UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

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

For the quarterly period ended July 31, 2003

OR

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

For the transition period from ______________ to ______________

Commission file number: 0-21969

CIENA CORPORATION

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**23-2725311** (I.R.S. Employer Identification No.)
1201 Winterson Road, Linthicum, MD (Address of Principal Executive Offices)	**21090** (Zip Code)

(410) 865-8500
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES (X) NO ( )

Indicate by check mark whether the registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2). YES ( ) NO (X)

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

Class	Outstanding at August 19, 2003
Common stock. $0.01 par value	468,759,342

CIENA CORPORATION

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FORM 10-Q

Item 1. Financial Statements

CIENA CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data)
(unaudited)

	Quarter Ended		Nine Months Ended	
	July 31, 2002	July 31, 2003	July 31, 2002	July 31, 2003
Revenues:				
Products	$ 41,029	$ 59,294	$ 254,428	$ 183,913
Services	8,999	9,184	44,809	28,579
Total Revenue	50,028	68,478	299,237	212,492
Costs:				
Products	37,450	39,249	191,595	123,335
Services	13,510	12,749	66,163	42,300
Provision (benefit) for excess and obsolete inventory costs	41,192	(55)	284,883	(4,158)
Total cost of goods sold	92,152	51,943	542,641	161,477
Gross profit (loss)	(42,124)	16,535	(243,404)	51,015
Operating expenses:				
Research and development *(exclusive of $3,860, $2,932, $11,277 and $10,136 deferred stock compensation costs)*	53,950	47,963	178,264	153,890
Selling and marketing *(exclusive of $842, $687, $2,649 and $2,122 deferred stock compensation costs)*	30,829	24,536	98,264	76,805
General and administrative *(exclusive of $256, $312, $658, and $1,032 deferred stock compensation costs)*	10,798	7,969	37,729	28,241
Deferred stock compensation costs	4,958	3,931	14,584	13,290
Amortization of intangible assets *(exclusive of $0, $966, $0, and $2,315 Included in cost of goods sold related to certain technology licenses)*	2,343	4,479	5,969	11,453
In-process research and development	—	1,500	—	1,500
Nortel Networks settlement costs	—	—	—	2,500
Restructuring costs	18,562	15,527	146,738	18,251
Provision for doubtful accounts	(1,242)	—	14,813	—
Total operating expenses	120,198	105,905	496,361	305,930
Loss from operations	(162,322)	(89,370)	(739,765)	(254,915)
Interest and other income (expense), net	13,558	8,865	44,775	33,297
Interest expense	(10,614)	(8,070)	(29,756)	(28,334)
Loss on equity investments, net	—	—	(5,740)	(10)
Loss on extinguishment of debt	—	—	—	(20,606)
Loss before income taxes	(159,378)	(88,575)	(730,486)	(270,568)
Provision for income taxes	607	299	112,243	909
Net loss	$(159,985)	$ (88,874)	$(842,729)	$(271,477)
Basic and dilutive net loss per common share and dilutive potential common share	$ (0.42)	$ (0.20)	$ (2.45)	$ (0.62)
Weighted average basic common and dilutive potential common shares outstanding	376,548	451,009	344,242	438,133

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

CIENA CORPORATION
CONSOLIDATED BALANCE SHEETS
(in thousands, except share and per share data)
(unaudited)

	October 31, 2002	July 31, 2003
ASSETS		
Current assets:		
Cash and cash equivalents	$ 377,189	$ 585,258
Short-term investments	1,130,414	727,078
Accounts receivable, net	28,680	41,966
Inventories, net	47,023	26,954
Prepaid expenses and other	54,351	33,863
Total current assets	1,637,657	1,415,119
Long-term investments	570,861	437,135
Equipment, furniture and fixtures, net	196,951	132,061
Goodwill	212,500	301,024
Other intangible assets, net	62,457	130,889
Other long term assets	70,596	62,635
Total assets	$ 2,751,022	$ 2,478,863
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 39,841	$ 40,390
Accrued liabilities	132,588	110,880
Restructuring liabilities	27,423	12,686
Unfavorable lease commitments	7,630	8,744
Income taxes payable	—	5,203
Deferred revenue	15,388	16,802
Other current obligations	948	—
Total current liabilities	223,818	194,705
Long-term deferred revenue	15,444	13,342
Long-term restructuring liabilities	65,742	53,657
Long-term unfavorable lease commitments	70,124	63,365
Other long-term obligations	5,009	2,886
Convertible notes payable	843,616	729,514
Total liabilities	1,223,753	1,057,469
Commitments and contingencies		
Stockholders' equity:		
Preferred stock – par value $0.01; 20,000,000 shares authorized; zero shares issued and outstanding	—	—
Common stock – par value $0.01; 980,000,000 shares authorized; 432,842,481 and 468,743,185 shares issued and outstanding	4,328	4,687
Additional paid-in capital	4,683,865	4,841,120
Deferred stock compensation	(24,983)	(14,878)
Notes receivable from stockholders	(3,866)	(545)
Accumulated other comprehensive income	8,840	3,402
Accumulated deficit	(3,140,915)	(3,412,392)
Total stockholders' equity	1,527,269	1,421,394
Total liabilities and stockholders' equity	$ 2,751,022	$ 2,478,863

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

CIENA CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(unaudited)

	Nine Months Ended July 31,	
	2002	2003
Cash flows from operating activities:		
Net loss	$ (842,729)	$ (271,477)
Adjustments to reconcile net income to net cash provided by operating activities:		
Early extinguishment of debt	—	20,606
Non-cash charges from equity transactions	3,755	10
Non-cash portion of restructuring charges and related asset write-downs	86,254	28,798
Accretion of notes payable	7,108	5,518
Non-cash charge for retirement of asset	—	1,329
Effect of accumulated other comprehensive income (loss)	2,861	(6,510)
In-process research and development	—	1,500
Depreciation	96,160	61,128
Amortization of other intangibles, deferred stock compensation and debt issuance costs	23,077	29,329
Provision (benefit) for inventory excess and obsolescence	248,865	(4,158)
Provision for doubtful accounts	14,813	—
Provision for warranty and other contractual obligations	10,933	4,417
Changes in assets and liabilities:		
Accounts receivable	347,266	(13,152)
Inventories	(44,670)	25,210
Deferred income tax asset	113,143	—
Prepaid expenses and other	418	874
Accounts payable and accruals	1,879	(62,265)
Income taxes payable	101	5,203
Deferred income tax liability	(5,754)	—
Deferred revenue and other obligations	3,668	(1,076)
Net cash provided by (used in) operating activities	67,148	(174,716)
Cash flows from investing activities:		
Additions to equipment, furniture and fixtures	(57,354)	(24,831)
Purchases of available-for-sale investments	(918,260)	(519,708)
Maturities of available-for-sale investments	1,107,275	1,056,770
Acquisition of businesses, inclusive of intellectual property and other intangibles, net of cash acquired	286,899	4,159
Minority equity investments	(4,999)	—
Net cash provided by investing activities	413,561	516,390
Cash flows from financing activities:		
Net repayment of other obligations	(633)	(832)
Net repurchase of convertible subordinated notes	(178,413)	(140,261)
Proceeds from issuance of common stock and warrants	13,312	5,858
Repayment of notes receivable from stockholders	2,315	1,630
Net cash used in financing activities	(163,419)	(133,605)
Net change in cash and cash equivalents	317,290	208,069
Cash and cash equivalents at beginning of period	397,890	377,189
Cash and cash equivalents at end of period	$ 715,180	$ 585,258

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

1) SIGNIFICANT ACCOUNTING POLICIES

Interim Financial Statements

The interim financial statements included herein for CIENA Corporation (the "Company" or "CIENA") have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. In the opinion of management, financial statements included in this report reflect all normal recurring adjustments which the Company considers necessary for the fair presentation of the results of operations for the interim periods covered and of the financial position of the Company at the date of the interim balance sheet. Certain information and footnote disclosures normally included in the annual financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. However, the Company believes that the disclosures are adequate to understand the information presented. The operating results for interim periods are not necessarily indicative of the operating results for the entire year. These financial statements should be read in conjunction with the Company's October 31, 2002 audited consolidated financial statements and notes thereto included in the Company's annual report on Form 10-K for the fiscal year ended October 31, 2002.

Critical Accounting Policies and Estimates

The preparation of consolidated financial statements requires CIENA to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, CIENA re-evaluates its estimates, including those related to bad debts, inventories, investments, intangible assets, goodwill, income taxes, warranty obligations, restructuring, and contingencies and litigation. CIENA bases its estimates on historical experience and on various other assumptions that CIENA believes to be reasonable under the circumstances. Among other things, these estimates form the basis for judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. CIENA believes the following critical accounting policies affect its more significant judgments and estimates used in the preparation of its consolidated financial statements.

Revenue Recognition

CIENA recognizes product revenue in accordance with the shipping terms specified and where collection is reasonably assured. For transactions where CIENA has yet to obtain customer acceptance, revenue is deferred until the terms of acceptance are satisfied. Revenue for installation services is recognized as the services are performed unless the terms of the supply contract combine product acceptance with installation. Revenue from installation services are recognized when the terms of acceptance are satisfied and installation is completed. Revenue from installation service fixed-price contracts is recognized on the percentage-of-completion method, measured by the percentage of costs incurred to date compared to estimated total costs for each contract. Amounts received in excess of revenue recognized are included as deferred revenue in the accompanying balance sheet. For transactions involving the sale of software, revenue is recognized in accordance with Statement of Position No. 97-2 ("SOP 97-2"), "Software Revenue Recognition", including deferral of revenue recognition in instances where vendor specific objective evidence for undelivered elements is not determinable. For distributor sales where risks of ownership have not transferred, CIENA recognizes revenue when the product is shipped through to the end user.

Allowances for Doubtful Accounts

CIENA maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. If the financial condition of CIENA's customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. As of July 31, 2003, CIENA's accounts receivable balance, net of allowances for doubtful accounts of $9.7 million, was $42.0 million, which included three customers who accounted for 20.4%, 15.5%, and 10.6% of the net trade accounts receivable.

Warranties

CIENA provides for the estimated cost of product warranties at the time revenue is recognized. CIENA engages in extensive product quality programs and processes including actively monitoring and evaluating the quality of its component suppliers and third party contractors. CIENA's warranty obligation is affected by product failure rates and material usage and service delivery costs incurred in correcting a product failure. Should actual product failure rates, material usage or service delivery costs differ from CIENA's estimates, a revision to the estimated warranty liability would be required.

Reserve for Inventory Obsolescence

CIENA writes down its inventory for estimated obsolescence or unmarketable inventory equal to the difference between the cost of inventory and the estimated market value based on assumptions about future demand and market conditions. During the nine months ended July 31, 2003, CIENA recorded a benefit for inventory reserves of $4.2 million, primarily related to the realization of sales from previously reserved excess inventory. If actual market conditions differ from those CIENA has projected, CIENA may be required to take additional inventory write-downs or to record additional benefits.

Restructuring

As part of its restructuring costs, CIENA provides for the estimated cost of the net lease expense for facilities that are no longer being utilized. The provision is equal to the future minimum lease payments under contractual obligations offset by estimated future sublease payments. As of the end of the first nine months of fiscal 2003, CIENA's accrued restructuring liability related to net lease expense and other related charges was $65.2 million. If actual market conditions are less favorable than those CIENA has projected, CIENA may be required to recognize additional restructuring costs associated with these facilities.

Minority Investments

CIENA holds minority interests in several companies having operations or technology in areas within its strategic focus. As of July 31, 2003, $11.0 million of these investments are included in other long-term assets. CIENA records an investment impairment charge when it believes an investment has experienced a decline in value that is other than temporary. During the nine months ended July 31, 2003, no material impairment charges were recorded. Future adverse changes in market conditions or poor operating results of underlying investments could result in losses or an inability to recover the carrying value of the investments that may not be reflected in an investment's current carrying value, thereby possibly requiring an impairment charge in the future.

Impairment of Goodwill

Effective November 1, 2001, CIENA adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142") and ceased to amortize goodwill. As of July 31, 2003, CIENA's assets include $301.0 million related to goodwill. SFAS 142 requires that CIENA ceases to amortize goodwill and test it for impairment on an annual basis and between annual tests if an event occurs or circumstances change that would, more likely than not, reduce the fair value of CIENA below its carrying value. CIENA performed the required annual impairment assessment of goodwill balances in accordance with the provisions of SFAS 142 during the fourth quarter of fiscal 2002, which resulted in a goodwill impairment charge of $557.3 million. Since no event occurred or circumstances changed during the first nine months of fiscal 2003 that would, more likely than not, reduce the fair value of CIENA below its carrying value, no impairment was recorded in the first nine months of fiscal 2003. If actual market conditions are less favorable than those CIENA projected, or if an event occurs or circumstances change that would, more likely than not, reduce the fair value of CIENA below its carrying value, CIENA may be required to recognize additional goodwill impairment charges.

Deferred Tax Valuation Allowance

As of July 31, 2003, CIENA has recorded a valuation allowance of $835.3 million against the gross deferred tax assets of $835.3 million. CIENA calculated the valuation allowance in accordance with the provisions of Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" ("SFAS 109") which requires an assessment of both positive and negative evidence when measuring the need for a valuation allowance. Positive evidence, such as operating results during the most recent three-year period, is given more weight when due to the current lack of visibility, there is a greater degree of uncertainty that the level of future profitability needed to record the deferred assets will be achieved. CIENA's results over the most recent three-year period were heavily affected by CIENA's recent deliberate and planned business restructuring activities. CIENA's cumulative loss in the most recent three-year period represents sufficient negative evidence to require a valuation allowance under the provisions of SFAS 109. CIENA intends to maintain a valuation allowance until sufficient positive evidence exists to support its reversal.

Accounting for Stock Options

In October 1995, the Financial Accounting Standards Board issued Statement of Financial Accounting Standard No. 123 (“SFAS 123”), “Accounting for Stock-Based Compensation”. SFAS 123 allows companies to account for stock-based compensation either under the new provisions of SFAS 123 or using the intrinsic value method provided by Accounting Principles Board Opinion No. 25 (“APB 25”), “Accounting for Stock Issued to Employees”, but requires pro forma disclosure in the footnotes to the financial statements as if the measurement provisions of SFAS 123 had been adopted.

In December 2002, the Financial Accounting Standards Board issued Statement of Financial Accounting Standard No. 148, “Accounting for Stock-Based Compensation-Transition and Disclosure” (“SFAS 148”). SFAS 148 amends SFAS 123, to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS 148 amends the disclosure requirements of SFAS 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. SFAS 148 is effective for financial statements for fiscal years ending after December 15, 2002.

The Company has elected to continue to account for its stock-based compensation in accordance with the provisions of APB 25 as interpreted by FASB Interpretation No. 44, “Accounting for Certain Transactions Involving Stock Compensation, an Interpretation of APB Opinion No. 25”, (“FIN 44”) and present the pro forma disclosures required by SFAS 123 as amended by SFAS 148. See Note 13.

Newly Issued Accounting Standards

In November 2002, the FASB issued FASB Interpretation No. 45 (“FIN 45”), “Guarantor’s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others.” FIN 45 requires that a liability be recorded in the guarantor’s balance sheet upon issuance of a guarantee. In addition, FIN 45 requires disclosures about the guarantees that an entity has issued, including a reconciliation of changes in the entity’s product warranty liabilities. The initial recognition and initial measurement provisions of FIN 45 are applicable on a prospective basis to guarantees issued or modified after December 31, 2002, irrespective of the guarantor’s fiscal year end. The disclosure requirements of FIN 45 are effective for financial statements of interim or annual periods ending after December 15, 2002. The adoption of this standard did not have a material impact on CIENA’s financial statements.

In November 2002, the Emerging Issues Task Force (“EITF”) reached a consensus on Issue No. 00-21, “Revenue Arrangements with Multiple Deliverables.” EITF Issue No. 00-21 provides guidance on how to account for arrangements that involve the delivery or performance of multiple products, services and/or rights to use assets. The provisions of EITF Issue No. 00-21 will apply to revenue arrangements entered into in fiscal periods beginning after June 15, 2003. The Company believes that the adoption of this standard will have no material impact on its financial statements.

In January 2003, the FASB issued FASB Interpretation No. 46 (“FIN 46”), “Consolidation of Variable Interest Entities, an Interpretation of Accounting Research Bulletin No. 51.” FIN 46 requires certain variable interest entities to be consolidated by the primary beneficiary of the entity if the equity investors in the entity do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. FIN 46 is effective for all new variable interest entities created or acquired after January 31, 2003. For variable interest entities created or acquired prior to February 1, 2003, the provisions of FIN 46 must be applied for the first interim or annual period beginning after June 15, 2003. The Company believes that the adoption of this standard will have no material impact on its financial statements.

