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

FORM 10-Q/A

Amendment No. 1

(Mark One)

☑	**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.**
	For the quarterly period ended January 29, 2005

OR

o	**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.**
	For the transition period from __________ to __________

Commission file number: 000-25601

BROCADE COMMUNICATIONS SYSTEMS, INC.
(Exact name of Registrant as specified in its charter)

Delaware	**77-0409517**
(State or other jurisdiction of incorporation)	(I.R.S. employer identification no.)

1745 Technology Drive
San Jose, CA 95110
(408) 333-8000
(Address, including zip code, of Registrant's principal executive offices and telephone number, including area code)

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

Yes o No ☑

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act).

Yes ☑ No o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No ☑

The number of shares outstanding of the Registrant's Common Stock on February 26, 2005 was 268,513,849 shares.

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EXPLANATORY NOTE:

This quarterly report on Form 10-Q/A constitutes Amendment No. 1 to the quarterly report on Form 10-Q filed by Brocade Communications Systems, Inc. (the "Company") originally filed with the Securities and Exchange Commission on March 9, 2005, for the quarterly period ended January 29, 2005. This Form 10-Q/A is being filed solely for the following purposes:

- Revising Item 1. Financial Statements; and
- Revising Item 4. Controls and Procedures

On January 24, 2005, we announced that our Audit Committee completed an internal review regarding our stock option granting process. As a result of certain findings of the review, on January 31, 2005 we filed our Form 10-K for the year ended October 30, 2004, which included the restatement of our historical financial statements for fiscal years ended October 25, 2003 and October 26, 2002, including the corresponding interim periods for fiscal year 2003, and the interim periods ended January 24, 2004, May 1, 2004, and July 31, 2004 ("January 2005 Restatement"). Please refer to Note 3, "Restatements of Consolidated Financial Statements," of the Notes to Condensed Consolidated Financial Statements.

Following the original filing of our Form 10-K on January 31, 2005, additional information came to our attention that indicated that we could not rely on the documentation used to support the recorded measurement dates for stock options granted in the period from August 2003 through November 2004. As a result, we recorded a cumulative increase in non-cash stock option compensation expense of approximately $0.9 million over fiscal years 2003 and 2004. In addition, we determined that from 1999 through 2004 we had not appropriately accounted for the cost of stock-based compensation for certain employees on leaves of absences ("LOA") and in transition or advisory roles prior to ceasing employment with us. This resulted in an increase in non-cash compensation expense of approximately $0.9 million, $0.2 million and $20.0 million in fiscal years 2004, 2003 and 2002, respectively, and an aggregate of approximately $49.9 million in fiscal years 1999 through 2001. We also determined that we could not rely on the documentation used to support the recorded dates for certain stock option exercises that resulted in immaterial adjustments included in the restatement, consisting of approximately $0.1 million in fiscal year 2002 and an aggregate of approximately $0.3 million in fiscal years 1999 through 2001. Accordingly, we have restated our Condensed Consolidated Balance Sheet as of January 29, 2005 to reflect the cumulative effect of the restatement. The foregoing restatement adjustments did not affect our previously reported net income or cash flows for the three months ended January 29, 2005.

In addition, we are revising Item 4, Controls and Procedures, to disclose that we believe that our controls and procedures were not effective as of the end of the period covered by this report resulting in the restatements to our financial statements as set forth above.

Unaffected items have not been repeated in this Amendment No. 1. This Amendment No. 1 should be read in conjunction with the Company's filings made with the Securities and Exchange Commission subsequent to the original filing date of the Form 10-Q.

BROCADE COMMUNICATIONS SYSTEMS, INC.

FORM 10-Q/A

QUARTER ENDED JANUARY 29, 2005

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PART I — FINANCIAL INFORMATION

Item 1. Financial Statements

BROCADE COMMUNICATIONS SYSTEMS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share amounts)
(Unaudited)

	Three Months Ended	
	January 29, 2005	January 24, 2004 Restated (1)
Net revenues	$ 161,578	$ 145,040
Cost of revenues	64,406	67,636
Gross margin	97,172	77,404
Operating expenses:		
Research and development	31,674	37,020
Sales and marketing	24,825	27,062
General and administrative	6,663	6,069
Internal review costs	3,741	—
Amortization of deferred stock compensation	107	184
Restructuring costs	—	(368)
Lease termination charge and other, net	—	75,591
Total operating expenses	67,010	145,558
Income (loss) from operations	30,162	(68,154)
Interest and other income, net	5,190	4,525
Interest expense	(2,237)	(2,670)
Gain on repurchases of convertible subordinated debt	150	521
Income (loss) before provision for income taxes	33,265	(65,778)
Income tax provision	5,322	3,707
Net income (loss)	$ 27,943	$ (69,485)
Net income (loss) per share — Basic	$ 0.10	$ (0.27)
Net income (loss) per share — Diluted	$ 0.10	$ (0.27)
Shares used in per share calculation — Basic	266,218	257,796
Shares used in per share calculation — Diluted	271,422	257,796

(1) See Note 3, “Restatement of Consolidated Financial Statements,” of the Notes to Condensed Consolidated Financial Statements.

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

BROCADE COMMUNICATIONS SYSTEMS, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except par value)
(Unaudited)

	January 29, 2005 Restated (1)	October 30, 2004 Restated (1)
Assets		
Current assets:		
Cash and cash equivalents	$ 242,310	$ 79,375
Short-term investments	248,614	406,933
Total cash, cash equivalents and short-term investments	490,924	486,308
Accounts receivable, net of allowances of $4,446 and $3,861 at January 29, 2005 and October 30, 2004, respectively	103,847	95,778
Inventories	6,933	5,597
Prepaid expenses and other current assets	16,291	19,131
Total current assets	617,995	606,814
Long-term investments	287,077	250,600
Property and equipment, net	118,976	124,701
Convertible subordinated debt issuance costs	2,954	3,389
Other assets	3,884	1,878
Total assets	$ 1,030,886	$ 987,382
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$ 39,755	$ 38,791
Accrued employee compensation	26,457	33,330
Deferred revenue	40,623	34,886
Current liabilities associated with lease losses	5,319	5,677
Other accrued liabilities	63,008	59,968
Total current liabilities	175,162	172,652
Non-current liabilities associated with lease losses	15,722	16,799
Convertible subordinated debt	348,109	352,279
Commitments and contingencies (Note 9)		
Stockholders' equity:		
Preferred stock, $0.001 par value 5,000 shares authorized, no shares outstanding	—	—
Common stock, $0.001 par value, 800,000 shares authorized:		
Issued and outstanding: 268,220 and 264,242 shares at January 29, 2005 and October 30, 2004, respectively	268	264
Additional paid-in capital	852,325	832,655
Deferred stock compensation	(4,431)	(5,174)
Accumulated other comprehensive income	(1,259)	860
Accumulated deficit	(355,010)	(382,953)
Total stockholders' equity	491,893	445,652
Total liabilities and stockholders' equity	$ 1,030,886	$ 987,382

(1) See Note 3, "Restatement of Consolidated Financial Statements," of the Notes to Condensed Consolidated Financial Statements.

