PULSE ELECTRONICS CORP
Form 10-Q
November 09, 2011

UNITED STATES
SECURITIES & EXCHANGE COMMISSION

Washington, D.C. 20549

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FORM 10-Q

x The Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended September 30, 2011, or

o Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from ______________ to ______________.

Commission File No. 1-5375

PULSE ELECTRONICS CORPORATION
(Exact name of registrant as specified in its Charter)

PENNSYLVANIA (State or other jurisdiction of incorporation or organization)	23-1292472 (IRS Employer Identification Number)
12220 World Trade Drive San Diego, CA (Address of principal executive offices)	92128 (Zip Code)
Registrant's telephone number, including area code:	858-674-8100
Former name of registrant:	Technitrol, Inc.

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 the filing requirements for at least the past 90 days.
Yes x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Yes x No o

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

Large accelerated filer o	Accelerated filer x	Non-accelerated filer o	Smaller reporting company o

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

Indicate the number of shares outstanding of each of the issuer's classes of Common Stock, as of November 9, 2011: 41,658,415

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PART I. FINANCIAL INFORMATION

Item 1: Financial Statements

Pulse Electronics Corporation and Subsidiaries
Consolidated Balance Sheets

(Unaudited)
In thousands

Assets	September 30, 2011 (Unaudited)	December 31, 2010
Current assets:		
Cash and cash equivalents	$ 16,404	$ 35,905
Accounts receivable, net	59,317	65,532
Inventory	37,154	35,741
Prepaid expenses and other current assets	19,577	14,804
Total current assets	132,452	151,982
Long-term assets:		
Property, plant and equipment	111,882	113,137
Less accumulated depreciation	80,434	82,456
Net property, plant and equipment	31,448	30,681
Deferred income taxes	29,632	33,669
Intangibles assets, net	4,589	5,657
Other assets	2,119	2,610
	$ 200,240	$ 224,599
Liabilities and Equity		
Current liabilities:		
Accounts payable	$ 48,093	$ 46,102
Accrued expenses and other current liabilities	42,554	54,602
Total current liabilities	90,647	100,704
Long-term liabilities:		
Long-term debt	32,950	32,150
Convertible senior notes	50,000	50,000
Deferred income taxes	9,382	8,890
Other long-term liabilities	8,775	10,081
Equity:		
Pulse Electronics Corporation shareholders' equity:		
Common stock and additional paid-in capital	218,152	219,393
Retained loss	(242,730)	(232,660)
Accumulated other comprehensive earnings	25,547	23,993
Total Pulse Electronics Corporation shareholders' equity	969	10,726
Non-controlling interest	7,517	12,048
Total equity	8,486	22,774

	$	200,240	$	224,599

See accompanying Notes to Unaudited Consolidated Financial Statements.

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Pulse Electronics Corporation and Subsidiaries
Consolidated Statements of Operations
(Unaudited)
In thousands, except per share data

	Three Months Ended		Nine Months Ended	
	September 30, 2011	October 1, 2010	September 30, 2011	October 1, 2010
Net sales	$ 96,014	$ 121,963	$ 278,811	$ 331,296
Cost of sales	73,913	88,895	215,913	247,768
Gross profit	22,101	33,068	62,898	83,528
Selling, general and administrative expenses	19,798	25,014	62,594	72,401
Severance, impairment and other associated costs	2,968	--	13,591	31,094
Cost related to unsolicited takeover attempt	--	--	1,916	--
Operating (loss) profit	(665)	8,054	(15,203)	(19,967)
Other (expense) income:				
Interest expense, net	(1,917)	(1,127)	(4,368)	(3,748)
Other (expense) income, net	(1,088)	3,386	621	(4,143)
Total other (expense) income	(3,005)	2,259	(3,747)	(7,891)
Earnings (loss) from continuing operations before income taxes	(3,670)	10,313	(18,950)	(27,858)
Income tax (benefit) expense	(2,682)	2,177	(8,512)	2,032
Net earnings (loss) from continuing operations	(988)	8,136	(10,438)	(29,890)
Net earnings (loss) from discontinued operations	(270)	6,188	342	(8,980)
Net (loss) earnings	(1,258)	14,324	(10,096)	(38,870)
Less: Net earnings (loss) attributable to non-controlling interest	(118)	117	(26)	714
Net earnings (loss) attributable to Pulse Electronics Corp.	$ (1,140)	$ 14,207	$ (10,070)	$ (39,584)
Amounts attributable to Pulse Electronics Corp. common shareholders:				
Net earnings (loss) from continuing operations	$ (870)	$ 8,019	$ (10,412)	$ (30,604)
	(270)	6,188	342	(8,980)

Net earnings (loss) from discontinued operations				
Net earnings (loss) attributable to Pulse Electronics Corp.	$ (1,140)	$ 14,207	$ (10,070)	$ (39,584)
Per share data:				
Basic earnings (loss) per share:				
Net earnings (loss) from continuing operations	$ (0.02)	$ 0.20	$ (0.25)	$ (0.75)
Net earnings (loss) from discontinued operations	(0.01)	0.15	0.01	(0.22)
Net earnings (loss) attributable to Pulse Electronics Corp.	$ (0.03)	$ 0.35	$ (0.24)	$ (0.97)
Diluted earnings (loss) per share:				
Net earnings (loss) from continuing operations	$ (0.02)	$ 0.18	$ (0.25)	$ (0.75)
Net earnings (loss) from discontinued operations	(0.01)	0.12	0.01	(0.22)
Net earnings (loss) attributable to Pulse Electronics Corp.	$ (0.03)	$ 0.30	$ (0.24)	$ (0.97)

See accompanying Notes to Unaudited Consolidated Financial Statements.

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Pulse Electronics Corporation and Subsidiaries
Consolidated Statements of Cash Flows
(Unaudited)
In thousands

	Nine Months Ended	
	September 30, 2011	October 1, 2010
Cash flows from operating activities - continuing operations:		
Net loss	$(10,096)	$(38,870)
(Earnings) loss from discontinued operations	(342)	8,980
Adjustment to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	7,770	14,047
Goodwill and intangible asset impairment, net of income taxes	--	27,963
Stock incentive plan expense, net of cash payments	983	993
Changes in assets and liabilities, net of the effect of divestitures:		
Accounts receivable	7,457	3,308
Inventory	(1,229)	2,621
Prepaid expenses and other current assets	(609)	(575)
Accounts payable and accrued expenses	(18,559)	9,961
Severance, impairment and other associated costs, net of cash payments (excluding goodwill and intangible asset impairments)	7,191	(449)
Other, net	1,919	128
Net cash (used in) provided by operating activities	(5,515)	28,107
Cash flows from investing activities – continuing operations:		
Cash received from dispositions, net	1,041	54,628
Capital expenditures	(8,765)	(7,676)
Proceeds from sale of property, plant and equipment	695	1,638
Foreign currency impact on intercompany lending	752	(3,877)
Net cash (used in) provided by investing activities	(6,277)	44,713
Cash flows from financing activities – continuing operations:		
Debt issuance costs	(1,007)	--
Long-term borrowings	25,000	25,000
Principal payments on long-term debt	(24,200)	(73,850)
Purchases of shares in non-controlling interest	(4,134)	--
Dividends paid	(3,119)	(3,100)
Net cash used in financing activities	(7,460)	(51,950)
Net effect of exchange rate changes on cash from continuing operations:	21	366
Cash flows of discontinued operations:		
Net cash used in operating activities	(270)	(8,868)
Net cash used in investing activities	--	(11,017)

Net effect of exchange rate changes on cash	--	(741)
Net decrease in cash and cash equivalents from discontinued operations	(270)	(20,626)
Net decrease in cash and cash equivalents	(19,501)	610
Cash and cash equivalents at beginning of period	35,905	39,707
Cash and cash equivalents at end of period	$16,404	$40,317

See accompanying Notes to Unaudited Consolidated Financial Statements.

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Pulse Electronics Corporation and Subsidiaries
Consolidated Statement of Changes in Equity

Nine Months Ended September 30, 2011

(Unaudited)
In thousands, except per share data

	Common stock and paid in capital Shares	Amount	Retained loss	Accumulated other comprehensive income	Non-controlling interest	Total equity	Comprehensive loss
Balance at December 31, 2010	41,490	$219,393	$(232,660)	$ 23,993	$12,048	$22,774	
Stock options, awards, and related compensation	168	1,511	--	--	--	1,511	
Dividends declared ($0.025 per share)	--	(3,123)	--	--	--	(3,123)	
Purchases of shares in non-controlling interest	--	371	--	--	(4,505)	(4,134)	
Net loss	--	--	(10,070)	--	(26)	(10,096)	$ (10,096)
Currency translation adjustments	--	--	--	1,554	--	1,554	1,554
Balance at September 30, 2011	41,658	$218,152	$(242,730)	$ 25,547	$7,517	$8,486	$ (8,542)

See accompanying Notes to Unaudited Consolidated Financial Statements.

Pulse Electronics Corporation and Subsidiaries
Notes to Unaudited Consolidated Financial Statements

(1)Accounting policies

Pulse Electronics Corporation is a global producer of precision-engineered electronic components and modules. We sometimes refer to Pulse Electronics Corporation as "Pulse Electronics", "Pulse", "the Company", "we" or "our." Based on estimates of the total annual revenues in our primary markets and our share of those markets relative to our competitors, we believe we are a leading global producer of electronic components and modules in the primary markets we serve. Our ticker symbol on the New York Stock Exchange is "PULS."

We operate our business in three segments:

- our Network product group which we refer to as Network,
- our Power product group which we refer to as Power, and
- our Wireless product group which we refer to as Wireless.

Network produces a variety of passive components that manage and regulate electronic signals for use in a variety of devices used in local area and wide area networks, such as connectors, filters, filtered connectors, transformers, splitters, micro-filters, baluns and chokes. Power primarily manufactures products that adjust and ensure proper current and voltage, limit distortion of voltage, sense and report current and voltage and cause mechanical movement or actuation, which includes power transformers, chokes, current and voltage sensors, ignition coils, automotive coils and military and aerospace products. Wireless manufactures products related to the capture or transmission of wireless communication signals, such as antennas, antenna modules and antenna mounting components.

We have discontinued operations that include our former electrical contact products business ("Electrical"), medtech components business ("Medtech") and microelectromechanical systems ("MEMS") microphone business. The results from these discontinued operations are presented in a single line on our Consolidated Statements of Operations for all periods presented and there are no remaining assets or liabilities related to our discontinued operations on our Consolidated Balance Sheets.

Our Consolidated Financial Statements include the accounts of Pulse Electronics and all of our subsidiaries. All material intercompany accounts, transactions and profits are eliminated in consolidation. For a complete description of our accounting policies refer to Note 1, Summary of significant accounting policies, of the Notes to Consolidated Financial Statements included in Pulse Electronics' Form 10-K filed for the year ended December 31, 2010.

In the quarter ended September 30, 2011, we incurred costs in connection with the implementation of an Enterprise Resource Planning (ERP) system. We have accounted for these costs in accordance with ASC 350-40, Intangibles – Goodwill and Other – Internal-Use Software. The costs of licensing and implementing ERP software are capitalized up to the point of implementation and then amortized over the estimated useful life of the software. The costs incurred during the preliminary project stage are expensed as incurred. During the nine months ended September 30, 2011, we capitalized $2.4 million of ERP costs in property, plant and equipment, which primarily includes one-time license fees and hardware. We will begin to amortize these costs once the system is in use. All other costs have been expensed as incurred.

The results for the nine months ended September 30, 2011 and October 1, 2010 have been prepared by our management without audit. In the opinion of management, the consolidated financial statements fairly present in all material respects, the financial position, results of operations and cash flows for the periods presented. To the best of our knowledge and belief, all adjustments have been made to properly reflect income and expenses attributable to the periods presented. Except for severance, impairment and other associated costs and costs related to unsolicited takeover attempt, all such adjustments are of a normal recurring nature. Our operating results for the nine months ended September 30, 2011 are not necessarily indicative of annual results.

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Pulse Electronics Corporation and Subsidiaries
Notes to Unaudited Consolidated Financial Statements, continued

(1) Accounting policies, continued

New accounting pronouncements

In June 2011, the FASB issued ASU 2011-05, Comprehensive Income (Topic 220)—Presentation of Comprehensive Income, which requires presentation of the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. ASU 2011-05 eliminates the option to present the components of other comprehensive income as part of the statement of equity. The items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income were not changed. Additionally, no changes were made to the calculation and presentation of earnings per share. ASU 2011-05 is effective for our fiscal year beginning January 1, 2012 and must be applied retrospectively. We expect to present comprehensive income in two separate but consecutive statements. Other than the change in presentation, we have determined these changes will not have an impact on the Consolidated Financial Statements.

In December 2010, FASB amended its authoritative guidance related to business combinations that are material on an individual or aggregate basis. These amendments clarify existing guidance for comparative financial statements that include a business combination. Specifically, revenue and earnings of the combined business are required to be disclosed as though the combination had occurred as of the beginning of the comparable prior annual reporting period. Also, the amendment expands supplemental pro forma disclosures to include a description of the nature and amount of nonrecurring pro forma adjustments, to revenue and earnings, which are directly attributable to the business combination. This guidance is prospective for business combinations with an acquisition date on or after the first day of our fiscal 2012. If we enter into any business combinations subsequent to 2011, we will evaluate the effect that this guidance may have on our Consolidated Financial Statements in accounting for such transactions.

(2) Divestitures

Electrical: On September 2, 2010, we completed the divestiture of our former Electrical business in Europe and Asia to Tinicum Capital Partners II, L.P., ("Tinicum"). Our net cash proceeds were approximately $53.3 million in cash, including normal working capital adjustments and other financial adjustments. On January 4, 2010, we divested Electrical's North American operations for an amount immaterial to our Consolidated Financial Statements. Electrical produced a full array of precious metal electrical contact products that range from materials used in the fabrication of electrical contacts to completed contact subassemblies. Net proceeds from each transaction, after funding related retirement plan obligations and transaction costs, were used to repay outstanding debt. In the quarter ended September 30, 2011, we incurred $0.3 million of expenses to reimburse Tinicum for certain contingent costs we were obligated to pay under the sale agreement. We have reflected the results of Electrical as a discontinued operation on the Consolidated Statements of Operations for all periods presented. We have no material continuing involvement with our former Electrical business in Europe and Asia. Electrical's net sales and earnings (loss) before income taxes for the three and six months ended September 30, 2011 and October 1, 2010, respectively, were as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30, 2011	October 1, 2010	September 30, 2011	October 1, 2010
Net sales	$--	$53,974	$--	$203,014
Earnings (loss) before income taxes	(270)	8,237	604	(7,677)

Medtech: On June 25, 2009, we completed the disposition of our Medtech components business to Altor Fund III ("Altor"). Medtech was headquartered in Roskilde, Denmark with manufacturing facilities in Denmark, Poland and Vietnam producing components for the hearing aid, high-end audio headset and medical device markets. We had no activity related to Medtech in the nine months ended September 30, 2011. We reflected the results of Medtech as a discontinued operation on the Consolidated Statement of Operations for the three and nine months ended October 1, 2010. Medtech's loss before income taxes for the three and nine months ended October 1, 2010 was approximately $0.9 million and $0.5 million, respectively, with no net sales in either period. We have no material continuing involvement with Medtech.