In April 2003, the FASB issued SFAS No. 149, “Amendment of Statement 133 on Derivative Instruments and Hedging Activities.” SFAS No. 149 amends and clarifies accounting for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities under SFAS No. 133. The statement requires that contracts with comparable characteristics be accounted for similarly and clarifies when a derivative contains a financing component that warrants special reporting in the statement of cash flows. SFAS No. 149 is effective for contracts entered into or modified after June 30, 2003, except in certain circumstances, and for hedging relationships designated after June 30, 2003. The Company does not expect that the adoption of this standard will have a material effect on its financial position or results of operations.

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity." This Statement establishes standards for how an issuer classifies and measures in its statement of financial position certain financial instruments with characteristics of both liabilities and equity. It requires that an issuer classify a financial instrument that is within its scope as a liability (or an asset in some circumstances) because that financial instrument embodies an obligation of the issuer. This Statement is effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003, except for mandatory redeemable financial instruments of nonpublic entities. The Company does not expect that the adoption of this standard will have a material effect on its financial position or results of operations.

Reclassification

Certain prior year amounts have been reclassified to conform to current year consolidated financial statement presentation.

2) BUSINESS COMBINATIONS

On June 16, 2003, CIENA completed the acquisition by merger of WaveSmith Networks, Inc., a privately held corporation headquartered in Acton, Massachusetts that is a leading innovator of multi-service switching equipment. Pursuant to the terms of the acquisition agreement, WaveSmith merged into CIENA, and the outstanding shares of WaveSmith common and preferred stock were exchanged for approximately 33,421,217 shares of CIENA common stock. The aggregate purchase price was $156.3 million, which included CIENA common stock valued at $142.7 million, CIENA options, warrants and restricted stock valued at $7.9 million, transaction costs of $0.7 million and an initial CIENA investment of $5.0 million. In determining the purchase price, CIENA used an estimated value of CIENA common stock of approximately $4.46 per share, based on the average closing price of CIENA's common stock for two trading days prior to, the trading day of and the two trading days after the April 10, 2003 announcement.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition (in thousands).

Cash, cash equivalents, long and short-term investments	$ 4,159
Inventory	983
Equipment, furniture and fixtures	999
Other tangible assets	472
Existing technology	54,300
Contracts and purchase orders	5,400
Goodwill	88,524
Deferred stock compensation	7,385
Other assumed liabilities	(2,405)
CIENA initial investment	(5,000)
In-process research and development	1,500
Total purchase price	$156,317

The $1.5 million assigned to in-process research and development is purchased in-process technology that, as of the date of the acquisition, had not reached technological feasibility and had no alternative future use. Based on valuation assessments, the value of these projects was determined by estimating the resulting net cash flows from the sale of the products resulting from the completion of the projects, reduced by the portion of the revenue attributable to developed technology and the percentage of completion of the project. The resulting cash flows were then discounted back to their present values at appropriate discount rates.

The $54.3 million assigned to the value of existing technology represents purchased technology for which development had been completed as of the date of acquisition. This amount was determined using the income approach. This method consisted of estimating future net cash flows attributable to existing technology for a discrete projection period and discounting the net cash flows to their present value. The existing technology will be amortized over a seven-year period. The $5.4 million assigned to the contracts and purchase orders will be amortized over a range of two months to five years.

The amount of goodwill allocated to the purchase price was $88.5 million and is not deductible for tax purposes. The Company operates in one operating segment and reports only certain enterprise-wide disclosures. Accordingly, the goodwill from this transaction is not part of a reportable segment. The operations of WaveSmith are not material to the consolidated financial statements of the Company and, accordingly, separate pro forma financial information has not been presented.

ONI Systems

On February 18, 2002, CIENA announced that it had entered into an agreement to acquire by merger ONI Systems Corp. ("ONI"), a NASDAQ-listed corporation headquartered in San Jose, California. ONI is a provider of optical networking equipment specifically designed to address bandwidth and service limitations of regional and metropolitan networks. Under the terms of the agreement, each outstanding share of capital stock of ONI was exchanged for 0.7104 shares of CIENA common stock, and CIENA assumed all ONI outstanding options and warrants as well as the ONI outstanding convertible debt. The acquisition was consummated on June 21, 2002. The stockholders of ONI received 101,120,724 shares of CIENA common stock of which 1,039,429 are restricted and subject to repurchase.

Additionally, CIENA converted approximately 18,193,345 ONI options and warrants into 12,924,552 options and warrants to purchase CIENA common stock. The aggregate purchase price was $978.2 million, including CIENA common stock valued at $875.7 million, CIENA options, warrants and restricted stock valued at $89.2 million and transaction costs of $13.3 million. In determining the purchase price, CIENA used an estimated value of CIENA common stock of approximately $8.75 per share based on the average closing price of CIENA's common stock for the two trading days before the February 18, 2002 announcement and the two trading days after the announcement.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition (in thousands).

Cash, cash equivalents, long and short-term investments	$ 623,559
Inventory	14,705
Equipment, furniture and fixtures	40,759
Other tangible assets and notes receivable from stockholders	25,847
Existing technology	13,000
Non-compete agreements	1,000
Contracts and purchase orders	1,100
Goodwill	590,895
Deferred stock compensation	8,826
Other assumed liabilities	(39,544)
Restructuring liabilities in connection with the business combination	(3,792)
Unfavorable lease commitments	(80,183)
Convertible subordinated notes payable	(218,013)
Total purchase price	$ 978,159

No amount of the purchase price was assigned to in-process research and development. In-process research and development is purchased in-process technology that, as of the date of the acquisition, had not reached technological feasibility and had no alternative future use. Based on valuation assessments, the value of these projects was determined by estimating the resulting net cash flows from the sale of the products resulting from the completion of the projects, reduced by the portion of the revenue attributable to developed technology and the percentage of completion of the project. The resulting cash flows were then discounted back to their present values at appropriate discount rates.

The $13.0 million assigned to the value of existing technology represents purchased technology for which development had been completed as of the date of acquisition. This amount was determined using the income approach. This method consisted of estimating future net cash flows attributable to existing technology for a discrete projection period and discounting the net cash flows to their present value. The existing technology will be amortized over a seven-year period. The $2.1 million assigned to the other intangible assets, non-compete agreements and contracts, will be amortized over a range of two months to one year.

During the quarter ended July 31, 2002, CIENA and ONI reduced their combined workforce by approximately 283 employees. Approximately $3.8 million of costs associated with the ONI workforce reduction qualify for treatment under EITF 95-3 "Recognition of Liabilities in Connection with a Purchase Combination" and were recorded as an element of the acquisition.

The $80.2 million assigned to the value of the unfavorable lease commitments was based upon the present value of the assumed lease obligations based upon current rental rates at the time of the acquisition. These unfavorable lease commitments will be paid over the respective lease terms through fiscal 2011. The $218.0 million assigned to the value of the ONI $300.0 million principal amount of 5.0% convertible subordinated notes due October 15, 2005 was based upon the present value of the notes at the time of the acquisition. CIENA is accreting the difference between the present value of the notes and the outstanding principal value over the remaining period to October 15, 2005, such that the carrying value of the notes equals the principal value at the time the notes become due.

The amount of goodwill allocated to the purchase price was $590.9 million and is not deductible for tax purposes. The Company operates in one operating segment and reports only certain enterprise-wide disclosures. Accordingly, the goodwill from this transaction is not part of a reportable segment.

The following unaudited pro forma data summarizes the results of operations for the period indicated as if the ONI acquisition had been completed as of the beginning of the periods presented. The unaudited pro forma data gives effect to actual operating results prior to the June 21, 2002 acquisition, adjusted to include the pro forma effect of amortization of intangibles, deferred stock compensation costs, and the tax effects to the pro forma adjustments. These pro forma amounts do not purport to be indicative of the results that would have actually been obtained if the acquisition occurred as of the beginning of the periods presented or that may be obtained in the future (in thousands, except per share data.)

	Quarter Ended July 31, 2002	Nine Months Ended July 31, 2002
Revenue	$ 57,247	$ 369,577
Net income (loss)	$(202,339)	$(948,096)
Diluted net income (loss) per common share and dilutive potential common share	$ (0.47)	$ (2.21)

3) RESTRUCTURING COSTS

The following table displays the activity and balances of the restructuring reserve account for the period ended July 31, 2003 (in thousands):

	Workforce reduction	Consolidation of excess facilities	Liabilities recorded in connection with purchase combination	Total
Initial reserve recorded	$ —	$ 15,439(a)	$ —	$ 15,439
Non-cash charges	—	—	—	—
Cash payments	—	—	—	—
Balance at October 31, 2001	—	15,439	—	15,439
Additional reserve recorded	32,929(b)	192,500(b)	3,792(c)	229,221
Non-cash charges	(893)	(113,596)	—	(114,489)
Cash payments	(26,837)	(6,498)	(3,671)	(37,006)
Balance at October 31, 2002	5,199	87,845	121	93,165
Additional reserve recorded	5,464(d)	14,468	355(e)	20,287
Adjustment to previous estimates	(523)	(1,160)	—	(1,683)
Non-cash charges	(1,913)	(24,558)	—	(26,471)
Cash payments	(7,178)	(11,444)	(333)	(18,955)
Balance at July 31, 2003	$ 1,049	$ 65,151	$ 143	$ 66,343
Current restructuring liabilities	$ 1,049	$ 11,494	$ 143	$ 12,686
Non-current restructuring liabilities	$ —	$ 53,657	$ —	$ 53,657

(a) During the fiscal year ended October 31, 2001, CIENA recorded a restructuring charge of $15.4 million relating to consolidation of excess facilities. The consolidation of excess facilities included the closure of certain manufacturing warehouse facilities and the consolidation of certain operational centers related to business activities that were restructured. The charge included $7.0 million primarily related to lease terminations and non-cancelable lease costs and also included an $8.4 million write-down related to property and equipment consisting primarily of leasehold improvements and production equipment.

(b) During the first quarter of fiscal 2002,CIENA had a workforce reduction of approximately 380 employees concentrated in manufacturing operations staff. CIENA recorded a restructuring charge of $6.8 million associated with this action.

During the second quarter of fiscal 2002, CIENA had a workforce reduction of approximately 400 employees largely concentrated in manufacturing operations and research and development activities associated with the closure of CIENA's Marlborough, Massachusetts research and development facility. On March 26, 2002, CIENA had a company-wide workforce reduction of approximately 650 employees. CIENA recorded a restructuring charge of $121.4 million associated with the workforce reductions, lease terminations, non-cancelable lease costs and the write-down of certain property, equipment and leasehold improvements associated with this action.

As a result of the CIENA and ONI Systems Corp. integration and restructuring activities, CIENA recorded a charge of $11.0 million during the quarter ended July 31, 2002 associated with workforce reductions of approximately 66 employees, lease terminations, non-cancelable lease costs and the write-down of certain property, equipment and leasehold improvements. Also during the quarter ended July 31, 2002, CIENA recorded an additional restructuring charge of approximately $7.6 million to increase the estimated cost of the net lease expense for previously restructured facilities.

During the fourth quarter of fiscal 2002, CIENA had a company-wide workforce reduction of approximately 450 employees. CIENA recorded a restructuring charge of $78.7 million associated with the workforce reductions, lease terminations, non-cancelable lease costs and the write-down of certain property, equipment and leasehold improvements associated with this action.

(c) During the third quarter of fiscal 2002, CIENA and ONI Systems Corp. reduced their combined workforce by approximately 283 employees. Approximately $3.8 million of costs associated with the ONI workforce reduction qualify for treatment under EITF 95-3 "Recognition of Liabilities in Connection with a Purchase Combination" and were recorded as an element of the acquisition.

(d) During the second quarter of fiscal 2003, CIENA reduced its workforce by approximately 75 employees. CIENA recorded a restructuring charge of $2.7 million associated with the workforce reduction.

During the quarter ended July 31, 2003, CIENA recorded a restructuring charge of $15.5 million associated with a workforce reduction of approximately 84 employees, lease terminations, non-cancelable lease costs and the write-down of certain property, equipment and leasehold improvements.

(e) During the third quarter of fiscal 2003, CIENA and WaveSmith reduced their combined workforce by approximately 8 employees. Approximately $0.4 million of cost associated with the WaveSmith workforce reduction qualify for treatment under EITF 95-3 "Recognition of Liabilities in Connection with a Purchase Combination" and were recorded as an element of the acquisition.

Since the fourth quarter of fiscal 2001, CIENA has recorded a net charge of $136.0 million related to the write-down and disposal of certain property, equipment and leasehold improvements. These assets are being carried at their fair market value less selling and disposal costs. The remaining facilities balance is related to the net lease expense. This will be paid over the respective lease terms through fiscal 2019.

4) MARKETABLE DEBT AND EQUITY SECURITIES

Cash, short-term and long-term investments are comprised of the following (in thousands):

	July 31, 2003			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Corporate bonds	$ 433,987	$ 849	$ 879	$ 433,957
Asset backed obligations	207,239	871	232	207,878
Municipal bonds	5,072	22	—	5,094
Commercial paper	19,969	34	—	20,003
US government obligations	494,094	3,187	—	497,281
Money market funds	585,258	—	—	585,258
	$1,745,619	$4,963	$1,111	$1,749,471
Included in cash and cash equivalents	$ 585,258	$ —	$ —	$ 585,258
Included in short-term investments	722,693	4,385	—	727,078
Included in long-term investments	437,668	578	1,111	437,135
	$1,745,619	$4,963	$1,111	$1,749,471

	October 31, 2002			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Loses	Estimated Fair Value
Corporate bonds	$ 669,699	$ 2,639	($521)	$ 671,817
Asset-backed obligations	109,755	625	—	110,380
Municipal bonds	20,745	92	—	20,837
Commercial paper	98,215	119	—	98,334
US obligations	793,327	6,580	—	799,907
Money market funds	377,189	—	—	377,189
	$2,068,930	$10,055	($521)	$2,078,464

Included in cash and cash equivalents	$ 377,189	$ —	$ —	$ 377,189
Included in short-term investments	1,126,733	4,202	(521)	1,130,414
Included in long-term investments	565,008	5,853	—	570,861
	$2,068,930	$10,055	($521)	$2,078,464

The following table summarizes maturities of debt investments (including restricted investments) at July 31, 2003 (in thousands):

	Amortized Cost	Estimated Fair Value
Less than one year	$ 722,693	$ 727,078
Due in 1-2 years	415,951	415,323
Due in 2-5 years	21,717	21,812
	$1,160,361	$1,164,213

5) ACCOUNTS RECEIVABLE

As of July 31, 2003, the trade accounts receivable included three customers who accounted for 20.4%, 15.5%, and 10.6% of the net trade accounts receivable. As of October 31, 2002, the net trade accounts receivable included three customers who accounted for 19.3%, 15.0%, and 12.8% of the net trade accounts receivable.

CIENA performs ongoing credit evaluations of its customers and generally has not required collateral or other forms of security from its customers. CIENA maintains an allowance for potential losses on a specific identification basis. CIENA's allowance for doubtful accounts as of July 31, 2003 and October 31, 2002 was $9.7 million and $9.5 million, respectively.

6) INVENTORIES

Inventories are comprised of the following (in thousands):

	October 31, 2002	July 31, 2003
Raw materials	$ 34,025	$ 18,535
Work-in-process	12,658	5,017
Finished goods	48,485	31,270
	95,168	54,822
Less reserve for excess and obsolescence	(48,145)	(27,868)
	$ 47,023	$ 26,954

During the nine months ended July 31, 2003, the Company recorded a benefit for excess inventory of $4.2 million, primarily related to the realization of sales from previously reserved excess inventory. The following is a summary of the change in the reserve for excess and obsolete inventory during the nine months ended July 31, 2003 (in thousands):

	Inventory Reserve
Reserve balance as of Oct. 31, 2002	$ 48,145
Benefit for excess inventory	(4,158)
Actual inventory scrapped	(16,119)
Reserve balance as of July 31, 2003	$ 27,868

The following is a summary of the change in the reserve for excess and obsolete inventory during the nine months ended July 31, 2002 (in thousands):

	Inventory Reserve
Reserve balance as of Oct. 31, 2001	$ 53,804
Provision for excess inventory	248,865
Adjustment for accrued excess inventory purchase commitments received into inventory	1,915
Actual inventory scrapped	(186,253)
Reserve balance as of July 31, 2002	$ 118,331

During the nine months ended July 31, 2002, the Company recorded a provision for excess inventory of $248.9 million and a charge for excess inventory purchase commitments of $36.0 million.

