MICRUS ENDOVASCULAR CORP
Form 10-Q
February 09, 2009

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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 December 31, 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 (State or other jurisdiction of incorporation or organization)	23-2853441 (I.R.S. Employer Identification No.)
821 Fox Lane San Jose, California (Address of principal executive offices)	95131 (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 £ NoR

As of February 3, 2009, there were 15,750,713 shares of common stock, par value $0.01, of the registrant outstanding.

MICRUS ENDOVASCULAR CORPORATION

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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)

	December 31, 2008	March 31, 2008
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 14,103	$ 25,526
Accounts receivable, net of allowance for doubtful accounts		
of $89 at December 31, 2008 and $95 at March 31, 2008	10,855	11,297
Inventories	12,410	11,495
Prepaid expenses and other current assets	1,676	1,570
Deferred tax assets	66	-
Total current assets	39,110	49,888
Property and equipment, net	7,366	5,285
Goodwill	6,887	8,549
Intangible assets, net	5,563	7,153
Deferred tax assets	99	9
Other assets	487	1,448
Total assets	$ 59,512	$ 72,332
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	$ 2,467	$ 3,680
Accrued payroll and other related expenses	5,616	7,930
Deferred tax liabilities	-	43
Short-term borrowings (Note 5)	2,500	-
Accrued liabilities	6,939	9,431
Total current liabilities	17,522	21,084
Deferred tax liabilities	-	314
Other non-current liabilities	1,675	2,754
Total liabilities	19,197	24,152
Commitments and contingencies (Note 7)		
Stockholders' equity:		
Common stock, $0.01 par value;		
Authorized: 50,000,000 shares		

Issued and outstanding:15,737,550 shares at December 31, 2008 and 15,614,760 shares at March 31, 2008	157	156
Additional paid-in capital	125,308	119,897
Accumulated other comprehensive loss	(2,158)	(511)
Accumulated deficit	(82,992)	(71,362)
Total stockholders' equity	40,315	48,180
Total liabilities and stockholders' equity	$ 59,512	$ 72,332

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

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

	Three months ended December 31,		Nine months ended December 31,	
	2008	2007	2008	2007
Revenues	$ 18,322	$ 18,343	$ 57,438	$ 49,495
Cost of goods sold	4,777	5,049	14,984	11,935
Gross profit	13,545	13,294	42,454	37,560
Operating expenses:				
Research and development	2,403	5,553	8,253	10,135
Sales and marketing	6,942	7,432	23,021	21,087
General and administrative	5,892	6,174	21,818	18,076
Total operating expenses	15,237	19,159	53,092	49,298
Loss from operations	(1,692)	(5,865)	(10,638)	(11,738)
Interest income	49	304	239	1,015
Interest expense	(10)	-	(14)	(2)
Other income (expense), net	(1,006)	67	(1,689)	427
Loss before income taxes	(2,659)	(5,494)	(12,102)	(10,298)
Provision for (benefit from) income taxes	(367)	210	(472)	(189)
Net loss	$ (2,292)	$ (5,704)	$ (11,630)	$ (10,109)
Net loss per share attributable to common stockholders:				
Basic and diluted	$ (0.15)	$ (0.37)	$ (0.74)	$ (0.66)
Weighted-average number of shares used in per share calculations:				
Basic and diluted	15,734	15,516	15,675	15,399

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

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

	Nine months ended December 31,	
	2008	2007
Cash flows from operating activities:		
Net loss	$ (11,630)	$ (10,109)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	2,466	2,383
Provision for doubtful accounts	17	(7)
Loss on disposal of equipment	14	23
Provision for excess and obsolete inventories	(53)	655
Stock-based compensation	4,307	3,501
Deferred income taxes	(498)	(194)
Changes in operating assets and liabilities, net of effect of acquisitions:		
Accounts receivable	(183)	(2,439)
Inventories	(1,186)	(3,421)
Prepaid expenses and other current assets	(131)	63
Other assets	(26)	16
Accounts payable	(1,157)	40
Accrued payroll and other related expenses	(2,072)	(14)
Accrued liabilities	(243)	861
Other non-current liabilties	(1,071)	1,437
Net cash used in operating activities	(11,446)	(7,205)
Cash flows from investing activities:		
Acquisition of property and equipment	(2,500)	(1,657)
Proceeds from sale of property and equipment	-	107
Proceeds from sale of assets and technologies in connection with Merit transaction	1,500	-
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	(4,832)	(3,782)
Cash flows from financing activities:		
Borrowings under bank line of credit	2,500	-
Proceeds from exercise of stock options	624	1,956
Proceeds from employee stock purchase plan	527	513
Net cash provided by financing activities	3,651	2,469
Effect of foreign exchange rate changes on cash	1,204	(675)

Net decrease in cash and cash equivalents	(12,627)	(8,518)
Cash and cash equivalents at beginning of period	25,526	34,536
Cash and cash equivalents at end of period	$ 14,103	$ 25,343

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

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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 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.

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 (“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 December 31, 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 December 31, 2008 and the cash expected to be generated from operations, together with the funds available under its credit facility (subject to compliance with the conditions and covenants of the credit agreement) (see Note 5 for more details), 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, together with the funds available under its credit facility (subject to compliance with the conditions and covenants of the credit agreement), are insufficient to fund its future activities, the Company may need to raise additional funds through public or private equity or debt financing and reduce certain discretionary spending. Additional funds may not be available on terms favorable to the Company

or at all.

Note 2 — Summary of Significant Accounting Policies

The Company's significant accounting policies are fully described in Note 2 to the Consolidated Financial Statements included in the Company's 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.

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. The resulting translation adjustments are recorded directly to accumulated other comprehensive income (loss).

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Reclassifications

Certain amounts in the prior year condensed 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.

Use of estimates

The preparation of consolidated financial statements in conformity with GAAP 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.

Revenue recognition – sales made to Latin American distributors

Sales to the Company's Latin American distributors are made according to similar contractual terms as sales to other distributors. 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 that through March 31, 2008 collectibility was not reasonably assured at the time that the distributor took title to the inventory. 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 beginning in the quarter ended June 30, 2008. Revenues recognized upon shipment to the Company's Latin American distributors were $482,000 and $1.9 million for the three and nine months ended December 31, 2008, respectively. Additionally, the deferred revenue balance at March 31, 2008 of $0.7 million for these distributors 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 on a cash basis on sales made to the Company's Latin American distributors were $480,000 and $1.2 million for the three and nine months ended December 31, 2007, respectively.

Product warranty

Once a sale has occurred, the customer has no right of return and the Company provides its customers with limited warranty privileges. To date, product returns under warranty have not been significant. The warranty accrual as of December 31, 2008 and March 31, 2008 was immaterial to the financial position of the Company and the change in the accrual for both the current-year quarter and prior-year quarter was immaterial to the Company's results of operations and cash flows.

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 December 31, 2008 and March 31, 2008 was comprised entirely of foreign currency translation adjustments. Total comprehensive loss for the three and nine

months ended December 31, 2008 was $3.7 million and $13.3 million, respectively. This included other comprehensive loss of $1.5 million and $1.7 million respectively, related to foreign currency translation adjustments. Total comprehensive loss for the three and nine months ended December 31, 2007 was $5.7 million and $10.2 million, respectively. This included other comprehensive loss of $0 and $112,000 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.

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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):

	Nine months ended December 31,	
	2008	2007
Shares issuable upon exercise of common stock options	4,059	3,492
Shares issuable upon settlement of restricted stock units	4	7
Shares issuable under employee stock purchase plan	28	18
	4,091	3,517

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.

Recent accounting pronouncements

In February 2007, the FASB issued Statement of Financial Accounting Standard ("SFAS") No. 159 ("SFAS 159"), "The Fair Value Option for Financial Assets and Financial Liabilities," which expands opportunities to use fair value measurements in financial reporting and permits entities to choose to measure many financial instruments and certain other items at fair value. SFAS 159 became effective for the Company on April 1, 2008. The adoption of SFAS 159 did not have a material impact on the Company's consolidated financial position, results of operations or cash flows.

