MICRUS ENDOVASCULAR CORP
Form 10-Q
August 11, 2008
Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2008

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: 000-51323

Micrus Endovascular Corporation
(Exact name of registrant as specified in its charter)

Delaware	23-2853441
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
821 Fox Lane San Jose, California	95131
(Address of principal executive offices)	(Zip Code)

(408) 433-1400
(Registrant's 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 R No £

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

£ Large accelerated filer R Accelerated filer £ Non-accelerated filer £ Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes £ No R

As of August 4, 2008, there were 15,662,892 shares of common stock, par value $0.01, of the registrant outstanding.

MICRUS ENDOVASCULAR CORPORATION

INDEX TO FORM 10-Q

Table of Contents

PART I — FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

MICRUS ENDOVASCULAR CORPORATION
Condensed Consolidated Balance Sheets
(unaudited)
(in thousands, except share and per share amounts)

	June 30, 2008	March 31, 2008
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 16,917	$ 25,526
Accounts receivable, net of allowance for doubtful accounts of $98 at June 30, 2008 and $95 at March 31, 2008	9,474	11,297
Inventories	11,688	11,495
Prepaid expenses and other current assets	1,175	1,570
Deferred tax assets	110	-
Total current assets	39,364	49,888
Property and equipment, net	5,771	5,285
Goodwill	9,006	8,549
Intangible assets, net	6,716	7,153
Deferred tax assets	9	9
Other assets	1,323	1,448
Total assets	$ 62,189	$ 72,332
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	$ 4,036	$ 3,680
Accrued payroll and other related expenses	4,547	7,930
Deferred tax liabilities	-	43
Accrued liabilities	8,238	9,431
Total current liabilities	16,821	21,084
Deferred tax liabilities	247	314
Other non-current liabilities	1,748	2,754
Total liabilities	18,816	24,152
Commitments and contingencies (Note 6)		
Stockholders' equity:		
Common stock, $0.01 par value; Authorized: 50,000,000 shares Issued and outstanding:15,647,912 shares at June 30, 2008 and 15,614,760 shares at March 31, 2008	156	156
Additional paid-in capital	121,770	119,897
Accumulated other comprehensive loss	(589)	(511)
Accumulated deficit	(77,964)	(71,362)

Total stockholders' equity	43,373	48,180
Total liabilities and stockholders' equity	$ 62,189	$ 72,332

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

Table of Contents

MICRUS ENDOVASCULAR CORPORATION
Condensed Consolidated Statements of Operations
(unaudited)
(in thousands, except per share amounts)

	Three months ended June 30,	
	2008	2007
Revenues	$ 18,324	$ 16,790
Cost of goods sold	4,593	3,735
Gross profit	13,731	13,055
Operating expenses:		
Research and development	2,973	1,965
Sales and marketing	8,118	6,510
General and administrative	9,562	6,276
Total operating expenses	20,653	14,751
Loss from operations	(6,922)	(1,696)
Interest income	110	360
Interest expense	(4)	-
Other income (expense), net	(2)	78
Loss before income taxes	(6,818)	(1,258)
Provision (benefit) for income taxes	(216)	135
Net loss	$ (6,602)	$ (1,393)
Net loss per share attributable to common stockholders:		
Basic and diluted	$ (0.42)	$ (0.09)
Weighted-average number of shares used in per share calculations:		
Basic and diluted	15,621	15,291

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

Table of Contents

MICRUS ENDOVASCULAR CORPORATION
Condensed Consolidated Statements of Cash Flows
(unaudited)
(in thousands)

	Three months ended June 30,	
	2008	2007
Cash flows from operating activities:		
Net loss	$ (6,602)	$ (1,393)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	806	791
Provision for doubtful accounts	3	23
Loss on disposal of equipment	-	27
Provision for excess and obsolete inventories	30	153
Unremitted issuance of stock for tentative settlement of patent litigation	1,650	-
Stock-based compensation	1,549	1,056
Deferred income taxes	(217)	-
Changes in operating assets and liabilities, net of effect of acquisitions and tentative settlement of patent litigation:		
Accounts receivable	1,684	(873)
Inventories	(255)	(1,466)
Prepaid expenses and other current assets	386	(363)
Other assets	122	6
Accounts payable	369	186
Accrued payroll and other related expenses	(3,362)	(2,101)
Accrued liabilities	549	277
Other non-current liabilties	(1,003)	(76)
Net cash used in operating activities	(4,291)	(3,753)
Cash flows from investing activities:		
Acquisition of property and equipment	(843)	(487)
Earn-out payment in connection with acquisition of Neurologic UK Ltd.	(3,454)	(2,232)
Earn-out payment in connection with acquisition of VasCon, LLC	(378)	-
Net cash used in investing activities	(4,675)	(2,719)
Cash flows from financing activities:		
Proceeds from exercise of stock options	302	522
Net cash provided by financing activities	302	522
Effect of foreign exchange rate changes on cash	55	(28)
Net decrease in cash and cash equivalents	(8,664)	(5,950)
Cash and cash equivalents at beginning of period	25,526	34,536
Cash and cash equivalents at end of period	$ 16,917	$ 28,558

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

Table of Contents

MICRUS ENDOVASCULAR CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1 — Formation and Business of the Company

Micrus Endovascular Corporation (the "Company") was incorporated under the laws of the state of Delaware in June 1996. The Company develops, manufactures and markets both implantable and disposable medical devices used in the treatment of cerebral vascular diseases. The Company's products are used by interventional neuroradiologists, interventional neurologist, and neurosurgeons to treat both cerebral aneurysms responsible for hemorrhagic stroke and intracranial atherosclerosis, which may lead to ischemic stroke. Hemorrhagic and ischemic stroke are both significant causes of death and disability worldwide.

Interim unaudited financial information

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") for interim financial information and in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X of the Securities and Exchange Commission ("SEC"). Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. The unaudited interim condensed consolidated financial statements have been prepared on the same basis as the annual financial statements. In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation of the Company's financial position as of the date of the interim balance sheet and results of operations and cash flows for the interim periods. These financial statements should be read in conjunction with the audited financial statements and notes thereto for the preceding fiscal year included in the Company's Annual Report on Form 10-K for the fiscal year ended March 31, 2008 which was filed with the SEC on June 12, 2008. Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. The condensed consolidated balance sheet at March 31, 2008 was derived from audited financial statements, but does not include all disclosures required by GAAP.

The results of operations for the interim periods ended June 30, 2008 may not necessarily be indicative of the results that may be expected for the fiscal year ended March 31, 2009, or any future period.

Liquidity

The Company has incurred net losses since inception. Management believes that the Company's current cash position as of June 30, 2008 and the cash expected to be generated from product sales will be sufficient to meet the Company's working capital and capital expenditure requirements for at least the next twelve months. There is no assurance that the Company will be profitable in the foreseeable future. To the extent that existing cash and cash generated from operations are insufficient to fund its future activities, the Company may need to raise additional funds through public or private equity or debt financing. Additional funds may not be available on terms favorable to the Company or at all.

Note 2 — Summary of Significant Accounting Policies

Principles of consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

The Company's international subsidiaries use their local currency as the functional currency. Assets and liabilities are translated at exchange rates prevailing at the balance sheet date. Revenue, expense, gain and loss accounts are translated at average exchange rates during the period. Resulting translation adjustments are recorded directly to accumulated other comprehensive income (loss).

Reclassifications

Certain amounts in the prior year consolidated financial statements have been reclassified to conform to the current year presentation. These reclassifications had no impact on previously reported total assets, stockholders' equity or net loss.

Table of Contents

Use of estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from these estimates. These estimates and assumptions include reserves and write-downs related to accounts receivable and inventories, the recoverability of long-term assets, deferred tax assets and liabilities and related valuation allowances and valuation of equity instruments.

Revenue recognition – sales made to Latin American distributors

Sales made to the Company's Latin American distributors are made according to similar contractual terms as sales made to other customers. However, due to historically longer delays in receiving payments and a higher level of write-offs relating to our Latin American distributors, the Company had concluded in previous fiscal periods that collectibility was not reasonably assured at the time that the customer took title to the inventory on sales to Latin American customers. Accordingly, the Company had recognized revenues from its sales to Latin American distributors when cash was collected. The Company has evaluated its experience with its Latin American distributors and has concluded that collectibility is now reasonably assured upon shipment, and began recognizing revenue upon shipment to these distributors in the quarter ended June 30, 2008. Revenues recognized upon shipment on sales made to the Company's Latin American distributors were $0.7 million for the three months ended June 30, 2008. Additionally, the deferred revenue balance at March 31, 2008 of $0.7 million for these customers and the related cost of goods sold of $273,000 that had been deferred has been recognized as revenue and cost of goods sold, respectively, in the three months ended June 30, 2008.

Revenues recognized for the Company's Latin American distributors were $349,000 for the three months ended June 30, 2007. Revenues recognized for these customers were $1.6 million, $1.1 million and $0.8 million for the fiscal years ended March 31, 2008, 2007 and 2006, respectively.

Comprehensive loss

Comprehensive loss generally represents all changes in stockholders' equity except those resulting from investments or contributions by stockholders. Accumulated other comprehensive loss as of June 30, 2008 and March 31, 2008 was comprised entirely of foreign currency translation adjustments. Total comprehensive loss for the three months ended June 30, 2008 and 2007 was $6.7 million and $1.4 million, respectively. This included other comprehensive loss of ($78,000) and ($42,000) respectively, related to foreign currency translation adjustments.

Net loss per share

Basic net loss per share is computed by dividing net loss by the weighted average number of common shares outstanding during the period. Diluted net loss per share is computed by giving effect to all potential dilutive common shares, including stock options, employee stock purchase plan shares and restricted stock units. There is no difference between basic and diluted net loss per share for all periods presented due to the Company's net losses.

Anti-dilutive securities

The following outstanding stock options, employee stock purchase plan shares and restricted stock units were excluded from the computation of diluted net loss per common share for the periods presented because their impact would have been anti-dilutive (in thousands):

	Three months ended June 30,	
	2008	2007
Shares issuable upon exercise of common stock options	4,095	3,239
Shares issuable upon settlement of restricted stock units	4	7
Shares issuable under employee stock purchase plan	36	16
	4,135	3,262

Table of Contents

Stock-based compensation

The Company has adopted various stock plans that provide for the grant of stock awards to employees, non-employee directors and consultants. The Company also has an employee stock purchase plan which enables employees to purchase the Company's common stock.

On April 1, 2006, the Company adopted the provisions of, and accounts for stock-based compensation in accordance with the Financial Accounting Standards Board's ("FASB") Statement of Financial Accounting Standards No. 123 — revised 2004 ("SFAS 123R"), "Share-Based Payment" which replaced Statement of Financial Accounting Standards No. 123 ("SFAS 123"), "Accounting for Stock-Based Compensation" and supersedes APB Opinion No. 25 ("APB 25"), "Accounting for Stock Issued to Employees." Under the fair value recognition provisions of SFAS 123R, stock-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense on a straight-line basis over the requisite service period, which is generally the vesting period. The Company elected the modified-prospective method of transition, under which prior periods were not revised for comparative purposes. The valuation provisions of SFAS 123R apply to new grants and to grants that were outstanding prior to the effective date and are subsequently modified. Estimated compensation for grants that were outstanding as of the effective date will be recognized over the remaining service period using the compensation cost estimated for the SFAS 123 pro forma disclosures.

Due to the adoption of SFAS 123R, some exercises result in tax deductions in excess of previously recorded benefits based on the option value at the time of grant ("windfall" tax benefits). The Company recognizes windfall tax benefits associated with the exercise of stock options directly to stockholders' equity only when realized. Accordingly, deferred tax assets are not recognized for net operating loss carryforwards resulting from windfall tax benefits occurring from April 1, 2006 onward. A windfall tax benefit occurs when the actual tax benefit realized by a company upon an employee's disposition of a share-based award exceeds the deferred tax asset, if any, associated with the award that a company had recorded. When assessing whether a tax benefit relating to share-based compensation has been realized, the Company has elected to follow the tax law ordering method, under which current year share-based compensation deductions are assumed to be utilized before net operating loss carryforwards and other tax attributes. Also, the Company has elected to ignore the indirect tax effects of share-based compensation deductions in computing its research and development tax credit. The Company will recognize the full effect of these deductions in the statements of operations when the valuation allowance is released.

Recent accounting pronouncements

In December 2007, the FASB issued Statement of Financial Accounting Standard ("SFAS") No. 141R (revised 2007), "Business Combinations," which replaces SFAS 141. SFAS 141R requires the acquiring entity in a business combination to recognize at full fair value all the assets acquired and liabilities assumed in the transaction; establishes the acquisition-date fair value as the measurement objective for all assets acquired and liabilities assumed; and requires the acquirer to disclose information needed to evaluate and understand the nature and financial effect of the business combination. SFAS 141R is effective for fiscal years beginning after December 15, 2008 and is to be applied prospectively to business combinations completed on or after the date of adoption. The Company is currently evaluating the impact of adopting SFAS 141R on the Company's consolidated financial position, results of operations or cash flows.

In February 2008, the FASB issued Financial Standard Position ("FSP") SFAS 157-2, "Effective Date for FASB Statement No. 157." This FSP permits the delayed application of SFAS 157 for all nonrecurring fair value measurements of non-financial assets and non-financial liabilities until fiscal years beginning after November 15,

2008. The Company is currently evaluating the impact of adopting the provisions of SFAS 157 for non-financial assets and liabilities that are recognized or disclosed on a non-recurring basis.

In April 2008, the FASB issued FASB Staff Position ("FSP") SFAS No. 142-3, "Determination of the Useful Life of Intangible Assets" ("FSP SFAS 142-3"). FSP SFAS 142-3 amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under SFAS 142, "Goodwill and Other Intangible Assets." The intent of this FSP is to improve the consistency between the useful life of a recognized intangible asset and the period of expected cash flows used to measure the fair value of the asset under SFAS 141 (revised 2007), "Business Combinations" and other U.S. generally accepted accounting principles (GAAP). FSP SFAS 142-3 is effective for the Company on April 1, 2009. The Company is currently evaluating the impact of adopting FSP SFAS 142-3 on the Company's consolidated financial position, results of operations or cash flows.

Table of Contents

In May 2008, the FASB issued SFAS No. 162, "The Hierarchy of Generally Accepted Accounting Principles" ("SFAS 162"), which becomes effective 60 days following the SEC's approval of the Public Company Accounting Oversight Board ("PCAOB") amendments to US Auditing Standards ("AU") Section 411, "The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles." SFAS 162 identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with US GAAP. This standard is not expected to have an impact on the Company's consolidated financial position, results of operations or cash flow.

