystems, Inc.:

NOTICE IS HEREBY GIVEN that the 2007 Annual Meeting of Stockholders (the Annual Meeting) of NetLogic Microsystems, Inc., a Delaware corporation (the Company), will be held on May 18, 2007, at 8:00 a.m., local time, at the offices of Bingham McCutchen LLP, 1900 University Avenue, East Palo Alto, California 94303, for the following purposes:

1. To elect two members of our board of directors to hold office until the 2010 annual meeting of stockholders or until their respective successors have been elected or appointed. The nominees are Leonard Perham and Alan Krock;

2. To ratify the Audit Committee s appointment of PricewaterhouseCoopers LLP as the Company s independent registered public accounting firm for the fiscal year ending December 31, 2007; and

3. To transact such other business as may properly come before the Annual Meeting or any adjournment of the Annual Meeting.

The foregoing items of business are more fully described in the Proxy Statement accompanying this Notice. Our board of directors has fixed the close of business on March 20, 2007 as the record date for the determination of stockholders entitled to notice of and to vote at the Annual Meeting and at any adjournments of the Annual Meeting. A list of such stockholders will be available for inspection at the principal office of the Company.

You are cordially invited to attend the Annual Meeting. However, to ensure that you are represented at the Annual Meeting, please register your vote as promptly as possible in accordance with the instructions set forth on the enclosed proxy card. A return addressed envelope is enclosed for your convenience. If you attend the Annual Meeting, you may vote in person even though you have returned a proxy card previously. Your proxy is revocable in accordance with the procedures set forth in the Proxy Statement.

BY ORDER OF THE BOARD OF DIRECTORS

Roland B. Cortes
Secretary

Mountain View, California

April 20, 2007

NETLOGIC MICROSYSTEMS, INC.

1875 Charleston Road

Mountain View, California 94043

PROXY STATEMENT

GENERAL INFORMATION

This Proxy Statement is furnished in connection with the solicitation by the board of directors of NetLogic Microsystems, Inc., a Delaware corporation (the Company), of proxies, in the accompanying form, to be used at the 2007 Annual Meeting of Stockholders (the Annual Meeting) to be held at the offices of Bingham McCutchen LLP, 1900 University Avenue, East Palo Alto, California 94303, on May 18, 2007, at 8:00 a.m., local time, and any adjournments of the Annual Meeting. Unless the context otherwise requires, the Company, we, us, and similar terms refer to NetLogic Microsystems, Inc.

This Proxy Statement and the accompanying proxy card are being mailed on or about April 20, 2007 to all stockholders entitled to notice of and to vote at the Annual Meeting.

SOLICITATION AND VOTING PROCEDURES

Shares represented by valid proxies in the form enclosed, received in time for use at the Annual Meeting and not revoked at or prior to the Annual Meeting, will be voted at the Annual Meeting, as discussed below. The presence, in person or by proxy, of the holders of a majority of the outstanding shares of our common stock is necessary to constitute a quorum at the Annual Meeting. Holders of our common stock are entitled to one vote per share on all matters. To vote in person, a stockholder must attend the Annual Meeting, and then complete and submit the ballot provided at the meeting. To vote by proxy, a stockholder must mark, sign, and date the enclosed proxy card and mail it to the Company s transfer agent or submit a proxy electronically by using the Internet and logging on to *www.eproxy.com/netl/* by following the instructions provided on the proxy card. An automated system administered by the Company s transfer agent tabulates stockholder votes submitted by proxy, and an officer of the Company will tabulate votes cast in person at the Annual Meeting.

Brokers holding shares in street name for customers have the discretionary authority to vote on certain matters when they have not received instructions from the beneficial owners of shares. Under applicable rules, brokers have the discretion to vote on routine matters such as the uncontested election of directors and the ratification of the appointment of an accounting firm. Brokers that do not receive instructions from the beneficial owners are entitled to vote on Proposal No. 1 (the election of directors) and Proposal No. 2 (the ratification of appointment by the Audit Committee of PricewaterhouseCoopers LLP as the Company s independent registered public accounting firm for the 2007 audit). Broker non-votes, if any, will be considered for purposes of determining a quorum, but they will not be considered as entitled to vote and will not have any effect on any of the votes contemplated by this Proxy Statement.

The voting requirements for the proposals that we will consider at the Annual Meeting are as follows:

Election of Directors. Directors are elected by a plurality of the votes of the shares present in person or represented by proxy and entitled to vote at the Annual Meeting, and the two directors who receive the most votes will be elected to our board of directors. Abstentions and votes that are withheld will not affect the election of directors.

Ratification of Appointment of PricewaterhouseCoopers LLP as Independent Registered Public Accounting Firm. An affirmative vote of the holders of a majority of the votes of the shares present in person or represented by proxy and entitled to vote at the Annual Meeting is necessary for approval of Proposal No. 2 to ratify the Audit Committee s appointment of PricewaterhouseCoopers LLP as our independent registered public accounting firm for the audit of our fiscal 2007 financial statements. Abstentions will have the effect of votes against this proposal.