In December 2007, the FASB issued SFAS No. 141R ("SFAS 141R"), "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. This provision will only impact the Company's accounting for any acquisition on or after April 1, 2009.

In February 2008, the FASB issued FASB Staff Position ("FSP") SFAS No. 157-2 ("FSP SFAS 157-2"), "Effective Date for FASB Statement No. 157." This FSP permits the delayed application of SFAS No. 157, "Fair Value Measurements," ("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 FSP SFAS 157-2 for non-financial assets and liabilities that are recognized or disclosed on a non-recurring basis.

In March 2008, the FASB issued SFAS No. 161 ("SFAS 161"), "Disclosures about Derivative Instruments and Hedging Activities, an amendment of FASB Statement No. 133." SFAS 161 requires enhanced disclosures about a company's derivative and hedging activities. SFAS 161 is effective for financial statements issued for fiscal years beginning after December 15, 2008. The Company is currently evaluating the impact of the adoption of the enhanced disclosures requirements of SFAS 161 and does not expect the adoption to have a material impact on its consolidated financial statements.

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In April 2008, the FASB issued FSP SFAS No. 142-3 (“FSP SFAS 142-3”), “Determination of the Useful Life of Intangible Assets.” 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 No. 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 141R , “Business Combinations” and other GAAP. FSP SFAS 142-3 is effective for the Company beginning 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.

In May 2008, the FASB issued SFAS No. 162 (“SFAS 162”), “The Hierarchy of Generally Accepted Accounting Principles,” which becomes effective 60 days following the SEC’s approval of the Public Company Accounting Oversight Board (“PCAOB”) amendments to U.S. 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 GAAP. This standard is not expected to have an impact on the Company’s consolidated financial position, results of operations or cash flows.

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.

During the quarter ended December 31, 2008, the Company entered into foreign currency forward contracts to buy U.S. dollars at fixed intervals in the retail market in an over-the-counter environment. As of December 31, 2008, the

Company had foreign currency forward contracts to sell 0.7 million Euros and 100,000 British pounds in exchange for approximately $1.1 million U.S. dollars maturing in January through March 2009. The counterparty to these contracts is UBS AG located in Switzerland. The Company’s foreign currency forward contract valuation inputs are based on quoted prices and quoted pricing intervals from public data and do not involve management judgment. Accordingly, the Company has classified this outstanding foreign currency forward contract within Level 2 of the fair value hierarchy and has recorded the fair value of the contract in other current assets and accrued liabilities on its condensed consolidated balance sheet as of December 31, 2008. The Company recorded a net unrealized loss of approximately $11,000 for the three months ended December 31, 2008.

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The following table presents assets and liabilities measured at fair value on a recurring basis at December 31, 2008 (in thousands):

	Level 1	Level 2	Level 3	Total
Assets:				
Money market funds	$ 6,722	$ -	$ -	$ 6,722
Foreign currency forward contracts	-	4	-	4
	$ 6,722	$ 4	$ -	$ 6,726
Liabilities:				
Foreign currency forward contracts	$ -	$ 15	$ -	$ 15

The Company's other financial liabilities that are required to be carried at fair value at December 31, 2008 consisted of the Swiss pension plan obligation, which was not material.

Note 4 — Balance Sheet Components

Inventories

Inventories consisted of the following (in thousands):

	December 31, 2008	March 31, 2008
Raw materials	$ 2,139	$ 2,154
Work-in-progress	1,852	1,667
Finished goods	3,432	3,002
Consigned inventory	4,987	4,331
Inventory held by distributors	-	341
	$ 12,410	$ 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 purchased by the customer, generally when used in a medical procedure.

Inventory held by distributors at March 31, 2008 consisted of $273,000 in inventory held by the Company's Latin American distributors (see Note 2 for more details) and $68,000 in inventory held by the Company's Chinese distributor. As of December 31, 2008, there was no inventory held by distributors.

Property and equipment, net

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

March 31,

	December 31, 2008	2008
Computer equipment and software	$ 2,016	$ 1,728
Furniture, fixtures and equipment	7,143	5,403
Leasehold improvements	2,120	1,010
Construction in progress	459	447
Total cost	11,738	8,588
Less accumulated depreciation and amortization	(4,372)	(3,303)
	$ 7,366	$ 5,285

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Goodwill

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

	December 31, 2008	March 31, 2008
Balance beginning of year	$ 8,549	$ 5,552
Addition related to earn-out payment associated with acquisition of Neurologic UK Ltd	457	2,997
Foreign currency translation	(2,119)	-
Balance end of period	$ 6,887	$ 8,549

All of the Company's goodwill has been allocated to the United Kingdom business segment.

Intangible assets, net

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

		Gross Carrying Amount			Accumulated Amortization				Net	
	Useful Life (Years)	March 31, 2008	Foreign currency translation	December 31, 2008	March 31, 2008	(Additions)	Foreign currency translation	December 31, 2008	December 31, 2008	March 31, 2008
Existing process technology	7	$ 4,590	$ -	$ 4,590	$ (874)	$ (492)	$ -	$ (1,366)	$ 3,224	$ 3,716
Distribution agreements	5	2,300	(454)	1,846	(1,164)	(347)	301	(1,210)	636	1,136
Capitalized license fee	7	1,565	-	1,565	(336)	(168)	-	(504)	1,061	1,229
Patents - microcoil	10	1,100	-	1,100	(880)	(82)	-	(962)	138	220
Non-compete agreements	6	700	(138)	562	(294)	(88)	75	(307)	255	406
Customer relationships	5	900	(178)	722	(454)	(136)	117	(473)	249	446
		$ 11,155	$ (770)	$ 10,385	$ (4,002)	$ (1,313)	$ 493	$ (4,822)	$ 5,563	$ 7,153

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

	Three months ended December 31,		Nine months ended December 31,	
	2008	2007	2008	2007

Cost of goods sold	$ 220	$ 234	$ 660	$ 755
Operating expenses	220	217	653	650
	$ 440	$ 451	$ 1,313	$ 1,405

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

For Years Ended March 31,	Amortization
2009 (remaining 3 months)	$ 399
2010	1,597
2011	1,215
2012	924
2013	879
Thereafter	549
	$ 5,563

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Accruals

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

	December 31, 2008	March 31, 2008
Accrued bonuses	$ 2,053	$ 2,642
Accrued salaries	670	1,071
Accrued vacation	1,943	1,750
Accrued commissions	453	1,660
Accrued payroll taxes	497	807
	$ 5,616	$ 7,930

Accrued liabilities consisted of the following (in thousands):

	December 31, 2008	March 31, 2008
Deferred gain from Merit Medical System, Inc. transaction	$ 1,862	$ 340
Milestone payment to The Cleveland Clinic Foundation	1,500	500
Professional fees	478	1,715
VAT payable	427	560
Other development costs	285	288
Accrued travel and entertainment	271	492
Biotronik AG development costs	166	443
Deferred revenue from Goodman Co., Ltd. distribution agreement	162	113
Earn-out payment in connection with acquisition of Neurologic UK Ltd acquistion	-	2,997
Earn-out payment in connection with acquisition of VasCon, LLC	-	378
Other	1,788	1,605
	$ 6,939	$ 9,431

On January 31, 2008, the Company entered into an Asset Purchase and Supply Agreement (the “Merit Agreement”) with Merit Medical Systems, Inc. (“Merit”) pursuant to which the Company sold its non-neurological cardiac and peripheral catheter assets and technology (the “Merit Transaction”). The majority of the assets sold were originally acquired by the Company in November 2006 in connection with its purchase of VasCon, LLC (“VasCon”). Pursuant to the Merit Agreement, the Company received an up-front payment of $1.5 million and received an additional payment of $1.5 million in December 2008 upon the completion of its obligation to help Merit build a production line for coronary guide catheters and get it fully operational. Though certain elements of this transaction (namely the acquired assets and licensing rights, and the production line assistance for coronary guide catheters) have been delivered as of December 31, 2008, the Company is still obligated to deliver the regulatory documentation and production line assistance for the peripheral guiding sheaths and/or cardiovascular microcatheters. The Company anticipates that the remaining obligations will be completed in the second quarter of fiscal 2010. Because the Company lacks the ability to separate the multiple obligations (elements) of this transaction, the up-front payment of $1.5 million and the

additional payment of $1.5 million, net of direct and incremental costs incurred and the net book value of assets transferred to Merit, have been deferred until such time as all elements of the transaction are delivered.