Pulse Electronics Corporation and Subsidiaries
Notes to Unaudited Consolidated Financial Statements, continued

(2) Divestitures, continued

MEMS: During 2009, we divested our microelectromechanical systems microphone business located in Denmark and Vietnam. We had no activity related to MEMS in the nine months ended September 30, 2011. We reflected the results of MEMS as a discontinued operation on the Consolidated Statements of Operations for the three and nine months ended October 1, 2010. MEMS' net sales and earnings before income taxes for the three months ended October 1, 2010 were both less than $0.1 million. MEMS' net sales and loss before income taxes for the nine months ended October 1, 2010 were $0.1 million and $0.2 million, respectively. We have no material continuing involvement with MEMS.

(3) Financial statement details

The following are details of certain financial statement captions at September 30, 2011 and October 1, 2010:

	September 30, 2011	December 31, 2010
Inventory:		
Finished goods	$13,210	$16,351
Work in process	6,277	6,896
Raw materials and supplies	17,667	12,494
	$37,154	$35,741
Accrued expenses and other current liabilities:		
Income taxes payable	$1,890	$14,828
Accrued compensation	11,592	13,054
Other accrued liabilities	29,072	26,720
	$42,554	$54,602

During the first quarter of 2011, a majority owned subsidiary announced a plan to purchase its own common stock that is publicly traded on a non-U.S. exchange. During the nine months ended September 30, 2011, the subsidiary purchased approximately $4.1 million of its own common stock using its cash on hand. These purchases were accounted for as equity transactions, and the difference between the book value and fair value of the stock acquired of approximately $4.1 million was credited to our additional paid-in capital.

(4) Intangible assets

We assess the impairment of long-lived assets, including identifiable intangible assets subject to amortization and property, plant and equipment, whenever events or changes in circumstances indicate the carrying value may not be recoverable. Factors we consider important that could trigger an impairment review include significant changes in the use of any asset, changes in historical trends in operating performance, changes in projected operating performance, stock price and other significant negative economic trends.

Prior to 2011, we had goodwill on our Consolidated Balance Sheets subject to an annual impairment review. The annual review of our indefinite-lived intangible assets was performed in our fourth fiscal quarter of each year, or more frequently if indicators of a potential impairment existed, to determine if the carrying amount of these intangible assets were impaired. The impairment review process compares the fair value of each reporting unit, where goodwill resided, with its carrying value. If the net book value of the reporting unit exceeded its fair value, we would perform the second step of the impairment test that required an allocation of the reporting unit's fair value to all of its assets and liabilities in a manner similar to a purchase price allocation, with any residual fair value being allocated to goodwill. An impairment charge was recognized only when the implied fair value of a reporting unit's goodwill was less than its carrying amount. Our impairment review incorporated both an income and comparable-companies market approach to estimate potential impairment. We believe the use of multiple valuation techniques resulted in a more accurate indicator of the fair value of each reporting unit, rather than the use of only an income approach.

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Pulse Electronics Corporation and Subsidiaries
Notes to Unaudited Consolidated Financial Statements, continued

(4) Intangible assets, continued

The income approach is based on estimating future cash flows using various growth assumptions and discounting based on a present value factor. We developed the future net cash flows during our annual budget process, which was completed in the fourth fiscal quarter of each year. However, estimates of future cash flows were updated in conjunction with any goodwill recoverability analysis that was performed independent of our annual review. The growth rates we used were an estimate of the future growth in the industries in which we participate and were adjusted, if necessary, for issues specific to our business and our position in the industry. Our discount rate assumption was based on an estimated cost of capital, which we determined annually based on market participant estimated costs of debt and equity relative to our capital structure. The comparable-companies market approach considered the trading multiples of our peer companies to compute our estimated fair value. The majority of the comparable-companies utilized in our evaluation were included in the Dow Jones U.S. Electrical Components and Equipment Industry Group Index.

The following is a summary of our intangible assets at September 30, 2011 and December 31, 2010 (in thousands):

	September 30, 2011	December 31, 2010
Intangible assets subject to amortization (definite lives):		
Customer relationships	$3,300	$3,300
Technology	2,000	2,000
Other	960	960
Total	6,260	6,260
Accumulated amortization:		
Customer relationships	(2,250)	(1,897)
Technology	(1,871)	(1,178)
Other	(150)	(128)
Total	(4,271)	(3,203)
Net intangible assets subject to amortization	1,989	3,057
Intangible assets not subject to amortization (indefinite lives):		
Tradename	2,600	2,600
Intangible assets, net	$4,589	$5,657

Amortization expense was approximately $1.1 million and $1.9 million for the nine months ended September 30, 2011 and October 1, 2010, respectively. The decrease in the amortization expense from the nine months ended October 1, 2010 to the nine months ended September 30, 2011 was primarily the result of lower amortizing intangibles due to impairment charges recorded during 2010.
The weighted average life of our finite intangible assets is approximately 6.4 years as of September 30, 2011. Estimated annual amortization expense for each of the next five years is as follows (in thousands):

Year Ending

2012	$ 539
2013	$ 539
2014	$ 68
2015	$ 68
2016	$ 68

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Pulse Electronics Corporation and Subsidiaries
Notes to Unaudited Consolidated Financial Statements, continued

(5) Income taxes

At September 30, 2011, we had approximately $11.3 million of unrecognized tax benefits, $6.8 million of which are classified as other long-term liabilities and are not expected to be realized within the next 12 months. All of these tax benefits would affect our effective tax rate, if recognized.

We recognize interest and penalties, if any, related to income tax matters as income tax expense. As of September 30, 2011, we have $0.2 million accrued for interest and/or penalties related to uncertain income tax positions. The amount accrued for interest and/or penalties decreased approximately $0.9 million from the year ended December 31, 2010 as a result of the release of a non-U.S. tax reserve during the nine months ended September 30, 2011. The release of the reserve and related accrued interest and/or penalties was due to the dissolution of a non-U.S. legal entity which we no longer operate.

We are subject to U.S. federal income tax as well as income tax in multiple state and non-U.S. jurisdictions. Federal and state income tax returns for all years after 2006 are subject to future examination by the respective tax authorities. With respect to material non-U.S. jurisdictions where we operate, we have open tax years ranging from two to ten years.

The effective tax rate for the nine months ended September 30, 2011 was a benefit of 44.9% compared to an expense of 7.3% for the nine months ended October 1, 2010. The increase in the effective tax benefit was due to the absence of the goodwill impairment charges that reduced the 2010 tax benefit and the release of certain tax reserves in 2011. These increases to the tax benefit were partially offset by restructuring charges incurred in lower tax rate jurisdictions during the nine months ended September 30, 2011, and additional reserve related to foreign jurisdiction.

During the nine months ended September 30, 2011, we paid $1.9 million related to an audit of one of our foreign subsidiaries' income tax filings. Settlement of this matter may result in additional payments of as much as $4.4 million. This amount has been fully accrued for as of September 30, 2011, however, we do not anticipate additional payments related to this matter before 2012.

(6) Defined benefit plans

We maintain defined benefit pension plans for certain U.S. and non-U.S. employees. However, the benefits under our domestic defined benefit plan were frozen as of December 31, 2010. Accrued benefits were based on years of service and average final compensation. We do not provide any post-retirement benefits outside of the U.S., except as may be required by certain foreign jurisdictions. Depending on the investment performance of our plan assets and other contributing factors, funding in a given year may not be required.

Our net periodic benefit income (expense) was $0.5 million of income and less than $0.1 million of expense for the nine months ended September 30, 2011 and October 1, 2010, respectively. In the nine months ended September 30, 2011, we contributed less than $0.1 million to our defined benefit plans.

Our domestic defined benefit retirement plan is currently under audit by the Pension Benefit Guarantee Corporation ("PBGC"). Initial communications from the PBGC have indicated that the sale of Electrical's North American operations may have resulted in a partial plan termination, which may require us to accelerate the funding of up to approximately $7.3 million to this defined benefit plan. A partial plan termination would only result in a cash payment to fund our plan and will not directly result in additional expenses to the Company. Recently, the PBGC has publicly stated that it will reconsider its 4062(e) proposed rule, a rule applicable to partial plan terminations. We are continuing to have discussions with the PBGC on this matter.

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Pulse Electronics Corporation and Subsidiaries
Notes to Unaudited Consolidated Financial Statements, continued

(7) Commitments and contingencies

We are a party to various legal proceedings, claims and assessments that arise in the ordinary course of business, and may continue to incur significant costs in defending or settling legal matters. The total amount and timing of the expected future payments related to these matters cannot be estimated due to the uncertainty of the duration of the legal proceedings and the ultimate scope of other claims. However, an unfavorable outcome in a single matter or in multiple legal matters during the same reporting period could have a material adverse effect on our consolidated financial position, results from operations and cash flows.

We are a defendant in a lawsuit filed in March 2007 by Halo Electronics, Inc. in the United States District Court, District of Nevada. The case is captioned Halo Electronics, Inc. v. Pulse Electronics, Inc. and Pulse Electronics Corp., Case No. 2:07-cv-00331-PMP-PAL. The plaintiff claims that we infringe certain U.S. patents related to an electronic surface mount package, and is seeking injunctive relief and damages. Discovery has ended, and on September 6, 2011, the Court ruled on numerous pending motions for summary judgment. The Court denied the plaintiff's motion for summary judgment of infringement by our products with the exception of one claim relating to one representative product. The Court partially granted one of our summary judgment motions, in effect, excluding any liability for direct infringement for products sold outside of North America on all of plaintiff's claims.

Although a trial date has not yet been scheduled, the Court has ordered the parties to file a proposed joint pre-trial order for the case by November 29, 2011. The plaintiff has previously produced expert reports asserting infringement and liability in the amount of $34.3 million, plus requests for trebling and attorneys fees. However, these reports do not take into account the Court's September 2011 ruling, which excluded direct foreign sales and therefore may reduce our potential exposure to significantly less than half of the amount claimed by the plaintiff. In addition, we are aware that similar cases have been brought by Halo Electronics against certain of our competitors, and that at least one of our competitors commenced a similar independent patent litigation against Halo Electronics. Although we are not familiar with the specific details of these cases or the plaintiff's claims, we believe that one of these cases has recently been settled on terms that, among other things, provide for significantly less up-front cash to Halo Electronics than the amount of damages that it has claimed in our case.

In light of the Court's summary judgment order and its ruling that we are not liable with respect to direct infringement for products sold outside North America we recorded a charge of approximately $0.2 million as selling, general and administrative expense in the three months ended September 30, 2011. We intend to continue presenting a vigorous defense against the remaining claims in the case, to maintain our counterclaim that Pulse owes no liability whatsoever to Halo due to the invalidity of the Halo patents, to contest the amount of damages asserted by Halo and its expert, and to consider our rights of appeal with respect to any adverse rulings. However, management is currently unable to determine whether any additional loss will occur or to estimate the range of such loss. Therefore, no additional liability has been accrued. During the nine months ended September 30, 2011 and October 1, 2010, we incurred approximately $0.8 million and $1.9 million of legal expenses, respectively, related to this matter.

In March 2011, we received an unsolicited proposal from Bel Fuse Inc. ("Bel Fuse") to acquire all of our outstanding shares. Our board of directors unanimously determined that Bel Fuse's proposal significantly undervalued our business and was not in the best interests of our company, our shareholders, and other constituents. Bel Fuse had also nominated two directors for election to our board. At our annual meeting of shareholders on May 18, 2011, the Bel Fuse director nominees were not elected to our board.

During the nine months ended September 30, 2011, we incurred $1.9 million of legal and professional fees and other costs related to Bel Fuse's unsolicited takeover attempt. The majority of these costs represent accruals for the fees of our financial and legal advisors. We do not expect to incur significant additional fees or similar costs related to this matter.

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Pulse Electronics Corporation and Subsidiaries
Notes to Unaudited Consolidated Financial Statements, continued

(8) Debt

We have $50.0 million in convertible senior notes which will mature on December 15, 2014. The notes bear a coupon rate of 7.0% per annum that is payable semi-annually in arrears on June 15 and December 15 of each year. We expect to pay approximately $3.5 million of interest on the convertible senior notes in 2011. These convertible notes rank junior to any secured indebtedness to the extent of the assets that secure such indebtedness, and are structurally subordinated in right of payment to all indebtedness and commitments of our subsidiaries.

Holders of our convertible notes may convert their shares to common stock at their option any day prior to the close of business on December 14, 2014. Upon conversion, for each $1,000 in principal amount outstanding, we will deliver a number of shares of our common stock equal to the conversion rate. The initial conversion rate for the notes is approximately 156.64 shares of common stock per $1,000 in principal amount of notes. The initial conversion price is approximately $6.38 per share of common stock. The conversion rate is subject to change upon the occurrence of specified normal and customary events as defined by the indenture, such as stock splits or stock dividends, but will not be adjusted for accrued interest. In addition, subject to certain fundamental change exceptions specified in the indenture, which generally pertain to circumstances in which the majority of our common stock is obtained, exchanged or no longer available for trading, holders may require us to repurchase all or part of their notes for cash at a price equal to 100% of the principal amount of the notes being repurchased plus any accrued and unpaid interest up to, but excluding, the relevant repurchase date. We are not permitted to redeem the notes prior to maturity.

On September 30, 2011, we had a senior revolving credit facility that provided for $60.8 million of borrowings in U.S. dollars, euro or yen, with a multi-currency facility that provides for the issuance of letters of credit in an aggregate amount not to exceed the equivalent of $10.0 million. Our senior revolving credit facility was amended on August 5, 2011 and the revised terms included a reduction to the borrowings permitted under the credit facility from $100.0 million to $70.0 million. The facility was further reduced to $60.8 million following a debt repayment in September 2011. The amendment on August 5, 2011 also included an increase in the interest rates on both the unborrowed portion of the commitment and on the outstanding borrowings, changes to our debt covenants, a change to our permitted capital expenditure levels, and restrictions on our ability to make dividend payments. The maturity date of the facility continues to be February 28, 2013.

We paid total fees and expenses of approximately $1.4 million in connection with the amendment, of which $1.2 million have been capitalized as debt issuance costs and will be amortized on a straight-line basis through the maturity date of the debt.