Note 3 — Fair Value Measurements

Effective April 1, 2008, the Company adopted the provisions of SFAS 157 for financial assets and liabilities, as well as for any other assets and liabilities that are carried at fair value on a recurring basis. The adoption of the provisions of SFAS 157 did not materially impact the Company's consolidated financial position and results of operations.

SFAS 157 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. SFAS 157 also establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. SFAS 157 describes three levels of inputs that may be used to measure fair value:

Level 1 Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

Level 2 Quoted prices in markets that are not active; or other inputs that are observable, either directly or indirectly, for substantially the full term of the asset or liability.

Level 3 Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable.

The Company's cash equivalents are classified within Level 1 of the fair value hierarchy because they are valued using quoted market prices, broker or dealer quotations, or alternative pricing sources with reasonable levels of price transparency.

The following table presents assets measured at fair value on a recurring basis at June 30, 2008 (in thousands):

	Level 1	Level 2	Level 3	Total
Money Market Mutual Funds	$ 13,013	$ -	$ -	$ 13,013

The Company's financial liabilities that are required to be carried at fair value at June 30, 2008 were not material.

Table of Contents

Note 4 — Balance Sheet Components

Inventories

Inventories consisted of the following (in thousands):

	June 30, 2008	March 31, 2008
Raw materials	$ 2,037	$ 2,154
Work-in-progress	2,183	1,667
Finished goods	3,202	3,002
Consigned inventory	4,198	4,331
Inventory held by distributor	68	341
	$ 11,688	$ 11,495

Consigned inventory is held at customer locations, primarily hospitals, and is under the physical control of the customer. The Company retains title to the inventory until used and purchased by the customer, generally when used in a medical procedure.

Inventory held by distributor at June 30, 2008 was held by the Company's Chinese distributor (see Note 2 in Notes to Condensed Consolidated Financial Statements). Inventory held by distributors at March 31, 2008 consists of $273,000 in inventory that was held by the Company's Latin American distributors and $68,000 in inventory that was held by the Company's Chinese distributor.

Property and equipment, net

Property and equipment, net, consisted of the following (in thousands):

	June 30, 2008	March 31, 2008
Computer equipment and software	$ 1,793	$ 1,728
Furniture, fixtures and equipment	5,568	5,403
Leasehold improvements	1,014	1,010
Construction in progress	1,040	447
Total cost	9,415	8,588
Less accumulated depreciation and amortization	(3,644)	(3,303)
	$ 5,771	$ 5,285

Goodwill

Activity related to goodwill consisted of the following (in thousands):

	June 30, 2008	March 31, 2008
Balance beginning of period	$ 8,549	$ 5,552
Addition related to Neurologic earn-out payment	457	2,997
Balance end of period	$ 9,006	$ 8,549

10

Table of Contents

At March 31, 2008, the Company accrued for additional consideration of approximately $3.0 million for the third year earn-out associated with the purchase of Neurologic UK Ltd. ("Neurologic"), which was recorded as goodwill and paid the accrued earn-out in April 2008. In June 2008, the Company paid the final earn-out for periods April and May of approximately $457,000.

Intangible assets, net

Intangible assets, net, consisted of the following (in thousands):

	Useful Life (Years)	Gross Carrying Amount			Accumulated Amortization			Net	
		March 31, 2008	Additions	June 30 2008	March 31, 2008	(Additions)	June 30, 2008	June 30, 2008	March 31, 2008
Existing process technology	7	$ 4,590	$ -	$ 4,590	$ (874)	$ (164)	$ (1,038)	$ 3,552	$ 3,716
Distribution agreements	5	2,300	-	2,300	(1,164)	(115)	(1,279)	1,021	1,136
Capitalized license fee	7	1,565	-	1,565	(336)	(56)	(392)	1,173	1,229
Patents - microcoil	10	1,100	-	1,100	(880)	(27)	(907)	193	220
Non-compete agreements	6	700	-	700	(294)	(29)	(323)	377	406
Customer relationships	5	900	-	900	(454)	(46)	(500)	400	446
		$ 11,155	$ -	$ 11,155	$ (4,002)	$ (437)	$ (4,439)	$ 6,716	$ 7,153

Amortization of intangible assets included in the results of operations is as follows (in thousands):

	Three months ended June 30,	
	2008	2007
Cost of goods sold	$ 220	$ 260
Operating expenses	217	217
Total	$ 437	$ 477

The expected future amortization of intangible assets is as follows (in thousands):

For Years Ended March 31,	Amortization
2009 (remaining 9 months)	$ 1,309
2010	1,746
2011	1,298
2012	935
2013	879
Thereafter	549

Total	$	6,716

11

Table of Contents

Accruals

Accrued payroll and other related expenses consisted of the following (in thousands):

	June 30, 2008	March 31, 2008
Accrued bonuses	$ 1,164	$ 2,642
Accrued salaries	534	1,071
Accrued vacation	1,892	1,750
Accrued 401K	68	-
Accrued commissions	455	1,660
Accrued payroll taxes	434	807
	$ 4,547	$ 7,930

Accrued liabilities consisted of the following (in thousands):

	June 30, 2008	March 31, 2008
Tentative settlement of patent litigation with Boston Scientific	$ 1,650	$ -
Milestone fee to The Cleveland Clinic Foundation	1,500	500
Professional fees	1,452	1,715
VAT payable	540	560
Accrued travel and entertainment	471	492
Biotronik AG development costs	282	443
Development costs	173	288
Milestone fee to Genesis Medical Interventional, Inc.	150	150
Deferred revenue from Japan distribution agreement	113	113
Earn-out payment in connection with Neurologic acquisition	-	2,997
Earn-out payment in connection with VasCon, LLC	-	378
Other	1,907	1,795
	$ 8,238	$ 9,431

Other non-current liabilities

Other non-current liabilities consisted of the following (in thousands):

	June 30, 2008	March 31, 2008
Contingent purchase price	$ 1,218	$ 1,218
Deferred revenue from Japan distribution agreement	253	281
Swiss pension plan obligation	80	82
Milestone fee to The Cleveland Clinic Foundation	-	1,000
Other non-current liabilities	197	173
	$ 1,748	$ 2,754

The negative goodwill of $1.6 million associated with the purchase of VasCon has been recorded as a contingent purchase price. The amount is being reduced by any earned contingent consideration of up to $10.0 million that will

be paid over the next three years, with any additional contingent consideration being recorded as goodwill. The Company paid the first year earn-out of approximately $378,000 in April 2008.

Table of Contents

Note 5 — Income Taxes

The Company has incurred net operating losses for both federal and state purposes since inception and, as a result, the Company has paid no federal or state income tax. For the three months ended June 30, 2008, the Company recorded an income tax benefit of approximately $216,000. The income tax benefit for the three months ended June 30, 2008 includes income tax benefit of $150,000 related to net operating losses for its Swiss subsidiary, and a non-current tax benefit of approximately $66,000 for the tax effect of the amortization related to the identifiable intangible assets acquired in the Neurologic transaction which are amortized for tax purposes and the tax benefit from net operating losses for its United Kingdom subsidiary.

As of March 31, 2008, the Company had federal, state and foreign net operating loss carryforwards ("NOLs") that are available to reduce future taxable income of approximately $42.5 million, $27.6 million and $1.6 million, respectively. The federal NOLs will expire at various dates beginning in 2012, state NOLs will expire beginning in 2013 and the foreign NOLs will expire beginning in 2013. The Company also has federal and state tax research and development credit carryforwards of approximately $1.2 million and $1.1 million, respectively. The federal tax credit carryforwards will expire beginning in 2012. The state tax credit carryforwards can be carried forward indefinitely. Due to the uncertainty of its ability to generate sufficient taxable income to realize the carryforwards prior to their expiration, the Company has recorded a valuation allowance at June 30, 2008 to offset its federal and state deferred tax assets.

Since the implementation of FIN 48, the Company has recognized a $232,000 increase in its unrecognized tax benefits. The Company does not expect its unrecognized tax benefits to change significantly over the next twelve months. At June 30, 2008, the Company had no accrued interest or penalties related to tax contingencies.

Note 6 — Commitments and Contingencies

Indemnification

In the normal course of business, the Company enters into contracts and agreements that contain a variety of representations and warranties and provide for general indemnification. The Company's exposure under these agreements is unknown because it involves claims that may be made against the Company in the future, but have not yet been made. To date, the Company has not paid any claims or been required to defend any action related to its indemnification obligations, and accordingly, the Company has not accrued any amounts for such indemnification obligations. However, the Company may record charges in the future as a result of these indemnification obligations.

Litigation

The Company is from time to time subject to various lawsuits. The Company does not believe that it is probable that resolution of pending litigation will have a material adverse effect on the Company's consolidated financial statements; however the outcome of litigation is inherently uncertain.

FCPA investigation

In August 2004, while reviewing sales and payment procedures, the Company identified certain payments made to physicians outside the United States that may have violated the Foreign Corrupt Practices Act ("FCPA") and the laws of certain foreign countries. In September 2004, following an internal investigation, the Company voluntarily disclosed to the United States Department of Justice ("DOJ") the factual information obtained in its internal investigation of potential violations of the FCPA.

After reviewing the results of the internal investigation and the compliance procedures implemented by the Company, the DOJ entered into an agreement (the "DOJ Agreement") with the Company in February 2005. Pursuant to that agreement, the DOJ agreed not to prosecute the Company for the conduct disclosed to the DOJ, and the Company agreed to various conditions, including establishing policies and procedures to assure compliance with the FCPA and other relevant anti-bribery laws, retaining an independent law firm to act as a monitor for purposes of reporting to the DOJ for a period of three years as to its compliance with the DOJ Agreement and to monitor its implementation of and adherence to FCPA compliance policies and procedures, and fully cooperating with the DOJ, the independent monitor, and the SEC.

Table of Contents

The monitor filed his final report with the DOJ in May 2008, and in July 2008, the DOJ confirmed that the monitorship had concluded. The Company has reaffirmed its commitment to take all reasonable steps to ensure that it remains in compliance with the FCPA.

The payments made to physicians in France, Germany, Spain and Turkey also may likely have violated the applicable laws in those foreign jurisdictions. The Company has not been notified by the authorities in France, Germany, Spain or Turkey whether or not such authorities intend to bring any action or impose any penalties on us relating to our activities in their respective countries. Therefore, we are unable to determine at this time what penalties or other sanctions, if any, such authorities may impose as a result of such violations. Such amounts could be material to the financial position, results of operations or cash flows of the Company.

Patent litigation

In September 2004, Boston Scientific Corporation and Target Therapeutics, Inc., a subsidiary of Boston Scientific Corporation, (collectively "Boston Scientific"), filed a patent infringement suit in the United States District Court for the Northern District of California, alleging that the Company's embolic coil products infringe two patents (United States Patent Nos. 5,895,385 (the "'385 Patent") and 6,010,498 (the "'498 Patent")) owned by the Regents of the University of California (the "Regents") and exclusively licensed to Boston Scientific and that this infringement is willful. Sales of the Company's embolic coil products currently represent approximately 94% of the Company's revenues. Boston Scientific is a large, publicly-traded corporation with significantly greater financial resources than the Company.

In November 2004, the Company answered Boston Scientific's complaint and counterclaimed, alleging that Boston Scientific's embolic coil products, and their use, infringe three of the Company's patents. In addition, the Company alleged that Boston Scientific has violated United States antitrust laws, and has violated certain California state laws by committing unfair business practices, disparaging its products, and interfering with its prospective economic advantage. Each party seeks an injunction preventing the making, using, selling, offering to sell, importing into the United States or exporting from the United States, of the other's embolic coil products in the United States, damages for past infringement, which may be trebled, and payment of its legal fees and costs. In addition, each party seeks a declaration that the patents of the other are invalid and not infringed and has alleged that certain of the asserted patents of the other are unenforceable due to inequitable conduct.

In January 2005, Boston Scientific filed a motion to dismiss the Company claims for disparagement, interference with prospective economic advantage and unfair business practices. In June 2008, the court issued an order dismissing these claims without prejudice and granting the Company leave to amend its counterclaims. The Company filed amended counterclaims in July 2008. Boston Scientific has not responded to the Company's amended counterclaims.

In November 2006, the Company withdrew one of its three asserted patents from the litigation to pursue a reissue application filed with the United States Patent and Trademark Office ("USPTO").

A hearing on claim construction was held in June 2007. In March 2008, the Court issued an order construing certain claim terms of patents that were asserted by Boston Scientific against Micrus or asserted by Micrus against Boston Scientific. On April 23, 2008, the district court entered a scheduling order on future events in this action, including the close of all discovery on January 26, 2009. A trial date has not been set by the district court.

Boston Scientific has also been a party in two other lawsuits against Cordis and Micro Therapeutics, Inc./ev3, Inc./Dendron GmbH (collectively "MTI") in which the two Boston Scientific patents asserted against the Company are or were also at issue. An outcome of either of these lawsuits adverse to Cordis or MTI, and related to the same patent claims Boston Scientific asserts against the Company, could have an adverse impact on certain of the Company

defenses in its litigation with Boston Scientific.

According to court records, the Regents, Boston Scientific and MTI entered into a settlement agreement on March 21, 2008, and on April 4, 2008 the Regents, Boston Scientific and MTI dismissed the action, including all claims and counter-claims, with prejudice.

Table of Contents

On January 18, 2008, in the Cordis case, the district court granted Boston Scientific's motion for summary judgment that Cordis' TRUFILL Detachable Coil System infringed claim 7 of the '385 Patent under the doctrine of equivalents. On January 25, 2008, the district court granted Boston Scientific's motion for summary judgment against Cordis that claims 10 and 35 of the '385 patent, and claims 1, 3, 7, 9, and 10 of the '498 patent, are not invalid for having been on-sale or in public use before the statutory bar period. On March 21, 2008, the district court granted-in-part Boston Scientific's motion for summary judgment that the '385 patent and '498 patent are not unenforceable for inequitable conduct. The district court also denied-in-part Boston Scientific's motion on the ground that triable issues of fact remained concerning the patent applicants' representations to the patent examiner during the application process. The district court's determinations on the validity and enforceability of the '385 and '498 patents are important because

Boston Scientific is asserting these same patents against the Company in its lawsuit and the Company is alleging that these patents are invalid and unenforceable.

In October 2004, Cordis requested ex parte reexamination of certain claims in Boston Scientific's '385 and '498 patents. In April 2007, the USPTO issued a Notice of Intent to Issue Ex Parte Reexamination Certificate for the '498 patent, apparently confirming all of the claims of that patent. In December 2006, the USPTO issued a Notice of Allowance for the '385 patent in which it apparently confirmed the patentability of the claims in that patent.

