RIVERSTONE NETWORKS INC
Form 10-K
May 31, 2002

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

x **ANNUAL REPORT UNDER SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended March 2, 2002

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to

Commission File Number 0-32269

Riverstone Networks, Inc.

(Exact name of Registrant as specified in its charter)

Delaware	**95-4596178**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

5200 Great America Parkway, Santa Clara, California 95054
(Address, including zip code)

Registrant s telephone number, including area code: (408) 878-6500

Securities registered pursuant to Section 12(b) of the Act:

None

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, $0.01 par value

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months, (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES x **NO** ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein and will not be contained, to the best of the registrant s knowledge, in definitive proxy for information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ¨

As of May 24, 2002, 122,704,863 shares of the Registrant s common stock were outstanding. The aggregate market value of the registrant s voting stock held by non-affiliates of the registrant as of May 24, 2002 was approximately $470 million, based on the closing sale price on The Nasdaq National Market on that date.

Items 10 (as to directors and Section 16 (a) Beneficial Ownership Reporting Compliance), 11 and 12 of Part III incorporate by reference information from the Registrant s Proxy Statement to be filed with Securities and Exchange Commission in connection with the Solicitation of Proxies for the Registrant s 2002 Annual Meeting of Stockholders to be held on July 30, 2002.

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PART I

In addition to historical information, this Annual Report on Form 10-K contains forward-looking statements. When used in this Report, the words expect, anticipate, estimate, believe, intend, plan, and similar expressions are intended to identify forward-looking statements. The statements that relate to future periods and include statements as to the features, benefits, performance and utility of our current and future products, services and technology, the expected benefits of our products and services to our customers, including reduced operating costs and expansion of metropolitan networks, our competitive position, our research and development efforts, customer mix, plans to expand sales organizations, our strategy for protecting our proprietary rights, the adequacy of our facilities, the impact and timing of current and future legal proceedings, the potential offer to repurchase certain options and shares received upon exercise of certain options, our strategic investments, our expectations regarding net income or losses, trends in average selling prices, gross margins and revenues, changes in product mix, inventory levels, the adequacy of allowances for doubtful accounts, expectations regarding expenses, cost of revenues and sources of revenues, expected stock-based compensation expenses, expected cost structure reductions as a result of restructuring, statements regarding our critical accounting policies, the adequacy of capital resources and expected variations in capital requirements, expectations regarding capital expenditures and growth of operations and infrastructure, strategic investments, plans to expand sales organizations, expectations regarding the development and maintenance of strategic distribution relationships and our exchange risk management strategy. Forward-looking statements involve risks, uncertainties and assumptions. The actual results may differ materially from those anticipated in these forward-looking statements as a result of many factors, including, but not limited to, our ability to successfully bring future products to market, gain market share and compete against established companies in our market, the impact of alternative technological advances and competitive products, our dependence on large orders from a small number of customers, our ability to protect our intellectual property rights, our dependence upon single or limited sources for components and upon a single manufacturer, our ability to develop and maintain strategic relationships, and those discussed in the section entitled Management s Discussion and Analysis of Financial Condition and Results of Operations Risk Factors That May Affect Future Results and Market Price of Our Stock. Readers are cautioned not to place undue reliance on these forward-looking statements, which reflect management s opinions only as of the date hereof. Riverstone Networks, Inc. (the Company, Riverstone, us or we) undertakes no obligation to revise or publicly release the results of any revision to these forward-looking statements. Readers should carefully review the risk factors described in this document as well as in other documents the Company files from time to time with the Securities and Exchange Commission, including the Quarterly Reports on Form 10-Q to be filed by the Company in fiscal year 2003.

ITEM 1. ***Business***

Overview

Separation from Cabletron

We were previously a subsidiary of Cabletron Systems, Inc. We completed our initial public offering on February 22, 2001. On August 6, 2001, Cabletron distributed all of its shares of our common stock to its stockholders and we ceased to be a subsidiary of Cabletron. On the same date, Cabletron merged its subsidiary Enterasys Networks, Inc. into itself and renamed itself Enterasys Networks, Inc.

We were initially incorporated as Yago Systems, Inc. in September 1996 in the state of Delaware. Yago was acquired by Cabletron in March 1998 and became a wholly owned subsidiary of Cabletron. In April 2000 Cabletron changed Yago s name to Riverstone Networks, Inc., and in June 2000 we entered into agreements with Cabletron, Aprisma Management Technologies, Inc., Enterasys and GlobalNetwork Technology Services, Inc. relating to the separation of our business from Cabletron.