7) EQUIPMENT, FURNITURE AND FIXTURES

Equipment, furniture and fixtures are comprised of the following (in thousands):

	October 31, 2002	July 31, 2003
Equipment, furniture and fixtures	$ 380,316	$ 341,212
Leasehold improvements	78,761	69,146
	459,077	410,358
Accumulated depreciation and amortization	(266,501)	(279,199)
Construction in-progress	4,375	902
	$ 196,951	$ 132,061

During the nine months ended July 31, 2003, the Company recorded net charges of $13.8 million related to the write-down and disposal of certain property, equipment and leasehold improvements as part of its restructuring program. See Note 3.

8) OTHER INTANGIBLE ASSETS

Other intangible assets are comprised of the following (in thousands):

	October 31, 2002			July 31, 2003		
	Gross Intangible	Accumulated Amortization	Net Intangible	Gross Intangible	Accumulated Amortization	Net Intangible
Developed technology	$60,700	$(11,409)	$49,291	$115,000(b)	(18,558)	96,442
Patents and licenses	14,155	(1,989)	12,166	36,655(a)	(7,088)	29,567
Covenants not to compete, outstanding purchase orders and contracts	2,100	(1,100)	1,000	7,500(b)	(2,620)	4,880
	$76,955		$62,457	$159,155		$130,889

(a) In January 2003, CIENA reached a settlement agreement with Nortel. Under the agreement, CIENA made a one-time payment of $25.0 million to Nortel, and Nortel granted CIENA a license under the patents in suit and certain related patents. CIENA accounted for the $25.0 million liability by recording an expense of $2.5 million in first quarter 2003 related to the settlement of the litigation, and recording the remaining $22.5 million as an intangible asset that will be amortized over eight years based upon the expected life of the patent rights acquired in the settlement.

(b) As a result of the WaveSmith acquisition, we recorded $54.3 million in developed technology and $5.4 millions in other intangibles related to contracts and outstanding purchase orders.

The aggregate amortization expense of other intangible assets was $6.0 million and $13.8 million for the nine months ended July 31, 2002 and 2003, respectively. Expected future amortization of other intangible assets is as follows (in thousands):

Year ended October 31,	
2003 (remaining three months)	$ 6,901
2004	21,253
2005	21,254
2006	21,253
2007	21,254
Thereafter	38,974
	$130,889

9) OTHER BALANCE SHEET DETAILS

Other long-term assets are comprised of the following (in thousands):

	October 31, 2002	July 31, 2003
Maintenance spares inventory, net	$27,170	$27,966
Deferred debt issuance costs	15,897	13,626
Investments in privately held companies	16,052	11,042
Other	11,477	10,001
	$70,596	$62,635

Accrued liabilities (in thousands):

	October 31, 2002	July 31, 2003
Warranty	$ 42,040	$ 35,532
Other contractual obligations	3,458	2,162
Accrued compensation, payroll related tax and benefits	37,466	46,578
Accrued excess inventory purchase commitments	1,892	1,482
Accrued interest payable	6,981	718
Accrued Pirelli settlement	11,000	—
Other	29,751	24,408
	$132,588	$110,880

The following is a summary of the change in the company's accrued warranty during the nine months ended July 31, 2003 (in thousands):

	Accrued Warranty
Balance as of Oct. 31, 2002	$ 42,040
Provisions for warranty	4,417
Settlements made	(10,925)
Balance as of July 31, 2003	$ 35,532

Deferred revenue (in thousands):

	October 31, 2002	July 31, 2003
Products	$ 8,175	$ 7,286
Services	22,657	22,858
Total deferred revenue	30,832	30,144
Less current portion	(15,388)	(16,802)
Long-term deferred revenue	$ 15,444	$ 13,342

10) CONVERTIBLE NOTES PAYABLE

On February 9, 2001, CIENA completed a public offering of 3.75% convertible notes, in an aggregate principal amount of $690 million, due February 1, 2008. Interest is payable on February 1 and August 1 of each year beginning August 1, 2001. The notes may be converted into shares of CIENA's common stock at any time before their maturity or their prior redemption or repurchase by CIENA. The conversion rate is 9.5808 shares per each $1,000 principal amount of notes, subject to adjustment in certain circumstances. On or after the third business day after February 1, 2004, CIENA has the option to redeem all or a portion of the notes that have not been previously converted at the following redemption prices (expressed as percentage of principle amount):

Period	Redemption Price
Beginning on the third business day after February 1, 2004 and ending on January 31, 2005	102.143%

Beginning on February 1, 2005 and ending on January 31, 2006	101.607%
Beginning on February 1, 2006 and ending on January 31, 2007	101.071%
Beginning on February 1, 2007 and ending on January 31, 2008	100.536%

On June 21, 2002, CIENA assumed the outstanding ONI 5.00% convertible subordinated notes, in an aggregate principal amount of $300 million, due October 15, 2005. Interest is payable on April 15 and October 15 of each year. The ONI convertible subordinated notes were initially recorded at a value of $218.0 million based upon the fair value of the outstanding notes at the time of the acquisition.

During the fourth quarter of fiscal 2002, CIENA purchased on the open market $97.1 million of the $300 million outstanding ONI convertible subordinated notes. The Company paid $75.2 million for notes with a cumulative accreted book value of $72.5 million, which resulted in a loss on early extinguishment of debt of $2.7 million.

During the first quarter of fiscal 2003, CIENA purchased $154.7 million of the remaining $202.9 million outstanding ONI convertible subordinated notes pursuant to a tender offer. The Company paid $140.3 million related to the tender offer for notes with a cumulative accreted book value of $119.7 million, which resulted in a loss on early extinguishment of debt of $20.6 million.

The remaining outstanding ONI convertible subordinated notes have a carrying value of $39.5 million and a face value of $48.3 million. CIENA is accreting the difference between the values over the remaining period to October 15, 2005, such that the carrying value of the outstanding notes equals the principal value at the time the notes become due. Accretion of the principal was $5.5 million for the first nine months of fiscal 2003.

The remaining ONI convertible subordinated notes may be converted into shares of CIENA's common stock at any time before their maturity. The conversion rate is 7.7525 shares per each $1,000 principal amount of notes, subject to adjustment in certain circumstances. On or after October 16, 2003, CIENA has the option to redeem all or a portion of the notes that have not been previously converted at the following redemption prices (expressed as percentage of principal amount):

Period	Redemption Price
October 16, 2003	102%
October 15, 2004	101%

11) EARNINGS (LOSS) PER SHARE CALCULATION

Basic EPS is computed using the weighted average number of common shares outstanding. Diluted EPS is computed using the weighted average number of common shares outstanding, stock options and warrants using the treasury stock method. Stock options to purchase 43.4 million and 35.8 million shares of common stock were outstanding during the quarters ended July 31, 2002 and July 31, 2003, respectively, but were not included in the computation of diluted EPS as the effect would be anti-dilutive. Stock options to purchase 52.2 million and 37.0 million shares of common stock were outstanding during the nine months ended July 31, 2002 and July 31, 2003, respectively, but were not included in the computation of diluted EPS as the effect would be anti-dilutive.

12) COMPREHENSIVE INCOME

The components of comprehensive income are as follows (in thousands):

	Quarter ended July 31,		Nine months ended July 31,	
	2002	2003	2002	2003
Net loss	$(159,985)	$(88,874)	$(842,729)	$(271,477)
Change in unrealized loss on available-for-sale securities, net of tax	5,231	(4,353)	3,845	(5,684)
Change in accumulated translation adjustments	93	44	203	246
Total comprehensive loss	$(154,661)	$(93,183)	$(838,681)	$(276,915)

13) PRO FORMA STOCK-BASED COMPENSATION

Had compensation cost for the Company's stock option plans and employee stock purchase plan been determined based on the fair value at the grant date for awards in the second quarter of fiscal 2002 and 2003 consistent with the provisions of SFAS 123 as amended by SFAS 148, the Company's net loss and net loss per share for the third quarter of fiscal 2002 and 2003 would have increased to the pro forma amounts indicated below (in thousands, except per share):

The below pro forma disclosures are not necessarily representative of the effects on reported net income or loss for future years.

The weighted average fair value of each option granted under the various stock option plans for the third quarter of fiscal 2002 and 2003 is $4.08 and $3.52 respectively. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions for fiscal years 2002 and 2003:

	Employee Stock Option Plans					
	January 31,	Quarter Ended April 30,	July 31,	January 31,	Quarter Ended April 30,	July 31,
	2002	2002	2002	2003	2003	2003
Expected volatility	92%	92%	92%	92%	84%	64%
Risk-free interest rate	2.6%	2.6%	2.6%	2.6%	2.6%	3.2%
Expected life (years)	4.5	4.5	4.5	4.5	4.5	4.5
Expected dividend yield	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%

	Employee Stock Purchase Plan					
	January 31,	Quarter Ended April 30,	July 31,	January 31,	Quarter Ended April 30,	July 31,
	2002	2002	2002	2003	2003	2003
Expected volatility	n/a	92%	n/a	n/a	84%	n/a
Risk-free interest rate	n/a	1.3%	n/a	n/a	1.3%	n/a
Expected life (years)	n/a	0.5	n/a	n/a	0.5	n/a
Expected dividend yield	n/a	0.0%	n/a	n/a	0.0%	n/a

n/a = no Employee Stock Purchase occurred during these periods

	Quarter ended July 31,		Nine months ended July 31,	
	2002	2003	2002	2003
Net loss applicable to common stockholders - as reported	$(159,985)	$(88,874)	$(842,729)	$(271,477)
Compensation benefit (expense) determined under the fair value method	194,403	19,647	50,926	(29,105)
Deferred compensation amortized	4,958	3,931	14,584	13,290
Net profit (loss) applicable to common stockholders - pro forma	39,376	(65,296)	(777,219)	(287,292)
Basic net loss per share - as reported	$ (0.42)	(0.20)	(2.45)	(0.62)
Basic net profit (loss) per share - pro forma	$ 0.10	(0.14)	(2.26)	(0.66)
Diluted net loss per share - as reported	$ (0.42)	(0.20)	(2.45)	(0.62)
Diluted net profit (loss) per share - pro forma	$ 0.10	(0.14)	(2.26)	(0.66)

The Black-Scholes option-pricing model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, option-pricing models require the input of highly subjective assumptions including the expected stock price volatility. The Company uses projected volatility rates, which are based upon historical volatility rates, trended into future years. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, existing models, including the Black-Scholes option-pricing model, do not necessarily provide a reliable single measure of the fair value of the Company's options.

14) SEGMENT REPORTING

In June 1997, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 131 (SFAS No.131), "Disclosures about Segments of an Enterprise and Related Information." SFAS No. 131 establishes annual and interim reporting standards for operating segments of a company. It also requires entity-wide disclosures about the products and services an entity provides, the material countries in which it holds assets and reports revenue, and its major customers. The Company is not organized by multiple operating segments for the purpose of making operating decisions or assessing performance. Accordingly, the Company operates in one operating segment and reports only certain enterprise-wide disclosures.

The Company's geographic distribution of revenue for the quarter and nine months ended July 31, 2002 and 2003 are as follows (in thousands):

	Quarter Ended July 31,				Nine Months Ended July 31,			
	2002	%	2003	%	2002	%	2003	%
Domestic	$29,387	58.7	$41,342	60.4	$204,775	68.4	$136,415	64.2
International	20,641	41.3	27,136	39.6	94,462	31.6	76,077	35.8
Total	$50,028	100.0	$68,478	100.0	$299,237	100.0	$212,492	100.0

The Company's revenue derived from products and services for the quarter and nine months ended July 31, 2002 and 2003 are as follows (in thousands):

	Quarter Ended July 31,				Nine Months Ended July 31 ,			
	2002	%	2003	%	2002	%	2003	%
Products	$41,029	82.0	$59,294	86.6	$254,428	85.0	$183,913	86.5
Services	8,999	18.0	9,184	13.4	44,809	15.0	28,579	13.5
Total	$50,028	100.0	$68,478	100.00	$299,237	100.0	$212,492	100.0

Historically, the Company has relied on a limited number of customers for its revenue. During the quarter and nine months ended July 31, 2002 and 2003, customers who each accounted for at least 10% of the Company's revenue during the respective periods are as follows (in thousands):

	Quarter Ended July 31,				Nine Months Ended July 31,			
	2002	%**	2003	%**	2002	%**	2003	%**
Company A	$ *	—	$ *	—	$ 62,241	20.8	$31,217	14.7
Company B	8,959	17.9	6,904	10.1	*	—	26,250	12.4
Company C	*	—	*	—	55,589	18.6	*	—
Company D	7,000	14.0	8,910	13.0	*	—	*	—
Total	$15,959	31.9	$15,814	23.1	$117,830	39.4	$57,467	27.1

* – denotes revenue recognized less than 10% of total revenue for the period.

** – denotes % of total revenue

15) CONTINGENCIES

Legal Proceedings

On October 3, 2000, Stanford University and Litton Systems filed a complaint in the United States District Court for the Central District of California alleging that optical fiber amplifiers incorporated into CIENA's products infringe U.S. Patent No. 4,859,016. The complaint seeks injunctive relief, royalties and damages. We were first served with this complaint on April 30, 2003. We believe that we have valid defenses to the lawsuit and intend to defend it vigorously.

On July 19, 2000, CIENA and CIENA Properties, Inc., a wholly owned subsidiary of CIENA, filed a complaint in the United States District Court for the District of Delaware requesting damages and injunctive relief against Corvis Corporation ("Corvis"). The suit charged Corvis with infringing four patents relating to CIENA's optical networking communication systems and technology. A jury trial to determine whether Corvis is infringing these patents commenced on February 10, 2003. On February 24, 2003, the jury decided that Corvis was infringing one of the patents and not infringing two others. The jury was deadlocked with respect to infringement on the fourth patent. This trial was immediately followed by a trial on Corvis' affirmative defenses based on the validity of two of the patents. On February 28, 2003, the jury in this trial determined that the patents were valid. In April 2003, following a third trial, another jury decided that Corvis had infringed the fourth patent on which the previous jury had deadlocked. Based on these favorable verdicts collectively holding that Corvis is infringing two valid CIENA patents, CIENA has moved for an injunction to prohibit the sale by Corvis of the infringing products. The court has not yet ruled on this motion.

As a result of the merger with ONI, we became a defendant in a securities class action lawsuit. Beginning in August 2001, a number of substantially identical class action complaints alleging violations of the federal securities laws were filed in the United

States District Court for the Southern District of New York. These complaints name ONI, Hugh C. Martin, ONI's former chairman, president and chief executive officer; Chris A. Davis, ONI's former executive vice president, chief financial officer and administrative officer; and certain underwriters of ONI's initial public offering as defendants. The complaints were consolidated into a single action, and a consolidated amended complaint was filed on April 24, 2002. The amended complaint alleges, among other things, that the underwriter defendants violated the securities laws by failing to disclose alleged compensation arrangements (such as undisclosed commissions or stock stabilization practices) in the initial public offering's registration statement and by engaging in manipulative practices to artificially inflate the price of our common stock after the initial public offering. The amended complaint also alleges that ONI and the named former officers violated the securities laws on the basis of an alleged failure to disclose the underwriters' alleged compensation arrangements and manipulative practices. No specific amount of damages has been claimed. Similar complaints have been filed against more than 300 other issuers that have had initial public offerings since 1998, and all of these actions have been included in a single coordinated proceeding. Mr. Martin and Ms. Davis have been dismissed from the action without prejudice pursuant to a tolling agreement. In July 2002, ONI and other issuers in the consolidated cases filed motions to dismiss the amended complaint for failure to state a claim, which was denied as to ONI on February 19, 2003. CIENA has participated, together with the other issuer defendants in these cases, in mediated settlement negotiations that have led to a preliminary agreement among the plaintiffs, the issuer defendants and their insurers. The settlement, which is subject to court approval, would result in the dismissal of the plaintiffs' cases against the issuers. CIENA has agreed in principle to the terms of this settlement. CIENA does not anticipate that it will be required to make any payment as a result of the settlement.

On May 3, 2002, a shareholder derivative complaint alleging violations of California state law was filed in the Superior Court of the State of California, County of Santa Clara against ONI. As a result of the merger with ONI, CIENA has also become a defendant in the lawsuit. The complaint names Hugh Martin; the other members of the ONI's board of directors; Terrence J. Schmid, ONI's former chief financial officer and vice president, finance and administration; and certain underwriters of ONI's initial public offering as defendants. The complaint alleges that the defendants breached their fiduciary duties, acted negligently and were unjustly enriched in determining the offering price of ONI Systems common stock in ONI's initial public offering. No specific amount of damages has been claimed. The complaint is encaptioned Sabrina Kurzman and Michael Kurzman, Derivatively on Behalf of ONI Systems Corp. v. Hugh C. Martin. In September 2002, CIENA filed a motion to dismiss the complaint. The Company's motion to dismiss was granted by the court on November 6, 2002. On December 2, 2002, the plaintiffs filed a notice of appeal from the court's order. Plaintiffs have withdrawn their appeal, and the lawsuit was dismissed on June 19, 2003.