All proxies will be voted as specified on the proxy cards submitted by stockholders, if the proxy is properly executed or electronically submitted and is received by the Company prior to the close of voting at the Annual Meeting or any adjournment or postponement of the Annual Meeting. If no choice has been specified, a properly completed and timely returned or electronically submitted proxy card will be voted for our board of directors nominees and for Proposal No. 2, which are described in detail elsewhere in this Proxy Statement. In addition, all properly completed and timely returned or electronically submitted proxy cards will be voted by the proxies in their discretion for any other matters properly and timely submitted for a vote at the Annual Meeting.

The close of business on March 20, 2007 has been fixed as the record date for determining the stockholders entitled to notice of and to vote at the Annual Meeting. Only holders of our common stock at the close of business on March 20, 2007 will be entitled to notice of and to vote at the Annual Meeting. As of that date, we had 20,727,898 shares of common stock outstanding and entitled to vote. Each share of our common stock is entitled to one vote per share.

The cost of soliciting proxies, including expenses in connection with preparing and mailing of this Proxy Statement, will be borne by the Company. Copies of solicitation material will be furnished to brokerage houses, fiduciaries and custodians holding shares in their names that are beneficially owned by others so that they may forward this solicitation material to such beneficial owners. The Company will reimburse brokerage firms and other persons representing beneficial owners of common stock for their expenses in forwarding proxy material to such beneficial owners. Solicitation of proxies by mail may be supplemented by telephone, telegram, electronic facsimile transmission and other electronic means, and personal solicitation by the directors, officers or employees of the Company. No additional compensation will be paid to directors, officers or employees for such solicitation. The Company has retained Wells Fargo Shareowner Services to assist in the distribution of proxies for a fee estimated to be approximately $5,000.00 plus reasonable out-of-pocket expenses.

Copies of the Company s 2006 Annual Report on Form 10-K are being mailed to stockholders with this Proxy Statement. Additional copies of the Company s 2006 Annual Report on Form 10-K, excluding exhibits, may be obtained by any stockholder without charge by making a request through the Company s website Investor Information pages at *www.netlogicmicro.com* or by written request addressed to: Investor Relations, NetLogic Microsystems, Inc., 1875 Charleston Road, Mountain View, California 94043.

REVOCABILITY OF PROXIES

You can revoke your proxy at any time before the voting at the Annual Meeting by sending a properly signed written notice of your revocation to the Secretary of the Company, by submitting another proxy that is properly signed and bearing a later date, by following the specified procedures for submitting a proxy electronically and changing your vote, or by voting in person at the Annual Meeting. Attendance at the Annual Meeting will not itself revoke an earlier submitted proxy. You should direct any written notices of revocation and related correspondence to NetLogic Microsystems, Inc., 1875 Charleston Road, Mountain View, California 94043, Attention: Secretary.

CORPORATE GOVERNANCE

Director Independence

Our board of directors has determined that Mr. Perham, Mr. Broyles, Mr. Krock, Mr. Godinho and Mr. Domenik are independent, as defined under Marketplace Rule 4200(a)(15) of the listing rules of the NASDAQ Stock Market (NASDAQ). No director qualifies as independent unless the board of directors determines that the director has no direct or indirect material relationship with the Company. On an annual basis, each director and executive officer is obligated to complete a Director and Officer Questionnaire which requires disclosure of any transactions with the Company in which the director or executive officer, or any member of his or her immediate family, have a direct or indirect material interest. The Company also independently reviews the relationship of the Company to any entity employing a director or on which the director serves as a member of the board of directors. Our board of directors has determined that all directors who served during our 2006 fiscal year and all of our director nominees, other than Mr. Jankov, are independent in accordance with SEC and the NASDAQ rules. The board has concluded that there are no business relationships that are material or that would interfere with the exercise of independent judgment by any of these directors in their service on the Company s board of directors or its committees. The board also considered share ownership of the directors and determined in the case of Mr. Godinho that his beneficial ownership of shares representing approximately 15.0% of the common stock does not result in his having a controlling block of shares or prevent him from acting independently.

Our board of directors has also determined that Mr. Perham is the lead independent director. Our board of directors has standing Audit, Compensation and Governance and Nominating Committees, each of which is comprised solely of independent directors in accordance with the NASDAQ listing rules.

Code of Business Conduct and Ethics

We have adopted a Code of Business Conduct and Ethics for Employees, Executive Officers and Directors that applies to all of our employees and directors. We have posted this Code of Business Conduct and Ethics on the Company s website at *www.netlogicmicro.com*.

Stockholder Communications with the Board

Stockholders who desire to communicate with the board, or to a specific director, may do so by delivering the communication addressed to either the board of directors or any director, c/o NetLogic Microsystems, Inc., 1875 Charleston Road, Mountain View, California 94043. These communications will be delivered to the board, or any individual director, as specified.

