



FORM 10-K

PMC SIERRA INC - PMCS

Filed: February 22, 2008 (period: December 30, 2007)

Annual report which provides a comprehensive overview of the company for the past year

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

FORM 10-K

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended: **December 30, 2007**

☐ **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 **0-19084**

PMC-Sierra, Inc.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

94-2925073
(I.R.S. Employer
Identification No.)

3975 Freedom Circle
Santa Clara, CA 95054
(Address of principal executive offices, including zip code)

Registrant's telephone number, including area code: **(408) 239-8000**

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of exchange on which registered
Common Stock, \$0.001 Par Value Preferred Stock Purchase Rights	The NASDAQ Stock Market LLC

Securities registered pursuant to Section 12(g) of the Act: **None**

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☒ No ☐

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ No ☒

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 ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

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

Large accelerated filer ☒ Accelerated filer ☐ Non-accelerated filer ☐ Smaller reporting company ☐

Indicate by check mark if the Registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes ☐ No ☒

The aggregate market value of the voting stock held by nonaffiliates of the Registrant, based upon the closing sale price of the Common Stock on June 30, 2007 as reported by the NASDAQ Global Market, was approximately \$1.1 billion. Shares of Common Stock held by each executive officer and director and by each

Source: PMC SIERRA INC, 10-K, February 22, 2008

person known to the Registrant who owns 5% or more of the outstanding voting stock have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

As of February 15, 2008, the Registrant had 218,380,467 shares of Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for Registrant's 2008 Annual Meeting of Stockholders are incorporated by reference into Part III of this Form 10-K Report.

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Item 1. Business

OVERVIEW

PMC-Sierra, Inc. (PMC or the Company) designs, develops, markets and supports communications semiconductors, storage semiconductors and system-on-chips primarily for the communications service provider, storage, and enterprise markets. We have approximately 350 different semiconductor devices that are sold to leading equipment and design manufacturers, who in turn supply their equipment principally to communications network service providers and enterprises. We provide superior semiconductor solutions for our customers by leveraging our intellectual property, design expertise and systems knowledge across a broad range of applications and industry protocols.

PMC-Sierra was incorporated in the State of California in 1983 and reincorporated in the State of Delaware in 1997. Our Common Stock trades on the NASDAQ Global Select Market under the symbol "PMCS".

Our principal executive offices are located at 3975 Freedom Circle, Santa Clara, California 95054, and our phone number is (408) 239-8000. Our internet webpage is located at www.pmc-sierra.com; however, the information in, or that can be accessed through, our webpage is not part of this report. Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to such reports are available, free of charge, on our webpage after we electronically file or furnish such material with the Securities and Exchange Commission, or SEC.

Our fiscal year normally ends on the last Sunday of the calendar year. Fiscal years 2007 and 2006 consisted of 52 weeks, and fiscal 2005 consisted of 53 weeks and ended on Saturday, December 31. In this Annual Report on Form 10-K, "PMC-Sierra", "PMC", "the Company", "us", "our" or "we", mean PMC-Sierra, Inc. together with our subsidiary companies.

FORWARD-LOOKING STATEMENTS

This Annual Report and the portions of our Proxy Statement incorporated by reference into this Annual Report contain forward-looking statements that involve risks and uncertainties. We use words such as "anticipates", "believes", "plans", "expects", "future", "intends", "may", "should", "estimates", "predicts", "potential", "continue", "becoming", "transitioning" and similar expressions to identify such forward-looking statements.

These forward-looking statements apply only as of the date of this Annual Report. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Our actual results could differ materially from those anticipated in these forward-looking statements for many reasons, including the risks we face as described under "Factors That You Should Consider Before Investing in PMC-Sierra" and elsewhere in this Annual Report and our other filings with the SEC. Investors are cautioned not to place undue reliance on these forward-looking statements, which reflect management's analysis only as of the date hereof. Such forward-looking statements include statements as to, among others:

- business strategy;
- sales, marketing and distribution;

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- wafer fabrication capacity;
- competition and pricing;
- critical accounting policies and estimates;
- customer product inventory levels, needs and order levels;
- demand for networking, storage and consumer equipment;
- net revenues;
- gross profit;
- research and development expenses;
- selling, general and administrative expenditures;
- interest and other income;
- foreign exchange rates;
- taxation rates;
- capital resources sufficiency;
- restructuring activities, expenses and associated annualized savings; and
- our business outlook.

We undertake no obligation to update the forward-looking statements in this Annual Report on Form 10-K. Accordingly, this Form 10-K should be read in conjunction with our periodic filings made with the SEC subsequent to the date of the original filing, including any amendments to those filings, as well as any Current Reports filed on Form 8-K subsequent to the date of the original filing.

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INDUSTRY OVERVIEW

Growth in Internet usage and digital consumer devices is continuing to drive demand for bandwidth and efficient networks that can manage these higher levels of data traffic. At the same time, communication service providers are seeking ways to increase their revenues by bundling and delivering a range of services to their customers in a cost-effective manner. Newer applications such as Voice Over Internet Protocol (VoIP), video-on-demand, Internet Protocol Television (IPTV), third generation wireless services, and network-attached storage are being deployed globally. This is resulting in increasing requirements for service providers and enterprises to upgrade and improve their network infrastructure and storage management capabilities. Enterprises, corporations, small offices and home offices are expanding their networks to better capture, store, and access large quantities of data efficiently and securely.

Different types of data transmitted at various speeds over the Internet require service providers and enterprises to invest in multi-service equipment that can aggregate and transport these varied types of network traffic. In simplified terms, Internet traffic moves over a series of distinct networks, with each network built using copper wires, coaxial cables or fiber optic cables. These networks carry high-speed traffic in the form of electrical and optical signals that are transmitted and received by complex networking equipment. To ensure this equipment and varied networks can communicate with each other, communications equipment manufacturers and makers of communications semiconductors have developed numerous communications standards and protocols for the industry. These communications and storage protocols make it easier for complex high-speed data traffic to be sent, received and stored reliably and efficiently — whether intra-office, across the country, or internationally. The products we sell, and the protocols used in development of our devices, are described below.

MARKETS THAT WE SERVE

We sell our semiconductor solutions primarily into five general areas of the worldwide network infrastructure, which we refer to as the Access, Metro, Enterprise Storage, Enterprise Networking, and Customer Premise markets. The products and solutions that we sell into the Metro and Access areas of the market are largely driven by the capital spending of service providers in the telecommunications industry. Our products and solutions that are sold into the Enterprise Storage, Enterprise Networking and Customer Premise areas are driven primarily by the capital spending of corporations, enterprises, and smaller businesses. In 2007 the mix of our revenues were derived approximately 50% from the telecommunications market and 50% from the enterprise and storage markets.

We acquired the Storage Semiconductor Business from Avago Technologies Inc. (“Avago”) in 2006. We purchased the Storage Semiconductor Business due to the market position it had in the Fibre Channel Controller market and the growth opportunities for standard semiconductor solutions in the enterprise storage market. Since the acquisition we have experienced the benefits from product synergies between the acquired business and PMC-Sierra’s storage disk interconnect integrated circuit (IC) business.

In 2006 we also purchased Passave, Inc., a company that develops system-on-chip semiconductor solutions for the Fiber-To-The-Home (FTTH) access market. We purchased Passave due to its market leadership in Passive Optical Networking (PON) solutions for central office and customer premise FTTH applications.

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The general market areas that we currently serve and some typical equipment in those markets that may contain our semiconductor solutions are described below. Due to the complexity of the telecommunications network, it is not possible to sharply delineate networking functions or markets served. In addition, many of our products may be used in multiple classes of networking equipment that are deployed across all of the market areas identified below, while some of our other products have highly specialized applications. For example, our microprocessors can be used in many networking equipment applications (such as color laser printers or high-speed routers), while a single wireless infrastructure chip may only be used in one specific application (e.g., pre-distortion of power amplification for a wireless base station). In some situations, different OEMs might use solutions in equipment addressing more than one of the market areas noted below. Further, during the lifecycle of their products, our customers may redesign their products and exclude our devices from the new design. We are not always aware when customers undertake such actions.

Access

The access area of the telecommunications network infrastructure encompasses both wired and wireless equipment that aggregates data traffic from homes and businesses and transmits it to the central offices in the metro and the wide area network (WAN). Our semiconductors are used in the access area of the network in equipment such as SONET/SDH multi-service provisioning platforms (which add and drop signals or streams of data from optical networks) and switches (which direct the data traffic to other destinations within the network). One key industry protocol that helps in packaging information into formats for transportation across various networks is the Internet Protocol (IP). As networks slowly converge over time, more data-centric and hybrid multi-service equipment is required to handle voice, video, and data services over the IP.

In Asia and some parts of North America, Passive Optical Networking (PON) is being deployed to facilitate a FTTH strategy. Instead of copper cables, fiber is deployed to the neighborhood, the multi-dwelling unit, or the residence, to increase bandwidth and reach in both uploading and downloading files in both directions. The two current industry standards related to PON are Ethernet Passive Optical Networking (EPON), which delivers bandwidth at a rate of 1 Gbps, and Gigabit Passive Optical Networking (GPON), which delivers bandwidth at a rate of 2.5 Gbps. The advantage of PON is that it provides high bandwidth without sensitivity to the distance between the central office and the subscriber.

The Access area of the network also involves the termination and distribution of separate higher speed data signals into lower speed data signals. Many of our networking devices used in wireline communications can be deployed in the transmission of wireless data traffic to the network in wireless base station transceivers. PMC-Sierra also recently introduced a wireless Radio Frequency (RF) device supporting a new protocol known as WiMax.

Metro

The metropolitan area of the telecommunications infrastructure is primarily a fiber optic-based network that provides high-speed communications and data transfer within a city center or regional area. This portion of the network manages traffic inside its own region, and also manages traffic between the access and long-haul transport networks for inter-city or international transmission. The Metro is made up of primarily routers, switches and optical transport equipment.

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For high-capacity data communication over fiber optic systems, the standard used is called SONET (for Synchronous Optical Network) in North America and parts of Asia, and called SDH (for Synchronous Digital Hierarchy) in the rest of the world. In addition to using SONET/SDH to increase the bandwidth, or capacity, of their networks, many service providers have also deployed equipment that uses an optical technology called dense wave division multiplexing. Rather than transmitting a single light signal over an optical fiber, dense wave division multiplexing allows many different light signals (each of a different wavelength) to be transmitted simultaneously. By deploying this technique at higher transmission rates, carriers can move more signals across transmission lines.

Our products and solutions are used in metro equipment such as multi-service switches and edge routers that gather and process signals in different protocols, and then transmit them to the next destination as quickly and efficiently as possible. The next-generation equipment in the metro portion of the network that can handle different data protocols is often referred to as multi-service provisioning platforms that facilitate the efficient transmission of internet protocol (IP) packets over optical fiber.

Enterprise Storage

Institutions and businesses connect to their data storage either directly or indirectly, the latter using network-attached systems (NAS) or storage area networks (SAN). Fibre Channel protocol, which is the standard for the transfer of information between computers and storage devices (hard disk drives), is the dominant standard in the storage area of the market, with the market transitioning from fibre channel operating at 2 Gbps to speeds of 4 and 8 Gbps. In addition, there is a shift occurring in storage networking from parallel to serial interconnections and two standards have emerged which are Serial-Attached SCSI (better known as SAS) and Serial ATA (SATA), both of which are being deployed in storage networks today. The SAS and SATA devices are operating at 3 Gbps today and devices are being introduced at 6 Gbps in this segment of the market. Another standard is called Internet Protocol SCSI (or iSCSI), but this has not yet gained broad acceptance and deployment.

Our products and solutions in this area enable the high-speed interconnection of the servers, switches and storage devices that comprise these systems so that large quantities of data can be stored, managed and moved securely. Our focus in this area is developing interconnect devices and controllers for Fibre Channel, SAS and SATA. We are also developing next-generation controllers for the server-attached storage systems.

Enterprise Networking

The enterprise area of the network includes equipment that is deployed primarily in the office for data communications and other local area network applications. Equipment such as switches and routers are used by both large and small businesses and enterprises to manage their data on an inter-office and intra-office basis. This market also includes office network equipment such as laser printers or multi-function printers, where we sell our standalone microprocessors and integrated SoCs or system-on-chip designs.

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OUR PRODUCTS

Most of our semiconductors can be divided into broadly defined functional categories identified below. As with descriptions of the network, particular categories may overlap and a device may be present in more than one category. In addition, some products may integrate several different functions and therefore could be classified in one or more categories. For example, some of our products convert high-speed analog signals to digital signals and split or combine various transmission signals.

Line interface units: these devices, also referred to as transceivers, transmit and receive signals over a physical medium such as wire, cable or fiber. The line interface unit determines the speed and timing characteristics of the signals, and may also convert them from a serial stream of data into a parallel stream before they are further processed for transmission to the next destination.

Framers and mappers: before the data can be sent to the next destination, it must be converted into a proper format for transmission in the network. For example, the framing function arranges the bits into different size formats, commonly referred to as “cell” or “packet” formats, and attaches the appropriate information to the formats to ensure they reach their destinations. In turn, this data may be inserted into other frames, such as SONET/SDH frames, for transmission across high-speed fiber optics.

Packet and cell processors: these devices examine the contents of cells, or packets, and perform various management and reporting functions. For instance, a switch or router may use a packet or cell processor to determine if a signal is voice or video in order to allocate the proper amount of bandwidth.

Controllers: rapid growth in data storage needs is driving a requirement for more cost-effective and larger capacity storage systems. Controller products based on Fibre Channel, SAS, and SATA, are enabling technologies for building network-attached storage system architectures that meet cost and capacity needs.

Microprocessor-based System-On-Chips (SOCs): these devices perform the high-speed computations that help identify and control the flow of signals and data in many different types of network equipment used in the communications, enterprise and consumer markets. With greater demand for integration of features and functions on a single device, more system-on-chip solutions are being developed.

Serializers/Deserializers: these devices convert networking traffic between slower speed parallel streams and higher speed serial streams. OEMs use serial streams to reduce networking equipment line connections, and parallel streams to allow them to apply lower cost traffic management technologies.

OUR STRATEGY

Our high-speed semiconductor solutions are based on our knowledge of network applications, system requirements and networking protocols, and high-speed mixed-signal and system-on-chip design expertise. To achieve our goal of profitably expanding our business, we are pursuing the following five strategies:

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1. Provide best-in-class products, customer service and technical support.

We work very closely with our customers to ensure they get the best service and technical support required to assist them with their product development efforts. We believe our largest customers and their products will take an increasing percentage of the overall market in their areas of expertise. End customers such as Alcatel/Lucent, Cisco, Dasan Networks, EMC, Hewlett Packard, Fujitsu, Hitachi, Huawei, LSI Corporation, Mitsubishi Electric, Nortel, Ricoh, and ZTE, are aligning their design and manufacturing operations with key suppliers such as PMC.

2. Expand our breadth of product solutions in the enterprise storage systems market.

We are broadening our product line in the enterprise storage markets. In addition to our Fibre Channel product line, we have leading edge high-performance interconnect devices designed on protocols such as SAS and SATA. We expect the need for faster and more complex devices based on these protocols to increase as next-generation storage systems are deployed. We offer controllers for server-attached storage systems for our OEM customers and we are working on a further integration of features and devices to increase performance and reduce cost.

3. Strengthen our overall position in the WAN of the telecommunications market and introduce solutions in the FTTH market as well as the Wireless Access market.

We are working very closely with large companies in the service provider and enterprise markets to help them design and develop standard semiconductor solutions that we anticipate will meet their performance requirements while lowering their costs. A significant number of our products are used by OEMs that sell network equipment to worldwide telecommunications service providers. We continue to focus our R&D on the growth segments including: last-mile access, metro optical transport, edge routing, wireless infrastructure (including WiMAX) and residential broadband gateways.

4. Continue to increase our presence in Asian markets.

We continue to strengthen our relationships and business activity with our Asian customers. In 2007, we expanded our presence in FTTH, which had been primarily in Japan, to include Korea and China. To support these customers, we have expanded our sales, service and design center in Shanghai, China and continue to expand our technology center in Bangalore, India. Our revenues continued to increase in the Asia Pacific region in 2007, which includes China and Japan. Some of our largest customers in the People's Republic of China were Huawei, ZTE, and Fiberhome, and in Japan our largest customers were Mitsubishi Electric, Fujitsu, Hitachi, and Ricoh. Our customers in Asia are broadening their product offerings in 3G wireless infrastructure, metro optical transport, edge routing, storage networking, laser and multi-function printers, and customer premise equipment.

5. Leverage our technical expertise across a diverse base of applications to pursue growth opportunities.

We have a strong history of analog, digital, mixed signal and microprocessor expertise and we are able to integrate many of these functions and protocols into complex devices. We leverage

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our common technologies and intellectual property across a broad range of networking equipment. Many OEMs recognize they can obtain highly complex, broadband communications technology from companies such as ours rather than dedicating their own resources to develop custom chips. We intend to take advantage of our customers' growing requirements to outsource more of the silicon content in their networking and storage equipment that allows the OEMs to reduce their development costs and improve time-to-market while differentiating their products in other ways. We constantly look for ways to enable new classes of services with the introduction of new technologies for our customers and carriers.

SALES, MARKETING AND DISTRIBUTION

Our sales and marketing strategy is to have our products designed into our customers' equipment by developing superb products for which we provide premium service and technical support. Our marketing team is focused on developing new products and solutions that meet the needs of our customers, including original equipment manufacturers and original design manufacturers. We are often involved in the early stages of design concerning our customers' plans for new equipment. This helps us determine if our existing products can be used in their new equipment or if new devices need to be created for the application. To assist us in our planning process, we are in regular contact with our key customers to discuss industry trends, emerging standards and ways in which we can assist in their new product requirements.

Our sales and marketing teams actively demonstrate our devices with other industry suppliers and provide technical information to our customers. Technical support is essential to our customers' success, and we provide this through field application engineers, technical marketing and systems engineers. We also provide more detailed information and support for our product line through our corporate website and special customer-accessible extranet sites. We believe that providing comprehensive product service and support is critical to shortening customers' design cycles and maintaining a competitive position in the markets that we serve.

Our sales team is focused on selling and supporting our chips and chipsets for equipment providers who are in turn selling their products to service providers, enterprises, or consumers. To better match our available sales resources to market opportunities we also focus our sales and support efforts on targeted customers.

We sell our products to end customers directly and through distributors and independent manufacturers' representatives. In 2007, approximately 27% of our orders were shipped through our distributors, approximately 46% were sent by us directly to contract manufacturers selected by OEMs, and the balance were sent directly to our OEM customers.

In 2007, our largest distributor was Avnet Inc., which represented our products worldwide (excluding Japan, Israel, and Taiwan). We recognize sales through Avnet on a sell-through basis, which occurs when Avnet ships our products to the end customer. In 2007, total sales shipped through Avnet worldwide were 19% of total revenues. Our second largest distributor is Macnica Inc. Sales shipped through this distributor in 2007 were approximately 11% of total revenues.

Our sales outside of the United States, based on customer billing location, accounted for 80% of total revenue in 2007, 76% in 2006, and 61% in 2005. Our sales to customers in Asia, including Japan and China, continued to increase in 2007 (65% of sales) from 2006 (57% of

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sales) in part because many of our OEM customers increased the use of Asia-based contract manufacturers for the assembly of their products. Sales to Cisco Systems and EMC Corporation through distributors, contract manufacturers and direct sales each represented more than 10% of our total revenues in 2007. Because we do business outside the United States, we are subject to risks related to changes in political and economic climate in the countries in which we operate. Please refer to the risk factor “Changes in the political and economic climate in the countries we do business in may adversely affect our operating results” set forth in Item 1A.

MANUFACTURING

PMC-Sierra is a fabless company, meaning that we do not own or operate foundries for the production of the silicon wafers from which our products are made. Instead, we work with independent merchant foundries and chip assemblers for the manufacture of our products. We believe our fabless approach to manufacturing provides us with the benefit of superior manufacturing capability, scalability, as well as the flexibility to move wafer manufacture, assembly and test of our products to the vendors that offer the best technology and service, at a competitive price.

Our lead-time, or the time required to manufacture our devices, is typically 10 to 14 weeks. Based on this lead-time, our team of production planners initiates purchase orders with our wafer suppliers and with our chip assemblers for the assembly and test of our parts so that, to the best of our ability, our products are available to meet customer demand.

Wafer Fabrication

We manufacture our products at independent foundries using standard Complementary Metal Oxide Semiconductor (CMOS) process techniques. We have in the past purchased substantially all of the silicon wafers from which we manufacture our products from Taiwan Semiconductor Manufacturing Corporation (TSMC), and Chartered Semiconductor Manufacturing Ltd. (Chartered). These independent foundries produce the wafers for our networking products at feature sizes down to 65 nanometer. By using independent foundries to fabricate our wafers, we are better able to concentrate our resources on designing, developing and testing of new products. In addition, we avoid the fixed costs associated with owning and operating fabrication and chip assembly facilities, and the costs associated with updating these facilities to manage constantly evolving process technologies.