The Company is currently in the process of negotiating a settlement with Boston Scientific and the U.C. Regents (which licensed some of the patents-in-suit to Boston Scientific but is not a party to the lawsuit). These negotiations currently contemplate the issuance by the Company of approximately $1.7 million in stock that would accompany patent cross-licenses between the Company and Boston Scientific. The accrued cost of approximately $1.7 million in connection with the tentative settlement of patent litigation with Boston Scientific was recorded as general and administrative expense in the first quarter of fiscal 2009. This issuance of stock, together with a payment of approximately $1.0 million by Boston Scientific to the U.C. Regents, would be made to the U.C. Regents to satisfy the Regents' claim related to these patents. However, there can be no assurance that a settlement agreement will be finalized on these or any terms.

Note 7 — Stock-based Compensation

Stock options

The Company's stock option program is a long-term retention program that is intended to attract, retain and provide incentives for talented employees, officers and directors, and to align stockholder and employee interests. The Company considers the stock option program critical to its operations and productivity. As of June 30, 2008, the Company has three stock option plans: the 1996 Stock Option Plan (the "1996 Plan"), the 1998 Stock Plan (the "1998 Plan"), and the 2005 Equity Incentive Plan (the "2005 Plan"). Currently, the Company grants options from the 2005 Plan, which permits the Company to grant options to all employees, including executive officers, and outside consultants, and directors. Effective June 16, 2005, no new options may be granted under the 1996 Plan or the 1998 Plan. As of June 30, 2008, there were no outstanding options under the 1996 Plan and 1,056,976 outstanding options under the 1998 Plan. As of June 30, 2008, there were 4,304,313 remaining shares reserved for issuance under the 2005 Plan, of which 1,262,841 were available for grant, 3,038,139 shares were subject to outstanding options and 3,333 shares were subject to outstanding restricted stock units. Stock options issued under the Company's stock option plans generally vest based on 4 years of continuous service and have 10-year contractual terms.

2005 Employee stock purchase plan

The 2005 Employee Stock Purchase Plan (the “Purchase Plan”) became effective upon the Company’s initial public offering. The Purchase Plan provides employees with an opportunity to purchase the Company’s common stock through accumulated payroll deductions. As of June 30, 2008, there were 678,572 shares reserved for issuance under the Purchase Plan.

Stock-based compensation

On April 1, 2006, the Company adopted the provisions of SFAS 123R. The Company’s financial statements for the three months ended June 30, 2008 and 2007 reflect the impact of SFAS 123R. The Company currently uses the Black-Scholes option pricing model to determine the fair value of employee stock options and employee stock purchase plan shares. The determination of the fair value of employee stock options and employee stock purchase plan shares has been estimated using the following weighted-average valuation assumptions:

Table of Contents

	Three months ended June 30,	
	2008	2007
Employee Stock Option Plans		
Expected term (in years)	6	6
Volatility	35%	42%
Risk-free interest rate	3.3%	4.8%
Expected dividend yield	0%	0%
Weighted average fair value at date of grant	$ 4.52	$ 10.96
Employee Stock Purchase Plan		
Expected term (in years)	0.5	0.5
Volatility	49%	41%
Risk-free interest rate	3.0%	5.1%
Expected dividend yield	0%	0%

The fair value of each purchase right granted under the Company's Purchase Plan during the three months ended June 30, 2008 and 2007 was estimated at the date of grant using the Black-Scholes option pricing model, and is not subject to revaluation as a result of subsequent stock price fluctuations.

The stock-based compensation expense related to SFAS 123R is as follows (in thousands):

	Three months ended June 30,	
	2008	2007
Cost of goods sold	$ 117	$ 110
Research and development	169	112
Sales and marketing	441	240
General and administrative	822	535
Total	$ 1,549	$ 997

Additionally, approximately $178,000 and $115,000 in stock-based compensation expense related to SFAS 123R has been capitalized in inventory as of June 30, 2008 and 2007, respectively.

As of June 30, 2008, there was approximately $14.1 million of total stock-based compensation expense, after estimated forfeitures, related to unvested employee stock options and restricted stock units, which is expected to be recognized over an estimated weighted average amortization period of 2.7 years.

Stock-based compensation expense recognized for the three months ended June 30, 2008 and 2007 related to the amortization of deferred stock-based compensation was $0 and $53,000, respectively. The Company had fully recognized amortization of deferred stock-based compensation in the fourth quarter ending March 31, 2008.

Stock-based compensation expense recognized for the three months ended June 30, 2008 and 2007 related to non-employee options was $0 and $6,000, respectively. There were no unvested non-employee options for the three months ended June 30, 2008.

Table of Contents

Total stock-based compensation expense included in the results of operations is as follows (in thousands):

	Three months ended June 30,	
	2008	2007
Cost of goods sold	$ 117	$ 116
Research and development	169	112
Sales and marketing	441	245
General and administrative	822	583
Total	$ 1,549	$ 1,056

General stock option information

The following table sets forth the summary of stock options activity for the three months ended June 30, 2008:

	Shares (in thousands)	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in thousands)
Options outstanding at March 31, 2008	3,656	$ 13.02		
Options granted	528	$ 11.35		
Options exercised	(31)	$ 9.81		
Options forfeited	(39)	$ 15.08		
Options expired	(19)	$ 7.31		
Options outstanding at June 30, 2008	4,095	$ 12.83	8.0	$ 13,244
Options exercisable at June 30, 2008	1,851	$ 9.83	7.0	$ 9,668

The total aggregate intrinsic value of options exercised during the three months ended June 30, 2008 and 2007 was $90,000 and $1.4 million, respectively. The closed market value per share of the Company's common stock as of June 30, 2008 was $14.02 per share as reported by The NASDAQ Stock Market.

The following table sets forth the summary of restricted stock units activity for the three months ended June 30, 2008:

	Shares (in thousands)	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in thousands)
Non-vested restricted stock units at March 31, 2008	7	$ -		

Awarded	-	$	-			
Released	(3)	$	-			
Forfeited	-	$	-			
Non-vested restricted stock units at June 30, 2008	4	$	-	1.0	$	47

Table of Contents

Note 8 — Segment and Geographic Information

Revenues from unaffiliated customers by geographic area, based on the customer's shipment locations were as follows (in thousands):

	Three months ended June 30,	
	2008	2007
United States	$ 8,696	$ 8,666
Japan	1,874	1,139
United Kingdom	1,943	2,255
Rest of the world	5,811	4,730
Total revenues	$ 18,324	$ 16,790

The Company's long lived assets by geographic area were as follows (in thousands):

	June 30, 2008	March 31, 2008
United States	$ 5,382	$ 4,907
United Kingdom	120	124
Rest of the world	269	254
	$ 5,771	$ 5,285

The Company identifies its operating segments based on how management views and evaluates the Company's operations, which is primarily based on geographic location. The Company has determined it operates in four business segments, the Americas, Europe (excluding the United Kingdom), the United Kingdom and Asia Pacific. The products and services sold by each segment are substantially the same and the Company evaluates performance and allocates resources primarily based on revenues and gross profit. Prior to the Company's annual report on Form 10-K for the fiscal year ended March 31, 2008, the Company's Europe (excluding the United Kingdom) and the United Kingdom segments were aggregated as a single business segment. Prior year information in the tables that follow have been restated to conform with the current year classification.

Revenues and gross profit for these segments were as follows (in thousands):

	Three months ended June 30,	
	2008	2007
Revenues:		
Americas	$ 10,533	$ 9,474
Europe (excluding the United Kingdom)	3,702	3,613
United Kingdom	1,943	2,255
Asia Pacific	2,146	1,448
Total	$ 18,324	$ 16,790
Gross Profit:		
Americas	$ 8,141	$ 7,950
Europe (excluding the United Kingdom)	2,681	2,464
United Kingdom	1,522	1,728

Asia Pacific	1,387	913
Total	$ 13,731	$ 13,055

Table of Contents

The Company's total assets by operating segment were as follows (in thousands):

	June 30, 2008	March 31, 2008
Americas	$ 42,868	$ 52,043
Europe (excluding the United Kingdom)	6,273	7,265
United Kingdom	13,048	13,024
	$ 62,189	$ 72,332

Item 2. Management's Discussion and Analysis of Financial Conditions and Results of Operations.

The following discussion and analysis of the financial condition and results of operations of the Company should be read in conjunction with the condensed consolidated financial statements and the related notes included elsewhere in this report, and with other factors described from time to time in our other filings with the Securities and Exchange Commission. This Quarterly Report on Form 10-Q contains forward-looking statements that involve risks and uncertainties. Actual results and the timing of events may differ materially from those contained in the forward-looking statements due to a number of factors, including those discussed in Part II, Item 1A "Risk Factors" in this Quarterly Report on Form 10-Q.

Overview

We develop, manufacture and market implantable and disposable medical devices used in the treatment of cerebral vascular diseases. Our products are used by interventional neuroradiologists, interventional neurologists and neurosurgeons to treat both cerebral aneurysms responsible for hemorrhagic stroke and intracranial atherosclerosis, which may lead to ischemic stroke. Hemorrhagic and ischemic stroke are both significant causes of death and disability worldwide. Our product lines consist of endovascular systems that enable a physician to gain access to the brain in a minimally invasive manner through the vessels of the arterial system. We believe our products provide a safe and reliable alternative to more invasive neurosurgical procedures for treating aneurysms. Our proprietary three-dimensional, embolic coils automatically and rapidly deploy within an aneurysm, forming a scaffold that conforms to a wide diversity of aneurysm shapes and sizes. We also supply accessories for use with our microcoils and other products for the treatment of neurovascular disease including microcatheters, guidewires and stents. We plan on growing our business by continuing to penetrate our existing hemorrhagic and ischemic stroke markets, bringing new products and technologies to interventional neuroradiologists, interventional neurologists and neurosurgeons, and by entering new geographic territories such as Asia where we commenced selling our products in Japan through our distribution partner, Goodman, Co., LTD ("Goodman"), in March 2006. Additionally, on July 31, 2007, we entered into an exclusive distribution agreement with Beijing Tianxinfu Medical Appliances Co., LTD ("TXF Medical") to market our products in China upon receiving regulatory approvals.

Our revenues are derived primarily from sales of our microcoils. We also sell stents, access products and accessories for use with our microcoils, which accounted for approximately 4% and 5% of our revenues in the first quarter of fiscal 2009 and 2008, respectively. Geographically, our revenues are generally from sales to customers in the Americas, Europe and Asia. Our products are shipped from our facilities in the United States, Switzerland, the United Kingdom, and a logistics facility in the Netherlands, to either hospitals or distributors. We invoice our customers upon shipment. In select hospitals, our products are held on consignment, and remain on site, free of charge until used.

We anticipate that our cost of goods sold will generally increase in absolute dollars during those quarters in which our sales increase or we incur additional manufacturing costs in anticipation of the commercial introduction of new products. Furthermore, our gross margin percentage may decrease in those quarters in which we initiate sales of new

products or product lines, or enter new geographic territories.

Table of Contents

Our product development efforts are primarily focused on expanding our current line of microcoils and broadening our product offerings in the hemorrhagic and ischemic stroke markets. In August 2004, we introduced our Cerecyte® microcoil product line and we have launched six new products in the last 24 months, including microcoils, stents, microcatheters and guidewires. During the first quarter of fiscal 2009, we began beta evaluation on two new products — the DeltaPaq™ microcoil system and Neuropath Guidecatheter. The DeltaPaq microcoil system is a new product line of our microcoil intended for endovascular embolization of intracranial aneurysms, other neurovascular abnormalities and are also intended for arterial and venous embolizations in the peripheral vasculature. The Neuropath Guidecatheter is used as a conduit for delivery of the microcatheter or other devices to the aneurysm. We intend to continue this product line expansion with the goal of continuing to increase our per-procedure revenue.

In June 2008, we obtained CE Mark authorization for our PHAROS™ Vitesse™ intracranial stent for commercial distribution in the European Union and all other countries recognizing the CE Mark. The PHAROS Vitesse is our second generation balloon-expandable stent for intracranial ischemic stenosis and wide-neck aneurysm treatment. We will begin selling the PHAROS Vitesse stent in the approved geographies through our direct sales and distribution networks in the second quarter of fiscal 2009. Additionally, we plan to pursue regulatory authorization in the United States ("U.S.") for our PHAROS Vitesse stent, which we believe represents a significant market opportunity for us. We have received U.S. Food and Drug Administration conditional approval of our PHAROS Vitesse Intracranial Stent Study for Ischemic Therapy (VISSIT) clinical trial designed to compare the clinical outcomes between patients treated with our stent and another medical therapy. We are in the process of initiating study sites in the United States, Europe and China.

We also intend to continue to expand our direct sales force in the North America and Europe as necessary and enter the Asian markets through distributors. In March 2006, we launched our sales and marketing efforts in Japan through our distribution partner, Goodman. In December 2007, we received regulatory approval to sell our stretch-resistant microcoils in Japan, and in July 2008, we received regulatory approval to sell our Cerecyte microcoils in Japan. We recorded product sales to Goodman of $1.9 million and $1.1 million in the first quarter of fiscal 2009 and 2008, respectively. We are also preparing to enter China and have selected TXF Medical to be our distributor in China. We will begin selling our products in China upon receiving regulatory approvals. However, the timing of these approvals are uncertain due to a pending review by the Chinese State Food and Drug Administration (SFDA) of drug and medical device approvals granted during the term of the former SFDA minister. We believe this review process along with more stringent approval procedures will delay review and approval of applications for new products. As a result, we did not recognize revenues from sales in China in the first quarter of fiscal 2009. We do not expect to recognize revenues from sales in China this fiscal year.

We currently anticipate that the broadening of our product line, the worldwide expansion of our direct sales force and our entry into the Asian market will be primarily funded with our currently available cash and cash expected to be generated from product sales.

We introduced our first proprietary, three-dimensional microcoil in May 2000. Our revenues have grown from $1.8 million in fiscal 2001 to $69.2 million in fiscal 2008. Our revenues were $18.3 million in the first quarter of fiscal 2009.

Since inception, we have been unprofitable. We have incurred net losses of $8.3 million in fiscal 2006, $5.5 million in fiscal 2007, $16.3 million in fiscal 2008 and $6.6 million in the first quarter of fiscal 2009. As of June 30, 2008, we had cash and cash equivalents of $16.9 million. We believe that our current cash position and the cash expected to be generated from product sales will be sufficient to meet our working capital and capital expenditure requirements for at least the next twelve months. There is no assurance that we will be profitable in the foreseeable future as we expand our research and development, manufacturing, and sales activities and expand geographically. As of June 30, 2008,

we had an accumulated deficit of $78.0 million.