Other non-current liabilities

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

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	December 31, 2008	March 31, 2008
Contingent purchase price	$ 1,218	$ 1,218
Deferred revenue from Goodman Co., Ltd. distribution agreement	197	281
Swiss pension plan obligation	77	82
Milestone payment to The Cleveland Clinic Foundation	-	1,000
Other non-current liabilities	183	173
	$ 1,675	$ 2,754

At the acquisition date of VasCon, the fair value of the net assets acquired exceeded the purchase consideration resulting in the negative goodwill of $1.6 million. Because the acquisition involves contingent consideration that may exceed the negative goodwill amount, the negative goodwill has been recorded as a contingent purchase price and is being reduced by any earned contingent consideration of up to $10.0 million that will be paid over 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.

Note 5— Line of Credit

On November 5, 2008, the Company entered into a credit agreement with Wells Fargo Bank to provide the Company with a revolving line of credit (the “Credit Agreement”). The Credit Agreement provides for maximum borrowings in an amount up to $15 million. If borrowings under the Credit Agreement exceed $7.5 million, all borrowings are subject to a borrowing base which is based on eligible accounts receivable. Borrowings are collateralized by a first priority security interest in all of the Company’s assets (except for certain permitted liens that are senior to the Wells Fargo Bank’s security interest). At the Company’s option, borrowings bear interest at either 2.25% over the bank’s prime rate or 3.50% over the one-month, two-month or three-month LIBOR. The Credit Agreement requires that the Company comply with certain financial and other covenants for borrowings to be permitted. The more significant financial covenants include (i) maintaining a minimum modified quick ratio and (ii) achieving not more than a certain amount of loss through December 31, 2008, and thereafter a minimum profitability, in each case excluding certain non-cash items. The maturity date of the Credit Agreement has been extended to February 1, 2010. At December 31, 2008, the Company had outstanding borrowings of $2.5 million under the line of credit, and was in compliance with all covenants of the Credit Agreement. The interest rate on the borrowings as of December 31, 2008 was 5.5%.

Note 6 — 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 and nine months ended December 31, 2008, the Company recorded an income tax benefit of approximately $367,000 and $472,000, respectively. The income tax benefit for the three months ended December 31, 2008 includes an income tax benefit of $174,000 related to operating losses for its Swiss subsidiary, and a non-current income tax benefit of approximately $193,000 for the tax effect of the amortization related to the identifiable intangible assets acquired in the Neurologic UK Limited (“Neurologic”) transaction which is not deductible for tax purposes and the tax benefit of operating losses for its United Kingdom subsidiary. The income tax benefit for the nine months ended December 31, 2008 includes an income tax benefit of $106,000 related to operating losses for its Swiss subsidiary, and a non-current tax benefit of approximately $366,000

for the tax effect of the amortization related to the identifiable intangible assets acquired in the Neurologic transaction which is not deductible for tax purposes and the tax benefit from 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, and the state and 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 September 30, 2008 to offset its federal and state deferred tax assets.

Since the adoption 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 December 31, 2008, the Company had no accrued interest or penalties related to tax contingencies.

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Note 7 — 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.

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

On September 22, 2008, the Company entered into a Settlement and License Agreement (the "Settlement and License Agreement") with Boston Scientific Corporation and Target Therapeutics, Inc., a subsidiary of Boston Scientific Corporation (collectively "Boston Scientific") and a Settlement and Release Agreement (the "Settlement and Release Agreement") with The Regents of the University of California (the "Regents") in order to resolve pending patent litigation between Boston Scientific and the Company (the "Patent Litigation"). On October 8, 2008, the Court entered an order dismissing the Patent Litigation with prejudice. The Patent Litigation is described in detail in the Company's prior filings with the SEC.

Under the Settlement and License Agreement, the Company and Boston Scientific agreed to cross license certain patents asserted in the Patent Litigation and release all claims (as defined in the Settlement and License Agreement) arising prior to the effective date (as defined in the Settlement and License Agreement) to which the rights, licenses, releases, and covenants expressly granted under the Settlement and License Agreement would be a complete defense had such claims arisen on or after the effective date. The Settlement and License Agreement includes a mutual release of claims and covenants not to sue with respect to certain specified patents. Boston Scientific also covenants not to sue end users of the Company's products for claims of infringement of specified patents.

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In connection with the Settlement and License Agreement, the Company entered into the Settlement and Release Agreement with the Regents. The Settlement and Release Agreement provided for the cash payment of approximately $1.7 million to the Regents in exchange for a mutual release of claims and a mutual covenant not to sue with respect to certain specified patents. The Regents also agreed not to sue end users of the Company's products for claims under the patents owned by the Regents and exclusively licensed to Boston Scientific and asserted by Boston Scientific in the Patent Litigation against the Company. The Company made the cash payment to the Regents on September 24, 2008.

The foregoing discussion of material terms does not constitute a complete summary of the terms of the Settlement and License Agreement and Settlement and Release Agreement, and reference is made to the Settlement and License Agreement and Settlement and Release Agreement which are filed as exhibits of Form 10-Q for the quarter ended September 30, 2008.

Note 8 — 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 December 31, 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 December 31, 2008, there were no outstanding options under the 1996 Plan and 1,047,431 outstanding options under the 1998 Plan. As of December 31, 2008, there were 4,274,421 remaining shares reserved for issuance under the 2005 Plan, of which 1,259,622 were available for grant, 3,011,466 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 December 31, 2008, there were 628,371 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 and nine months ended December 31, 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:

	Three months ended December 31,		Nine months ended December 31,	
	2008	2007	2008	2007
Employee Stock Option Plans				
Expected term (in years)	6	6	6	6
Volatility	40%	41%	35%	41%
Risk-free interest rate	2.9%	4.0%	3.2%	4.4%
Expected dividend yield	0%	0%	0%	0%
Weighted average fair value at date of grant	$ 4.89	$ 8.25	$ 4.65	$ 9.60
Employee Stock Purchase Plan				
Expected term (in years)	0.5	0.5	0.5	0.5
Volatility	41%	44%	45%	44%
Risk-free interest rate	1.9%	3.8%	2.5%	4.2%
Expected dividend yield	0%	0%	0%	0%

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The fair value of each purchase right granted under the Company's Purchase Plan during the three and nine months ended December 31, 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 December 31,		Nine months ended December 31,	
	2008	2007	2008	2007
Cost of goods sold	$ 188	$ 103	$ 450	$ 310
Research and development	95	151	435	379
Sales and marketing	272	379	1,112	932
General and administrative	642	651	2,310	1,737
	$ 1,197	$ 1,284	$ 4,307	$ 3,358

Additionally, approximately $25,000 in stock-based compensation expense related to SFAS 123R has been released from inventory for the nine months ended December 31, 2008 as compared to $181,000 that has been capitalized in inventory for the nine months ended December 31, 2007.

As of December 31, 2008, there was approximately $11.9 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 2.4 years for employee stock options and 0.5 years for restricted stock units.

Stock-based compensation expense recognized for the three months ended December 31, 2008 and 2007 related to the amortization of deferred stock-based compensation was $0 and $40,000, respectively. For the nine months ended December 31, 2008 and 2007, the amortization of deferred stock-based compensation was $0 and $139,000, respectively. The Company had fully recognized amortization of deferred stock-based compensation in the fourth quarter ended March 31, 2008.