We have supply agreements with both TSMC and Chartered that were renewed through December 30, 2008. PMC has a secured capacity agreement through deposits with one of its foundry partners, which ensures continuous supply during periods of tight capacity. Under these supply agreements, the foundries must supply certain quantities of wafers per year. Neither of these agreements have minimum unit volume requirements but we are obliged under one of the agreements to purchase a minimum percentage of our total annual wafer requirements provided that the foundry is able to continue to offer competitive technology, pricing, quality and delivery. These agreements may be terminated at any time if either party violates the terms of the agreements. We do not currently anticipate any problems in renewing these supply agreements beyond the current expiry dates.

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Assembly and Test

Once our wafers are fabricated, they must be probed, or inspected, to identify which individual units, referred to as die, were properly manufactured. Most wafers that we purchase are sent directly to an outside assembly house where the die are individually cut and packaged into semiconductor devices. The individual devices are then run through various electrical, mechanical and visual tests before customer delivery. PMC has recently outsourced the remaining in-house portion of its wafer probe and final test capability to several of its key subcontract test providers. With most of our products, we have the option to probe the wafers or test the final chips in-house or subcontract the probing or testing to independent subcontractors.

Quality Assurance

The industries that we serve require high quality, reliable semiconductors for incorporation into their equipment. We pre-qualify each vendor, foundry, assembly and test subcontractor. Wafers supplied by outside foundries must meet our incoming quality and test standards. We conduct a portion of our test operations on advanced mixed signal and digital test equipment in our Burnaby facility. The remainder of our testing is performed predominantly by independent Asian and U.S. companies.

Since 2006, there has been an increase in the proportion of products being produced for PMC by turnkey ASIC vendors due to the acquisitions. Although PMC does not physically manage the bulk of this production, these products follow approved and audited flows conforming to PMC's Quality Assurance requirements.

RESEARCH AND DEVELOPMENT

Our research and development efforts are market and customer-focused and can involve the development of both hardware and software. These devices and reference designs are targeted for use in enterprise, storage and service provider markets. Increasingly, our OEM customers that serve these end markets are demanding complete solutions with software support and complex feature sets and we are developing products to fill this need.

From time to time we announce new products to the public once development of the product is substantially completed, and there are no longer significant costs to be incurred. As we have a portfolio of more than 350 products, we do not consider any individual new product or group of products released in a year to be material, beyond our continuing development of a portfolio of products that meet our customers' future needs.

At the end of fiscal 2007, we had design centers in the United States (California, Oregon, and Pennsylvania), Canada (British Columbia and Quebec), Israel (Herzliya), China (Shanghai) and India (Bangalore).

Our research and development spending was \$159.1 million in 2007, \$158.7 million in 2006 and \$118.7 million in 2005. These figures exclude in-process research and development acquired in business combinations.

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BACKLOG

Our sales originate from customer purchase orders. However, our customers frequently revise order quantities and shipment schedules to reflect changes in their requirements. As of December 30, 2007, our backlog of products scheduled for shipment within three months totaled approximately \$95.5 million. Unless our customers cancel or defer to a subsequent year a portion of this backlog, we expect this entire backlog to be filled in 2008. Our backlog of products as of December 31, 2006 for shipment within three months totaled approximately \$75.3 million.

Our backlog includes our backlog of shipments to direct customers, minor distributors and a portion of shipments by our major distributor to end customers. Our customers may cancel or defer backlog orders. Accordingly, we believe that our backlog at any given time is not a meaningful indicator of future long-term revenues.

COMPETITION

We typically face competition at the customer design stage when our customers are determining which semiconductor components to use in their equipment designs.

Most of our customers choose a particular semiconductor component primarily based on whether the component:

- meets the functional requirements;
- interfaces easily with other components in the product;
- meets power usage requirements;
- is priced competitively; and
- is commercially available on a timely basis.

OEMs are becoming more price conscious as semiconductors sourced from third party suppliers start to comprise a larger portion of the total materials cost in OEM equipment. This price sensitivity from our customers can lead to aggressive price competition by competing suppliers that may force us to decrease our prices significantly to win a design and therefore decrease our gross profit.

OEMs also consider the quality of the supplier when determining which component to include in a design. Many of our customers will consider the breadth and depth of the supplier's technology, as using one supplier for a broad range of technologies can often simplify and accelerate the design of next generation equipment. OEMs will also consider a supplier's design execution reputation, as many OEMs design their next generation equipment concurrently with the semiconductor component design. OEMs also consider whether a supplier has been pre-qualified, as this ensures that components made by that supplier will meet the OEM's quality standards.

We compete against established peer-group semiconductor companies that focus on the communications and storage semiconductor business. These companies include Applied Micro Circuits, Broadcom, Conexant, Cortina, Emulex, Exar, Freescale, Infineon, LSI Logic, Marvell, Maxim, and Texas Instrument. Many of these companies are well financed, have significant communications semiconductor technology assets and established sales channels, and depend on the market in which we participate for the bulk of their revenues.

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Over the next few years, it is possible for additional competitors to enter the market with new products, some of which may also have greater financial and other resources than us.

We are also continuing to expand into certain markets, such as storage and wireless infrastructure that have established incumbents with substantial financial and other resources. Some of these incumbents derive a majority of their earnings from these markets. We expect continued strong competition in these markets.

LICENSES, PATENTS AND TRADEMARKS

We rely in part on patents to protect our intellectual property and have been awarded 242 U.S. and 78 foreign patents for circuit designs and other innovations used in the design and architecture of our products. In addition, we have 60 patent applications pending in the U.S. Patent and Trademark office. Our patents typically expire 20 years from the patent application date, with our existing patents expiring between 2010 and 2027.

We do not consider our business to be materially dependent upon any one patent. We believe that a strong portfolio of patents combined with other factors such as our ability to innovate, technological expertise and the experience of our personnel are important to compete effectively in our industry. Our patent portfolio also provides the flexibility to negotiate or cross license intellectual property with other semiconductor companies to broaden the features in our products.

We also rely on mask work protection, trademarks, copyrights, trade secret laws, employee and third-party nondisclosure agreements, and licensing arrangements to protect our intellectual property.

Our only material license is the MIPS microprocessor architecture license from MIPS Technologies Inc., on which our microprocessor-based products are based. While complex instruction set computing, or CISC architecture, is predominant in the desktop computer microprocessor market, several competing microprocessor architectures have emerged for other microprocessor markets such as the embedded computing market. Because of their higher performance and smaller space requirements, most of the competing architectures, such as the MIPS architecture, utilize reduced instruction set computing, or RISC architectures. The MIPS architecture is widely supported through semiconductor design software, operating systems and companion integrated circuits. Because this license supports the architecture behind our microprocessors, we must retain the MIPS license in order to produce our next generation microprocessor products. This license may be terminated only if we do not make the required royalty payments or breach confidentiality obligations.

PMC, PMCS, PMC-Sierra and our logo are our registered trademarks and service marks. We own other trademarks and service marks not appearing in this Annual Report. Any other trademarks used in this Annual Report are owned by other entities.

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EMPLOYEES

As of December 30, 2007, we had 1,027 employees, including 585 in Research and Development, 97 in Production and Quality Assurance, 214 in Sales and Marketing and 131 in Administration. Our employees are not represented by a collective bargaining agreement and we have never experienced any related work stoppage.

ITEM 1A. Risk Factors.

Our company is subject to a number of risks – some are normal to the fabless semiconductor industry, some are the same or similar to those disclosed in previous SEC filings, and some may be present in the future. You should carefully consider all of these risks and the other information in this report before investing in PMC. The fact that certain risks are endemic to the industry does not lessen the significance of the risk.

As a result of the following risks, our business, financial condition, operating results and/or liquidity could be materially adversely affected. This could cause the trading price of our securities to decline, and you may lose part or all of your investment.

We are subject to rapid changes in demand for our products due to:

- variations in our turns business;
- short order lead time;
- customer inventory levels;
- production schedules; and
- fluctuations in demand.

Our revenues and profits may fluctuate because of factors that are beyond our control. As a result, we may fail to meet the expectations of security analysts and investors, which could cause our stock price to decline.

Our ability to project revenues is limited because a significant portion of our quarterly revenues may be derived from orders placed and shipped in the same quarter, which we call our “turns business.” Our turns business varies widely from quarter to quarter. Our customers may delay product orders and reduce delivery lead-time expectations, which may reduce our ability to project revenues beyond the current quarter. While we regularly evaluate end users’ and contract manufacturers’ inventory levels of our products to assess the impact of their inventories on our projected turns business, we do not have complete information on their inventories. This could cause our projections of a quarter’s turns business to be inaccurate, leading to lower revenues than projected.

We may fail to meet our forecasts if our customers cancel or delay the purchase of our products or if we are unable to meet their demand.

We rely on customer forecasts in order to estimate the appropriate levels of inventory to build and to project our future revenues. Many of our customers have numerous product lines, numerous component requirements for each product, sizeable and complex supplier structures, and typically engage contract manufacturers for additional manufacturing capacity. This complex supply chain creates several variables that make it complicated to accurately forecast

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our customers' demand and accurately monitor their inventory levels of our products. If customer forecasts are not accurate, we may build too much inventory, potentially leaving us with excess and obsolete inventory, which would reduce our profit margins and adversely affect our operating results. Conversely, we may build too little inventory to meet customer demand causing us to miss revenue-generating opportunities.

Our customers often shift buying patterns as they manage inventory levels, market different products, or change production schedules. This makes forecasting their production requirements difficult and can lead to an inventory surplus or shortage of certain of their components. In addition, our products vary in terms of profit margins they generate. If our customers purchase a greater proportion of our lower margin parts in a particular period, it would adversely impact our results of operations.

Further, our distributors provide us with periodic reports of their backlog to end customers, sales to end customers and quantities of our products that they have on hand. If the data that is provided to us is inaccurate, it could lead to inaccurate forecasting of our revenues or errors in our reported revenues, gross profit and net income.

While backlog is our best estimate of our next quarter's revenues, it is industry practice to allow customers to cancel, change or defer orders with limited advance notice prior to shipment. As such, backlog may be an unreliable indicator of future revenue levels. Because a significant portion of our operating expenses are fixed, even a small revenue shortfall can have a disproportionately negative effect on our operating results.

If the demand for our customers' products declines, demand for our products will be similarly affected and our revenues, gross margins and operating performance will be adversely affected.

Our customers are subject to their own business cycles, most of which are unpredictable in commencement, depth and duration. We cannot accurately predict the continued demand of our customers' products and the demands of our customers for our products. In the past, networking customers have reduced capital spending without notice, adversely affecting our revenues. As a result of this uncertainty, our past operating results may not be indicative of our future operating results. It is possible that, in future periods, our results may be below the expectations of public market analysts and investors. This could cause the market price of our common stock to decline.

We rely on a few customers for a major portion of our sales, any one of which could materially impact our revenues should they change their ordering pattern. The loss of a key customer could materially impact our results of operations.

We depend on a limited number of customers for a major portion of our revenues. Through direct, distributor and subcontractor purchases, Cisco Systems and EMC Corporation each accounted for more than 10% of our revenues in 2007. We do not have long-term volume purchase commitments from any of our major customers. We sell our products solely on the basis of purchase orders. Those customers could decide to cease purchasing products with little or no notice and without significant penalties. A number of factors could cause our customers to cancel or defer orders, including interruptions to their operations due to a

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downturn in their industries, delays in manufacturing their own product offerings into which our products are incorporated, and natural disasters. Accordingly, our future operating results will continue to depend on the success of our largest customers and on our ability to sell existing and new products to these customers in significant quantities.

The loss of a key customer, or a reduction in our sales to any major customer or our inability to attract new significant customers could materially and adversely affect our business, financial condition or results of operations.

The loss of personnel could delay us from designing new products.

To succeed, we must retain and hire technical personnel highly skilled at the design and test functions needed to develop high-speed networking products. The competition for such employees is intense.

We do not have employment agreements in place with many of our key personnel. As employee incentives, we issue common stock options and restricted stock grants that are subject to time vesting, and, in the case of options, have exercise prices at the market value on the grant date. As our stock price varies substantially, the equity awards to employees are effective as retention incentives only if they have economic value.

Retirement of our Chief Executive Officer

In the fourth quarter of 2007, we announced that our Chief Executive Officer and President, Robert Bailey, intends to retire from the positions of President and Chief Executive Officer once his successor has been appointed. Mr. Bailey has been nominated to be re-elected as the Chairman of the Board of Directors at the upcoming 2008 Annual Stockholder Meeting. The Search Committee of Board of Directors is actively searching for a successor to Mr. Bailey. While we do not believe that our business has been adversely affected by the announcement of Mr. Bailey's retirement plans, it is important that we identify a successor to Mr. Bailey to mitigate any potential uncertainty in the market or the senior management team.

Changes in the political and economic climate in the countries we do business may adversely affect our operating results.

Our results of operations are increasingly dependent on our sales in China, which accounted for 20% of our revenues in 2007. Government agencies in China have broad discretion and authority over all aspects of the telecommunications and information technology industry in China; accordingly their decisions may impact our ability to do business in China. Therefore, significant changes in China's political and economic conditions and governmental policies could have a substantial impact on our business. The growth of FTTH technology in China has continued to be strong, however, a slowdown in that growth would have an adverse impact on our operating results.

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We earned a substantial portion of our FTTH revenues in Japan in 2007. We procure substantially all of our wafers from Taiwan and use assemblers throughout Asia.

Given the depth of our sales and operations in Asia, we face these additional risks that could negatively impact our results of operations, including economic sanctions imposed by the U.S. government, imposition of tariffs and other potential trade barriers or regulations, uncertain protection for intellectual property rights and generally longer receivable collection periods.

We are subject to the risks of conducting business outside North America, which may impair our sales, development or manufacturing of our products.

In addition to selling our products in a number of countries, an increasing portion of our research and development and manufacturing is conducted outside North America, in particular, India and China. The geographic diversity of our business operations could hinder our ability to coordinate design, manufacturing and sales activities. If we are unable to develop systems and communication processes to support our geographic diversity, we may suffer product development delays or strained customer relationships.

Hostilities in the Middle East may have a significant impact on our Israeli subsidiary's ability to conduct its business.

One of our research and development facilities is located in Israel, and employs approximately 176 people. On an on-going basis, some of our Israeli employees are periodically called into active military duty. In the event of severe hostilities breaking out, a significant number of our Israeli employees may be called into active military duty, resulting in delays, including product development schedules.

Our revenues may decline if we do not maintain a competitive portfolio of products.

We are experiencing significantly greater competition from many different market participants as the market in which we participate matures. In addition, we are expanding into markets, such as the wireless infrastructure, enterprise storage, customer premise equipment, and generic microprocessor markets, which have established incumbents with substantial financial and technological resources. We expect more intense competition than that which we have traditionally faced as some of these incumbents derive a majority of their earnings from these markets.

We typically face competition at the design stage, where customers evaluate alternative design approaches requiring integrated circuits. The markets for our products are intensely competitive and subject to rapid technological advancement in design tools, wafer manufacturing techniques, process tools and alternate networking technologies. We may not be able to develop new products at competitive pricing and performance levels. Even if we are able to do so, we may not complete a new product and introduce it to market in a timely manner. Our customers may substitute use of our products in their next generation equipment with those of current or future competitors, reducing our future revenues. With the shortening product life and design-in cycles in many of our customers' products, our competitors may have more opportunities to supplant our products in next generation systems.

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Our customers are increasingly price conscious, as semiconductors sourced from third party suppliers comprise a greater portion of the total materials cost in networking equipment. We continue to experience aggressive price competition from competitors that wish to enter into the market segments in which we participate. These circumstances may make some of our products less competitive, and we may be forced to decrease our prices significantly to win a design. We may lose design opportunities or may experience overall declines in gross margins as a result of increased price competition.

Over the next few years, we expect additional competitors, some of which may also have greater financial and other resources, to enter these markets with new products. These companies, individually or collectively, could represent future competition for many design wins, and subsequent product sales.

Design wins do not translate into near-term revenues and the timing of revenues from newly designed products is often uncertain.

From time to time, we announce new products and design wins for existing and new products. While some industry analysts may use design wins as a metric for future revenues, many design wins have not, and will not, generate any revenues for us, as customer projects are cancelled or unsuccessful in their end market. In the event a design win generates revenues, the amount of revenues will vary greatly from one design win to another. In addition, most revenue-generating design wins do not translate into near-term revenues. Most revenue-generating design wins take more than two years to generate meaningful revenues.

We may be unsuccessful in transitioning the design of our new products to new manufacturing processes.

Many of our new products are designed to take advantage of new manufacturing processes offering smaller device geometries as they become available, since smaller geometries can provide a product with improved features such as lower power requirements, increased performance, more functionality and lower cost. We believe that the transition of our products to, and introduction of new products using, smaller device geometries is critical for us to remain competitive. We could experience difficulties in migrating to future smaller device geometries or manufacturing processes, which would result in the delay of the production of our products. Our products may become obsolete during these delays, or allow competitors' parts to be chosen by customers during the design process.

Since many of the products we develop do not reach full production sales volumes for a number of years, we may incorrectly anticipate market demand and develop products that achieve little or no market acceptance.

Our products generally take between 12 and 24 months from initial conceptualization to development of a viable prototype, and another 3 to 18 months to be designed into our customers' equipment and sold in production quantities. We sell products whose

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characteristics include evolving industry standards, short product life spans and new manufacturing and design technologies. Our products often must be redesigned because manufacturing yields on prototypes are unacceptable or customers redefine their products to meet changing industry standards or customer specifications. As a result, we develop products many years before volume production and may inaccurately anticipate our customers' needs. Redesigning our products is expensive and may delay production of our products. Our products may become obsolete during these delays, resulting in our inability to recoup our initial investments in product development.

The final determination of our income tax liability may be materially different from our income tax provision.

We are subject to income taxes in both the United States and international jurisdictions. Significant judgment is required in determining our worldwide provision for income taxes. In the ordinary course of our business, there are many transactions where the ultimate tax determination is uncertain. Additionally our calculations of income taxes are based on our interpretations of applicable tax laws in the jurisdictions in which we file. Although we believe our tax estimates are reasonable, there is no assurance that the final determination of our income tax liability will not be materially different than what is reflected in our income tax provisions and accruals. Should additional taxes be assessed as a result of new legislation, an audit or litigation, if our effective tax rate should change as a result of changes in federal, international or state and local tax laws, or if we were to change the locations where we operate, there could be a material effect on our income tax provision and results of operations in the period or periods in which that determination is made, and potentially to future periods as well. For instance, we significantly increased our tax provision at the end of 2006 due to an increase in our estimated tax liability following receipt in 2007 of a written communication from a tax authority examining the historic transfer pricing policies and practices of certain companies within the PMC-Sierra group.

If foreign exchange rates fluctuate significantly, our profitability may decline.

We are exposed to foreign currency rate fluctuations because a significant part of our development, test, and selling and administrative costs are incurred in Canadian dollars, and our selling costs are incurred in a variety of currencies around the world. The U.S. dollar has devalued significantly compared to the Canadian dollar and this trend may continue. To protect against reductions in value and the volatility of future cash flows caused by changes in foreign exchange rates, we enter into foreign currency forward contracts. The contracts reduce, but do not eliminate, the impact of foreign currency exchange rate movements. In addition, this foreign currency risk management policy may not be effective in addressing long-term fluctuations since our contracts do not extend beyond a 12-month maturity.

We regularly limit our exposure to foreign exchange rate fluctuations from our foreign net asset or liability positions. Our accrual for income taxes is partially hedged against foreign exchange gains and losses, however, we recorded a net \$18.2 million foreign exchange loss on the revaluation of our tax liability because of the weakening of the U.S. dollar. Our profitability would be materially impacted by a 5% shift in the foreign exchange rates between U.S. and Canadian currencies.

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We are exposed to the credit risk of some of our customers.

Many of our customers employ contract manufacturers to produce their products and manage their inventories. Many of these contract manufacturers represent greater credit risk than our OEM customers, who do not guarantee our credit receivables related to their contract manufacturers.

In addition, a significant portion of our sales flows through our distribution channel, which generally represents a higher credit risk. Should these companies encounter financial difficulties, our revenues could decrease, and collection of our significant accounts receivables with these companies could be jeopardized.

Our business strategy contemplates acquisition of other products, technologies, or businesses, which could adversely affect our operating performance.

Acquiring products, intellectual property, technologies, or businesses from third parties is a core part of our business strategy. That strategy depends on the availability of suitable acquisition candidates at reasonable prices and our ability to resolve challenges associated with integrating acquired businesses into our existing business. These challenges include integration of product lines, sales forces, customer lists and manufacturing facilities, development of expertise outside our existing business, diversion of management time and resources, possible divestitures, inventory write-offs and other charges. We also may be forced to replace key personnel who may leave our Company as a result of an acquisition. We cannot be certain that we will find suitable acquisition candidates or that we will be able to meet these challenges successfully.

An acquisition could absorb substantial cash resources, require us to incur or assume debt obligations, or issue additional equity. If we are not able to obtain financing, then we may not be in a position to consummate acquisitions. If we issue equity securities in connection with an acquisition, we may dilute our common stock with securities that have an equal or a senior interest in our Company.