Table of Contents

Results of Operations

The following table sets forth the results of our operations, expressed as percentages of revenues, for the three months ended June 30, 2008 and 2007:

	Three months ended June 30,	
	2008	2007
Consolidated Statements of Operations Data:		
Revenues	100%	100%
Cost of goods sold	25%	22%
Gross profit	75%	78%
Operating expenses:		
Research and development	17%	12%
Sales and marketing	44%	39%
General and administrative	52%	37%
Total operating expenses	113%	88%
Loss from operations	(38%)	(10%)
Interest income	1%	2%
Interest expense	0%	0%
Other income (expense), net	0%	1%
Loss before income taxes	(37%)	(7%)
Provision (benefit) for income taxes	(1%)	1%
Net loss	(36%)	(8%)
Accretion of redeemable convertible preferred stock to		

Three Months Ended June 30, 2008 and 2007

Revenues

	Three months ended June 30,		Change	
	2008	2007	$	%
	(Dollars in thousands)			
Americas	$ 10,533	$ 9,474	$ 1,059	11%
Europe (excluding the United Kingdom)	3,702	3,613	89	2%
United Kingdom	1,943	2,255	(312)	(14%)
Asia Pacific	2,146	1,448	698	48%
Total Revenues	$ 18,324	$ 16,790	$ 1,534	9%

Our revenues are derived primarily from sales of our microcoils used in the treatment of cerebral vascular diseases. The overall increase in revenues in the first quarter of fiscal 2009 compared to the first quarter of fiscal 2008 was primarily due to an increase in the number of microcoil products sold during this period. Factors driving the increase included growth in the overall market for embolic coils, an increase in our share of both the domestic and foreign markets in which we participate, expansion of our direct and distributor sales force and the introduction of new products.

21

Table of Contents

Revenues from embolic coils increased 11% to $17.5 million for the first quarter of fiscal 2009 as compared to the first quarter of fiscal 2008 primarily due to the increased market penetration of the Cashmere™ microcoil system launched in the third quarter of fiscal 2008 and an increase in distributor sales primarily in Japan and Latin America. Revenues from Asia Pacific increased to $2.1 million in the first quarter of fiscal 2009 and included product sales to our distributor in Japan of $1.9 million, compared with revenues of $1.4 million in the first quarter of fiscal 2008 which included sales of $1.1 million to our distributor in Japan. In December 2007, we received regulatory approval to sell our stretch-resistant microcoils in Japan which had a favorable impact on product sales to our distributor in Japan in the quarter. Revenues from Latin America increased to $1.3 million in the first quarter of fiscal 2009 compared with revenues of $374,000 in the first quarter of fiscal 2008 primarily due to the recognition of approximately $0.7 million in the quarter resulting from a change in our revenue recognition policy for sales made to Latin American distributors from a cash collection basis to upon shipment basis (see Note 2 in Notes to Condensed Consolidated Financial Statements) and an overall increase in product sales to our distributors in the region. Procedure volume in the United Kingdom slowed in the first quarter of fiscal 2009, resulting in a decline in revenue to $1.9 million compared with revenues of $2.3 million in the first quarter of fiscal 2008. Revenues from our non-embolic and accessories products were $0.8 million in the first quarter of fiscal 2009 compared with revenues of $0.9 million in the first quarter of fiscal 2008. We expect our embolic and non-embolic sales to increase in the future as a result of market growth, continued market penetration of products released during the past two years and our planned launch of the next-generation microcoil system and an occlusion balloon catheter family. Products introduced in the past 24 months comprised 22% of our revenues in the first quarter of fiscal 2009.

In July 2008, we received regulatory approval to sell our Cerecyte microcoils in Japan, and we will begin shipping these products to Goodman in the second quarter of fiscal 2009. We will also begin selling our products in China upon receiving regulatory approvals. However, the timing of product approvals in China will be delayed due to a pending review by the SFDA of drug and medical device approvals granted during the term of the former SFDA minister. We currently believe this review process along with more stringent approval procedures will delay review and approval of applications for new products. As a result, we did not recognize revenues from sales in China in the first quarter of fiscal 2009. We do not expect to recognize revenues from sales in China this fiscal year.

Gross Profit

	Three months ended June 30,		Change	
	2008	2007	$	%
	(Dollars in thousands)			
Cost of goods sold	$ 4,593	$ 3,735	$ 858	23%
Gross profit	$ 13,731	$ 13,055	$ 676	5%

Cost of goods sold consists primarily of materials, direct labor, depreciation, overhead costs associated with manufacturing, impairments of inventory, warranty expenses, amortization of intangible assets that were acquired by us as part of the acquisition of VasCon, LLC (“VasCon”), amortization of capitalized license technology associated with our PHAROS stent product and royalties related to certain access device products. The increase in cost of goods sold during the first quarter of fiscal 2009 as compared to the first quarter of fiscal 2008 was primarily related to the increase in sales of our products.

Gross margin was 75% in the first quarter of fiscal 2009 and 78% in the first quarter of fiscal 2008. The decrease was primarily due to higher sales to distributors at lower margins primarily in Japan and Latin America. We expect our gross margin to fluctuate in future periods based on the mix of our product sales and the level of distributor sales.

22

Table of Contents

Operating Expenses

Research and Development

	Three months ended June 30,		Change	
	2008	2007	$	%
	(Dollars in thousands)			
Research and development	$ 2,973	$ 1,965	$ 1,008	51%

Research and development expenses consist primarily of costs associated with the design, development, and testing of new products. Such costs are expensed as they are incurred and include salaries and related personnel costs, fees paid to outside consultants, and other direct and indirect costs related to research and product development. Research and development expenses increased in the first quarter of fiscal 2009 compared to the first quarter of fiscal 2008 primarily due to an increase of $498,000 related to increased headcount and an increase of $321,000 related to product testing, outside services and supplies.

Sales and Marketing

	Three months ended June 30,		Change	
	2008	2007	$	%
	(Dollars in thousands)			
Sales and marketing	$ 8,118	$ 6,510	$ 1,608	25%

Sales and marketing expenses consist primarily of compensation costs of our direct sales force and marketing personnel, as well as overhead costs related to these activities. Also included are costs associated with promotional literature and videos, trade show participation, and education and training of physicians. Sales and marketing expenses increased in the first quarter of fiscal 2009 compared to the first quarter of fiscal 2008 primarily due to an increase of $0.6 million in travel, recruiting and personnel costs due to an increase in sales and marketing personnel in the North America, Europe and Asia, an increase of $420,000 in sales incentives resulting from the higher level of sales and changes in the sales compensation structure, an increase of $197,000 in trade show, meeting and conference costs, as well as an increase of $196,000 in stock-based compensation expense.

General and Administrative

	Three months ended June 30,		Change	
	2008	2007	$	%
	(Dollars in thousands)			
General and administrative	$ 9,562	$ 6,276	$ 3,286	52%

General and administrative expenses consist primarily of compensation and related costs for finance, human resources, regulatory, insurance, and professional services. Professional services are principally comprised of outside legal, audit and Sarbanes Oxley compliance. General and administrative expenses increased in the first quarter of fiscal 2009 compared to the first quarter of fiscal 2008 primarily due to the accrued costs of approximately $1.7 million in connection with the tentative settlement of patent litigation with Boston Scientific, an increase of $0.7 million related to higher finance and administrative personnel costs due to increased headcount, an increase of

$335,000 in legal fees primarily related to professional fees for the services of attorneys and third-party accountants in connection with the United States Department of Justice monitorship, which has now concluded and an increase of $239,000 in stock-based compensation expense.

Table of Contents

Other Income, Net

Other income, net consists primarily of interest and investment income and foreign currency gains and losses. Total other income, net decreased in the first quarter of fiscal 2009 compared to the first quarter of fiscal 2008 primarily due to a decrease in interest income resulting from lower average cash and cash equivalent balances earning interest.

	Three months ended June 30,		Change	
	2008	2007	$	%
	(Dollars in thousands)			
Interest income	$ 110	$ 360	$ (250)	(69%)
Interest expense	(4)	-	(4)	0%
Other income (expense), net	(2)	78	(80)	(103%)
Total other income, net	$ 104	$ 438	$ (334)	(76%)

Income Taxes

We have incurred net operating losses for both federal and state purposes since inception and, as a result, we have paid no federal or state income tax. For the three months ended June 30, 2008, we recorded an income tax benefit of approximately $216,000. The income tax benefit for the three months ended June 30, 2008 includes income tax benefit of $150,000 related to net operating losses for our Swiss subsidiary, and a non-current tax benefit of approximately $66,000 for the tax effect of the amortization related to the identifiable intangible assets acquired in the Neurologic transaction which are amortized for tax purposes and the tax benefit from net operating losses for our United Kingdom subsidiary.

As of March 31, 2008, we had federal, state and foreign net operating loss carryforwards (“NOLs”) that are available to reduce future taxable income of approximately $42.5 million, $27.6 million and $1.6 million, respectively. The federal NOLs will expire at various dates beginning in 2012, state NOLs will expire beginning in 2013 and the foreign NOLs will expire beginning in 2013. We also have federal and state tax research and development credit carryforwards of approximately $1.2 million and $1.1 million, respectively. The federal tax credit carryforwards will expire beginning in 2012. The state tax credit carryforwards can be carried forward indefinitely. Due to the uncertainty of our ability to generate sufficient taxable income to realize the carryforwards prior to their expiration, we have recorded a valuation allowance at June 30, 2008 to offset our federal and state deferred tax assets.

Since the implementation of FIN 48, we have recognized a $232,000 increase in our unrecognized tax benefits. We do not expect our unrecognized tax benefits to change significantly over the next twelve months. At June 30, 2008, we had no accrued interest or penalties related to tax contingencies.

Liquidity and Capital Resources

	Three months ended June 30,	
	2008	2007
	(in thousands)	
Cash flow activities:		
Net cash used in operating activities	$ (4,291)	$ (3,753)
Net cash used in investing activities	$ (4,675)	$ (2,719)

Net cash provided by financing activities	$ 302	$ 522

Table of Contents

Since our inception, we have funded our operations primarily through issuances of stock and related warrants.

As of June 30, 2008, we had cash and cash equivalents of $16.9 million, compared to $25.5 million at March 31, 2008. We believe that our current cash position and the cash expected to be generated from product sales will be sufficient to meet our working capital and capital expenditure requirements for at least the next twelve months.

Net cash used in operating activities was $4.3 million during the first quarter of fiscal 2009 compared to $3.8 million during the first quarter of fiscal 2008. Net cash used in operating activities during the first quarter of fiscal 2009 resulted primarily from operating losses, an increase in inventory due to an increase in the number of consignment locations, an increase in the number of units in existing consignment locations due to new products released and the buildup of finished goods inventory in anticipation of future sales upon regulatory approvals in Japan, a decrease in accrued payroll and related expenses attributable to the payment of fiscal 2008 employee cash bonuses and a decrease in other non-current liabilities primarily due to a reclass of an accrued milestone payment from long-term to short-term. These factors were partially offset by a decrease in accounts receivable resulting from lower revenues during the quarter, a decrease in prepaid expense and other assets, an increase in accounts payable due to timing of payments made to our vendors, an increase in accrued liabilities due to a reclass of an accrued milestone payment from long-term to short-term, and non-cash items such as unremitted issuance of stock for tentative settlement of patent litigation, stock-based compensation expense primarily due to SFAS 123R, depreciation and amortization, deferred tax benefit and provision for excess and obsolete inventories.

Net cash used in operating activities during the first quarter of fiscal 2008 resulted primarily from operating losses, an increase in accounts receivable primarily due to an increase in the number of microcoil products sold, an increase in inventory due to the buildup of finished goods inventory in anticipation of future sales and an increase in the number of consignment locations, an increase in prepaid expenses and other current assets primarily related to the payment of directors and officers insurance premiums, a decrease in accrued payroll and related expenses attributable to the payment of fiscal 2007 employee cash bonuses. These factors were partially offset by an increase in accounts payable due to timing of payments made to our vendors, an increase in accrued liabilities due to accrued professional fees associated with legal fees and Sarbanes Oxley compliance and higher VAT payables, and non-cash items such as stock-based compensation expense primarily due to SFAS 123R, depreciation and amortization, and provision for excess and obsolete inventories.

Net cash used in investing activities was $4.7 million during the first quarter of fiscal 2009 compared to $2.7 million during the first quarter of fiscal 2008. Net cash used in investing activities during the first quarter of fiscal 2009 was related to the earn-out payment associated with the purchase of Neurologic and VasCon and the purchase of capital equipment.

Net cash used in investing activities during the first quarter of fiscal 2008 was primarily related to the earn-out payment associated with the purchase of Neurologic and the purchase of capital equipment.

Net cash provided by financing activities was $302,000 during the first quarter of fiscal 2009 compared to $522,000 during the first quarter of fiscal 2008. Net cash provided by financing activities during the first quarter of fiscal 2009 and 2008 consisted of proceeds from the exercise of stock options.

To the extent that existing cash and cash generated from operations are insufficient to fund our future activities, we may need to raise additional funds through public or private equity or debt financing. Although we are currently not a party to any definitive agreement with respect to potential investments in, or acquisitions of, complementary businesses, services or technologies, we may enter into such agreements in the future, which could require us to seek additional funds through public or private equity or debt financing. Additional funds may not be available on terms

favorable to us or at all.

Table of Contents

Critical Accounting Policies and Estimates

We prepare our consolidated financial statements in accordance with accounting principles generally accepted in the United States (GAAP). In doing so, we have to make estimates and assumptions that affect our reported amounts of assets, liabilities, revenues and expenses, as well as related disclosure of contingent assets and liabilities. In many cases, we could reasonably have used different accounting policies and estimates. In some cases, changes in the accounting estimates are reasonably likely to occur from period to period. Accordingly, actual results could differ materially from our estimates. To the extent that there are material differences between these estimates and actual results, our financial condition or results of operations will be affected. We base our estimates on past experience and other assumptions that we believe are reasonable under the circumstances, and we evaluate these estimates on an ongoing basis. We refer to accounting estimates of this type as critical accounting policies and estimates, which we discuss below. Our management has reviewed our critical accounting policies and estimates with our accounting advisors, audit committee and board of directors.

Our significant accounting policies are fully described in Note 2 to our Consolidated Financial Statements included in our annual report filed on Form 10-K for the fiscal year ended March 31, 2008, that was filed with the SEC on June 12, 2008.

Recent Accounting Pronouncements

In December 2007, the FASB issued SFAS 141R (revised 2007), “Business Combinations,” which replaces SFAS 141. SFAS 141R requires the acquiring entity in a business combination to recognize at full fair value all the assets acquired and liabilities assumed in the transaction; establishes the acquisition-date fair value as the measurement objective for all assets acquired and liabilities assumed; and requires the acquirer to disclose information needed to evaluate and understand the nature and financial effect of the business combination. SFAS 141R is effective for fiscal years beginning after December 15, 2008 and is to be applied prospectively to business combinations completed on or after the date of adoption. We are currently evaluating the impact of adopting SFAS 141R on our consolidated financial position, results of operations or cash flows.