Stock-based compensation expense recognized for the three months ended December 31, 2008 and 2007 related to non-employee options was $0 and ($2,000), respectively. For the nine months ended December 31, 2008 and 2007, stock-based compensation expense recognized related to non-employee options was $0 and $4,000, respectively.

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

	Three months ended December 31,		Nine months ended December 31,	
	2008	2007	2008	2007
Cost of goods sold	$ 188	$ 105	$ 450	$ 324
Research and development	95	151	435	379
Sales and marketing	272	382	1,112	943
General and administrative	642	684	2,310	1,855
	$ 1,197	$ 1,322	$ 4,307	$ 3,501

General stock option information

The following table sets forth the summary of stock options activity for the nine months ended December 31, 2008:

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	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	677	$ 11.64		
Options exercised	(70)	$ 8.93		
Options forfeited	(179)	$ 15.84		
Options expired	(25)	$ 10.60		
Options outstanding at December 31, 2008	4,059	$ 12.75	7.5	$ 7,685
Options exercisable at December 31, 2008	2,281	$ 10.88	6.6	$ 7,030

The total aggregate intrinsic value of options exercised during the three months ended December 31, 2008 and 2007 was $22,000 and $567,000, respectively. For the nine months ended December 31, 2008 and 2007, the total aggregate intrinsic value of options exercised was $299,000 and $3.3 million, respectively. The closing market value per share of the Company’s common stock as of December 31, 2008 was $11.61 per share as reported by The NASDAQ Stock Market.

The following table sets forth the summary of restricted stock units activity for the nine months ended December 31, 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 December 31, 2008	4	$ -	0.5	$ 39

Note 9 — 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 December 31,		Nine months ended December 31,	
	2008	2007	2008	2007
United States	$ 9,889	$ 7,942	$ 28,906	$ 24,389
Japan	1,477	2,989	6,302	4,128
United Kingdom	1,715	2,333	5,903	6,853
Rest of the world	5,241	5,079	16,327	14,125
	$ 18,322	$ 18,343	$ 57,438	$ 49,495

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

	December 31, 2008	March 31, 2008
United States	$ 7,041	$ 4,907
United Kingdom	75	124
Rest of the world	250	254
	$ 7,366	$ 5,285

The Company identifies its operating segments based on how management views and evaluates the Company's operations, which are 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 European (excluding the United Kingdom) and 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 December 31,		Nine months ended December 31,	
	2008	2007	2008	2007
Revenues:				
Americas	$ 10,788	$ 9,077	$ 32,728	$ 27,015
Europe (excluding the United Kingdom)	3,949	3,741	11,446	10,611
United Kingdom	1,715	2,333	5,903	6,853
Asia Pacific	1,870	3,192	7,361	5,016
	$ 18,322	$ 18,343	$ 57,438	$ 49,495
Gross Profit:				
Americas	$ 8,170	$ 6,730	$ 24,601	$ 21,794
Europe (excluding the United Kingdom)	2,745	2,687	8,116	7,365
United Kingdom	1,333	1,795	4,651	5,232
Asia Pacific	1,297	2,082	5,086	3,169
	$ 13,545	$ 13,294	$ 42,454	$ 37,560

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

	December 31, 2008	March 31, 2008
Americas	$ 41,856	$ 52,043
Europe (excluding the United Kingdom)	7,899	7,265

United Kingdom		9,757		13,024
	$	59,512	$	72,332

Note 10 — Subsequent Event

The Company merged Micrus Design Technology, Inc. into Micrus Endovascular Corporation effective January 1, 2009.

On February 3, 2009, the Company amended the Credit Agreement with Wells Fargo Bank extending the maturity date to February 1, 2010.

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

Forward-Looking Statements

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 SEC. In addition to current and historical information, this Quarterly Report on Form 10-Q contains forward-looking statements as defined in Section 27.A of the Securities Act of 1933, as amended, and section 21E of the Securities Exchange Act of 1934, as amended that involve risks and uncertainties. These statements can, in some cases, be identified by the use of terms such as "may," "will," "expects," "anticipates," "estimates," "predicts," "continues," "plans," "believes," "projects," "should "intends" or statements concerning "potential" or "opportunity," and any variations thereof, comparable terminology or the negative thereof. 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. We do not intend, and undertake no obligation, to update any of our forward-looking statements after the date of this Report to reflect actual results or future events or circumstances.

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, balloon catheters, 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. We have also entered into an exclusive distribution agreement 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, balloon catheters and accessories for use with our microcoils, which accounted for approximately 7% and 6% of our revenues in the third quarter and the first nine months of fiscal 2009, 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 fluctuate depending on the level of sales to distributors and in those quarters in which we initiate sales of new products or product lines, or enter new geographic territories.

Our product development efforts are primarily focused on expanding our product offerings for the hemorrhagic and ischemic stroke markets. In August 2004, we introduced our Cerecyte® microcoil product line and we have launched ten new products in the last 24 months, including microcoils, stents, microcatheters, guidewires and balloon catheters. During the first nine months of fiscal 2009, we launched the Neuropath® guide catheter, which combines robust proximal support with a highly flexible and visible tip facilitating atraumatic vascular access. The Neuropath guide catheter is used as a conduit for delivery of the microcatheter or other devices such as coils to the aneurysm. We intend to continue to pursue this non-coil product line expansion with the goal of increasing our revenue opportunity per procedure. We also launched Cerecyte and stretch resistant versions of our DeltaPaq™ microcoil system for the treatment of cerebral aneurysms. Our DeltaPaq microcoil system is designed to enable the physicians to achieve greater coil packing density within the aneurysm which may reduce the rate of recanalization and the need for re-treatment. The DeltaPaq microcoil system supplements our framing and finishing coils in the filling segment of the coil market. Additionally, we launched the 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 have received U.S. Food and Drug Administration conditional approval of our PHAROS Vitesse Intracranial Stent Study for Ischemic Therapy ("VISSIT"). The VISSIT study is the first industry sponsored randomized prospective clinical trial designed to compare the clinical outcomes between patients who are stented for intracranial ischemic stenosis versus treated with medical therapy. We are in the process of initiating study sites in the United States, Europe and China.

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We intend to continue to expand our direct sales force in North America and Europe as necessary and increase our presence in 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 $6.3 million and $4.1 million in the first nine months of fiscal 2009 and 2008, respectively. We will begin selling our products in China upon receiving regulatory approvals. The timing of these approvals is 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 nine months of fiscal 2009. We do not expect to recognize revenues from sales to China during this fiscal year.

We currently anticipate that the expansion of our product line and our further expansion into the Asian market will be primarily funded with our currently available cash and cash expected to be generated from operations.

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 $57.4 million in the first nine months 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 $11.6 million in the first nine months of fiscal 2009. As of December 31, 2008, we had cash and cash equivalents of $14.1 million. We believe that our current cash position and the cash expected to be generated from operations, together with the funds available under our credit facility (subject to compliance with the conditions and covenants of the credit agreement) (see Part I, Item 2—Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources), 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 December 31, 2008, we had an accumulated deficit of $83.0 million.