We had approximately $33.0 million of borrowings outstanding and one standby letter of credit outstanding in the aggregate amount of $1.2 million securing transactions entered into in the ordinary course of business.

The weighted-average interest rate on our credit facility borrowings for the three and nine months ended September 30, 2011 including the credit margin spread was approximately 3.4% and 2.3%, respectively. Average borrowings outstanding on our senior revolving credit facility during the three and nine months ended September 30, 2011 were approximately $44.6 million and $42.5 million.

Interest: Under the amendment, the fee on the unborrowed portion of the commitment ranges from 0.40% to 0.50% of the total commitment, depending on the following total debt-to-EBITDA ratios:

Total debt-to-EBITDA ratio	Commitment fee percentage
Less than 1.50	0.40%
Less than 2.25	0.40%
Less than 3.00	0.45%
Less than 4.00	0.50%
Less than 5.00	0.50%
Greater than 5.00	0.50%

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Pulse Electronics Corporation and Subsidiaries
Notes to Unaudited Consolidated Financial Statements, continued

(8) Debt, continued

The credit margin spread on the outstanding borrowings ranges from 3.25% to 4.50% depending on the following total debt-to-EBITDA ratios:

Total debt-to-EBITDA ratio	Credit margin spread
Less than 1.50	3.25%
Less than 2.25	3.50%
Less than 3.00	3.75%
Less than 4.00	4.00%
Less than 5.00	4.25%
Greater than 5.00	4.50%

In calculating the total debt-to-EBITDA ratio, the total debt includes the debt outstanding under the credit facility and the convertible senior notes.

Debt covenants: Outstanding borrowings under our credit facility are subject to leverage and fixed charges covenants, which are computed as of the most recent quarter-end. These covenants require the calculation of a rolling four quarter EBITDA according to the definition prescribed by the amended senior revolving credit facility agreement, including certain restructuring cost addbacks in 2011 and 2012.

Our fixed charges covenant requires that our EBITDA be equal to or greater than the following levels:

Quarter ended	Level
September 30, 2011	1.10 times fixed charges
December 30, 2011	0.75 times fixed charges
March 30, 2012	1.10 times fixed charges
June 29, 2012 and thereafter	1.50 times fixed charges

Our leverage covenant requires that our total debt outstanding, excluding our senior convertible notes, is not to exceed the following levels:

Quarter ended	Level
September 30, 2011	3.75 times EBITDA
December 30, 2011	6.00 times EBITDA
March 30, 2012	3.50 times EBITDA
June 29, 2012	3.00 times EBITDA

September 28, 2012	2.25 times EBITDA
December 28, 2012	2.00 times EBITDA

In addition, we will be required to comply with a minimum six month rolling EBITDA level as follows:

Quarter ended		Level
September 30, 2011	$	6.00 million
December 30, 2011	$	8.25 million
March 30, 2012	$	9.50 million
June 29, 2012	$	13.50 million
September 28, 2012	$	15.00 million
December 28, 2012	$	15.50 million

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Pulse Electronics Corporation and Subsidiaries
Notes to Unaudited Consolidated Financial Statements, continued

(8) Debt, continued

Borrowing base, capital expenditures and dividend payments: We have agreed to limit our borrowings to an amount not to exceed total eligible accounts receivable and cash, to maintain available cash of $5.8 million, and to suspend payment of dividends following a payment in the quarter ended December 30, 2011. We have also agreed to limit our capital expenditures to the following levels:

Period	Capital expenditure level	
Six months ended December 30, 2011	$	13.5 million
Six months ended June 29, 2012	$	8.5 million
Six months ended December 28, 2012	$	10.0 million

The amended senior revolving credit facility also has other customary and normal provisions. Multiple subsidiaries, both domestic and international, have guaranteed obligations specified by our senior revolving credit facility agreement. Also, certain domestic and international subsidiaries have pledged shares of certain subsidiaries, as well as selected accounts receivable, inventory, machinery and equipment and other assets as collateral. If we default on our obligations, our lenders may take possession of the collateral and may license, sell or otherwise dispose of those related assets in order to satisfy our obligations. As of September 30, 2011, we were in compliance with all covenants of our senior revolving credit facility agreement.

(9) Stock-based compensation

We have an incentive compensation plan for our employees. One component of this plan is restricted stock, which grants the recipient the right of ownership of our common stock, generally conditional on continued employment for a specified period. Another component is stock options. The following table presents the amount of stock-based compensation expense included in our Consolidated Statements of Operations for the three and nine months ended September 30, 2011 and October 1, 2010 (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30, 2011	October 1, 2010	September 30, 2011	October 1, 2010
Restricted Stock	$167	$543	$850	$1,453
Stock options	177	(61)	596	1
Total stock-based compensation included in:				
Selling, general and administrative expenses	344	482	1,262	1,454
Severance, impairment and other associated costs	--	--	184	--
Income tax benefit	(120)	(169)	(506)	(509)
Total after-tax stock-based compensation expense	$224	$313	$940	$945

Restricted stock: The value of restricted stock issued is based on the market price of the stock at the award date. We retain the restricted shares until the continued employment requirement has been met. The market value of the shares at the date of grant is charged to expense on a straight-line basis over the three-year vesting period. Cash awards, which have been made in the past, were intended to assist recipients with their resulting personal tax liability, were based on the market value of the shares and were accrued over the vesting period. If the recipient made an election under Section 83(b) of the Internal Revenue Code, the expense related to the cash award was generally fixed based on the value of the awarded stock on the grant date. If the recipient did not make the election under Section 83(b), the expense related to the cash award would fluctuate based on the current market value of the shares, subject to limitations set forth in our restricted stock plan. The Company does not expect to make cash awards in the future.

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Pulse Electronics Corporation and Subsidiaries
Notes to Unaudited Consolidated Financial Statements, continued

(9) Stock-based compensation, continued

A summary of the restricted stock activity is as follows (in thousands, except per share data):

	Shares	Weighted Average Stock Grant Price (Per Share)
Nonvested at December 31, 2010	420	$6.69
Granted	120	$4.99
Vested	(100)	$12.54
Forfeited/cancelled	(50)	$4.67
Nonvested at September 30, 2011	390	$4.93

As of September 30, 2011, there was approximately $1.0 million of unrecognized compensation costs related to restricted stock grants. This unrecognized compensation is expected to be recognized over a weighted-average period of approximately 1.7 years.

Stock options: Stock options are granted at no cost to the employee and, under our incentive compensation plan, the exercise price of these options cannot be less than the fair market value of our common shares on the date of grant. These options expire seven years from the date of grant and generally vest equally over four years. We value our stock options according to the fair value method using the Black-Scholes option pricing model.

A summary of the stock options activity is as follows (in thousands, except per share data):

	Shares	Weighted Average Option Grant Price (Per Share)	Aggregate Intrinsic Value
Outstanding as of December 31, 2010	157	$ 7.41	
Granted	929	$ 5.36	
Exercised	(1)	$ 3.72	$ 1
Forfeited/cancelled	(95)	$ 4.66	
Outstanding as of September 30, 2011	990	$ 5.75	--
Exercisable at September 30, 2011	42	$ 15.39	--

The per share weighted average fair value of stock options granted during 2011 was calculated as $3.02 on the date of grant using the Black-Scholes option-pricing model. The weighted average assumptions based on the date of grant are as follows:

	2011
Dividend yield	1.9 %
Volatility	79.9 %
Risk-free interest rate	2.0 %

Expected life (years)	4.8

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Pulse Electronics Corporation and Subsidiaries
Notes to Unaudited Consolidated Financial Statements, continued

(9) Stock-based compensation, continued

Tax benefits from deductions in excess of the compensation cost of stock options exercised are required to be classified as cash inflows from financing. There was no effect of excess tax benefits on the current or prior year net cash used in or provided by operating activities or the net cash used in or provided by financing activities. During the nine months ended September 30, 2011, there were 900 stock options exercised, however we have not realized any excess tax benefits in connection with the exercise of these stock options due to the fact that we have recorded a net loss in the period. In the nine months ended October 1, 2010, there were no stock options exercised. There have been no amounts of stock-based compensation cost capitalized into inventory or other assets during the nine months ended September 30, 2011 or October 1, 2010.

In the quarter ended September 30, 2011, we issued 33,558 common shares to our CEO. He agreed to acquire these shares in lieu of cash for reimbursement of moving-related expenses, which he incurred in connection with moving his family to San Diego. We have recorded $0.1 million expense in connection with this share issuance.

(10) Per share amounts

Basic loss (earnings) per share was calculated by dividing our net loss (earnings) by the weighted average number of common shares outstanding during the period, excluding restricted shares which are considered to be contingently issuable. To calculate diluted earnings per share, common share equivalents would be added to the weighted average number of common shares outstanding. Common share equivalents are computed based on the number of outstanding options to purchase common stock and unvested restricted shares as calculated using the treasury stock method. However, in periods when we have a net loss, or the exercise price of our stock options, by grant, are greater than the actual price of a share of our common stock as of the end of the period, those common share equivalents are anti-dilutive and we exclude them from the calculation of diluted earnings per share. There were approximately 86,000 common share equivalents for the three months ended October 1, 2010. As we had net losses in the three and nine months ended September 30, 2011 and in the nine months ended October 1, 2010, we did not include any common stock equivalents in our calculation of diluted loss per share. There were approximately 1.0 million and 0.1 million stock options outstanding as of September 30, 2011 and October 1, 2010, respectively. Also, we had unvested restricted shares outstanding of approximately 0.4 million as of September 30, 2011 and October 1, 2010.

The dilutive effect of our convertible senior notes is included in our diluted earnings per share calculation using the if-converted method. Interest attributable to the convertible senior notes, net of tax, is added back to net earnings for the period and the total shares that would be converted, if the notes were settled at the end of the period, are added to the weighted average common shares outstanding. However, in periods when we have a net loss or the amount of interest attributable to the convertible senior notes, net of tax, per the potential common shares obtainable in a conversion exceeds our basic earnings per share, the overall effects of the convertible senior notes are considered anti-dilutive and are excluded from the calculation of diluted earnings per share. For the three months ended October 1, 2010, we added approximately $0.7 million of after-tax interest expense to our diluted earnings which represents the interest attributable to our convertible senior notes. Also, we included approximately 7.8 million shares in our dilutive shares outstanding for the three months ended October 1, 2010, which represents the conversion of the notes into common shares as if the notes were settled at the end of the period. For the three and nine months ended September 30, 2011 and for the nine months ended October 1, 2010, the effects of the convertible notes were anti-dilutive and excluded from our per share calculation.

Unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents are required to be treated as participating securities. Under our restricted stock plan, non-forfeitable dividends are paid on unvested shares of restricted stock, which meets the qualifications of participating securities and requires the two-class method of calculating earnings per share to be applied. We have calculated basic and diluted earnings per share under both the treasury stock method and the two-class method for the three and nine months ended September 30, 2011 and October 1, 2010 and there were no significant differences in the per share amounts calculated under the two methods. Therefore, we have not presented the reconciliation of earnings per share under the two class method for any period presented.

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Pulse Electronics Corporation and Subsidiaries
Notes to Unaudited Consolidated Financial Statements, continued

(10) Per share amounts, continued

(Loss) earnings per share calculations are as follows (in thousands, except per share amounts):

	Three Months Ended		Nine Months Ended	
	September 30, 2011	October 1, 2010	September 30, 2011	October 1, 2010
Net (loss) earnings from continuing operations	$(988)	$8,136	$(10,438)	$(29,890)
Net (loss) earnings from discontinued operations	(270)	6,188	342	(8,980)
Less: net (loss) earnings attributable to non-controlling interest	(118)	117	(26)	714
Net (loss) earnings attributable to Pulse Electronics Corporation	$(1,140)	$14,207	$(10,070)	$(39,584)
Basic (loss) earnings per share:				
Shares	41,252	41,047	41,211	40,963
Continuing operations	$(0.02)	$0.20	$(0.25)	$(0.75)
Discontinued operations	(0.01)	0.15	0.01	(0.22)
Per share amount	$(0.03)	$0.35	$(0.24)	$(0.97)
Diluted (loss) earnings per share:				
Shares	41,252	48,965	41,211	40,963
Continuing operations	$(0.02)	$0.18	$(0.25)	$(0.75)
Discontinued operations	(0.01)	0.12	0.01	(0.22)
Per share amount	$(0.03)	$0.30	$(0.24)	$(0.97)

(11) Severance, impairment and other associated costs

We continue to simplify our operations so that costs are optimally matched to current and anticipated future revenue and unit demand and, also, to focus resources on our core businesses. The amounts and timing of charges depend on specific actions taken. The actions taken, including plant closures and relocations, asset impairments and reduction in personnel worldwide, have resulted in the elimination of a variety of costs. The majority of these costs, not related to the impairment of long-lived assets, represent severance benefits for terminated employees, including both those related to our manufacturing and those that provide selling, general and administrative services. Also, the eliminated costs include depreciation from disposed equipment and rental payments from the termination of lease agreements. During the nine months ended September 30, 2011, we incurred charges of $13.6 million for a number of cost reduction actions approved by management. These charges include severance and related costs of $12.6 million, $0.8 million of write-downs of fixed assets no longer in use, and a $0.2 million write-down of a manufacturing facility to its fair value.

Of the $12.6 million severance charge incurred during the nine months ended September 30, 2011, approximately $3.1 million related to the transition and reorganization of our corporate headquarters in North America, which was initiated in the first quarter of 2011 and is expected to be completed in the fourth quarter of 2011. Approximately 30 employees have been or will be severed under this program.

In the fourth quarter of 2010, we initiated a restructuring program to reduce and reorganize the capacity of our Chinese manufacturing plants, which we expect to complete by the end of our fiscal 2011 year. During the nine months ended September 30, 2011, we incurred approximately $6.7 million of severance, $0.8 million of write-downs of fixed assets no longer in use and $0.2 million of a write-down of a manufacturing facility to its fair value. These costs were primarily related to two plant closures in China and reductions in staff at other facilities in China as we shift manufacturing to lower cost facilities. There were approximately 2,100 employees of our direct labor severed under this program.

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Pulse Electronics Corporation and Subsidiaries
Notes to Unaudited Consolidated Financial Statements, continued

(11) Severance, impairment and other associated costs, continued

During 2010, we decided to withdraw from Wireless' audio components business. In the first quarter of 2011, we initiated a restructuring program to shutdown our audio operations, which was also materially completed during the first quarter of 2011. Related to this program, we incurred approximately $1.0 million of severance and other closure fees during the nine months ended September 30, 2011, which was primarily for the severance of approximately 25 employees. We expect that cash payments resulting from these severance charges incurred during the nine months ended September 30, 2011 will be completed within approximately one year.