Business

We are a leading provider of metropolitan area networking solutions that enable service providers to convert raw bandwidth into profitable services over legacy and next-generation infrastructures. Our routers are specifically designed for the metropolitan area network, or MAN, which encompasses service providers, the Internet infrastructure connecting these service providers with their customers and the Internet backbone within the geographic area of a city. Service providers today are seeking to build scalable networks to deliver new revenue-generating services to their end-customers. Our products combine carrier-class routing features and interface versatility with important service creation technologies such as Multiprotocol Label Switching, or MPLS, for layer-2 virtual private networks or VPNs, bandwidth management, dynamic provisioning, hardware-based accounting data collection, and quality of service.

Historically the public network infrastructure, including MANs, was traditional telephone networks optimized for transporting voice traffic. With the advent of the Internet, these networks began to carry data traffic in addition to voice traffic. The Internet is a network of public and private networks interconnected using Internet Protocol, or IP, that allow millions of users worldwide to share information and conduct electronic commerce. Since inception, the Internet and IP traffic have continued to grow exponentially, creating a need for service providers to build IP-centric networks optimized to carry data traffic. In addition to the rapid growth of the Internet, end-user demand has developed beyond basic bandwidth and connectivity to sophisticated business applications and advanced services. Service providers are seeking to build networks with advanced capabilities to deliver these services to their customers in a cost effective manner. Our products are built to meet the needs of the growing MAN and offer service providers an optimized solution for the cost-effective delivery of advanced applications and services to their customers.

Our target customers include communications service providers worldwide, which include local exchange carriers, long distance carriers, Internet service providers, metropolitan service providers, content hosting providers, and cable operators. We sell and market our products primarily through our direct sales organization, original equipment manufacturers, or OEMs, and value-added resellers.

Our Solution

We design and manufacture routers that enable service providers to convert network bandwidth into differentiated services for their customers. We provide both metro access and metro aggregation solutions that combine versatile connectivity with important service creation technologies such as MPLS for layer-2 VPNs, bandwidth management, dynamic provisioning, hardware-based accounting data collection, and quality of service. These features allow service providers in the metro area to penetrate new markets quickly, build solid revenue streams, and establish a competitive advantage. Specifically, our products benefit customers in the following ways:

Network Availability, Reliability and Security

Our products provide high levels of network availability, reliability, and resilience even under heavy network traffic conditions. We achieve this by combining our custom application specific integrated circuits, or ASICs, with our RapidOS software in a scalable, modular architecture. Our routers are interoperable with a variety of products from other vendors. In collaboration with our customers, we have developed a testing environment that includes real world configurations, allowing us to deliver reliable products. Our products meet numerous regulatory requirements and our most advanced products are designed to be Network Equipment Building Systems, or NEBS, compliant. Our products also incorporate numerous security protocols for supporting VPNs and secure network access.

Service Creation

We have designed our products as platforms on which service providers can deliver sophisticated and differentiated services. The key service enablers that are embedded in our products are:

Multiprotocol Label Switching (MPLS). Our products offer advanced, secure service capabilities through the use of MPLS technology. MPLS promotes higher performance of IP networks and allows traffic engineering. With MPLS, service providers can maximize their capital returns by selling premium levels of service, such as bandwidth guarantees, fast recovery times, customized backup resources, as well as nation- or world-wide Transparent LAN Services.

Bandwidth Management. Our products offer advanced capabilities to manage bandwidth in real-time, without sacrificing network performance. Our products allow our customers to remotely set bandwidth limits from one kilobit to one gigabit and easily integrate with leading bandwidth management software.

Dynamic Provisioning. As customer and application bandwidth needs change, commands sent remotely to our products can instantly and inexpensively set-up, modify or terminate connections.

Accounting Data Collection. Our products support hardware-based accounting data collection, allowing service providers to collect real-time customer usage data and billing information without affecting network performance. This allows service providers to create and offer advanced pricing structures tailored to their customers needs by usage, by time-of-day and by location.

Quality of Service. Our products separate traffic into multiple service classes based on end-user identity, application type, time-of-day and other attributes. Our quality of service features allow service providers to improve service quality by assigning priority to delay-sensitive or high-priority traffic such as voice or video.

Content Delivery. To increase the speed of content delivery, our products offer network-wide capabilities to create the shortest and most reliable path between the end-user and the content. This is accomplished through advanced traffic management using a broad range of Internet routing protocols.