Results of Operations

The following table sets forth the results of our operations, expressed as percentages of revenues, for the three and nine months ended December 31, 2008 and 2007:

	Three months ended December 31,		Nine months ended December 31,	
	2008	2007	2008	2007
Consolidated Statements of Operations Data:				
Revenues	100%	100%	100%	100%
Cost of goods sold	26%	28%	26%	24%
Gross profit	74%	72%	74%	76%
Operating expenses:				

Research and development	13%	30%	14%	21%
Sales and marketing	38%	41%	40%	43%
General and administrative	32%	33%	38%	36%
Total operating expenses	83%	104%	92%	100%
Loss from operations	(9%)	(32%)	(18%)	(24%)
Interest income	0%	2%	0%	2%
Interest expense	0%	0%	0%	0%
Other income (expense), net	(6%)	0%	(3%)	1%
Loss before income taxes	(15%)	(30%)	(21%)	(21%)
Provision (benefit) for income taxes	(2%)	1%	(1%)	0%
Net loss	(13%)	(31%)	(20%)	(21%)

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Three Months Ended December 31, 2008 and 2007

Revenues

	Three months ended December 31,		Change	
	2008	2007	$	%
	(Dollars in thousands)			
Americas	$ 10,788	$ 9,077	$ 1,711	19%
Europe (excluding the United Kingdom)	3,949	3,741	208	6%
United Kingdom	1,715	2,333	(618)	(26%)
Asia Pacific	1,870	3,192	(1,322)	(41%)
	$ 18,322	$ 18,343	$ (21)	(0%)

Our revenues are derived primarily from sales of our microcoils used in the treatment of cerebral vascular diseases. Our total revenues in the third quarter of fiscal 2009 remained flat as compared with the third quarter of fiscal 2008. Revenues from the Americas increased 19% to $10.8 million and revenues from Europe (excluding the United Kingdom) increased 6% to $3.9 million, both compared with the third quarter of fiscal 2008. Revenues from the United Kingdom decreased 26% to $1.7 million as compared with the third quarter of fiscal 2008, primarily due to the unfavorable impact on revenues from the weakening of the British pound against the U.S. dollar and to a lesser extent a decline in procedure volume. Revenues from Asia Pacific decreased to $1.9 million in the third quarter of fiscal 2009 and included product sales to our distributor in Japan of $1.5 million, compared with revenues of $3.2 million in the third quarter of fiscal 2008 which included sales to our distributor in Japan of $3.0 million. Asia Pacific sales in the prior year third quarter were favorably impacted by increased sales to our distributor in Japan as a result of the regulatory approval in Japan of our stretch resistant microcoils in December 2007. We will also begin selling our products in China upon receiving regulatory approvals. We do not expect to recognize revenues from sales to China during this fiscal year.

Revenues from embolic coils decreased 3% to $16.9 million for the third quarter of fiscal 2009 as compared to the third quarter of fiscal 2008 primarily due to the unfavorable impact of foreign currency exchange rates, most notably the weakening of the British pound against the U.S. dollar, and lower distributor sales, particularly in Japan. In the third quarter of fiscal 2009, approximately 32% of our revenues were denominated in currencies other than the U.S. dollar. Revenues from our non-embolic products increased 56% to $1.4 million for the third quarter of fiscal 2009 compared with revenues of $0.9 million in the third quarter of fiscal 2008. Sales of non-embolic products during the third quarter of fiscal 2009 were approximately 7% of total revenues, which is a quarterly record due in part to the introduction of our Neuropath guide catheter. The sales contribution of our non-embolic products is expected to accelerate due to the launch of our Ascent balloon catheter next quarter. 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 including our launch of the next-generation DeltaPaq microcoil system, and an occlusion balloon catheter family.

New products continue to represent an important component of our growth strategy, with 26% of our revenues in the third quarter of fiscal 2009 coming from products introduced in the past 24 months. Among these, our Cashmere microcoil line represented 15% of the quarter's total. We are also pleased with the strong reception for our newly

launched DeltaPaq microcoil system, which comprised 8% of third quarter revenues. With the launch of the Ascent balloon catheter and the Neuropath guide catheter, we are now in a position to capture a significantly greater portion of hemorrhagic procedure revenues.

Gross Profit

	Three months ended December 31,		Change	
	2008	2007	$	%
	(Dollars in thousands)			
Cost of goods sold	$ 4,777	$ 5,049	$ (272)	(5%)
Gross profit	$ 13,545	$ 13,294	$ 251	2%

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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, amortization of capitalized license technology associated with our PHAROS stent product and royalties related to certain access device products. The decrease in cost of goods sold during the third quarter of fiscal 2009 as compared to the third quarter of fiscal 2008 was primarily due to increased manufacturing efficiencies. Additionally, the cost of goods sold in the third quarter of fiscal 2008 included an impairment of excess inventory primarily related to slower consignment inventory turns.

Gross margin was 74% in the third quarter of fiscal 2009 and 72% in the third quarter of fiscal 2008. The increase was primarily due to higher sales to direct customers. We expect our gross margin to fluctuate in future periods based on the mix of our product sales and the level of distributor sales.

Operating Expenses

Research and Development

	Three months ended December 31,		Change	
	2008	2007	$	%
	(Dollars in thousands)			
Research and development	$ 2,403	$ 5,553	$ (3,150)	(57%)

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 decreased in the third quarter of fiscal 2009 compared to the third quarter of fiscal 2008 primarily due to a $3.0 million charge in the third quarter of fiscal 2008 for in-process research and development in connection with the acquisition of ReVasc Technologies, Inc. to obtain the rights to pre-regulatory approved revascularization technology.

Sales and Marketing

	Three months ended December 31,		Change	
	2008	2007	$	%
	(Dollars in thousands)			
Sales and marketing	$ 6,942	$ 7,432	$ (490)	(7%)

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 decreased in the third quarter of fiscal 2009 compared to the third quarter of fiscal 2008 primarily due to a decrease of $220,000 in personnel costs due to reduced marketing headcount, a decrease of $193,000 related to consulting fees, a decrease of $163,000 in sales incentives compensation and a decrease of $109,000 in stock-based compensation

expense. These decreases were partially offset by an increase of $295,000 in costs associated with the launch of new products.

General and Administrative

	Three months ended December 31,		Change	
	2008	2007	$	%
	(Dollars in thousands)			
General and administrative	$ 5,892	$ 6,174	$ (282)	(5%)

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General and administrative expenses consist primarily of compensation and related costs for finance, human resources, regulatory, insurance, and professional services. Professional services principally relate to fees for outside legal, audit and Sarbanes Oxley compliance. General and administrative expenses decreased in the third quarter of fiscal 2009 compared to the third quarter of fiscal 2008 primarily due to a decrease of $574,000 related to legal fees resulting from the settlement of the patent litigation with Boston Scientific and the conclusion of the United States Department of Justice ("DOJ") monitorship. This decrease was partially offset by an increase of $234,000 related to higher finance and administrative personnel costs due to increased headcount.

Other Income (Expense), Net

	Three months ended December 31,		Change	
	2008	2007	$	%
	(Dollars in thousands)			
Interest income	$ 49	$ 304	$ (255)	(84%)
Interest expense	(10)	-	(10)	(100%)
Other income (expense), net	(1,006)	67	(1,073)	(1,601%)
Total other income (expense)	$ (967)	$ 371	$ (1,338)	(361%)

Total other income (expense) consists primarily of interest income and foreign exchange gains and losses. Total other income (expense) decreased by $1.3 million in the third quarter of fiscal 2009 compared to the third quarter of fiscal 2008 primarily due to foreign exchange losses resulting from the remeasurement of foreign currency transactions, most notably the impact of the weakening of the British pound against the U.S. dollar and a decrease in interest income resulting from lower average cash and cash equivalents balances earning interest and a decline in interest rates.

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 December 31, 2008, we recorded an income tax benefit of approximately $367,000. The income tax benefit for the three months ended December 31, 2008 includes an income tax benefit of $174,000 related to operating losses for our Swiss subsidiary and a non-current tax benefit of approximately $193,000 for the tax effect of the amortization related to the identifiable intangible assets acquired in the Neurologic transaction which is not deductible for tax purposes, and the tax benefit from 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, and the state and 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 December 31, 2008 to offset our federal and state deferred tax assets.

Since the adoption 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 December 31, 2008, we had no accrued interest or penalties related to tax contingencies.