From time to time, we license, or acquire, technology from third parties to incorporate into our products. Incorporating technology into our products may be more costly or more difficult than expected, or require additional management attention to achieve the desired functionality. The complexity of our products could result in unforeseen or undetected defects or bugs, which could adversely affect the market acceptance of new products and damage our reputation with current or prospective customers.

Our current product road map will, in part, be dependent on successful acquisition and integration of intellectual property cores developed by third parties. If we experience difficulties in obtaining or integrating intellectual property from these third parties, it could delay or prevent the development of our products in the future.

Although our customers, our suppliers, and we rigorously test our products, our highly complex products may contain defects or bugs. We have in the past experienced, and may in

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the future experience, defects and bugs in our products. If any of our products contain defects or bugs, or have reliability, quality or compatibility problems that are significant to our customers, our reputation may be damaged and customers may be reluctant to buy our products. This could materially and adversely affect our ability to retain existing customers or attract new customers. In addition, these defects or bugs could interrupt or delay sales to our customers.

We may have to invest significant capital and other resources to alleviate problems with our products. If any of these problems are not found until after we have commenced commercial production of a new product, we may be required to incur additional development costs and product recall, repair or replacement costs. These problems may also result in claims against us by our customers or others. In addition, these problems may divert our technical and other resources from other development efforts. Moreover, we would likely lose, or experience a delay in, market acceptance of the affected product or products, and we could lose credibility with our current and prospective customers.

Our business may be adversely affected if our customers or suppliers cannot obtain sufficient supplies of other components needed in their product offerings to meet their production projections and target quantities.

Some of our products are used by customers in conjunction with a number of other components, such as transceivers, microcontrollers and digital signal processors. If, for any reason, our customers experience a shortage of any component, their ability to produce the forecasted quantity of their product offerings may be affected adversely and our product sales would decline until the shortage is remedied. Such a situation could harm our operating results, cash flow and financial condition.

We rely on limited sources of wafer fabrication, the loss of which could delay and limit our product shipments.

We do not own or operate a wafer fabrication facility. Two outside wafer foundries supply more than 95% of our semiconductor wafer requirements. Our wafer foundry suppliers also make products for other companies and some make products for themselves, thus we may not have access to adequate capacity or certain process technologies. We have less control over delivery schedules, manufacturing yields and costs than competitors with their own fabrication facilities. If the wafer foundries we use are unable or unwilling to manufacture our products in required volumes, or at specified times, we may have to identify and qualify acceptable additional or alternative foundries. This qualification process could take six months or longer. We may not find sufficient capacity quickly enough, if ever, at an acceptable cost, to satisfy our production requirements.

Some companies that supply our customers are similarly dependent on a limited number of suppliers to produce their products. These other companies' products may be designed into the same networking equipment into which our products are designed. Our order levels could be reduced materially if these companies are unable to access sufficient production capacity to produce in volumes demanded by our customers because our customers may be forced to slow down or halt production on the equipment into which our products are designed.

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We depend on third parties for assembly of our semiconductor products that could delay and limit our product shipments.

We depend on third parties in Asia for assembly of our semiconductor products. In addition, subcontractors in Asia assemble all of our semiconductor products into a variety of packages. Raw material shortages, political and social instability, assembly house service disruptions, currency fluctuations, or other circumstances in the region could force us to seek additional or alternative sources of supply or assembly. This could lead to supply constraints or product delivery delays that, in turn, may result in the loss of revenues. Capacity in the assembly industry has become scarce and lead times have lengthened. This could become more severe, which could in turn adversely affect our revenues. We have less control over delivery schedules, assembly processes, quality assurances, raw material supplies, and costs than competitors that do not outsource these tasks.

Due to the amount of time that it usually takes us to qualify assemblers and testers, we could experience significant delays in product shipments if we are required to find alternative assemblers or testers for our components. Any problems that we may encounter with the delivery, quality or cost of our products could damage our customer relationships and materially and adversely affect our results of operations. We are continuing to develop relationships with additional third-party subcontractors to assemble and test our products. However, even if we use these new subcontractors, we will continue to be subject to all of the risks described above.

Our business is vulnerable to interruption by earthquake, fire, power loss, telecommunications failure, terrorist activity and other events beyond our control.

We do not have sufficient business interruption insurance to compensate us for actual losses from interruption of our business that may occur, and any losses or damages incurred by us could have a material adverse effect on our business. We are vulnerable to a major earthquake and other calamities. We have operations in seismically active regions in California, and we rely on third-party wafer fabrication facilities in seismically active regions in Asia. We have not undertaken a systematic analysis of the potential consequences to our business and financial results from a major earthquake in either region. We are unable to predict the effects of any such event, but the effects could be seriously harmful to our business.

Our estimated restructuring accruals may not be adequate.

In 2005, 2006 and 2007, we implemented restructuring plans to streamline production and reduce and reallocate operating costs. In 2001 and 2003, we implemented plans to restructure our operations in response to the decline in demand for our networking products. We reduced the workforce and consolidated or shut down excess facilities in an effort to bring our expenses into line with our revenue expectations.

While management uses all available information to estimate these restructuring costs, particularly facilities costs, our estimated accruals may prove to be inadequate. If our actual sublease revenues or the results of our exiting negotiations differ from our assumptions, we may have to record additional charges, which could materially affect our results of operations, financial position and cash flow.

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From time to time, we become defendants in legal proceedings about which we are unable to assess our exposure and which could become significant liabilities upon judgment.

We become defendants in legal proceedings from time to time. Companies in our industry have been subject to claims related to patent infringement and product liability, as well as contract and personal claims. We may not be able to accurately assess the risk related to these suits, and we may be unable to accurately assess our level of exposure. These proceedings may result in material charges to our operating results in the future if our exposure is material and if our ability to assess our exposure becomes clearer.

If we cannot protect our proprietary technology, we may not be able to prevent competitors from copying or misappropriating our technology and selling similar products, which would harm our revenues.

To compete effectively, we must protect our intellectual property. We rely on a combination of patents, trademarks, copyrights, trade secret laws, confidentiality procedures and licensing arrangements to protect our intellectual property rights. We hold numerous patents and have a number of pending patent applications. However some of our patents are expiring in 2010, which could have a negative affect on our ability to prevent competitors from duplicating certain of our products.

We might not succeed in obtaining patents from any of our pending applications. Even if we are awarded patents, they may not provide any meaningful protection or commercial advantage to us, as they may not be of sufficient scope or strength, or may not be issued in all countries where our products can be sold. In addition, our competitors may be able to design around our patents.

To protect our product technology, documentation and other proprietary information, we enter into confidentiality agreements with our employees, customers, consultants and strategic partners. We require our employees to acknowledge their obligation maintain confidentiality with respect to PMC's products. Despite these efforts, we cannot guarantee that these parties will maintain confidentiality our proprietary information in the course of future employment or working with other business partners. We develop, manufacture and sell our products in Asia and other countries that may not protect our products or intellectual property rights to the same extent as the laws of the United States. This makes piracy of our technology and products more likely. Steps we take to protect our proprietary information may not be adequate to prevent theft of our technology. We may not be able to prevent our competitors from independently developing technologies that are similar to or better than ours.

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Our products employ technology that may infringe on the intellectual property and the proprietary rights of third parties, which may expose us to litigation and prevent us from selling our products.

Vigorous protection and pursuit of intellectual property rights or positions characterize the semiconductor industry. This often results in expensive and lengthy litigation. We, and our customers or suppliers, may be accused of infringing patents or other intellectual property rights owned by third parties in the future. An adverse result in any litigation could force us to pay substantial damages, stop manufacturing, using and selling the infringing products, spend significant resources to develop non-infringing technology, discontinue using certain processes or obtain licenses to the infringing technology. In addition, we may not be able to develop non-infringing technology, or find appropriate licenses on reasonable terms or at all.

Patent disputes in the semiconductor industry are often settled through cross-licensing arrangements. Our portfolio of patents may not have the breadth to enable us to settle an alleged patent infringement claim through a cross-licensing arrangement. We may therefore be more exposed to third party claims than some of our larger competitors and customers.

The majority of our customers are required to obtain licenses from and pay royalties to third parties for the sale of systems incorporating our semiconductor devices. Customers may also make claims against us with respect to infringement.

Furthermore, we may initiate claims or litigation against third parties for infringing our proprietary rights or to establish the validity of our proprietary rights. This could consume significant resources and divert the efforts of our technical and management personnel, regardless of the litigation's outcome.

Securities we issue to fund our operations could dilute your ownership.

We may decide to raise additional funds through public or private debt or equity financing. If we raise funds by issuing equity securities, the percentage ownership of current stockholders will be reduced and the new equity securities may have priority rights to your investment. We may not obtain sufficient financing on terms that are favorable to you or us. We may delay, limit or eliminate some or all of our proposed operations if adequate funds are not available.

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

We expect that the price of our common stock will continue to fluctuate significantly, as it has in the past. In particular, fluctuations in our stock price and our price-to-earnings multiple may have made our stock attractive to momentum, hedge or day-trading investors who often shift funds into and out of stocks rapidly, exacerbating price fluctuations in either direction particularly when viewed on a quarterly basis.

Securities class action litigation has often been instituted against a company following periods of volatility and decline in the market price of their securities. If instituted against us, regardless of the outcome, such litigation could result in substantial costs and diversion of our management's attention and resources and have a material adverse effect on our business, financial condition and operating results. In addition, we could incur substantial punitive and other damages relating to such litigation.

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Provisions in Delaware law, our charter documents and our stockholder rights plan may delay or prevent another entity from acquiring us without the consent of our Board of Directors.

We adopted a stockholder rights plan in 2001, pursuant to which we declared a dividend of one share purchase right for each outstanding share of common stock. If certain events occur, including if an investor tenders for or acquires more than 15% of our outstanding common stock, stockholders (other than the acquirer) may exercise their rights and receive \$650 worth of our common stock in exchange for \$325 per right, or we may, at our option, issue one share of common stock in exchange for each right, or we may redeem the rights for \$0.001 per right. The issuance of the rights could have the effect of delaying or preventing a change in control of us.

In addition, our Board of Directors has the right to issue preferred stock without stockholder approval, which could be used to dilute the stock ownership of a potential hostile acquirer. Delaware law imposes some restrictions on mergers and other business combinations between us and any holder of 15% or more of our outstanding common stock.

Although we believe these provisions of our charter documents, Delaware law and our stockholder rights plan will provide for an opportunity to receive a higher bid by requiring potential acquirers to negotiate with our Board of Directors, these provisions apply even if the offer may be considered beneficial by some stockholders.

ITEM 2. Properties.

PMC leases properties in 23 locations worldwide. Approximately 35% of the space leased by PMC was excess at December 30, 2007. Approximately 63% of the excess space has been subleased and we are actively pursuing opportunities to sublease or negotiate our exit from the remaining excess facilities.

We lease a total of 108,000 square feet in Santa Clara, California, to house our US design, engineering, sales and marketing operations. In 2007, we vacated approximately 12,500 additional square feet of office space Santa Clara in connection with our workforce reduction activities.

Our Canadian operations are located in Burnaby, British Columbia where we lease 173,000 square feet of office space in three separate buildings. These locations support a significant portion of our product development, manufacturing, marketing, sales and testing activities. In mid 2007, we vacated approximately 45,250 square feet in Burnaby, British Columbia, Saskatoon, Saskatchewan, Winnipeg, Manitoba and Montreal, Quebec in connection with operational consolidation activities.

In addition to the two major sites in Santa Clara and Burnaby, during 2007 we also operated seven additional research and development centers: one in Canada, three in the US, one in Bangalore, India, one in Herzliya, Israel and one in Shanghai, China.

We have fourteen sales/operations offices located in Europe, Asia, the Middle East and North America.

ITEM 3. Legal Proceedings.

Stockholder Derivative Lawsuits

Three derivative actions have been filed against the Company, as a nominal defendant, and various current and former officers and/or directors: (1) *Meissner v. Bailey, et al.*, Santa Clara Superior Court Case No. 1-06-CV-071329 (filed September 18, 2006); (2) *Beiser v. Bailey, et al.*, United States District Court for the Northern District of California Case No. 5:06-CV-05330-RS (filed August 29, 2006); and (3) *Barone v. Bailey, et al.*, United States District Court for the Northern District of California Case No. 4:06-CV-06473-SBA (filed October 16, 2006). On November 21, 2006, the Beiser and Barone actions were consolidated into one case. On January 18, 2007, the Santa Clara County Superior Court in California ordered that the Meissner action be stayed pending the outcome of the consolidated, federal Beiser/Baron action. A consolidated complaint in the Beiser/Baron action was filed on January 29, 2007 (the "Consolidated Complaint").

The Consolidated Complaint generally alleged that various current and former Company directors and/or officers breached their duty of loyalty and/or duty of care to the Company and its shareholders, that these purported breaches of fiduciary duties caused harm to the Company and the plaintiffs seek to recover damages on behalf of the Company. The Consolidated Complaint also alleged violations of federal securities laws. The Company is a nominal defendant in the cases, but any recovery in the litigation would be paid to the Company, rather than to its shareholders. The defendants have entered into joint defense arrangements.

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On March 15, 2007, the Company filed three separate motions aimed at having the federal lawsuit dismissed on various legal grounds. One of these motions was on the basis that plaintiffs failed to plead with particularity facts establishing that a litigation demand on the board of directors of the Company would have been futile at the time they commenced the derivative lawsuit. On June 20, 2007, the Court heard the motion to dismiss plaintiffs' complaint for failure to plead demand futility with particularity. The Court ruled on the motion to dismiss on August 22, 2007 finding that the plaintiffs' Consolidated Complaint had not met the pleading burden and gave plaintiffs leave to amend. The plaintiffs filed their Amended Consolidated Complaint on October 2, 2007. While the plaintiffs' claims are substantially similar, they have reduced the scope of their allegations. The Company filed motions to dismiss the Amended Consolidated Complaint consistent with its previous motions which were argued before the Court on January 30, 2008. The Court also took argument on a motion to compel the production of certain documents filed by the plaintiffs December 26, 2007. The Court has not yet ruled on the motions.

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

None.

ITEM 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

Stock Price Information. Our Common Stock trades on the NASDAQ Global Select Market under the symbol PMCS. The following table sets forth, for the periods indicated, the high and low closing sale prices for our Common Stock as reported by the NASDAQ Global Select Market:

Fiscal 2007	High	Low
First Quarter	\$ 7.40	\$ 6.11
Second Quarter	8.15	6.94
Third Quarter	8.54	7.13
Fourth Quarter	9.75	6.54
Fiscal 2006	High	Low
First Quarter	\$ 12.45	\$ 7.97
Second Quarter	13.57	8.55
Third Quarter	9.25	4.86
Fourth Quarter	7.96	5.92

Stockholders

To maintain consistency, the information provided above is based on the last day of the calendar quarter rather than the last day of the fiscal quarter. As of February 15, 2008 there were 1,039 holders of record of our Common Stock. On February 15, 2008, the last reported sales price of our common stock was \$4.58 per share.

Dividends

We have never paid cash dividends on our Common Stock. We currently intend to retain earnings, if any, for use in our business or to fund acquisitions and do not anticipate paying any cash dividends in the foreseeable future.

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Stock Performance Graph

The following graph shows a comparison of cumulative total stockholder returns for PMC, the line-of-business index for semiconductors and related devices (SIC code 3674) furnished by Georgeson Shareholder Communications Inc., and the S&P 500 Index. The graph assumes the investment of \$100 on December 31, 2002. The performance shown is not necessarily indicative of future performance.

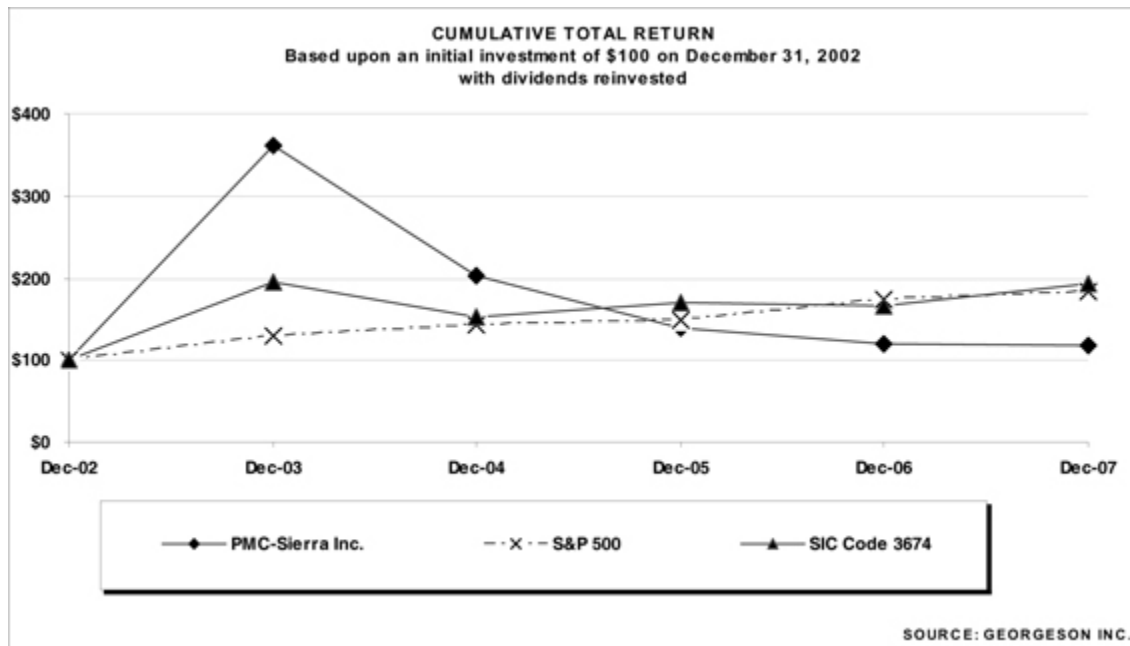


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ITEM 6. Selected Financial Data

The following tables set forth data from our consolidated financial statements for each of our last five fiscal years.

	Year Ended (in thousands, except for per share data)				
	December 30, 2007 ⁽¹⁾	December 31, 2006 ⁽²⁾	December 31, 2005 ⁽³⁾	December 26, 2004 ⁽⁴⁾	December 28, 2003 ⁽⁵⁾
STATEMENT OF OPERATIONS DATA:					
Net revenues	\$ 449,381	\$ 424,992	\$ 291,411	\$ 297,383	\$ 249,483
Cost of revenues	158,297	146,456	80,963	87,542	87,875
Gross profit	291,084	278,536	210,448	209,841	161,608
Research and development	159,134	158,661	118,720	120,492	119,790
Selling, general and administrative	100,486	102,363	56,278	46,832	46,665
Amortization of purchased intangible assets	39,343	33,381	—	—	—
In-process research and development	—	35,300	—	—	—
Restructuring costs and other charges	14,837	6,119	13,833	3,520	15,314
Acquisition costs	—	—	—	1,212	—
(Loss) income from operations	(22,716)	(57,288)	21,617	37,785	(20,161)
Interest income, net	9,914	8,979	12,106	4,859	1,709
Foreign exchange loss	(18,486)	(109)	(3,259)	(1,295)	(954)
(Loss) gain on extinguishment of debt and amortization of debt issue costs	(968)	(968)	(1,809)	(2,233)	287
(Loss) gain on investments	—	(1,269)	1,439	9,242	2,416
(Provision for) recovery of income taxes	(16,848)	(49,237)	(2,108)	3,323	8,712
Net (loss) income	\$ (49,104)	\$ (99,892)	\$ 27,986	\$ 51,681	\$ (7,991)
Net income (loss) per share—basic:	\$ (0.23)	\$ (0.49)	\$ 0.15	\$ 0.29	\$ (0.05)
Net income (loss) per share—diluted:	\$ (0.23)	\$ (0.49)	\$ 0.15	\$ 0.27	\$ (0.05)
Shares used in per share calculation—basic	216,330	203,470	184,098	180,353	173,568
Shares used in per share calculation—diluted	216,330	203,470	189,132	188,903	173,568

	(in thousands)									
BALANCE SHEET DATA:										
Working capital	\$	280,575	\$	192,146	\$	565,501	\$	152,306	\$	317,444
Cash, cash equivalents, and short-term investments		364,922		258,914		627,476		274,686		411,928
Long-term investment in bonds and notes		—		—		—		139,111		41,569
Total assets		1,131,998		1,006,557		732,949		507,024		552,956
Long-term debt (including current portion)		225,000		225,000		225,000		68,071		175,000
Stockholders' equity		595,996		570,428		354,047		299,337		226,297

- Results for the year ended December 30, 2007 include \$1.7 million stock-based compensation expense included in Cost of revenues; \$16.6 million stock-based compensation expense included in Research and development expenses; \$17.1 million stock-based compensation expense and \$2.2 million reversal of an accrual for payroll-related taxes, included in Selling, general and administrative expenses; \$14.8 million restructuring costs; \$18.2 million foreign exchange loss on an income tax liability; \$4.0 million recovery of prior years' income taxes, and \$3.8 million recovery of future income taxes, offset by \$13.1 million of interest relating to the liability for unrecognized tax benefit of prior years.
- Results for the year ended December 31, 2006 include \$8.2 million purchase accounting adjustments to inventory, \$1.8 million stock-based compensation expense, and \$0.8 million in additional contractor costs included in Cost of revenues; \$16.2 million stock-based compensation expense included in Research and development expenses; \$19.9 million stock-based compensation expense, \$2.4 million for employee-related taxes, and \$0.2 million acquisition-related relocation expenses included in Selling, general and administrative expenses; \$6.1 million restructuring costs; a \$0.5 million foreign exchange gain on an income tax liability; \$29.9 million increase in our estimated tax provision for previous years as a result of a written communication received in 2007 from a tax authority and \$7.0 million withholding and other taxes on repatriation of funds included in the provision for income taxes.