Flexible Service Delivery Platform

We design our products to operate and adapt to the rapidly evolving demands of our customers network infrastructure. Our open application programming interface allows our products to be easily integrated with the customers bandwidth management, provisioning, accounting, data collection, quality of service and content delivery tools. Our Intelligent Service Router architecture scales with the needs of service providers. Additional line cards can be inserted into our modular chassis to increase bandwidth capacity. If bandwidth is exhausted in one chassis, service providers can link multiple chassis together to obtain additional capacity. Our RapidOS operating system can scale in the face of increasing Internet traffic while continuing to manage bandwidth, deliver routing throughput, and provide differentiated services. New technology interfaces and RapidOS upgrades can be added to in-service chassis without disrupting existing operations. The modular design of our products enable the rapid and easy addition of new services without requiring re-design of network architecture or replacement of existing infrastructure equipment.

Our products support optical and electrical interfaces to ensure that services can be quickly provisioned across a broad range of media types. This means that service providers using our routers can rapidly offer services across almost any infrastructure. This broad range of support is delivered in a single chassis, eliminating the need to purchase multiple solutions or consume limited space.

Cost-effective Infrastructure

Our products allow service providers to start with a low initial capital expenditure while retaining the ability to add bandwidth as demand increases. Using our advanced provisioning capabilities, we believe service providers can reduce their operating costs by eliminating the need to send technicians out into the field to provision service. Our products also offer high port density, which means our chassis occupy less space in expensive hosting facilities. Using our wide array of media interfaces, service providers have the flexibility to choose the most appropriate telecommunications medium to connect customers to their service.

Technology

Our core technology consists of our Intelligent Service Router architecture, our RapidOS software operating system, and our ASICs. These key elements of our technology are incorporated into all of our products. By internally developing and maintaining the critical components for our systems, we believe the performance and features of our systems are superior to those of systems based upon third-party general purpose components. Our modular system architecture, coupled with our core hardware and software, enable us to create new products and solutions by rapidly developing new interfaces, new features and new form factors or sizes.

Intelligent Service Router Architecture. Our product architecture consists of ASIC-based packet forwarding engines distributed on each line card and a centrally located routing engine running our RapidOS operating system, connected together by high-performance ASIC-based switching devices. Our product architecture allows us to deliver the capacity, reliability and features that we believe are necessary to build and expand our customers metropolitan networks.

By distributing packet-processing functions on ASICs located on each line card, rather than on a centrally located general purpose CPU, we are able to offer advanced functions while maintaining wirespeed performance. With this architecture, our products can increase bandwidth by adding line cards without degrading overall performance. Our RS 38000 platform is designed to handle up to 90 million packets per second when all of its line cards are installed.

Programmable Hardware Architecture. This line card architecture, centered on a wire-speed, programmable packet-processing engine, enables service providers to implement new networking technologies such as MPLS as they are introduced in the market through field upgrades.

RapidOS Operating System. RapidOS, our standards-based software operating system, controls the features and functionality of our router platforms. RapidOS incorporates a set of service enabling capabilities to meet the demands of service providers, such as traffic engineering, bandwidth control, network traffic classification and network security. We do not sell RapidOS on a stand-alone basis. We have continued to improve RapidOS since its introduction in 1998 based upon feedback from our customers.

RapidOS allows service providers to collect traffic statistics and billing data in real time. RapidOS also supports all standard Internet class routing protocols, a complete set of industry standards-based layer 2 features and MPLS. RapidOS provides traffic load balancing and content management of electronic-commerce applications. Our RapidOS is also capable of delivering network level redundancy at layer 2 and layer 3.

ASIC Technology. The switching devices and forwarding engines in our products use internally developed ASICs that are designed specifically for our router architecture. These ASICs implement service enabling features such as network traffic classification, accounting, security and bandwidth management. The ASICs are designed to facilitate the rapid implementation of various electrical and optical network interfaces that support transmission speeds from 1.5 megabits per second for a T1 line up to 10 gigabits per second for an optical carrier 192, or OC-192, line. We believe our control over the design and development of ASICs and the close interaction between our hardware and software teams have enabled us to achieve enhanced performance.

Riverstone Products

We offer a wide variety of products to effectively address the broad metropolitan area network needs for aggregation and edge routing applications.

RS 38000 Metro Aggregation Router. The RS 38000 is our high density metro aggregation router. Aggregation routers aggregate and route network traffic at carrier and service provider facilities before it is routed to the Internet backbone. Aggregation routers are also used for aggregating and routing network traffic in co-location centers. The RS 38000 combines service creation tools, dynamic bandwidth provisioning, and a connection-oriented data collection architecture. The RS 38000 is capable of aggregating and delivering these services over a complete range of optical and legacy interfaces and is MPLS enabled. The RS 38000 provides high performance, high port density and high reliability, and has the capability to support OC-192 and 10 Gigabit Ethernet. It can provide up to 90 million data packets per second routing performance.