Annual Meeting Attendance

Our board of directors encourages each director to attend our annual meetings of stockholders, but attendance is not required. Mr. Godinho attended our 2006 annual meeting of stockholders.

Board of Directors

The names of each of our directors at April 1, 2007 and certain information about them are set forth below:

Name	Age	Position
Leonard Perham (1)(2)	63	Chairman of the Board
Douglas Broyles (3)	65	Director
Steve Domenik (1)(2)(3)	55	Director
Norman Godinho	66	Director
Ronald Jankov	48	Director, Chief Executive Officer and President
Alan Krock (1)	46	Director

(1) Member of the audit committee.

(2) Member of the compensation committee.

(3) Member of the governance and nominating committee.

The principal occupations and positions for at least the past five years of our directors and director nominees are described below. There are no family relationships among any of our directors or executive officers.

Leonard Perham has served as a member of or Chairman of our board since March 2000. Mr. Perham is a private investor who holds officer and director positions with various private companies. From April 1991 to January 2000, Mr. Perham was the Chief Executive Officer of Integrated Device Technology, Inc.

Douglas Broyles has served as a member of our board since December 1999. Mr. Broyles has been a General Partner with Huntington Ventures since September 2000. For the past 25 years, Mr. Broyles has been associated, as an investor and board member, with several Silicon Valley technology companies. Mr. Broyles also currently serves on the board of Peak International Ltd.

Steve Domenik has served as a member of our board since January 2001. Since 1995, Mr. Domenik has been with Sevin Rosen Funds, a venture capital firm, where he is a General Partner. During his tenure at Sevin Rosen Funds he has led numerous investments in private companies. Mr. Domenik also sits on the boards of directors of various private companies.

Norman Godinho is one of our founders and has served as a member of our board since the Company s inception. From December 1997 to April 2000, Mr. Godinho served as our Chief Executive Officer. In August 1980, Mr. Godinho co-founded Integrated Device Technology, Inc. Mr. Godinho was also a director and Vice President of Paradigm Technology Limited, a semiconductor company, which he co-founded in 1987.

Ronald Jankov has served as our President, Chief Executive Officer and as a member of our board of directors since April 2000. From September 1995 to September 1999, Mr. Jankov was Vice President of Sales and then Vice President and General Manager for the Multimedia Division of NeoMagic Corporation, a provider of semiconductors for handheld systems. Prior to that time, Mr. Jankov was Vice President of Cyrix Corporation, a microprocessor company, and held various engineering, sales and management positions at other semiconductor companies, including LSI Logic Corp. and Texas Instruments.

Alan Krock has served as a member of our board since August 2005. Mr. Krock was Vice President and Chief Financial Officer of PMC-Sierra, Inc. from November 2002 until March 1, 2007 when he became Vice President of Corporate Affairs for PMC-Sierra, Inc. Mr. Krock was Vice President and Chief Financial Officer of Integrated Device Technology, Inc. from January 1998 until November 2002. Previously Mr. Krock held management positions at Rohm Corporation and Price Waterhouse, now PricewaterhouseCoopers LLP. Mr. Krock has served on the board of directors of Sipex Corporation since September 2006.

Board Classification

Our board of directors is divided into three classes, as follows:

- Class I consists of Norman Godinho and Ronald Jankov whose terms will expire at our annual meeting of stockholders to be held in 2008;
- Class II consists of Douglas Broyles and Steve Domenik whose terms will expire at our annual meeting of stockholders to be held in 2009; and
- Class III consists currently of Leonard Perham and Alan Krock whose terms will expire at the Annual Meeting.

Our Class III directors terms will expire at the Annual Meeting. Upon expiration of the term of a class of directors, directors for that class will be elected for three-year terms at the annual meeting of stockholders in the year in which such term expires. Each director s term is subject to the election and qualification of his successor, or his earlier death, resignation or removal. The authorized number of directors may be changed by resolution of our board of directors or a majority vote of the stockholders. Any increase or decrease in the number of directors will be distributed among the three classes so that, as nearly as possible, each class will consist of one-third of the directors. Because no more than two directors may be elected at each annual meeting, this classification of our board of directors may have the effect of delaying or preventing changes in control or management.

Board Meetings and Committees

Board of Directors

Mr. Perham serves as chairman of our board. Our board of directors held four meetings in 2006. In addition, our board acted at times by unanimous written consent pursuant to Delaware law. None of the directors attended fewer than 75 percent of the total number of meetings held during the year or the total number of meetings held by all committees of the board on which he served during the year.