As a result of the merger with ONI, we also became a defendant in two substantially identical purported class actions on behalf of ONI security holders originally brought against ONI and members of its board of directors. The complaints allege that the director defendants breached their fiduciary duties to ONI in approving the merger with CIENA and seek declaratory, injunctive and other relief permitted by equity. The plaintiffs failed to obtain an injunction against completion of the merger. The first of these cases was filed on February 20, 2002, in the Superior Court of the State of California, County of San Mateo, and is encaptioned K.W. Sams, On Behalf of Himself and All Others Similarly Situated v. ONI Systems Corporation, et al. The second case was brought on March 19, 2002, in the Superior Court of the State of California, County of Santa Clara, and is encaptioned Steven Myeary, On Behalf of Himself and All Others Similarly Situated v. ONI Systems Corporation. On April 14, 2003, the plaintiffs in these cases filed a consolidated amended complaint and named four additional defendants: CIENA Corporation, James F. Jordan, Kleiner Perkins Caufield & Byers and Mohr Davidow Ventures. We believe that these lawsuits are without merit and will continue to defend them vigorously.

16) SUBSEQUENT EVENTS

On August 21, 2003, CIENA announced that it had entered into an agreement to acquire by merger Akara Corporation, a privately held corporation headquartered in Kanata, Ontario. Akara is an emerging leader in the market for SONET/SDH based storage area (SAN), or storage-over-distance solutions. Under the terms of the acquisition agreement, Akara will merge with a wholly-owned subsidiary of CIENA, and all the remaining shares of Akara common and preferred stock will be exchanged for aggregate consideration of $45 million consisting of $31 million in cash and $14 million in shares of CIENA common stock. The number of shares to be issued will be determined based on the average closing prices of CIENA common stock on the Nasdaq Stock Market on the ten trading days preceding the closing date. The board of directors and the required percentage of holder's of Akara's stock have approved the transaction and CIENA expects to complete the transaction during the fourth quarter of fiscal 2003. However, the completion of the acquisition is still subject to certain conditions.

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

This Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements that involve risks and uncertainties. Under the heading "Risk Factors", we have described what we believe to be some of the major risks related to these forward-looking statements, as well as the general outlook for our business. Investors should review these risk factors and the rest of this quarterly report in combination with the more detailed description of our business in our annual report on Form 10-K, which we filed with the Securities and Exchange Commission on December 12, 2002, for a more complete understanding of the risks associated with an investment CIENA's common stock.

Overview

CIENA is a leading global provider of innovative network solutions to service providers and enterprises worldwide. Our customers include long distance carriers, local exchange carriers, cable operators, internet service providers, wireless and wholesale carriers, resellers, governments, large businesses and non-profit institutions.

In early 2001, the telecommunications industry began a severe decline, which has affected almost all of its segments, including equipment suppliers like CIENA. This decline has caused the market for our equipment to shrink substantially, with a resulting adverse impact on our revenue and profitability. In response, we have embarked upon a corporate strategy that is, among other things, designed to increase our addressable market by increasing our product offerings. Through internal development, acquisitions and strategic alliances, we plan to add new products that can be used to offer data communications services and products designed to be deployed at the edge of carrier networks, where we expect a large portion of carrier spending to occur over the next few years.

As part of our efforts to implement this strategy, we recently completed the acquisition of WaveSmith Networks, Inc., a privately held corporation that offers a multi-service switching product designed to be deployed at the edge of carrier networks. On August 21, 2003, we announced an agreement to acquire Akara Corporation, a provider of SONET/SDH based storage extension devices for storage area networks. We expect to complete this transaction in the fourth quarter of fiscal 2003.

Over the last two years, in parallel with steps to increase our addressable market, we have also executed a program to reduce and restructure our costs to align them better with our market opportunities and changing product mix. Since the fourth quarter of fiscal 2001, we have reduced our quarterly research and development, selling and marketing, and general and administrative expenses (exclusive of deferred stock compensation) from $127.2 million to $80.5 million. Consistent with our overall strategy, over the next year we anticipate taking actions designed to reduce our operating expenses by an additional 10% to 20%, with the bulk of the reductions taking effect in the first half of fiscal 2004.

As of July 31, 2003, CIENA and its subsidiaries employed approximately 2,024 persons, which was a net reduction of 94 persons from the approximate 2,118 employed on October 31, 2002.

Critical Accounting Policies and Estimates

The preparation of consolidated financial statements requires CIENA to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, CIENA re-evaluates its estimates, including those related to bad debts, inventories, investments, intangible assets, goodwill, income taxes, warranty obligations, restructuring, contingencies and litigation. CIENA bases its estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. Among other things, these estimates form the basis for judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. CIENA believes the following critical accounting policies affect its more significant judgments and estimates used in the preparation of its consolidated financial statements.

Revenue Recognition

CIENA recognizes product revenue in accordance with the terms of the contract of sale and where collection is reasonably assured. For transactions in which sales are not complete until the customer has accepted the product, revenue is deferred until the terms of acceptance are satisfied. Revenue for installation services is recognized as the services are performed unless the terms of the supply contract combine product acceptance with installation. Revenue from installation services is recognized when the terms of acceptance are satisfied and installation is completed. Revenue from installation service fixed-price contracts is recognized on the percentage-of-completion method, measured by the percentage of costs incurred to date compared to estimated total costs for each contract. Amounts received in excess of revenue recognized are included as deferred revenue in the balance sheet. For transactions involving the sale of software, revenue is recognized in accordance with Statement of Position No. 97-2 ("SOP 97-2"), "Software Revenue Recognition", including deferral of revenue recognition in instances where vendor specific objective evidence for undelivered elements is not determinable. For distributor sales where risks of ownership have not transferred, CIENA recognizes revenue when the product is shipped through to the end user.

Allowances for Doubtful Accounts

CIENA maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. If the financial condition of CIENA's customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. As of July 31, 2003, our accounts receivable balance, net of allowances for doubtful accounts of $9.7 million, was $42.0 million, which included three customers that accounted for 20.4%, 15.5%, and 10.6% of the net trade accounts receivable.

Warranties

CIENA provides for the estimated cost of product warranties at the time revenue is recognized. CIENA engages in extensive product quality programs and processes including actively monitoring and evaluating the quality of its component suppliers and third party contractors. CIENA's warranty obligation is affected by product failure rates and material usage and service delivery costs incurred in correcting a product failure. Should actual product failure rates, material usage or service delivery costs differ from CIENA's estimates, revisions to the estimated warranty liability would be required.

Reserve for Inventory Obsolescence

CIENA writes down its inventory for estimated obsolescence or unmarketable inventory equal to the difference between the cost of inventory and the estimated market value based on assumptions about future demand and market conditions. During the nine months ended July 31, 2003, CIENA recorded a benefit for inventory reserves of $4.2 million primarily related to the realization of sales from previously reserved excess inventory. If actual market conditions differ from those CIENA has projected, CIENA may be required to take additional inventory write-downs or to record additional benefits.

Restructuring

As part of its restructuring costs, CIENA provides for the estimated cost of the net lease expense for facilities that are no longer being utilized. The provision is equal to the future minimum lease payments under contractual obligations offset by estimated future sublease payments. As of the end of the first nine months of fiscal 2003, CIENA's accrued restructuring liability related to net lease expense and other related charges was $65.2 million. If actual market conditions are less favorable than those CIENA has projected, CIENA may be required to recognize additional restructuring costs associated with these facilities.

Minority Investments

CIENA holds minority interests in several companies having operations or technology in areas within its strategic focus. As of July 31, 2003, $11.0 million of these investments are included in other long-term assets. CIENA records an investment impairment charge when it believes an investment has experienced a decline in value that is other than temporary. During the nine months ended July 31, 2003, no material impairment charges were recorded. Future adverse changes in market conditions or poor operating results of underlying investments could result in losses or an inability to recover the carrying value of the investments that may not be reflected in an investment's current carrying value, thereby possibly requiring an impairment charge in the future.

Impairment of Goodwill

Effective November 1, 2001, CIENA adopted Statement of Financial Accounting Standard No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142") and ceased to amortize goodwill. As of July 31, 2003, CIENA's assets include $301.0 million related to goodwill. SFAS 142 requires that we cease to amortize goodwill and to test it for impairment on an annual basis, and between annual tests if an event occurs or circumstances change that would, more likely than not, reduce the fair value of CIENA below its carrying value. Since no event occurred or circumstances changed during the first nine months of fiscal 2003 that would, more likely than not, reduce the fair value of CIENA below its carrying value, no impairment was recorded in the first nine months of fiscal 2003. If actual market conditions are less favorable than those we have projected or if an event occurs or circumstances change that would, more likely than not, reduce the fair value of CIENA below its carrying value, we may be required to recognize additional goodwill impairment charges.

Deferred Tax Valuation Allowance

As of July 31, 2003, CIENA has recorded a valuation allowance of $835.3 million against our gross deferred tax assets of $835.3 million. We calculated the valuation allowance in accordance with the provisions of Statement of Financial Accounting Standard No. 109, "Accounting for Income Taxes" ("SFAS 109") which requires an assessment of both positive and negative evidence when measuring the need for a valuation allowance. Positive evidence, such as operating results during the most recent three-year period, is given more weight when due to our current lack of visibility, there is a greater degree of uncertainty that the level of future profitability needed to record the deferred assets will be achieved. Our results over the most recent three-year period were heavily affected by our recent deliberate and planned business restructuring activities. Our cumulative loss in the most recent three-year period represents sufficient negative evidence to require a valuation allowance under the provisions of SFAS 109. We intend to maintain a valuation allowance until sufficient positive evidence exists to support its reversal.

Accounting for Stock Options

In October 1995, the Financial Accounting Standards Board issued SFAS 123, "Accounting for Stock-Based Compensation". SFAS 123 allows companies to account for stock-based compensation either under the new provisions of SFAS 123 or using the intrinsic value method provided by Accounting Principles Board Opinion No. 25 ("APB 25"), "Accounting for Stock Issued to Employees", but requires pro forma disclosure in the footnotes to the financial statements as if the measurement provisions of SFAS 123 had been adopted.

In December 2002, the Financial Accounting Standards Board issued Statement of Financial Accounting Standard No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure" ("SFAS 148"). SFAS 148 amends SFAS 123, to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS 148 amends the disclosure requirements of SFAS 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. SFAS 148 is effective for financial statements for fiscal years ending after December 15, 2002.

We have elected to continue to account for stock-based compensation in accordance with the provisions of APB 25 as interpreted by FASB Interpretation No. 44, "Accounting for Certain Transactions Involving Stock Compensation, an Interpretation of APB Opinion No. 25", ("FIN 44") and present the pro forma disclosures required by SFAS 123 as amended by SFAS 148.

Results of Operations

Three Months Ended July 31, 2002 Compared to Three Months Ended July 31, 2003

Revenue. CIENA recognized $50.0 million and $68.5 million in revenue for the quarters ended July 31, 2002 and 2003, respectively. The increase of $18.5 million, or 36.9%, was primarily due to increased product sales of metro transport and switching products. We had sales to 72 customers in the quarter ended July 31, 2003, as compared to 57 customers in the same quarter of the prior year. During the quarter ended July 31, 2003, two customers accounted for 13.0% and 10.1% of CIENA's quarterly revenue and combined accounted for 23.1%. This compares to the quarter ended July 31, 2002, in which two customers accounted for 17.9% and 14.0% of revenue and combined accounted for 31.9%.

CIENA's geographic distribution of revenues for the quarters ended July 31, 2002 and 2003 was as follows (in thousands):

	Quarter Ended July 31,			
	2002	%	2003	%
Domestic	$29,387	58.7	$41,342	60.4
International	20,641	41.3	27,136	39.6
Total	$50,028	100.0	$68,478	100.0

During the third quarter of fiscal 2003, the majority of our revenue was from sales of metro transport equipment, metro switching products, intelligent core switching products and multi-service switching products. Revenues during the third quarter of fiscal 2002 were primarily from sales of intelligent core switching products, metro transport products and long distance transport products. CIENA's revenues from products and services for the quarters ended July 31, 2002 and 2003 were as follows (in thousands):

	Quarter Ended July 31,			
	2002	%	2003	%
Products	$41,029	82.0	$59,294	86.6
Services	8,999	18.0	9,184	13.4
Total	$50,028	100.0	$68,478	100.0

Gross Profit (Loss). Cost of goods sold consists of component costs, direct compensation costs, warranty and other contractual obligations, royalties, license fees, direct technical support costs, cost of excess and obsolete inventory and overhead related to manufacturing, technical support and engineering, furnishing and installation ("EF&I") operations. Gross profit (loss) was ($42.1) million and $16.5 million for the quarters ended July 31, 2002 and 2003, respectively. The $58.6 million increase was the result of a $41.2 million decrease in inventory obsolescence cost and an increase in product sales.

Gross profit (loss) as a percentage of revenue was (84.2%) and 24.1% for the third quarters of fiscal 2002 and 2003, respectively. The increase was largely attributable to decreases in inventory obsolescence costs, increases in manufacturing efficiencies, higher margin product mix and improvements in margin from installation and technical support services. Gross profit on products as a percentage of product revenue was 8.7% and 33.8% for the third quarters of fiscal 2002 and 2003, respectively. The improvement was largely attributable to increases in manufacturing efficiencies and higher margin product mix. Gross loss on services as a percentage of services revenue was 50.1% and 38.8% for the third quarters of fiscal 2002 and 2003, respectively. The improvement in services gross margin was largely attributable to reductions in services overhead costs.

Research and Development Expenses. Research and development expenses (exclusive of deferred stock compensation costs of $3.9 and $2.9 million) were $54.0 million and $48.0 million for the quarters ended July 31, 2002 and 2003, respectively. During the third quarters of fiscal 2002 and 2003, research and development expenses were 107.8% and 70.0% of revenue, respectively. The $6.0 million, or 11.1%, decrease was the result of decreases in staffing levels, consumption of prototype parts and depreciation expense. We expense research and development costs as incurred.

Selling and Marketing Expenses. Selling and marketing expenses (exclusive of deferred stock compensation costs of $0.8 and $0.7 million) were $30.8 million and $24.5 million for the quarters ended July 31, 2002 and 2003, respectively. During the third quarters of fiscal 2002 and 2003, selling and marketing expenses were 61.6% and 35.8% of revenue, respectively. The $6.3 million, or 20.4%, decrease was primarily the result of reduced levels of sales staff, advertising costs, outside consultants, facility costs and depreciation expense.

General and Administrative Expenses. General and administrative expenses (exclusive of deferred stock compensation costs of $0.3 and $0.3 million) were $10.8 million and $8.0 million for the quarters ended July 31, 2002 and 2003, respectively. During the third quarters of fiscal 2002 and 2003, general and administrative expenses were 21.6% and 11.6% of revenue, respectively. The $2.8 million, or 25.9%, decrease was primarily the result of decreases in staffing levels, outside consultants and facility costs.

Deferred Stock Compensation Costs. Deferred stock compensation costs were $5.0 million and $3.9 million for the quarters ended July 31, 2002 and 2003, respectively. As part of our acquisition of Cyras, ONI and WaveSmith, we recorded $98.5, $8.8 and $7.4 million of deferred stock compensation relating to the unvested stock options and restricted stock assumed in the acquisitions, respectively. Deferred stock compensation is presented as a reduction of stockholders' equity and is amortized over the remaining vesting period of the applicable options. As July 31, 2003, the balance of deferred stock compensation is $14.9 million.

Amortization of Intangible Assets. Amortization of intangible assets (exclusive of $0 and $1.0 million included in cost of goods sold related to certain technology licenses) was $2.3 million and $4.5 million for the quarters ended July 31, 2002 and 2003, respectively. In purchasing companies, we have acquired intangible assets such as certain developed technology, patents and covenants not to compete. As part of our March 2001 acquisition of Cyras, we recorded $47.7 million worth of other intangible assets. The intangible assets from the Cyras purchase will be amortized over a seven-year period. As part of our June 2002 acquisition of ONI, we recorded $15.1 million worth of other intangibles assets. The intangible assets from our ONI purchase will be amortized over periods ranging from two months to seven years. As part of our June 2003 acquisition of WaveSmith, we recorded $59.7 million worth of other intangible assets. The intangible assets from the WaveSmith acquisition will be amortized over a period ranging from 2.5 months to seven years.