The change in our accrual related to severance and other associated costs (excluding asset write-downs) is summarized as follows (in millions):

Balance accrued at December 31, 2010	$0.6	
Net expense during the nine months ended September 30, 2011	12.6	
Severance payments	(6.4	)
Other associated costs	(0.2	)
Balance accrued at September 30, 2011	$6.6	

(12) Financial instruments

We utilize derivative financial instruments, primarily forward exchange contracts, to manage certain foreign currency risk. While these instruments are subject to fluctuations in value, such fluctuations are generally offset by the value of the underlying exposure being hedged. During the nine months ended September 30, 2011, we utilized forward contracts to sell forward euro to receive Chinese renminbi. These contracts were used to mitigate the risk of currency fluctuations in our Chinese operations. At September 30, 2011, we had six foreign exchange forward contracts outstanding to sell forward approximately 3.0 million euro, or approximately $4.2 million, to receive Chinese renminbi. The fair value of these forward contracts was an asset of $0.1 million as determined through the use of Level 2 fair value inputs as defined in ASC Topic 815. During the nine months ended September 30, 2011 and October 1, 2010, no financial instruments were designated as hedges.

The following presents the classifications and fair values of our derivative instruments not designated as hedges in our Consolidated Balance Sheets (in millions):

Consolidated Balance Sheets
(Asset (Liability) derivative)

Derivatives	Classification		September 30, 2011		October 1, 2010	
Foreign exchange forward contracts	Prepaid expenses and other current assets	$	0.1	$	--	
	Total:	$	0.1	$	--	
Foreign exchange forward contracts	Accrued expenses and other current liabilities	$	--	$	(0.7	)
	Total:	$	--	$	(0.7	)

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Pulse Electronics Corporation and Subsidiaries
Notes to Unaudited Consolidated Financial Statements, continued

(12) Financial instruments, continued

The following presents the classifications and fair values of our derivative instruments not designated as hedges in our Consolidated Statement of Operations (in millions):

		Consolidated Statements of Operations (Unrealized/realized (losses)/gains)			
		Three months ended		Nine months ended	
Derivatives	Classification	September 30, 2011	October 1, 2010	September 30, 2011	October 1, 2010
Foreign exchange forward contracts	Other (expense) income, Net	$ 0.2	$ (1.1)	$ (0.3)	$ 0.5
	Total:	$ 0.2	$ (1.1)	$ (0.3)	$ 0.5

During the nine months ended September 30, 2011, there were no changes in the fair value level used in the valuation of our financial assets and liabilities measured at fair value on a recurring basis.

We categorize our financial assets and liabilities on our Consolidated Balance Sheets into a three-level fair value hierarchy based on inputs used for valuation, which are categorized as follows:

Level 1 – Financial assets and liabilities whose values are based on quoted prices for identical assets or liabilities in an active public market.

Level 2 – Financial assets and liabilities whose values are based on quoted prices in markets that are not active or a valuation using model inputs that are observable for substantially the full term of the asset or liability.

Level 3 – Financial assets and liabilities whose values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. These inputs reflect management's assumptions and judgments when pricing the asset or liability.

The following table presents our fair value hierarchy for those financial assets and liabilities measured at fair value on a recurring basis in our Consolidated Balance Sheets as of September 30, 2011 (in millions):

	September 30, 2011	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Other (1)	$0.1	$--	$0.1	$ --
Total	$0.1	$--	$0.1	$ --

(1) Amounts include forward contracts outstanding in our Consolidated Balance Sheet.

Pulse Electronics Corporation and Subsidiaries
Notes to Unaudited Consolidated Financial Statements, continued

(12) Financial instruments, continued

The majority of our financial instruments and financial assets approximate fair value, as presented on our Consolidated Balance Sheets. As of September 30, 2011, the estimated fair value of the outstanding borrowings under our senior revolving credit facility was approximately $34.1 million and the estimated fair value of our convertible senior notes was approximately $39.4 million, as determined through the use of Level 2 fair value inputs as defined in the fair value hierarchy of ASC topic 815. These liabilities are not measured at their fair value in our Consolidated Balance Sheets for any period presented.

During the nine months ended September 30, 2011, we did not have any non-financial assets or non-financial liabilities that were required to be measured at fair value on a recurring basis. Management believes that there is no material risk of loss from changes in inherent market rates or prices in our financial instruments due to the materiality of our financial instruments in relation to our Consolidated Balance Sheets.

Our financial instruments, including cash and cash equivalents and long-term debt, our financial assets, including accounts receivable and inventory, and our financial liabilities, including accounts payable and accrued expenses, are exposed to interest rate, credit risk and foreign currency risk. We have policies relating to these financial instruments and their associated risks and monitor compliance with those policies.

(13) Business segment information

We operate our business in three reportable segments: Network, Power and Wireless. Network produces a variety of passive components that manage and regulate electronic signals for use in a variety of devices used in local area and wide area networks, such as connectors, filters, filtered connectors, transformers, splitters, micro-filters, baluns and chokes. Power primarily manufactures products that adjust and ensure proper current and voltage, limit distortion of voltage, sense and report current and voltage and cause mechanical movement or actuation, which includes power transformers, chokes, current and voltage sensors, ignition coils, automotive coils and military and aerospace products. Wireless manufactures products related to the capture or transmission of wireless communication signals, such as antennas, antenna modules and antenna mounting components.

Selling, general and administrative expenses related to our world-wide operations, primarily related to selling, finance, information technology, human resources and other administrative functions, are allocated to each segment based on the ratio of the segment’s respective budgeted net sales to our consolidated total budgeted net sales.

Our Chief Operating Decision Maker (“CODM”), which we have identified as our Chief Executive Officer, allocates resources and assesses the performance of each segment based on a review of each segment’s net sales and operating profit excluding severance, impairment and other associated charges and costs related to unsolicited takeover attempt. We do not allocate severance, impairment and other associated charges, costs related to unsolicited takeover attempt, interest income, interest expense, other income, other expense or income taxes per segment. Also, the CODM does not review a measure of segment assets. Many of our long-term assets, including manufacturing facilities and equipment, are shared between our segments, therefore expenditures and expenses related to long-term assets cannot be assigned to a specific segment.

Our segments’ net sales and operating loss excluding severance, impairment and other associated costs and costs related to unsolicited takeover attempt for the three and nine months ended September 30, 2011 and October 1, 2010 were as follows (in thousands):

	Three months ended		Nine months ended	
	September 30, 2011	October 1, 2010	September 30, 2011	October 1, 2010
Net sales:				
Network	$ 43,832	$ 65,228	$ 129,767	$ 169,447
Power	36,580	36,848	107,147	95,147
Wireless	15,602	19,887	41,897	66,702
Total net sales	$ 96,014	$ 121,963	$ 278,811	$ 331,296

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Pulse Electronics Corporation and Subsidiaries
Notes to Unaudited Consolidated Financial Statements, continued

(13) Business segment information, continued

Profit (Loss) from continuing operations before severance, impairment and other associated costs and income taxes:				
Network	$1,090	$9,171	$2,777	$19,817
Power	4,012	2,550	7,939	2,796
Wireless	(2,799)	(3,667)	(10,412)	(11,486)
Operating profit excluding severance, impairment and other associated costs and costs related to unsolicited takeover attempt	2,303	8,054	304	11,127
Severance, impairment and other associated costs	2,968	--	13,591	31,094
Costs related to unsolicited takeover attempt	--	------	1,916	--
Operating (loss) profit	(665)	8,054	(15,203)	(19,967)
Interest expense, net	(1,917)	(1,127)	(4,368)	(3,748)
Other (expense) income, net	(1,088)	3,386	621	(4,143)
Net (loss) earnings from continuing operations before income taxes	$(3,670)	$10,313	$(18,950)	$(27,858)

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

Introduction

This discussion and analysis of our financial condition and results of operations as well as other sections of this report contain certain "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995 and involve a number of risks and uncertainties. Actual results may differ materially from those anticipated in these forward-looking statements for many reasons, including the risks we face described in the "Risk Factors" section of this report on pages 37 through 44. Except to the extent required by law, we assume no obligation to update or revise any forward-looking statements.

Critical Accounting Policies

The preparation of financial statements and related disclosures in conformity with U.S. generally accepted accounting principles requires us to make judgments, assumptions and estimates that affect the amounts reported in the Consolidated Financial Statements and accompanying notes. Note 1, Summary of significant accounting policies, to the Consolidated Financial Statements in our Annual Report on Form 10-K for the period ended December 31, 2010 describes the significant accounting policies and methods used in the preparation of the Consolidated Financial Statements.

Item 7., Management's Discussion and Analysis of Financial Condition and Results of Operations, in our Annual Report on Form 10-K for the period ended December 31, 2010 describes the following critical accounting policies, which are significantly impacted by judgments, assumptions and estimates used in the preparation of our Consolidated Financial Statements:

- Inventory valuation;
- Divestiture accounting;
- Purchase accounting;
- Goodwill and identifiable intangibles;
- Income taxes;
- Defined benefit plans;
- Contingency accruals; and
- Severance, impairment and other associates costs.

In the quarter ended September 30, 2011, we incurred costs in connection with the implementation of an Enterprise Resource Planning (ERP) system. We have accounted for these costs in accordance with ASC 350-40, Intangibles – Goodwill and Other – Internal-Use Software. The costs of licensing and implementing ERP software are capitalized up to the point of implementation and then amortized over the estimated useful life of the software. The costs incurred during the preliminary project stage are expensed as incurred. During the nine months ended September 30, 2011, we capitalized $2.4 million of ERP costs in property, plant and equipment, which primarily includes one-time license fees and hardware. We will begin to amortize these costs once the software is in use. All other costs have been expensed as incurred.

Actual results could differ from our estimates as described in the significant and critical accounting policies in our Annual Report on Form 10-K for the period ended December 31, 2010.

Overview

We are a global producer of precision-engineered electronic components and modules. Based on our estimates of the total annual revenues in our primary markets and our share of those markets relative to our competitors, we believe we are a leading global producer of electronic components and modules in the primary markets we serve. We operate our business in three segments:

- our Network product group which we refer to as Network,
- our Power product group which we refer to as Power, and
- our Wireless product group which we refer to as Wireless.

Network produces a variety of passive components that manage and regulate electronic signals for use in various devices used in local area and wide area networks, such as connectors, filters, filtered connectors, transformers, splitters, micro-filters, baluns and chokes. Power primarily manufactures products that adjust and ensure proper current and voltage, limit distortion of voltage, sense and report current and voltage and cause mechanical movement or actuation, which includes power transformers, chokes, current and voltage sensors, ignition coils, automotive coils and military and aerospace products. Wireless manufactures products related to the capture or transmission of wireless communication signals, such as antennas, antenna modules and antenna mounting components.

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General. We define net sales as gross sales less returns and allowances. We sometimes refer to net sales as revenue.

Historically, our gross margin has been significantly affected by product mix and capacity utilization. The markets served by each of our segments are characterized by relatively short product life cycles, which causes significant product turnover each year and, subsequently, frequent variations in the prices of products sold. Due to the constantly changing quantity of parts each segment offers and the frequent changes in our average selling prices, we cannot isolate the impact of changes in unit volume and unit prices on our net sales or gross margin in any given period. In addition, our operations are subject to changes in foreign exchange rates, especially the U.S. dollar as compared to the euro and Chinese renminbi, which affect our U.S. dollar reported results of operations.

We believe our focus on technology and other strategic investments, both internal and external, provides us opportunities for future growth in net sales and operating profit in all our segments. However, unfavorable economic and market conditions, as well as customer preferences, may result in a reduction in demand for our products, thus negatively impacting our financial performance. Also, we may divest portions of our business, close certain locations or complete other cost reduction programs to enable our management to focus on our core businesses and to improve our overall long-term financial performance.

Technology and strategic investments. Our products evolve along with changes in technology, changes in the availability and price of raw materials and changes in design preferences of the end users of our products. Also, regulatory requirements can occasionally impact the design and functionality of our products. We address these dynamic conditions, as well as our customers' desires, by continually investing in the development of each of our segments' products and by maintaining a diverse product portfolio which contains both mature and emerging technologies. We remain committed to technological development through investing in research, development and engineering activities focused on designing next generation products, improving our existing products and improving our manufacturing processes. If we determine that any of our segments' manufacturing processes would benefit from capital investment, we may allocate resources to fund the expansion of property, plant and equipment used in these processes. For example, we have committed capital to advanced three dimensional antenna equipment which are used to produce the next-generation of our Wireless products. We have also committed capital to automate certain manual manufacturing processes and to implement an enterprise resource planning ("ERP") system to enhance visibility, reduce cost, and enhance customer service. In the future, similar investments in property, plant and equipment or research, development and engineering may be funded through internally generated cash flows or through other external resources.

Cost reduction programs. We continue to simplify our operations to optimally match our capacity to the current and anticipated revenues and unit demand of each of our operating segments. Specific actions to simplify our operations will dictate the future expenses associated with our cost reduction programs. Actions taken over the past several years, such as divestitures, plant closures, plant relocations, asset impairments and reduction in personnel, have resulted in the elimination of a variety of future costs. The majority of these costs, not related to the impairment of long-lived assets, represent the annual salaries and benefits of terminated employees, including both those related to manufacturing and those that provided selling, general and administrative services. Also, we have experienced depreciation savings from disposed equipment and reductions in rental expense from the termination of lease agreements. Historically, we have also reduced labor and overhead costs as a result of relocating factories to lower-cost locations, specifically China. The savings created by these cost reduction programs impact cost of goods sold and selling, general and administrative expenses, but the timing of such savings may not be apparent due to other performance factors such as unanticipated changes in demand, changes in unit selling prices, operational challenges and changes in operating strategies.

During the nine months ended September 30, 2011, we incurred expenses of $13.6 million for a number of cost reduction actions approved by our management. These charges include severance and related costs of $12.6 million,

$0.8 million of write-downs of fixed assets no longer in use and a $0.2 million write-down of a manufacturing facility to its fair value. The impaired assets were identified in 2011 and primarily include machinery and equipment that were unable to be cost-efficiently repaired or refitted for other manufacturing purposes. During the nine months ended October 1, 2010, we determined that approximately $29.7 million of our wireless reporting unit's goodwill and identifiable intangible assets were impaired. Also, we recorded a charge of $1.4 million for a number of cost reduction actions. These charges include severance and related payments of $1.0 million and fixed asset impairments of $0.4 million. The impaired assets were identified in 2010 and primarily include machinery and equipment that were unable to be cost-efficiently repaired or refitted for other manufacturing purposes.