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- (3) Results for the year ended December 31, 2005 include \$0.9 million reversal of provision for doubtful accounts receivable included in Selling, general and administrative expenses, \$13.8 million restructuring costs; \$6.3 million tax benefits comprised of \$5.3 million excess R&D tax credits and \$1.0 million recovery of prior year sales tax, and \$3.4 million foreign exchange loss on an income tax liability.
- (4) Results for the year ended December 26, 2004 include \$3.5 million net charge for additional excess facilities costs related to our 2001 restructurings, \$1.3 million elimination of a provision for employee-related taxes included in Selling, general and administrative expenses, \$9.2 million gain on sale of investments, \$5.1 million recovery of prior year taxes, \$9.4 million tax recovery based on agreements and assessments with a tax authority and \$1.5 million foreign exchange loss on an income tax liability.
- (5) Results for the year ended December 28, 2003 include a \$15.3 million net charge for restructuring costs comprised of \$7.2 million for workforce reduction, \$11.9 million for excess facilities, \$1.4 for asset impairments, \$4.5 million reversal of excess facilities costs related to our October 2001 restructuring and \$0.7 million reversal of excess workforce reduction costs related to our January 2003 restructuring plan, the \$1.8 million elimination of a provision for potential litigation costs included in Selling, general and administrative expenses, and a \$3.5 million receipt of prior year income taxes.

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Quarterly Comparisons

The following tables set forth the consolidated statements of operations for each of our last eight quarters. This quarterly information is derived from unaudited interim financial statements and has been prepared on the same basis as the annual Consolidated Financial Statements. In management's opinion, this quarterly information reflects all adjustments necessary for fair presentation of the information for the periods presented. The operating results for any quarter are not necessarily indicative of results for any future period.

	Quarterly Data (in thousands except for per share data)							
	Year Ended December 30, 2007				Year Ended December 31, 2006			
	Fourth ⁽¹⁾	Third ⁽²⁾	Second ⁽³⁾	First ⁽⁴⁾	Fourth ⁽⁵⁾	Third ⁽⁶⁾	Second ⁽⁷⁾	First ⁽⁸⁾
STATEMENT OF OPERATIONS DATA:								
Net revenues	\$ 123,569	\$ 117,455	\$ 104,692	\$ 103,665	\$ 101,917	\$ 116,514	\$ 118,780	\$ 87,781
Cost of revenues	43,205	39,871	37,650	37,571	37,125	39,146	43,560	26,625
Gross profit	80,364	77,584	67,042	66,094	64,792	77,368	75,220	61,156
Research and development	37,418	35,557	41,635	44,524	41,713	41,611	41,587	33,749
Selling, general and administrative	24,493	24,124	25,171	26,698	26,362	29,235	27,174	19,593
Amortization of purchased intangible assets	9,836	9,836	9,836	9,835	10,136	11,202	9,934	2,110
In-process research and development	—	—	—	—	—	—	20,500	14,800
Restructuring costs and other charges	2,593	1,564	3,786	6,894	453	6,404	—	(738)
Income (loss) from operations	6,024	6,503	(13,386)	(21,857)	(13,872)	(11,084)	(23,975)	(8,358)
Interest income, net	2,877	2,728	2,472	1,837	2,297	1,849	1,267	3,566
Foreign exchange (loss) gain	(2,511)	(7,052)	(7,926)	(996)	3,508	(252)	(3,378)	13
Amortization of debt issue costs	(242)	(242)	(242)	(242)	(242)	(242)	(242)	(242)
(Loss) gain on investments	—	—	—	—	—	—	(3,118)	1,849
(Provision for) recovery of income taxes	(11,229)	(7,877)	(3,177)	5,435	(33,891)	(1,796)	(2,388)	(11,161)
Net (loss)	<u>\$ (5,081)</u>	<u>\$ (5,940)</u>	<u>\$ (22,259)</u>	<u>\$ (15,823)</u>	<u>\$ (42,200)</u>	<u>\$ (11,525)</u>	<u>\$ (31,834)</u>	<u>\$ (14,333)</u>
Net income (loss) per share—basic	\$ (0.02)	\$ (0.03)	\$ (0.10)	\$ (0.07)	\$ (0.20)	\$ (0.05)	\$ (0.16)	\$ (0.08)
Net income (loss) per share—diluted	\$ (0.02)	\$ (0.03)	\$ (0.10)	\$ (0.07)	\$ (0.20)	\$ (0.05)	\$ (0.16)	\$ (0.08)
Shares used in per share calculation—basic	218,912	216,837	215,688	213,881	212,295	211,298	203,067	187,218
Shares used in per share calculation—diluted	218,912	216,837	215,688	213,881	212,295	211,298	203,067	187,218

- (1) Results include \$0.3 million stock-based compensation expense included in Cost of revenues, \$4.1 million stock-based compensation expense included in Research and development expenses, \$3.7 million stock-based compensation expense included in Selling, general and administrative expenses, \$2.1 million foreign exchange loss on our income tax liability, and \$4.1 million of interest relating to the liability for unrecognized tax benefit of prior years.
- (2) Results include \$0.3 million stock-based compensation expense included in Cost of revenues, \$3.8 million stock-based compensation expense included in Research and development expenses, \$4.0 million stock-based compensation expense and \$1.2 million employee-related taxes included in Selling, general and administrative expenses, and \$6.8 million foreign exchange loss on our income tax liability.
- (3) Results include \$0.5 million stock-based compensation expense included in Cost of revenues, \$4.4 million stock-based compensation expense included in Research and development expenses, \$4.7 million stock-based compensation expense and \$2.2 million reversal of a payroll tax accrual in a foreign jurisdiction included in Selling, general and administrative expenses and \$8.3 million foreign exchange loss on our income tax liability.
- (4) Results include \$0.5 million stock-based compensation expense included in Cost of revenues; \$4.3 million stock-based compensation expense included in Research and Development expenses; \$4.6 million stock-based compensation expense included in Selling, General and administrative expenses; \$1.0 million foreign exchange loss on our income tax liability; and \$4.0 million tax recovery relating to prior years.
- (5) Results include \$0.5 million stock-based compensation expense included in Cost of revenues, \$5.5 million stock-based compensation expense included in Research and development expenses, \$5.4 million stock-based compensation expense included in Selling, general and administrative expenses, \$3.5 million foreign exchange gain on our income tax liability, and \$29.9 million increase in our estimated tax provision for previous years as a result of a written communication received in 2007 from a tax authority.
- (6) Results include \$0.4 million stock-based compensation expense included in Cost of revenues, \$4.2 million stock-based compensation expense included in Research and development expenses, \$6.0 million stock-based compensation expense and \$2.4 million employee-related taxes included in Selling, general and administrative expenses, and \$0.1 million foreign exchange gain on our income tax liability.

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- (7) Results include \$5.4 million purchase accounting adjustments to inventory and \$0.5 million stock-based compensation expense included in Cost of revenues, \$4.0 million stock-based compensation expense included in Research and development expenses, \$5.5 million stock-based compensation expense included in Selling, general and administrative expenses and \$3.3 million foreign exchange loss on Canadian taxes.
- (8) Results include \$2.8 million purchase accounting adjustments to inventory, \$0.5 million in additional contractor costs, and \$0.4 million stock-based compensation expense included in Cost of revenues; \$2.5 million stock-based compensation expense included in Research and Development expenses; \$3.0 million stock-based compensation expense and \$0.2 million relocation expenses included in Selling, General and administrative expenses; \$0.1 million foreign exchange gain on Canadian taxes; and \$7.0 million withholding and other taxes on repatriation of funds.

ITEM 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion of the financial condition and results of our operations should be read in conjunction with the Consolidated Financial Statements and notes thereto included elsewhere in this Annual Report.

OVERVIEW

We generate revenues from the sale of semiconductor devices and solutions that we have acquired, designed and developed. Almost all of our revenues in any given year come from the sale of semiconductors that are developed prior to that year. For example, the majority of our revenues in 2007 came from products that were acquired through business combinations in 2006 or developed in 2005 and earlier. After an individual product is completed and announced it may take several years before that device generates any significant revenues. Our products' success is dependent on the market acceptance of our customers' products into which our products are designed. Our current revenue is generated by a portfolio of approximately 350 products.

In addition to incurring costs for the marketing, sales and administration of selling existing products, we expend a substantial amount every year for the development of new semiconductor devices. We determine the amount to invest in the development of new semiconductors based on our assessment of the future market opportunities for those components, and the estimated return on investment. To compete globally we must invest in the businesses and technologies that are both growing in demand and cost competitive in the geographic markets that we serve. We continue to aggressively focus on cost reduction and finding ways to improve on operational efficiencies.

We are benefiting from the acquisitions that we completed in 2006. We are experiencing product synergies between the Fibre Channel controllers acquired from the Storage Semiconductor Business we acquired from Avago in 2006 and our Fibre Channel and SAS disk-interconnect products. We have introduced 8 gigabit Fibre Channel Controller products into the market, which improve data access times that have been made more challenging by data consolidation through virtualization and fixed content storage. These products are backward compatible with our 4 Gbps Fibre Channel products, allowing our customers to preserve their software investments.

We will continue to expand our FTTH product offerings for the Asian market in the coming year. Our largest end market for EPON solutions is Japan which is the worldwide leader in FTTH deployment. In China, our EPON products are gaining traction in the marketplace due to the maturity and stability of this technology. We expect revenue growth in our FTTH business in

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China as the technology gains acceptance in this market. In Korea, the government is expected to complete the regulatory policy for IPTV in 2008, and select IPTV service providers which will result in resumption in EPON FTTH deployments in Korea in the second half of the year.

We are also offering customers a multi-service fiber access gateway solution with an integrated GPON interface. This product will enable carriers to expand high definition video offerings to consumers through mass deployment of higher bandwidth application such as video picture sharing, peer-to-peer and data storage.

We are closely aligning with leading OEM customers who supply carriers who are investing in their networks to enable delivery of residential video services. We are well positioned for these network upgrade opportunities with solutions that have high data throughput and require lower power for our customers. Our current business strategy also includes broadening our semiconductor solutions into the WiMax market.

With regard to our communications business, we continue to see the convergence of networks and build-outs driving service provider requirements and large contracts for metro-optical transport and access equipment. We are seeing growth in demand for our access products as service providers expand their wired and wireless networks around the world.

We expect our SOC solutions to continue to penetrate the laser printer market as well as the network-attached storage market for small to medium sized businesses. We will also continue to pursue ASIC design wins with our leading OEM customers in this market.

On January 1, 2007, we adopted FIN48 resulting in a net decrease in a \$4.7 million in our accumulated deficit, a decrease in our unrecognized tax benefit and a \$1.1 million increase to the deferred tax asset. See Note 14 for further information on Income Taxes. During the year, our liability for unrecognized tax benefits increased significantly due to the accrual of additional taxes, related interest expense and foreign exchange revaluation related to this liability. See Note 14 to the Consolidated Financial statements for further information about our FIN48 liability. The adoption of FIN48 will continue to have an adverse impact on our results of operations in future periods.

In the fourth quarter of 2007, we announced that our Chief Executive Officer and President, Robert L. Bailey, will be retiring from the positions of President and Chief Executive Officer once his successor has been appointed. Mr. Bailey has been nominated to be re-elected as the Chairman of the Board at the upcoming 2008 Annual Stockholder Meeting. The Search Committee of the Board of Directors is actively searching for a successor to Mr. Bailey.

In order to align our fiscal year end with the calendar year end, fiscal 2005 consisted of 53 weeks compared to 52 weeks in fiscal 2007 and fiscal 2006.

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Net Revenues (\$ millions)

	<u>2007</u>	<u>Change</u>	<u>2006</u>	<u>Change</u>	<u>2005</u>
Net revenues	\$ 449.4	6%	\$ 425.0	46%	\$ 291.4

Net revenues for 2007 increased \$24.4 million, or 6% compared to net revenues for 2006. In 2007, the products we acquired from Passave and the Storage Semiconductor Business from Avago contributed an incremental \$18.2 million to our net revenues due to full versus partial year of revenues in 2006. However, there was a year over year decrease in revenues from the acquired Storage Semiconductor Business as certain products reached their end of life. We had growth in our printer business and organic storage business of \$8.8 million and \$21.8 million, respectively, partially offset by declines in revenues from our telecommunications products of \$24.4 million.

Net revenues for 2006 increased \$133.6 million, or 46% compared to net revenues for 2005. The increase was driven by \$95.7 million of additional revenue from the acquisition of the Storage Semiconductor Business from Avago and \$30.7 million of additional revenue from the acquisition of Passave. Apart from revenues from the acquisitions, in 2006 our revenues were \$7.2 million higher than in 2005. Despite the overall increase for the year, in the second half of 2006 revenues declined sequentially due to lower activity in the telecommunications market. This was caused by a slowdown in equipment orders by carriers in China, Japan, and North America, in addition to an electronics components supply chain inventory correction primarily in Japan and North America, and US carrier and communications OEM mergers.

Over the past three years, we have seen significant growth in net revenues generated in Asia. Net revenues from Asia were 65% of total net revenues in 2007, 57% of total net revenues in 2006, and 50% in 2005. We attribute this trend primarily to our increasing presence in the Fiber-to-the-home market, which is concentrated in Japan, Korea, China and Taiwan, and increased manufacturing outsourcing into Asia by our OEM customers.

Gross Profit (\$ millions)

	<u>2007</u>	<u>Change</u>	<u>2006</u>	<u>Change</u>	<u>2005</u>
Gross profit	\$ 291.1	5%	\$ 278.5	32%	\$ 210.4
<i>Percentage of net revenues</i>	65%		66%		72%

Total gross profit for 2007 increased by \$12.6 million over gross profit in 2006. The acquisitions we completed in 2006 and growth in sales of our microprocessor and organic storage products had positive impacts on our gross profit, partially offset by the impact of declines in sales of our telecommunications products on gross profit.

The most significant items impacting our gross margin as a percentage of net revenues were:

- a change in product mix away from our telecommunications products toward our storage, FTTH and SOC products, which decreased gross margin by 2%;

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- in 2006, we sold inventory acquired from the Storage Semiconductor Business of Avago that was valued at its selling price, less related selling costs, as opposed to the lower manufacturing cost; there was no such expense incurred in 2007 and our gross margin increased by 2% compared to 2006; and
- the combined impact of increased obsolescence provision and royalty expense decreased gross margin by 1%.

Total gross profit for 2006 increased by \$68.1 million over gross profit in 2005. Gross profits increased in 2006 due to higher sales volumes, primarily resulting from the acquisitions. In 2005, gross profit improved due in part to the centralizing of our manufacturing logistics teams into a single location through our restructuring activities, as well as tightly managing our manufacturing costs.

Gross profit as a percentage of revenues decreased to 66% in 2006 from 72% in 2005 primarily as a result of the following factors:

- the acquisitions changed the overall mix of revenues, decreasing gross profit as a percentage of revenues by 3%;
- lower margins on our existing products decreased gross profit as a percentage of revenues by 1%; and
- we recorded \$4.2 million higher provisions for excess and obsolete inventory, which decreased gross profit as a percentage of net revenues by 1%.

Other Costs and Expenses (\$ millions)

	<u>2007</u>	<u>Change</u>	<u>2006</u>	<u>Change</u>	<u>2005</u>
Research and development	\$ 159.1	—	\$ 158.7	34%	\$ 118.7
Percentage of net revenues	35%		37%		41%
Selling, general and administrative	\$ 100.5	(2)%	\$ 102.4	82%	\$ 56.3
Percentage of net revenues	22%		24%		19%
Amortization of purchased intangible assets	\$ 39.3	18%	\$ 33.4	100%	—
Percentage of net revenues	9%		8%		—
In-process research and development	—	(100)%	\$ 35.3	100%	—
Percentage of net revenues	—		8%		—
Restructuring costs	\$ 14.8	143%	\$ 6.1	(56)%	\$ 13.8
Percentage of net revenues	3%		1%		5%

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Research and Development Expenses

Our research and development, or R&D, expenses were flat in 2007 compared to 2006. Payroll costs increased by approximately \$0.3 million due to an increase in stock based compensation expense. Office and facilities costs increased by \$0.8 million due to supporting our Israel R&D facility for a full year in 2007 compared to seven months in 2006, and operating our Shanghai R&D facility that opened in 2007. These increases were partially offset by \$0.6 million in material costs.

Our R&D expenses were \$40 million, or 34%, higher in 2006 compared to 2005. Total payroll costs, including the acquired businesses, were higher by \$16.1 million due to salary increases, and additional headcount from Passave and the Storage Semiconductor Business for 2006, which were partially offset by savings from our workforce reduction initiatives. In addition, we recorded \$16.2 million stock-based compensation expense compared to none in 2005. Material costs were higher by \$6.1 million, office and facilities costs were higher by \$1.8 million, depreciation increased by \$1.2 million, and training and travel costs also increased by \$0.9 million due to the acquisitions. These increases were offset by lower hardware and software costs of \$1.4 million and other cost reductions of \$0.9 million.

Selling, General and Administrative Expenses

Our selling, general and administrative, or SG&A, expenses were lower by \$1.9 million, or 2%, in 2007 compared to 2006.

In 2006, we accrued \$2.4 million for payroll withholding taxes associated with transactions from 2000 and prior. In 2007, we settled this matter for \$0.2 million and reversed the remaining accrual, thus reducing SG&A by \$4.6 million compared to 2006. Partially offsetting this reduction in costs was a \$2.2 million increase in professional fees related to our settlement of litigation inherited from our Passave acquisition and the ongoing examination of our historic transfer pricing practices and policies of certain companies within the PMC-Sierra group. In 2007, we also received a capital tax refund of \$0.5 million.

While we incurred increased payroll-related costs during the year, due to the significant increase in the Canadian dollar relative to the US dollar, this was offset by decreases in our stock-based compensation expense.

Our SG&A expenses were \$46.1 million, or 82% higher in 2006 compared to 2005. The primary reasons for the increase in SG&A expense as a percentage of revenues were that we recorded \$19.9 million of stock-based compensation expense compared to \$0.2 million in 2005, and payroll-related costs were higher by \$14.0 million due to increased headcount. We also incurred an additional \$3.8 million in professional fees, the majority of which related to the investigation by the Audit Committee into stock option dating and the resulting restatement of our financial statements, and \$2.4 million in additional payroll withholding taxes associated with transactions from years 2000 and prior. Sales commissions were higher by \$2.0 million, training and travel increased by \$1.8 million primarily due to the acquisitions, and office and facilities costs increased by \$1.1 million. Lastly, the reversal of \$0.9 million provision for doubtful accounts receivable in 2005 and an increase in other costs of \$0.3 million in 2006 contributed to the remainder of the overall increase in SG&A expenses in 2006.

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Amortization of purchased intangible assets and in-process research and development

Amortization of intangible assets acquired from the Storage Semiconductor Business and Passave was \$18.9 million and \$20.4 million, respectively, for the year.

Passave

A portion of the purchase for Passave was allocated to in-process research and development projects and was expensed in the second quarter of 2006 because technological feasibility had not been established and no future alternative uses existed. Projects acquired from Passave included Ethernet Passive Optical Network (EPON) and Analog Front End (AFE) products, which are based on technology that provides a low-cost method of deploying optical access lines between a carrier's central office and a customer site and which provide further enhancements and functionality to the existing EPON series, and Gigabit Passive Optical Network (GPON) products, which are more complex and support multiple protocols and provide further enhancements to the GPON series.

At the acquisition date of Passave, early revisions of the AFE products were in the final stage of testing and had been sent out to be manufactured or "taped out," with estimated costs to complete of approximately \$0.4 million. At the end of the second quarter of 2007, production testing on AFE products was complete and no further development efforts were required. The EPON products are also complete and released to production, with no additional costs required to complete. By the end of the third quarter of 2007, the EPON products were shipping to customers.

GPON products were in the early design and prototype stages at acquisition, with estimated costs to complete of approximately \$4.5 million at the acquisition date. We are now shipping these products to customers. Another product is now being incorporated with other PMC technology and is part of a larger scope project that is expected to be completed in 2008. Remaining efforts for completion include final stages of development, design testing, tape out, and final testing, as well as customer acceptance.

Storage Semiconductor Business

A portion of the purchase for the Storage Semiconductor Business was allocated to in-process research and development projects and was expensed in the first quarter of 2006 because technological feasibility had not been established and no future alternative uses existed. Projects acquired and expensed include three next-generation Tachyon storage protocol products.