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Nine Months Ended December 31, 2008 and 2007

Revenues

(Dollars in thousands)	Nine months ended December 31, 2008	Nine months ended December 31, 2007	Change $	Change %
	(Dollars in thousands)			
Americas	$ 32,728	$ 27,015	$ 5,713	21%
Europe (excluding the United Kingdom)	11,446	10,611	835	8%
United Kingdom	5,903	6,853	(950)	(14%)
Asia Pacific	7,361	5,016	2,345	47%
	$ 57,438	$ 49,495	$ 7,943	16%

The overall increase in revenues in the first nine months of fiscal 2009 compared to the first nine months of fiscal 2008 was primarily due to an increase in the number of embolic and non-embolic products sold during this period. Revenues from the Americas increased 21% to $32.7 million and revenues from Europe (excluding the United Kingdom) increased 8% to $11.4 million, both compared with the first nine months of fiscal 2008. Revenues from the United Kingdom decreased 14% to $5.9 million as compared with the first nine months of fiscal 2008, primarily due to the unfavorable impact on revenues from the weakening of the British pound against the U.S. dollar as well as a decline in procedure volume. Revenues from Asia Pacific increased to $7.4 million in the first nine months of fiscal 2009 and included product sales to our distributor in Japan of $6.3 million, compared with revenues of $5.0 million in the first nine months of fiscal 2008 which included sales to our distributor in Japan of $4.1 million. 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, both of which had a favorable impact on product sales to our distributor in Japan in the first nine months of fiscal 2009. We will also begin selling our products in China upon receiving regulatory approvals. We do not expect to recognize revenues from sales to China this fiscal year. Revenues from Latin America increased to $2.5 million in the first nine months of fiscal 2009 compared with revenues of $1.2 million in the first nine months of fiscal 2008 due to an overall increase in product sales to our distributors in the region and 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 to our Condensed Consolidated Financial Statements included in Part 1, Item 1 of this Quarterly Report). As a result of a change in our revenue recognition policy for sales made to Latin American distributors, we recognized approximately $0.7 million of Latin American deferred revenue in the first nine months of fiscal 2009.

Revenues from embolic coils increased 15% to $53.8 million for the first nine months of fiscal 2009 as compared to the first nine months of fiscal 2008 primarily due to the increased market penetration of the Cashmere™ microcoil system launched in the third quarter of fiscal 2008, the launch of our DeltaPaq microcoil system and an increase in distributor sales, particularly in Japan and Latin America. Revenues from our non-embolic products increased 40% to $3.5 million for the first nine months of fiscal 2009 compared with revenues of $2.5 million in the first nine months of fiscal 2008. Products introduced in the past two years comprised 19% of our revenues in the first nine months of fiscal 2009.

Gross Profit

	Nine months ended December 31,		Change	
	2008	2007	$	%
	(Dollars in thousands)			
Cost of goods sold	$ 14,984	$ 11,935	$ 3,049	26%
Gross profit	$ 42,454	$ 37,560	$ 4,894	13%

The increase in cost of goods sold during the first nine months of fiscal 2009 as compared to the first nine months of fiscal 2008 was primarily related to the increase in sales of our products.

Gross margin was 74% in the first nine months of fiscal 2009 and 76% in the first nine months of fiscal 2008. The decrease was primarily due to higher sales to distributors at lower margins particularly 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.

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Operating Expenses

Research and Development

	Nine months ended December 31,		Change	
	2008	2007	$	%
	(Dollars in thousands)			
Research and development	$ 8,253	$ 10,135	$ (1,882)	(19%)

Research and development expenses decreased in the first nine months of fiscal 2009 compared to the first nine months of fiscal 2008 primarily due to a $3.0 million charge in the third quarter of fiscal 2008 for in-process research and development in connection with the acquisition of ReVasc to obtain the rights to pre-regulatory approved revascularization technology. This decrease was partially offset by higher personnel costs of $1.0 million related to increased headcount and increased salaries for current employees, and an increase of $350,000 related to materials and supplies purchased for engineering projects.

Sales and Marketing

	Nine months ended December 31,		Change	
	2008	2007	$	%
	(Dollars in thousands)			
Sales and marketing	$ 23,021	$ 21,087	$ 1,934	9%

Sales and marketing expenses increased in the first nine months of fiscal 2009 compared to the first nine months of fiscal 2008 primarily due to an increase of $0.9 million in travel and personnel costs resulting from an increase in sales and marketing personnel in North America, Europe and Asia, an increase of $0.7 million in sales incentives compensation resulting from the higher level of sales and changes in the sales compensation structure, as well as an increase of $171,000 in stock-based compensation expense.

General and Administrative

	Nine months ended December 31,		Change	
	2008	2007	$	%
	(Dollars in thousands)			
General and administrative	$ 21,818	$ 18,076	$ 3,742	21%

General and administrative expenses increased in the first nine months of fiscal 2009 compared to the first nine months of fiscal 2008 primarily due to the settlement cost of approximately $1.7 million in connection with the patent litigation with Boston Scientific, an increase of $2.0 million related to higher finance and administrative personnel costs due to increased headcount and salary increases for current employees, an increase of $458,000 in stock-based compensation expense and an increase of $208,000 in travel expenses. These increases were partially offset by a

decrease of $0.8 million in legal fees resulting from the settlement of the patent litigation with Boston Scientific and the conclusion of the DOJ monitorship.

Other Income (Expense), Net

	Nine months ended December 31,		Change	
	2008	2007	$	%
	(Dollars in thousands)			
Interest income	$ 239	$ 1,015	$ (776)	(76%)
Interest expense	(14)	(2)	(12)	600%
Other income (expense), net	(1,689)	427	(2,116)	(496%)
Total other income (expense)	$ (1,464)	$ 1,440	$ (2,904)	(202%)

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Total other income (expense) decreased by $2.9 million in the first nine months of fiscal 2009 compared to the first nine months of fiscal 2008 primarily due to foreign exchange losses resulting from the remeasurement of foreign currency transactions, most notably the impact of the weakening of the British pound against the U.S. dollar, and a decrease in interest income resulting from lower average cash and cash equivalent balances earning interest as well as a decline in interest rates.

Income Taxes

In the first nine months of fiscal 2009, we recorded an income tax benefit of approximately $472,000. The income tax benefit includes an income tax benefit of $106,000 related to net losses for our Swiss subsidiary, and a non-current tax benefit of approximately $366,000 for the tax effect of the amortization related to the identifiable intangible assets acquired in the Neurologic transaction which are amortized for tax purposes, in addition to the tax benefit from net operating losses for our United Kingdom subsidiary.

Liquidity and Capital Resources

	Nine months ended December 31,	
	2008	2007
	(in thousands)	
Cash flow activities:		
Net cash used in operating activities	$ (11,446)	$ (7,205)
Net cash used in investing activities	$ (4,832)	$ (3,782)
Net cash provided by financing activities	$ 3,651	$ 2,469

Since our inception, we have funded our operations primarily through issuances of stock and related warrants, and product sales. As of December 31, 2008, we had cash and cash equivalents of $14.1 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 operations, together with the funds available under our credit facility (subject to compliance with the conditions and covenants of the credit agreement) (see below), 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 $11.4 million during the first nine months of fiscal 2009 compared to $7.2 million during the first nine months of fiscal 2008. Net cash used in operating activities during the first nine months of fiscal 2009 resulted primarily from operating losses, an increase in finished goods and consigned inventory due to the launch of new products, a decrease in accounts payable due to the timing of payments made to our vendors, a decrease in accrued payroll and related expenses attributable primarily to the payment of fiscal 2008 employee cash bonuses in the first quarter of fiscal 2009 and lower accrued commissions and a decrease in other non-current liabilities primarily due to a reclass of an accrued milestone payments from long-term to short-term. These factors were partially offset by non-cash items such as stock-based compensation expense primarily due to SFAS 123R, deferred tax benefits and depreciation and amortization.