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Divestitures. We complete divestitures to streamline our operations, to focus on our core businesses, to reduce our external debt and to strengthen our financial position. For example, we divested the European and Asian businesses of our former Electrical contact products segment in September 2010 for net proceeds of approximately $53.3 million. Also, we completed the sale of Electrical's North American business for an amount immaterial to our Consolidated Financial Statements during January 2010. We have had no continuing material involvement with any of our divested operations after each respective sale.

Management focus. Our executives focus on a number of metrics to evaluate our consolidated financial condition and operating performance. For example, we use consolidated revenue growth, gross margin, operating margin and return on research, development and engineering as performance measures. Operating leverage, or incremental operating profit as a percentage of incremental sales, is also reviewed, which reflects the benefit of absorbing fixed overhead and operating expenses. In evaluating consolidated working capital, liquidity and cash flow, our executives also use performance measures such as days sales outstanding, days payables outstanding, inventory turnover, debt-to-EBITDA leverage, cash conversion efficiency and free cash flow. We define free cash flow as cash flow from operations less capital spending. Additionally, as the continued success of our business is largely dependent on meeting and exceeding our customers' expectations, non-financial performance measures relating to product development, product quality and on-time delivery assists in monitoring customer satisfaction on an on-going basis.

International operations. At September 30, 2011, we had manufacturing operations in the United States of America and China. However, nearly all of our products are manufactured in China and sold to customers in China and other foreign countries. Our net sales are denominated primarily in U.S. dollars, euros and Chinese renminbi. Changing exchange rates often impact our financial results and our period-over-period comparisons. This is particularly true of movements in the U.S. dollar's exchange rate with the Chinese renminbi and the euro, and each of these and other foreign currencies relative to each other. Sales and net earnings denominated in currencies other than the U.S. dollar may result in higher or lower net sales and net earnings upon translation for our U.S. dollar denominated Consolidated Financial Statements. For example, sales in certain divisions of Power and Wireless are denominated primarily in renminbi and euro. Also, net earnings may be affected by the mix of sales and expenses by currency within each of our segments. Foreign currency gains or losses may be incurred when non-functional currency denominated transactions are remeasured to an operation's functional currency for financial reporting purposes. An increase in the percentage of our transactions denominated in non-U.S. currencies may result in increased foreign exchange exposure on our Consolidated Statements of Operations. In addition, we may also experience a positive or negative translation adjustment to equity because our investments in non-U.S. dollar-functional subsidiaries may translate to more or less U.S. dollars in our U.S. Consolidated Financial Statements.

In order to reduce our exposure to currency fluctuations, we may purchase foreign exchange forward contracts and/or currency options. These contracts provide a predetermined exchange rate or range of rates at the time the contract is purchased. This allows us to shift the majority of the risk of currency fluctuation from the date of the contract to a third party for a fee. In determining the use of forward exchange contracts and currency options, we consider the amount of sales, purchases and net assets or liabilities denominated in local currencies, the currency to be hedged and the costs associated with the contracts. At September 30, 2011, we had six foreign exchange forward contracts outstanding to sell forward approximately 3.0 million euro, or approximately $4.2 million, to receive Chinese renminbi. The fair value of these forward contracts was an asset of $0.1 million as determined through the use of Level 2 fair value inputs. These contracts were used to mitigate the risk of currency fluctuations at our Chinese operations.

Income taxes. Our effective income tax rate is affected by the proportion of our income earned in higher tax jurisdictions, such as those in Europe and the United States, and income earned in lower tax jurisdictions, such as Hong Kong and China. This mix of income can vary significantly from one period to another. Additionally, our effective income tax rate will be impacted from period to period by significant transactions and the deductibility of severance and impairment costs and other similar costs. Changes in operations, tax legislation, estimates, judgments and forecasts may also affect our tax rate from period to period. We have benefited over the years from favorable tax incentives and other tax policies. However, there is no guarantee as to how long these benefits will continue to exist, which could materially impact our Consolidated Financial Statements.

Except in limited circumstances, we have not provided for U.S. income and foreign withholding taxes on our non-U.S. subsidiaries' undistributed earnings. Such earnings may include our pre-acquisition earnings of foreign entities acquired through stock purchases, which, with the exception of approximately $8.5 million, are intended to be reinvested outside of the U.S. indefinitely.

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Results of Operations

Three months ended September 30, 2011 compared to the three months ended October 1, 2010

The table below presents our results of operations and the change in those results from period to period in both U.S dollars and percentage (in thousands):

	Three Months Ended September 30, 2011	October 1, 2010	Fav (Unfav) $	Change %	Results as % of net sales 2011	2010
Net sales	$96,014	$121,963	$(25,949)	(21.3)%	100.0 %	100.0 %
Cost of sales	73,913	88,895	14,982	16.9	(77.0)	(72.9)
Gross profit	22,101	33,068	(10,967)	(33.2)	23.0	27.1
Selling, general and administrative expenses	19,798	25,014	5,216	20.9	(20.6)	(20.5)
Severance, impairment and other associated costs	2,968	--	(2,968)	100.0	(3.1)	--
Operating (loss) profit	(665)	8,054	(8,719)	(108.3)	(0.7)	(6.6)
Interest expense, net	(1,917)	(1,127)	790	(70.1)	(2.0)	(0.9)
Other (expense) income, net	(1,088)	3,386	(4,474)	(132.1)	(1.1)	2.8
Loss from continuing operations before income taxes	(3,670)	10,313	(13,983)	(135.6)	(3.8)	8.5
Income tax (benefit) expense	(2,682)	2,177	4,859	223.2	2.8	1.8
Net (loss) earnings from continuing operations	(988)	8,136	(9,124)	(112.1)	(1.0)	(6.7)
Net (loss) earnings from discontinued operations	(270)	6,188	(6,458)	(104.4)	--	(5.1)
Net (loss) earnings	$(1,258)	$14,324	$(15,582)	(108.8)%	(1.3)%	11.7 %

Net sales. Our consolidated net sales decreased by 21.3% primarily as a result of lower demand in Network due to lower industry demand and the utilization of remaining inventory purchased by certain customers during 2010. We also experienced a decline in sales of our wireless products in the mobile handset market. These declines were partially offset by an increase in sales to new antenna customers by Wireless.

Net sales for our three segments for the three months ended September 30, 2011 and October 1, 2010 were as follows (in thousands):

	September 30, 2011	October 1, 2010
Network	$ 43,832	$ 65,228

Power		36,580		36,848
Wireless		15,602		19,887
Net sales	$	96,014	$	121,963

Gross profit. Our consolidated gross margin for the three months ended September 30, 2011 was 23.0% as compared to 27.1% for the three months ended October 1, 2010. The decrease in our gross profit during the three months ended September 30, 2011 was primarily the result of lower demand, higher wage rates, higher raw material costs, and lower pricing for certain Network and Power products. Partially offsetting these decreases was the effect of continued migration of our manufacturing to lower-cost existing facilities located in central China in 2011.

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Selling, general and administrative expenses. Total selling, general and administrative expenses decreased by $5.2 million primarily due to lower costs as a result of expense reductions announced earlier in 2011, lower business volumes, and the effects of prudent expense management.

Research, development and engineering expenses ("RD&E") are included in selling, general and administrative expenses. For the three months ended September 30, 2011 and October 1, 2010, respectively, RD&E was as follows (in thousands):

	2011	2010
RD&E	$ 6,021	$ 7,716
Percentage of sales	6.3 %	6.3 %

Our RD&E spending as a percentage of sales in the quarter ended September 30, 2011 is consistent with the quarter ended October 1, 2010. We believe that future sales in the electronic components markets will be driven by next-generation products. As a result, design and development activities with our OEM customers continue at an aggressive pace that is consistent with market activity. Also, included in RD&E expense for both the three months ended September 30, 2011 and October 1, 2010 was approximately $0.1 million and $0.5 million of legal expenses, respectively, which we incurred in connection with the patent lawsuit filed by Halo Electronics. Refer to further discussion in Note 7, Commitments and contingencies.

Severance, impairment and other associated costs. During the three months ended September 30, 2011, we incurred a charge of $2.2 million for a number of cost reduction actions approved by management and $0.8 million for write-downs of fixed assets that are no longer in use. Refer to Note 11, Severance, impairment and other associated costs, in the Notes to the Unaudited Consolidated Financial Statements for further details. During the three months ended October 1, 2010, we recognized no expense related to severance, impairment or other associated costs.

Interest. Net interest expense increased by $0.8 million in the three months ended September 30, 2011 than October 1, 2010, primarily due to an increase in our debt fee amortization of $0.3 million due to fees incurred in connection with the amendment to our senior revolving credit facility in August 2011 and a write-down of previously capitalized debt fees. In addition, interest expense on our senior revolving credit facility had been allocated between continuing operations and discontinued operations on a pro rata basis based upon the debt repaid from the disposition of our discontinued operations as compared to our total debt outstanding in the quarter ended October 1, 2010 resulting in lower interest expense from continuing operations.

Other. Net other income (expense) is primarily attributable to our net foreign exchange activity related to changes in the varying currencies of our intercompany lending program. During the three months ended September 30, 2011 and October 1, 2010, we recorded net foreign currency losses of approximately $1.6 million and net foreign currency gains of approximately $3.8 million, respectively. The decreased exposure in foreign currency changes from October 1, 2010 to September 30, 2011 was the result of continued simplification efforts and the reduction of legal entities.

Income taxes. For the three months ended September 30, 2011, we recorded a tax benefit of $2.7 million compared to a tax expense of $2.2 million for the three months ended October 1, 2010. The increase in our benefit was primarily due to the absence of the non-deductible goodwill impairment charges that reduced the 2010 tax benefit, partially offset by higher restructuring charges incurred in lower rate tax jurisdictions during the three months ended September 30, 2011.

Discontinued operations. Net (loss) earnings from discontinued operations was ($0.3) million and $6.2 million in the three months ended September 30, 2011 and October 1, 2010, respectively. During the three months ended October 1, 2010, our results from discontinued operations included a gain recorded upon the completion of the sale of our

Electrical business and a gain recorded on the Medtech divestiture as a result of settling an unresolved matter that existed at the date of sale. During the three months ended September 30, 2011, we incurred \$0.3 million of costs in connection with the Electrical sale to reimburse the buyer for certain contingent costs that we were obligated to pay under the sale agreement.

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Also included in our results for the three months ended September 30, 2011 were the release of a $0.7 million reserve for possible warranty claims, a $0.5 million adjustment to decrease our pension liability based on an actuarially determined estimate of our pension expense for 2011, $0.2 million contingent liability recorded in connection with a legal matter (refer to discussion of legal matter in Note 7, Commitments and contingencies), $0.1 million accural for a dispute with a service provider and $0.4 million for certain ERP implementation costs expensed in the quarter. These items in total had a net favorable impact on net operating loss in the quarter ended September 30, 2011 of approximately $0.5 million.

A summary of our net earnings (loss) from each of our discontinued operations for the three months ended September 30, 2011 and October 1, 2010 is as follows (in thousands):

	Three months ended September 30, 2011	October 1, 2010
Electrical	$ (270)	$ 5,203
Medtech	--	924
MEMS	--	61
Total	$ (270)	$ 6,188

Results of Operations

Nine months ended September 30, 2011 compared to the nine months ended October 1, 2010

The table below presents our results of operations and the change in those results from period to period in both U.S dollars and percentage (in thousands):

	Nine Months Ended		Fav (Unfav)	Change	Results as % of net sales	
	September 30, 2011	October 1, 2010	$	%	2011	2010
Net sales	$ 278,811	$ 331,296	$ (52,485)	(15.8)%	100.0 %	100.0 %
Cost of sales	215,913	247,768	31,855	12.9	(77.4)	(74.8)
Gross profit	62,898	83,528	(20,630)	(24.7)	22.6	25.2
Selling, general and administrative expenses	62,594	72,401	9,807	13.5	(22.5)	(21.9)
Severance, impairment and other associated costs	13,591	31,094	17,503	56.3	(4.9)	(9.4)
Cost related to unsolicited takeover attempt	1,916	--	(1,916)	--	(0.7)	--
Operating loss	(15,203)	(19,967)	4,764	(23.9)	(5.5)	(6.0)
Interest expense, net	(4,368)	(3,748)	(620)	16.5	(1.6)	(1.1)
Other income (expense), net	621	(4,143)	4,764	(115.0)	0.2	(1.3)

Loss from continuing operations before income taxes	(18,950)	(27,858)	8,908	(32.0)	(6.8)	(8.4)
Income tax (benefit) expense	(8,512)	2,032	10,544	518.9	3.1	(0.6)
Net loss from continuing operations	(10,438)	(29,890)	19,452	(65.1)	(3.7)	(9.0)
Net income (loss) from discontinued operations	342	(8,980)	9,322	(103.8)	0.1	(2.7)
Net loss	$(10,096)	$(38,870)	$28,774	(74.0)%	(3.6)%	(11.7)%

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Net Sales. Our consolidated net sales decreased by 15.8% in the nine months ended September 30, 2011 as compared to the prior year period primarily as a result of the decline in Network sales due to lower industry demand, utilization of inventory purchased by certain customers in 2010, and due to sales of our wireless products in the mobile handset market, which were negatively impacted by the loss of certain business with a major OEM customer due to a sourcing change. The foreign currency effect on our US dollar reported sales were neutral when comparing the results for the nine months ended September 30, 2011 and October 1, 2010.

Net sales for our three segments for the nine months ended September 30, 2011 and October 1, 2011 were as follows (in thousands):

		September 30, 2011		October 1, 2010
Network	$	129,767	$	169,446
Power		107,147		95,147
Wireless		41,897		66,703
Net sales	$	278,811	$	331,296

Gross profit. Our consolidated gross margin for the nine months ended September 30, 2011 was 22.6% as compared to 25.2% for the nine months ended October 1, 2010. The decrease in our gross profit during the nine months ended September 30, 2011 was primarily the result of lower demand in Network and Wireless, higher wage rates, higher raw material costs, and price concessions for certain Network products. Partially offsetting these decreases to our gross profit was increased demand in Power products and the continued migration of our manufacturing to existing facilities located in lower cost areas in central China.

Selling, General and Administrative Expenses. Total selling, general and administrative expenses decreased $9.8 million primarily due to prudent expense management in light of lower sales in Wireless and Network and lower costs as a result of expense reduction actions announced earlier this year.

Research, development and engineering expenses (“RD&E”) are included in selling, general and administrative expenses. For the nine months ended September 30, 2011 and October 1, 2010, respectively, RD&E was as follows (in thousands):

		2011			2010	
RD&E	$	20,525		$	22,487	
Percentage of sales		7.4	%		6.8	%

Our RD&E spending tends to develop at a rate which is less dramatic than our sales changes. Due to decreased sales levels experienced in the nine months ended September 30, 2011, our RD&E as a percentage of sales increased. We believe that future sales in the electronic components markets will be driven by next-generation products. As a result, design and development activities with our OEM customers continue at an aggressive pace that is consistent with market activity. Also, included in RD&E expense for both the nine months ended September 30, 2011 and October 1, 2010 was approximately $0.8 million and $1.9 million of legal expenses, respectively, which we incurred in connection with the patent lawsuit filed by Halo Electronics. Refer to further discussion in Note 7, Commitments and contingencies.