At the acquisition date, two of the next-generation Tachyon products had been taped out, with estimated costs to complete of approximately \$0.8 million. These products are now in production.

The third next-generation Tachyon product, a multi-protocol storage controller, was in the early design stage at acquisition, with estimated costs to complete of approximately \$10 million. By the end of the first quarter of 2006, the product was still in the design stage, and based on feedback from our customers, we re-directed our design resources from this project to other Tachyon controller projects addressing other storage applications. Remaining efforts for completion of the product would include further design, tape out, testing, and final customer acceptance procedures.

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Restructuring Costs and Other Charges

The activity related to excess facility and severance accruals under the Company's restructuring plans during the three years ended December 30, 2007, by year of plan, were as follows:

Excess facility and contract termination costs

<i>(in thousands)</i>	By Year of Plan					Total
	2007	2006	2005	2003	2001	
Balance at December 26, 2004	\$ —	\$ —	\$ —	\$ 3,895	\$ 9,840	\$ 13,735
New charges	—	—	5,288	—	—	5,288
Cash payments	—	—	(417)	(884)	(2,974)	(4,275)
Balance at December 31, 2005	—	—	4,871	3,011	6,866	14,748
Reversals and adjustments	—	—	776	(2,300)	776	(748)
New charges	—	2,338	—	—	—	2,338
Cash payments	—	(227)	(1,379)	(162)	(2,546)	(4,314)
Balance at December 31, 2006	—	2,111	4,268	549	5,096	12,024
Reversals and adjustments	23	(441)	450	(549)	978	461
New charges	2,768	—	—	—	—	2,768
Cash payments	(860)	(1,081)	(1,389)	—	(2,130)	(5,460)
Balance at December 30, 2007	<u>\$ 1,931</u>	<u>\$ 589</u>	<u>\$ 3,329</u>	<u>\$ —</u>	<u>\$ 3,944</u>	<u>\$ 9,793</u>

Severance costs

<i>(in thousands)</i>	By Year of Plan			
	2007	2006	2005	Total
Balance at December 26, 2004	\$ —	\$ —	\$ —	\$ —
New charges	—	—	7,675	7,675
Cash payments	—	—	(7,190)	(7,190)
Balance at December 31, 2005	—	—	485	485
Reversals and adjustments	—	—	(350)	(350)
New charges	—	2,968	1,562	4,530
Cash payments	—	(2,432)	(1,600)	(4,032)
Balance at December 31, 2006	—	536	97	633
Reversals and adjustments	144	(409)	(59)	(324)
New charges	9,863	—	—	9,863
Cash payments	(8,889)	(127)	(38)	(9,054)
Balance at December 30, 2007	<u>\$ 1,118</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 1,118</u>

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2007

In the first quarter of 2007, the Company initiated a cost-reduction plan that involved staff reductions of 175 employees at various sites and the closure of design centers in Saskatoon, Saskatchewan and Winnipeg, Manitoba. The Company also vacated excess office space at its Santa Clara facility. We continued to rationalize costs in the fourth quarter of 2007 by reducing headcount by 18 employees primarily at our Burnaby facility.

To date, the Company has incurred \$9.9 million in termination and relocation costs, \$2.8 million for excess facilities and contract termination costs, and \$2.5 million in asset impairment charges.

The Company has made payments of \$9.7 million in connection with this plan. As of December 30, 2007, \$1.1 million in severance costs remained to be paid and payments related to the excess facilities may extend until 2011.

2006

In the third quarter of 2006, we closed our Ottawa development site in order to reduce operating expenses and the space was vacated by the end of the fourth quarter of 2006. Approximately 35 positions were eliminated, primarily from research and development, resulting in one-time termination benefit and relocation costs of \$2.2 million, and \$2.0 million for excess facilities. We also eliminated 10 positions from research and development in our Portland development site, resulting in restructuring charges of \$1.4 million, comprised of \$0.8 million in severance, \$0.3 million for excess facilities, \$0.1 million for contract termination and \$0.2 million in asset impairment.

During the fourth quarter of 2007 we reduced our estimated severance accrual by \$0.3 million and our accrual for excess facilities by \$0.4 million as we fulfilled a portion of these obligations. We have made \$3.9 million in payments relating to the 2006 plan. As of December 30, 2007, all severance costs have been paid and payments related to the excess facilities will extend to 2010.

2005

During 2005, we completed various restructuring activities aimed at streamlining production and reducing our operating expenses. In the first quarter of 2005, we recorded restructuring charges of \$0.9 million in severance costs related to the termination of 24 employees across all business functions. In the second quarter of 2005, we expanded the workforce reduction activities initiated during the first quarter and terminated 63 employees from research and development located in the Santa Clara facility. In addition, we consolidated our two manufacturing facilities (Santa Clara, California and Burnaby, British Columbia) into one facility (Burnaby), which involved the termination of 26 employees from production control, quality assurance, and product engineering. As a result, we recorded total second quarter restructuring charges of \$7.6 million, including \$6.7 million for termination benefits and a \$0.9 million write-down of equipment and software assets whose value was impaired as a result of these plans. In the third quarter of 2005, we consolidated our facilities and vacated excess office space in the Santa Clara location, and recorded a restructuring charge of \$5.3 million for excess facilities and an additional \$0.1 million in severance costs.

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In the first quarter of 2006, we continued the workforce reduction plans initiated in 2005 and recorded \$1.6 million in restructuring charges related to the termination of 19 employees, primarily from research and development, in the Santa Clara facility. During the third quarter of 2006 we reduced our estimated severance accrual related to the 2005 workforce reduction activities by \$0.4 million, and increased the accrual for excess facilities related to the 2005 restructuring by \$0.8 million. We further increased our accrual for excess facilities by \$0.5 million in the fourth quarter of 2007. To date, we have made payments relating to these activities of \$12.0 million. As of December 30, 2007, all severance costs have been paid. Payments related to the excess facilities will extend to 2011.

2003 and 2001

In 2003 and 2001, we implemented three restructuring plans aimed at focusing development efforts on key projects and reducing operating costs in response to the severe and prolonged economic downturn in the semiconductor industry. Our assessment of the market demand for our products, and the development efforts necessary to meet this demand, were key factors in our decisions to implement these restructuring plans. As end markets for our products had contracted, certain projects were curtailed in an effort to cut costs. Cost reductions in all other functional areas were also implemented, as fewer resources were required to support the reduced level of development and sales activities during these periods.

The January 2003 restructuring included the termination of 175 employees and the closure of design centers in Maryland, Ireland and India, and vacating office space in the Santa Clara facility. To date, we have recorded restructuring charges of \$18.3 million in accordance with SFAS 146, "Accounting for Costs Associated with Exit or Disposal Activities", including \$1.5 million for asset write-downs. These charges related to workforce reduction, lease and contract settlement costs, and the write-down of certain property, equipment and software assets whose value was impaired as a result of this restructuring plan. We have disposed of the property improvements and computer equipment, and software licenses have been cancelled or are no longer being used. In 2006, we reversed \$2.3 million of our restructuring accrual because certain floors in the Santa Clara facility that had been vacated in 2003 were re-occupied in 2006 due to the addition of personnel that occurred with the acquisition of the Storage Semiconductor Business. We reversed a further \$0.5 million in 2007 as we completed a portion of our lease obligation at this site.

The October 2001 restructuring plan included the termination of 341 employees, the consolidation of excess facilities, and the curtailment of certain research and development projects, resulting in a restructuring charge of \$175.3 million, including \$12.2 million of asset write-downs. Due to the continued downturn in real estate markets, we recorded additional provisions for abandoned office facilities of \$1.3 million in the fourth quarter of 2004.

In the first quarter of 2001, we recorded a charge of \$19.9 million for a restructuring plan that included the termination of 223 employees across all business functions, the consolidation of a number of facilities and the curtailment of certain research and development projects. Due to the continued downturn in real estate markets, we recorded additional provisions for abandoned office facilities of \$2.2 million in the fourth quarter of 2004, \$0.8 million in the third quarter of 2006, and \$0.9 million in the fourth quarter of 2007.

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To date, we have made cash payments of \$12.7 million and \$176.6 million related to the 2003 and 2001 plans, respectively. We have completed the activities contemplated in these restructuring plans, but have not yet terminated the leases on all of our surplus facilities. Efforts to exit these sites are ongoing, but the payments related to these facilities could extend to 2011.

Other Income and Expenses (\$ millions)

	<u>2007</u>	<u>Change</u>	<u>2006</u>	<u>Change</u>	<u>2005</u>
Interest income, net	\$ 9.9	10%	\$ 9.0	(26)%	\$ 12.1
<i>Percentage of net revenues</i>	2%		2%		4%
Foreign exchange loss	\$ (18.5)	184%	\$ (0.1)	(97)%	\$ (3.3)
<i>Percentage of net revenues</i>	(4)%		—		(1)%
Loss on extinguishment of debt and amortization of debt issue costs	\$ (1.0)	—	\$ (1.0)	(44)%	\$ (1.8)
<i>Percentage of net revenues</i>	—		—		(1)%
(Loss) Gain on investments	—	(100)%	\$ (1.3)	(193)%	\$ 1.4
<i>Percentage of net revenues</i>	—		—		—

Interest income, net

Our net interest income for 2005, 2006 and 2007 was \$12.1, \$9.0 and \$9.9 respectively. In the fourth quarter of 2005, we issued \$225.0 million of 2.25% senior convertible notes, resulting in higher net interest income in 2005 of approximately \$0.7 million as the yield on short-term deposits exceeded the interest rate on the notes. In the first quarter of 2006, we acquired the Storage Semiconductor Business for \$431.3 million in cash, which lowered our cash balance and resulted in a significant decrease in interest income that year. We did not have any comparable investing activities in 2007 that consumed significant cash and we were able to increase our cash balances through operations during the year. Partially offsetting the impact of the higher cash balances was reduced interest income from prior year tax refunds.

Foreign exchange loss

Foreign exchange loss increased to \$18.5 million in 2007 compared to \$0.1 million in 2006 and \$3.3 million in 2005.

We have a significant design presence outside the United States, especially in Canada. In 2007, the United States dollar declined 15.8% against the Canadian dollar. Accordingly, the majority of our operating expense exposures to changes in the value of the Canadian dollar relative to the United States dollar have been hedged through December 2008. The foreign exchange loss for all years presented relates primarily to the re-measurement each period of accrued income tax amounts in our Canadian subsidiary. We hedge less than twenty percent of our recorded tax accrual, net of deferred tax assets generated in this local jurisdiction.

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Loss on extinguishment of debt and amortization of debt issue costs

In the fourth quarter of 2005, we issued \$225.0 million 2.25% senior convertible notes and recognized amortization of debt issue costs of \$1.0 million during 2007, \$1.0 million in 2006 and \$0.2 million in 2005.

On January 18, 2005, we redeemed our remaining outstanding 3.75% convertible subordinated notes. We expensed the \$1.0 million call premium and the remaining unamortized debt issue costs of \$0.6 million, resulting in an aggregate net loss on redemption of \$1.6 million.

(Loss) gain on investments

During 2006, we sold our investment in Ikanos Communications Inc. for proceeds of \$5.1 million and recorded a gain of \$3.1 million, which has been included in (Loss) gain on sale of investments on the Statement of Operations. Also included in (Loss) gain on sale of investments were a gain on sale of another investment, as well as an impairment loss of \$3.2 million on our investment in a private company, and a \$1.3 million loss on sales of other short-term investments that were redeemed prior to maturity to fund the acquisition of the Storage Semiconductor Business.

In 2005, we received \$2.2 million as final satisfaction of the mortgage owed to us for a property we sold in 2003. As part of the agreement we surrendered an option to purchase the property. The difference between the proceeds and the carrying value of the mortgage receivable was recorded as a gain of \$0.6 million on the Statement of Operations. In addition, we received \$0.7 million that had been in escrow for one year pending final settlement of the sale of our investment in a private technology company. As a result we recorded a gain for this amount, which has been included in (Loss) gain on investments on the Statement of Operations.

Provision for Income Taxes

Our provision for income taxes for the year ended December 30, 2007 was \$16.8 million, resulting in an effective tax rate of 52% on a net loss of \$32.3 million. Despite this net loss, income taxes were incurred primarily from a \$28 million additional accrual relating to an ongoing FIN 48 liability arising from the examination of our historic transfer pricing policies and practices of certain companies within the PMC Group by a certain tax authority. Of the \$28 million increase in our FIN 48 liability, \$13 million is related to arrears interest. Our FIN 48 liability is partially offset by available investment tax credits of \$18 million. The remainder of the provision for income taxes primarily relates to \$6 million of deferred taxes recorded with respect to a past acquisition and net \$1 million due to various items, including revisions of prior estimates.

Our provision for income taxes for the year ended December 31, 2006 was \$49.2 million on a net loss before taxes of \$50.7 million, or 97% of the net loss before taxes, compared to a United States federal statutory tax rate of 35%. Our effective tax rate represents a rate that is applicable to all of our operations crossing multiple tax jurisdictions with tax rates that are

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different than the United States federal statutory tax rate. A significant portion of our net loss for 2006 consisted of expenses that have no associated tax benefits due to their non-deductibility and the fact that deferred tax assets primarily relating to the operating loss carryforwards in the U.S. are fully offset by a valuation allowance. These expenses include amortization of non-deductible intangible assets and in-process research and development, and stock-based compensation. Our effective tax rate in all years presented reflects recoveries and refunds of prior year taxes paid and tax credits received by our Canadian subsidiary for research and development expenses incurred, offset by valuation allowances on losses carried forward.

Our estimated tax provision rate increased significantly at the end of 2006 due to an increase in our estimated tax liability following receipt in 2007 of a written communication from a tax authority examining the historical transfer pricing policies and practices of certain companies within the PMC-Sierra group. As a result, we increased our provision for periods prior to 2006 by \$29.9 million. We recorded \$7.1 million tax expense in the first quarter of 2006 for withholding and other taxes on the repatriation of funds used to purchase the Storage Semiconductor Business and recorded \$3.8 million in net deferred tax expense associated with both of the acquisitions of the Storage Semiconductor Business and Passave, Inc.

See Note 14 to the Consolidated Financial Statements for additional information regarding income taxes.

Critical Accounting Policies and Estimates

General

Management's Discussion and Analysis of Financial Condition and Results of Operations is based upon our Consolidated Financial Statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and assumptions that affect the amounts we report as assets, liabilities, revenue and expenses, and the related disclosure of contingent assets and liabilities. Management bases its estimates on historical experience and on various other assumptions that are reasonable in the circumstances. These estimates could change under different assumptions or conditions.

Our significant accounting policies are outlined in Note 1 to the Consolidated Financial Statements. In management's opinion the following critical accounting policies require the most significant judgment and involve complex estimation. We also have other policies that we consider to be key accounting policies, such as our policies of revenue recognition, including the deferral of revenues on sales to major distributors; however these policies do not meet the definition of critical accounting estimates as they do not generally require us to make estimates or judgments that are difficult or subjective.

Valuation of Goodwill and Intangible Assets

The purchase method of accounting for acquisitions requires estimates and assumptions to allocate the purchase price to the fair value of net tangible and intangible assets acquired, including in-process research and development (IPR&D). The amounts allocated to IPR&D are expensed immediately. The amounts allocated to, and the useful lives estimated for, other

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intangible assets, affect future amortization. There are a number of generally accepted valuation methods used to estimate fair value of intangible assets, and we use primarily a discounted cash flow method, which requires significant management judgment to forecast the future operating results and to estimate the discount factors used in the analysis. If assumptions and estimates used to allocate the purchase price or used to access impairment prove to be inaccurate, future asset impairment charges could be required.

Goodwill and intangible assets determined to have indefinite lives are not amortized, but are subject to an annual impairment test. To determine any goodwill impairment, we perform a two-step process on an annual basis, or more frequently if necessary, to determine 1) whether the fair value of the relevant reporting unit exceeds carrying value and 2) the amount of impairment loss, if any. We review our intangible assets for impairment whenever events or changes in circumstances indicate that their carrying value may not be recoverable. Measurement of an impairment loss is based on the fair value of the asset compared to carrying value.

We performed an annual test for impairment of goodwill and intangible assets in the fourth quarter of 2007 and determined that there was no impairment. The assumptions used to test for impairment, including expected revenues, discount rates, and terminal values, are highly subjective. Valuation models are sensitive to changes in assumptions, and therefore changes in these assumptions in the future could result in significant impairment charges or changes to our expected amortization.

Stock-based compensation

Since January 1, 2006, we recognize compensation expense for all share-based payment awards. Under SFAS 123(R) we measure the fair value of awards of equity instruments and under SFAS 123(R) recognize the cost, net of an estimated forfeiture rate, on a straight-line basis over the period during which services are provided in exchange for the award, generally the vesting period.

Calculating the fair value of stock-based compensation awards requires the input of highly subjective assumptions, including the expected life of the awards and expected volatility of PMC's stock price. Expected volatility is a statistical measure of the amount by which a stock price is expected to fluctuate during a period. Our estimates of expected volatilities are based on a weighted historical and market-based implied volatility. In order to determine the expected life of the awards, we use historical data to estimate option exercises and employee terminations; separate groups of employees that have similar historical exercise behavior, such as directors or executives, are considered separately for valuation purposes. The expected forfeiture rate applied in calculating stock-based compensation cost is estimated using historical data.

The assumptions used in calculating the fair value of stock-based awards involve estimates that require management judgment. If factors change and we use different assumptions, our stock-based compensation expense could change significantly in the future. In addition, if our actual forfeiture rate is different from our estimate, our stock-based compensation could change significantly in the future. See Notes 1 and 4 to the Consolidated Financial Statements for further information on stock-based compensation.

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Restructuring charges - Facilities

In calculating the cost to dispose of our excess facilities we estimate for each location the amount to be paid in lease termination payments, the future lease and operating costs to be paid until the lease is terminated, and the amount of sublease revenues. This calculation includes an estimate of the timing and costs of each lease to be terminated, the amount of operating costs for the affected facilities, and the timing and rate at which we might be able to sublease each site. To form our estimates for these costs we performed an assessment of the affected facilities and considered the current market conditions for each site.

Restructuring activities during the past several years have resulted in facilities charges as follows:

During 2001, we recorded total charges of \$155 million for the restructuring of excess facilities as part of restructuring plans implemented that year. The total remaining estimate of \$3.9 million related to the 2001 restructuring plans represents 100% of the estimated total future operating costs and lease obligations for the affected sites.

In the first quarter of 2003, we announced a further restructuring of our operations, which resulted in the closing of an additional four product development sites and the recording of \$9.6 million charge related to these facilities. During 2006 we reversed \$2.3 million of this provision because a portion of the space was re-occupied. During 2007, we reversed the remaining \$0.5 million of this provision as we subleased space and were able to terminate our lease obligations earlier than we had previously estimated.

In the third quarter of 2005, we recorded charges of \$5.3 million for the restructuring of excess facilities in connection with the restructuring plans implemented in 2005. The total remaining estimate of \$3.3 million represents 100% of the estimated total future operating costs and lease obligations for the site.

In the third quarter of 2006, we announced the closure of our development site in Ottawa and recorded total charges of \$2.3 million for the restructuring of excess facilities. During 2007, we reversed \$0.4 million of this provision because we subleased a portion of this space earlier than originally anticipated. The total remaining estimate of \$0.6 million represents 100% of the estimated total future operating costs and lease obligations for the site.

In the first quarter of 2007, we recorded charges of \$2.8 million related to the closure of our design centers in Saskatoon and Winnipeg, Canada, and exit of a portion of our Santa Clara facility. The total remaining estimate of \$1.9 million represents 100% of the estimated total future operating costs and lease obligations for the site.

Income Taxes

In estimating our annual effective tax rate we review our forecasted net income for the year by geographic area and apply the appropriate tax rates. We also consider the income tax credits available in each tax jurisdiction.

Our operations are conducted in a number of countries with complex tax legislation and regulations pertaining to our activities. We have recorded income tax liabilities based on our

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estimates and interpretations of those regulations for the countries we operate in. However, our estimates are subject to review and assessment by the tax authorities and the courts of those countries. For example, our estimated tax provision rate increased significantly at the end of 2006 due to an increase in our estimated tax liability following receipt in 2007 of a written communication from a tax authority concerning past transfer pricing policies and practices of certain companies within the PMC-Sierra group. As a result, we increased our provision for periods prior to and including 2006 by \$29.9 million and continued to accrue additional taxes and interest during 2007. The timing of any such review and final assessment of our liabilities by local authorities is substantially out of our control and is dependent on the actions by those authorities in the countries we operate in. Any re-assessment of our tax liabilities by tax authorities may result in adjustments of the income taxes we pay or refunds that are due to us.

In certain jurisdictions we have incurred losses and other costs that can be applied against future taxable earnings to reduce our tax liability on those earnings. As we are uncertain of realizing the future benefit of those losses and expenditures, we have taken a valuation allowance against all domestic and certain foreign deferred tax assets.