Audit Committee

Mr. Krock, Mr. Perham and Mr. Domenik are the current members of our Audit Committee. All are independent, as defined by Marketplace Rule 4350(d) of the NASDAQ listing rules. Mr. Krock serves as the chairman of the committee. The Audit Committee held ten meetings in 2006. The board of directors has determined that Mr. Krock is the audit committee financial expert, as defined under Item 407(d)(5)(i) of Regulation S-K under the Securities Act of 1933 and the Securities Exchange Act of 1934, but that status does not impose on him duties, liabilities or obligations that are greater than the duties, liabilities or obligations otherwise imposed on him as a member of our audit committee and our board of directors. Our Audit Committee oversees, reviews and evaluates our financial statements, accounting and financial reporting processes, internal control functions and the audits of our financial statements, including the appointment, compensation, retention and oversight of our independent auditor. Our Audit Committee also is charged with reviewing reports or complaints with respect to the accounting, auditing and/or internal controls of the Company, including possible violations under our whistleblower policy. The responsibilities of our audit committee are described in the Audit Committee Charter adopted by our Board of Directors, a current copy of which is available on the Company s website at *www.netlogicmicro.com*.

Compensation Committee

Mr. Perham and Mr. Domenik are the current members of our Compensation Committee. Mr. Domenik serves as the chairman of the Committee. Our Compensation Committee held seven meetings in 2007. In addition, the Compensation Committee acted at times by unanimous written consent pursuant to Delaware law.

Our Compensation Committee does not have a charter; rather, its duties and obligations have been specified by the board of directors. The Compensation Committee reviews and makes recommendations to our board of directors concerning the compensation and benefits of our executive officers (including our chief executive officer) and directors, develops performance objectives for our officers and evaluates their performance in light of these objectives, administers our stock option and employee benefits plans, reviews general policies relating to compensation and benefits, and produces an annual report on executive compensation for inclusion in our annual proxy statement.

Governance and Nominating Committee

Mr. Broyles and Mr. Domenik are the current members of our Governance and Nominating Committee. Mr. Broyles serves as the chairman of the Committee. Our Governance and Nominating Committee held one meeting in 2006. Our Governance and Nominating Committee identifies prospective board candidates, recommends nominees for election to our board of directors, develops and recommends board member selection criteria, considers committee member qualification, recommends corporate governance principles to the board of directors, and provides oversight in the evaluation of our board of directors and each committee. The responsibilities of our Governance and Nominating Committee are described in the Governance and Nominating Committee Charter approved by our board of directors, a current copy of which is available on the Company s website at *www.netlogicmicro.com.*

As the only two Class III directors, Mr. Perham and Mr. Krock are the only candidates for director to be elected at the Annual Meeting. Their nominations have been approved by the entire board of directors, including all of the independent directors.

When there is a need to identify or evaluate a prospective nominee, our Governance and Nominating Committee undertakes a careful review process which may involve, among other things, candidate interviews, inquiries of the person or persons recommending the candidate, engagement of an outside firm to gather additional information and/or discussions with management and incumbent directors. In evaluating candidates, including current directors eligible for re-election, our Governance and Nominating Committee considers various factors that it considers necessary or appropriate, including the size and composition of our board of directors and our committees, the needs of our board of directors and our committees, the candidate s expertise and experience, the candidate s independence and potential conflicts of interest, the candidate s character and integrity, and the candidate s existing commitments. Upon completion of its review and evaluation, our Governance and Nominating Committee makes its recommendations to our board of directors regarding the candidate(s). After considering our Governance and Nominating Committee s recommendations, our board of directors determines and approves which candidate(s) shall be nominated for election to our board of directors, subject to stockholder approval.

Our Governance and Nominating Committee will consider candidates for nomination as director who are recommended by the Company s stockholders and will not evaluate such candidates differently than other nominations for director. To recommend a prospective candidate for consideration by our Governance and Nominating Committee, stockholders of the Company must hold at least $2,000 in market value or one percent of the Company s outstanding voting securities continuously for at least one year prior to the date of the submission of the recommendation. Recommendations received after the date that is 120 days prior to the one year anniversary of the mailing of the previous year s proxy statement, will likely not be considered timely for consideration at that year s annual meeting. The submission deadline for next year s annual meeting is set forth under Stockholder Proposals for 2008 Annual Meeting elsewhere in this proxy statement. Stockholders may suggest qualified candidates for director by giving timely notice in writing to the committee at the following address: NetLogic Microsystems, Inc., 1875 Charleston Road, Mountain View, California 94043, Attention: Secretary, and must include the candidate s name, home and business contact information, detailed biographical data and qualifications and an explanation of the reasons why the stockholder believes this candidate is qualified for service on the Company s board of directors. The stockholder must also provide such other information about the candidate that would be required by the SEC rules to be included in a proxy statement. In addition, the stockholder must include the consent of the candidate and describe any arrangements or undertakings between the stockholder and the candidate regarding the nomination. The Secretary will then forward this information to our Governance and Nominating Committee. Our Governance and Nominating Committee charter, which sets forth the policies and procedures for director candidates, is posted on our website at *www.netlogicmicro.com*.

To date, the Company has not rejected any candidate timely recommended by any stockholder or group of stockholders owning more than five percent (5%) of our common stock.

Compensation Committee Interlocks and Insider Participation

No member of our Compensation Committee serves on or has served on the board of directors or compensation committee of another entity that has one or more members serving on our board of directors or Compensation Committee. None of our executive officers served on the board of directors or compensation committee of another entity during the past fiscal year.