Severance, Impairment and Other Associated Costs. During the nine months ended September 30, 2011, we incurred expenses of $12.8 million for a number of cost reduction actions approved by management and $0.8 million of write-downs of fixed assets that are no longer in use. The $12.8 million of charges related to cost reduction actions includes severance and related payments of $12.6 million and a $0.2 million write down of a manufacturing facility to its fair value.

During the nine months ended October 1, 2010, we determined that approximately $29.7 million of our wireless segment's goodwill and identifiable intangible assets were impaired, including $3.6 million of patented technology related to our audio products. Additionally, we incurred a charge of $1.4 million for a number of cost reduction actions, which included severance and related payments of $1.0 million and fixed asset impairments of $0.4 million. The impaired assets primarily included machinery and equipment that was unable to be repaired.

Interest. Net interest expense was $0.6 million higher in the nine months ended September 30, 2011 than October 1, 2010, primarily due to an increase in our debt fee amortization of $0.3 million due to fees incurred in connection with the amendment to our senior revolving credit facility in August 2011 and a write-down of our previously capitalized fees. In addition, during the nine months ended October 1, 2010, interest expense on our senior revolving credit facility had been allocated between continuing operations and discontinued operations on a pro rata basis based upon the debt repaid from the disposition of our discontinued operations as compared to our total debt outstanding.

Other. Other income for the nine months ended September 30, 2011 was primarily attributable to the reversal of a contingency accrual that was originally recorded in purchase accounting for a legacy acquisition and, also, net foreign currency loss of approximately $1.2 million. The primary components of other expense during the nine months ended October 1, 2010 were net foreign currency losses of approximately $3.7 million, which were primarily related to changes in the varying currencies of our intercompany lending program. The decreased exposure in foreign currency changes from October 1, 2010 to September 30, 2011 was the result of continued simplification efforts and the reduction of legal entities.

Income Taxes. The effective tax rate for the nine months ended September 30, 2011 was a tax benefit of 44.9% compared to an expense of 7.3% for the nine months ended October 1, 2010. The increase in our benefit was primarily due to the absence of the non-deductible goodwill impairment charges that reduced the 2010 tax benefit and the release of certain tax reserves in the nine months ended September 30, 2011. The release was due to actions we are taking to streamline our legal entity structure, specifically the dissolution of a non-U.S. legal entity which we no longer operate, and expiration of statute. These favorable changes were partially offset by higher restructuring charges incurred in lower tax rate jurisdictions during the nine months ended September 30, 2011 and additional reserve related to a foreign jurisdiction.
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Discontinued Operations. Net earnings from discontinued operations were approximately $0.3 million during the nine months ended September 30, 2011 as compared to a loss of approximately $9.0 million in the nine months ended October 1, 2010. During the nine months ended September 30, 2011, we recorded $0.6 million of income to reflect updated estimates of the net proceeds we expect to receive upon the disposition of the remaining operations of Electrical, partially offset by $0.3 million of costs incurred in connection with the Electrical sale to reimburse the buyer for certain contingent costs that we were obligated to pay under the sale agreement.
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The loss from discontinued operations in the nine months ended October 1, 2010 was primarily attributable to a charge to reduce the assets of Electrical to the net proceeds we received upon completion of its sale.

A summary of our net earnings (loss) from each of our discontinued operations for the nine months ended September 30, 2011 and October 1, 2010 is as follows (in thousands):

	Nine Months Ended	
	September 30, 2011	October 1, 2010
Electrical	$ 342	$ (9,251)
Medtech	--	493
MEMS	--	(222)
Total	$ 342	$ (8,980)

Business Outlook

Our levels of net sales, customer portfolio and product mix have a significant impact on our gross margin, results of operations and cash flow. Specifically, we experienced consolidated sales and operating performance during 2011 which were lower than 2010 levels. This was primarily a result of decreased sales volume across Wireless and Network. In addition, higher costs resulted from wage rates and material costs. To address these issues, we continue to focus on transitioning our manufacturing from locations with higher wage rates, such as those in southern China, to lower-cost areas in the central regions of China. Also, we implemented overall price increases where possible to combat rising material costs and increasing minimum wage rates. We continue to gain design wins with new Wireless OEM's and further our existing relationships with other Wireless customers in an effort to address the declining segment revenues caused by the loss of the majority of our sales from a former major handset OEM customer due to the customer's decision to make a sourcing change. Also, our efforts toward streamlining our overall general and administrative expenses to achieve an optimal level of spending that is appropriate for the size and structure of our company have been initially evidenced by the lower expenses incurred during the three and nine months ended September 30, 2011. However, we remain focused on reducing our general and administrative expenses, and expect to experience further improvements during 2011 and 2012. Finally, we plan to enhance our information technology capabilities by implementing a new ERP system. We believe that the ERP will enable us to realize working capital efficiencies, streamline our operations and enable us to further reduce our overall cost structure.

We continue to commit resources to the development of new technologies and products that have higher forecasted margins, to the automation of certain manufacturing processes and to the expansion of our international sales, marketing and engineering teams in regions closest to our customers. Also, we plan on continuing to adjust our marketing and engineering efforts at Wireless in order to increase revenue streams from a more diverse base of customers. Our focus will be on Wireless products with higher forecasted margins, while shifting from those markets where we expect limited returns. For example, we decided to eliminate the audio components business to streamline our operations and focus on those Wireless products that are forecasted with better returns.

Liquidity and Capital Resources

Our working capital as of September 30, 2011 was $41.8 million, compared to $51.3 million as of December 31, 2010. The decrease of $9.5 million was primarily due to a decline in cash and cash equivalents and accounts receivable, which were partially offset by a decrease in accrued expenses and other current liabilities. Cash and cash equivalents declined $19.5 million from $35.9 million as of December 31, 2010 to $16.4 million as of September 30, 2011. We used cash primarily to repay debt and fund cost reduction actions.

We present our statement of cash flows using the indirect method. Our management has found that investors and analysts typically refer to changes in accounts receivable, inventory and other components of working capital when analyzing operating cash flows. Also, changes in working capital are more directly related to the way we manage our business' cash flow than items such as cash receipts from the sale of goods, which would appear using the direct method. Cash flows from discontinued operations have been separated from continuing operations and are disclosed in aggregate by each cash flow activity. A majority of the cash used in 2011 was used to repay debt and fund cost reduction actions as planned.

Net cash used in operating activities was $5.5 million for the nine months ended September 30, 2011 as compared to net cash provided by operating activities of $28.1 million in the comparable period of 2010, a decrease of $33.6 million. The decline was primarily attributable to a net decrease in cash provided by working capital changes in the first nine months of 2011 as compared to the same period in 2010 and higher net operating losses, excluding goodwill and intangible asset impairments, incurred in 2011 as compared to the same period of 2010. Although we experienced a net operating cash outflow during the nine months ended September 30, 2011, we believe we will have appropriate liquidity to support our operations in the future.

Capital expenditures were $8.8 million during the nine months ended September 30, 2011 and $7.7 million for the nine months ended October, 2010. The increase of $1.1 million was due to a focus in the first half of 2011 to expand new investment to programs which we believe are essential to our future growth, primarily related to our wireless and network segments and to the implementation of our ERP system. We make capital expenditures to invest in new products, expand production capacity and to improve our operating efficiency. We plan to continue making such expenditures at a similar or increased manner in the future when necessary.

We made $3.1 million of dividend payments during the nine months ended September 30, 2011. We do not anticipate that we will make dividend payments in periods subsequent to the quarter ended December 30, 2011. We believe that use of these funds can generate a higher return if utilized to continue the execution of our strategic initiatives, in particular in the near term to improve our wireless business, to continue our restructuring program and to implement a new ERP system.

Our domestic defined benefit retirement plan is currently under audit by the Pension Benefit Guarantee Corporation ("PBGC"). Initial communications from the PBGC have indicated that the sale of Electrical's North American operations may have resulted in a partial plan termination, which may require us to accelerate the funding of up to approximately $7.3 million to this defined benefit plan. A partial plan termination would result in a cash payment to fund our plan and will not directly result in additional expenses. Recently, the PBGC has publicly stated that it will reconsider its 4062(e) proposed rule, a rule applicable to partial plan terminations. We are continuing discussions with the PBGC on this matter.

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On September 30, 2011, we had a senior revolving credit facility that provided for borrowings not to exceed $60.8 million in U.S. dollars, euros and yen, with a multicurrency facility that provides for the issuance of letters of credit in an aggregate amount not to exceed the U.S. dollar equivalent of $10.0 million. We had approximately $33.0 million of borrowings outstanding under the credit facility as of September 30, 2011 and one standby letter of credit outstanding in the aggregate amount of $1.2 million securing transactions entered into in the ordinary course of business. This letter of credit was terminated subsequent to September 30, 2011. The average borrowings outstanding on our senior credit facility during both the three and nine months ended September 30, 2011 was approximately $44.6 million and $42.5 million, respectively. As of September 30, 2011, we were in compliance with all covenants of our senior revolving credit facility agreement.

In order to continue execution on our strategic priorities, we amended our senior revolving credit facility on August 5, 2011. We worked closely with the banks to ensure that the amended credit facility provides us with the additional flexibility we need to continue making progress on our strategic turnaround plan. These revisions included a reduction to the borrowings permitted under the credit facility from $100.0 million to $70.0 million, which was further reduced to $60.8 million following a debt repayment in September 2011, and an increase in the interest rates on both the unborrowed portion of the commitment and on the outstanding borrowings., The maturity date of the facility continues to be February 28, 2013.

We paid total fees and expenses of approximately $1.4 million in connection with the amendment, of which $1.2 million have been capitalized as debt issuance costs and will be amortized on a straight-line basis through the maturity date of the debt.

Under the amended credit facility, the fee on the unborrowed portion of the commitment ranges from 0.40% to 0.50% of the total commitment and the credit margin spread on the outstanding borrowings ranges from 3.25% to 4.50%, depending on the total debt-to-EBITDA ratio. In calculating the total debt-to-EBITDA ratio, the total debt includes debt outstanding under the credit facility and the convertible senior notes.

We must maintain certain financial covenants which are measured at the end of each fiscal quarter. The primary covenants are total debt, excluding our convertible senior notes, and fixed charges as compared to our rolling 12-month EBITDA and a minimum rolling six-month EBITDA. We revised the EBITDA definition used in the covenant calculations to include certain restructuring cost addbacks in 2011 and 2012 and have amended the covenant levels. As amended, our minimum required six-month rolling EBITDA as defined in the credit agreement is $8.25 million for the six-month period ended December 30, 2011 and $9.5 million for the six-month period ended March 30, 2012. If we are unable to maintain the required EBITDA levels relative to our total debt or fixed charges and to the minimum levels required, we would default on our covenants. A default, if not waived by our lenders, may result in our lenders electing to declare our outstanding borrowings immediately due and payable and terminate all commitments to extend further credit. Based on our current outlook and forecast of financial results, we believe that we will continue generating sufficient EBITDA to remain compliant with the amended debt covenants. See also Item 1a—Risk Factors—"Our debt levels could adversely affect our financial position, our liquidity and the perception of our financial condition in the financial markets."=

We have also agreed to limit our borrowings to an amount not to exceed total eligible accounts receivable and cash, to maintain available cash of $5.8 million, to limit our capital expenditures to specific levels in 2011 and 2012, and to suspend payment of dividends following a payment in the quarter ended December 30, 2011.

Refer to Note 8, Debt, to the Consolidated Financial Statements for further details regarding the amended credit facility.

We have $50.0 million in convertible senior notes, which will mature on December 15, 2014. The notes bear a coupon rate of 7.0% per annum that is payable semi-annually in arrears on June 15 and December 15 of each year. We expect to pay approximately $3.5 million of interest on the convertible senior notes during 2011. Refer to Note 8, Debt, to the Consolidated Financial Statements for further details.

We are a party to various legal proceedings, claims and assessments that arise in the ordinary course of business, and may continue to incur significant costs in defending or settling legal matters. The total amount and timing of the expected future payments related to these matters cannot be estimated due to the uncertainty of the duration of the legal proceedings and the ultimate scope of other claims. However, an unfavorable outcome in a single matter or in multiple legal matters during the same reporting period could have a material adverse effect on our consolidated financial position, results from operations and cash flows.

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We are a defendant in a lawsuit filed in March 2007 by Halo Electronics, Inc. in the United States District Court, District of Nevada. The case is captioned Halo Electronics, Inc. v. Pulse Electronics, Inc. and Pulse Electronics Corp., Case No. 2:07-cv-00331-PMP-PAL. The plaintiff claims that we infringe certain U.S. patents related to an electronic surface mount package, and is seeking injunctive relief and damages. Discovery has ended, and on September 6, 2011, the Court ruled on numerous pending motions for summary judgment. The Court denied the plaintiff's motion for summary judgment of infringement by our products with the exception of one claim relating to one representative product. The Court partially granted one of our summary judgment motions, in effect, excluding any liability for direct infringement for products sold outside of North America on all of plaintiff's claims.

Although a trial date has not yet been scheduled, the Court has ordered the parties to file a proposed joint pre-trial order for the case by November 29, 2011. The plaintiff has previously produced expert reports asserting infringement and liability in the amount of $34.3 million, plus requests for trebling and attorneys fees. However, these reports do not take into account the Court's September 2011 ruling, which excluded direct foreign sales and therefore may reduce our potential exposure to significantly less than half of the amount claimed by the plaintiff. In addition, we are aware that similar cases have been brought by Halo Electronics against certain of our competitors, and that at least one of our competitors commenced a similar independent patent litigation against Halo Electronics. Although we are not familiar with the specific details of these cases or the plaintiff's claims, we believe that one of these cases has recently been settled on terms that, among other things, provide for significantly less up-front cash to Halo Electronics than the amount of damages that it has claimed in our case.

In light of the Court's summary judgment order and its ruling that we are not liable with respect to direct infringement for products sold outside North America we recorded a charge of approximately $0.2 million as selling, general and administrative expense in the three months ended September 30, 2011. We intend to continue presenting a vigorous defense against the remaining claims in the case, to maintain our counterclaim that Pulse owes no liability whatsoever to Halo due to the invalidity of the Halo patents, to contest the amount of damages asserted by Halo and its expert, and to consider our rights of appeal with respect to any adverse rulings. However, management is currently unable to determine whether any additional loss will occur or to estimate the range of such loss. Therefore, no other liability has been accrued.