Business Outlook

We expect our revenues for the first quarter of 2008 to be approximately \$120 to \$125 million based on typical order patterns. As in the past, and consistent with business practice in the semiconductor industry, a portion of our revenues are likely to be derived from orders placed and shipped during the same quarter, which we call our “turns business.” Our turns business varies from quarter to quarter. In the fourth quarter of 2007, net orders booked and shipped within the quarter were approximately 21% of quarterly sales, and we expect the turns percentage to be higher in the first quarter of 2008 compared with the fourth quarter of 2007.

We anticipate our first quarter 2008 gross margin percentage to remain in the 65% range including approximately \$0.5 million stock-based compensation expense. As in past quarters this could vary depending on the volumes of products sold, since many of our costs are fixed. Margins will also vary depending on the mix of products sold.

We expect our first quarter 2008 research and development and selling, general and administrative expenses to be approximately \$63.1 million to \$64.1 million respectively including stock-based compensation expense of approximately \$6.6 million to \$7.6 million. Therefore, we expect our first quarter core operating research and development and selling, general and administrative expenses to be approximately \$56.5 million.

We expect that we will continue to incur significant amortization of purchased intangible assets related to the 2006 acquisitions in the first quarter of 2008.

We anticipate that net interest income will be approximately \$2 million in the first quarter of 2008.

Liquidity and Capital Resources

Our principal source of liquidity at December 30, 2007 was \$364.9 million in cash and cash equivalents.

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In 2007, we generated \$91.2 million of cash from operating activities. Changes in working capital accounts included:

- a \$13.7 million increase in our income taxes payable primarily due to accruing arrears interest of \$13.1 million on our FIN48 liability;
- a \$6.9 million increase in accounts payable and accrued liabilities due primarily to \$4.8 million in increased accruals for photomasks and accounts payable for our Israeli operations and \$2.2 million in increased payroll related accruals;
- a \$2 million decrease in prepaids and other assets attributable to a decrease in prepaid hardware and software maintenance, and software rentals;
- a \$2.1 million increase in accounts receivable, due to increased revenues and the reversal of \$0.2 million reserve for doubtful accounts.
- a \$1.6 million net decrease in accrued restructuring costs due to \$ 11.9 million of additional charges recorded in 2007, offset by \$10.2 million in payments; and
- a \$2.3 million increase in deferred income due to increased shipments to our major distributor.

Cash flows from our investment activities included \$18.6 million purchases of property, equipment and intangible assets.

Cash flows from our financing activities included cash proceeds of \$32 million from the issuance of common stock under our equity-based compensation plans.

As of December 30, 2007 we have the following commitments:

<i>(in thousands)</i>	Total	2008	2009	2010	2011	2012	After 2012
Contractual Obligations							
Operating Lease Obligations:							
Minimum Rental Payments	\$ 36,709	\$ 11,742	\$ 12,583	\$ 7,604	\$ 4,682	\$ 82	\$ 16
Estimated Operating Cost Payments	11,726	4,386	3,481	2,524	1,330	4	1
Long Term Debt:							
Principal Repayment	225,000	—	—	—	—	—	225,000
Interest Payments	91,128	5,063	5,063	5,063	5,063	5,063	65,813
Purchase and other Obligations	20,130	9,531	8,235	2,364	—	—	—
Liability for Unrecognized Tax Benefit (see comments below)							
	<u>\$ 384,693</u>	<u>\$ 30,722</u>	<u>\$ 29,362</u>	<u>\$ 17,555</u>	<u>\$ 11,075</u>	<u>\$ 5,149</u>	<u>\$ 290,830</u>

In addition to the amounts shown in the table above, we have recorded \$179.4 million of unrecognized tax benefits in accordance with FIN 48 as of December 30, 2007 and we are uncertain as to if or when such amounts may be settled. Included in this liability is \$46.8 million accrual for potential interest and penalties. In the event we are required to pay all or a significant portion of such amounts in one payment, our cash reserves will be significantly reduced. This could hinder our ability to enter into strategic transactions and could affect our operations. Should we seek additional financing for operational needs, we cannot be certain that financing will be available on favorable terms or at all.

On October 26, 2005, we issued \$225 million aggregate principal amount of 2.25% senior convertible notes due 2025 (the "Notes") and have recorded these Notes as long-term debt. Issuance costs of \$6.8 million have been deferred and are being amortized over seven years.

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The notes rank equal in right of payment with our other unsecured senior indebtedness and mature on October 15, 2025 unless earlier redeemed by us at our option, or converted or put to us at the option of the holders. Interest is payable semi-annually in arrears on April 15 and October 15 of each year, commencing on April 15, 2006. We may redeem all or a portion of the notes at par on and after October 20, 2012. The holders may require that we repurchase notes on October 15, 2012, 2015 and 2020 respectively.

Holders may convert the notes into the right to receive the conversion value (i) when our stock price exceeds 120% of the approximately \$8.80 per share initial conversion price for a specified period, (ii) in certain change in control transactions, and (iii) when the trading price of the notes does not exceed a minimum price level. For each \$1,000 principal amount of notes, the conversion value represents the amount equal to 113.6687 shares multiplied by the per share price of our common stock at the time of conversion. If the conversion value exceeds \$1,000 per \$1,000 in principal of notes, we will pay \$1,000 in cash and may pay the amount exceeding \$1,000 in cash, stock or a combination of cash and stock, at our election.

We entered into a Registration Rights Agreement with the holders of the Notes, under which we are required to keep the shelf registration statement effective until the earlier of (i) the sale pursuant to the shelf registration statement of all of the Notes and/or shares of common stock issuable upon conversion of the Notes, and (ii) the expiration of the holding period applicable to such securities held by non-affiliates under Rule 144(k) under the Securities Act, or any successor provision, subject to certain permitted exceptions.

We will be required to pay liquidated damages, subject to some limitations, to the holders of the Notes if we fail to comply with our obligations to register the notes and the common stock issuable upon conversion of the notes or the registration statement does not become effective within the specified time periods. In no event will liquidated damages accrue after the second anniversary of the date of issuance of the notes or at a rate exceeding 0.50% of the issue price of the notes. We will have no other liabilities or monetary damages with respect to any registration default. If the holder has converted some or all of its notes into common stock, the holder will not be entitled to receive any liquidated damages with respect to such common stock or the principal amount of the notes converted.

Purchase obligations are comprised of commitments to purchase design tools and software for use in product development, which will be spent between 2008 and 2010. We have not included open purchase orders for inventory or other expenses issued in the normal course of business in the purchase obligations shown above. We estimate these other commitments to be approximately \$13.7 million at December 30, 2007 for inventory and other expenses that will be received in the coming 90 days and that will require settlement 30 days thereafter.

We have a line of credit with a bank that allows us to borrow up to \$0.8 million provided we maintain eligible investments with the bank equal to the amount drawn on the line of credit. At December 30, 2007 we had committed \$0.8 million under letters of credit as security for office leases.

We expect to use approximately \$22.3 million of cash in 2008 for capital expenditures including purchases of intellectual property. Based on our current operating prospects, we believe that existing sources of liquidity will be sufficient to satisfy our projected operating, working capital, capital expenditure, purchase obligations, and remaining restructuring requirements through the end of 2008.

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While we believe our current liquidity will be sufficient to meet our long-term needs for capital, we operate in an industry that is subject to rapid technological and economic changes. Accordingly, we regularly review our capital structure in light of such market changes and changes in our business or finance strategy. In addition, we may contemplate mergers and acquisitions of other companies or assets as part of our business strategy. Consequently in the future we may determine that our sources of liquidity are insufficient and we may proceed with financing or other activities, which may dilute your investment or impact our liquidity and operating results.

Recent Accounting Pronouncements

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, "Fair Value Measurements" (SFAS 157). This Statement defines fair value, establishes guidelines for measuring fair value and expands disclosures regarding fair value measurements. SFAS 157 does not require any new fair value measurements but rather eliminates inconsistencies in guidance found in various prior accounting pronouncements. SFAS 157 is effective for fiscal years beginning after November 15, 2007. The Company expects that adoption of SFAS 157 will not have a material impact on its financial condition or results of operations.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities—Including an amendment of FASB Statement No. 115" (SFAS 159). This statement gives entities the option to measure certain financial assets and liabilities at fair value, with changes in fair value recorded in earnings. SFAS 159 is effective for fiscal years beginning after November 15, 2007. The Company expects that adoption of SFAS 159 will not have a material impact on its financial condition or results of operations.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 141 (revised 2007), "*Business Combinations*" ("SFAS 141(R)"). SFAS 141(R) changes accounting for acquisitions that close beginning in 2009. More transactions and events will qualify as business combinations and will be accounted for at fair value under the new standard. SFAS 141(R) promotes greater use of fair values in financial reporting. Some of the changes will introduce more volatility into earnings. SFAS 141(R) is effective for fiscal years beginning on or after December 15, 2008. We are currently assessing the impact that SFAS 141(R) may have on our financial position, results of operations, and cash flows.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 160, "*Noncontrolling Interests in Consolidated Financial Statements*" ("SFAS 160"), an amendment of ARB No. 51. SFAS 160 will change the accounting and reporting for minority interests which will be recharacterized as noncontrolling interests and classified as a component of equity. SFAS 160 is effective for fiscal years beginning on or after December 15, 2008. SFAS 160 requires retroactive adoption of the presentation and disclosure requirements for existing minority interests. We are currently assessing the impact that SFAS 160 may have on our financial position, results of operations, and cash flows.

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In December 2007, the FASB issued EITF Issue 07-1 “Accounting for Collaborative Arrangements” (EITF 07-1). Collaborative arrangements are agreements between parties to participate in some type of joint operating activity. The task force provided indicators to help identify collaborative arrangements and provides for reporting of such arrangements on a gross or net basis pursuant to guidance in existing authoritative literature. The task force also expanded disclosure requirements about collaborative arrangements. Conclusions within EITF 07-1 are to be applied retrospectively. We are currently assessing the impact that EITF 07-1 may have on our financial position, results of operations, and cash flows.

Off-balance Sheet Arrangements

As of December 30, 2007, the Company had no off-balance sheet financing arrangements.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

The following discussion regarding our risk management activities contains “forward-looking statements” that involve risks and uncertainties. Actual results may differ materially from those projected in the forward-looking statements.

Cash and Cash Equivalents and Short-term Investments

We regularly maintain a short and long term investment portfolio of various types of government and corporate debt instruments. We do not hold any asset-backed commercial paper. Our investments are made in accordance with an investment policy approved by our Board of Directors. Maturities of these instruments are less than three years, with the majority being within one year. To minimize credit risk, we diversify our investments and select minimum ratings of P-1 or A by Moody's, or A-1 or A by Standard and Poor's, or equivalent. We classify these securities as available-for-sale and they are carried at fair market value.

Investments in instruments with both fixed and floating rates carry a degree of interest rate risk. Fixed rate securities may have their fair market value adversely impacted because of a rise in interest rates, while floating rate securities may produce less income than expected if interest rates fall. Due in part to these factors, our future investment income may fall short of expectations because of changes in interest rates, or we may suffer losses in principal if we were to sell securities that have declined in market value because of changes in interest rates.

We do not attempt to reduce or eliminate our exposure to interest rate risk through the use of derivative financial instruments.

Based on a sensitivity analysis performed on the financial instruments held at December 30, 2007, the impact to the fair value of our investment portfolio by a shift in the yield curve of plus or minus 150 basis points would result in a decline, or increase, in portfolio value of less than \$0.1 million.

Senior Convertible Notes:

At December 30, 2007, all \$225 million of the 2.25% senior convertible Notes were outstanding. Because we pay fixed interest coupons on these Notes, market interest rate fluctuations do not impact our debt interest payments. However, the fair value of the senior convertible Notes will fluctuate as a result of changes in the price of our common stock, changes in market interest rates and changes in our credit worthiness.

Our 2.25% senior convertible Notes are not listed on any exchange or included in any automated quotation system, but are registered for resale under the Securities Act of 1933.

The Notes rank equal in right of payment with our other unsecured senior indebtedness and mature on October 15, 2025 unless earlier redeemed by us at our option, or converted or put to us at the option of the holders. Interest is payable semi-annually in arrears on April 15 and October 15 of each year, commencing on April 15, 2006. We may redeem all or a portion of the Notes at par on and after October 20, 2012. The holders may require that we repurchase notes on October 15, 2012, 2015 and 2020 respectively.

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Holders may convert the Notes into the right to receive the conversion value (i) when our stock price exceeds 120% of the approximately \$8.80 per share initial conversion price for a specified period, (ii) in certain change in control transactions, and (iii) when the trading price of the Notes does not exceed a minimum price level. For each \$1,000 principal amount of Notes, the conversion value represents the amount equal to 113.6687 shares multiplied by the per share price of our common stock at the time of conversion. If the conversion value exceeds \$1,000 per \$1,000 in principal of Notes, we will pay \$1,000 in cash and may pay the amount exceeding \$1,000 in cash, stock or a combination of cash and stock, at our election.

Foreign Currency

Our sales and corresponding receivables are denominated primarily in United States dollars. We generate a significant portion of our revenues from sales to customers located outside the United States including Canada, Europe, the Middle East and Asia. We are subject to risks typical of an international business including, but not limited to, differing economic conditions, changes in political climate, differing tax structures, other regulations and restrictions and foreign exchange rate volatility. Accordingly, our future results could be materially adversely affected by changes in these or other factors.

Through our operations in Canada and elsewhere outside the United States, we incur research and development, sales, customer support and administrative expenses in Canadian and other foreign currencies. We are exposed, in the normal course of business, to foreign currency risks on these expenditures, particularly in Canada. In our effort to manage such risks, we have adopted a foreign currency risk management policy intended to reduce the effects of potential short-term fluctuations on our operating results stemming from our exposure to these risks. As part of this risk management strategy, we enter into foreign exchange forward contracts on behalf of our Canadian subsidiary. These forward contracts offset the impact of exchange rate fluctuations on forecasted cash flows or firm commitments. We limit the forward contracts operational period to twelve months or less and we do not enter into foreign exchange forward contracts for trading purposes. Because we do not engage in foreign exchange risk management techniques beyond these periods, our cost structure is subject to long-term changes in foreign exchange rates.

As at December 30, 2007, we had twelve currency forward contracts outstanding that qualified and were designated as cash flow hedges. The U.S. dollar notional amount of these contracts was \$62.2 million and the contracts had a fair value of \$2.2 million.

We attempt to limit our exposure to foreign exchange rate fluctuations from our Canadian dollar net asset or liability positions. We hedge less than twenty percent of our Canadian income tax accrual in the ordinary course of business, and consequently in 2007 we recorded a \$18.2 million foreign exchange loss relating to this item. Our profitability would be materially impacted by a shift in the foreign exchange rates between United States and Canadian currencies. For example, if the value of the United States dollar decreased by 5% relative to the Canadian dollar, our profitability would decrease by \$5.4 million.

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Other Investments

Our other investments include strategic investments in privately held companies that are carried on our balance sheet at cost, net of write-downs for non-temporary declines in market value. We expect to make additional investments like these in the future. These investments are inherently risky, as they typically are comprised of investments in companies and partnerships that are still in the start-up or development stages. The market for the technologies or products that they have under development is typically in the early stages, and may never materialize. We could lose our entire investment in these companies and partnerships or may incur an additional expense if we determine that the value of these assets has been impaired. For example, in the second quarter of 2006 we recorded a charge of \$3.2 million for impairment of an investment in a private company. We may record additional impairment charges should we determine that our investments have incurred a non-temporary decline in value.

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Item 8. Financial Statements and Supplementary Data.

The chart entitled “Quarterly Data” contained in Item 6 Part II hereof is hereby incorporated by reference into the Item 8 of Part II of this Form 10-K.

Consolidated Financial Statements Included in Item 8:

	<u>Page</u>
Report of Independent Registered Public Accounting Firm	56
Consolidated Balance Sheets	57
Consolidated Statements of Operations	58
Consolidated Statements of Cash Flows	59
Consolidated Statements of Stockholders' Equity	60
Notes to Consolidated Financial Statements	61

Reports on Internal Control Over Financial Reporting included in Item 9A:

Management's Annual Report on Internal Control over Financial Reporting	94
Report of Independent Registered Public Accounting Firm	96

Schedules for each of the three years in the period ended December 30, 2007 included in Item 15 (a):

Valuation and Qualifying Accounts	106
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Schedules not listed above have been omitted because they are not applicable or are not required, or the information required to be set forth therein is included in the financial statements or the notes thereto.

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of PMC-Sierra, Inc.

We have audited the accompanying consolidated balance sheets of PMC-Sierra, Inc. and subsidiaries (the “Company”) as of December 30, 2007 and December 31, 2006 and the related consolidated statements of operations, cash flows, and stockholders’ equity for each of the three years in the period ended December 30, 2007. Our audits also included the financial statement schedules listed in the Index at Item 15(a). These financial statements and financial statement schedules are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements and financial statement schedules based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of PMC-Sierra Inc. and subsidiaries as of December 30, 2007 and December 31, 2006, and the results of their operations and their cash flows for each of the three years in the period ended December 30, 2007, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedules, when considered in relation to the basic consolidated financial statements taken as a whole, present fairly, in all material respects the information set forth therein.

As discussed in Note 1 to the consolidated financial statements, the Company adopted Statement of Financial Accounting Standard No. 123(R), “Share-Based Payment”, effective January 1, 2006, and Financial Accounting Standards Board Interpretation No. 48 “Accounting for Uncertainty in Income Taxes”, effective January 1, 2007.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company’s internal control over financial reporting as of December 30, 2007, based on the criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 22, 2008 expressed an unqualified opinion on the Company’s internal control over financial reporting.

/s/ DELOITTE & TOUCHE LLP
Independent Registered Public Accountants
Vancouver, Canada
February 22, 2008

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PMC-Sierra, Inc.
CONSOLIDATED BALANCE SHEETS
(in thousands, except par value)

	December 30, 2007	December 31, 2006
ASSETS:		
Current assets:		
Cash and cash equivalents	\$ 364,922	\$ 258,914
Accounts receivable, net of allowance for doubtful accounts of \$1,546 (2006—\$1,768)	39,362	37,303
Inventories, net	34,246	34,505
Prepaid expenses and other current assets	16,266	17,164
Income tax receivable	2,365	—
Total current assets	457,161	347,886
Investments and other assets	10,747	14,653
Property and equipment, net	18,725	18,904
Goodwill	398,418	395,943
Intangible assets, net	187,126	223,629
Deposits for wafer fabrication capacity	5,145	5,145
Deferred tax assets	54,676	397
	<u>\$ 1,131,998</u>	<u>\$ 1,006,557</u>
LIABILITIES AND STOCKHOLDERS' EQUITY:		
Current liabilities:		
Accounts payable	\$ 24,011	\$ 19,074
Accrued liabilities	53,617	51,199
Income taxes payable	—	59,428
Liability for unrecognized tax benefit	71,586	—
Deferred income taxes	2,787	2,042
Accrued restructuring costs	10,911	12,657
Deferred income	13,674	11,340
Total current liabilities	176,586	155,740
Senior convertible notes	225,000	225,000
Long-term obligations	958	—
Deferred taxes and other tax liabilities	23,023	52,657
Liability for unrecognized tax benefit	107,764	—
PMC special shares convertible into 2,065 (2006—2,099) shares of common stock	2,671	2,732
Commitments and contingencies (Note 10)		
Stockholders' equity		
Common stock, par value \$.001; 900,000 shares authorized; 217,285 shares issued and outstanding (2006—210,650)	237	230
Additional paid in capital	1,394,946	1,327,578
Accumulated other comprehensive income (loss)	1,437	(1,127)
Accumulated deficit	(800,624)	(756,253)
Total stockholders' equity	595,996	570,428
	<u>\$ 1,131,998</u>	<u>\$ 1,006,557</u>

See notes to the consolidated financial statements.

PMC-Sierra, Inc.
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except for per share amounts)
(unaudited)

	Year Ended		
	December 30, 2007	December 31, 2006	December 31, 2005
Net revenues	\$ 449,381	\$ 424,992	\$ 291,411
Cost of revenues	158,297	146,456	80,963
Gross profit	291,084	278,536	210,448
Other costs and expenses:			
Research and development	159,134	158,661	118,720
Selling, general and administrative	100,486	102,363	56,278
Amortization of purchased intangible assets	39,343	33,381	—
In-process research and development	—	35,300	—
Restructuring costs and other charges	14,837	6,119	13,833
(Loss) income from operations	(22,716)	(57,288)	21,617
Other income (expense)			
Interest income, net	9,914	8,979	12,106
Foreign exchange loss	(18,486)	(109)	(3,259)
Loss on extinguishment of debt and amortization of debt issue costs	(968)	(968)	(1,809)
(Loss) gain on investments	—	(1,269)	1,439
(Loss) income before provision for income taxes	(32,256)	(50,655)	30,094
Provision for income taxes	(16,848)	(49,237)	(2,108)
Net (loss) income	\$ (49,104)	\$ (99,892)	\$ 27,986
Net (loss) income per common share—basic	\$ (0.23)	\$ (0.49)	\$ 0.15
Net (loss) income per common share—diluted	\$ (0.23)	\$ (0.49)	\$ 0.15
Shares used in per share calculation—basic	216,330	203,470	184,098
Shares used in per share calculation—diluted	216,330	203,470	189,132

See notes to the consolidated financial statements.