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COMPENSATION OF NON-EMPLOYEE DIRECTORS

Director Compensation Table

The following Director Compensation Table sets forth summary information concerning the compensation paid to our non-employee directors in 2006 for their services as directors.

Name	Fees Earned or Paid in Cash ($)	Option Awards ($) (1)(2)	All Other Compensation ($)	Total ($)
Leonard Perham	20,000	91,326(3)		111,326
Steve Domenik	15,000	91,326(3)		106,326
Norman Godinho	10,000	91,326(3)		101,326
Douglas Broyles	15,000	91,326(3)		106,326
Alan Krock	20,000	213,618(4)		111,326
Total	**80,000**	**578,922**		**658,922**

(1) Amounts in the table reflect the compensation cost recognized by the Company for financial statement reporting purposes for the fiscal year ended December 31, 2006 in accordance with the provisions of Statement of Financial Accounting Standards No. 123R, Share-based Payments, (SFAS 123R), but excluding any estimate of future forfeitures. These compensation costs reflect equity awards granted in and prior to fiscal year 2006. See Note 10 of the consolidated financial statements in the Company s Annual Report on Form 10-K for the year ended December 31, 2006 regarding the assumptions underlying the valuation of equity awards.

(2) As of December 31, 2006, each of our non-employee directors held outstanding options to purchase the following number of shares of our common stock: Leonard Perham, 14,166; Steve Domenik, 14,166; Norman Godinho, 14,166; Douglas Broyles, 14,166; and Alan Krock, 17,399.

(3) Reflects the compensation costs recognized in fiscal 2006 for stock option grants with the following fair values as of the grant date: an option to purchase 10,000 shares granted on July 14, 2005 with a fair value of $88,781, and an option to purchase 10,000 shares granted on July 19, 2006 with a fair value of $136,853.

(4) Reflects the compensation costs recognized in fiscal 2006 for stock option grants with the following fair values as of the grant date: an option to purchase 40,000 shares granted on August 5, 2005 with a fair value of $412,918, and an option to purchase 10,000 shares granted on July 19, 2006 with a fair value of $136,853.

We reimburse our non-employee directors for all reasonable out-of-pocket expenses incurred in the performance of their duties as directors. Employee directors are not compensated for board services in addition to their compensation as employees. Consequently, during fiscal year 2006, Mr. Jankov did not receive compensation for his role as a director.

Cash Compensation

We provide annual cash compensation to our non-employee directors payable after the first regularly scheduled meeting of our board of directors following each annual meeting of stockholders. In fiscal 2006, we awarded cash compensation to our non-employee directors as follows:

- $10,000 to each of our non-employee directors for service on our board of directors, and $1,000 for each board meeting attended in person when traveling from out-of-town;
- An additional $10,000 to Mr. Krock for service as the chairman of the Audit Committee;
- An additional $5,000 to each of Mr. Domenik and Mr. Broyles for services as the chairmen of each of the Compensation and Governance and Nominating Committees, respectively; and
- An additional $10,000 to Mr. Perham for service as the lead independent director.

Equity Compensation

In connection with their board service, outside directors are eligible to receive, and have received, stock options under our 2004 Equity Incentive Plan (the 2004 Plan). Under the terms of the 2004 Plan, each outside director receives an initial option grant to purchase 40,000 shares of our common stock upon first becoming a member of our board of directors. The initial option vests and becomes exercisable over three years from the date of grant, with the first 25% of the shares subject to the initial option vested on the date of grant, and the remainder vesting monthly thereafter.

In addition, at the first regularly scheduled meeting of our board of directors following each annual meeting of stockholders, each outside director is automatically granted a nonstatutory option to purchase 10,000 shares of our common stock, provided the director has served on our board or directors for at least six months. These options vest on a monthly basis and become exercisable in full on the first anniversary of the date of grant or immediately prior to our next annual meeting of stockholders, if earlier. The exercise price of stock options granted to directors is equal to the fair market value of a share of our common stock on the date of grant, which under the 2004 Plan is the closing price per share of our common stock on the principal public market on which it is listed for trading. Currently, our common stock is listed and traded on the NASDAQ Global Select Market, or Nasdaq GSM. The accounting value of stock option grants to directors is calculated using the same methodology that we use to determine the accounting charge associated with similar equity-based awards for the fiscal period immediately preceding the grant date. We measure the fair value of option awards using the Black-Scholes option pricing model which requires a number of complex and subjective assumptions including our stock price volatility, option exercise patterns (expected life of options), future forfeiture rates and related tax effects.

During fiscal 2006, all option grants to board members were to continuing board members, each of whom received options to purchase 10,000 shares of our common stock. The grants were made on July 19, 2006 at an exercise price of $26.28 per share, which was the closing price of our common stock on the Nasdaq GSM on the same date.