In February 2008, the FASB issued Financial Standard Position (“FSP”) SFAS 157-2, “Effective Date for FASB Statement No. 157.” This FSP permits the delayed application of SFAS 157 for all nonrecurring fair value measurements of non-financial assets and non-financial liabilities until fiscal years beginning after November 15, 2008. We are currently evaluating the impact of adopting the provisions of SFAS 157 for non-financial assets and liabilities that are recognized or disclosed on a non-recurring basis.

In April 2008, the FASB issued FASB Staff Position (“FSP”) SFAS No. 142-3, “Determination of the Useful Life of Intangible Assets” (“FSP SFAS 142-3”). FSP SFAS 142-3 amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under SFAS 142, “Goodwill and Other Intangible Assets.” The intent of this FSP is to improve the consistency between the useful life of a recognized intangible asset and the period of expected cash flows used to measure the fair value of the asset under SFAS 141 (revised 2007), “Business Combinations” and other U.S. generally accepted accounting principles (GAAP). FSP SFAS 142-3 is effective for us on April 1, 2009. We are currently evaluating the impact of adopting FSP SFAS 142-3 on our consolidated financial position, results of operations or cash flows.

In May 2008, the FASB issued SFAS No. 162, “The Hierarchy of Generally Accepted Accounting Principles” (“SFAS 162”), which becomes effective 60 days following the SEC’s approval of the Public Company Accounting Oversight Board (“PCAOB”) amendments to US Auditing Standards (“AU”) Section 411, “The Meaning of Present Fairly

in Conformity With Generally Accepted Accounting Principles." SFAS 162 identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with US GAAP. This standard is not expected to have an impact on our consolidated financial position, results of operations or cash flow.

Table of Contents

Contractual Obligations

We have obligations under non-cancelable operating leases with various expiration dates through 2013 and purchase commitments for inventory, capital equipment and operating expenses, such as materials for research and development and consulting.

As of June 30, 2008, our contractual commitments were as follows:

		Payments Due by Period			
Contractual obligations:	Total	Less than 1 year	1-3 years	3-5 years	Beyond 5 years
Non-cancelable operating lease obligations	$ 7,228	$ 1,067	$ 3,046	$ 1,287	$ 1,828
Purchase obligations	4,089	4,089	-	-	-
Minimum milestone payments to The Cleveland Clinic	1,500	1,500	-	-	-
Milestone payment to Genesis	150	150	-	-	-
Total	$ 12,967	$ 6,806	$ 3,046	$ 1,287	$ 1,828

We paid the first year earn-out amount of $378,000 associated with the purchase of VasCon in April 2008. The future earn-out payments will be an amount not to exceed $10.0 million based on the sales and manufacturing performance of Micrus Design Technology, Inc. as set forth in the asset purchase agreement.

We are required to pay The Cleveland Clinic Foundation up to $5.0 million in payments upon the achievement of certain milestones set forth in the stock purchase agreement, with minimum milestone payments of at least $2.0 million to The Cleveland Clinic Foundation upon the earlier of achieving the milestones or October 26, 2010. The first milestone payment in the amount of $500,000 was paid in March 2008.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Foreign Currency Market Risks. Historically, we have been exposed to risks from fluctuations in currency exchange rates due to intercompany loans made to Micrus SA, our Swiss subsidiary, in 2001 in connection with its incorporation. These loans are denominated in Swiss francs and will fluctuate in value against the U.S. dollar, causing us to recognize foreign exchange gains and losses. The functional currency of our Swiss subsidiary is the Swiss franc. The functional currency of our UK subsidiary is the pound sterling. In Europe, our revenues are denominated in Swiss francs, euros, pounds sterling and other currencies. Accordingly, we are exposed to market risk related to changes between the Swiss franc and these other currencies. If the Swiss franc appreciates against the currencies in which our receivables are denominated, we will recognize foreign currency losses. For the preparation of our consolidated financial statements, the financial results of our Swiss subsidiary are translated into U.S. dollars based on average exchange rates during the applicable period. A hypothetical 10% decline in the value of the Swiss franc versus the U.S. dollar would cause us to recognize a loss of $199,000 related to our loan with Micrus SA and a $67,000 decrease in our comprehensive loss from our investment in Micrus SA as of June 30, 2008. A hypothetical 10% decline in the value of the pound sterling versus the U.S. dollar would cause us to recognize a $278,000 decrease in our comprehensive loss from our investment in Micrus UK as of June 30, 2008. A hypothetical 10% decline in the value of the Euro versus the Swiss franc would cause us to recognize a loss of $230,000 based on our foreign denominated receivables as of June 30, 2008.

In the first quarter of fiscal 2009, approximately 33% of our revenues were denominated in currencies other than the U.S. dollar. In future periods, we believe a greater portion of our revenues could be denominated in currencies other

than the U.S. dollar, thereby increasing our exposure to exchange rate gains and losses on non-U.S. currency transactions. We do not currently enter into forward exchange contracts to hedge exposure denominated in foreign currencies or any other derivative financial instruments for trading or speculative purposes. In the future, if we believe our currency exposure merits, we may consider entering into transactions to help mitigate that risk.

Interest Rate Market Risk. Our cash is invested in bank deposits and money market funds denominated in U.S. dollars. The carrying value of these cash equivalents approximates fair market value. Our investments in marketable securities are subject to interest rate risk, which is the risk that our financial condition and results of operations could be adversely affected due to movements in interest rates.

At June 30, 2008, our cash and cash equivalent balance was $16.9 million. Based on our annualized average interest rate, a 10% decrease in the interest rate on such balances would result in a reduction in interest income of approximately $40,000 on an annual basis.

Table of Contents

Item 4. Controls and Procedures

(1) Disclosure controls and procedures

Our management, with the participation of our Chairman of the Board of Directors and Chief Executive Officer, John T. Kilcoyne, and our Chief Financial Officer, Gordon T. Sangster, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act). Based on their evaluation, they concluded that our disclosure controls and procedures as of June 30, 2008 were effective in providing reasonable assurance that material information relating to our company is made known to management on a timely basis during the period when our periodic reports are being prepared.

(2) Changes in internal controls

There were no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended June 30, 2008 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Part II — OTHER INFORMATION

Item 1. Legal Proceedings.

FCPA Investigation

See the risk factor regarding international operations on page 34 below for a discussion of the FCPA investigation we carried out in 2004 and our resulting agreement with the Department of Justice.

The monitor filed his final report with the DOJ in May 2008, and in July 2008, the DOJ confirmed that the monitorship had concluded. We have reaffirmed our commitment to take all reasonable steps to ensure that we remain in compliance with the FCPA.

Patent Litigation

See the risk factor regarding patent litigation below on page 30 for a detailed discussion of our patent litigation with Boston Scientific Corporation.

A hearing on claim construction was held in June 2007. In March 2008, the Court issued an order construing certain claim terms of patents that were asserted by Boston Scientific against Micrus or asserted by Micrus against Boston Scientific. On April 23, 2008, the district court entered a scheduling order on future events in this action, including the close of all discovery on January 26, 2009. A trial date has not been set by the district court.

We are is in the process of negotiating a settlement with Boston Scientific and the U.C. Regents (which licensed some of the patents-in-suit to Boston Scientific but is not a party to the lawsuit). These negotiations currently contemplate the issuance by us of approximately $1.7 million in stock that would accompany patent cross-licenses between us and Boston Scientific. The accrued cost of approximately $1.7 million in connection with the tentative settlement of patent litigation with Boston Scientific was recorded as general and administrative expense in the first quarter of fiscal 2009. This issuance of stock, together with a payment of approximately $1.0 million by Boston Scientific to the U.C. Regents, would be made to the U.C. Regents to satisfy the Regents' claim related to these patents. However, there can be no assurance that a settlement agreement will be finalized on these or any terms.

28

Table of Contents

Item 1A. Risk Factors.

Certain Factors that May Affect Our Business and Future Results

Some of the information included herein contains forward-looking statements as defined in Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Such forward-looking statements are based on the beliefs of, estimates made by and information currently available to our management and are subject to certain risks, uncertainties and assumptions. Any statements contained herein (including, without limitation, statements to the effect that the Company, we, or management "may," "will," "expects," "anticipates," "estimates," "continues," "plans," "believes," or "projects," or statements concerning "potential" or "opportun any variations thereof, comparable terminology or the negative thereof) that are not statements of historical fact should be construed as forward-looking statements. Our actual results may vary materially from those expected in these forward-looking statements. The realization of such forward-looking statements may be impaired by risks including, but not limited to the following:

Our future success is dependent on the continued growth in embolic coiling procedures and our ability to convince a concentrated customer base of neurointerventionalists to use our products as an alternative to other available products.

Our future success and revenue growth are significantly dependent upon an increase in the use of embolic coiling as a procedure to treat cerebral aneurysms. If the number of embolic coiling procedures does not increase or if a new procedure that does not employ our products becomes a more acceptable alternative among neurointerventionalists, our business would be seriously harmed.

The number of interventional neuroradiologists and neurosurgeons trained to conduct embolic coiling procedures is relatively small, both in the United States and abroad. There are currently approximately 300 neurointerventionalists in the United States who perform embolic coiling procedures. We believe less than one-third of these physicians perform a substantial majority of the total number of embolic coiling procedures per year. For the first quarter of fiscal 2009, a substantial portion of our product sales were to approximately 148 hospitals in the United States. The growth in the number of interventional neuroradiologists and neurosurgeons in the United States is constrained by the lengthy training programs required to educate these physicians. Accordingly, our revenue growth will be primarily dependent on our ability to increase sales of our products to our existing customers and to increase sales of products to trained neurointerventionalists that currently use products offered by our competitors. We believe that neurointerventionalists who do not currently use our products will not widely adopt our products unless they determine, based on experience, clinical data and published peer reviewed journal articles, that our products provide benefits or an attractive alternative to the clipping of aneurysms or the use of competitors' products. We believe neurointerventionalists base their decision to use an alternative procedure or product on the following criteria, among others:

- extent of clinical evidence supporting patient benefits;
- their level of experience with the alternative product;
- perceived liability risks generally associated with the use of new products and procedures;
- availability of reimbursement within healthcare payment systems; and
- costs associated with the purchase of new products and equipment.

In addition, we believe that recommendations and support of our products by influential physicians are essential for market acceptance and adoption. If we do not receive continued support from such influential physicians, neurointerventionalists and hospitals may not use our products. In such circumstances, we may not achieve expected revenue levels and our business will suffer.

Table of Contents

We are currently involved in a patent litigation action involving Boston Scientific and, if we do not prevail in this action, we could be liable for past damages and be prevented from making, using, selling, offering to sell, importing into the United States or exporting from the United States, our microcoils, our primary product line.

In September 2004, Boston Scientific, filed a patent infringement suit in the United States District Court for the Northern District of California, alleging that our embolic coil products infringe two patents (United States Patent Nos. 5,895,385 (the "'385 Patent") and 6,010,498 (the "'498 Patent")) owned by the Regents of the University of California (the "Regents") and exclusively licensed to Boston Scientific and that this infringement is willful. Sales of our embolic coil products currently represent approximately 94% of our revenues. Boston Scientific is a large, publicly-traded corporation with significantly greater financial resources than us.

In November 2004, we answered Boston Scientific's complaint and counterclaimed, alleging that Boston Scientific's embolic coil products, and their use, infringe three of our patents. In addition, we alleged that Boston Scientific has violated United States antitrust laws, and has violated certain California state laws by committing unfair business practices, disparaging our products, and interfering with our prospective economic advantage. Each party seeks an injunction preventing the making, using, selling, offering to sell, importing into the United States or exporting from the United States, of the other's embolic coil products in the United States, damages for past infringement, which may be trebled, and payment of its legal fees and costs. In addition, each party seeks a declaration that the patents of the other are invalid and not infringed and has alleged that certain of the asserted patents of the other are unenforceable due to inequitable conduct.

In January 2005, Boston Scientific filed a motion to dismiss our claims for disparagement, interference with prospective economic advantage and unfair business practices. In June 2008, the court issued an order dismissing these claims without prejudice and granting us leave to amend our counterclaims. We filed amended counterclaims in July 2008. Boston Scientific has not responded to our amended counterclaims.

In November 2006, we withdrew one of our three asserted patents from the litigation to pursue a reissue application filed with the United States Patent and Trademark Office ("USPTO").

A hearing on claim construction was held in June 2007. In March 2008, the Court issued an order construing certain claim terms of patents that were asserted by Boston Scientific against Micrus or asserted by Micrus against Boston Scientific. On April 23, 2008, the district court entered a scheduling order on future events in this action, including the close of all discovery on January 26, 2009. A trial date has not been set by the district court.

Boston Scientific has also been a party in two other lawsuits against Cordis and Micro Therapeutics, Inc./ev3, Inc./Dendron GmbH (collectively "MTI") in which the two Boston Scientific patents asserted against us are or were also at issue. An outcome of either of these lawsuits adverse to Cordis or MTI, and related to the same patent claims Boston Scientific asserts against us, could have an adverse impact on certain of our defenses in our litigation with Boston Scientific.

According to court records, the Regents, Boston Scientific and MTI entered into a settlement agreement on March 21, 2008, and on April 4, 2008 the Regents, Boston Scientific and MTI dismissed the action, including all claims and counter-claims, with prejudice.

On January 18, 2008, in the Cordis case, the district court granted Boston Scientific's motion for summary judgment that Cordis' TRUFILL Detachable Coil System infringed claim 7 of the '385 Patent under the doctrine of equivalents. On January 25, 2008, the district court granted Boston Scientific's motion for summary judgment against Cordis that claims 10 and 35 of the '385 patent, and claims 1, 3, 7, 9, and 10 of the '498 patent, are not invalid for having been

on-sale or in public use before the statutory bar period. On March 21, 2008, the district court granted-in-part Boston Scientific's motion for summary judgment that the '385 patent and '498 patent are not unenforceable for inequitable conduct. The district court also denied-in-part Boston Scientific's motion on the ground that triable issues of fact remained concerning the patent applicants' representations to the patent examiner during the application process. The district court's determinations on the validity and enforceability of the '385 and '498 patents are important because Boston Scientific is asserting these same patents against us in our lawsuit and we are alleging that these patents are invalid and unenforceable.

In October 2004, Cordis requested ex parte reexamination of certain claims in Boston Scientific's '385 and '498 patents. In April 2007, the USPTO issued a Notice of Intent to Issue Ex Parte Reexamination Certificate for the '498 patent, apparently confirming all of the claims of that patent. In December 2006, the USPTO issued a Notice of Allowance for the '385 patent in which it apparently confirmed the patentability of the claims in that patent.