Net cash used in operating activities during the first nine months of fiscal 2008 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 the launch of new products and the buildup of finished goods inventory in anticipation of future sales upon regulatory approvals in Japan and an increase in accounts receivable resulting from an increase in the number of embolic and non-embolic products sold. These factors were partially offset by an increase in accrued liabilities primarily due to higher accrued legal fees and contributions to our employee stock purchase plan and other non-current liabilities due to accrued milestone payments to ReVasc, and non-cash items such as 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 investing activities was $4.8 million during the first nine months of fiscal 2009 compared to $3.8 million during the first nine months of fiscal 2008. Net cash used in investing activities during the first nine months of fiscal 2009 was related to the earn-out payment associated with the purchase of Neurologic and VasCon and the purchase of capital equipment, partially offset by proceeds from the sale of certain assets and technologies in connection with the Merit Medical Systems, Inc transaction.

Net cash used in investing activities during the first nine months of fiscal 2008 was related to the earn-out payment associated with the purchase of Neurologic and the purchase of capital equipment partially offset by proceeds from the sale of property and equipment.

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Net cash provided by financing activities was $3.7 million during the first nine months of fiscal 2009 compared to $2.5 million during the first nine months of fiscal 2008. Net cash provided by financing activities during the first nine months of fiscal 2009 consisted of proceeds from the exercise of stock options, the employee stock purchase plan, and borrowings under the line of credit with Wells Fargo Bank.

Net cash provided by financing activities during the first nine months of fiscal 2008 consisted of proceeds from the exercise of stock options and the employee stock purchase plan.

As discussed in Note 5 to our Condensed Consolidated Financial Statements included in Part 1, Item 1 of this Quarterly Report, on November 5, 2008 we entered into a Credit Agreement with Wells Fargo Bank to provide us with a revolving line of credit. The Credit Agreement provides for maximum borrowings in an amount up to $15 million. If borrowings under the Credit Agreement exceed $7.5 million, all borrowings are subject to a borrowing base which is based on eligible accounts receivable. The maturity date of the Credit Agreement has been extended to February 1, 2010. At December 31, 2008, we had outstanding borrowings of $2.5 million under the line of credit, and were in compliance with all covenants of the Credit Agreement.

To the extent that existing cash and cash generated from operations, together with the funds available under our credit facility (subject to compliance with the conditions and covenants of the Credit Agreement), 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 and reduce certain discretionary spending. Additional funds may not be available on terms favorable to us, or at all.

Critical Accounting Policies and Estimates

We prepare our consolidated financial statements in accordance with 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 February 2007, the FASB issued Statement of Financial Accounting Standard (“SFAS”) No. 159 (“SFAS 159”), “The Fair Value Option for Financial Assets and Financial Liabilities,” which expands opportunities to use fair value measurements in financial reporting and permits entities to choose to measure many financial instruments and certain other items at fair value. SFAS 159 became effective for us on April 1, 2008. The adoption of SFAS 159 did not have a material impact on our consolidated financial position, results of operations or cash flows.

In December 2007, the FASB issued SFAS No. 141R (“SFAS 141R”), “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. This provision will only impact our accounting for any acquisition on or after April 1, 2009.

In February 2008, the FASB issued FASB Staff Position (“FSP”) SFAS No. 157-2 (“FSP SFAS 157-2”), “Effective Date for FASB Statement No. 157.” This FSP permits the delayed application of SFAS No. 157, "Fair Value Measurements," (“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 FSP SFAS 157-2 for non-financial assets and liabilities that are recognized or disclosed on a non-recurring basis.

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In March 2008, the FASB issued SFAS No. 161 (“SFAS 161”), “Disclosures about Derivative Instruments and Hedging Activities, an amendment of FASB Statement No. 133.” SFAS 161 requires enhanced disclosures about a company’s derivative and hedging activities. SFAS 161 is effective for financial statements issued for fiscal years beginning after December 15, 2008. We are currently evaluating the impact of the adoption of the enhanced disclosures requirements of SFAS 161 and do not expect the adoption to have a material impact on our consolidated financial statements.

In April 2008, the FASB issued FSP SFAS No. 142-3 (“FSP SFAS 142-3”), “Determination of the Useful Life of Intangible Assets.” 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 No. 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 141R, “Business Combinations” and other 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 (“SFAS 162”), “The Hierarchy of Generally Accepted Accounting Principles,” which becomes effective 60 days following the SEC’s approval of the PCAOB amendments to U.S. 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 GAAP. This standard is not expected to have an impact on our consolidated financial position, results of operations or cash flows.

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 December 31, 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	$ 6,937	$ 1,057	$ 3,166	$ 1,069	$ 1,645
Purchase obligations	3,551	3,551	-	-	-
Minimum milestone payments to The Cleveland Clinic	1,500	1,500	-	-	-
Royalty payments to Vascular FX, LLC	1,250	250	750	250	-
Total	$ 13,238	$ 6,358	$ 3,916	$ 1,319	$ 1,645

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. These future earn-out payments will be paid over three years.

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.

We are required to pay Vascular FX, LLC a royalty equal to 25% of the greater of (i) the applicable aggregate mandatory minimum sales of $1.0 million or (ii) the actual net selling price of our deflectable catheter product. The royalty period is six years beginning in November 2007.

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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 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. The functional currency of our Swiss subsidiary is the Swiss franc. The functional currency of our UK subsidiary is the British pound. In Europe, our revenues are denominated in Swiss francs, Euros, British pounds 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 approximately $192,000 related to our loan with Micrus SA and an approximate $36,000 decrease in our comprehensive loss from our investment in Micrus SA as of December 31, 2008. A hypothetical 10% decline in the value of the British pound versus the U.S. dollar would cause us to recognize an approximate $463,000 increase in our comprehensive loss from our investment in Micrus UK as of December 31, 2008. A hypothetical 10% decline in the value of the Euro versus the Swiss franc would cause us to recognize a loss of approximately $248,000 based on our foreign denominated receivables as of December 31, 2008.

In the first nine months of fiscal 2009, approximately 32% 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.

During the quarter ended December 31, 2008, we entered into foreign currency forward contracts to buy U.S. dollars to minimize the impact of the currency movements on intercompany payables for our Micrus SA subsidiary. The use of foreign currency forward contracts allows us to offset exposure to rate fluctuations because the gains or losses incurred on the derivative instruments will offset, in whole or in part, losses or gains on the underlying foreign currency exposure. We use derivative instruments only for risk management purposes and do not use them for speculation or for trading.

As of December 31, 2008, we had outstanding foreign currency forward contracts to sell 0.7 million Euros for approximately $1.0 million, expiring through March 20, 2009, and to sell 100,000 British pounds for approximately $150,000, expiring through January 20, 2009. If we were to settle our Euro and British pound-based contracts at the reporting date, the net result would be an unrealized loss of approximately $11,000. A sensitivity analysis of changes in the fair value of our Euros and British pounds forward contracts at December 31, 2008 indicates that, if the U.S. dollar uniformly strengthened/ weakened by 10 percent against the Euros and British pounds, the fair value of these contracts would decrease/increase by $111,000, respectively.

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 December 31, 2008, our cash and cash equivalent balance was $14.1 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 $24,000 on an annual basis.

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 December 31, 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 over financial reporting

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 December 31, 2008 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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Part II — OTHER INFORMATION

Item 1. Legal Proceedings.

FCPA Investigation

See Note 7 to our Condensed Consolidated Financial Statements included in Part 1, Item 1 of this Quarterly Report for a discussion of the FCPA investigation we carried out in 2004 and our resulting agreement with the DOJ.

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

On September 22, 2008, we entered into a Settlement and License Agreement (the "Settlement and License Agreement") with Boston Scientific Corporation and Target Therapeutic, Inc., a subsidiary of Boston Scientific Corporation (collectively "Boston Scientific") and a Settlement and Release Agreement (the "Settlement and Release Agreement") with The Regents of the University of California (the "Regents") in order to resolve pending patent litigation between Boston Scientific and us (the "Patent Litigation"). On October 8, 2008, the Court entered an order dismissing the Patent Litigation with prejudice. The Patent Litigation is described in detail in our prior filings with the Securities and Exchange Commission (the "SEC").