EXECUTIVE COMPENSATION

COMPENSATION DISCUSSION AND ANALYSIS

Compensation Committee

Our Compensation Committee is composed of Mr. Domenik and Mr. Perham, who are independent, non-employee directors. The Compensation Committee reviews and makes recommendations to our board of directors concerning the compensation and benefits of our executive officers (including our chief executive officer) and directors, reviews and approves performance objectives for our officers and evaluates their performance in light of these objectives, administers our stock option and employee benefits plans, reviews and approves our general policies relating to compensation and benefits, and reviews and approves this Compensation Discussion and Analysis report for inclusion in this Proxy Statement.

Compensation Philosophy and Objectives

Our compensation philosophy and the objective of our compensation program is to align the interests of our stockholders and management by integrating executive compensation with our annual and long-term corporate strategic and financial objectives. We believe that the overall compensation for our executive officers should be fair, reasonable and competitive to attract, retain, motivate and reward well-qualified executives who contribute to our long-term success. Accordingly, our compensation program is designed to reward the performance of each executive officer and recognize the officer s contribution to the overall performance of the Company in a particular fiscal year, as well as their contribution to our long-term strategic and financial objectives.

Consistent with our compensation philosophy and objectives, we consider many factors in determining appropriate compensation for our executive officers, including:

- the individual performance of each officer relative to pre-determined individual and Company performance goals;
- the experience and career potential of each officer;
- the competitive market for both short-term and long-term compensation;
- the prior compensation earned and awarded to each officer;
- the success of the Company in achieving its strategic and financial goals; and
- our need to obtain, retain and motivate highly qualified individuals.

To guide in the implementation of our compensation philosophy, our compensation program is designed to:

- include equity grants that typically vest over multiple years to align long-term employee interests with the interests of our stockholders;

- provide a direct and meaningful link between the Company s goals and individual achievement of pre-determined, objective and well-defined goals; and

- provide a competitive blend of short-term and long-term compensation to provide meaningful incentives for individual achievement.

Our total compensation packages may include base salary, annual cash bonuses and commissions, all paid in cash, as well as long-term compensation in the form of stock options. Additionally, our compensation packages include a 401(k) plan, medical and other benefits, and severance and change in control and other post-termination benefits.

Competitive Market Data

Determining the competitive landscape is an essential step in implementing our compensation objectives. The Company and the Compensation Committee annually review competitive market information for its executive officers including short-term incentives such as base salaries, cash bonuses and commissions, and long-term incentives such as various forms of equity compensation including stock options, performance shares and restricted stock. As a part of this annual assessment, the Company engages an independent compensation consultant to assist the Company in determining relevant market data for a selected peer group of companies.

For fiscal year 2006, the Compensation Committee retained Radford Surveys and Consulting, a business unit of AON Consulting, Inc. (Radford), as an independent, third-party consulting firm. Working with Radford and the Company s CEO, CFO and Corporate Secretary, the Compensation Committee selected a peer group of companies for comparative market analysis in the Company s determination of 2006 executive officer compensation. The peer group was selected from companies included in the 2005 Radford Executive Survey and 2005 Radford Benchmark Surveys (collectively the Surveys) based on multiple factors, including industry segment, revenue, number of employees, geographical location, age, growth rate and market capitalization. The competitive information from the selected peer group included total cash compensation (i.e., base salary, bonuses and commissions) and total long-term incentive compensation (i.e., equity in the form of stock options) for executive officers.

Compensation Elements

Based on competitive market information and the Company s compensation philosophy and objectives, the CEO submits his recommendations for executive compensation for the upcoming fiscal year to the Compensation Committee toward the end of the fiscal year. The Compensation Committee reviews these recommendations and can decide to accept or modify them. The Compensation Committee then submits its recommended proposal to the full board of directors for approval at the first meeting in the new fiscal year.

The Company s executive officer compensation packages combine and allocate cash and equity-based compensation taking into account the role of each executive officer of the Company, market practices, and the total value of all forms of compensation including benefits and perquisites available to the individual. Our total compensation packages include base salary, annual cash bonuses and commissions, all paid in cash, as well as long-term compensation in the form of stock options. The rationale, design, reward process, and related information regarding the components of compensation are described generally below.

We do not currently have any equity or other security ownership policy that mandates ownership of certain amounts of our common stock by our executive officers. We have change of control arrangements with each of our executive officers, which provide for such executives to receive certain payments and benefits if their employment with the Company is terminated. These arrangements are discussed in detail below. The board of directors has determined that such payments and benefits are an integral part of a competitive compensation package for our executive officers.

Cash Compensation

Base Salary. Base salaries are provided as compensation for day-to-day responsibilities and services to the Company. Executive salaries are reviewed annually. Other than the annual bonus program described below, there are no profit-sharing or deferred compensation programs.