In-Process Research and Development. In connection with the WaveSmith acquisition, the Company recorded a $1.5 million charge related to in-process research and development for the quarter ended July 31, 2003. This generally represents the estimated value of purchased in-process technology related to WaveSmith's multi-service switching product development that had not yet reached technological feasibility and had no alternative future use at the time of the acquisition. The amount of purchase price allocated to in-process research and development was determined using the discounted cash flow method. This method consisted of estimating future net cash flows attributable to the in-process technology for a discrete projection period and discounting the net cash flows back to their present value.

Restructuring Costs. During the third quarter of fiscal 2002, we recorded a restructuring charge of $18.6 million associated with workforce reductions, lease terminations, non-cancelable lease costs and the write-down of certain property, equipment and leasehold improvements. During the third quarter fiscal 2003, we recorded restructuring charges of $15.5 million associated with workforce reductions and the write-down of certain property and equipment. We expect to incur similar charges over the next several quarters as a result of our ongoing program to restructure our business.

Provision for Doubtful Accounts. We recorded a $1.2 million benefit related to the reversal of a previously recorded provision for doubtful accounts in the third quarter of fiscal 2002. The reversal was due to the receipt of an unanticipated payment. No provision or benefit was recorded in the third quarter of fiscal 2003.

Interest and Other Income (Expense), Net. Interest income and other income (expense), net were $13.6 million and $8.9 million for the quarters ended July 31, 2002 and 2003, respectively. The $4.7 million decrease was attributable to the impact of lower average interest rates and lower average cash and invested balances.

Interest Expense. Interest expense was $10.6 million and $8.1 million for the quarters ended July 31, 2002 and 2003, respectively. The $2.5 million decrease was attributable to a decrease in our debt obligations outstanding between the two periods.

Provision for Income Taxes. CIENA's provision for income taxes was $0.6 million and $0.3 million for the quarters ended July 31, 2002 and 2003, respectively. The provisions are primarily attributable to foreign tax related to CIENA's foreign operations. No tax benefit was recorded for CIENA's domestic losses during the comparable periods. CIENA will continue to maintain a valuation allowance against certain deferred tax assets until sufficient positive evidence exists to support its reversal.

Net Loss. CIENA's net loss for the quarters ended July 31, 2002 and 2003 was $160.0 million and $88.9 million, respectively.

Nine Months Ended July 31, 2002 Compared to Nine Months Ended July 31, 2003

Revenue. CIENA recognized $299.2 million and $212.5 million in revenue for the nine months ended July 31, 2002 and 2003, respectively. The decrease of $86.7 million, or 29.0%, resulted primarily from the reduction in demand for long distance transport products and intelligent core switching products worldwide. This decrease in revenue occurred even though we had sales to 85 customers in the nine months ended July 31, 2003, as compared to 71 customers in the same period of the prior year. During the nine months ended July 31, 2003, two customers accounted for 14.7% and 12.4% of CIENA's revenue and combined accounted for 27.1%. This compares to the nine months ended July 31, 2002, in which two customers accounted for 20.8% and 18.6% of CIENA's revenues and combined accounted for 39.4%. Revenues derived from international sales accounted for 31.6% and 35.8% of CIENA's revenues during the nine months ended July 31, 2002 and 2003, respectively. The Company's geographic distribution of revenues for the nine months ended July 31, 2002 and 2003 was as follows (in thousands):

	Nine months ended July 31,			
	2002	%	2003	%
Domestic	$204,775	68.4	$136,415	64.2
International	94,462	31.6	76,077	35.8
Total	$299,237	100.0	$212,492	100.0

Revenues during the nine months ended July 31, 2003 were primarily from sales of metro transport equipment, metro switching products, intelligent core switching products and multi-service switching products. Revenues during the nine months ended July 31, 2002 were primarily from sales of intelligent core switching products, metro switching products and long distance transport products. CIENA's revenues derived from products and services for the nine months ended July 31, 2002 and 2003 were as follows (in thousands):

	Nine months ended July 31,			
	2002	%	2003	%
Products	$254,428	85.0	$183,913	86.5
Services	44,809	15.0	28,579	13.5
Total	$299,237	100.0	$212,492	100.0

Gross Profit (Loss). Gross profits (loss) were ($243.4) million and $51.0 million for the nine months ended July 31, 2002 and 2003, respectively. The $294.4 million increase was primarily the result of a $289.0 million decrease in inventory obsolescence cost.

Gross profit (loss) as a percentage of revenue was (81.3%) and 24.0% for the nine months ended July 31, 2002 and 2003, respectively. The increase was largely attributable to decreases in inventory obsolescence costs, increases in manufacturing efficiencies, and higher margin product mix. Gross profit on products as a percentage of product revenue was 24.7% and 32.9% for the nine months ended July 31, 2002 and 2003, respectively. The increase was largely attributable to increases in manufacturing efficiencies and higher margin product mix. Gross loss on services as a percentage of services was 47.7% and 48.0% for the nine months ended July 31, 2002 and 2003, respectively.

Research and Development Expenses. Research and development expenses (exclusive of deferred stock compensation costs of $11.3 and $10.1 million) were $178.3 million and $153.9 million for the nine months ended July 31, 2002 and 2003, respectively. During the first nine months of fiscal 2002 and 2003, research and development expenses were 59.6% and 72.4% of revenue, respectively. The $24.4 million or 13.7% decrease was the result of decreased employee related expenses, prototype costs, consulting expenses, and depreciation expense. CIENA expenses research and development costs as incurred.

Selling and Marketing Expenses. Selling and marketing expenses (exclusive of deferred stock compensation costs of $2.6 and $2.1 million) were $98.3 million and $76.8 million for the nine months ended July 31, 2002 and 2003, respectively. During the first nine months of fiscal 2002 and 2003, selling and marketing expenses were 32.8% and 36.1% of revenue, respectively. The $21.5 million, or 21.8%, decrease was the result of reduced levels of sales staff, advertising costs, outside consultants, facility costs and depreciation expense.

General and Administrative Expenses. General and administrative expenses (exclusive of deferred stock compensation costs of $0.7 and $1.0 million) were $37.7 million and $28.2 million for the nine months ended July 31, 2002 and 2003, respectively. During the first nine months of 2002 and 2003, general and administrative expenses were 12.6% and 13.3% of revenue, respectively. The $9.5 million or 25.2% decrease was primarily the result of decreases in staffing levels, outside consultants and facility costs.

Deferred Stock Compensation Costs. Deferred stock compensation costs were $14.6 million and $13.3 million for the nine months ended July 31, 2002 and 2003, respectively. As part of our acquisition of Cyras, ONI and WaveSmith, we recorded $98.5, $8.8 million and $7.4 of deferred stock compensation relating to the unvested stock options and restricted stock assumed in the acquisition, respectively. Deferred stock compensation is presented as a reduction of stockholders' equity and is amortized over the remaining vesting period of the applicable options. As of July 31, 2003, the balance of deferred stock compensation is $14.9 million.

Amortization of Intangible Assets. Amortization of intangible assets (exclusive of $0 and $2.3 million included in cost of goods sold related to certain technology licenses) was $6.0 million and $11.5 million for the nine months ended July 31, 2002 and 2003, respectively. In purchasing companies, we have acquired intangible assets such as certain developed technology, patents and covenants not to compete. As part of our March 2001 acquisition of Cyras, we recorded $47.7 million worth of other intangible assets. The intangible assets from the Cyras purchase will be amortized over a seven-year period. As part of our June 2002 acquisition of ONI, we recorded $15.1 million worth of other intangibles assets. The intangible assets from our ONI purchase will be amortized over periods ranging from two-months to seven years. As part of our June 2003 acquisition of WaveSmith, we recorded $59.7 million worth of other intangible assets. The intangible assets from the WaveSmith acquisition will be amortized over a period ranging from 2.5 months to seven years.

In-Process Research and Development. In connection with the WaveSmith acquisition, the Company recorded a $1.5 million charge related to in-process research and development for the nine-months ended July 31, 2003. This generally represents the estimated value of purchased in-process technology related to WaveSmith's multi-service switching product development that had not yet reached technological feasibility and had no alternative future use at the time of the acquisition. The amount of purchase price allocated to in-process research and development was determined using the discounted cash flow method. This method consisted of estimating future net cash flows attributable to the in-process technology for a discrete projection period and discounting the net cash flows back to their present value.

Nortel Networks Settlement Costs. In January 2003, we reached an agreement with Nortel. Under the settlement agreement, we made a one-time payment of $25.0 million to Nortel, and Nortel granted CIENA a license under the patents in suit and certain related patents. CIENA accounted for the $25.0 million liability by recording an expense of $2.5 million in first quarter 2003 related to the settlement of the litigation, and recording the remaining $22.5 million as an intangible asset that will be amortized over eight years based upon the expected life of the patent rights acquired in the settlement.

Restructuring Costs. During the nine months ended July 31, 2002, we recorded a restructuring charge of $146.7 million associated with workforce reductions, lease terminations, non-cancelable lease costs and the write-down of certain property, equipment and leasehold improvements associated with our restructuring activities. During the nine months ended July 31, 2003, we recorded a restructuring charge of $19.9 associated with workforce reductions and the write-down of certain property and equipment. This was offset by a credit of $1.6 million related to the adjustment of previously estimated restructuring charges. We expect to incur similar charges over the next several quarters as a result of our ongoing program to restructure our business.

Provision for Doubtful Accounts. We recorded a net provision for doubtful accounts of $14.8 million in the nine months ended July 31, 2002. This provision relates to the estimated losses from two customers whose financial condition suggested that they would not be able to make required payments to CIENA. No provision was recorded in the first nine months of fiscal 2003.

Interest and Other Income, Net. Interest income and other income, net were $44.8 million and $33.3 million for the nine months ended July 31, 2002 and 2003, respectively. The $11.5 million decrease was attributable to the impact of lower average interest rates and lower average cash and invested balances.

Interest Expense. Interest expense was $29.8 million and $28.3 million for the nine months ended July 31, 2002 and 2003, respectively. The $1.4 million, or 4.8%, decrease was attributable to the decrease in our debt obligations between the two periods.

Loss on Equity Investments, Net. Loss on equity investments, net was $5.7 million for the nine months ended July 31, 2002. We realized a loss of $1.9 million from the sale of a public equity investment and a loss of $6.6 million from a decline in the fair value of a public equity investment that was determined to be other than temporary. On November 16, 2001, CIENA sold 80.1% of its ownership in ATI International Investments, Inc., the parent company of ATI Telecom International Ltd. (“Alta”), which resulted in a gain of $2.8 million. CIENA retains a 19.9% ownership in ATI International Investments, Inc.

Loss on Extinguishment of Debt. In the first nine months of fiscal 2003, CIENA conducted a tender offer to purchase the remaining outstanding $202.9 million of ONI 5.00% convertible subordinated notes which resulted in its purchase of $154.7 million of those notes. CIENA paid $140.3 million for notes with a cumulative accreted book value of $119.7 million, which resulted in a loss on early extinguishment of debt of $20.6 million.

Provision for Income Taxes. CIENA’s provision for income taxes was $112.2 million for the nine months ended July 31, 2002. This was inclusive of a net income tax benefit of $193.6 million or 34% of the net loss for the period, offset by a $305.8 million non-cash charge to a valuation allowance against our gross deferred tax assets. CIENA’s provision for income taxes was $0.9 million for the first nine months of fiscal 2003. This provision was primarily attributable to foreign taxes related to CIENA’s foreign operations. We did not record a tax benefit for CIENA’s domestic losses during the first nine months of fiscal 2003. CIENA intends to maintain a valuation allowance against certain deferred tax assets until sufficient positive evidences exists to support its reversal.

Net Loss. CIENA’s net loss for the nine months ended July 31, 2002 and 2003 was $842.7 million and $271.5 million, respectively.

Liquidity and Capital Resources

At July 31, 2003, CIENA’s principal source of liquidity was its cash and cash equivalents of $585.3 million, short-term investments of $727.1 million and long-term investments of $437.1 million.

Cash provided by operations was $67.1 million for the nine months ended July 31, 2002. This was comprised of a large net loss offset by the provision for inventory obsolescence, collection of accounts receivable, the change in the deferred income tax asset and the charge due to the non-cash portion of restructuring charges and related asset write-downs.

Cash used in operations was $174.7 million for the nine months ended July 31, 2003. This was comprised of the net loss, and the reduction in accounts payable offset by the early extinguishment of debt, the non-cash portion of restructuring charges and related asset write-downs, depreciation and amortization expense, amortization of intangibles and the reduction of inventory.

During the nine months ended July 31, 2002, cash provided by investing activities was $413.6 million. Investment activities included the net maturities of $189.0 million worth of short and long-term investments and purchases of $57.3 million of capital expenditures, $5.0 million for equity investments in non-public companies and a receipt of $286.9 million from the ONI acquisition.

During the nine months ended July 31, 2003, cash provided by investing activities was $516.4 million. Investment activities included the net maturities of $537.1 million worth of short and long-term investments and purchases of $24.8 million of capital expenditures and a receipt of $4.2 million from the WaveSmith acquisition.

Cash used in financing activities for the nine months ended July 31, 2002 was $163.4 million. On April 30, 2002, we redeemed all the outstanding Cyras Systems LLC 4.5% convertible subordinated notes at a total redemption price of $178.4 million.

Cash used in financing activities for the nine months ended July 31, 2003 was $133.6 million. The primary use was related to the purchase of $154.7 million of the remaining $202.9 million outstanding ONI convertible subordinated notes. We paid $139.2 million for the notes and fees of $1.1 million related to the purchase. Also, during the nine months ended July 31, 2003, we received $5.8 million from the exercise of stock options and $1.6 million from the repayment of notes receivable from stockholders.

The following is a summary of our future minimum payments under contractual obligations as of July 31, 2003 (in thousands):

	Total	Less than one year	One to three years	Four to five years	Thereafter
Convertible notes (1)	$ 860,749	$ 28,289	$103,648	$728,812	$ —
Operating leases	259,064	37,047	72,378	57,871	91,768
Purchase obligations (2)	40,010	40,010	—	—	—
Total	$1,159,823	$105,346	$176,026	$786,683	$91,768

The following is a summary of our other commercial commitments by commitment expiration date as of July 31, 2003 (in thousands):

	Total	Less than one year	One to three years	Four to five years	Thereafter
Standby letters of credit	$10,890	$10,280	$360	$250	$—

Notes to above tables:

(1) The terms of our convertible notes with a principal value of $690.0 million include interest at 3.75% payable on a semi-annual basis on February 1 and August 1 of each year; the notes are due February 1, 2008. The terms of the ONI convertible subordinated notes with a principal value of $48.3 million include interest at 5.00% payable on a semi-annual basis on April 15 and October 15 of each year; the notes are due October 15, 2005

(2) Purchase commitments related to amounts we are obligated to pay to our contract manufacturers and component suppliers for inventory. In the quarter ending October 31, 2003, we expect inventory to increase as a result of providing a sizeable amount of equipment for a large customer trial. If we are unsuccessful in winning this contract, we may be required to take a charge for the write down or write off of this inventory.

On August 21, 2003, CIENA announced that it had entered into an agreement to acquire by merger Akara Corporation, a privately held corporation headquartered in Kanata, Ontario. Under the terms of the acquisition agreement, Akara will merge with a wholly-owned subsidiary of CIENA, and all the remaining shares of Akara common and preferred stock will be exchanged for aggregate consideration of $45 million consisting of $31 million in cash and $14 million in shares of CIENA common stock. The number of shares to be issued will be determined based on the average closing prices of CIENA common stock on the Nasdaq Stock Market on the ten trading days preceding the closing date. We expect to complete the transaction during the fourth quarter of fiscal 2003.

We have also agreed in principle to invest up to $15 million in other private companies. We anticipate that we will complete these other transactions in the fourth quarter of fiscal 2003.

Based on past performance and current expectations, we believe that our cash and cash equivalents, short-term investments, and cash generated from operations will satisfy our working capital needs, capital expenditures, investment requirements, commitments, and other liquidity requirements associated with our existing operations through at least the next 12 months.

Risk Factors

Investing in our securities involves a high degree of risk. In addition to the other information contained in this quarterly report, including the reports we incorporate by reference, you should consider the following factors before investing in our securities.

Our business could continue to be adversely affected by unfavorable and uncertain conditions in the communications industry and the economy in general

The last three years have seen substantial changes in the communications industry. Most of our customers and potential customers have confronted static or declining revenues. Many have experienced significant financial distress, and some have gone out of business. This has resulted in a significant change in the structure of the equipment industry, with greater concentration of purchasing power in a small number of large services providers, combined with a substantial reduction in overall demand. Together these factors have adversely affected our revenue and operating results. In addition, most of our customers have become more conservative and uncertain about their future purchases which has made managing our business difficult.