In March 2011, we received an unsolicited proposal from Bel Fuse to acquire all of our outstanding shares. Our board of directors unanimously determined that Bel Fuse's proposal significantly undervalued our business and was not in the best interests of our company, our shareholders and other constituents. Bel Fuse had also nominated two directors for election to our board. At our annual meeting of shareholders on May 18, 2011, the Bel Fuse nominees were not elected to our board. During the nine months ended September 30, 2011 we incurred $1.9 million of legal and professional fees and other costs related to Bel Fuse's unsolicited takeover attempt. The majority of these costs represent fees of our financial and legal advisors. We do no not expect to incur significant additional fees or similar costs related to this matter.

During the nine months ended September 30, 2011, we paid $1.9 million related to an audit of one of our foreign subsidiaries' income tax filings. Settlement of this matter may result in additional payments of as much as $4.4 million. This amount has been fully accrued for as of September 30, 2011, however, we do not anticipate additional payments related to this matter before 2012.

On February 10, 2011, we announced that our corporate headquarters located in Trevose, Pennsylvania would be consolidated into our U.S. operational headquarters in San Diego, California. This consolidation will occur during 2011 in connection with our actions to simplify and streamline our organizational structure. We estimate that we will incur approximately $3.1 million of total severance and other associated costs over the remainder of 2011 and 2012 related to the consolidation of our headquarters, which will generate an estimated annual cost savings of approximately $1.5 million once the transition is complete. Cash payments resulting from the severance charges recorded in the nine months ended September 30, 2011 will be completed within approximately one year.

We continue to streamline our administrative functions and lower our overall production costs. As a result, we anticipate incurring further charges and cash payments for severance and other related adjustments throughout 2011. As of November 9, 2011, these plans were not finalized or estimable and there has been no formal notification of further actions.

During the nine months ended September 30, 2011, we experienced no material changes to our contractual obligations as disclosed in our Annual Report on Form 10-K for the year ended December 31, 2010.

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Considering the business issues mentioned above and other risks inherent in our company, we believe we have appropriate liquidity to fund our business requirements. This belief is primarily based on our current balances of cash and cash equivalents and our access to our amended credit facility. At September 30, 2011, we were in compliance with all covenants of our credit facility agreement.

We believe that the combination of cash on hand and, if necessary, borrowings under our amended credit facility will be sufficient to satisfy our operating cash requirements. In addition, we may use internally generated funds or obtain additional borrowings or equity offerings for suitable acquisitions of businesses or assets.

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Currently, a majority owned subsidiary holds approximately $1.9 million of our consolidated cash and cash equivalents. During the third quarter of 2011, $9.2 million of this cash was used to make payments on outstanding borrowings under our senior revolving credit facility. Permanent access to funds from this subsidiary could be in the form of a dividend to its shareholders, which could result in income withholding taxes and distributions to minority shareholders. As of September 30, 2011, there are no plans to repatriate funds held at this majority owned subsidiary. Earlier in 2011, this majority owned subsidiary announced a plan to purchase its own common stock that is publicly traded on a non-U.S. exchange and has purchased approximately $4.1 million of its own common stock using its cash on hand during the nine months ended September 30, 2011. We do not anticipate any additional spending for common stock buyback plans in the foreseeable future.

Our retained earnings are free from legal or contractual restrictions as of September 30, 2011, with the exception of approximately $29.8 million of subsidiary retained earnings primarily in China, that are restricted in accordance with Section 58 of the PRC Foreign Investment Enterprises Law. The $29.8 million includes approximately $6.7 million of retained earnings of a majority owned subsidiary. The amount restricted in accordance with the PRC Foreign Investment Enterprise Law is applicable to all foreign investment enterprises doing business in China. The restriction applies to 10% of our net earnings in China, limited to 50% of the total capital invested.

We do not maintain any off-balance sheet arrangements, transactions, obligations or other relationships with unconsolidated entities that would be expected to have a material current or future effect on our financial condition or results of operations.

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New and Recently Adopted Accounting Pronouncements

Please see Note 1, Accounting policies, to the Notes to Unaudited Consolidated Financial Statements beginning on page 7 for a description of new and recently adopted accounting pronouncements.

Item 3: Quantitative and Qualitative Disclosures About Market Risk

There were no material changes in market risk exposures that affect the quantitative and qualitative disclosures presented in our Form 10-K for the year ended December 31, 2010.

Item 4: Controls and Procedures

An evaluation was performed under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the disclosure controls and procedures pursuant to Rule 13a-15 under the Exchange Act of 1934 as of September 30, 2011. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that the disclosure controls and procedures are effective to ensure that information required to be disclosed by us in the reports that we file or submit is recorded, processed, summarized and reported, as specified in the Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Act is accumulated and communicated to the issuer's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

There were no changes in these controls or procedures that occurred during the nine months ended September 30, 2011 that have materially affected, or are reasonably likely to materially affect, these controls or procedures.

A company’s internal control over financial reporting is a process designed to provide reasonable, not absolute, assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company’s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company’s assets that could have a material effect on the financial statements. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate.

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PART II. OTHER INFORMATION

Item 1 Legal Proceedings

Refer to Note 7, Commitments and contingencies, on page 12 of this Form 10-Q for a discussion of certain legal proceedings.

Item 1a Risk Factors

Risk Factors are on page 37

Item 6 Exhibits

(a) Exhibits

The Exhibit Index is on page 45

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Item 1aRisk Factors

Factors That May Affect Our Future Results (Cautionary Statements for Purposes of the "Safe Harbor" Provisions of the Private Securities Litigation Reform Act of 1995)

Our disclosures and analysis in this report contain forward-looking statements. Forward-looking statements reflect our current expectations of future events or future financial performance. You can identify these statements by the fact that they do not relate strictly to historical or current facts. They often use words such as "anticipate", "estimate", "expect", "project", "intend", "plan", "believe" and other similar terms. These forward-looking statements are based on o current plans and expectations.

Any or all of our forward-looking statements in this report may prove to be incorrect. They may be affected by inaccurate assumptions we might make or by risks and uncertainties which are either unknown or not fully known or understood. Accordingly, actual outcomes and results may differ materially from what is expressed or forecasted in this report.

We sometimes provide forecasts of future financial performance and liquidity. The risks and uncertainties described under "Risk Factors" as well as other risks identified from time to time in other Securities and Exchange Commission reports, registration statements and public announcements, among others, should be considered in evaluating our prospects for the future. We undertake no obligation to release updates or revisions to any forward-looking statement, whether as a result of new information, future events or otherwise.

The following factors represent what we believe are the major risks and uncertainties in our business and are listed in no particular order. These risks are not the only ones that we face. Additional risks not presently or fully known to us or that we currently deem immaterial may also impair our business operations.

Cyclical changes in the markets we serve could result in a significant decrease in demand for our products, which may reduce our profitability and/or our cash flow.

Our components are used in various products sold in the electronics market. Generally these markets are cyclical based on the end consumers' demand, so interest in our components also reflects the overall demand for products in the electronics market. A contraction in the electronics market would result in a decrease in sales of our products, as our customers:

- may cancel existing orders;
- may introduce fewer new products;
- may discontinue current product lines; and
- may decrease their inventory levels.

A decrease in demand for our products could have a significant adverse effect on our operating results, profitability and cash flows which may adversely affect our liquidity, our ability to retire debt or our ability to comply with debt covenants. Accordingly, we may experience volatility in our revenues, profits and cash flows.

Reduced prices for our products may adversely affect our profit margins if we are unable to reduce our cost structure.

The average selling prices for our products tend to decrease over their life cycle. In addition, foreign currency movements and the desire to retain market share increase the pressure on our customers to seek lower prices from their suppliers. As a result, our customers are likely to continue to demand lower prices from us. To maintain our margins and remain profitable, we must continue to meet our customers' design needs while concurrently reducing costs through efficient raw material procurement, process and product improvements and focusing our operating expense levels. Our profit margins and cash flows may suffer if we are unable to reduce our overall cost structure relative to decreases in sales prices.

Rising raw material and production costs may decrease our gross margin.

We use commodities such as copper and plastic resins in manufacturing our products. Prices of these and other raw materials have experienced significant volatility in the past. Other manufacturing costs, such as direct and indirect labor, energy, freight and packaging costs, also directly impact the costs of our products. If we are unable to pass these increased costs to our customers or recover the increased costs through production efficiencies, our gross margins may suffer.

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An inability to adequately respond to changes in technology, applicable standards or customer needs may decrease our sales.

We operate in an industry characterized by rapid change caused by the frequent emergence of new technologies and standards. Generally, we expect life cycles for products in the electronic components industry to be relatively short. This requires us to anticipate and respond rapidly to changes in industry standards and customer needs, and, also, to develop and introduce new and enhanced products on a timely and cost effective basis. Our engineering and development teams place a priority on working closely with our customers to design innovative products and to improve our manufacturing processes. Improving performance and reducing costs for our customers requires the continual development of new products and/or improvement to the components of existing products. Our inability to react quickly and efficiently to changes in technology, standards or customer needs may decrease our sales or margins.

If our inventory becomes obsolete, then our future performance and operating results will be adversely affected.

The life cycles of our products depend heavily upon the life cycles of the end products for which our products are designed. End products with short life cycles require us to closely manage our production and inventory levels, as adverse changes in end market demand may make our products obsolete. Specifically, during market slowdowns this may result in significant charges for inventory write-offs. Our future operating results may be adversely affected by material levels of inventory reserves for obsolete or excess inventory.

Our decisions to strategically divest current businesses or our inability to capitalize on prior or future acquisitions may adversely affect our business.

We have completed numerous acquisitions and divestitures in the past and we may continue to seek acquisitions to grow our businesses or divest operations to focus on our core businesses. We may fail to derive significant benefits from such transactions. Also, if we fail to achieve sufficient financial performance from an acquisition, certain long-lived assets, such as property, plant and equipment and goodwill and other intangible assets, could become impaired and result in the recognition of an impairment loss similar to the losses recorded in 2010.

The success of our acquisitions depends on our ability to:

- successfully execute the integration or consolidation of the acquired operations into our existing businesses;
- develop or modify the financial reporting and information systems of the acquired entity to ensure overall financial integrity and adequacy of internal control procedures;
- identify and take advantage of cost reduction opportunities; and
- further penetrate existing markets with the product capabilities we may acquire.

Integration of acquisitions may take longer than we expect and may never be achieved to the extent originally anticipated. This could result in lower than expected business growth or higher than anticipated costs. In addition, acquisitions may:

- cause a disruption in our ongoing business;
- distract our managers;
- increase our debt and leverage;
- unduly burden other resources in our company; and
- result in an inability to maintain our historical standards, procedures and controls, which may result in non-compliance with external laws and regulations or contractual requirements.

Alternatively, we may also consider making strategic divestitures, which may also:

- cause a disruption in our ongoing business;
- distract our managers;
- unduly burden other resources in our company; and
- result in an inability to maintain our historical standards, procedures and controls, which may result in non-complaince with external laws and regulations or contractual requirements.

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We may record impairment losses in the future. We assess the impairment of long-lived assets whenever events or changes in circumstances indicate an asset's carrying value may not be recoverable. Factors we consider important that could trigger an impairment review include significant changes in the use of any asset, changes in trends of historical operating performance, a significant decline in the price of our common stock, changes in projected operating performance and significant negative economic trends.

An inability to identify, consummate or integrate acquisitions or a lack of appropriate investment in capital expenditure and research, development and engineering may slow our future growth.

We may identify and possibly consummate additional acquisitions in the future to further diversify our businesses and to penetrate or expand important markets. We may not be able to identify suitable acquisition candidates at reasonable prices. Even if we identify promising acquisition candidates, the timing, price, structure and success of future acquisitions are uncertain. An inability to consummate or integrate attractive acquisitions may reduce our growth rate and our ability to penetrate new markets.

We remain committed to technological development through investing in research, development and engineering activities focused on designing next-generation products, improving our existing products and improving our manufacturing processes. If we determine that any of our manufacturing processes would benefit from capital investment, we may allocate resources to fund the expansion of property, plant and equipment used in these processes. An inability to allocate resources to the appropriate investment or an inability to allocate the appropriate amount of resources to an investment may reduce our ability to grow organically.

If any of our major customers terminates a substantial amount of existing agreements, chooses not to enter into new agreements or elects not to submit additional purchase orders for our products, then our business may suffer.

Most of our sales are made on a purchase order basis. We have a concentration of several primary customers that we rely on for a material amount of these purchase orders. To the extent we have agreements in place with these customers, most of these agreements are either short-term in nature or provide these customers with the ability to terminate the arrangement. Such agreements typically do not provide us with any material recourse in the event of non-renewal or early termination.

We will lose business and our revenues may decrease if one or more of these major customers:

- does not submit additional purchase orders;
- does not enter into new agreements with us;
- elects to reduce or prolong their purchase orders; or
- elects to terminate their relationship with us.

If we do not effectively manage our business when facing fluctuations in the size of our organization, then our business may be disrupted.

We have grown both organically and as a result of acquisitions. We have also contracted as a result of declines in global demand, cost reduction initiatives and through divestitures. We may significantly reduce or expand our workforce and facilities in response to rapid changes in demand for our products due to prevailing global market conditions. These rapid fluctuations place strains on our resources and systems. If we do not effectively manage our resources and systems, our business may be adversely affected.

Uncertainty in demand for our products may adversely affect our results of operations and financial condition.

We have very little visibility into our customers' future purchasing patterns and are highly dependent on customer forecasts. However, these forecasts are non-binding and can often significantly change. Given the fluctuation in growth rates and the occasional cyclicality of demand for our products, as well as our reliance on our customer's forecasts, it is difficult to accurately manage our production schedule, equipment and personnel needs, as well as our raw material and working capital requirements.

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Our failure to effectively manage these issues may result in:

- production delays;
- increased costs of production;
- excessive inventory levels and reduced financial liquidity;
- an inability to make timely deliveries; and
- a decrease in profits or cash flows

A decrease in the availability of our key raw materials could adversely affect our profit margins.

We use several types of raw materials in the manufacturing of our products, including:

- base metals such as copper;
- ferrite cores;
- plastics and plastic resins; and
- rare earth metals.

Some of these materials are only produced by a limited number of suppliers. The limited amount of suppliers may restrict our ability to obtain these raw materials in sufficient quantities, at reasonable prices or in a timely manner to meet customer demand for our products. A lack of availability or a delay in obtaining any of the raw materials used in our products could adversely affect our manufacturing costs and profit margins. In addition, if the price of our raw materials increases significantly over a short period of time due to increased market demand or shortage of supply, customers may be unwilling to bear the increased price for our products and we may be forced to sell our products containing these materials at lower prices causing a reduction in our profit margins.