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

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BROCADE COMMUNICATIONS SYSTEMS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Three Months Ended	
	January 29, 2005	January 24, 2004 Restated (1)
Cash flows from operating activities:		
Net income (loss)	$ 27,943	$ (69,485)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	12,904	12,689
Loss on disposal of property and equipment	161	471
Amortization of debt issuance costs	398	495
Net gains on investments and marketable equity securities	—	(202)
Gain on repurchases of convertible subordinated debt	(150)	(521)
Non-cash compensation expense (benefit)	(935)	2,201
Provision for doubtful accounts receivable and sales returns	1,243	797
Non-cash restructuring charges	—	(3,243)
Changes in operating assets and liabilities:		
Accounts receivable	(9,312)	(3,823)
Inventories	(1,336)	(73)
Prepaid expenses and other assets	2,766	926
Accounts payable	964	2,172
Accrued employee compensation	(6,873)	(4,090)
Deferred revenue	5,737	2,170
Other accrued liabilities	3,061	5,391
Liabilities associated with lease losses	(1,402)	(1,475)
Net cash provided by (used in) operating activities	35,169	(55,600)
Cash flows from investing activities:		
Purchases of property and equipment	(5,827)	(36,171)
Purchases of short-term investments	(16,283)	(11,045)
Proceeds from maturities of short-term investments	195,452	49,227
Purchases of long-term investments	(70,125)	(91,551)
Purchases of non-marketable equity investments	(500)	—
Proceeds from maturities of long-term investments	7,500	32,078
Net cash provided by (used in) investing activities	110,217	(57,462)
Cash flows from financing activities:		
Purchases of convertible subordinated debt	(3,983)	(8,580)
Settlement of repurchase obligation	—	(9,029)
Proceeds from issuance of common stock, net	21,352	6,510
Net cash provided by (used in) financing activities	17,369	(11,099)
Effect of exchange rate fluctuations on cash and cash equivalents	180	143
Net increase (decrease) in cash and cash equivalents	162,935	(124,018)
Cash and cash equivalents, beginning of period	79,375	360,012
Cash and cash equivalents, end of period	$ 242,310	$ 235,994

(1) See Note 3, "Restatement of Consolidated Financial Statements," of the Notes to Condensed Consolidated Financial Statements.

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

BROCADE COMMUNICATIONS SYSTEMS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. Organization and Operations of Brocade

Brocade Communications Systems, Inc. (Brocade or the Company) designs, develops, markets, sells, and supports data storage networking products and services, offering a line of storage networking products that enables companies to implement highly available, scalable, manageable, and secure environments for data storage applications. The Brocade SilkWorm® family of storage area networking (SAN) products is designed to help companies reduce the cost and complexity of managing business information within a data storage environment. Brocade products and services are marketed, sold, and supported worldwide to end-user customers through distribution partners, including original equipment manufacturers (OEMs), value-added distributors, systems integrators, and value-added resellers.

Brocade was incorporated on May 14, 1999 as a Delaware corporation, succeeding operations that began on August 24, 1995. The Company's headquarters are located in San Jose, California.

Brocade, SilkWorm, and the Brocade logo are trademarks or registered trademarks of Brocade Communications Systems, Inc. in the United States and/or in other countries. All other brands, products, or service names are or may be trademarks or service marks of, and are used to identify, products or services of their respective owners.

2. Summary of Significant Accounting Policies

Fiscal Year

The Company's fiscal year is the 52 or 53 weeks ending on the last Saturday in October. As is customary for companies that use 52/53-week convention, every fifth year contains a 53-week year. Fiscal year 2005 is a 52-week fiscal year and fiscal year 2004 was a 53-week fiscal year. The second quarter of fiscal year 2004 consisted of 14 weeks, which is one week more than a typical quarter.

Basis of Presentation

The accompanying financial data as of January 29, 2005, and for the three months ended January 29, 2005 and January 24, 2004, has been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations. The October 30, 2004 Condensed Consolidated Balance Sheet was derived from audited consolidated financial statements, but does not include all disclosures required by generally accepted accounting principles in the United States of America. However, the Company believes that the disclosures are adequate to make the information presented not misleading. These Condensed Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended October 30, 2004.

In the opinion of management, all adjustments (which include only normal recurring adjustments, except as otherwise indicated) necessary to present a fair statement of financial position as of January 29, 2005, results of operations for the three months ended January 29, 2005 and January 24, 2004, and cash flows for the three months ended January 29, 2005 and January 24, 2004, have been made. The results of operations for the three months ended January 29, 2005 are not necessarily indicative of the operating results for the full fiscal year or any future periods.

Cash and Cash Equivalents

The Company considers all highly liquid investments with an original or remaining maturity of three months or less at the date of purchase to be cash equivalents.

Investments and Equity Securities

Investment securities with original or remaining maturities of more than three months but less than one year are considered short-term investments. Investment securities with original or remaining maturities of one year or more are considered long-term investments. Short-term and long-term investments consist of auction rate securities, debt securities issued by United States government agencies, municipal government obligations, and corporate bonds and notes. In the first quarter of fiscal year 2005, the Company concluded that it was appropriate to classify its auction rate securities as short-term investments. These investments were previously classified as cash and cash equivalents. Accordingly, we have revised our October 30, 2004 balance sheet to report these securities as short-term investments on the accompanying Condensed Consolidated Balance Sheets.

Short-term and long-term investments are maintained at three major financial institutions, are classified as available-for-sale, and are recorded on the accompanying Condensed Consolidated Balance Sheets at fair value. Fair value is determined using quoted market prices for those securities. Unrealized holding gains and losses are included as a separate component of accumulated other comprehensive income on the accompanying Condensed Consolidated Balance Sheets, net of any related tax effect. Realized gains and losses are calculated based on the specific identification method and are included in interest and other income, net, on the Condensed Consolidated Statements of Operations.

Marketable equity securities consist of equity holdings in public companies and are classified as available-for-sale when there are no restrictions on the Company's ability to immediately liquidate such securities. Marketable equity securities are recorded on the accompanying Condensed Consolidated Balance Sheets at fair value. Fair value is determined using quoted market prices for those securities. Unrealized holding gains and losses are included as a separate component of accumulated other comprehensive income on the accompanying Condensed Consolidated Balance Sheets, net of any related tax effect. Realized gains and losses are calculated based on the specific identification method and are included in interest and other income, net on the Condensed Consolidated Statements of Operations.

The Company recognizes an impairment charge when the declines in the fair values of its investments below the cost basis are judged to be other-than-temporary. The Company considers various factors in determining whether to recognize an impairment charge, including the length of time and extent to which the fair value has been less than the Company's cost basis, the financial condition and near-term prospects of the investee, and the Company's intent and ability to hold the investment for a period of time sufficient to allow for any anticipated recovery in market value.

From time to time the Company makes equity investments in non-publicly traded companies. These investments are included in other assets on the accompanying Condensed Consolidated Balance Sheets, and are generally accounted for under the cost method as the Company does not have the ability to exercise significant influence over the respective company's operating and financial policies. The Company monitors its investments for impairment on a quarterly basis and makes appropriate reductions in carrying values when such impairments are determined to be other-than-temporary. Impairment charges are included in interest and other income, net on the Condensed Consolidated Statements of Operations. Factors used in determining an impairment include, but are not limited to, the current business environment including competition and uncertainty of financial condition; going concern considerations such as the rate at which the investee company utilizes cash, and the investee company's ability to obtain additional private financing to fulfill its stated business plan; the need for changes to the investee company's existing business model due to changing business environments and its ability to successfully implement necessary changes; and comparable valuations. If an investment is determined to be impaired, a determination is made as to whether such impairment is other-than-temporary. As of January 29, 2005 and October 30, 2004, the carrying values of the Company's equity investments in non-publicly traded companies were \$1.0 million and \$0.5 million, respectively.

Concentrations

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of cash, cash equivalents, short-term and long-term investments, and accounts receivable. Cash, cash equivalents, and short-term and long-term investments are primarily maintained at five major financial institutions in the United States. Deposits held with banks may be redeemed upon demand and may exceed the amount of insurance provided on such deposits. The Company principally invests in United States government agency debt securities, municipal government obligations, and corporate bonds and notes, and limits the amount of credit exposure to any one entity.