Table of Contents

Patent lawsuits involve complex legal and factual issues which can take a number of years and a great deal of expense and management attention to resolve. We may also be subject to negative publicity due to the litigation. In the event it is determined that we infringe patent claims asserted by Boston Scientific and that those claims are not invalid and not unenforceable we may, among other things, be required to do one or more of the following:

- pay damages, including up to treble damages and Boston Scientific's attorney's fees and costs, which may be substantial;

- cease, because of an injunction, the making, using, selling, offering to sell, importing into the United States or exporting from the United States of our embolic coil products, which currently represent virtually all of our revenues, found to infringe the patent claims asserted by Boston Scientific;

- expend significant resources to redesign our technology so that it does not infringe the patent claims asserted by Boston Scientific, which may not be possible;

- discontinue manufacturing or other processes that incorporate technology that infringes the patent claims asserted by Boston Scientific;

- become subject to a compulsory license order under which we would be required to pay Boston Scientific a royalty on future sales of our products; and/or

- obtain a license from Boston Scientific to use the relevant patents, which may not be available to us on acceptable terms, or at all.

If our embolic coil products were found to infringe, any development or acquisition of products or technologies that do not infringe the patent claims asserted by Boston Scientific could require the expenditure of substantial time and other resources and could have a material adverse effect on our business and financial results. If we were required to but could not obtain a license under the patent claims asserted by Boston Scientific, we would likely be prevented from commercializing or further commercializing the relevant products. We believe that it is unlikely that we would be able to obtain a license under the patent claims being asserted by Boston Scientific. If we need to redesign our products to avoid the patent claims being asserted by Boston Scientific, we may suffer significant regulatory delays associated with conducting additional studies or submitting technical, manufacturing or other information related to the redesigned product and, ultimately, in obtaining approval.

As a result of Boston Scientific's answer to our counterclaim that Boston Scientific infringes our two remaining patents-in-suit, the validity of those patents is now at issue in the lawsuit. The court could find that those patents are invalid, which would prevent us from asserting those patents against third parties.

We are is in the process of negotiating a settlement with Boston Scientific and the U.C. Regents (which licensed some of the patents-in-suit to Boston Scientific but is not a party to the lawsuit). These negotiations currently contemplate the issuance by us of approximately $1.7 million in stock that would accompany patent cross-licenses between us and Boston Scientific. The accrued cost of approximately $1.7 million in connection with the tentative settlement of patent litigation with Boston Scientific was recorded as general and administrative expense in the first quarter of fiscal 2009. This issuance of stock, together with a payment of approximately $1.0 million by Boston Scientific to the U.C. Regents, would be made to the U.C. Regents to satisfy the Regents' claim related to these patents. However, there can be no assurance that a settlement agreement will be finalized on these or any terms.

An unfavorable outcome for us in this patent litigation would significantly harm our business and may cause us to materially change our business model. In addition, costs of defense and any damages resulting from the litigation may materially adversely affect our business and financial results. The litigation may also harm our relationships with existing customers and subject us to negative publicity, each of which could harm our business and financial results.

Table of Contents

Our industry is experiencing increased scrutiny by governmental authorities, which has led to increased compliance costs and potentially more rigorous regulation

The medical device industry is subject to rigorous regulation by the FDA and numerous other federal, state and foreign governmental authorities. These authorities have been increasing their scrutiny of certain activities of medical device companies, including their conduct of clinical trials, their handling of conflicts of interests and financial arrangements with health care providers and consultants, and their product promotional practices. We anticipate that government authorities will continue to scrutinize our industry closely and we may be subject to more rigorous regulation by governmental authorities in the future. This increased government scrutiny has lead us to incur increased costs on compliance, human resources costs and the diversion of management and employee focus and we anticipate that such costs will continue to increase. Though we have adopted a number of compliance procedures in response to the increased scrutiny, we cannot assure you that our activities will not be subject to inquiry or greater action or oversight by governmental authorities or that we will be able to comply with any new regulations. Any failure by us to adopt appropriate compliance procedures and ensure that our employees and agents comply with applicable laws and regulations could result in substantial penalties and/or restrictions in our business activities and the sales of our products.

We have a limited operating history, have incurred significant operating losses since inception, and expect to continue to incur losses, and we cannot assure you that we will achieve profitability.

We were incorporated in the State of Delaware in 1996, and began commercial sales of our microcoil products in 2000. We have yet to demonstrate that we can generate sufficient sales of our products to become profitable. The extent of our future operating losses and the timing of profitability are uncertain, and we may never achieve profitability. We have incurred significant net losses since our inception, including losses of approximately $16.3 million, $5.5 million and $8.3 million for the fiscal years ended March 31, 2008, 2007 and 2006, respectively. We incurred net losses of $6.6 million and $1.4 million in the first quarter of fiscal 2009 and 2008, respectively. As of June 30, 2008, we had an accumulated deficit of $78.0 million. It is possible that we will never generate sufficient revenues from product sales to achieve profitability. Even if we do achieve significant revenues from our product sales, we expect our operating expenses to increase as we, among other things:

- grow our internal and third-party sales and marketing forces to expand the sales of our products in the United States and internationally;
- increase our research and development efforts to improve upon our existing products and develop new products;
- perform clinical research and trials on our existing products and product candidates;
- expand our regulatory resources in order to obtain governmental approvals for our existing product enhancements and new products;
- acquire and/or license new technologies; and
- expand manufacturing.

As a result of these activities, we may never become profitable. Even if we do achieve profitability, we may not be able to sustain or increase profitability on an ongoing basis.

Our quarterly operating and financial results and our gross margins are likely to fluctuate significantly in future periods.

Our quarterly operating and financial results are difficult to predict and may fluctuate significantly from period to period. The level of our revenues, gross margins and results of operations at any given time will be based primarily on the following factors:

- neurointerventionalist and patient acceptance of our products;
- changes in the number of embolic coiling procedures performed to treat cerebral aneurysms;
- the seasonality of our product sales;
- the mix of our products sold;
- stocking patterns for distributors;
- the development of new procedures to treat cerebral aneurysms;

Table of Contents

- results of clinical research and trials on our existing products and products in development;
- demand for, and pricing of, our products;
- levels of third-party reimbursement for our products;
- timing of new product offerings, acquisitions, licenses or other significant events involving us or our competitors;
- increases in the costs of manufacturing and selling our products;
- the amount and timing of our operating expenses;
- litigation expenses;
- fluctuations in foreign currency exchange rates;
- regulatory approvals and legislative changes affecting the products we may offer or those of our competitors;
- the effect of competing technological and market developments;
- changes in our ability to obtain and maintain FDA and other domestic and foreign regulatory approval or clearance for our products;
- inventory adjustments we may have to make in any quarter;
- interruption in the manufacturing or distribution of our products;
- our ability to maintain and expand our sales force and operational personnel;
- the ability of our suppliers to timely provide us with an adequate supply of materials and components; and
- amount and timing of capital expenditures and other costs relating to any potential expansion of our operations.

Many of the products we may seek to develop and introduce in the future will require FDA approval or clearance and will be required to meet similar regulatory requirements in other countries where we seek to market our products, without which we cannot begin to commercialize them. Forecasting the timing of sales of our products is difficult due to the delay inherent in seeking FDA and other clearance or approval, or the failure to obtain such clearance or approval. In addition, we will be increasing our operating expenses as we build our commercial capabilities. Accordingly, we may experience significant, unanticipated quarterly losses. Because of these factors, our operating results in one or more future quarters may fail to meet the expectations of securities analysts or investors, which could cause our stock price to decline significantly.

We may not be able to develop new products or product enhancements that will be accepted by the market.

Our success will depend in part on our ability to develop and introduce new products and enhancements to our existing products. We cannot assure you that we will be able to successfully develop or market new products or that any of our future products will be accepted by the neurointerventionalists who use our products or the payors who

reimburse for many of the procedures performed with our products. The success of any new product offering or enhancement to an existing product will depend on several factors, including our ability to:

- properly identify and anticipate neurointerventionalist and patient needs;
- develop new products or enhancements in a timely manner;
- obtain the necessary regulatory approvals for new products or product enhancements;
- provide adequate training to potential users of our products;
- receive adequate reimbursement for our procedures; and

Table of Contents

- results of clinical research and trials on our existing products and products in development;
- demand for, and pricing of, our products;
- levels of third-party reimbursement for our products;
- develop an effective marketing and distribution network.

If we do not develop new products or product enhancements in time to meet market demand or if there is insufficient demand for our products or enhancements, we may not achieve expected revenue levels and our business will suffer.

Our international operations and our relationships with physicians and other consultants require us to comply with a number of United States and international regulations.

We are required to comply with a number of international regulations related to sales of medical devices and contractual relationships with physicians in countries outside of the United States. In addition, we must comply with the Foreign Corrupt Practices Act ("FCPA") which prohibits United States companies or their agents and employees from providing anything of value to a foreign official for the purposes of influencing him or her to help obtain or retain business, direct business to any person or corporate entity, or obtain any unfair advantage.

In August 2004, while reviewing our sales and payment procedures, we identified certain payments we made to physicians outside the United States that may have violated the FCPA and the laws of certain foreign countries. Following an internal investigation, we voluntarily disclosed to the United States Department of Justice ("DOJ") the factual information obtained in our internal investigation of potential violations of the FCPA.

After reviewing the results of the internal investigation and the compliance procedures implemented by us, the DOJ entered into an agreement (the "DOJ Agreement") with us in February 2005. Pursuant to that agreement, the DOJ agreed not to prosecute us for the conduct disclosed to the DOJ, and we agreed to various conditions, including establishing policies and procedures to assure compliance with the FCPA and other relevant anti-bribery laws, retaining an independent law firm to act as a monitor for purposes of reporting to the DOJ for a period of three years as to our compliance with the DOJ Agreement and to monitor our implementation of and adherence to FCPA compliance policies and procedures, and fully cooperating with the DOJ, the independent monitor, and the SEC. The monitor filed his final report with the DOJ in May 2008, and in July 2008, the DOJ confirmed that the monitorship had concluded. We have reaffirmed our commitment take all reasonable steps to ensure that we remain in compliance with the FCPA.

The payments we made to physicians in France, Germany, Spain and Turkey are also likely to have violated the applicable laws in those foreign jurisdictions. We have not been notified by the authorities in France, Germany, Spain or Turkey whether or not such authorities intend to bring any action or impose any penalties on us relating to our activities in their respective countries. Therefore, we are unable to determine at this time what penalties or other sanctions, if any, such authorities may impose on us as a result of such violations. Such amounts could be material to our financial position, results of operations or cash flows. We have been notified by the Swiss Federal Prosecutor that it does not intend to bring any action or impose any penalties on us relating to our activities in Switzerland.

Though we have adopted a number of compliance procedures, including a Foreign Corrupt Practices Act Policy and related procedures, and appointed a Compliance Officer, we cannot assure you that we will be able to comply with the various regulations in foreign jurisdictions, which vary from country to country. Implementing and monitoring such compliance procedures in a number of foreign jurisdictions can be very expensive and time-consuming. Any failure

by us to adopt appropriate compliance procedures and ensure that our employees and agents comply with applicable laws and regulations in foreign jurisdictions could result in substantial penalties and/or restrictions in our ability to sell products in certain foreign jurisdictions.

We are in a highly competitive market segment, face competition from large, well-established medical device manufacturers with significant resources, and may not be able to increase penetration in our markets or otherwise compete effectively.

The market for medical devices for treatment of cerebral vascular diseases is intensely competitive, subject to rapid change and significantly affected by new product introductions and other market activities of industry participants. We compete primarily with the Target Therapeutics division of Boston Scientific, the market leader, as well as Cordis, ev3/Micro Therapeutics and Terumo/MicroVention. At any time, other companies may develop alternative treatments, products or procedures for the treatment of cerebral aneurysms that compete directly or indirectly with our products. If alternative treatments prove to be superior to our microcoil or other products, continued use or adoption of our products could be negatively affected and our future revenues could suffer.

Table of Contents

In addition, most of our current and potential competitors are either large publicly traded or divisions or subsidiaries of large publicly traded companies, and enjoy several competitive advantages over us, including:

- greater financial and personnel resources;
- significantly greater name recognition;
- established relationships with neurointerventionalists;
- established distribution networks;
- greater experience in obtaining and maintaining FDA, and other regulatory approvals for products and product enhancements, and greater experience in developing compliance programs for compliance with numerous federal, state, local and similar laws in non-United States jurisdictions;
- greater resources for product research and development;
- greater experience in, and resources for, launching, marketing, distributing and selling products; and
- broader product lines.

Except for our agreements with our distributors, we have no material long-term purchase agreements with our customers, who may at any time switch to the use of our competitors' products.

For these reasons, we may not be able to compete successfully against our current or potential future competitors and sales of our products and our revenues may decline.

Our sales in international markets subject us to foreign currency exchange and other risks and costs that could harm our business.

A substantial portion of our revenues are derived from outside the United States. For the fiscal years ended March 31, 2008, 2007 and 2006, revenues from customers outside the United States represented approximately 51%, 51% and 53%, respectively, of our revenues. For the first quarter of fiscal 2009, revenues from customers outside the United States represented 53% of our revenues. We anticipate that revenues from international customers will continue to represent a substantial portion of our revenues as we continue to expand in new international markets including China and Japan. Because we generate revenues in foreign currencies, we are subject to the effects of exchange rate fluctuations. For the first quarter of fiscal 2009, approximately 33% of our revenues were denominated in currencies other than the U.S. dollar. The functional currency of our Swiss subsidiary is the Swiss franc. In Europe, our revenues are denominated in Swiss francs, euros, pounds sterling and U.S. dollars. Accordingly, we are exposed to market risk related to changes between the Swiss franc and these other currencies in which we conduct business. If the Swiss franc appreciates against the currencies in which our receivables are denominated, we will recognize foreign currency losses. For the preparation of our consolidated financial statements, the financial results of our Swiss and UK subsidiaries are translated into U.S. dollars based on average exchange rates during the applicable period. If the U.S. dollar appreciates against the Swiss franc and pound sterling, the revenues we recognize from sales by our European subsidiaries will be adversely impacted. Historically, we have also been exposed to risks from fluctuations in currency exchange rates due to intercompany loans made to Micrus Endovascular SA ("Micrus SA"), our Swiss subsidiary, in 2001 in connection with its incorporation. These loans are denominated in Swiss francs and will fluctuate in value against the U.S. dollar, causing us to recognize foreign exchange gains and losses. Foreign exchange

gains or losses as a result of exchange rate fluctuations in any given period could harm our operating results and negatively impact our revenues. Additionally, if the effective price of our products were to increase as a result of fluctuations in foreign currency exchange rates, demand for our products could decline and adversely affect our results of operations and financial condition. We currently do not enter into foreign currency forward contracts and other arrangements intended to hedge our exposure to adverse fluctuations in exchange rates.