We expect the factors described above to continue to affect our business for an indeterminate period, in several significant ways:

- capital expenditures by many of our customers will be flat or reduced;
- we will continue to have only limited ability to forecast the volume and product mix of our sales;
- managing our expenditures will be difficult in light of the uncertainties surrounding our business;
- increased competition resulting from reduced demand will put substantial downward pressures on the pricing of our products, tending to reduce our profit margins;
- increased competition will enable customers to insist on more favorable terms and conditions for sales, including extended payment terms or other financing assistance, as a condition of procuring their business; and
- the bankruptcies or weakened financial condition of some of our customers may require us to write off amounts due to us from prior sales.

The result of any one or a combination of these factors could lead to further reduced revenue and increased operating losses.

We face intense competition that could hurt our sales and profitability

The market for networking solutions is extremely competitive. Competition in this market is based on varying combinations of price, functionality, manufacturing capability, installation, services, scalability and the ability of the system solutions to meet customers' immediate and future network requirements. A small number of very large companies, including Alcatel, Cisco Systems, Telefon AB LM Ericsson, Fujitsu Group, Hitachi Ltd., Huawei Technologies Co., Ltd, Lucent Technologies Inc., Marconi Corporation, NEC Corporation, Nortel Networks, Siemens AG and Tellabs, Inc., have historically dominated the telecommunications equipment industry. They all have greater financial, marketing, manufacturing and intellectual property resources than CIENA. They also often have existing relationships with our potential customers.

Because we sell systems that compete directly with product offerings of these companies, and in some cases displace or replace their equipment, we represent a competitive threat. The decline in the market for communications networking products has resulted in even greater competitive pressures. We expect that the aggressive tactics we have confronted on the part of many of these competitors will continue, and perhaps become more severe. These tactics include:

- intense price competition in sales of new equipment, resulting in lower profit margins;
- discounting resulting from sales of used equipment or inventory that a competitor has written down or written off;
- early announcements of competing products and other marketing efforts;
- "one-stop shopping" options;
- customer financing assistance;
- marketing and advertising assistance; and
- intellectual property disputes.

In addition, several of our largest competitors have experienced financial difficulties. We have confronted situations in which the competitor contends that unless the customer awards it the business, the competitor may fail, leaving the customer without support for the competitor's equipment already in the network. To the extent that such arguments are successful, we may be at a disadvantage in winning new business.

Tactics such as those described above can be particularly effective in a concentrated customer base like ours. Our customers are under increasing competitive pressure to deliver their services at the lowest possible cost. This pressure may result in the pricing of communications networking systems becoming a more important factor in customer decisions. This may favor larger competitors that can spread the effect of price discounts across a larger array of products and services and across a larger customer base than ours. If we are unable to offset any reductions in the average sales price for our products by a reduction in the cost of our products, our gross profit margins will be adversely affected. Our inability to compete successfully against our competitors and maintain our gross profit margins would harm our business, financial condition and results of operations.

Many of our customers have indicated that they intend to establish a relationship with at least two vendors for communication networking products. With respect to customers for whom we are the only supplier of networking solutions, we do not know when or if these customers will select a second vendor or what impact the selection might have on purchases from us. If a second supplier is chosen, these customers could reduce their purchases from us, which could in turn have a material adverse effect on us.

New competitors continue to emerge to compete with our products. They often base their products on the latest available technology. They may achieve commercial availability of their products more quickly due to the narrower focus of their efforts. Our inability to compete successfully against these companies would harm our business, financial condition and results of operations.

Product performance problems could limit our sales prospects

The development and production of new products with high technology content often involves problems with software, components and manufacturing methods. If significant reliability, quality or network monitoring problems develop, including those due to defects in software or faulty components, a number of negative effects on our business could result, including:

- costs associated with fixing software defects or reworking our manufacturing processes;
- high service and warranty expenses;
- payment of liquidated damages for performance failures;
- high inventory obsolescence expense;
- high levels of product returns;
- delays in collecting accounts receivable;
- reduced orders from existing customers; and
- declining interest from potential customers.

Although we maintain accruals for product warranties, actual costs could exceed these amounts. From time to time, there will be interruptions or delays in the activation of our products at a customer's site. These interruptions or delays may result from product performance problems or from aspects of the installation and activation activities, some of which are outside our control. If we experience significant interruptions or delays that we cannot promptly resolve, confidence in our products could be undermined, which could cause us to lose customers or otherwise harm our business.

Economic conditions may require us to reduce the size of our business further

Since November 2001, we have undertaken reductions in force, some of which were accompanied by dispositions of assets, as part of our effort to reduce the size of our operations to better match the reduced sales of our products and services. Weakness in the global economy generally, and the telecommunications equipment market in particular, continue to affect our business substantially. We will be required to take additional steps to reduce our costs, including further reductions in force. Any such steps would likely result in significant charges from write-downs or write-offs of assets, costs of lease terminations, and expenses resulting from the termination of personnel.

Selling our products requires substantial investments of our resources which may not produce anticipated benefits.

In order to sell our products to both potential and existing customers, we must invest in financial, engineering, manufacturing and logistics support resources, even though we are unsure of the volume, duration or timing of customer purchases. Our customers are generally technically sophisticated and demanding. Consequently, we may incur substantial expenses and devote resources to potential relationships that never materialize or fulfill our expectations, in which event our investment may largely be lost. For example, we often provide equipment and services to our customers, free of charge, for the purpose of performing laboratory testing. In the quarter ending October 31, 2003, we expect inventory to increase as a result of providing a sizeable amount of equipment for a large customer trial. If we are unsuccessful in winning this contract, we may be required to take a charge for the write down or write off of this inventory.

Our results can fluctuate unpredictably

Purchases by many of our potential and existing customers can be unpredictable, sporadic and subject to unanticipated changes. Our results, in turn, tend to fluctuate unpredictably. A decision to purchase our products requires a significant investment and commitment of resources by our customers. As a result, the sales cycles for many of our products are long, often as much as a year or two between initial contact with a potential customer and the recognition of revenue from sales to the customer. Further, purchases by our existing customers tend to be large and sporadic, depending upon their need to build a customer base, their plans for expanding their networks, the availability of financing, and the effects of regulatory and business conditions in the countries in which they operate. Current economic and market conditions have made it even more difficult to make reliable estimates of future revenue.

Fluctuations in our revenue can lead to even greater fluctuations in our operating profits. Our budgeted expense levels depend in part on our expectations of long-term future revenue. Any substantial adjustment to expenses to account for lower levels of revenue is difficult and takes time. Consequently, if our revenue does decline, our levels of inventory, operating expenses and general overhead would be high relative to our revenue, reducing our profitability, and perhaps resulting in additional operating losses.

Other factors can also contribute to fluctuations in our revenue and operating results, including:

- fluctuations in demand for our products;
- changes in our pricing policies or the pricing policies of our competitors;
- the timing and size of orders from customers;
- changes in customers’ requirements, including changes or cancellations to orders from customers;
- the introduction of new products by us or our competitors;
- changes in the price or availability of components for our products;
- readiness of customer sites for installation;
- satisfaction of contractual customer acceptance criteria and related revenue recognition issues;
- manufacturing and shipment delays and deferrals;
- increased service, installation, warranty or repair costs;
- the timing and amount of employer payroll tax to be paid on employee gains on stock options exercised; and
- changes in general economic conditions as well as those specific to the telecommunications industry.

Our future success will depend on our ability to acquire new customers, expand our distribution channels and increase our product portfolio

Historically, a large percentage of our sales have been made to emerging carriers, many of which have experienced severe financial difficulties. Consequently, we expect our sales to emerging carriers to be limited, and our future success will depend, to a large extent, on our ability to increase our sales to incumbent carriers, including, in the United States, the regional Bell operating companies ("RBOCs"), and abroad, the large, traditional telecommunications operators ("TOs"), many of which were formerly government-owned "post, telephone and telegraph" enterprises. If we do not succeed in continuing to penetrate this segment of the market, our business could suffer.

We are beginning to sell some of our products through systems integrators, distributors, resellers, and similar sales channels. We also are attempting to sell some of our products to large enterprises and federal, state and local governments. Since we have only limited experience in these sales efforts, it is uncertain to what extent we will be successful.

In order to make our offerings more attractive both to our existing customers and the new customers we hope to attract, we believe it is important that we increase our portfolio to include products that operate at the edge of the network and products that enable sophisticated services, including data services, beyond transport and switching. We plan to implement this strategy through a combination of internal development, acquisitions of smaller companies, and forming strategic alliances with other vendors. If we fail to execute this strategy, our addressable market may not be large enough to enable us to reach profitability at our current size.

Our strategy calls for us to expand the range of our product offerings and to sell to a greater variety of customers, both of which involve our entry into markets with which we have limited familiarity. In doing so, we will be confronted with new development challenges and sales and service issues with which we have limited experience to date. A failure to address those issues satisfactorily would harm our prospects for growth.

Selling to large, incumbent carriers is often more difficult and time-consuming than selling to newer carriers

We have relatively limited experience in selling to large RBOCs and TOs. Many of them have long-standing supplier relationships with other vendors, which present additional challenges to the sales process. The sales cycles for these larger customers is often substantially longer than for sales to smaller customers; and they often require extensive testing of products before deciding to purchase them. Even after we have signed a sales contract with a customer, we are typically unable to recognize revenue until final acceptance tests are completed satisfactorily. The certification process for new telecommunications equipment used in the networks of the RBOCs and TOs tends to be particularly lengthy and difficult. Complying with these certification requirements may involve unanticipated delays that could adversely affect the timing of our ability to sell our products to these larger carriers.

The success of our strategy depends on our ability to increase our revenue substantially

We believe, as a matter of strategy, we must maintain a size and breadth of our product portfolio that enables us to be successful in selling to the largest communications providers. In order to carry out that strategy, we have deliberately chosen to continue to spend on research and development, sales, and other operating expenses at levels that will not permit us to return to profitability unless we can increase our revenue substantially. If we fail to do so, we will be required to modify our strategy, which would likely have an adverse effect on our financial condition.

We may not be successful in enhancing and upgrading our products

The market for communications networking solutions is characterized by rapid technological change, frequent introductions of new products, and recurring changes in customer requirements. To succeed in this market, we must continue to develop new products and new features for existing products. Doing so is difficult and costly and there is no assurance that we will continue to be successful. In addition, we must be able to identify and gain access to promising new technologies. Failure to keep pace with technological advances would impair the competitiveness of our products and sooner or later do serious harm to our business.

Our products are based on complex technology that could result in unanticipated delays in developing, improving, manufacturing or deploying them. Modifying our products to enable customers to integrate them into a new type of network architecture entails similar development risks.

Certain enhancements to our products are in the development phase and are not yet ready for commercial manufacturing or deployment. The maturing process from laboratory prototype to customer trials, and subsequently to general availability, involves a number of steps, including:

- completion of product development;
- the qualification and multiple sourcing of critical components, including ASICs;
- validation of manufacturing methods and processes;
- extensive quality assurance and reliability testing, and staffing of testing infrastructure;
- validation of software; and
- establishment of systems integration and systems test validation requirements.

Each of these steps, in turn, presents serious risks of failure, rework or delay, any one of which could decrease the speed and scope of product introduction and marketplace acceptance of the product. Specialized ASICs and intensive software testing and validation are key to the timely introduction of enhancements to several of our products and schedule delays are common in the final validation phase, as well as in the manufacture of specialized ASICs. In addition, unexpected intellectual property disputes, failure of critical design elements, and a host of other execution risks may delay or even prevent the introduction of these products. If we do not develop and successfully introduce these products in a timely manner, our business, financial condition and results of operations would be harmed.

Our strategy involves pursuing strategic acquisitions and investments that may not be successful

Our business strategy includes acquiring or making strategic investments in other companies with a view to expanding our portfolio of products and services, acquiring new technologies, and accelerating the development of new or improved products. To do so, we may issue equity that would dilute our current shareholders' percentage ownership or incur debt or assume indebtedness. In addition, we may incur significant amortization expenses related to intangible assets. In the fourth quarter fiscal 2001 and fourth quarter fiscal 2002, we incurred a significant write-off of goodwill associated with our previous acquisitions. Strategic investments and acquisitions involve numerous risks, including:

- potential large cash expenditures;
- difficulties in integrating the operations, technologies and products of the acquired companies;
- diversion of management's attention from our core business;
- potential difficulties in completing projects of the acquired company;
- the potential loss of key employees of the acquired company;
- dependence on unfamiliar or relatively small supply partners; and
- exposure to unanticipated liabilities.

In addition, acquisitions and strategic investments may involve risks of entering markets in which we have no or limited direct prior experience and where competitors in such markets have stronger market positions and of obtaining insufficient revenue to offset increased expenses associated with acquisitions.

We may not be able to achieve the benefits we anticipate from the mergers of WaveSmith and Akara

In June 2003, we completed our merger with WaveSmith, and we anticipate completing a merger with Akara in the fourth quarter of fiscal 2003. The process of integrating these two companies into CIENA is complex and exposes us to a variety of risks, including the possible loss of key personnel and failure to integrate these two product lines. It is possible, therefore, that we will not achieve all of the benefits we anticipate from the mergers.

In addition to these operational risks, the mergers creates additional risks that could have a material adverse effect on CIENA's business, results of operations and financial condition. The mergers have and will result in CIENA succeeding to all known and unknown liabilities of WaveSmith and Akara. These liabilities may include liabilities to shareholders, customers, suppliers or employees, as well as liabilities related to intellectual property disputes. Further, CIENA estimated the fair market value of certain acquired assets and liabilities based on predictions about future developments. If these predictions are incorrect

CIENA may be required to record adjustments to its financial statements in the future.

There is also some uncertainty as to whether obtaining the agreements of WaveSmith stockholders to vote in favor of the WaveSmith merger prior to filing a registration statement with the SEC complied with the registration requirements of the Securities Act. While CIENA believes that the merger was effected in compliance with applicable securities and other laws, there can be no assurance that this is the case.

We face risks in reselling the products of other companies

We have recently entered into agreements that permit us to distribute the products of other companies and may enter into other agreements in the future. To the extent we succeed in reselling the products of these companies, we may be required by customers to assume warranty and service obligations. While these suppliers have agreed to support us with respect to those obligations, they are relatively small companies with limited financial resources. If they should be unable, for any reason, to provide the required support, we may have to expend our own resources on doing so. This risk is amplified by the fact that the equipment has been designed and manufactured by others, and is thus subject to warranty claims whose magnitude we are currently unable to evaluate fully.

We may not be successful in selling our products into new markets or through new channels

We have limited experience and capability in direct sales into the enterprise, government markets or certain geographic markets. We are accordingly taking steps to develop new sales channels through distributors and systems integrators for sales of those of our products that are suitable for those markets. We have limited experience in developing and managing such channels, and it is possible that our efforts may not succeed according to plan, which could reduce our revenue and profitability.

In addition, sales to federal, state and local governments often require compliance with complex procurement rules and regulations with which we have little experience. We may be unable to compete for government opportunities if we cannot comply with these rules and regulations.

We depend on a limited number of suppliers, and for some items we do not have a substitute supplier

We depend on a limited number of suppliers for components of our products, as well as for equipment used to manufacture and test our products. Our products include several high-performance components for which reliable, high-volume suppliers are particularly limited. Furthermore, some key optical and electronic components we use in our products are currently available only from sole or limited sources, and in some cases, that source also is a competitor. Any delay in component availability for any of our products could result in delays in deployment of these products and in our ability to recognize revenue. These delays could also harm our customer relationships and our results of operations.

Furthermore, the market for optical components is undergoing consolidation and contraction. This is resulting in reduced competition which could lead to higher prices and lower availability of components we purchase. In addition, the loss of a source of supply of key components could require us to re-engineer products that use those components, which would increase our costs.

On occasion, we have experienced delays in receipt of components and have received components that do not perform according to their specifications. Any future difficulty in obtaining sufficient and timely delivery of components could result in delays or reductions in product shipments, which, in turn, could harm our business. A consolidation among suppliers of these components or adverse developments in their businesses affecting their ability to supply us, could adversely impact the availability of components on which we depend. Delayed deliveries of key components from these sources could adversely affect our business.

Any delays in component availability for any of our products or test equipment could result in delays in deployment of these products and in our ability to recognize revenue from them. These delays could also harm our customer relationships and our results of operations.