A majority of the Company's trade receivable balance is derived from sales to OEM partners in the computer storage and server industry. As of January 29, 2005 and October 30, 2004, 95 percent and 85 percent, respectively, of accounts receivable were concentrated with five customers. The Company performs ongoing credit evaluations of its customers and generally does not require collateral on accounts receivable balances. The Company has established reserves for credit losses and sales returns, and other allowances. The Company has not experienced material credit losses in any of the periods presented.

For the three months ended January 29, 2005 and January 24, 2004, four customers and three customers, respectively, each represented ten percent or more of the Company's total revenues for combined totals of 82 percent and 69 percent of total revenues, respectively. The level of sales to any one of these customers may vary, and the loss of, or a decrease in the level of sales to, any one of these customers, could seriously harm the Company's financial condition and results of operations.

The Company currently relies on single and limited supply sources for several key components used in the manufacture of its products. Additionally, the Company relies on two contract manufacturers for the production of its products. The inability of any single and limited source suppliers or the inability of either contract manufacturer to fulfill supply and production requirements, respectively, could have a material adverse effect on the Company's future operating results.

The Company's business is concentrated in the SAN industry, which from time to time has been impacted by unfavorable economic conditions and reduced information technology (IT) spending rates. Accordingly, the Company's future success depends upon the buying patterns of customers in the SAN industry, their response to current and future IT investment trends, and the continued demand by such customers for the Company's products. The Company's future success, in part, will depend upon its ability to enhance its existing products and to develop and introduce, on a timely basis, new cost-effective products and features that keep pace with technological developments and emerging industry standards.

Revenue Recognition

Product revenue. Product revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable, and collection is probable. However, for newly introduced products, many of the Company's large OEM customers require a product qualification period during which the Company's products are tested and approved by the OEM customer for sale to their customers. Revenue recognition, and related cost, is deferred for shipments to new OEM customers and for shipments of newly introduced products to existing OEM customers until satisfactory evidence of completion of the product qualification has been received from the OEM customer. Revenue from sales to the Company's master reseller customers is recognized in the same period in which the actual sell-through occurs.

The Company reduces revenue for estimated sales returns, sales programs, and other allowances at the time of shipment. Sales returns, sales programs, and other allowances are estimated based upon historical experience, current trends, and the Company's expectations regarding future experience. In addition, the Company maintains allowances for doubtful accounts, which are also accounted for as a reduction in revenue. The allowance for doubtful accounts is estimated based upon analysis of accounts receivable, historical collection patterns, customer concentrations, customer creditworthiness, current economic trends, and changes in customer payment terms and practices.

Service revenue. Service revenue consists of training, warranty, and maintenance arrangements, including post-contract customer support (PCS) services. PCS services are offered under renewable, annual fee-based contracts or as part of multiple element arrangements and typically include upgrades and enhancements to the Company's software operating system, and telephone support. Service revenue, including revenue allocated to PCS elements, is deferred and recognized ratably over the contractual period. Service contracts are typically one to three years in length. Training revenue is recognized upon completion of the training. Service revenue was not material in any of the periods presented.

Multiple-element arrangements. The Company's multiple-element product offerings include computer hardware and software products, and support services. The Company also sells certain software products and support services separately. The Company's software products are essential to the functionality of its hardware products and are, therefore, accounted for in accordance with Statement of Position 97-2, "Software Revenue Recognition" (SOP 97-2), as amended. The Company allocates revenue to each element based upon vendor-specific objective evidence (VSOE) of the fair value of the element or, if VSOE is not available, by application of the residual method. VSOE of the fair value for an element is based upon the price charged when the element is sold separately. Revenue allocated to each element is then recognized when the basic revenue recognition criteria are met for each element.

Warranty Expense. The Company provides warranties on its products ranging from one to three years. Estimated future warranty costs are accrued at the time of shipment and charged to cost of revenues based upon historical experience.

Stock-Based Compensation.

The Company has several stock-based compensation plans that are described in the Company's Annual Report on Form 10-K for the fiscal year ended October 30, 2004. The Company accounts for stock-based awards using the intrinsic value method of accounting in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" (APB 25), whereby the difference between the exercise price and the fair market value on the date of grant is recognized as compensation expense. Under the intrinsic value method of accounting, no compensation expense is recognized in the Company's Condensed Consolidated Statements of Operations when the exercise price of the Company's employee stock option grants equals the market price of the underlying common stock on the date of grant, and the measurement date of the option grant is certain. The measurement date is certain when the date of grant is fixed and determinable. When the measurement date is not certain, the Company records stock compensation expense using variable accounting under APB 25. From May 1999 through July 2003, the Company granted 98.8 million options that were subject to variable accounting under APB 25 because the measurement date of the options grant was not certain. As of January 29, 2005, 3.5 million options with a weighted average exercise price of $13.67 and a weighted average remaining life of 6.8 years remain outstanding and continue to be accounted for under variable accounting. When variable accounting is applied to stock option grants, the Company remeasures the intrinsic value of the options at the end of each reporting period until the options are exercised, cancelled or expire unexercised. Compensation expense in any given period is calculated as the difference between total earned compensation at the end of the period, less total earned compensation at the beginning of the period. Compensation earned is calculated under an accelerated vesting method in accordance with FASB Interpretation 28.

Statement of Financial Accounting Standards No. 123, *"Accounting for Stock-Based Compensation,"* (SFAS 123), established a fair value based method of accounting for stock-based plans. Companies that elect to account for stock-based compensation plans in accordance with APB 25 are required to disclose the pro forma net income (loss) that would have resulted from the use of the fair value based method under SFAS 123.

Statement of Financial Accounting Standards No. 148, *"Accounting for Stock-Based Compensation — Transition and Disclosure an Amendment of FASB Statement No. 123"* (SFAS 148), amended the disclosure requirements of SFAS 123 to require more prominent disclosures in both annual and interim financial statements regarding the method of accounting for stock-based employee compensation and the effect of the method used on reported results. The pro forma information resulting from the use of the fair value based method under SFAS 123 is as follows (in thousands except per share amounts):

	Three Months Ended	
	January 29, 2005	January 24, 2004 (Restated)
Net income (loss) — as reported	$ 27,943	$ (69,485)
Add: Stock-based compensation expense (benefit) included in reported net loss, net of tax	(935)	2,202
Deduct: Stock-based compensation expense determined under the fair value based method, net of tax	(4,636)	(11,314)
Pro forma net income (loss)	$ 22,372	$ (78,597)
Basic net income (loss) per share:		
As reported	$ 0.10	$ (0.27)
Pro forma	$ 0.08	$ (0.30)
Diluted net income (loss) per share:		
As reported	$ 0.10	$ (0.27)
Pro forma	$ 0.08	$ (0.30)

The assumptions used for the three months ended January 29, 2005 and January 24, 2004 are as follows:

	Three Months Ended	
Stock Options	January 29, 2005	January 24, 2004
Expected dividend yield	0.0%	0.0%
Risk-free interest rate	3.0 — 3.7%	1.2 — 3.1%
Expected volatility	47.1%	57.3%
Expected life (in years)	2.9	2.6

	Three Months Ended	
Employee Stock Purchase Plan	January 29, 2005	January 24, 2004
Expected dividend yield	0.0%	0.0%
Risk-free interest rate	2.0 — 2.5%	1.0 — 1.5%
Expected volatility	50.3%	61.7%
Expected life from vest date (in years)	0.5	0.5

Computation of Net Income (Loss) per Share

Basic net income (loss) per share is computed using the weighted-average number of common shares outstanding during the period, less shares subject to repurchase. Diluted net income (loss) per share is computed using the weighted-average number of common shares and dilutive potential common shares outstanding during the period. Dilutive potential common shares result from the assumed exercise of outstanding stock options, by application of the treasury stock method, that have a dilutive effect on earnings per share, and from the assumed conversion of outstanding convertible debt if it has a dilutive effect on earnings per share.