Competition may result in reduced demand for our products and reduce our sales.

We frequently encounter strong competition within individual product lines from various competitors throughout the world. We compete principally on the basis of:

- engineering expertise;
- product quality and reliability;
- global design and manufacturing capabilities;
- breadth of product line;
- price;
- customer service; and
- delivery time.

Our inability to successfully compete on any or all of the above or other factors may result in reduced sales.

Fluctuations in foreign currency exchange rates may adversely affect our operating results.

We manufacture, assemble, and sell our products in various regions of the world and export and import these products to and from a large number of countries. Fluctuations in exchange rates could negatively impact our cost of production and sales which, in turn, could decrease our operating results and cash flow. In addition, if the functional currency of our manufacturing costs strengthen as compared to the functional currency of our competitors' manufacturing costs, our products may become more costly than our competitors. Although we engage in limited derivative transactions, including foreign currency forward contracts, which may reduce our transaction and economic exposure to foreign currency fluctuations, these measures may not eliminate or substantially reduce our risk in the future.

Our international operations subject us to the risks of unfavorable political, regulatory, labor and tax conditions in other countries.

We manufacture and assemble most of our products in locations outside the United States, such as China, and a majority of our revenues are derived from sales to customers outside the United States. Our future operations and earnings may be adversely affected by the risks related to, or any other problems arising from, operating in international locations and markets.

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Risks inherent in doing business internationally may include:

- the inability to repatriate or transfer cash on a timely or efficient basis;
- economic and political instability;
- expropriation and nationalization;
- trade restrictions;
- capital and exchange control programs;
- transportation delays;
- uncertain rules of law; and
- unexpected changes in the laws and policies of the United States or of the countries in which we manufacture and sell our products.

The majority of our manufacturing occurs in the PRC. Although the PRC has a large and growing economy, its political, legal and labor developments entail uncertainties and risks. For example, at certain times in the past we have encountered difficulties in attracting and retaining the level of labor required to meet our customers' demands. Also, wages have been increasing rapidly over the last several years in China. While China has been receptive to foreign investment, its investment policies may not continue indefinitely into the future and future policy changes may adversely affect our ability to conduct our operations in these countries or the costs of such operations.

We have benefited in prior years from favorable tax incentives and we operate in countries where we realize favorable income tax treatment relative to the U.S. statutory rate. We have been granted special tax incentives, including tax holidays, in jurisdictions such as the PRC. This favorable situation could change if these countries were to increase rates or discontinue the special tax incentives, or if we discontinue our manufacturing operations in any of these countries and do not replace them with operations in locations with similar tax incentives or policies. Accordingly, in the event of changes in laws and regulations affecting our international operations, we may not be able to continue to recognize or take advantage of similar benefits in the future.

Liquidity requirements could necessitate movements of existing cash balances which may be subject to restrictions or may cause unfavorable tax and earnings consequences.

A significant portion of our cash is held offshore by international subsidiaries and may be denominated in currencies other than the U.S. dollar. While we intend to use a significant amount of the cash held overseas to fund our international operations and growth, if we encounter a significant need for liquidity domestically or at a particular location that we cannot fulfill through borrowings, equity offerings, or other internal or external sources, we may experience unfavorable tax and earnings consequences due to cash transfers. For example, these adverse consequences would occur if the transfer of cash into the United States is taxed with no available foreign tax credit to offset the U.S. tax liability, resulting in lower earnings. Also, we may be prohibited or significantly delayed when transferring cash from a country such as the PRC, as there are foreign exchange ceilings imposed by local governments and often lengthy approval processes which foreign governments require for international cash transfers. We have not experienced any significant liquidity restrictions in any of the countries in which we operate and we do not presently foresee any.

At September 30, 2011, a majority owned subsidiary holds approximately $1.9 million of our consolidated cash and cash equivalents. During the third quarter of 2011, $9.2 million of this cash was used to make payments on outstanding borrowings under our senior revolving credit facility. Permanent access to funds from this subsidiary could be in the form of a dividend to its shareholders, which could result in income withholding taxes and distributions to minority shareholders. As of September 30, 2011, there are no plans to repatriate funds held at this majority owned subsidiary. During 2011, this majority owned subsidiary announced a plan to purchase its own common stock that is publically traded on a foreign exchange and purchased approximately $4.1 million of its own common stock using its cash on hand. We do not anticipate any additional spending for common stock buyback plans in the foreseeable future.

As of September 30, 2011, our retained earnings are free from legal or contractual restrictions, with the exception of approximately $29.8 million of subsidiary retained earnings, primarily in China that are restricted in accordance with the PRC Foreign Investment Enterprises Law. This law restricts 10% of our net earnings in China, up to a maximum amount equal to 50% of the total capital we have invested. The $29.8 million includes approximately $6.7 million of retained earnings of a majority owned subsidiary.

Losing the services of our executive officers or other highly qualified and experienced employees could adversely affect our businesses.

Our success depends upon the contributions of our executive officers and senior management, many of whom have numerous years of experience and would be extremely difficult to replace. We must also attract and maintain experienced and highly skilled engineering, sales and marketing, finance and manufacturing personnel. Competition for qualified personnel is often intense, and we may not be successful in hiring and retaining these people. If we lose the services of these key employees or cannot attract and retain other qualified personnel, our businesses could be adversely affected.

In 2011, we announced that our corporate headquarters, previously located in Trevose, Pennsylvania, would be consolidated into our U.S. operational headquarters in San Diego, California. This consolidation is occurring during 2011 in connection with our actions to simplify and streamline our company's organizational structure. We are currently increasing the staff at our San Diego headquarters to address those positions for employees who will not relocate and, also, are undergoing transitions for certain positions where replacements have already been identified.

Public health epidemics (such as flu strains or severe acute respiratory syndrome) or natural disasters (such as earthquakes or fires) may disrupt operations in affected regions and affect operating results.

We maintain extensive manufacturing operations in the PRC, similar to many of our customers and suppliers. A sustained interruption of our manufacturing operations, or those of our customers or suppliers, resulting from complications caused by a public health epidemic or a natural disaster could have a material adverse effect on our business and our results of operations.

The unavailability of insurance against certain business and product liability risks may adversely affect our future operating results.

As part of our comprehensive risk management program, we purchase insurance coverage against certain business and product liability risks. However, not all risks are insurable and those that are insured may differ in the amount covered due to the type of risk, end market and customer location. If any of our insurance carriers discontinues an insurance policy, significantly reduces available coverage or increases our deductibles and we cannot find another insurance carrier to provide comparable coverage at similar costs or we are not fully insured for a particular risk in a particular place, than we may be subject to increased costs of uninsured or under-insured losses which may adversely affect our operating results.

Also, our components, modules and other products are used in a broad array of representative end products. If our insurance program does not adequately cover liabilities arising from the direct use of our products or liabilities that arise from use of our customers' products, we may be subject to increased costs of uninsured losses which may adversely affect our operating results.

Environmental liability and compliance obligations may adversely affect our operations and results.

Our manufacturing operations are subject to a variety of environmental laws and regulations, as well as internal programs and policies governing:

- air emissions;
- wastewater discharges;
- the storage, use, handling, disposal and remediation of hazardous substances, wastes and chemicals; and
- employee health and safety.

If violations of environmental laws occur, we could be held liable for damages, penalties, fines and remedial actions for contamination discovered at our present or former facilities. Our operations and results could be adversely affected by any material obligations arising from existing laws or new regulations that may be enacted in the future. We may also be held liable for past disposal of hazardous substances generated by our business or businesses we acquire.

Our debt levels could adversely affect our financial position, our liquidity and the perception of our financial condition in the financial markets.

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We were in compliance with the existing covenants of our credit agreement as of September 30, 2011. Outstanding borrowings under this agreement were $33.0 million at September 30, 2011. In order to continue execution on our strategic priorities, we amended our credit agreement on August 5, 2011. We worked closely with the banks to ensure that the amended credit facility provides us with the additional flexibility we need to continue making progress on our strategic turnaround plan. These revisions included an increase in interest rates, changes to our debt covenant levels and definitions, a change to our permitted capital expenditure levels, and restrictions on our ability to make dividend payments. We also agreed to reduce the borrowings permitted under the credit facility from $100.0 million to $70.0 million, which was further reduced to $60.8 million following a debt repayment in September 2011. Refer to Note 8, Debt, for additional information. In addition to the debt outstanding under our credit agreement, we have $50.0 million of convertible senior notes.

Covenants with our lenders require compliance with specific financial ratios that may make it difficult for us to obtain additional financing on acceptable terms for future acquisitions or other corporate needs. Although we anticipate meeting our covenants in the normal course of operations, our ability to remain in compliance with the covenants may be adversely affected by future events, some of which may be beyond our control. Violating any of these covenants could result in being declared in default, which, if not waived by our lenders, may result in our lenders electing to declare our outstanding borrowings immediately due and payable and terminate all commitments to extend further credit. No assurance can be given that we would be successful in obtaining any waivers from our lenders nor that any such waivers we might be able to negotiate would be on terms as favorable as those presently contained in our debt agreements. If the lenders accelerate the repayment of borrowings, we cannot provide assurance that we will have sufficient liquidity to repay our credit facilities or other indebtedness. In addition, certain domestic and international subsidiaries have pledged the shares of certain subsidiaries, as well as selected accounts receivable, inventory, machinery and equipment and other assets as collateral. If we default on our obligations, our lenders may take possession of the collateral and may license, sell or otherwise dispose of those related assets in order to satisfy our obligations.

Our results may be negatively affected by changing interest rates.

We are subject to market risk exposure related to changes in interest rates. To mitigate the risk of changing interest rates, we may utilize derivatives or other financial instruments. We do not expect changes in interest rates to have a material effect on our income or cash flows for the foreseeable future, although there can be no assurances that interest rates will not significantly change or that our results would not be materially affected by such adverse changes.

Our intellectual property rights may not be adequately protected or third parties may claim we have violated their intellectual property rights.

We may not be successful in protecting our intellectual property through patent laws, other regulations or by contract. As a result, other companies may be able to develop and market similar products which could materially and adversely affect our market share. Also, we may be sued by third parties for alleged infringement of their proprietary rights, which may result in defense costs, royalty obligations or the overall loss of the right to use technology important to our business.

From time to time, we receive claims by third parties asserting that our products violate their intellectual property rights. Any intellectual property claims, with or without merit, could be time consuming, expensive to litigate or settle and could divert management's attention from administering our business. A third party asserting infringement claims against us or our customers with respect to our current or future products may have a material and adverse effect on our business. For example, it may cause us to enter into costly royalty arrangements or force us to incur settlement or litigation costs.

Our stock price has been and may continue to be volatile.

The market price of our common stock may fluctuate as a result of variations in our quarterly operating results and other factors, some of which are beyond our control. These fluctuations may be exaggerated if the trading volume of our common stock is low.

In addition, the market price of our common stock may rise and fall in response to the following factors, or based on the perception or anticipation of the following factors:

- employee health and safety.announcements of technological or competitive developments;

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- acquisitions or strategic alliances by us or our competitors;
- divestitures of core and non-core businesses;
- the gain or loss of a significant customer or order;
- the existence of debt levels in excess of our cash levels;
- changes in our liquidity, capital resources or financial position;
- changes in estimates or forecasts of our financial performance or changes in recommendations by securities analysts regarding us, our competitors or our industry;
- general market or economic conditions; or
- future business prospects.

Complications with our current enterprise resource planning system ("ERP") or a transition to an updated ERP system may disrupt operations and affect our operating results.

We currently operate an ERP system that is reaching the end of its useful life. This system is used at the majority of our locations for many areas of operation, including purchasing, logistics and finance. A disruption or failure with any component or module of our ERP system may result in a delay to our operations, which could negatively affect our financial results. We are undertaking a full replacement of the system. We are subject to inherent costs and risks associated with replacing and changing our systems, including the following:

- the ability to accept and fulfill customer orders;
- the potential disruption of our internal control structure;
- the use of funds for the software and training; and
- an overall strain on management resources.

The new ERP system will be deployed for use throughout our company in a number of "go live" phases with company-wide deployment expected to be completed in 2012. Implementing a new ERP system is costly and involves risks inherent in the conversion to a new computer system, including loss of information, disruption to our normal operations, changes in accounting procedures and internal control over financial reporting, as well as problems achieving accuracy in the conversion of electronic data. While the new ERP system is intended to further improve and enhance our information systems, large scale implementation of a new information system exposes us to the risks of starting up the new system and integrating that system with our existing systems and processes, including possible disruption of our financial reporting.

Also, an implementation of a new ERP may not result in financial gains which fully offset the potential costs of implementation.

Our decision to suspend payment of quarterly dividends may impact our stock price

In August 2011, we decided that following a quarterly dividend payment of $.025 per common share to be paid on October 22, 2011 to shareholders of record on October 7, 2011, we will not make dividend payments in subsequent periods. We believe use of these funds can generate a higher return if utilized to continue the execution of our strategic initiatives, in particular in the near term to improve our wireless business, to continue our restructuring program, and to implement a new ERP system. The decision to suspend our quarterly dividend could result in fluctuations in the market price of our common stock.

Exhibit Index

3.1	Articles of Incorporation, amended and restated as of May 18, 2011 (incorporated by reference to Exhibit 3.1 to our Form 8-K dated May 24, 2011).
3.3	By-Laws, amended and restated as of May 18, 2011 (incorporated by reference to Exhibit 3.3 to our Form 8-K dated May 24, 2011).
10.5(3)	Amendment No. 2 dated as of August 5, 2011 among Pulse Electronics Corporation (formerly known as Technitrol, Inc.) and certain subsidiaries, JPMorgan Chase Bank, N.A. as administrative agent, swing line lender, and a letter of credit issuer, and other lenders party thereto.
31.1	Certification of Principal Executive Officer pursuant to Section 302(a) of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Principal Financial Officer pursuant to Section 302(a) of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Principal Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Principal Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.1	The following financial statements from the Pulse Electronics Corporation Quarterly Report on Form 10-Q for the quarter ended September 30, 2011, formatted in Extensive Business Reporting Language (“XBRL”): (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Operations, (iii) Consolidated Statements of Cash Flows, (iv) Consolidated Statement of Changes in Equity and (v) the Notes to the Unaudited Consolidated Financial Statements.
10.30	Amendment to Employment Agreement Between Ralph E. Faison and Pulse Electronics Corporation dated September 16, 2011 (incorporated by reference to Exhibit 10.29 to our Form 8-K dated September 16, 2011).

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.

Pulse Electronics Corporation
(Registrant)

November 9, 2011
(Date)

/s/ Drew A. Moyer
Drew A. Moyer
Senior Vice President and Chief Financial Officer
(duly authorized officer, principal accounting officer)