We rely on contract manufacturers for our products

We rely on a small number of contract manufacturers to perform the majority of the manufacturing operations for our products. The qualification of these manufacturers is an expensive and time-consuming process, and these contract manufacturers build modules for other companies, including our competitors. In addition, we do not have contracts in place with some of these manufacturers. We may not be able to effectively manage our relationships with our manufacturers and we cannot be certain that they will be able to fill our orders in a timely manner. If we underestimate our future product requirements, the contract manufacturers may not have enough product to meet our customer requirements, and this could result in delays in the shipment of our products and our ability to recognize revenue. If we cannot effectively manage these manufacturers and forecast future demand, or if they fail to deliver products or components on time, our business may suffer.

Our ability to compete could be harmed if we are unable to protect and enforce our intellectual property rights or if we infringe on intellectual property rights of others

We rely on a combination of patent, copyright, trademark and trade secret laws and restrictions on disclosure to protect our intellectual property rights. We enter into non-disclosure and proprietary rights agreements with our employees and consultants, license agreements with our corporate partners, and control access to and distribution of our products, documentation and other proprietary information. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy or otherwise obtain and use our products or technology. Monitoring unauthorized use of our products is difficult and we cannot be certain that the steps we have taken will prevent unauthorized use of our technology, particularly in foreign countries where the laws may not protect our proprietary rights as fully as in the United States. If competitors are able to use our technology, our ability to compete effectively could be harmed. We have filed an intellectual property lawsuit to enforce our intellectual property right, and may become involved with additional disputes in the future. Such lawsuits can be costly and may significantly divert the time and attention of our personnel.

We have been subject to several claims of patent infringement, which in some cases have required us to pay the patent holders substantial sums or enter into license agreements requiring ongoing royalty payments. The frequency of assertions of patent infringement in the field of telecommunications networking solutions seems to be increasing as patent holders seek alternative sources of revenue. There is a possibility that we may again find ourselves required to take patent licenses or to redesign or stop selling products that allegedly infringe patents belonging to others. If we are sued for infringement and are unsuccessful in defending the suit, we could be subject to significant damages, and our business and customer relationships could be adversely affected.

We face risks associated with our international operations

We market, sell and service our products globally. We have established offices around the world, including in North America, Europe, Latin America and in the Asia Pacific region. We will continue to expand our international operations and enter new international markets. This expansion will require significant management attention and financial resources to develop successfully direct and indirect international sales and support channels. In some countries, our success will depend in part on our ability to form relationships with local partners. We cannot be sure that we will be able to identify appropriate partners or reach mutually satisfactory arrangements with them for sales of our products. There is a risk that we may sometimes choose the wrong partner. For these reasons, we may not be able to maintain or increase international market demand for our products.

International operations are subject to inherent risks, and our future results could be adversely affected by a variety of uncontrollable and changing factors. These include:

- greater difficulty in collecting accounts receivable and longer collection periods;
- difficulties and costs of staffing and managing foreign operations;
- the impact of recessions in economies outside the United States;
- unexpected changes in regulatory requirements;
- certification requirements;
- reduced protection for intellectual property rights in some countries;
- potentially adverse tax consequences;
- political and economic instability;
- trade protection measures and other regulatory requirements;
- service provider and government spending patterns; and
- natural disasters and epidemics.

Such factors could have a material adverse impact on our operating results and financial condition.

If we are unable to retain and attract qualified personnel, we may be unable to effectively manage our business.

If we are unable to retain and motivate our existing employees and attract qualified personnel to fill key positions, we may be unable to effectively develop our existing products, make timely product introductions and increase sales. Since we generally do not have employment contracts with our employees, we must rely upon providing competitive compensation packages and a dynamic work environment to retain and motivate employees. In response to the decline in our revenue and weakness in the telecommunications equipment market, we have not increased salaries for or paid bonuses to most of our employees since the end of fiscal 2001. Since our compensation packages include equity-based incentives, pressure on our stock price could affect our ability to continue to offer competitive compensation packages to our employees. In addition to these compensation issues, we must continue to motivate employees to execute our strategies and achieve our goals, which may be difficult due to morale challenges posed by the workforce reductions and uncertainty in our industry and the economy in general.

If we lose members of our management team or other key personnel, it may be difficult to replace them. Even in the current economic downturn, competition for highly skilled technical and other personnel can be intense. As a result, we may not be successful in identifying, recruiting and hiring qualified engineers and other key personnel.

Some of our suppliers are also competitors

Some of our component suppliers are both primary sources for components and major competitors in the market for system equipment. We buy components from Alcatel, NEC and Siemens. Each of these companies offers optical communications systems and equipment that compete against our products. A decline in reliability or other adverse change in these supply relationships could harm our business.

We are exposed to the credit risk of our customers

Industry and economic conditions have weakened the financial position of some of our customers. To sell to some of these customers, we may be required to take risks of uncollectible accounts. While we monitor these situations carefully and attempt to take appropriate measures to protect ourselves, it is possible that we may have to write down or write off doubtful accounts. Such write-downs or write-offs, if large, could have a material adverse effect on our operating results and financial condition.

Our stock price is volatile

Our common stock price has experienced substantial volatility in the past, and is likely to remain volatile in the future. Volatility can arise as a result of divergence between our actual or anticipated financial results and published expectations of analysts, and announcements that we, our competitors, or our customers may make.

Divergence between our actual results and our anticipated results, analyst estimates and public announcements by us, our competitors, or by customers will occur from time to time in the future, with resulting stock price volatility, irrespective of our overall year-to-year performance or long-term prospects. As long as we continue to depend on a limited customer base, and particularly when a substantial majority of their purchases consist of newly-introduced products, there is substantial chance that our quarterly results will vary widely.

Forward-Looking statements

Some of the statements contained, or incorporated by reference, in this quarterly report discuss future expectations, contain projections of results of operations or financial condition or state other “forward-looking” information. Those statements are subject to known and unknown risks, uncertainties and other factors that could cause the actual results to differ materially from those contemplated by the statements. The “forward-looking” information is based on various factors and was derived using numerous assumptions. In some cases, you can identify these so-called “forward-looking statements” by words like “may,” “will,” “should,” “expects,” “plans,” “anticipates,” “believes,” “estimates,” “predicts,” “potential” or “continue” or the negative of those words and other comparable words. You should be aware that those statements only reflect our predictions. Actual events or results may differ substantially. Important factors that could cause our actual results to be materially different from the forward-looking statements are disclosed throughout this report, particularly under the heading “Risk Factors” above.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The following discussion about the Company's market risk disclosures involves forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements. The Company is exposed to market risk related to changes in interest rates and foreign currency exchange rates. The Company does not use derivative financial instruments for speculative or trading purposes.

Interest Rate Sensitivity. The Company maintains a short-term and long-term investment portfolio. These available-for-sale securities are subject to interest rate risk and will fall in value if market interest rates increase. If market interest rates were to increase immediately and uniformly by 10% from levels at July 31, 2003, the fair value of the portfolio would decline by approximately $80.8 million.

Foreign Currency Exchange Risk. As a global concern, the Company faces exposure to adverse movements in foreign currency exchange rates. These exposures may change over time as business practices evolve and could have a material adverse impact on the Company's financial results. Historically CIENA's primary exposures have been related to non-dollar denominated operating expenses in Europe and Asia where the Company sells primarily in U.S. dollars. CIENA is prepared to hedge against fluctuations in foreign currency if this exposure becomes material. As of July 31, 2003, the assets and liabilities of the Company related to non-dollar denominated currencies were not material. Therefore we do not expect an increase or decrease of 10% in the foreign exchange rate would have a material impact on the Company's financial position.

Item 4. Controls and Procedures

The Chief Executive Officer and Chief Financial Officer of CIENA have evaluated the effectiveness of the disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), as required by paragraph (b) of Rules 13a-15 and 15d-15 under the Exchange Act, and have concluded that as of the end of the period covered by this report the disclosure controls and procedures were effective at meeting their objectives.

There was no change in CIENA's internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Rules 13a-15 and 15d-15 under the Exchange Act during CIENA's last fiscal quarter that materially affected, or is reasonably likely to materially affect, CIENA's internal control over financial reporting.

PART II. - OTHER INFORMATION

Item 1. Legal Proceedings

On October 3, 2000, Stanford University and Litton Systems filed a complaint in the United States District Court for the Central District of California alleging that optical fiber amplifiers incorporated into CIENA's products infringe U.S. Patent No. 4,859,016. The complaint seeks injunctive relief, royalties and damages. We were first served with this complaint on April 30, 2003. We believe that we have valid defenses to the lawsuit and intend to defend it vigorously.

On July 19, 2000, CIENA and CIENA Properties, Inc., a wholly owned subsidiary of CIENA, filed a complaint in the United States District Court for the District of Delaware requesting damages and injunctive relief against Corvis Corporation ("Corvis"). The suit charged Corvis with infringing four patents relating to CIENA's optical networking communication systems and technology. A jury trial to determine whether Corvis is infringing these patents commenced on February 10, 2003. On February 24, 2003, the jury decided that Corvis was infringing one of the patents and not infringing two others. The jury was deadlocked with respect to infringement on the fourth patent. This trial was immediately followed by a trial on Corvis' affirmative defenses based on the validity of two of the patents. On February 28, 2003, the jury in this trial determined that the patents were valid. In April 2003, following a third trial, another jury decided that Corvis had infringed the fourth patent on which the previous jury had deadlocked. Based on these favorable verdicts collectively holding that Corvis is infringing two valid CIENA patents, CIENA has moved for an injunction to prohibit the sale by Corvis of the infringing products. The court has not yet ruled on this motion.

As a result of the merger with ONI, we became a defendant in a securities class action lawsuit. Beginning in August 2001, a number of substantially identical class action complaints alleging violations of the federal securities laws were filed in the United States District Court for the Southern District of New York. These complaints name ONI, Hugh C. Martin, ONI's former chairman, president and chief executive officer; Chris A. Davis, ONI's former executive vice president, chief financial officer and administrative officer; and certain underwriters of ONI's initial public offering as defendants. The complaints were consolidated into a single action, and a consolidated amended complaint was filed on April 24, 2002. The amended complaint alleges, among other things, that the underwriter defendants violated the securities laws by failing to disclose alleged compensation arrangements (such as undisclosed commissions or stock stabilization practices) in the initial public offering's registration statement and by engaging in manipulative practices to artificially inflate the price of our common stock after the initial public offering. The amended complaint also alleges that ONI and the named former officers violated the securities laws on the basis of an alleged failure to disclose the underwriters' alleged compensation arrangements and manipulative practices. No specific amount of damages has been claimed. Similar complaints have been filed against more than 300 other issuers that have had initial public offerings since 1998, and all of these actions have been included in a single coordinated proceeding. Mr. Martin and Ms. Davis have been dismissed from the action without prejudice pursuant to a tolling agreement. In July 2002, ONI and other issuers in the consolidated cases filed motions to dismiss the amended complaint for failure to state a claim, which was denied as to ONI on February 19, 2003. CIENA has participated, together with the other issuer defendants in these cases, in mediated settlement negotiations that have led to a preliminary agreement among the plaintiffs, the issuer defendants and their insurers. The settlement, which is subject to court approval, would result in the dismissal of the plaintiffs' cases against the issuers. CIENA has agreed in principle to the terms of this settlement. CIENA does not anticipate that it will be required to make any payments as a result of the settlement.

On May 3, 2002, a shareholder derivative complaint alleging violations of California state law was filed in the Superior Court of the State of California, County of Santa Clara against ONI. As a result of the merger with ONI, CIENA has also become a defendant in the lawsuit. The complaint names Hugh Martin; the other members of the ONI's board of directors; Terrence J. Schmid, ONI's former chief financial officer and vice president, finance and administration; and certain underwriters of ONI's initial public offering as defendants. The complaint alleges that the defendants breached their fiduciary duties, acted negligently and were unjustly enriched in determining the offering price of ONI Systems common stock in ONI's initial public offering. No specific amount of damages has been claimed. The complaint is encaptioned Sabrina Kurzman and Michael Kurzman, Derivatively on Behalf of ONI Systems Corp. v. Hugh C. Martin. In September 2002, CIENA filed a motion to dismiss the complaint. The Company's motion to dismiss was granted by the court on November 6, 2002. On December 2, 2002, the plaintiffs filed a notice of appeal from the court's order. Plaintiffs have withdrawn their appeal, and the lawsuit was dismissed on June 19, 2003.

As a result of the merger with ONI, we also became a defendant in two substantially identical purported class actions on behalf of ONI security holders originally brought against ONI and members of its board of directors. The complaints allege that the director defendants breached their fiduciary duties to ONI in approving the merger with CIENA and seek declaratory, injunctive and other relief permitted by equity. The plaintiffs failed to obtain an injunction against completion of the merger. The first of these cases was filed on February 20, 2002, in the Superior Court of the State of California, County of San Mateo, and is encaptioned K.W. Sams, On Behalf of Himself and All Others Similarly Situated v. ONI Systems Corporation, et al. The second case was brought on March 19, 2002, in the Superior Court of the State of California, County of Santa Clara, and is encaptioned Steven Myeary, On Behalf of Himself and All Others Similarly Situated v. ONI Systems Corporation. On April 14, 2003, the plaintiffs in these cases filed a consolidated amended complaint and named four additional defendants: CIENA Corporation, James F. Jordan, Kleiner Perkins Caufield & Byers and Mohr Davidow Ventures. We believe that these lawsuits are without merit and will continue to defend them vigorously.

Item 2. Changes in Securities and Use of Proceeds

Not applicable

Item 3. Defaults Upon Senior Securities

Not applicable

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

Not Applicable

Item 5. Other Information

Not applicable

Item 6. Exhibits and Reports on Form 8-K

(a)

Exhibit	Description
10.36	WaveSmith Networks, Inc. 2000 Stock Option and Incentive Plan
31.1	Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934 as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934 as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief 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 Chief Financial Officer Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(b) Reports on Form 8-K:

- Form 8-K (Item 9 reported) filed June 17, 2003
- Form 8-K (Item 7 and Item 12 reported) filed August 21, 2003

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.

	CIENA CORPORATION	
Date: August 21, 2003	By:	/s/ Gary B. Smith Gary B. Smith President, Chief Executive Officer and Director (Duly Authorized Officer)
Date: August 21, 2003	By:	/s/ Joseph R. Chinnici Joseph R. Chinnici Senior Vice President, Finance and Chief Financial Officer (Principal Financial Officer)

Exhibit 10.36

WAVESMITH NETWORKS, INC.

2000 STOCK OPTION AND INCENTIVE PLAN

1. Purpose and Eligibility

The purpose of this 2000 Stock Option and Incentive Plan (the "Plan") of WaveSmith Networks, Inc. (the "Company") is to provide stock options and other equity interests in the Company (each, an "Award") to employees, officers, directors, consultants and advisors of the Company and its Subsidiaries, all of whom are eligible to receive Awards under the Plan. Any person to whom an Award has been granted under the Plan is called a "Participant." Additional definitions are contained in Section 8.

2. Administration

a. Administration by Board of Directors. The Plan will be administered by the Board of Directors of the Company (the "Board"). The Board, in its sole discretion, shall have the authority to grant and amend Awards, to adopt, amend and repeal rules relating to the Plan and to interpret and correct the provisions of the Plan and any Award. All decisions by the Board shall be final and binding on all interested persons. Neither the Company nor any member of the Board shall be liable for any action or determination relating to the Plan.

b. Appointment of Committees. To the extent permitted by applicable law, the Board may delegate any or all of its powers under the Plan to one or more committees or subcommittees of the Board (a "Committee"). All references in the Plan to the "Board" shall mean such Committee or the Board.

c. Delegation to Executive Officers. To the extent permitted by applicable law, the Board may delegate to one or more executive officers of the Company the power to grant Awards and exercise such other powers under the Plan as the Board may determine, *provided that* the Board shall fix the maximum number of Awards to be granted and the maximum number of shares issuable to any one Participant pursuant to Awards granted by such executive officers.

3. Stock Available for Awards

a. Number of Shares. Subject to adjustment under Section 3(c), the aggregate number of shares of common stock, par value $.01 per share, of the Company (the "Common Stock") that may be issued pursuant to the Plan is 8,900,000 shares. If any Award, or shares of Common Stock issued pursuant to an Award, expires, or is terminated, repurchased, surrendered, forfeited or settled in cash (other than repurchases or cash settlements purported to be made at fair market value), in whole or in part, the Common Stock issued or issuable pursuant to such Award as to which such event has occurred shall again be available for the grant of Awards under the Plan. Shares issued under the Plan may consist in whole or in part of authorized but unissued shares or treasury shares.

b. Per-Participant Limit. Subject to adjustment under Section 3(c), no Participant may be granted Awards during any one fiscal year to purchase more than 6,230,000 shares of Common Stock.

c. Adjustment to Common Stock. In the event of any stock split, stock dividend, extraordinary cash dividend, recapitalization, reorganization, merger, consolidation, combination, exchange of shares, liquidation, spin-off, split-up, or other similar change in capitalization or event, (i) the number and class of securities available for Awards under the Plan and the per-Participant share limit, (ii) the number and class of securities, vesting schedule and exercise price per share subject to each outstanding Option, (iii) the repurchase price per security subject to repurchase, and (iv) the terms of each other outstanding stock-based Award shall be adjusted by the Company (or substituted Awards may be made) to the extent the Board shall determine, in good faith, that such an adjustment (or substitution) is appropriate. If Section 7(e)(i) applies for any event, this Section 3(c) shall not be applicable.