Comprehensive Income (Loss)

The components of comprehensive income (loss), net of tax, are as follows (in thousands):

	Three Months Ended	
	January 29, 2005	**January 24, 2004** (Restated)
Net income (loss)	$ 27,943	$ (69,485)
Other comprehensive income (loss):		
Change in net unrealized gains (losses) on marketable equity securities and short-term investments	(2,299)	(62)
Cumulative translation adjustments	180	143
Total comprehensive income (loss)	$ 25,824	$ (69,404)

Recent Accounting Pronouncements

In December 2004, the FASB issued a revision of Statement of Financial Accounting Standards No. 123, *"Accounting for Stock-Based Compensation"* (SFAS 123R). SFAS 123R supersedes APB Opinion No. 25, *"Accounting for Stock Issued to Employees,"* and its related implementation guidance. SFAS 123R establishes standards for the accounting for transactions in which an entity incurs liabilities in exchange for goods or services that are based on the fair value of the entity's equity instruments or that may be settled by the issuance of those equity instruments. SFAS 123R does not change the accounting guidance for share-based payment transactions with parties other than employees provided in SFAS 123 as originally issued and EITF Issue No. 96-18, *"Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services."* SFAS 123R is effective for interim reporting period that begins after June 15, 2005. The Company is in the process of determining the effect of the adoption of SFAS 123R will have on its financial position, results of operations, or cash flows.

Reclassifications

Certain reclassifications have been made to prior year balances in order to conform to the current year presentation.

3. Restatement of Consolidated Financial Statements

November 2005 Restatement

In May 2005, Brocade determined that the Company's financial statements for the fiscal years ended October 30, 2004, October 25, 2003, and October 26, 2002, and the interim periods contained therein, should no longer be relied upon because of errors in such financial statements. Brocade has restated those financial statements, which appear in Brocade's Annual Report on Form 10-K/A for the year ended October 30, 2004. In addition, the Company made adjustments to its financial information for fiscal years ended October 27, 2001, October 28, 2000, and October 31, 1999.

More specifically, following the completion of an Audit Committee review announced on January 24, 2005 and the related restatement (as described below in "January 2005 Restatement"), additional information came to Brocade's attention that indicated that it could not rely on the documentation used to support the recorded measurement dates for stock options granted in the period from August 2003 through November 2004. As a result, Brocade recorded a cumulative increase in non-cash stock option compensation expense of approximately $0.9 million over fiscal years 2003 and 2004.

In addition, Brocade determined that from 1999 through 2004 it had not appropriately accounted for the cost of stock-based compensation for certain employees on leaves of absences ("LOA") and in transition or advisory roles prior to ceasing employment with Brocade. This resulted in an increase in non-cash compensation expense of approximately $0.9 million, $0.2 million and $20.0 million in fiscal years 2004, 2003 and 2002, respectively, and an aggregate of approximately $49.9 million in fiscal years 1999 through 2001. Brocade also determined that it could not rely on the documentation used to support the recorded dates for certain stock option exercises that resulted in immaterial adjustments included in the restatement, consisting of approximately $0.1 million in fiscal year 2002 and an aggregate of approximately $0.3 million in fiscal years 1999 through 2001.

Impact of the Financial Statement Adjustments on the Condensed Consolidated Balance Sheets

The following table presents the impact of the financial statement adjustments related to the November 2005 Restatement on the Company's previously reported Condensed Consolidated Balance Sheets as of January 29, 2005 and October 29, 2004.

	January 29, 2005		
	As Previously Reported (1)	Adjustments (3)	As Restated
ASSETS			
Total assets	$ 1,030,886	$ —	$ 1,030,886
LIABILITIES AND STOCKHOLDERS' EQUITY			
Total liabilities	$ 538,993	$ —	$ 538,993
Stockholders' equity:			
Preferred stock	—	—	—
Common stock:	268	—	268
Additional paid-in capital	776,747	75,578	852,325
Deferred stock compensation	(1,194)	(3,237)	(4,431)
Accumulated other comprehensive income	(1,259)	—	(1,259)
Accumulated earnings (deficit)	(282,669)	(72,341)	(355,010)
Total stockholders' equity	491,893	—	491,893
Total liabilities and stockholders' equity	$ 1,030,886	$ —	$ 1,030,886

	October 30, 2004		
	As Previously Reported (2)	Adjustments (3)	As Restated
ASSETS			
Total assets	$ 987,382	$ —	$ 987,382
LIABILITIES AND STOCKHOLDERS' EQUITY			
Total liabilities	$ 541,730	$ —	$ 541,730
Stockholders' equity:			
Preferred stock	—	—	—
Common stock:	264	—	264
Additional paid-in capital	757,077	75,578	832,655
Deferred stock compensation	(1,937)	(3,237)	(5,174)
Accumulated other comprehensive income	860	—	860
Accumulated earnings (deficit)	(310,612)	(72,341)	(382,953)
Total stockholders' equity	445,652	—	445,652
Total liabilities and stockholders' equity	$ 987,382	$ —	$ 987,382

(1) These amounts were reported in the Company's Form 10-Q filed with the SEC on March 9, 2005.

(2) These amounts were reported in the Company's Form 10-K filed with the SEC on January 31, 2005. Amounts reflect the Company's January 2005 Restatement described below.

(3) Adjustments reflect additional stock-based compensation expense for certain employees on LOA and in transition or advisory roles prior to ceasing employment with the Company and additional stock-based compensation expense associated with change in measurement dates for certain stock options.

January 2005 Restatement

On January 24, 2005, the Company announced that its Audit Committee completed an internal review regarding the Company's stock option granting process. As a result of certain findings of the review, the Company restated certain of its historical financial statements.

Specifically, the Company determined that the restatement was required because it incorrectly accounted for: (A) stock option grants that were made to new hires on their offer acceptance date, rather than the date of their commencement of employment, during the period May 1999 to July 2000; (B) stock option grants that were made to persons engaged on a part-time basis prior to their new hire full-time employment during the period August 2000 to October 2002; and (C) stock option grants where there was insufficient basis to rely on the Company's process and related documentation to support recorded measurement dates used to account for certain stock options granted prior to August 2003. Therefore, the Company recorded additional stock-based compensation charges relating to many of its stock option grants made during the period 1999 through the third quarter of fiscal year 2003. In addition, the Company recorded a valuation allowance associated with deferred tax assets related to previously recorded stock option tax benefits. The Company also concluded that there were improprieties in connection with the documentation of stock option grants and related employment records of a small number of employees prior to mid-2002, which resulted in immaterial adjustments included in the January 2005 restatement.

These charges affected the previously filed financial statements for fiscal years ended October 25, 2003, and October 26, 2002, including the corresponding interim periods for fiscal year 2003, and the interim periods ended January 24, 2004, May 1, 2004 and July 31, 2004. The Company also recorded stock-based compensation and associated income tax adjustments to previously announced financial results for the fourth quarter and year ended October 30, 2004. These adjustments related solely to matters pertaining to stock options granted prior to August 2003.

As a result of the stock compensation adjustments, the Company's deferred tax assets previously recognized have now been fully reserved. The Company expects to realize a tax benefit in future reporting periods when it is able to utilize net operating loss carryforwards to offset future taxable income.

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4. Restructuring Costs

Fiscal 2004 Second Quarter Restructuring

During the three months ended May 1, 2004, the Company implemented a restructuring plan designed to optimize the Company's business model to drive improved profitability through reduction of headcount as well as certain structural changes in the business. The plan announced on May 19, 2004 encompassed organizational changes, which included a reduction in force of 110 people, or nine percent of the Company's then workforce. As a result, the Company recorded $10.5 million in restructuring costs consisting of severance and benefit charges, equipment impairment charges, and contract termination and other charges. Severance and benefits charges of $7.5 million consisted of severance and related employee termination costs, including outplacement services, associated with the reduction of the Company's workforce. Equipment impairment charges of $1.2 million primarily consisted of excess equipment that is no longer being used as a result of the restructuring program. Contract termination and other charges of $1.7 million were primarily related to the cancellation of certain contracts in connection with the restructuring of certain business functions.