For fiscal year 2006, the Compensation Committee reviewed salaries recommended by the Company s CEO for the executive officers, and recommended the base salary of each executive officer on a case-by-case basis taking into account the individual officers responsibilities and performance, the competitive market information provided by Radford and the compensation objectives of the Company. For fiscal year 2006, the Company referenced the 50th percentile of the base salaries of executives in the Radford comparative peer group having similar responsibilities to the Company s executive officers, along with other relevant information. The Compensation Committee approved and recommended to the board of directors the following base salary increases for fiscal 2006 for our named executive officers effective January 1, 2006:

Mr. Jankov s base salary was increased by 20.0% from 2005 to $285,000;

Mr. Witmer s base salary was increased by 7.5% from 2005 to $242,000;

Mr. Srinivasan s base salary was increased by 7.5% from 2005 to $212,000;

Mr. Korgav s base salary was increased by 8.0% from 2005 to $207,000; and

Ms. Zander s base salary was increased by 8.0% from 2005 to $227,000.

In addition to base salary, Ms. Zander, our Vice President of Sales, was paid a commission of 0.13% on all product sales, or $124,998, in fiscal 2006.

Additionally, after reviewing competitive market compensation information and the performance of the Company and each individual executive officer in fiscal 2006, and based on the recommendation of the Company s CEO, the Compensation Committee approved and recommended the following base salary increases for our named executive officers for fiscal 2007, which were approved by the board of directors on January 17, 2007:

Mr. Jankov s base salary was increased by 10% from 2006 to $313,500;

Mr. Witmer s base salary was increased by 5% from 2006 to $254,100;

Mr. Srinivasan s base salary was increased by 5% from 2006 to $222,600;

Mr. Korgav s base salary was increased by 5% from 2006 to $217,400; and

Ms. Zander s base salary was increased by 5% from 2006 to $238,400.

In addition, the Compensation Committee recommended that Ms. Zander receive a commission of 0.13% on all product sales in fiscal 2007, which also was approved by the board of directors.

Mr. Hamamatsu served as our interim chief financial officer from October 24, 2006 to January 17, 2007 while Mr. Witmer was on medical leave. Mr. Hamamatsu received a base salary increase of 5.0% in August 2006 in connection with his annual performance review, but did not receive a salary increase for serving as interim.

Bonuses. Our annual cash bonus plan is designed to reward our executive officers and other key contributors for achieving annual individual and Company strategic and financial goals. The Compensation Committee reviews annual bonuses recommended by the Company s CEO for the executive officers, and sets the annual bonus of each executive officer on a case-by-case basis taking into account the individual s level of responsibilities and performance. The Compensation Committee gives substantial weight to the recommendations of the Company s CEO with regard to the bonus payable to the other executive officers. The Compensation Committee also considers market information and the annual bonuses and other incentives paid to executive officers within the peer groups. The Compensation Committee recommends annual executive cash bonuses to the Company s board of directors for their approval at their first meeting after the end of a fiscal year. Based on the CEO s recommendation, the Compensation Committee and board of directors set the following bonus targets for each executive officer as a percentage of their respective 2006 base salaries: 42.2% for Mr. Jankov; 26.7% for Mr. Witmer; 26.1% for Mr. Korgav; 23.8% for Ms. Zander; and 25.4% for Mr. Srinivasan. Each executive officer s performance goals for 2006 were established by the CEO and the Compensation Committee to be achievable by each officer when performing at or above a performance level that the Company believes would be expected of a similarly situated officer of a competitive peer company.

For fiscal year 2006, our Compensation Committee and board of directors set approved a cash bonus pool equal to 5.5% of our non-GAAP net income for fiscal 2006. Our Non-GAAP net income for fiscal year 2006 can be calculated by removing the following expenses from GAAP net income reported our Form 10-K for the year ended December 31, 2006: (1) stock-based compensation expense of $11.9 million, and (2) the following charges totaling $13.0 million associated with the acquisition of the network search engine business from Cypress Semiconductor Corporation: amortization of intangible assets, an in-process research and development charge and the effect of a fair value adjustment to acquired inventory.

Because we exceeded our non-GAAP net income target for fiscal year 2006, the annual cash bonus pool was larger than we had anticipated. Consequently, based on recommendations by the CEO and the Compensation Committee, the board of directors approved larger cash bonuses for the executive officers for fiscal year 2006. These bonuses are disclosed in the Non-Equity Incentive Compensation Plan Compensation column under Summary Compensation Table below. The fiscal year 2006 bonuses were paid in January 2007.

Long-Term Incentive Compensation

Stock Options. Based on our compensation philosophy and objectives, we intend to pay a substantial portion of the total compensation for our executive officers in the form of long-term equity incentives. Historically, this has been in the form of stock option awards that vest over a defined period of employment, which we believe best encourages employee retention and long-term performance, and aligns employee and stockholder interests. Stock options typically have been granted to executive officers when the executive first joins the Company, and annually as part of each executive s annual performance review.

In general, options are granted with an exercise price equal to the fair market value of the common stock on the grant date. As defined in our stock option plans fair market value is the closing price of our common stock as quoted on the applicable trading market on the grant date. Typically, the Compensation Committee awards stock options that vest and become exercisable solely on the basis of continued employment, or other service, usually with respect to 25% of the total shares within one year after the date of grant and 1/48th of the total shares per month of service thereafter.