RS 16000 Gigabit Ethernet Aggregation Router. The RS 16000 is our high density Gigabit Ethernet aggregation router. The RS 16000, designed to aggregate Gigabit Ethernet, provides full metro service-creation capabilities through our hardware-based architecture. The RS 16000 delivers 60 wire-speed Gigabit Ethernet ports on a 5 rack unit chassis. The RS 16000 is designed to support 10 Gigabit Ethernet.

RS 8000/8600 Metro Service Routers. The RS 8000 and RS 8600 are our metro service router products. Metro service routers are used as the Internet access or network traffic aggregation platform where small form factor and low power consumption are required. Metro service routers must support a wide variety of interfaces and service-enabling features. These products aggregate the network traffic and pass it on to the intelligent edge router.

The RS 8000 and RS 8600 are designed specifically to be service delivery platforms across both the optical and electrical segments of the metro network infrastructure. As an aggregation platform, the RS 8000 and RS 8600 offer high port density in a small form factor. As an access platform, the RS 8000 and RS 8600 are ideal for fiber optic cable connectivity in building backbones and data center in co-location facilities. The RS 8000 and RS 8600 are capable of aggregating traffic from a wide variety of access technologies. The RS 8000 and RS 8600 use the same line cards, thus offering maximum flexibility for upgrades.

RS 1000 and RS 3000 Metro Access Routers. The RS 1000 and RS 3000 are our metro access routers with hardware routing capability. Metro access routers are used to connect end-users with metro aggregation facilities. Metro access routers must support traditional connectivity and advanced optical modules for Gigabit, ATM and Packet over SONET up-links.

The RS 1000 and RS 3000 routers support traditional connectivity and advanced optical modules. The RS 1000 and RS 3000 products incorporate all the routing, switching, traffic engineering, accounting and security features of the rest of our router platform but in a smaller, lower cost platform. The RS 1000 and RS 3000 share the same line cards, thus offering maximum flexibility for upgrades.

Wide Array of Supported Line Cards

Our products include line cards that support all of the network technologies identified in this table. All line cards contain all of the service enabling features of Riverstone s architecture.

	RS 38000	RS 16000	RS 8000/8600	RS 1000/3000
10 Gigabit Ethernet	D	D		
MPLS Gigabit Ethernet	ü	D	ü	ü
Packet over SONET OC-192c	D			
Packet over SONET OC-48c/STM-16	ü			
Packet over SONET OC-12c/STM-4			ü	
Packet over SONET OC-3c/STM-1			ü	
MPLS Packet over SONET OC-48c/STM-16	D			
MPLS Packet over SONET OC-12c/STM-4	D		D	
MPLS Packet over SONET OC-3c/STM-1	D		D	
Resilient Packet Ring OC-48c	D		D	
4 or 8 Gigabit CWDM	ü	ü		
Pluggable Gigabit Interface				
1000 Base-LH-70Km reach	ü	ü	ü	ü
1000 Base-LX	ü	ü	ü	ü
1000 Base-SX	ü	ü	ü	ü
1000 Base-T-copper GigE			ü	
ATM OC-12c	D		ü	
ATM OC-3c/DS3	ü		ü	ü
10/100 Base-TX	ü		ü	ü
100 Base-FX			ü	ü
Channelized T3 with CSU/DSU	ü		ü	
Channelized T1 with CSU/DSU			ü	ü
Multi-rate serial WAN			ü	ü
Cable modem termination system-CMTS			ü	

A checkmark indicates that the line card is available now for the listed product. A D indicates that the line card is under development.

Research and Development

As of March 2, 2002, we employed 215 people in our engineering and research and development organization with the majority located in our Santa Clara, California corporate headquarters. We believe that our future success depends on our ability to continually enhance our existing products and develop new products. To achieve this goal, our research and development department is organized into two teams that work in parallel to develop successive generations of networking products. We have assembled a team of skilled engineers with extensive experience in the fields of high-speed microprocessor design, high-end computing, network system design, Internet routing protocols and embedded software. These individuals have been drawn from leading computer, data networking and telecommunications companies. The engineering team s collective experience ranges from building complex hardware and software to delivering very large, highly integrated ASICs and scalable Internet software.

We are using our fourth generation ASICs in our products. We are also developing additional network interfaces targeted to our customer demands and continuing to develop next generation technology to support the anticipated growth in network size and service requirements, such as Resilient Packet Ring/Spatial Reuse Protocol (RPR/SRP), 10-Gigabit Ethernet, OC-48 and OC-192. We continue to expand the functionality and scalability of our RapidOS including advanced MPLS implementations.

Our research and development expenses totaled $50.4 million for the fiscal year ended March 2, 2002, $42.0 million for the fiscal year ended March 3, 2001 and $30.7 million for the fiscal year ended February 29, 2000.