PMC-Sierra, Inc.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	Year Ended		
	December 30, 2007	December 31, 2006	December 31, 2005
Cash flows from operating activities:			
Net (loss) income	\$ (49,104)	\$ (99,892)	\$ 27,986
Adjustments to reconcile net (loss) income to net cash provided by operating activities:			
Stock-based compensation	35,334	37,908	215
In-process research and development	—	35,300	—
Amortization of intangible assets	45,891	36,990	2,344
Deferred income taxes	5,409	4,541	—
Depreciation of property and equipment	10,959	10,820	9,563
Amortization of debt issuance costs	968	968	191
Loss (gain) on investments and other assets	512	1,269	(1,255)
Foreign exchange loss (gain)	18,221	(446)	3,410
Reversal of write-down of excess inventory, net	—	—	(1,904)
Gain on disposal of property and equipment	—	—	(184)
Loss on extinguishment of debt	—	—	1,618
Impairment of purchased intangible assets	1,855	—	538
Changes in operating assets and liabilities, net of the effect of acquisitions:			
Accounts receivable	(2,059)	2,203	(11,868)
Inventories	(156)	(6,181)	3,681
Prepaid expenses and other current assets	1,998	(15,416)	3,489
Accounts payable and accrued liabilities	6,933	(14,296)	6,416
Income taxes payable	13,710	40,569	1,339
Accrued restructuring costs	(1,595)	(2,576)	2,095
Deferred income	2,334	336	3,357
Net cash provided by operating activities	<u>91,210</u>	<u>32,097</u>	<u>51,031</u>
Cash flows from investing activities:			
Acquisition of business, net of cash acquired	—	(419,436)	—
Purchases of short-term available-for-sale investments	—	—	(138,759)
Proceeds from sales and maturities of short-term available-for-sale investments	—	222,357	173,422
Purchases of long-term available-for-sale investments in bonds and notes	—	—	(35,231)
Proceeds from sales and maturities of long-term available-for-sale investments in bonds and notes	—	—	71,021
Purchases of investments and other assets	—	—	(5,693)
Proceeds from sales of other investments	—	5,445	772
Proceeds from refund of wafer fabrication deposits	—	—	1,634
Purchases of property and equipment	(9,824)	(8,011)	(5,156)
Proceeds from sale of property	—	—	2,604
Purchase of intangible assets	(8,754)	(5,144)	(3,454)
Net cash (used in) provided by investing activities	<u>(18,578)</u>	<u>(204,789)</u>	<u>61,160</u>
Cash flows from financing activities:			
Repurchase of convertible subordinated notes	—	—	(70,177)
Proceeds from issuance of senior convertible notes	—	—	225,000
Payment of debt issuance costs	—	—	(6,788)
Proceeds from issuance of common stock	31,980	26,040	24,064
Net cash provided by financing activities	<u>31,980</u>	<u>26,040</u>	<u>172,099</u>
Effect of exchange rate changes on cash and cash equivalents	1,396	—	—
Net increase (decrease) in cash and cash equivalents	106,008	(146,652)	284,290
Cash and cash equivalents, beginning of the year	258,914	405,566	121,276
Cash and cash equivalents, end of the year	<u>\$ 364,922</u>	<u>\$ 258,914</u>	<u>\$ 405,566</u>
Supplemental disclosures of cash flow information:			
Cash paid for interest	\$ 5,063	\$ 5,063	\$ 1,085
Cash refund of income taxes	4,975	2,241	3,224
Cash paid for income taxes	1,596	6,891	3,200
Supplemental disclosures of non-cash investing and financing activities:			
Issuance of common stock and assumption of stock options on acquisition	\$ —	\$ 254,546	\$ —
Conversion of PMC-Sierra special shares into common stock	61	629	1,072

See notes to the consolidated financial statements.

PMC-Sierra, Inc.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(in thousands)

	Shares of Common Stock	Common Stock	Additional Paid in Capital	Deferred Stock Compensation	Accumulated Other Comprehensive (Loss) Income	Retained Earnings (Accumulated Deficit)	Total Stockholders' Equity
Balances at December 26, 2004	178,510	179	983,155	—	350	(684,347)	299,337
Net income	—	—	—	—	—	27,986	27,986
Other comprehensive income (loss):							
Change in net unrealized gains on investments	—	—	—	—	929	—	929
Change in fair value of derivatives	—	—	—	—	444	—	444
Comprehensive income							<u>29,359</u>
Conversion of special shares into common stock	438	—	1,072	—	—	—	1,072
Issuance of common stock under stock benefit plans	4,358	5	24,059	—	—	—	24,064
Deferred stock compensation	—	—	215	(215)	—	—	—
Amortization of deferred stock compensation	—	—	—	215	—	—	215
Balances at December 31, 2005	183,306	184	1,008,501	—	1,723	(656,361)	354,047
Net loss	—	—	—	—	—	(99,892)	(99,892)
Other comprehensive income (loss):							
Change in net unrealized gains on investments	—	—	—	—	(12)	—	(12)
Change in fair value of derivatives	—	—	—	—	(2,838)	—	(2,838)
Comprehensive loss							<u>(102,742)</u>
Issuance of common stock and assumption of stock options on acquisition of Passave Inc.	19,851	19	254,527	—	—	—	254,546
Conversion of special shares into common stock	361	—	629	—	—	—	629
Issuance of common stock under stock benefit plans	7,132	27	26,013	—	—	—	26,040
Stock-based compensation expense	—	—	37,908	—	—	—	37,908
Balances at December 31, 2006	210,650	230	1,327,578	—	(1,127)	(756,253)	570,428
Net loss	—	—	—	—	—	(49,104)	(49,104)
Adjustments related to adoption of FIN48	—	—	—	—	—	4,733	4,733
Other comprehensive income (loss):							
Change in fair value of derivatives	—	—	—	—	2,564	—	2,564
Comprehensive loss							<u>(41,807)</u>
Conversion of special shares into common stock	34	—	61	—	—	—	61
Issuance of common stock under stock benefit plans	6,601	7	31,974	—	—	—	31,981
Stock-based compensation expense	—	—	35,333	—	—	—	35,333
Balances at December 30, 2007	217,285	\$ 237	\$ 1,394,946	\$ —	\$ 1,437	\$ (800,624)	\$ 595,996

See notes to the consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 30, 2007

NOTE 1. Summary of Significant Accounting Policies

Description of business. PMC-Sierra, Inc (the Company or PMC) designs, develops, markets and supports high-speed broadband communications semiconductors, storage semiconductors and microprocessor-based System-on-Chips (SOCs) for metro, access, Fiber-To-The-Home, wireless infrastructure, storage, laser printers and customer premise equipment. The Company offers worldwide technical and sales support through a network of offices in North America, Europe and Asia.

Basis of presentation. The accompanying Consolidated Financial Statements have been prepared pursuant to the rules and regulations of the United States Securities and Exchange Commission (SEC) and United States Generally Accepted Accounting Principles (GAAP). Fiscal 2007 consisted of 52 weeks and ended on Sunday, December 30. Fiscal 2006 consisted of 52 weeks and ended on Sunday, December 31. Fiscal 2005 consisted of 53 weeks and ended on Saturday, December 31. The Company's reporting currency is the United States dollar. The accompanying Consolidated Financial Statements include the accounts of PMC-Sierra, Inc. and any of its subsidiaries or investees in which PMC exercises control. As at December 30, 2007 and December 31, 2006, all subsidiaries included in these Consolidated Financial Statements were wholly owned by PMC. All inter-company accounts and transactions have been eliminated.

Estimates. The preparation of financial statements and related disclosures in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Estimates are used for, but not limited to, stock-based compensation, purchase accounting assumptions including those used to calculate the fair value of intangible assets, the accounting for doubtful accounts, inventory reserves, depreciation and amortization, asset impairments, sales returns, warranty costs, income taxes including uncertain tax positions, restructuring costs, and contingencies. Actual results could differ from these estimates.

Cash and cash equivalents. At December 30, 2007, Cash and cash equivalents included \$0.8 million (December 31, 2006—\$0.8 million) pledged with a bank as collateral for letters of credit issued as security for leased facilities. Cash equivalents are defined as highly liquid debt instruments with maturities at the date of purchase of 3 months or less. Short-term investments are defined as money market instruments or bonds and notes with original maturities greater than 3 months, but less than one year. Investments in bonds and notes are defined as bonds and notes with original or remaining maturities greater than 365 days. Any investments in bonds and notes maturing within one year of the balance sheet date are reported as short-term investments.

Under Statement of Financial Accounting Standards No. 115, "Accounting for Certain Investments in Debt and Equity Securities", management classifies investments as available-for-sale or held-to-maturity at the time of purchase and re-evaluates such designation as of each balance sheet date. Investments classified as held-to-maturity securities are stated at amortized cost with corresponding premiums or discounts amortized against interest income over the life of the investment. Marketable equity and debt securities not classified as held-to-maturity are classified as available-for-sale and reported at fair value. The cost of securities sold is based on the specific identification method. Unrealized gains and losses on these investments, net of any related tax effect are included in equity as a separate component of stockholders' equity.

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Inventories. Inventories are stated at the lower of cost (first-in, first out) or market (estimated net realizable value). Cost is computed using standard cost, which approximates actual average cost. The Company provides inventory allowances on obsolete inventories and inventories in excess of twelve-month demand for each specific part.

Inventories (net of reserves of \$9.8 million and \$8.4 million at December 30, 2007 and December 31, 2006, respectively) were as follows:

<i>(in thousands)</i>	December 30, 2007	December 31, 2006
Work-in-progress	\$ 13,698	\$ 17,463
Finished goods	20,548	17,042
	<u>\$ 34,246</u>	<u>\$ 34,505</u>

In fiscal 2007, the Company decreased inventory reserves by \$1.5 million (2006 - \$2.3 million, 2005 - \$1.8 million) for inventory that was scrapped during the year.

Investments in private entities. The Company has investments in privately traded companies in which it has less than 20% of the voting rights and in which it does not exercise significant influence. The Company monitors these investments for impairment and makes appropriate reductions in carrying values when necessary. These investments are included in Investments and other assets on the Company's balance sheet and are carried at cost, net of write-downs for impairment.

Investments in public companies. In 2005 the Company had an investment in a publicly traded company in which it had less than 20% of the voting rights and in which it did not exercise significant influence. These securities were classified as available-for-sale and reported at fair value, based upon quoted market prices, with the unrealized gains or losses, net of any related tax effect, included as a separate component of stockholders' equity. The Company sold this investment in 2006 (See Note 7. Investments and Other Assets).

Deposits for wafer fabrication capacity. The Company has wafer supply agreements with two independent foundries. Under these agreements, the Company has deposits of \$5.1 million (2006—\$5.1 million) to secure access to wafer fabrication capacity. During 2007, the Company purchased \$43.3 million (\$42 million and \$34.7 million in 2006 and 2005, respectively) from these foundries. Purchases in any year may or may not be indicative of any future period since wafers are purchased based on current market pricing and the Company's volume requirements change in relation to sales of its products.

In each year, the Company is entitled to receive a refund of a portion of the deposits based on the annual purchases from these suppliers compared to the target levels in the wafer supply agreements. In 2006, PMC renewed its supply agreements through December 30, 2008 with its two main foundries with no changes in terms. No deposit refunds were received in 2007 and 2006.

Property and equipment, net. Property and equipment is stated at cost, net of write-downs for impairment, and accumulated depreciation. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets, ranging from two to five years. Leasehold improvements are capitalized and amortized over the shorter of their estimated useful lives or the lease term.

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The components of property and equipment, net are as follows:

December 30, 2007 (in thousands)	Gross	Accumulated Amortization	Net
Software	\$ 56,794	\$ (50,464)	\$ 6,330
Machinery and equipment	124,826	(115,264)	9,562
Leasehold improvements	14,458	(12,009)	2,449
Furniture and fixtures	13,188	(12,804)	384
Total	<u>\$ 209,266</u>	<u>\$ (190,541)</u>	<u>\$ 18,725</u>

December 31, 2006 (in thousands)	Gross	Accumulated Amortization	Net
Software	\$ 52,828	\$ (49,012)	\$ 3,816
Machinery and equipment	125,799	(113,784)	12,015
Leasehold improvements	14,384	(11,811)	2,573
Furniture and fixtures	14,370	(13,870)	500
Total	<u>\$ 207,381</u>	<u>\$ (188,477)</u>	<u>\$ 18,904</u>

Goodwill. Goodwill is recorded when the purchase price paid for an acquisition exceeds the estimated fair value of the net identified tangible and intangible assets acquired. The Company performs a two-step process on an annual basis, or more frequently if necessary, to determine 1) whether the fair value of the relevant reporting unit exceeds carrying value and 2) the amount of an impairment loss, if any. The Company completed this process in December 2007, 2006 and 2005 and determined that there was no impairment to goodwill.

Intangible assets, net. Intangible assets, net, consist of intangible assets acquired through business combinations (See Note 2. Business Combinations), which are amortized over their estimated useful lives ranging from four to ten years or have indefinite lives, and purchased developed technology assets that are amortized over their economic lives, which are normally three years. The components of intangible assets, net are as follows:

December 30, 2007 (in thousands)	Gross	Accumulated Amortization	Net	Estimated life
Backlog	\$ 4,000	\$ (4,000)	\$ —	< 1 year
Core technology	129,700	(32,610)	97,090	8 years
Customer Relationships	66,600	(16,947)	49,653	4-10 years
Existing technology	46,000	(19,167)	26,833	4 years
Trademarks	3,600	—	3,600	indefinite
Acquired developed technology assets	24,446	(14,496)	9,950	3 years
Total	<u>\$ 274,346</u>	<u>\$ (87,220)</u>	<u>\$ 187,126</u>	

December 31, 2006 (in thousands)	Gross	Accumulated Amortization	Net	Estimated life
Backlog	\$ 4,000	\$ (4,000)	\$ —	< 1 year
Core technology	129,700	(14,473)	115,227	8 years
Customer Relationships	66,600	(7,242)	59,358	8 years
Existing technology	46,000	(7,667)	38,333	4 years
Trademarks	3,600	—	3,600	indefinite
Acquired developed technology assets	14,619	(7,508)	7,111	3 years
Total	<u>\$ 264,519</u>	<u>\$ (40,890)</u>	<u>\$ 223,629</u>	

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Estimated future amortization expense for intangible assets is as follows:

<i>(in thousands)</i>	\$
2008	43,450
2009	42,406
2010	27,380
2011	19,818
2012	19,143
Thereafter	31,329
Total	<u>\$183,526</u>

Impairment of long-lived assets. The Company reviews its long-lived assets, other than goodwill, for impairment whenever events or changes in circumstances indicate that the carrying value of such assets may not be recoverable. To determine recoverability, the Company compares the carrying value of the assets to the estimated future undiscounted cash flows. Measurement of an impairment loss for long-lived assets held for use is based on the fair value of the asset determined through discounted cash flows. Long-lived assets classified as held for sale are reported at the lower of carrying value and fair value less estimated selling costs. For assets to be disposed of other than by sale, an impairment loss is recognized when the carrying value is not recoverable and exceeds the fair value of the asset.

Accrued liabilities. The components of accrued liabilities are as follows:

<i>(in thousands)</i>	December 30, 2007	December 31, 2006
Accrued compensation and benefits	\$ 25,114	\$ 21,977
Other accrued liabilities	28,503	29,222
	<u>\$ 53,617</u>	<u>\$ 51,199</u>

Foreign currency translation. For all foreign operations, the U.S. dollar is used as the functional currency. Monetary assets and liabilities in foreign currencies are translated into U.S. dollars using the exchange rate as of the balance sheet date. Revenues and expenses are translated at average rates of exchange during the year. Gains and losses from foreign currency transactions are reported separately as foreign exchange gain (loss) under Other income (expense) on the Statement of Operations.

Derivatives and Hedging Activities. Fluctuating foreign exchange rates may significantly impact PMC's net income and cash flows. The Company periodically hedges forecasted foreign currency transactions related to certain operating expenses. All derivatives are recorded in the balance sheet at fair value. For a derivative designated as a fair value hedge, changes in the fair value of the derivative and of the hedged item attributable to the hedged risk are recognized in net (loss) income. For a derivative designated as a cash flow hedge, the effective portions of changes in the fair value of the derivative are recorded in other comprehensive income and are recognized in net (loss) income when the hedged item affects net (loss) income. Ineffective portions of changes in the fair value of cash flow hedges are recognized in net (loss) income. If the derivative used in an economic hedging relationship is not designated in an accounting hedging relationship or if it becomes ineffective, changes in the fair value of the derivative are recognized in net income. During the year ended December 30, 2007, all hedges were designated as cash flow hedges.

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Fair value of financial instruments. The estimated fair value of financial instruments has been determined by the Company using available market information and appropriate valuation methodologies. However, considerable judgment is required in interpreting market data to develop the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts that the Company could realize in a current market exchange.

The carrying values of cash equivalents, accounts receivable and accounts payable approximate fair value because of their short maturities.

The fair value of the Company's short-term investments, and investment in bonds and notes are determined using estimated market prices provided for those securities (see Note 7). The fair value of investments in public companies is determined using quoted market prices for those securities. The fair value of investments in private entities is not readily determinable due to the illiquid market for these investments. The fair value of the deposits for wafer fabrication capacity is not readily determinable because the timing of the related future cash flows is not determinable and there is no market for the sale of these deposits.

Our 2.25% senior convertible notes are not listed on any securities exchange or included in any automated quotation system, but have been traded over the counter, on the Portal Market or under Rule 144 of the Securities Act of 1933. The exchange prices from these trades are not always available to us and may not be reliable. Trades under the Portal Market do not reflect all trades of the securities and the figures recorded are not independently verified. The price of our senior convertible notes as quoted by Bloomberg on December 30, 2007 was \$103.90 per \$100 in face value, resulting in an aggregate fair value of approximately \$233.8 million.

As of and for the year ended December 30, 2007, the use of derivative financial instruments was not material to the results of operations or our financial position (see "Derivatives and Hedging Activities" in this Note.)

Concentrations. The Company maintains its cash, cash equivalents, short-term investments and long-term investments in investment grade financial instruments with high-quality financial institutions, thereby reducing credit risk concentrations.

At December 30, 2007, approximately 24% (2006—21%) of accounts receivable represented amounts due from one of the Company's distributors. The Company believes that this concentration and the concentration of credit risk resulting from trade receivables owing from high-technology industry customers is substantially mitigated by the Company's credit evaluation process, relatively short collection periods and the geographical dispersion of the Company's sales. The Company generally does not require collateral security for outstanding amounts.

The Company relies on a limited number of suppliers for wafer fabrication capacity.

Revenue recognition. The Company recognizes product revenue when persuasive evidence of an arrangement exists, delivery has occurred, the sales price is fixed or determinable, and collectibility is reasonably assured. PMC generates revenues from direct sales, sales to distributors and sales of consignment inventory. The Company recognizes revenues on goods shipped directly to customers at the time of shipping as that is when title passes to the customer and all revenue recognition criteria specified above are met.

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PMC has a two-tier distribution network, distinguishing between major and minor distributors. The Company currently has one major distributor for which it recognizes revenue on a sell-through basis, utilizing information provided by the distributor. This distributor maintains significantly higher levels of inventory than minor distributors and is given business terms to return a portion of inventory and receive credits for changes in selling prices to end customers, the magnitude of which is not known at the time goods are shipped to this distributor. PMC personnel are often involved in the sales from this distributor to end customers and the Company may utilize inventory at the major distributor to satisfy product demand by other customers.

PMC recognizes revenues from minor distributors at the time of shipment. These distributors are also given business terms to return a portion of inventory and receive credits for changes in selling prices to end customers. At the time of shipment, product prices are fixed and determinable and the amount of future returns and pricing allowances to be granted in the future can be reasonably estimated and accrued.

The Company has consignment inventory which is held at the customer's premises. PMC recognizes revenue on these goods when the customer uses them in production, as that is when title passes to the customer. These sales from consignment inventory are subject to the same warranty terms that are applied to direct sales.

PMC product sales are subject to warranty claims against regular mechanical or electrical failure. PMC maintains accruals for potential returns based on its historical experience.

Research and development expenses. The Company expenses research and development (R&D) costs as incurred. R&D costs include payroll and related costs, materials, services and design tools used in product development, depreciation, and other overhead costs including facilities and computer equipment costs. Intellectual property (IP) purchased from third parties is capitalized and amortized over the expected useful life of the IP. For the years ended December 30, 2007, December 31, 2006 and 2005, research and development expenses were \$159.1 million, \$158.7 million, and \$118.7 million.