4. Stock Options

a. General. The Board may grant options to purchase Common Stock (each, an "Option") and determine the number of shares of Common Stock to be covered by each Option, the exercise price of each Option and the conditions and limitations applicable to the exercise of each Option and the Common Stock issued upon the exercise of each Option, including vesting provisions, repurchase provisions and restrictions relating to applicable federal or state securities laws, as it considers advisable.

b. Incentive Stock Options. An Option that the Board intends to be an "incentive stock option" as defined in Section 422 of the Code (an "Incentive Stock Option") shall be granted only to employees of the Company and shall be subject to and shall be construed consistently with the requirements of Section 422 of the Code. The Board and the Company shall have no liability if an Option or any part thereof that is intended to be an Incentive Stock Option does not qualify as such. An Option or any part thereof that does not qualify as an Incentive Stock Option is referred to herein as a "Nonstatutory Stock Option."

c. Exercise Price. The Board shall establish the exercise price (or determine the method by which the exercise price shall be determined) at the time each Option is granted and specify it in the applicable option agreement.

d. Duration of Options. Each Option shall be exercisable at such times and subject to such terms and conditions as the Board may specify in the applicable option agreement.

e. Exercise of Option. Options may be exercised only by delivery to the Company of a written notice of exercise signed by the proper person together with payment in full as specified in Section 4(f) for the number of shares for which the Option is exercised.

f. Payment Upon Exercise. Common Stock purchased upon the exercise of an Option shall be paid for by one or any combination of the following forms of payment:

(i) by check payable to the order of the Company;

(ii) except as otherwise explicitly provided in the applicable option agreement, and only if the Common Stock is then publicly traded, delivery of an irrevocable and unconditional undertaking by a creditworthy broker to deliver promptly to the Company sufficient funds to pay the exercise price, or delivery by the Participant to the Company of a copy of irrevocable and unconditional instructions to a creditworthy broker to deliver promptly to the Company cash or a check sufficient to pay the exercise price; or

(iii) to the extent explicitly provided in the applicable option agreement, by (x) delivery of shares of Common Stock owned by the Participant valued at fair market value (as determined by the Board or as determined pursuant to the applicable option agreement), (y) delivery of a promissory note of the Participant to the Company (and delivery to the Company by the Participant of a check in an amount equal to the par value of the shares purchased), or (z) payment of such other lawful consideration as the Board may determine.

5. Restricted Stock

a. Grants. The Board may grant Awards entitling recipients to acquire shares of Common Stock, subject to (i) delivery to the Company by the Participant of a check in an amount at least equal to the par value of the shares purchased, and (ii) the right of the Company to repurchase all or part of such shares at their issue price or other stated or formula price from the Participant in the event that conditions specified by the Board in the applicable Award are not satisfied prior to the end of the applicable restriction period or periods established by the Board for such Award (each, a "Restricted Stock Award").

b. Terms and Conditions. The Board shall determine the terms and conditions of any such Restricted Stock Award. Any stock certificates issued in respect of a Restricted Stock Award shall be registered in the name of the Participant and, unless otherwise determined by the Board, deposited by the Participant, together with a stock power endorsed in blank, with the Company (or its designee). After the expiration of the applicable restriction periods, the Company (or such designee) shall deliver the certificates no longer subject to such restrictions to the Participant or, if the Participant has died, to the beneficiary designated by a Participant, in a manner determined by the Board, to receive amounts due or exercise rights of the Participant in the event of the Participant's death (the "Designated Beneficiary"). In the absence of an effective designation by a Participant, Designated Beneficiary shall mean the Participant's estate.

6. Other Stock-Based Awards

The Board shall have the right to grant other Awards based upon the Common Stock having such terms and conditions as the Board may determine, including, without limitation, the grant of shares based upon certain conditions, the grant of securities convertible into Common Stock and the grant of stock appreciation rights, phantom stock awards or stock units.

7. General Provisions Applicable to Awards

a. Transferability of Awards. Except as the Board may otherwise determine or provide in an Award, Awards shall not be sold, assigned, transferred, pledged or otherwise encumbered by the person to whom they are granted, either voluntarily or by operation of law, except by will or the laws of descent and distribution, and, during the life of the Participant, shall be exercisable only by the Participant. References to a Participant, to the extent relevant in the context, shall include references to authorized transferees.

b. Documentation. Each Award under the Plan shall be evidenced by a written instrument in such form as the Board shall determine or as executed by an officer of the Company pursuant to authority delegated by the Board. Each Award may contain terms and conditions in addition to those set forth in the Plan *provided that* such terms and conditions do not contravene the provisions of the Plan.

c. Board Discretion. The terms of each type of Award need not be identical, and the Board need not treat Participants uniformly.

d. Termination of Status. The Board shall determine the effect on an Award of the disability, death, retirement, authorized leave of absence or other change in the employment or other status of a Participant and the extent to which, and the period during which, the Participant, or the Participant's legal representative, conservator, guardian or Designated Beneficiary, may exercise rights under the Award.

e. Acquisition of the Company

(i) Consequences of an Acquisition.

(A) Acquisition Intended to be Accounted for as a Pooling-of-Interests. Upon the consummation of an Acquisition intended to be accounted for as a pooling-of-interests: all outstanding Awards shall remain the obligation of the Company or be assumed by the surviving or acquiring entity, and there shall be automatically substituted for the shares of Common Stock then subject to such Awards the consideration payable with respect to the outstanding shares of Common Stock in connection with the Acquisition.

(B) Acquisition Intended to be Accounted for under the Purchase Method. Unless otherwise expressly provided in the applicable Option or Award, upon the occurrence of an Acquisition intended to be accounted for under the purchase method, the Board or the board of directors of the surviving or acquiring entity (as used in this Section 7(e)(i)(B), also the "Board"), shall, as to outstanding Awards (on the same basis or on different bases, as the Board shall specify), make appropriate provision, subject to Section 7(e)(i)(C), for the continuation of such Awards by the Company or the assumption of such Awards by the surviving or acquiring entity and by substituting on an equitable basis for the shares then subject to such Awards either (a) the consideration payable with respect to the outstanding shares of Common Stock in connection with the Acquisition, (b) shares of stock of the surviving or acquiring corporation or (c) such other securities as the Board deems appropriate, the fair market value of which (as determined by the Board in its sole discretion) shall not materially differ from the fair market value of the shares of Common Stock subject to such Awards immediately preceding the Acquisition. In addition to or in lieu of the foregoing, with respect to outstanding Options, the Board may, upon written notice to the affected optionees, provide that one or more Options must be exercised, to the extent then exercisable or to be exercisable as a result of the Acquisition in accordance with Section 7(e)(i)(C) and as permitted by Section 7(i), within a specified number of days of the date of such notice, at the end of which period such Options shall terminate; or terminate one or more Options in exchange for a cash payment equal to the excess of the fair market value (as determined by the Board in its sole discretion) of the shares subject to such Options (to the extent then exercisable or to be exercisable as a result of the Acquisition or as permitted by Section 7(i)) over the exercise price thereof.

(C) Acquisitions Generally. Upon the consummation of an Acquisition, the exercisability of Options, the vesting provisions of Restricted Stock Awards, and the exercisability of and/or vesting provisions under other stock-based Awards shall be accelerated, if at all, in accordance with the terms and conditions of the written instrument evidencing any such Options, Restricted Stock Awards or other stock-based Awards approved by the Board.

(D) Acquisition Defined. An "Acquisition" shall mean: (x) the consolidation with or acquisition by another entity in a merger, reorganization, consolidation of other form of business combination in which the other entity is the surviving or successor entity and the holders of outstanding voting stock of the Company immediately preceding the consummation of such event, shall, immediately following such event, hold, as a group, less than a majority of the voting securities of the surviving or successor entity; or (y) any sale of all or substantially all of the assets or capital stock of the Company (other than in a spin-off or similar transaction) or (z) any other acquisition of the business of the Company, as determined by the Board.

(ii) Assumption of Options Upon Certain Events. In connection with a merger or consolidation of an entity with the Company or the acquisition by the Company of property or stock of an entity, the Board may grant Awards under the Plan in substitution for stock and stock-based awards issued by such entity or an affiliate thereof. The substitute Awards shall be granted on such terms and conditions as the Board considers appropriate in the circumstances.

(iii) Pooling-of-Interests Accounting. If the Company proposes to engage in an Acquisition intended to be accounted for as a pooling-of-interests, and in the event that the provisions of this Plan or of any Award hereunder, or any actions of the Board taken in connection with such Acquisition, are determined by the Company's or the acquiring company's independent public accountants to cause such Acquisition to fail to be accounted for as a pooling-of-interests, then such provisions or actions shall be amended or rescinded by the Board, without the consent of any Participant, to be consistent with pooling-of-interests accounting treatment for such Acquisition.

(iv) Parachute Awards. Notwithstanding the provisions of any Option, Restricted Stock Award or other stock-based Award, if, in connection with the consummation of an Acquisition as described in Section 7(e)(i)(D), a tax under Section 4999 of the Code would be imposed on the Participant (after taking into account the exceptions set forth in Sections 280G(b)(4) and 280G(b)(5) of the Code), then the number of Awards which shall become exercisable, realizable or vested as provided in such written instrument evidencing such Option, Restricted Stock Award or other stock-based Award shall be reduced (or delayed), to the minimum extent necessary, so that no such tax would be imposed on the Participant (the Awards not becoming so accelerated, realizable or vested, the "Parachute Awards"); *provided, however,* that if the "aggregate present value" of the Parachute Awards would exceed the tax that, but for this sentence, would be imposed on the Participant under Section 4999 of the Code in connection with the Acquisition, then the Awards shall become immediately exercisable, realizable and vested without regard to the provisions of this sentence. For purposes of the preceding sentence, the "aggregate present value" of an Award shall be calculated on an after-tax basis (other than taxes imposed by Section 4999 of the Code) and shall be based on economic principles rather than the principles set forth under Section 280G of the Code and the regulations promulgated thereunder. All determinations required to be made under this Section 7(e)(iv) shall be made by the Company.

f. Withholding. Each Participant shall pay to the Company, or make provisions satisfactory to the Company for payment of, any taxes required by law to be withheld in connection with Awards to such Participant no later than the date of the event creating the tax liability. The Board may allow Participants to satisfy such tax obligations in whole or in part by transferring shares of Common Stock, including shares retained from the Award creating the tax obligation, valued at their fair market value (as determined by the Board or as determined pursuant to the applicable option agreement). The Company may, to the extent permitted by law, deduct any such tax obligations from any payment of any kind otherwise due to a Participant.

g. Amendment of Awards. The Board may amend, modify or terminate any outstanding Award including, but not limited to, substituting therefor another Award of the same or a different type, changing the date of exercise or realization, and converting an Incentive Stock Option to a Nonstatutory Stock Option, *provided that,* except as otherwise provided in Section 7(e)(iii), the Participant's consent to such action shall be required unless the Board determines that the action, taking into account any related action, would not materially and adversely affect the Participant.

h. Conditions on Delivery of Stock. The Company will not be obligated to deliver any shares of Common Stock pursuant to the Plan or to remove restrictions from shares previously delivered under the Plan until (i) all conditions of the Award have been met or removed to the satisfaction of the Company, (ii) in the opinion of the Company's counsel, all other legal matters in connection with the issuance and delivery of such shares have been satisfied, including any applicable securities laws and any applicable stock exchange or stock market rules and regulations, and (iii) the Participant has executed and delivered to the Company such representations or agreements as the Company may consider appropriate to satisfy the requirements of any applicable laws, rules or regulations.

i. Acceleration. The Board may at any time provide that any Options shall become immediately exercisable in full or in part, that any Restricted Stock Awards shall be free of some or all restrictions, or that any other stock-based Awards may become exercisable in full or in part or free of some or all restrictions or conditions, or otherwise realizable in full or in part, as the case may be, despite the fact that the foregoing actions may (i) cause the application of Sections 280G and 4999 of the Code if a change in control of the Company occurs, or (ii) disqualify all or part of the Option as an Incentive Stock Option.

8. Miscellaneous

a. Definitions.

(i) "Company," for purposes of eligibility under the Plan, shall include any present or future subsidiary corporations of WaveSmith Networks, Inc., as defined in Section 424(f) of the Code (a "Subsidiary"), and any present or future parent corporation of WaveSmith Networks, Inc., as defined in Section 424(e) of the Code. For purposes of Awards other than

Incentive Stock Options, the term "Company" shall include any other business venture in which the Company has a direct or indirect significant interest, as determined by the Board in its sole discretion.

(ii) "Code" means the Internal Revenue Code of 1986, as amended, and any regulations promulgated thereunder.

b. No Right To Employment or Other Status. No person shall have any claim or right to be granted an Award, and the grant of an Award shall not be construed as giving a Participant the right to continued employment or any other relationship with the Company. The Company expressly reserves the right at any time to dismiss or otherwise terminate its relationship with a Participant free from any liability or claim under the Plan.

c. No Rights As Stockholder. Subject to the provisions of the applicable Award, no Participant or Designated Beneficiary shall have any rights as a stockholder with respect to any shares of Common Stock to be distributed with respect to an Award until becoming the record holder thereof.

d. Effective Date and Term of Plan. The Plan shall become effective on the date on which it is adopted by the Board. No Awards shall be granted under the Plan after the completion of ten years from the date on which the Plan was adopted by the Board, but Awards previously granted may extend beyond that date.

e. Amendment of Plan. The Board may amend, suspend or terminate the Plan or any portion thereof at any time.

f. Governing Law. The provisions of the Plan and all Awards made hereunder shall be governed by and interpreted in accordance with the laws of Delaware, without regard to any applicable conflicts of law.

Adopted by the Board of Directors on:
, 2000

Approved by the stockholders on:
, 2000

Register of Amendments

Date	Section Amended

EXHIBIT 31.1

CIENA CORPORATION

CERTIFICATION OF CHIEF EXECUTIVE OFFICER

I, Gary B. Smith, certify that:

1. I have reviewed this quarterly report of CIENA Corporation;

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

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

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

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

(b) [Paragraph reserved pursuant to SEC Release 33-8238];

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

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

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

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

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

Date: August 21, 2003

/s/ Gary B. Smith
Gary B. Smith
President and Chief Executive Officer

EXHIBIT 31.2

CIENA CORPORATION

CERTIFICATION OF CHIEF FINANCIAL OFFICER

I, Joseph R. Chinnici, certify that:

1. I have reviewed this quarterly report of CIENA Corporation;

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

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

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

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

   (b) [Paragraph reserved pursuant to SEC Release 33-8238];

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

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

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

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

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

Date: August 21, 2003

/s/ Joseph R. Chinnici
Joseph R. Chinnici
Senior Vice President and Chief Financial Officer

EXHIBIT 32.1

CIENA CORPORATION

Written Statement of Chief Executive Officer
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

The undersigned, the Chief Executive Officer of CIENA Corporation (the "Company"), hereby certifies that, to his knowledge, on the date hereof:

(a) the Report on Form 10-Q of the Company for the three months ended July 31, 2003 filed on the date hereof with the Securities and Exchange Commission (the "Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(b) information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Gary B. Smith

Gary B. Smith
President and Chief Executive Officer
August 21, 2003

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to CIENA Corporation and will be retained by CIENA Corporation and furnished to the Securities and Exchange Commission or its staff upon request.

EXHIBIT 32.2

CIENA CORPORATION

Written Statement of Chief Financial Officer
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

The undersigned, the Chief Financial Officer of CIENA Corporation (the “Company”), hereby certifies that, to his knowledge, on the date hereof:

(a) the Report on Form 10-Q of the Company for the three months ended July 31, 2003 filed on the date hereof with the Securities and Exchange Commission (the “Report”) fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(b) information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Joseph R. Chinnici

Joseph R. Chinnici
Senior Vice President and Chief Financial Officer
August 21, 2003

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to CIENA Corporation and will be retained by CIENA Corporation and furnished to the Securities and Exchange Commission or its staff upon request.