Customers

Our customers include local exchange carriers, long distance carriers, Internet service providers, metropolitan service providers, content hosting providers, and cable operators. As of March 2, 2002, we had approximately 150 customers, the majority of which were located in the United States, Asia Pacific and Europe.

For fiscal year 2000, British Telecommunications plc accounted for 15% of our net revenue, EarthLink, Inc. accounted for 14% of our net revenue, Metricom Corporation accounted for 12% of our net revenue and Vitts Networks accounted for 11% of our net revenue. For fiscal year 2001, Telseon accounted for 11% of our net revenue. During fiscal year 2002 no individual customer accounted for 10% or more of our net revenues. Although our largest customers may vary from period to period, we anticipate that our operating results for any given period will continue to depend significantly on large orders from a small number of customers. We do not have binding commitments from any of our customers, and if any of our large customers cancel, reduce or delay purchases, our revenue and profitability would be harmed.

Sales and Marketing

We sell and market our products primarily through our direct sales organization, value-added resellers and original equipment manufacturers. As of March 2, 2002, we employed 229 people in our sales and marketing organizations.

Sales

Americas Sales. Our direct sales force for the Americas is divided into two operations: Carrier and Americas. The carrier group focuses on local exchange carriers and long distance carriers and the Americas group focuses on Internet service providers, metropolitan service providers, content hosting providers, and cable operators. Account managers within each operation work as a team with account-focused systems engineers to provide our customers with guidance and assistance on incorporating our products into their network. Our systems engineers also help in defining the features that are required for our products to be successful in specific applications. Our sales team maintains contact with key individuals who have service planning and infrastructure build-out responsibility within our customers organizations.

Value-added Resellers. We have complemented our direct sales effort in the United States and internationally with several value-added resellers. Our arrangements with value-added resellers typically have been non-exclusive and provide the value-added reseller with discounts based upon the volume of their orders.

International Sales. Our international sales are made through a combination of direct and indirect sales efforts. Our European operation is headquartered near London, with sales offices in France and Spain. Our Asia Pacific operation is headquartered in Singapore with offices in China, Japan and Korea. Additionally, we have a sales office in Brazil. Our indirect sales are made through various international network integrators including Telindus Group NV, CommVerge Solutions, CTC Itochu-Techno Science Corporation, KDC Corporation, Vodatel Networks Holdings Limited and ZTE Corporation. Our export sales represented 52%, 32% and 23% of net revenue in fiscal years 2002, 2001 and 2000, respectively. Our sales by geographic region are disclosed in Note (13) to the consolidated financial statements included in this Form 10-K. Our efforts to expand international distribution of our products continue to subject us to the risks of conducting business internationally, including those set forth under Management s Discussion and Analysis of Financial Condition and Results of Operations Factors that May affect Future Results and Market Price of Our Stock We continue to expand our international sales efforts, and marketing and distributing our products outside of the United States may require increased expenses and greater exposure to risks that we may not be able to successfully address.

Marketing

Our marketing objectives include building market awareness and acceptance of the Riverstone brand and our products, and creating qualified customer leads. Our marketing activities include participation in tradeshows and technical conferences, preparation of sales tools, business cases, competitive analyses and other marketing collateral and sales training. Our marketing activities also include the publication of press releases, new product information and educational articles in industry journals, maintenance of our website and direct marketing to prospective customers.

Service and Support

We believe that a broad range of support services is critical to the development of long-term relationships with customers. We are committed to providing our customers with a high level of service and support through our internal organization and arrangements with third parties. As of March 2, 2002, we employed 17 people in our customer service and support organization, the majority of whom are located in our Santa Clara, California corporate headquarters.

Currently our customer service and support functions are provided by a combination of our customer service organization, Riverstone Technical Assistance Center, or RTAC, organization and Field Technical Support organization. We deliver our support services to customers using a three-tier support model. Our first tier of support services is technical assistance through Web self-help and internal telephone support. During the past twelve months, we transitioned the services previously provided by Digital Equipment (India) to internal support services. We provide field support services, our second tier of support services, to our contract customers when telephone support is not sufficient to address an issue. To enhance our internal field support services, we have an infrastructure of field-based technical support resources as well as partnerships with several third-party engineer, furnish and install, or EF&I, providers and professional services and maintenance service providers, including Fujitsu, Tele-Tech, Greenwich Technology Partners and ViTAL Network Services to augment our capabilities and coverage globally. If the first two tiers of our customer service and support team are unable to resolve an issue themselves, they obtain assistance from members of our engineering department who serve as the third level of the customer support. We have established problem escalation guidelines to focus appropriate technical resources and management attention on customers problems in a timely manner.