Table of Contents

We are subject to various additional risks as a consequence of doing business internationally which could harm our business, including the following:

- unexpected delays or changes in regulatory requirements;
- local economic and political instability or other potentially adverse conditions;
- lack of experience in certain geographical markets;
- increased difficulty in collecting accounts receivables in certain foreign countries;
- delays and expenses associated with tariffs and other trade barriers;
- difficulties and costs associated with attracting and maintaining third party distributors;
- compliance with foreign laws and regulations; and
- adverse tax consequences or overlapping tax structures.

If we fail to increase our direct sales force in a timely manner, our business could suffer.

We have a limited domestic and international direct sales force. We also have a distribution network for sales in the major markets in Europe, Latin America, Asia and the Middle East. As we launch new products and increase our marketing efforts with respect to existing products, we will need to expand the number of our direct sales personnel on a worldwide basis. The establishment and development of a more extensive sales force will be expensive and time consuming. There is significant competition for sales personnel experienced in interventional medical device sales. If we are unable to attract, motivate and retain qualified sales personnel and thereby increase our sales force, we may not be able to increase our revenues.

If we fail to properly manage our anticipated growth, our business could suffer.

We have experienced, and may continue to experience, periods of rapid growth and expansion, which have placed, and will likely continue to place, a significant strain on our limited personnel and other resources. In particular, the expansion of our fabrication facility and the continuing expansion of our direct sales force will require significant management, technical and administrative resources. Any failure by us to manage our growth effectively, could have an adverse effect on our ability to achieve our development and commercialization goals.

To achieve our revenue goals, we must successfully increase production in our fabrication facility as required by customer demand. We may in the future experience difficulties in increasing production, including problems with production yields and quality control and assurance and in satisfying and maintaining compliance with regulatory requirements. These problems could result in delays in product availability and increases in expenses. Any such delay or increased expense could adversely affect our ability to generate revenues.

Future growth will also impose significant added responsibilities on management, including the need to identify, recruit, train and integrate additional employees. In addition, rapid and significant growth will place a strain on our administrative and operational infrastructure. In order to manage our operations and growth we will need to continue to improve our operational, financial and management controls, reporting systems and procedures. If we are unable to manage our growth effectively, it may be difficult for us to execute our business strategy and our operating results and

business could suffer.

Table of Contents

We are required to evaluate our internal control over financial reporting under Section 404 of the Sarbanes-Oxley Act of 2002 and are exposed to future risks of non compliance.

Pursuant to Section 404 of the Sarbanes-Oxley Act of 2002 ("Section 404"), we are required to furnish a report by our management on our internal control over financial reporting. The report contains, among other matters, an assessment of the effectiveness of our internal control over financial reporting as of the end of our fiscal year, including a statement as to whether or not our internal control over financial reporting is effective. This assessment must include disclosure of any material weaknesses in our internal control over financial reporting identified by management. The report must also contain a statement that our independent registered public accounting firm has issued an attestation report on the effectiveness of internal control over financial reporting.

We completed our assessment of our internal control over financial reporting as required by Section 404 for the fiscal year ended March 31, 2008. Our assessment, testing and evaluation resulted in our conclusion that as of March 31, 2008, our internal control over financial reporting was effective. Our independent registered accounting firm has also expressed the opinion that our internal controls over financial reporting were effective during that period. However, our controls, may not prove to be adequate for the future periods, and we cannot predict the outcome of our testing in future periods. If our internal controls are deemed to be ineffective in future periods, our financial results or the market price of our stock could be adversely affected. In any event, we will incur additional expenses and commitment of management's time in connection with further evaluations, which may adversely affect our future operating results and financial condition.

Our future capital needs are uncertain and we may need to raise additional funds in the future, and such funds may not be available on acceptable terms or at all.

We believe that our current cash position, together with the cash to be generated from expected product sales will be sufficient to meet our projected operating requirements for at least the next 12 months. However, after such period we may be required to seek additional funds from public and private stock or debt offerings, borrowings under lease lines or other sources. Our capital requirements will depend on many factors, including:

- the revenues generated by sales of our products;
- the costs associated with expanding our sales and marketing efforts;
- the expenses we incur in manufacturing and selling our products;
- the costs of developing and or acquiring new products or technologies;
- the cost of obtaining and maintaining FDA and other domestic and foreign approval or clearance of our products and products in development;
- costs associated with our litigation with Boston Scientific and our securities litigation;
- the expenses we incur related to compliance with the United States FCPA and laws and regulations in non-United States jurisdictions;
- costs associated with compliance with the Sarbanes-Oxley Act of 2002 and rules and regulations affecting public companies promulgated by the SEC and The NASDAQ Stock Market;

- the costs associated with our facilities expansion, if any; and
- the costs associated with increased capital expenditures.

Table of Contents

As a result of these factors, we may need to raise additional funds, and such funds may not be available on favorable terms, or at all. Furthermore, if we issue equity or debt securities to raise additional funds, our existing stockholders may experience dilution, and the new equity or debt securities may have rights, preferences and privileges senior to those of our existing stockholders. In addition, if we raise additional funds through collaboration, licensing or other similar arrangements, it may be necessary to relinquish valuable rights to our potential products or proprietary technologies, or grant licenses on terms that are not favorable to us. If we cannot raise funds on acceptable terms, we may not be able to develop or enhance our products, execute our business plan, take advantage of future opportunities, or respond to competitive pressures or unanticipated customer requirements. In these events, our ability to achieve our development and commercialization goals would be adversely affected.

If we choose to acquire new and complementary businesses, products or technologies instead of developing them ourselves, we may be unable to complete these acquisitions or to successfully integrate them in a cost effective and non-disruptive manner.

Our success depends on our ability to continually enhance and broaden our product offerings in response to changing customer demands, competitive pressures and technologies. We may in the future pursue the acquisition of additional complementary businesses, products or technologies instead of developing them ourselves. We do not know if we will be able to successfully complete any such acquisitions, or whether we will be able to successfully integrate any acquired business, product or technology or retain any key employees. Integrating any business, product or technology we acquire could be expensive and time consuming, disrupt our ongoing business and distract our management. If we are unable to integrate any acquired businesses, products or technologies effectively, our business will suffer. In addition, any amortization or charges resulting from the costs of acquisitions could harm our business and operating results.

We are dependent on single source suppliers for components and materials used in our devices, and the loss of any of these suppliers, or their inability to supply us with an adequate supply of materials, could harm our business.

We rely on third-party suppliers for components and materials used in our products and rely on single sources for many of the microcoil and delivery system components, including tubing, connectors and sterilization services. Our dependence on third-party suppliers involves several risks, including limited control over pricing, availability, quality, delivery schedules and supplier compliance with regulatory requirements. Any delays in delivery of such components or provision of such services or shortages of such components could cause delays in the shipment of our products, which could significantly harm our business. We generally acquire our single source components pursuant to purchase orders placed in the ordinary course of business, and we have no guaranteed supply arrangements with any of our single source suppliers. Because of our reliance on these vendors, we may also be subject to increases in component costs. These increases could significantly harm our business. For us to be successful, our third-party suppliers must also be able to provide us with the materials and components of our products in substantial quantities, in compliance with regulatory requirements, in accordance with agreed upon specifications, at acceptable cost and on a timely basis. Our anticipated growth may strain the ability of suppliers to deliver an increasingly large supply of materials and components. If we are unable to obtain sufficient quantities of high quality components and materials to meet customer demand on a timely basis, we could lose customers, our reputation may be harmed and our business could suffer. If any one or more of our third-party suppliers cease to provide us with sufficient quantities of our materials or components in a timely manner or on terms acceptable to us, we would have to seek alternative sources of supply. We could incur delays while we locate and engage alternative qualified suppliers and we might be unable to engage alternative suppliers on favorable terms. Any such disruption or increased expenses could harm our commercialization efforts and adversely affect our ability to generate revenues.

We rely on independent contract manufacturers for the manufacture and assembly of certain of our products and components. Reliance on independent contract manufacturers involves several risks, including the potential inadequacy of capacity, the unavailability of or interruptions in access to certain process technologies and reduced control over product quality, compliance with regulatory requirements, delivery schedules, manufacturing yields and costs. Such manufacturers have possession of and at times title to molds for certain manufactured components of our products. Shortages of raw materials, production capacity constraints or delays by our contract manufacturers could negatively affect our ability to meet our production obligations and result in increased prices for affected parts. Any such reduction, constraint or delay may result in delays in shipments of our products or increases in the prices of components, either of which could have a material adverse effect on our business, operating results and financial condition. We have no supply agreements with our current contract manufacturers and utilize purchase orders which are subject to supplier acceptance. The unanticipated loss of any of our contract manufacturers could cause delays in our ability to deliver product while we identify and qualify a replacement manufacturer. If our current or future independent contract manufacturers are unable to meet our requirements for manufactured components, our business could suffer.

Table of Contents

Our operations are currently conducted at several locations that may be at risk from earthquakes or other natural disasters.

We currently conduct our manufacturing, development and management activities at two locations in Silicon Valley, California, near known earthquake fault zones and in Doral, Florida, where there is a risk of hurricanes. We have taken precautions to safeguard our facilities, including insurance, health and safety protocols, and off-site storage of computer data. However, any future natural disaster, such as an earthquake or hurricane, could cause substantial delays in our operations, damage or destroy our equipment or inventory, and cause us to incur additional expenses. A disaster could seriously harm our business and results of operations.

If we are unable to effectively manage our inventory held on consignment by our intended customers, we will not achieve our expected results.

A significant portion of our inventory is held on consignment by hospitals that purchase the inventory as they use it. In these consignment locations, we do not have physical possession of the consigned inventory. We therefore have to rely on information from our customers as well as periodic inspections by our sales personnel to determine when our products have been used. We have in the past experienced problems managing appropriate consigned inventory levels and as a result we recorded an impairment of inventory for anticipated obsolescence in fiscal 2004 and an impairment of excess inventory in both fiscal 2004 and 2005. If we are not able to effectively manage appropriate consigned inventory levels, we may suffer inventory losses that will reduce our gross profit levels. There can be no assurance that any efforts to strengthen our monitoring and management of consigned inventory will be adequate to meaningfully reduce the risk of inventory loss.

We are dependent on our senior management team, key clinical advisors and scientific personnel, and the loss of any of them could harm our business.

Our continued success depends in part upon the continued availability and contributions of our senior management team and the continued participation of our key clinical advisors. We have entered into agreements with certain members of our senior management team, but none of these agreements guarantee the services of the individual for a specified period of time. We also rely on the skills and talents of our scientific personnel because of the complexity of our products. The loss of members of our senior management, key clinical advisors or scientific personnel, or our inability to attract or retain other qualified personnel or advisors could have a material adverse effect on our results of operations and financial condition.

The medical device industry is characterized by patent litigation, which could be costly, result in the diversion of management’s time and efforts and require us to pay damages.

The medical device industry is characterized by extensive litigation and administrative proceedings over patent and other intellectual property rights. Accordingly, we may in the future be subject to further litigation and administrative proceedings over such rights with other companies in our industry. As we have discussed above with respect to our current litigation with Boston Scientific, whether a product or method infringes a patent involves complex legal and factual issues rendering the outcome of any patent dispute largely unpredictable. In the future, other competitors may assert that at least one of our products, its components, or the methods we employ in the use or manufacture of our products are covered by and infringe the competitors’ United States or foreign patents held by them. In addition, should our patents or applications have claims that encompass the same scope as claims pending or issued to a third party competitor, that third party may claim that its claims have priority over ours because they invented the claimed subject matter first. Because patent applications generally take many years to issue, there may be third party applications presently pending of which we are unaware, that may in the future result in issued patents that at least one

of our products, its components, or the methods we employ in the use or manufacture of our product(s) may infringe. There could also be issued patents that one or more components of our products may inadvertently be infringing, of which we are unaware. As the number of participants in the market for cerebral vascular treatments and the number of issued patents in this technology area grows, the possibility of being charged with patent infringement increases.

As we have discussed above with respect to our litigation with Boston Scientific, any infringement claims against us may cause us to incur substantial costs, could place a significant strain on our financial resources, divert the attention of management from our core business and harm our reputation. If the relevant patent claims are upheld as valid and enforceable and we are found to infringe, we could be required to pay substantial damages and/or royalties and could be prevented from selling our products unless we could obtain a license or were able to redesign our products to avoid infringement. Any such license may not be available on reasonable terms, if at all. If we fail to obtain any required licenses or make any necessary changes to our products or technologies, we may be unable to commercialize one or more of our products or practice the methods we employ in the use or manufacture of our products.

Table of Contents

Our ability to protect our intellectual property and proprietary technology through patents and other means is uncertain.

Our success depends significantly on our ability to procure proprietary rights to the technologies used in our products. We rely on patent protection, as well as a combination of copyright, trade secret and trademark laws, and nondisclosure, confidentiality and other contractual restrictions to protect our proprietary technology. However, these legal means afford only limited protection and may not be sufficient to adequately protect our intellectual property or permit us to gain or keep any competitive advantage. For example, any of our pending United States or foreign patent applications may ultimately not issue as a patent or, alternatively, may issue with claims that are of little or no value to us. In addition, once issued, a valuable patent may be challenged successfully by third parties and invalidated, such as is being attempted by Boston Scientific in our presently ongoing litigation. In addition, our patent protection for material aspects of our products and methods is presently being pursued with applications that have been filed but not issued, such that these material aspects are not presently protected by patents. Competitors may further be able to get around having to license our technology in order to avoid infringement by designing around our issued and published patent claims, thereby staying clear of our proprietary rights. Similarly, competitors may develop products and methods that are equivalent or superior to ours. Our confidentiality agreements and intellectual property assignment agreements with our employees, consultants and advisors may not be enforceable or may not provide meaningful protection for our trade secrets or other proprietary information in the event of unauthorized use or disclosure or other breaches of the agreements. Furthermore, the laws of some foreign countries may not protect our intellectual property rights to the same extent as do the laws of the United States. Both the process of procuring patent rights and the process of managing patent disputes can be time consuming and expensive.

In the event a competitor infringes upon our patent or other intellectual property rights, enforcing those rights may be difficult and time consuming. Even if successful, litigation to enforce our intellectual property rights or to defend our patents against challenge could be prolonged, costly and could divert our management's attention. We may not have sufficient resources to enforce our intellectual property rights or to defend our patents against a challenge.

If we fail to obtain, or experience significant delays in obtaining, FDA clearances or approvals for our future products or product enhancements, or to comply with similar regulatory requirements in other countries where we market our products, our ability to commercially distribute and market our products could suffer.