Remaining accrued liabilities related to the Company's fiscal 2004 second quarter restructuring program are included in other accrued liabilities on the accompanying Condensed Consolidated Balance Sheets. During the three months ended October 30, 2004, the Company recorded a reduction of $1.0 million to restructuring costs, primarily because actual payments were lower than the estimated amount. No other material changes in estimates were made to the fiscal 2004 second quarter restructuring accrual. The Company expects to pay or otherwise substantially settle the remaining accrued liabilities during the fiscal year 2005.

The following table summarizes the total restructuring costs incurred and charged to restructuring expense during the second quarter of fiscal year 2004, costs paid or otherwise settled, and the remaining unpaid or otherwise unsettled accrued liabilities (in thousands) as of January 29, 2005:

	Severance and Benefits	Contract Terminations and Other	Equipment Impairment	Total
Restructuring costs incurred	$ 7,480	$ 1,740	$ 1,241	$ 10,461
Cash payments	(5,661)	(1,692)	—	(7,353)
Non-cash charges	—	—	(1,241)	(1,241)
Adjustments	(981)	(48)	—	(1,029)
Remaining accrued liabilities at October 30, 2004	838	—	—	838
Cash payments	(496)	—	—	(496)
Remaining accrued liabilities at January 29, 2005	$ 342	$ —	$ —	$ 342

5. Balance Sheet Details

The following tables provide details of selected balance sheet items (in thousands):

	January 29, 2005	October 30, 2004
Inventories:		
Raw materials	$ 2,177	$ 1,950
Finished goods	4,756	3,647
Total	$ 6,933	$ 5,597
Property and equipment, net:		
Computer equipment and software	$ 64,462	$ 63,524
Engineering and other equipment	112,054	111,109
Furniture and fixtures	4,394	4,429
Leasehold improvements	39,723	39,520
Land and building	30,000	30,000
	250,633	248,582
Less: Accumulated depreciation and amortization	(131,657)	(123,881)
Total	$ 118,976	$ 124,701
Other accrued liabilities:		
Income taxes payable	$ 31,578	$ 27,769
Accrued warranty	1,971	4,669
Inventory purchase commitments	7,188	4,326
Accrued sales programs	9,461	8,231
Accrued restructuring	342	866
Other	12,468	14,107
Total	$ 63,008	$ 59,968

Leasehold improvements as of January 29, 2005 and October 30, 2004, are shown net of estimated asset impairments related to facilities lease losses (see Note 7).

6. Investments and Equity Securities

The following tables summarize the Company's investments and equity securities (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
January 29, 2005				
U.S. government agencies and municipal obligations	$314,352	$ 16	$ (1,335)	$313,033
Corporate bonds and notes	225,139	16	(2,497)	222,658
Equity securities	694	118	—	812
Total	$540,185	$ 150	$ (3,832)	$536,503
Reported as:				
Short-term investments				$248,614
Other current assets				812
Long-term investments				287,077
Total				$536,503
October 30, 2004				
U.S. government agencies and municipal obligations	$526,953	$ 1,307	$ (972)	$527,288
Corporate bonds and notes	130,604	146	(505)	130,245
Equity securities	694	164	—	858
Total	$658,251	$ 1,617	$ (1,477)	$658,391
Reported as:				
Short-term investments				$406,933
Other current assets				858
Long-term investments				250,600
Total				$658,391

For the three months ended January 29, 2005 and January 24, 2004, total gains realized on the sale of investments or marketable equity securities were zero and $0.2 million, respectively. As of January 29, 2005 and October 30, 2004, net unrealized holding gains (losses) of $(3.7) million and $0.1 million, respectively, were included in accumulated other comprehensive income in the accompanying Condensed Consolidated Balance Sheets.

The following table summarizes the maturities of the Company's investments in debt securities issued by United States government agencies, municipal government obligations, and corporate bonds and notes as of January 29, 2005 (in thousands):

	Amortized Cost	Fair Value
Less than one year	$249,024	$248,614
Due in 1 — 2 years	170,130	168,374
Due in 2 — 3 years	120,337	118,703
Total	$539,491	$535,691

7. Liabilities Associated with Facilities Lease Losses

Lease Termination Charge and Other, Net

On November 18, 2003, the Company purchased a building located near its San Jose headquarters. This 194,000 square foot facility was previously leased, and certain unused portions of the facility were previously reserved and included in the facilities lease losses liability noted below. The total consideration for the building purchase was $106.8 million plus transaction costs, consisting of the purchase of land and building valued at $30.0 million and a lease termination fee of $76.8 million. The fair value of the land and building as of the purchase date was determined based on the estimated fair value of the land and building. As a result of the building purchase, during the first quarter of fiscal 2004, the Company recorded adjustments of $23.7 million to the previously recorded facilities lease loss reserve, deferred rent, and leasehold improvement impairments related to the purchased facility.

During the first quarter of fiscal 2004, the Company consolidated the engineering organization and development, test and interoperability laboratories into the purchased facilities and vacated other existing leased facilities. As a result, the Company recorded a charge of $20.9 million related to estimated facilities lease losses, net of expected sublease income, on the vacated facilities. These charges represented the fair value of the lease liability based on assumptions regarding the vacancy period, sublease terms, and the probability of subleasing this space. The assumptions that the Company used were based on market data, including the then current vacancy rates and lease activities for similar facilities within the area. Should there be changes in real estate market conditions or should it take longer than expected to find a suitable tenant to sublease the remaining vacant facilities, adjustments to the facilities lease losses reserve may be necessary in future periods based upon then current actual events and circumstances.

The following table summarizes the activity related to the lease termination charge and other, net incurred in the first three months ended January 24, 2004 (in thousands):

Lease termination charge	$ 76,800
Closing costs and other related charges	1,234
Reversal of previously recorded lease loss reserve	(16,933)
Reversal of previously recorded leasehold impairment reserve	(2,954)
Reversal of previously recorded deferred rent liability	(3,844)
Additional reserve booked as a result of facilities consolidation	20,855
Asset impairments associated with facilities consolidation	433
Total lease termination charge and other, net	$ 75,591

Facilities Lease Losses Liability

During the three months ended October 27, 2001, the Company recorded a charge of $39.8 million related to estimated facilities lease losses, net of expected sublease income, and a charge of $5.7 million in connection with the estimated impairment of certain related leasehold improvements. These charges represented the low-end of the then estimated range of $39.8 million to $63.0 million and may be adjusted upon the occurrence of future triggering events.

During the three months ended July 27, 2002, the Company completed a transaction to sublease a portion of these vacant facilities. Accordingly, based on then current market data, the Company revised certain estimates and assumptions, including those related to estimated sublease rates, estimated time to sublease the facilities, expected future operating costs, and expected future use of the facilities. The Company reevaluates its estimates and assumptions on a quarterly basis and makes adjustments to the reserve balance if necessary.

As previously described, in November 2003 the Company purchased a previously leased building. In addition, the Company consolidated the engineering organization and development, test and interoperability laboratories into the purchased facilities and vacated other existing leased facilities. As a result, the Company recorded adjustments to the previously recorded facilities lease loss reserve, deferred rent and leasehold improvement impairments, and recorded additional reserves in connection with the facilities consolidation.

The following table summarizes the activity related to the facilities lease losses reserve, net of expected sublease income (in thousands), as of January 29, 2005:

	Lease Loss Reserve
Reserve balances at October 30, 2004	$ 22,476
Cash payments on facilities leases	(1,402)
Non-cash charges	(33)
Reserve balances at January 29, 2005	$ 21,041

Cash payments for facilities leases related to the above noted facilities lease losses will be paid over the respective lease terms through fiscal year 2010.