Manufacturing

We out-source our manufacturing activities to Flextronics International. Flextronics manufactures our products in San Jose, California.

Under our relationship with Flextronics, we design, specify and monitor all of the tests that are required to meet internal and external quality standards. Flextronics obtains materials, undertakes final assembly of prototype and production products, tests our products and ships them to our customers. This strategic relationship allows us to concentrate on further developing our offerings and eliminates the need to dedicate resources to manufacturing activities. This arrangement also allows us to adjust manufacturing volumes quickly to meet changes in demand.

We design our ASICs and printed circuit boards and work closely with our partners on future component selection and design support. All materials used in our products are processed through a full qualification cycle and our sourcing is controlled by the use of an approved vendor listing. We perform extensive examinations of all printed circuit board assemblies, full functionality verifications, 24-hour burn-in and power-cycling at maximum and minimum configuration levels. Our ASICs are manufactured by NEC Corporation using its 0.35 micron process, Agere Systems using its 0.25 micron process and LSI Logic Corporation using its 0.18 micron process. NEC, Agere and LSI Logic are responsible for all aspects of the production of our ASICs using our proprietary designs. We periodically evaluate these and other ASIC vendors to identify the best fit with our ASIC technology needs.

Competition

There is significant competition in the market for network equipment. This market has historically been dominated by Cisco Systems, Inc. Other existing and potential competitors are numerous and include established companies such as Extreme Networks, Inc., Foundry Networks, Inc., Juniper Networks, Inc., Nortel Networks Corporation and other smaller public and private companies. Several of these companies have been in business longer than us and have substantially greater financial, marketing and development resources than we have, which we believe may put us at a competitive disadvantage. Many of these competitors are in a better position than us to provide customers total network infrastructure solutions. Many of these competitors have announced plans to introduce or develop new products that are likely to compete with our product offerings. Future consolidation in our industry is a distinct possibility, and acquisitions by, or mergers among, our competitors could expand their product offerings and hasten their development of new technologies, providing them with a competitive advantage.

Our customers include local exchange carriers, long distance carriers, Internet service providers, metropolitan service providers, content hosting providers, and cable operators. We believe that the principal competitive factors in this market include product performance, reliability, security, expandability, features and cost-effectiveness. Our products provide:

- high network reliability, security and performance;
- the ability to allow carriers and service providers to offer differentiated services;
- easy scalability and minimal network disruption;
- interoperability with existing network designs and equipment vendors;
- versatility of interfaces; and
- cost-effective solutions for carriers and service providers.

We believe these capabilities, when combined with our exclusive focus on carriers and service providers in the MAN, and our commitment to providing superior support services provide us with a competitive advantage.

Intellectual Property

Our ASICs are the key components in our products. One of our ASIC families is manufactured by NEC, another by Agere and another by LSI Logic. Each successive ASIC design has allowed faster network interfaces, greater service provider functionality and increased port density. Both we and Enterasys share the basic technology embedded in the ASICs manufactured by NEC. However, we do not share with Enterasys our later ASIC families manufactured by Agere and LSI Logic or our service provider specific network interfaces.

Our router architecture requires an operating system that takes full advantage of the features in our ASIC system. Our RapidOS management system includes enhancements and customizations to address specific needs of service providers in the metropolitan area.

To establish and protect our intellectual property, we generally rely on a combination of patent, copyright, trademark and trade secret laws and contractual restrictions. As of March 2, 2002, we had 15 patents in the United States and 53 patents pending in the United States and abroad. Our issued patents expire at various times between January 2016 and November 2018. Our RapidOS management system is protected by United States and other trade secret and copyright laws. These legal protections provide only limited protection. Further, the market for Internet infrastructure solutions is subject to rapid technological change. While we intend to continue to protect our proprietary rights where appropriate, we believe that our success in maintaining a technology leadership position is more dependent on the technical expertise and innovative abilities of our personnel rather than on these legal protections.

Despite our efforts to protect our proprietary technology, we cannot assure you that the steps we take will be adequate to prevent misappropriation of our technology or that our competitors will not independently develop technologies that are substantially equivalent or superior to our technology. The laws of many countries do not protect our proprietary technology to as great an extent as do the laws of the United States. We may need to resort to litigation in the future to enforce our intellectual property rights, to protect our trade secrets, to determine the validity and scope of the proprietary rights of others or to defend against claims of invalidity. We are also subject to the risk of adverse claims and litigation alleging infringement of the intellectual property rights of others. Any resulting litigation could result in substantial costs and diversion of management and other resources and could have a material adverse effect on our business and financial condition.