Our medical devices are subject to rigorous regulation by the FDA and numerous other federal, state and foreign governmental authorities. Our failure to comply with such regulations could lead to the imposition of injunctions, suspensions or loss of regulatory clearances or approvals, product recalls, termination of distribution or product seizures or the need to invest substantial resources to comply with various existing or new requirements. In the more egregious cases, criminal sanctions, civil penalties, disgorgement of profits or closure of our manufacturing facilities are possible. The process of obtaining regulatory clearances or approvals to market a medical device, particularly from the FDA, can be costly and time consuming, and there can be no assurance that such clearances or approvals will be granted on a timely basis, if at all. In particular, the FDA permits commercial distribution of most new medical devices only after the device has received 510(k) clearance or is the subject of an approved pre-market approval application, or PMA. The FDA will clear the marketing of a medical device through the 510(k) process if it is demonstrated that the new product has the same intended use, is substantially equivalent to another legally marketed device, including a 510(k)-cleared product, and otherwise meets the FDA's requirements. The PMA approval process is more costly, lengthy and uncertain than the 510(k) clearance process and requires the development and submission of clinical studies supporting the safety and effectiveness of the device. Product modifications may also require the submission of a new 510(k) clearance, or the approval of a PMA before the modified product can be marketed. Changes in labeling and manufacturing site for a PMA approved device may require the submission and approval of a PMA supplement. Any products we develop that require regulatory clearance or approval may be delayed, if approved

at all. In addition, we believe that some of our new products will require an approved PMA before we can commercially distribute the device and we cannot assure you that any new products or any product enhancements we develop will be subject to the shorter 510(k) clearance process instead of the more lengthy PMA requirements. Additionally, certain of our products under development may involve both device and drug or biologic regulation and we will need to comply with drug and biologic regulations in addition to medical device requirements. Accordingly, we anticipate that the regulatory review and approval process for some of our future products or product enhancements may take significantly longer than anticipated or that we have experienced in the past. We will also be required to pay a medical device user fee and may also be required to pay a drug or biologic user fee. There is no assurance that the FDA will not require that a certain new product or product enhancement go through the lengthy and expensive PMA approval process. We have no experience in obtaining PMA approval. We also have no experience in obtaining drug or biologic approval, and will need to rely on third party assistance in navigating the regulatory approval pathway for future combination products.

Table of Contents

Further, pursuant to FDA regulations, we can only market our products for cleared or approved uses. Certain of our products may be used by physicians for indications other than those cleared or approved by the FDA, but we cannot promote the products for such off-label uses.

Modifications to our marketed products may require new 510(k) clearances or pre-market approvals, or may require us to cease marketing or recall the modified products until clearances are obtained.

Any modification to a 510(k)-cleared device that could significantly affect its safety or effectiveness, or that would constitute a change in its intended use, requires a new 510(k) clearance or, possibly, PMA approval. The FDA requires every manufacturer to make this determination in the first instance, but the FDA may review a manufacturer's decision. The FDA may not agree with any of our past or future decisions regarding whether new clearances or approvals are necessary. If the FDA requires us to seek 510(k) clearance or PMA approval for any modification to a previously cleared product, we may be required to cease marketing and/or to recall the modified product until we obtain clearance or approval, and we may be subject to significant regulatory fines or penalties. Further, our products could be subject to recall if the FDA determines, for any reason, that our products are not safe, including but not limited to new safety data from use of the product, or manufacturing defects. Any recall or FDA requirement that we seek additional approvals or clearances could result in delays, fines, costs associated with modification of a product, loss of revenue and potential operating restrictions imposed by the FDA

If we or our suppliers fail to comply with the FDA's quality system regulations, the manufacture of our products could be delayed.

We and our suppliers are required to comply with the FDA's quality system regulations, which cover the methods and documentation of the design, testing, production, control, quality assurance, labeling, packaging, storage and shipping of our products. The FDA enforces these quality system regulations through unannounced inspections. If we or one of our suppliers fail a quality system regulations inspection or if any corrective action plan is not sufficient, or is very expensive or time consuming to implement, the manufacture of our products could be delayed until satisfactory corrections are made, or in the event we are unable to correct the problems we may not be able to continue manufacturing and distributing the particular device or devices. Such a delay potentially could disrupt our business, harm our reputation and adversely affect our sales and revenues.

If neurointerventionalists are unable to obtain sufficient reimbursement for procedures performed with our products, it is unlikely that our products will be widely used.

Successful sales of our products will depend on the availability of adequate reimbursement from third-party payors. Healthcare providers that purchase medical devices for treatment of their patients, generally rely on third-party payors to cover the use of the product for the particular procedure and reimburse all or part of the costs and fees associated with the procedures performed with these devices. Currently, the costs of our products distributed domestically are being reimbursed by third party payors. There is no guarantee that coverage and adequate reimbursement will be available in the future for our existing and/or new products. Both public and private insurance reimbursement plans are central to new product acceptance. Neurointerventionalists are unlikely to use our products if they do not receive reimbursement adequate to cover the cost of our products and related procedures.

In international markets, market acceptance may depend, in part, upon the availability of reimbursement within prevailing healthcare payment systems. Reimbursement and healthcare payment systems in international markets vary significantly by country, and include both government sponsored healthcare and private insurance. Currently, the costs of our products distributed internationally, other than in some Latin American countries, are being reimbursed by

public and private healthcare insurers. We may not obtain international reimbursement approvals in a timely manner, if at all, our failure to receive international reimbursement approvals would negatively impact market acceptance of our products in the international markets in which those approvals are sought.

In addition, in certain countries, such as France, Germany, China and Japan, we are required to obtain regulatory clearance for our products to be eligible for reimbursements by third party payors, even though reimbursement for embolic coiling procedures is already in place.

Future reimbursement may be subject to increased restrictions both in the United States and in international markets. Third-party reimbursement and coverage may not be available or adequate in either the United States or international markets. Future legislation, regulation or reimbursement policies of third-party payors may adversely affect the demand for our existing products or our products currently under development and limit our ability to sell our products on a profitable basis.

Table of Contents

Changes to existing accounting pronouncements or taxation rules or practices may affect how we conduct our business and affect our reported results of operations.

New accounting pronouncements or tax rules and varying interpretations of accounting pronouncements or taxation practice have occurred and may occur in the future. A change in accounting pronouncements or interpretations or taxation rules or practices can have a significant effect on our reported results and may even affect our reporting of transactions completed before the change is effective. Changes to existing rules and pronouncements, future changes, if any, or the questioning of current practices or interpretations may adversely affect our reported financial results or the way we conduct our business.

We may become subject to product liability claims which could require us to pay damages that exceed our insurance coverage.

Our business exposes us to potential product liability claims that are inherent in the testing, manufacture and sale of medical devices for neurointerventional procedures. These procedures involve significant risk of serious complications, including intracranial bleeding, brain injury, paralysis and even death. Any product liability claim brought against us, with or without merit, could result in the increase of our product liability insurance rates or the inability to secure coverage in the future. In addition, we could have to pay an amount in excess of policy limits, which would have to be paid out of cash reserves. If longer-term patient results and experience indicate that our products or any component cause tissue damage, motor impairment or other adverse effects, we could be subject to significant liability. Finally, even a meritless or unsuccessful product liability claim could harm our reputation in the industry, lead to significant legal fees and could result in the diversion of management's attention from managing our business.

We may be subject to damages resulting from claims that we or our employees have wrongfully used or disclosed alleged trade secrets of their former employers.

Many of our employees were previously employed at other medical device companies, including our competitors or potential competitors. Although no claims against us are currently pending, we may be subject to claims that these employees have wrongfully used or disclosed alleged trade secrets of their former employers or we have inadvertently or otherwise used or disclosed trade secrets or other proprietary information of their former employers. Litigation may be necessary to defend against these claims. Even if we are successful in defending against these claims, litigation could result in substantial costs and be a distraction to management. If we fail in defending such claims, in addition to paying monetary damages, we may lose valuable intellectual property rights or personnel. A loss of key research personnel or their work product could hamper or prevent our ability to commercialize product candidates, which could severely harm our business.

The price of our common stock has fluctuated and we expect will continue to fluctuate substantially and you may not be able to sell your shares at or above your purchase price.

The market price of our common stock has been and we expect will continue to be highly volatile and may fluctuate substantially due to many factors, including:

- volume and timing of orders for our products;
- the introduction of new products or product enhancements by us or our competitors;
- disputes or other developments with respect to intellectual property rights;

- our ability to develop, obtain regulatory clearance for, and market, new and enhanced products on a timely basis;
- product liability claims or other litigation;
- quarterly variations in our or our competitors' results of operations;
- sales of large blocks of our common stock, including sales by our executive officers and directors;

Table of Contents

- changes in governmental regulations or in the status of our regulatory approvals or applications;
- changes in the availability of third-party reimbursement in the United States or other countries;
- changes in revenues or earnings estimates or recommendations by securities analysts; and
- general market conditions and other factors, including factors unrelated to our operating performance or the operating performance of our competitors.

Furthermore, to the extent there is an inactive market for our common stock, the value of your shares and your ability to sell your shares at the time you wish to sell them may be impaired. An inactive market may also impair our ability to raise capital by selling shares and may impair our ability to acquire other companies, products or technologies by using our shares as consideration.

Because of their significant stock ownership, our executive officers, directors and principal stockholders may be able to exert control over us and our significant corporate decisions.

Based on shares outstanding at June 30, 2008, our executive officers, directors, and stockholders holding more than 5% of our outstanding common stock and their affiliates, in the aggregate, beneficially owned approximately 52% of our outstanding common stock. As a result, these persons, acting together, may have the ability to determine the outcome of all matters submitted to our stockholders for approval, including the election and removal of directors and any merger, consolidation, or sale of all or substantially all of our assets. This concentration of ownership may harm the market price of our common stock by, among other things:

- delaying, deferring or preventing a change in control of our company;
- impeding a merger, consolidation, takeover or other business combination involving our company; or
- causing us to enter into transactions or agreements that are not in the best interests of all stockholders.

Future sales of our common stock may depress our stock price.

Our current stockholders hold a substantial number of shares of our common stock that they are able to sell in the public market A significant portion of these shares are held by a small number of stockholders. Sales by our current stockholders of a substantial number of shares could significantly reduce the market price of our common stock. Moreover certain holders of our common stock have the right to require us to file registration statements covering their shares or to include their shares in registration statements that we may file for ourselves or other stockholders.

We have registered 6,749,963 shares of common stock that we may issue under our 1998 Stock Plan (the “1998 Plan”), 2005 Equity Incentive Plan (the “2005 Plan”) and 2005 Employee Stock Purchase Plan. These shares can be freely sold in the public market upon issuance. The sale by any of these holders of a large number of securities in the public market could reduce the trading price of our common stock and impede our ability to raise future capital.

We do not intend to pay cash dividends.

We have never declared or paid cash dividends on our capital stock. We currently intend to retain all available funds and any future earnings for us in the operation and expansion of our business and do not anticipate paying any cash dividends in the foreseeable future. In addition, the terms of any future debtor credit facility may preclude us from

paying any dividends. As a result, capital appreciation, if any, of our common stock will be your sole source of potential gain for the foreseeable future.

Table of Contents

We may become involved in securities class action litigation that could divert management's attention and harm our business.

The stock market in general, The NASDAQ Stock Market and the market for medical device companies in particular, continues to experience extreme price and volume fluctuations that are unrelated or disproportionate to companies' operating performance. Further, the market prices of securities of medical device companies have been particularly volatile. These broad market and industry factors may materially harm the market price of our common stock, regardless of our operating performance. In the past, following periods of volatility in the market price of a particular company's securities, securities class action litigation has often been brought against that company. We may become involved in this type of litigation in the future. Litigation often is expensive and diverts management's attention and resources, which could materially harm our financial condition and results of operations.

Anti-takeover provisions in our organizational documents and Delaware law may discourage or prevent a change of control, even an acquisition which would be beneficial to our stockholders, and thereby affect our stock price adversely and prevent attempts by our stockholders to replace or remove our current management.

Our amended and restated certificate of incorporation and amended bylaws contain provisions that could delay or prevent a change of control of our company or changes in our board of directors that our stockholders might consider favorable. Some of these provisions:

- authorize the issuance of preferred stock which can be created and issued by the board of directors without prior stockholder approval, with rights senior to those of the common stock;
- provide for a classified board of directors, with each director serving a staggered three-year term;
- prohibit our stockholders from filling board vacancies, calling special stockholder meetings, or taking action by written consent;
- prohibit our stockholders from making certain changes to our amended and restated certificate of incorporation or bylaws except with 66 2/3% stockholder approval; and
- require advance written notice of stockholder proposals and director nominations.

In addition, we are subject to the provisions of Section 203 of the Delaware General Corporation Law, which may prohibit certain business combinations with stockholders owning 15% or more of our outstanding voting stock. These and other provisions in our amended and restated certificate of incorporation, restated bylaws and Delaware law could make it more difficult for stockholders or potential acquirers to obtain control of our board of directors or initiate actions that are opposed by our then-current board of directors, including delaying or impeding a merger, tender offer, or proxy contest involving our company. Any delay or prevention of a change of control transaction or changes in our board of directors could cause the market price of our common stock to decline.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None

Item 3. Defaults Upon Senior Securities.

None

Item 4. Submission of Matters to a Vote of Security Holders.

None

Table of Contents

Item 5. Other Information.

None

Item 6. Exhibits.

See the Index to Exhibits on Page 47 of this report

Table of Contents

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.

Date: August 8, 2008

By: /s/ John T. Kilcoyne
John T. Kilcoyne
Chairman and Chief Executive Officer

By: /s/ Gordon T. Sangster
Gordon T. Sangster
Chief Financial Officer

Table of Contents

INDEX TO EXHIBITS

Exhibit Number	Description
3.1	Certificate of Incorporation (incorporated by reference to Exhibit 3.2 of Amendment No. 3 to the Registrant's Registration Statement on Form S-1 filed on May 17, 2005 Registration No. 333-123154) ("Amendment No. 3")
3.2	Bylaws (incorporated by reference to Exhibit 3.4 of Amendment No. 3)
4.1	Specimen Stock Certificate (incorporated by reference to Exhibit 4.1 of the Registrant's Registration Statement on Form S-1 filed on March 4, 2005 (Registration No. 333-123154) ("Form S-1")
4.2	Warrant dated as of December 11, 2000 among the Registrant and Roberts Mitani Capital, LLC (incorporated by reference to Exhibit 4.2 of Form S-1)
4.3	Amended and Restated Stockholders' Rights Agreement dated as of February 21, 2005 among the Registrant and the parties listed therein (incorporated by reference to Exhibit 4.3 of Form S-1)
4.4	Form of Common Stock Warrant issued in connection with the Series E Preferred Stock and Warrant Purchase Agreement dated February 21, 2005, among the Registrant and the purchasers of the Registrant's Series E Preferred Stock (incorporated by reference to Exhibit 4.4 of Form 10-Q filed on February 14, 2006)
31.1#	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2#	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32#	Certifications Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

_____

Filed herewith