8. Convertible Subordinated Debt

On December 21, 2001, and January 10, 2002, the Company sold, in private placements pursuant to Section 4(2) of the Securities Act of 1933, as amended, an aggregate of $550 million in principal amount, two percent convertible subordinated notes due January 2007 (the notes or convertible subordinated debt). The initial purchasers purchased the notes from the Company at a discount of 2.25 percent of the aggregate principal amount. Holders of the notes may, in whole or in part, convert the notes into shares of the Company’s common stock at a conversion rate of 22.8571 shares per $1,000 principal amount of notes (approximately 8.0 million shares may be issued upon conversion based on outstanding debt of $348.1 million as of January 29, 2005) at any time prior to maturity on January 1, 2007. At any time on or after January 5, 2005, the Company may redeem the notes in whole or in part at the following prices expressed as a percentage of the principal amount:

Redemption Period	Price
Beginning on January 5, 2005 and ending on December 31, 2005	100.80%
Beginning on January 1, 2006 and ending on December 31, 2006	100.40%
On January 1, 2007 and thereafter	100.00%

The Company is required to pay interest on January 1 and July 1 of each year, beginning July 1, 2002. Debt issuance costs of $12.4 million are being amortized over the term of the notes. The amortization of debt issuance costs will accelerate upon early redemption or conversion of the notes. The net proceeds remain available for general corporate purposes, including working capital and capital expenditures. As of January 29, 2005, the remaining balance of unamortized debt issuance costs was $3.0 million.

During the first quarter of fiscal years 2005 and 2004, the Company repurchased $4.2 million and $9.2 million in face value of its convertible subordinated debt, respectively, on the open market. For the three months ended January 29, 2005, the Company paid an average of $0.955 on each dollar of face value for an aggregate purchase price of $4.0 million, which resulted in a pre-tax gain of $0.15 million. For the three months ended January 24, 2004, the Company paid an average of $0.93 on each dollar of face value for an aggregate purchase price of $8.6 million, which resulted in a pre-tax gain of $0.5 million. To date, the Company has repurchased a total of $201.9 million in face value of its convertible subordinated notes. As of January 29, 2005, the remaining balance outstanding of the convertible subordinated debt was $348.1 million.

The notes are not listed on any securities exchange or included in any automated quotation system; however, the notes are eligible for trading on the Portal[SM] Market. On January 28, 2005, the average bid and ask price on the Portal Market of the notes was 95.25, resulting in an aggregate fair value of approximately $331.6 million.

9. Commitments and Contingencies

Leases

The Company leases its facilities and certain equipment under various operating lease agreements expiring through August 2010. In connection with its facilities lease agreements, the Company has signed unconditional, irrevocable letters of credit totaling $8.3 million as security for the leases. Future minimum lease payments under all non-cancelable operating leases as of January 29, 2005 were $78.3 million. In addition to base rent, many of the facilities lease agreements require that the Company pay a proportional share of the respective facilities' operating expenses.

As of January 29, 2005, the Company had recorded $21.0 million in facilities lease loss reserves related to future lease commitments, net of expected sublease income (see Note 7).

Product Warranties

The Company provides warranties on its products ranging from one to three years. Estimated future warranty costs are accrued at the time of shipment and charged to cost of revenues based upon historical experience. The Company's accrued liability for estimated future warranty costs is included in other accrued liabilities on the accompanying Condensed Consolidated Balance Sheets. For the three months ended January 29, 2005, the Company recorded a warranty benefit of approximately $1.9 million as a result of a change in warranty terms with a customer. The following table summarizes the activity related to the Company's accrued liability for estimated future warranty costs during the three months ended January 29, 2005 (in thousands):

	Accrued Warranty
Balance at October 30, 2004	$ 4,669
Liabilities accrued for warranties issued during the period	281
Warranty claims paid during the period	(104)
Changes in liability for pre-existing warranties during the period	(2,875)
Balance at January 29, 2005	$ 1,971

In addition, the Company has standard indemnification clauses contained within its various customer contracts. As such, the Company indemnifies the parties to whom it sells its products with respect to the Company's product infringing upon any patents, trademarks, copyrights, or trade secrets, as well as against bodily injury or damage to real or tangible personal property caused by a defective Company product. As of January 29, 2005, there have been no known events or circumstances that have resulted in an indemnification related liability to the Company.

Manufacturing and Purchase Commitments

The Company has manufacturing agreements with Solectron Corporation (Solectron) and Hon Hai Precision Industry Co. (Foxconn) under which the Company provides twelve-month product forecasts and places purchase orders in advance of the scheduled delivery of products to the Company's customers. The required lead-time for placing orders with both Solectron and Foxconn depends on the specific product. As of January 29, 2005, the Company's aggregate commitment to Solectron and Foxconn for inventory components used in the manufacture of Brocade products was $56.7 million, net of purchase commitment reserves of $7.2 million, which the Company expects to utilize during future normal ongoing operations. The Company's purchase orders placed with Solectron and Foxconn are cancelable, however if cancelled, the agreements with Solectron and Foxconn require the Company to purchase from Solectron and Foxconn all inventory components not returnable, usable by, or sold to, other customers of Solectron or Foxconn. Our purchase commitments reserve reflects our estimate of purchase commitments we do not expect to consume in normal operations.

Legal Proceedings

From time to time, claims are made against the Company in the ordinary course of its business, which could result in litigation. Claims and associated litigation are subject to inherent uncertainties and unfavorable outcomes could occur, such as monetary damages, fines, penalties or injunctions prohibiting the Company from selling one or more products or engaging in other activities. The occurrence of an unfavorable outcome in any specific period could have a material adverse affect on the Company's results of operations for that period or future periods.

On July 20, 2001, the first of a number of putative class actions for violations of the federal securities laws was filed in the United States District Court for the Southern District of New York against the Company, certain of its officers and directors, and certain of the underwriters for the Company's initial public offering of securities. A consolidated amended class action captioned In Re Brocade Communications Systems, Inc. Initial Public Offering Securities Litigation was filed on April 19, 2002. The complaint generally alleges that various underwriters engaged in improper and undisclosed activities related to the allocation of shares in the Company's initial public offering and seeks unspecified damages on behalf of a purported class of purchasers of common stock from May 24, 1999 to December 6, 2000. The lawsuit against the Company is being coordinated for pretrial proceedings with a number of other pending litigations challenging underwriter practices in over 300 cases as In Re Initial Public Offering Securities Litigation, 21 MC 92(SAS). In October 2002, the individual defendants were dismissed without prejudice from the action, pursuant to a tolling agreement. On February 19, 2003, the Court issued an Opinion and Order dismissing all of the plaintiffs' claims against the Company. In July 2004, a stipulation of settlement for the claims against the issuer defendants, including the Company, was submitted to the Court for approval. The settlement is subject to a number of conditions, including approval by the Court.

10. Segment Information

The Company is organized and operates as one operating segment: the design, development, marketing and selling of infrastructure for SANs. The CEO is the Company's Chief Operating Decision Maker (CODM), as defined by SFAS 131, "Disclosures about Segments of an Enterprise and Related Information." The CODM allocates resources and assesses the performance of the Company based on revenues and overall profitability.

Revenues are attributed to geographic areas based on the location of the customer to which products are shipped. Domestic revenues include sales to certain OEM customers who take possession of Brocade products domestically and then distribute these products to their international customers. Domestic and international revenues were approximately 66 percent and 34 percent of total revenues, respectively, for the three months ended January 29, 2005. Domestic and international revenues were approximately 63 percent and 37 percent of total revenues, respectively, for the three months ended January 24, 2004. To date, service revenue has not exceeded 10 percent of total revenues. Identifiable assets located in foreign countries were not material as of January 29, 2005 and October 30, 2004. For the three months ended January 29, 2005, four customers accounted for 82 percent of total revenues. For the three months ended January 24, 2004, three customers accounted for 69 percent of total revenues.