Employees

As of March 2, 2002, we had 525 full-time employees, 215 of whom were engaged in engineering, research and development, 229 in sales and marketing, 26 in manufacturing, 17 in customer support and 38 in finance, administration and operations. None of our employees is represented by a labor union. We have not experienced any work stoppages and we consider our relations with our employees to be good.

ITEM 2. ***Properties***

Our principal administrative, sales, marketing and research and development facilities are located in an approximately 129,200 square foot facility located in Santa Clara, California. Cabletron Systems Sales and Service, Inc. entered into a lease for this facility in January 1999, and assigned this lease to us on August 28, 2000 following the separation of our business from Cabletron. The initial term of the lease expires on February 28, 2006. We also lease space in various other geographic locations, including Alpharetta, Georgia; Denver, Colorado; Frisco, Texas; McLean, Virginia; New York, New York; Portsmouth, New Hampshire; Reading, United Kingdom; Beijing, PRC; Hong Kong, PRC; Shanghai, PRC; Taiwan, ROC; Singapore; Seoul, Korea; Tokyo, Japan; Sao Paolo, Brazil and other international locations where principally sales and service personnel and engineers are based.

We believe that our existing facilities are adequate to meet current requirements, and that suitable additional or substitute space will be available as needed to accommodate any further physical expansion of corporate operations and for any additional sales offices.

ITEM 3. ***Legal Proceedings***

A consolidated class action lawsuit raising claims against Cabletron and some officers and directors of Cabletron was filed in the United States District Court for the District of New Hampshire and, following transfer, is pending in the District of Rhode Island. The complaint alleges that Cabletron and several of its officers and directors made materially false and misleading statements about Cabletron s operations and acted in violation of Section 10(b) of and Rule 10b-5 under the Securities Exchange Act of 1934 during the period between March 3, 1997 and December 2, 1997. The complaint also alleges that Cabletron s accounting practices resulted in the disclosure of materially misleading financial results during the same period. More specifically, the complaint challenged Cabletron s revenue recognition policies, accounting for product returns, and the validity of some sales. The complaint does not specify the amount of damages sought on behalf of the class. The plaintiffs served a second consolidated class action complaint and Cabletron filed a motion to dismiss this complaint. In a ruling dated May 23, 2001, the district court dismissed this complaint with prejudice. The plaintiffs have appealed this ruling to the First Circuit Court of Appeals. If the plaintiffs were to prevail on appeal, and ultimately prevail on the merits of the case, Enterasys (formerly known as Cabletron) could be required to pay substantial damages.

We have not assumed any liabilities from Enterasys for this litigation. We have not been named as a defendant in this litigation and none of our officers or directors is named as a defendant to this litigation. However, the plaintiffs might attempt to involve us in this litigation or might seek to have us pay damages if

Enterasys has insufficient assets to cover any resulting damages. Any involvement in this litigation could be protracted and may result in a diversion of management and other resources. The payment of substantial legal costs or damages, or the diversion of our management and other resources, could have a material adverse effect on our business, financial condition or results of operations.

On August 28, 2001, Tellabs Operations, Inc. filed an action against us in the Chancery Division of the Circuit Court of Cook County, Illinois alleging that Riverstone breached the Strategic Alliance Agreement dated as of November 17, 2000 between Riverstone and Tellabs and committed various torts by (i) failing to provide Tellabs with CMTS products that met the technical specifications in the agreement; (ii) misrepresenting to Tellabs the technical capabilities of Riverstone s CMTS products; and (iii) improperly selling Riverstone products to Tellabs customers. Tellabs complaint seeks compensatory damages in excess of $15 million, plus punitive damages and costs in unspecified amounts. On that same date, Tellabs terminated the agreement and is seeking a declaratory judgment that it has no further obligations under the agreement. We believe that Tellabs claims are without merit and intend to vigorously defend this proceeding. On August 29, 2001, Riverstone filed suit against Tellabs in the Superior Court for Santa Clara County, California seeking compensatory damages in excess of $60 million, including over $56 million in unfulfilled minimum purchase obligations Tellabs was required to make under the agreement. On December 7, 2001, Riverstone withdrew its suit without prejudice to re-file at a later time. On January 9, 2002, Riverstone asserted numerous affirmative defenses and counterclaims against Tellabs in the Illinois action, including claims for breach of contract, fraud, negligent misrepresentation, and violations of the Illinois Consumer Fraud and Deceptive Business Practice Act. Through its counterclaims, Riverstone seeks $57 million in compensatory damages, in addition to punitive damages, attorneys fees and costs.