Option Grant Practices. Our board of directors has delegated to the Compensation Committee the authority to grant stock and other equity awards including awards to our executive officers. The Compensation Committee believes that having pre-determined grant dates throughout the year reduces the degree of subjectivity of option grant date selection, provides greater transparency to its option granting practices, and informs potential grantees of dates certain when grants may occur. In May 2006, the Compensation Committee adopted the following general procedures relating to the grant of stock options and other awards.

All new employee equity grants and existing employee annual performance-based equity grants will be presented by management for consideration by the Compensation Committee at each of the quarterly regularly scheduled Committee meetings;

The Compensation Committee will consider management s recommendations and determine, in its judgment, the appropriate equity grants to be awarded to each employee of the Company with reference to guidelines previously approved by the Compensation Committee for the fiscal year; and

In each calendar quarter the Compensation Committee may grant equity awards to new and existing employees of the Company including executive officers only on the fourth trading day after the public release by the Company of its financial results for the most recently ended fiscal quarter.

In early fiscal year 2007, senior management and the Compensation Committee determined that the Company needed more opportunities to grant stock options to better match option grant dates with the hiring of new employees and the annual performance reviews of existing employees. Starting in April 2007, the Compensation Committee will grant stock options to executive officers and other employees of the Company only on the fifth day of each calendar month, or the next trading day if the NASDAQ Stock Market is closed on that date. In all circumstances, however, options will be considered granted only on the date the Compensation Committee meets and approves the grants, or the date on which all members of the Compensation Committee sign a unanimous written consent approving the grants.

The Compensation Committee annually reviews the long-term equity compensation provided to the Company s executive officers to further the Company s compensation philosophy and objectives to attract, retain and motivate its executive officers. Toward the end of each year the CEO submits his recommendations for target equity awards for the executive officers as group and for each executive officer for the following fiscal year to the Compensation Committee, which may accept or modify his recommendations. The Committee then recommends target annual equity awards to the board of directors for approval at the first meeting of the board in the new fiscal year. The board of directors has given the Compensation Committee discretion to grant equity awards to the executive officers on a case-by-case basis taking into account the target annual equity award and each individual s performance and need of the Company to retain, reward and motivate the individual executive officers.

In determining the size of option awards for fiscal year 2006, the Compensation Committee and the board of directors took into account a number of standard compensation factors, as well as the following special considerations:

- the Company s size, industry and growth rate;
- hiring of new employees in connection with the acquisition of the network search engine business of Cypress Semiconductor Corporation;
- the competitive market for highly skilled talent; and
- that the target stock option pool for the Company in 2006 would be approximately 6% to 8% of the common shares outstanding.

The Compensation Committee and the board of directors also determined that all executive officers as a group, including executive officers that are not named executive officers, should be targeted to receive approximately 1.5% of the number of shares outstanding on December 31, 2005. Based on the foregoing, in fiscal year 2006 the Compensation Committee granted our executive officers as a group options to purchase 256,625 shares of common stock, which represented approximately 1.4% of the 18,061,897 shares of common outstanding on December 31, 2005, and approximately 1.3% of the 20,415,801 shares of our common outstanding on December 31, 2006. These grants are presented in the Summary Compensation Table and Grants of Plan-Based Awards table, below.

The Compensation Committee also determines when to grant stock options to executive officers under the procedures outlined above. The Compensation Committee determines when to grant stock options to our executive officers based on a variety of factors including performance of the individual officers and the Company, volatility of the Company s stock price, and the need of the Company to retain, motivate and promote the executive officers.

Based on a recommendation from the Company s CEO, the Compensation Committee granted stock options to our executive officers on February 23, 2006, August 1, 2006 and October 31, 2006. Each grant was approximately one-third of the annual target grant for each individual, and is listed in the Grants of Plan-Based Awards table below. The Compensation Committee granted multiple installments of stock options to the executive officers in an attempt to average the exercise price of stock option grants to recipients over the course of the year, and to recognize individual and Company achievement of performance goals, which included exceeding the strategic and financial goals for the Company for fiscal year 2005, successfully acquiring a network search engine business from Cypress Semiconductor Corporation, successfully developing our new and most-advanced NL7000 and NL8000 knowledge-based processors, and increasing product revenue, gross margins, and non-GAAP net income in fiscal 2005 and fiscal 2006.

In determining the size of target option awards for fiscal year 2007, the Compensation Committee and the board of directors considered the same compensation factors they considered for fiscal year 2006, and targeted the stock option pool for the Company at approximately 5% to 7% of the common shares outstanding, and all executive officers as a group, at approximately 1.5% of the number of shares outstanding. Based on recommendations by the CEO, the Compensation Committee awarded approximately two-thirds of the 2007 executive officer pool early in the year to enhance the incentive and retention benefits of the awards. Each award vests and becomes exercisable solely on the basis of continued employment, or other service, with respect to