11. Net Income (Loss) per Share

The following table presents the calculation of basic and diluted net income (loss) per common share (in thousands, except per share amounts):

	Three Months Ended	
	January 29, 2005	January 24, 2004 (Restated)
Net income (loss)	$ 27,943	$ (69,485)
Basic and diluted net income (loss) per share:		
Weighted-average shares of common stock outstanding	266,391	258,281
Less: Weighted-average shares of common stock subject to repurchase	(173)	(485)
Weighted-average shares used in computing basic net income (loss) per share	266,218	257,796
Dilutive effect of common share equivalents	5,204	—
Weighted-average shares used in computing diluted net loss per share	271,422	257,796
Basic net income (loss) per share	$ 0.10	$ (0.27)
Diluted net income (loss) per share	$ 0.10	$ (0.27)

For the three months ended January 29, 2005, potential common shares in the form of stock options to purchase 3.0 million weighted-average shares of common stock were antidilutive and, therefore, not included in the computation of diluted earnings per share. For the three months ended January 24, 2004, stock options outstanding of 47.5 million shares were antidilutive as the Company had net loss for the period, and therefore, not included in the computation of diluted earnings per share. In addition, for the three months ended January 29, 2005 and January 24, 2004, potential common shares resulting from the potential conversion, on a weighted average basis, of the Company's convertible subordinated debt of 8.0 million and 9.9 million common shares, respectively, were antidilutive and therefore not included in the computation of diluted earnings per share.

12. Subsequent Events

At the meeting of the Board of Directors (the "Board") on January 18, 2005, the Board appointed Dave House as the Executive Chairman of the Board and L. William Krause as the Lead Director. No compensation arrangements were made. Effective on January 18, 2005, Greg Reyes ceased being the Company's Chief Executive Officer and Chairman. On February 18, 2005, Mr. Reyes announced that he would not stand for re-election at the Company's annual meeting on April 22, 2005. Mr. Reyes resigned from the Company's Board of Directors effective on April 21, 2005. At a meeting of the Board on January 21, 2005, the Board elected Michael Klayko as the Chief Executive Officer of the Company and appointed him as a member of the Board.

On May 3, 2005, the Company completed its acquisition of Therion Software Corporation ("Therion"), a privately held developer of software management solutions for the automated provisioning of servers over a storage network based in Redmond, Washington. As of the acquisition date the Company owned approximately 13% of Therion's equity interest through investments totaling $1.0 million. Therion was a development stage company with no recognized revenue and a core technology that had not yet reached technological feasibility. Accordingly, the acquisition of Therion was accounted for as an asset purchase.

The total purchase price was $12.1 million, consisting of $9.3 million cash consideration for Therion's preferred and common stock holders, assumed stock options valued at $1.7 million, the Company's initial investment of $1.0 million, and direct acquisition cost of $0.1 million. Of the $9.3 million cash consideration, the Company paid $7.3 million upon closing the transaction and recorded the remaining liability of $2.0 million to be paid over the next eighteen months. The fair value of the assumed stock options was determined using the Black-Scholes option-pricing model. In connection with this acquisition, in the three months ended July 30, 2005 the Company recorded a $7.8 million in-process research and development charge, and allocated the remaining purchase price to net assets of $2.9 million, deferred stock compensation of $1.5 million, and net liabilities of $0.1 million, based on fair values.

Also in May 2005, the Company signed an investment agreement in a non-publicly traded company, under which it may be required to make additional investments of up to $3.8 million if certain milestones are met. In addition, the Company signed a licensing agreement with the same company, under which it may be required to pay up to $5.7 million of prepaid license fees if certain milestones are met.

Beginning on or about May 19, 2005, several securities class action complaints were filed against Brocade and certain of its current and former officers. These actions were filed on behalf of purchasers of Brocade's stock from February 2001 to May 2005. The securities class action complaints allege, among other things, violations of sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder. The complaints seek unspecified monetary damages and other relief against the defendants. The complaints generally allege that Brocade and the individual defendants made false or misleading public statements regarding Brocade's business and operations. These lawsuits followed Brocade's restatement of certain financial results due to stock-based compensation accounting issues.

Beginning on or about May 24, 2005, several derivative actions were also filed against certain of Brocade's current and former directors and officers. The complaints allege that certain of Brocade's officers and directors breached their fiduciary duties to Brocade by engaging in alleged wrongful conduct including conduct complained of in the securities litigation described above. Brocade is named solely as a nominal defendant against whom the plaintiffs seek no recovery.

On June 9, 2005, Brocade received notice that the Securities and Exchange Commission's informal inquiry regarding the Company's previous accounting for certain stock options was now the subject of a formal order of investigation. Brocade also announced that the Department of Justice is working with the Securities and Exchange Commission in a joint investigation regarding Brocade's stock option granting practice.

On August 23, 2005, in accordance with the terms of the indenture agreement dated December 21, 2001 with respect to the Company's 2% Convertible Subordinated Notes Due 2007 (the "Notes"), the Company elected to deposit funds with the trustee of the Notes (the "Trustee") and to discharge the indenture agreement. The Company deposited an aggregate of $276.1 million in interest-bearing U.S. securities with the Trustee. Pursuant to this election, the Company provided an irrevocable letter of instruction to the Trustee to issue a notice of redemption on June 26, 2006 and to redeem the Notes on August 22, 2006 (the "Redemption Date"). Over the course of the next year, the Trustee, using the securities deposited with them, will pay to the noteholders (1) all the interest scheduled to become due per the original note prior to the Redemption Date, and (2) all the principal and remaining interest, plus a call premium of 0.4% of the face value of the Notes, on the Redemption Date. The funds will remain on the Company's balance sheet as restricted securities until the Redemption Date. The Company expects to record a loss on investments of approximately $4.7 million in the quarter ending October 29, 2005 with respect to the disposition of certain short-term and long-term investments that was necessary to deposit the funds with the Trustee.

In October 2004, the American Jobs Creation Act of 2004 ("AJCA") was signed into law. The AJCA introduces a special one-time dividends received deduction on the repatriation of certain foreign earnings to a U.S. taxpayer, provided that certain criteria are met. In the fourth fiscal quarter of 2005, the Company determined, with approval by the Company's Chief Executive Officer and Board of Directors, to repatriate foreign earnings pursuant to the AJCA. In the fourth fiscal quarter of fiscal year 2005, the Company expects to record a tax charge of approximately $5.0 million based on a repatriation amount of approximately $78.0 million. No provision has been made for federal income taxes on the remaining balance of the unremitted earnings of the Company's foreign subsidiaries since the Company plans to permanently reinvest all such earnings outside the U.S.

Item 4. Controls and Procedures

(a) *Evaluation of Disclosure Controls and Procedures.* Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, as of the end of the period covered by this Quarterly Report on Form 10-Q (the "Evaluation Date").

The purpose of this evaluation is to determine if, as of the Evaluation Date, our disclosure controls and procedures were operating effectively such that the information relating to Brocade, required to be disclosed in our Securities and Exchange Commission ("SEC") reports (i) was recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, and (ii) was accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Based on this evaluation, as of the Evaluation Date, our Chief Executive Officer and Chief Financial Officer concluded that there existed material weaknesses in our disclosure controls and procedures as of January 29, 2005 and, therefore, our disclosure controls and procedures were not operating effectively as of such date, for the reasons discussed below.

Identification of Material Weaknesses.