We have granted options to purchase shares of our common stock under our 2000 Equity Incentive Plan to our employees and employees of Cabletron and its affiliates and to our advisors and consultants. As a result of the nature of the persons who received these options and the vesting provisions of these options granted prior to February 22, 2001, we may have violated the California state securities laws. Because these option grants may not have been qualified or exempt from qualification under California state securities laws, certain persons residing in California who received these options may have a claim against us. Accordingly, we may offer to repurchase, from persons who resided in California at the time of grant, outstanding options to purchase shares of our common stock granted under our 2000 Equity Incentive Plan prior to February 22, 2001 and shares acquired upon exercise of options granted prior to February 22, 2001. We have not yet determined whether or when to make the offer to repurchase. If an offer to repurchase is actually made and if all of the holders of these options (and shares acquired upon exercise of these options) accept the offer, our cash position could be adversely impacted. As of the date hereof, we are not aware of any claims for rescission against us.

On January 31, 2002, the Securities and Exchange Commission notified Enterasys Networks that it had commenced an Order of Investigation into Enterasys and certain of its affiliates accounting practices. This SEC investigation may cover periods during which Riverstone was an affiliate of Enterasys. We have not been notified that we are part of the SEC investigation, nor have we received any inquiry with respect to the investigation. On August 6, 2001, when Cabletron distributed all of its shares of our common stock to its stockholders, we ceased to be a subsidiary of Cabletron and an affiliate of Enterasys. We have been operating with our own management and board of directors since our IPO in February 2001.

We are not aware of any other legal proceedings against us that, individually or in the aggregate, would have a material adverse effect on our business, operating results or financial condition. We may in the future be party to litigation arising in the course of our business, including claims that we allegedly infringe third-party trademarks and other intellectual property rights. These claims, even if not meritorious, could result in the expenditure of significant financial and managerial resources.

ITEM 4. ***Submission of Matters to a Vote of Security Holders***

No matters were submitted to a vote of security holders during the fourth quarter of fiscal year 2002.

PART II

ITEM 5. ***Market for Registrant s Common Equity and Related Stockholder Matters***

Price Range of Common Stock

Our common stock commenced trading on The Nasdaq National Market on February 16, 2001 and is traded under the symbol RSTN. Prior to this time, there was no public market for our stock. The following table sets forth for the periods indicated the high and low closing sale prices for our common stock as reported on The Nasdaq National Market.

Fiscal Year 2001	**High**	**Low**
Fourth Quarter: February 16, 2001 to March 3, 2001	$ 14.50	$ 10.50
Fiscal Year 2002		
First Quarter: March 4, 2001 to June 2, 2001	$ 23.66	$ 6.63
Second Quarter: June 3, 2001 to September 2, 2001	23.04	9.48
Third Quarter: September 3, 2001 to December 1, 2001	16.21	5.25
Fourth Quarter: December 2, 2001 to March 2, 2002	20.55	3.82
Fiscal Year 2003		
First Quarter: March 3, 2002 to May 24, 2002	$ 6.86	$ 3.53

As of May 24, 2002, there were approximately 2,500 holders of record of our common stock.

Dividend Policy

We have never declared or paid any cash dividends on our common stock. We intend to retain any future earnings for funding growth and do not expect to pay any dividends in the near future.

Recent Sales of Unregistered Securities

On July 24, 2001, we issued 7,117,757 shares of our common stock to Cabletron in exchange for approximately $122.2 million in cash and certain strategic investments, with a historic cost of approximately $13.0 million.

On August 6, 2001, concurrently with the distribution by Cabletron of our capital stock to its stockholders, we were required to issue warrants to certain strategic investors to purchase 230,364 shares of our common stock, which is based on the number of shares that the investors would have received in such distribution if the investors had exercised the Cabletron warrants they held immediately prior to the record date related to the distribution. These warrants have a weighted average exercise price of $29.18 per share and will expire on August 29, 2007.

The issuances described in this Item 5 were deemed to be exempt from registration in reliance upon Section 4(2) of the Securities Act of 1933, as amended, as a transaction by an issuer not involving any public offering.

ITEM 6. ***Selected Consolidated Financial Data***

The data set forth below should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations and the Consolidated Financial Statements and related Notes included in Item 8 of this Report.

We have prepared the accompanying tables to reflect our historical consolidated financial information in a manner consistent with stand-alone operations by reflecting transactions of Cabletron and balances attributable to us in our financial statements for all periods presented. The historical financial information may not be indicative of our future performance and does not necessarily reflect what our financial position and results of operations would have been had we operated as a separate, stand-alone entity during the periods covered.

	Years Ended			
Mar 2, 2002	**Mar 3, 2001**	**Feb 29, 2000**	**Feb 28, 1999**	**Feb 28, 1998**