Under the Settlement and License Agreement, we and Boston Scientific agreed to cross license certain patents asserted in the Patent Litigation and release all claims (as defined in the Settlement and License Agreement) arising prior to the effective date (as defined in the Settlement and License Agreement) to which the rights, licenses, releases, and covenants expressly granted under the Settlement and License Agreement would be a complete defense had such claims arisen on or after the effective date. The Settlement and License Agreement includes a mutual release of claims and covenants not to sue with respect to certain specified patents. Boston Scientific also covenants not to sue end users of our products for claims of infringement of specified patents.

In connection with the Settlement and License Agreement, we entered into the Settlement and Release Agreement with the Regents. The Settlement and Release Agreement provided for the cash payment of approximately $1.7 million within to the Regents in exchange for a mutual release of claims and a mutual covenant not to sue with respect to certain specified patents. The Regents also agreed not to sue end users of our products for claims under the patents owned by the Regents and exclusively licensed to Boston Scientific and asserted by Boston Scientific in the Patent Litigation against us. We made the cash payment to the Regents on September 24, 2008.

The foregoing discussion of material terms does not constitute a complete summary of the terms of the Settlement and License Agreement and Settlement and Release Agreement, and reference is made to the Settlement and License Agreement and Settlement and Release Agreement which are filed as exhibits of Form 10-Q for the quarter ended September 30, 2008.

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," "predict," "continues," "plans," "believes," or "projects," "should," "could," "would," "intends concerning "potential" or "opportunity," and 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:

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Current worldwide economic conditions may adversely affect our business, operating results and financial condition, as well as further decrease our stock price.

General worldwide economic conditions have experienced a downturn due to the effects of the subprime lending crisis, general credit market crisis, collateral effects on the finance and banking industries, concerns about inflation, slower economic activity, decreased consumer confidence, reduced corporate profits and capital spending, adverse business conditions and liquidity concerns. Our business is not immune. Some of the procedures that use our products are elective and therefore can be deferred by patients. In light of the current economic conditions, patients who do not have insurance covering the total cost of elective procedures may chose to defer or forego them. In addition, in the U.S. and other countries where healthcare coverage is heavily dependent on employment status, increasing numbers of patients may have no or reduced healthcare coverage.

The worldwide economic crisis also may have other adverse implications on our business. For example, our customers' and distributors' ability to borrow money from their existing lenders or to obtain credit from other sources to purchase our products may be impaired. Although we maintain allowances for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments and such losses have historically been within our expectations and the provisions established, we cannot guarantee that we will continue to experience the same loss rates that we have in the past, especially given the current turmoil in the worldwide economy. A significant change in the liquidity or financial condition of our customers could cause unfavorable trends in our receivable collections and additional allowances may be required, which could adversely affect our operating results. In addition, the worldwide economic crisis may adversely impact our suppliers' ability to provide us with materials and components, which could adversely affect our business and operating results. Like the stock prices of many other companies, our stock price has decreased substantially recently and if investors have concerns that our business, operating results and financial condition will be negatively impacted by a worldwide economic downturn, our stock price could further decrease.

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 nine months of fiscal 2009, a substantial portion of our product sales in the United States was to approximately 112 hospitals. 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 a preferable 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.

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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 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 $11.6 million and $10.1 million in the first nine months of fiscal 2009 and 2008, respectively. As of December 31, 2008, we had an accumulated deficit of $83.0 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;

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- stocking patterns for distributors;
- the development of new procedures to treat cerebral aneurysms;
- 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;
- our ability to develop new products or enhancements in a timely manner;
- our ability to obtain the necessary regulatory approvals for new products or product enhancements;

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- our ability to provide adequate training to potential users of our products;
- our ability to receive adequate reimbursement for our procedures;
- 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; and
- 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 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 United States and international laws and regulations related to our financial relationships with physicians and other healthcare providers. 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. While the Company has taken numerous steps to ensure compliance with these laws and regulations, they are subject to evolving interpretations, making it difficult to ensure compliance. If we are found to be in violation of any of these laws or regulations, we may face serious consequences, including civil and criminal penalties for the Company and its officers and directors, exclusion of our products from government-funded healthcare programs, termination of customer contracts, and reputational harm.

We operate 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.

In addition, most of our current and potential competitors are either large publicly traded or divisions or subsidiaries of large publicly traded companies, and they 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

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- 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 nine months of fiscal 2009, revenues from customers outside the United States represented approximately 50% 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 nine months of fiscal 2009, approximately 32% 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, British pounds 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 British pounds, 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 SA 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.

During the quarter ended December 31, 2008, we entered into foreign currency forward contracts to buy U.S. dollars to minimize the impact of the currency movements on intercompany payables for our Micrus SA subsidiary. We use derivative instruments only for risk management purposes and do not use them for speculation or for trading. Our hedging activities involve risk and may not limit our underlying exposure from currency fluctuations or minimize our net sales and earnings volatility associated with foreign currency exchange rate changes.

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.

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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.

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 and the cash to be generated from expected product sales, together with the funds available under our credit facility (subject to compliance with the conditions and covenants of the credit agreement) (see Part I, Item 2—Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources), 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:

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- 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 litigation that may arise from time to time;
- 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.

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.

We face a risk of non-compliance with certain financial covenants in our credit agreement with Wells Fargo Bank. If we are unable to meet the financial or other covenants under the credit agreement or negotiate future waivers or amendments of the covenants, an event of default would occur under the credit agreement, which would give Wells Fargo Bank a range of remedies, including without limitation declaring all outstanding debt to be immediately due and payable, foreclosing on the assets securing the obligation arising under the credit agreement and/or ceasing to provide the additional revolving loans, which could have a material adverse effect on us

On November 5, 2008, we entered into a credit agreement with Wells Fargo Bank to provide us with a revolving line of credit (the “Credit Agreement”). The Credit Agreement provides for maximum borrowings outstanding at any time in an amount of up to $15 million. As of December 31, 2008, we had outstanding borrowings of $2.5 million under the Credit Agreement. If borrowings under the Credit Agreement exceed $7.5 million, all borrowings are subject to a

borrowing base which is based on eligible accounts receivable. Borrowings are secured by a first priority security interest in all of our assets (except for certain permitted liens that are senior to the Wells Fargo Bank's security interest). At our option, borrowings bear interest at either 2.25% over the bank's prime rate or 3.50% over the one-month, two-month or three-month LIBOR. The Credit Agreement requires that we comply with certain financial and other covenants for borrowings to be permitted. The more significant financial covenants include (i) maintaining a minimum modified quick ratio and (ii) achieving not more than a certain amount of loss through December 31, 2008, and thereafter a minimum profitability, in each case excluding certain non-cash items.

Although we were in compliance with the covenants at December 31, 2008, it is possible that we may not be in compliance or failure to comply with certain covenants or other agreements in the future. If we are unable to meet the financial or other covenants under the Credit Agreement or negotiate future waivers or amendments of such covenants, an event of default could occur under the Credit Agreement. Upon the occurrence and during the continuance of an event of default under the Credit Agreement, Wells Fargo Bank has available a range of remedies customary in these circumstances, including without limitation declaring all outstanding debt, together with accrued and unpaid interest thereon, to be immediately due and payable, foreclosing on the assets securing the obligations arising under the Credit Agreement and/or ceasing to provide additional revolving loans, which could have a material adverse effect on us.

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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.

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.

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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. 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.

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.

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. 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.

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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.

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.

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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.

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.

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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;
- 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 December 31, 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 48% of our outstanding common stock. As a result, these persons, acting together, may have the ability to determine the outcome of 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:

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- 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.

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.

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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

Item 5. Other Information.

None

Item 6. Exhibits.

See the Index to Exhibits on Page 46 of this report

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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: February 6, 2009

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

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

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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)
10.1#	Amendment to Offer Letter John R. Kilcoyne
10.2#	Amendment to Offer Letter Robert A. Stern
10.3#	Amendment to Offer Letter Carolyn M. Bruguera
10.4#	Amendment to Offer Letter Robert C. Colloton
10.5#	Amendment to Credit Agreement
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