In January 2005, following an internal review by our Audit Committee, we determined that we had not correctly accounted for: (A) stock option grants that were made to new hires on their offer acceptance date, rather than the date of their commencement of employment, during the period May 1999 to July 2000; (B) stock option grants that were made to persons engaged on a part-time basis prior to their new hire full-time employment during the period August 2000 to October 2002; and (C) stock option grants where there was insufficient basis to rely on our internal process and related documentation to support recorded measurement dates used to account for certain stock options granted prior to August 2003. As a result, we restated our financial statements to record additional stock-based compensation charges relating to many stock option grants from the periods 1999 though the third quarter of fiscal 2003 as well as a valuation allowance associated with deferred tax assets related to previously recorded stock option tax benefits (the "January 2005 Restatement"). In addition, it was concluded that there were improprieties in connection with the documentation of stock option grants and related employment records of a small number of employees prior to mid-2002, which resulted in immaterial adjustments included in this restatement.

Following the January 2005 Restatement, we discovered additional information that caused us to identify a material weakness relating to failure to adhere to our stock option granting policies during the period from August 2003 through November 2004. As a result, we determined that we could not rely on the documentation used to support the recorded measurement dates for the stock options granted during such period. We also identified a material weakness relating to failure to adhere to our policy regarding leaves of absence ("LOA") and transition or advisory roles. Specifically, we determined that from 1999 through 2004, we had not appropriately accounted for the cost of stock-based compensation for certain employees on LOA and in transition and advisory roles. As a result, in connection with an internal review by the Audit Committee, we determined to further restate our financial statements to record additional charges for stock-based compensation expense (the "November 2005 Restatement").

In connection with each of the January 2005 Restatement and November 2005 Restatement, our Audit Committee, with the assistance of independent legal counsel who engaged a forensic accounting firm, undertook a review of the matters referenced above.

(b) *Changes in Internal Control Over Financial Reporting.*

Since the beginning of fiscal year 2003, we have implemented numerous measures in connection with our ongoing effort to improve our control processes and corporate governance, many of which have been enhanced further as a result of the findings of our Audit Committee internal reviews and the determination that material weaknesses existed. As discussed below, there have been changes to our internal control over financial reporting during the quarter ended January 29, 2005 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Changes from December 2002 through October 30, 2004

1. Improvements in Disclosure Controls and Internal Control over Financial Reporting:

    - We improved the documentation of our significant accounting policies, which are reviewed with our Audit Committee.
    - Improvements have been made to the Audit Committee charter and committee functions. The Audit Committee charter was expanded to include in its scope the responsibility to review and approve all new, or changes to, significant accounting policies and positions. In addition, we expanded both the number of Audit Committee meetings from four to eight standing meetings, and the duration of those meetings. This allows a more in-depth review of complex accounting issues.
    - We formed a Disclosure Committee composed of representatives from our accounting, legal and investor relations departments, and our financial management, the minutes of which are reviewed with the Audit Committee.

2. Improvements in stock option granting process and related Internal Controls:

    - We implemented cross functional teams composed of members of our legal, accounting and human resources departments to develop improvements in the stock option granting process.
    - We formalized guidelines relating to the size and vesting schedule of stock option grants for all new employees and on-going employee grants.
    - We improved the documentation of the actions of the Compensation Committee and grant subcommittee regarding stock option granting.
    - We made personnel changes in areas associated with the stock option granting process to increase the levels of experience of the personnel involved.
    - We increased the frequency of stock option grants, moving to grants on a two to three week routine cycle, and significantly reduced the processing time between grant dates and the delivery of option paperwork to employees.

Changes from October 30, 2004 through January 29, 2005

Between October 30, 2004 and January 29, 2005, we took a number of steps to strengthen our disclosure controls and procedures and internal control over financial reporting. These remedial measures include personnel and procedural changes to improve the stock option granting process. Specifically, we have implemented the following additional internal control improvements:

- Increased the Compensation Committee of the Board of Directors to three independent members.
- The Compensation Committee refined and limited delegation of authority to a subcommittee to grant stock options.
- Documented into a formal written policy our stock option granting process.
- Created a pre-determined schedule for employee stock option grants, including enhancements with respect to the grant routine cycle.
- Adopted a policy not to grant executive officers options when trading is restricted for executives under the Company’s Insider Trading Policy.

Changes Subsequent to January 29, 2005

Subsequent to January 29, 2005, we have taken a number of steps to further strengthen our disclosure controls and procedures and internal control over financial reporting. These remedial measures include personnel and procedural changes to improve the stock option granting and employee change in status processes. Specifically, we have implemented the following additional internal control improvements:

- Improved the documentation and revised the approval process for initial, or changes to, policies associated with change in employee status, including leaves of absence and in transition and advisory roles.
- Established cross-functional teams comprised of members of our accounting, information technology and human resource departments to develop improvements in the employee change of status systems and processes.
- Performed additional training for personnel in areas associated with the stock option granting and employee change in status processes to increase competency levels of the personnel involved.

We also completed further testing of the policies and procedures and related controls that we recently implemented as discussed above.

Based on the above changes and related testing, we believe we have remedied the material weaknesses indicated above as of July 30, 2005.

Limitations on the Effectiveness of Disclosure Controls and Procedures.

Our management, including our Chief Executive Officer and Chief Financial Officer, do not expect that our disclosure controls and procedures or internal control over financial reporting will prevent all error and all fraud. A control system no matter how well designed and implemented, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues within a company are detected. The inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistakes. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people or by management override of the controls. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and may not be detected.

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PART II — OTHER INFORMATION

Item 6. Exhibits

31.1	Rule 13a-14(a)/15d-14(a) Certification by the Chief Executive Officer.
31.2	Rule 13a-14(a)/15d-14(a) Certification by the Chief Financial Officer.
32.1	Certification by the Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

BROCADE COMMUNICATIONS SYSTEMS, INC.

Date: November 14, 2005

By: /s/ ANTONIO CANOVA
Antonio Canova
Vice President, Administration and
Chief Financial Officer

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Exhibit Index

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31.2	Rule 13a-14(a)/15d-14(a) Certification by the Chief Financial Officer.
32.1	Certification by the Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

EXHIBIT 31.1

CERTIFICATION

I, Michael Klayko, certify that:

1. I have reviewed this amended quarterly report on Form 10-Q/A for the first fiscal quarter of 2005 ended January 29, 2005 of Brocade Communications Systems, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

   a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   c. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 14, 2005

/s/ Michael Klayko

Michael Klayko
Chief Executive Officer
(Principal Executive Officer)

EXHIBIT 31.2

CERTIFICATION

I, Antonio Canova, certify that:

1. I have reviewed this amended quarterly report on Form 10-Q/A for the first fiscal quarter of 2005 ended January 29, 2005 of Brocade Communications Systems, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

   a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   c. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 14, 2005

/s/ Antonio Canova
Antonio Canova
Chief Financial Officer
(Principal Accounting Officer)

EXHIBIT 32.1

CERTIFICATION OF CHIEF EXECUTIVE OFFICER
AND CHIEF FINANCIAL OFFICER PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

I, Michael Klayko, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the amended Quarterly Report of Brocade Communications Systems, Inc. on Form 10-Q/A for the fiscal quarter ended January 29, 2005 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such amended Quarterly Report on Form 10-Q fairly presents in all material respects the financial condition and results of operations of Brocade Communications Systems, Inc.

By: /s/ Michael Klayko
Michael Klayko
Chief Executive Officer

I, Antonio Canova, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the amended Quarterly Report of Brocade Communications Systems, Inc. on Form 10-Q/A for the fiscal quarter ended January 29, 2005 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such amended Quarterly Report on Form 10-Q/A fairly presents in all material respects the financial condition and results of operations of Brocade Communications Systems, Inc.

By: /s/ Antonio Canova
Antonio Canova
Vice President, Administration and
Chief Financial Officer