Product warranties. The Company provides a limited warranty on most of its standard products and accrues for the expected cost at the time of shipment. The Company estimates its warranty costs based on historical failure rates and related repair or replacement costs. The following table summarizes the activity related to the product warranty liability during fiscal 2007, 2006 and 2005:

<i>(in thousands)</i>	December 30, 2007	December 31, 2006	December 31, 2005
Beginning balance	\$ 4,331	\$ 3,997	\$ 3,492
Accrual for new warranties issued	2,098	1,541	1,398
Reduction for payments	(584)	(759)	(207)
Adjustments related to changes in estimate of warranty accrual	394	(448)	(686)
Ending balance	<u>\$ 6,239</u>	<u>\$ 4,331</u>	<u>\$ 3,997</u>

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Other Indemnifications. From time to time, on a limited basis, the Company indemnifies customers, as well as suppliers, contractors, lessors, and others with whom it has contracts, against combinations of loss, expense, or liability arising from various triggering events related to the sale and use of Company products, the use of their goods and services, the use of facilities, the state of assets that we sell and other matters covered by such contracts, normally up to a specified maximum amount. The Company evaluates estimated losses for such indemnifications under SFAS No. 5, *Accounting for Contingencies*, as interpreted by FASB Interpretation No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*. The Company has no history of indemnification claims for such obligations and has not accrued any liabilities related to such indemnifications in the consolidated financial statements.

Stock-based compensation. On January 1, 2006, the Company adopted Statement of Financial Accounting Standards No. 123 (revised 2004), "Share-Based Payment" (SFAS 123(R)), which requires the recognition of compensation expense for all share-based payment awards. SFAS 123(R) requires the Company to measure the cost of services received in exchange for an award of equity instruments based on the grant-date fair value of the award. The cost of such award will be recognized over the period during which services are provided in exchange for the award, generally the vesting period. The Company adopted SFAS 123(R) using the modified prospective transition method and therefore prior period results have not been restated.

In March 2005, the SEC issued Staff Accounting Bulletin No. 107 (SAB 107). The interpretations in SAB 107 express the views of the SEC staff regarding the interaction between SFAS 123(R) and certain SEC rules and regulations and provide the staff's views regarding the valuation of share-based payment arrangements for public companies. The Company applied the principles of SAB 107 in connection with its adoption of SFAS 123(R).

During the year ended December 30, 2007, the Company recognized \$35.3 million in stock-based compensation expense or \$0.16 per share. No domestic tax benefits were attributed to the tax timing differences arising from stock-based compensation expense because a full valuation allowance was maintained for all domestic deferred tax assets.

Prior to the adoption of SFAS 123(R), the Company recognized stock-based compensation using the intrinsic value method prescribed by Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" (APB 25), and applied the disclosure provisions of SFAS 123, "Accounting for Stock-Based Compensation" (SFAS 123) as if the Company had applied the fair value method to measuring stock-based compensation expense.

If the Company had accounted for stock-based compensation in accordance with the fair value method as prescribed by SFAS 123, net loss and net loss per share for 2005 would have been:

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	December 31, 2005
<i>(in thousands, except per share amounts)</i>	
Net income, as reported	\$ 27,986
Adjustments:	
Stock-based employee compensation expense included in net income	215
Additional stock-based employee compensation expense under fair value based method for all awards, net of related tax effects	(47,531)
Net loss, adjusted	\$ (19,330)
Basic net income per share, as reported	\$ 0.15
Basic net loss per share, adjusted	\$ (0.10)
Diluted net income per share, as reported	\$ 0.15
Diluted net loss per share, adjusted	\$ (0.10)

On October 28, 2005, the Board of Directors of the Company approved an acceleration of vesting of the Company's stock options granted on December 29, 2003 to employees and executive officers under the Company's 1994 Incentive Stock Plan and its 2001 Stock Option Plan that have an exercise price per share of \$20.13 (the "Acceleration"). As a result of the Acceleration, options to purchase approximately 2.4 million shares of the Company's common stock became immediately exercisable, of which options to purchase 0.8 million shares were held by executive officers. As these options had exercise prices in excess of the current market value of the Company's common stock, based on the closing price of \$6.34 per share on October 28, 2005, and were not fully achieving their original objectives of incentive compensation and employee retention, the Company expected the acceleration to have a positive effect on employee morale, retention and perception of option value. In addition, the accelerated vesting eliminated future compensation expense the Company would otherwise recognize in its statement of operations with respect to these accelerated options upon the then subsequent adoption of Statement of Financial Accounting Standards No. 123 (revised 2004), "Share-Based Payment" (SFAS 123R).

See Note 4 to the Consolidated Financial Statements for further information on stock-based compensation.

Interest income, net. The components of interest income, net are as follows:

	Year ended		
<i>(in thousands)</i>	December 30, 2007	December 31, 2006	December 31, 2005
Interest income	\$ 15,051	\$ 13,942	\$ 13,502
Interest expense on long-term debt	(5,137)	(4,963)	(1,396)
	\$ 9,914	\$ 8,979	\$ 12,106

Income taxes. Income taxes are reported under Statement of Financial Accounting Standards No. 109 and, accordingly, deferred income taxes are recognized using the asset and liability method, whereby deferred tax assets and liabilities are recognized for the future tax

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consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and operating loss and tax credit carry forwards. Valuation allowances are provided if, after considering available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized.

On July 13, 2006, the FASB issued interpretation No. 48, "Accounting for Uncertainty in Income Taxes – An Interpretation of FASB Statement No. 109" ("FIN 48"). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements in accordance with FASB Statement No. 109, "Accounting for Income Taxes" and prescribes a recognition threshold and measurement attributes for financial statement disclosure of tax positions taken or expected to be taken on a tax return. Under FIN 48, the impact of an uncertain income tax position on the income tax return must be recognized at the largest amount that is more-likely-than-not to be sustained upon audit by the relevant taxing authority. An uncertain income tax position will not be recognized if it has less than a 50% likelihood of being sustained. Additionally, FIN 48 provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006.

The Company adopted the provisions of FIN 48 on January 1, 2007. As a result of the implementation of FIN 48, the Company recognized a \$4.7 million net decrease in the liability for unrecognized tax benefits which was accounted for as a reduction to the retained deficit. Included in this opening adjustment was a \$6.9 million increase in the liability for unrecognized tax benefits relating to additional uncertain tax positions the Company identified as existing at December 31, 2006.

In addition, the Company had \$44.2 million for the payment of interest and penalties accrued at December 31, 2006. Upon adoption of FIN 48 on January 1, 2007, the Company decreased its accrual for interest and penalties to \$32.6 million. The Company recognizes interest and penalties related to income tax liabilities as a component of income tax expense.

Further, as part of the implementation of FIN 48, the Company reclassified \$57 million from current income taxes payable to current liability for unrecognized tax benefit and \$42 million from long term income taxes payable to long term liability for unrecognized tax benefit. In addition, the Company reclassified \$27.5 million of tax benefits to the deferred tax asset account with a corresponding increase to the unrecognized tax benefit account.

Included in the balance of unrecognized tax benefits at January 1, 2007, are \$125 million of tax benefits that, if recognized, would affect the effective tax rate. The Company does not reasonably estimate that the unrecognized tax benefit will change significantly within the next twelve months.

Net income (loss) per common share. Basic net income (loss) per share is computed using the weighted average number of common shares outstanding during the period. The PMC-Sierra Ltd. Special Shares have been included in the calculation of basic net income (loss) per share. Diluted net income (loss) per share is computed using the weighted average number of common and dilutive common equivalent shares outstanding during the period. Dilutive common equivalent shares consist of stock options, shares issuable on our Employee Share Purchase Plan and common shares issuable on conversion of our senior convertible notes.

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Segment reporting. Segmented information is reported in accordance with Statement of Financial Accounting Standards No. 131 (SFAS 131), “Disclosures about Segments of an Enterprise and Related Information”. SFAS 131 uses a management approach to report financial and descriptive information about a company’s operating segments. Operating segments are revenue-producing components of a company for which separate financial information is produced internally for the company’s management. In all periods presented, the Company operated in one reportable segment: networking products.

Recent Accounting Pronouncements. In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, “Fair Value Measurements” (SFAS 157). This Statement defines fair value, establishes guidelines for measuring fair value and expands disclosures regarding fair value measurements. SFAS 157 does not require any new fair value measurements but rather eliminates inconsistencies in guidance found in various prior accounting pronouncements. SFAS 157 is effective for fiscal years beginning after November 15, 2007. In February 2008, the FASB issued the related FASB Staff Position No. FAS 157-2, “Effective Date of FASB Statement No. 157” (FSP157-2), which delays the effective date of SFAS 157 for all nonrecurring fair value measurements of nonfinancial assets and nonfinancial liabilities until fiscal years beginning after November 15, 2008. FSP 157-2 is effective upon issuance. The Company expects that adoption of SFAS 157 will not have a material impact on its financial condition or results of operations.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, “The Fair Value Option for Financial Assets and Financial Liabilities—Including an amendment of FASB Statement No. 115” (SFAS 159). This statement gives entities the option to measure certain financial assets and liabilities at fair value, with changes in fair value recorded in earnings. SFAS 159 is effective for fiscal years beginning after November 15, 2007. The Company expects that adoption of SFAS 159 will not have a material impact on its financial condition or results of operations.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 141 (revised 2007), “*Business Combinations*” (“SFAS 141(R)”). SFAS 141(R) changes accounting for acquisitions that close beginning in 2009. More transactions and events will qualify as business combinations and will be accounted for at fair value under the new standard. SFAS 141(R) promotes greater use of fair values in financial reporting. Some of the changes will introduce more volatility into earnings. SFAS 141(R) is effective for fiscal years beginning on or after December 15, 2008. We are currently assessing the impact that SFAS 141(R) may have on our financial position, results of operations, and cash flows.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 160, “*Noncontrolling Interests in Consolidated Financial Statements*” (“SFAS 160”), an amendment of ARB No. 51. SFAS 160 will change the accounting and reporting for minority interests which will be recharacterized as noncontrolling interests and classified as a component of equity. SFAS 160 is effective for fiscal years beginning on or after December 15, 2008. SFAS 160 requires retroactive adoption of the presentation and disclosure requirements for existing minority interests. We are currently assessing the impact that SFAS 160 may have on our financial position, results of operations, and cash flows.

In December 2007, the FASB issued EITF Issue 07-1 “Accounting for Collaborative Arrangements” (EITF 07-1). Collaborative arrangements are agreements between parties to

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participate in some type of joint operating activity. The task force provided indicators to help identify collaborative arrangements and provides for reporting of such arrangements on a gross or net basis pursuant to guidance in existing authoritative literature. The task force also expanded disclosure requirements about collaborative arrangements. Conclusions within EITF 07-1 are to be applied retrospectively. We are currently assessing the impact that EITF 07-1 may have on our financial position, results of operations, and cash flows.

Reclassifications. Certain prior year amounts have been reclassified in order to conform to the 2007 presentation.

NOTE 2. Business Combinations

Storage Semiconductor Business

On February 28, 2006, the Company completed the acquisition of the former storage semiconductor business of Agilent Technologies, Inc. (the "Storage Semiconductor Business") pursuant to the terms of the Purchase and Sale Agreement dated October 28, 2005 (the "Purchase Agreement") between PMC and Avago Technologies Pte. Limited ("Avago"). These financial statements include the results of operations of the acquired business from the acquisition date.

PMC purchased the Storage Semiconductor Business due to its strategic and product fit with PMC, the market position the Storage Semiconductor Business has in the Fibre Channel controller market, the design capabilities of its engineering team, and the growth opportunities for standard semiconductor solutions in the enterprise storage market. The Storage Semiconductor Business was part of Agilent's Semiconductor Products Group (as defined in the Purchase Agreement), which Avago, an entity created by Kohlberg Kravis Roberts & Co. and Silver Lake Partners, acquired in December 2005. Under the terms of the Purchase Agreement, Palau Acquisition Corporation, a Delaware corporation and direct wholly owned subsidiary of PMC purchased the Storage Semiconductor Business for the following consideration:

<i>(in thousands)</i>	
Cash paid on closing date	\$424,505
Additional cash for post-closing adjustments	7,022
Merger costs	<u>5,602</u>
Total consideration	<u>\$437,129</u>

Merger costs include investment banking, legal and accounting fees, and other external costs directly related to the acquisition.

The total purchase price has been allocated to the fair value of assets acquired and liabilities assumed, and the excess of the purchase price over the net assets acquired was recorded as goodwill, which for this acquisition is deductible for tax purposes. The allocation was determined by management based on a third-party valuation. Subsequent to the acquisition date, the initial purchase price and residual goodwill were adjusted by \$1.1 million for additional inventory, by \$4 million for design software licenses, and by \$1.9 million for settlement of a legal matter. The allocation of the purchase price was as follows:

<i>(in thousands)</i>	
In-process research and development	\$ 14,800
Inventory	10,720
Property and equipment	7,177
Intangible assets	167,400
Goodwill	244,252
Liabilities assumed	<u>(7,220)</u>
Net assets acquired	<u>\$437,129</u>

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Intangible assets acquired, and their respective estimated remaining useful lives, over which each asset will be amortized on a straight-line basis, are:

<i>(in thousands)</i>	Estimated fair value	Estimated average remaining useful life
Core technology	\$ 114,300	8 years
Customer relationships	46,300	10 years
Trademarks	3,600	indefinite
Backlog	3,200	six months
In-process research and development	14,800	N/A
Total intangible assets acquired	<u>\$ 182,200</u>	

The amount allocated to in-process research and development (IPR&D) represented an estimate of the fair value of research projects that had not reached technological feasibility and had no alternative future use. The estimated fair value of IPR&D was expensed immediately following the consummation of the acquisition.

PMC acquired three next-generation Tachyon storage protocol IPR&D projects related to the Storage Semiconductor Business. One of the projects is a multi-protocol storage controller which was in the early stage of development, and two projects were next-generation Tachyon projects in later stages of development. The value assigned to IPR&D was calculated using the income approach by determining cash flow projections related to the identified projects. The assumptions included information on revenues from existing products and future expected trends for each technology, with an estimated useful life of 5 to 9 years. The rates used to discount the net cash flows to their present values were based upon a weighted average cost of capital of 19%. The discount rate was determined after consideration of market rates of return on debt and equity capital and the risk associated with achieving forecasted sales related to the assets acquired.

The fair value, expected costs to complete, and anticipated completion date for each project was as follows:

<i>(in thousands)</i>	Estimated fair value
Next generation Tachyon products	\$ 9,400
Multi-protocol storage controller	5,400
Total in-process research and development	<u>\$ 14,800</u>

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Passave Inc.

On May 4, 2006, the Company acquired Passave, Inc. ("Passave"), a privately held Delaware corporation, pursuant to the Agreement and Plan of Merger (the "Merger Agreement"), dated April 4, 2006, among the Company, a newly formed direct wholly-owned subsidiary of the Company ("Merger Sub"), Passave, and a representative of certain securityholders of Passave. Under the terms of the Merger Agreement, the Company issued shares of its common stock and assumed stock options, and incurred merger costs having a total value of \$304 million for all of the outstanding capital stock, warrants and outstanding stock options of Passave. Of this amount, \$257.5 million was allocated to the purchase price, and \$46.5 million related to unvested stock and stock options of Passave which will be recorded as stock-based compensation over the requisite service period in accordance with FAS 123R. The fair value of options assumed was calculated using a lattice-binomial method. The Company and the securityholders of Passave have each agreed to indemnify the other for, among other things, breaches of representations, warranties and covenants of the Company and Passave in the Merger Agreement. These financial statements include the results of operations of Passave from the acquisition date.

PMC purchased Passave due to its market share leadership in Passive Optical Networking solutions. This acquisition fits with PMC's strategic intent to address the high-growth Fiber Access market and is aligned with PMC's developments in Customer Premises Equipment. The final purchase price was:

(in thousands)

PMC shares (19.3 million)	\$224,411
Vested Passave stock options assumed by PMC	30,135
Additional post-closing adjustment	2,275
Merger costs	<u>2,950</u>
Total consideration	<u>\$259,771</u>

The total purchase price was allocated to the fair value of assets acquired and liabilities assumed, and the excess of the purchase price over the net assets acquired was recorded as goodwill, which for this acquisition is not deductible for tax purposes. The allocation was determined by management based on a third-party valuation. Merger costs include investment banking fees, legal and accounting fees and other external costs directly related to the merger.

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Net assets acquired consist of the following:

(in thousands)

Tangible assets, net of liabilities	\$ 10,512
Intangible assets	82,500
In-process research and development	20,500
Goodwill	146,259
Net assets acquired	<u>\$259,771</u>

Intangible assets acquired, and their respective estimated remaining useful lives, over which each asset will be amortized on a straight-line basis, are:

<i>(in thousands)</i>	Estimated fair value	Estimated average remaining useful life
Existing technology	\$ 46,000	4 years
Customer relationships	20,300	4 years
Core technology	15,400	4 years
Backlog	800	eight months
In-process research and development	20,500	N/A
Total intangible assets	<u>\$ 103,000</u>	

The amount allocated to in-process research and development (IPR&D) represented an estimate of the fair value of research projects that had not reached technological feasibility and had no alternative future use. The estimated fair value of IPR&D was expensed immediately following the consummation of the acquisition.

PMC acquired IPR&D projects related to EPON and AFE products from Passave.

The value assigned to IPR&D was calculated using the income approach by determining cash flow projections related to identified projects. The assumptions included information on revenues from existing products and future expected trends for each technology, with an estimated useful life of 6 years. The stage of completion of each project was estimated to determine the discount rates to be applied to the valuation of the in-process technology. Based upon the level of completion and the risk associated with in-process technology, we applied discount rates that ranged from 20% – 23% to value the projects acquired.

The fair value, expected costs to complete, and anticipated completion date for each project is as follows:

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<i>(in thousands)</i>	Estimated fair value
EPON products	\$ 18,500
AFE projects	2,000
Total in-process research and development	<u>\$ 20,500</u>

Goodwill represents the excess of the purchase price over the fair value of the net tangible and intangible assets acquired. In accordance with Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets," goodwill will not be amortized but will instead be tested for impairment annually or more frequently if certain indicators are present.

The pro forma financial information presented below gives effect to the acquisitions of Passave and the Storage Semiconductor Business as if both acquisitions had occurred as of the beginning of each fiscal year presented below. If the acquisitions had occurred at the beginning of 2005, the \$35.3 million charge for in-process research and development and acquisition-related costs would have been expensed in 2005. Amortization of intangible assets would have been higher by \$43.3 million, and \$6.0 million, in 2005 and 2006, respectively. In addition, stock-based compensation would have been higher by \$17.4 million and \$3.9 million in 2005 and 2006, respectively, due to amortization of expense associated with unvested options assumed with exercise prices below fair market value on the acquisition date.

The pro forma results do not purport to represent what the Company's results of operations actually would have been if the transactions had occurred on the date indicated or what the results of operations will be in future periods.

<i>(in thousands)</i>	December 31, 2006	December 31, 2005
Pro forma revenues	\$ 461,429	\$ 446,387
Pro forma net loss	(66,454)	(64,775)
Pro forma basic and diluted net loss per share	\$ (0.33)	\$ (0.32)

NOTE 3. Derivative Instruments

The Company generates revenues in U.S. dollars but incurs a portion of its operating expenses in various foreign currencies, primarily the Canadian dollar. To minimize the short-term impact of foreign currency fluctuations on the Company's operating expenses, the Company uses currency forward contracts.

Currency forward contracts that are used to hedge exposures to variability in forecasted foreign currency cash flows are designated as cash flow hedges. The maturities of these instruments are less than twelve months. For these derivatives, the gain or loss from the effective portion of the hedge is initially reported as a component of other comprehensive income in stockholders' equity and subsequently reclassified to earnings in the same period in which the hedged transaction affects earnings. The gain or loss from the ineffective portion of the hedge is recognized as interest income or expense immediately.

At December 30, 2007, the Company had twelve currency forward contracts outstanding that qualified and were designated as cash flow hedges. The U.S. dollar notional amount of these

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contracts was \$62.2 million and the contracts had a fair value of \$2.2 million. No portion of the hedging instrument's gain or loss was excluded from the assessment of effectiveness and the ineffective portions of hedges had no impact on earnings.

NOTE 4. Stock-Based Compensation

At December 30, 2007, the Company has two stock-based compensation programs, which are described below. None of the Company's stock-based awards are classified as liabilities. The Company did not capitalize any stock-based compensation cost, and recorded compensation expense as follows:

<i>(in thousands)</i>	Year ended	
	December 30, 2007	December 31, 2006
Cost of revenues	\$ 1,691	\$ 1,809
Research and development	16,563	16,210
Selling, general and administrative	17,078	19,889
Total	<u>\$ 35,332</u>	<u>\$ 37,908</u>

The Company received cash of \$32.0 million from the exercise of stock-based awards during the year ended December 30, 2007. The total intrinsic value of stock awards exercised during the year ended December 30, 2007, was \$19.4 million.

As of December 30, 2007 there was \$41.7 million of total unrecognized compensation cost related to nonvested stock options granted under the Company's stock option plans, which is expected to be recognized over a period of 2.3 years. As of December 30, 2007 there was \$4.1 million of total unrecognized compensation cost related to nonvested Restricted Stock Units ("RSUs") awarded under the Company's stock option plans, which is expected to be recognized over a period of 3.4 years.

The fair value of the Company's stock option awards granted to employees during the year ended December 30, 2007 was estimated using a lattice-binomial valuation model. Prior to the second quarter of 2005, the fair value of the Company's stock option awards to employees was estimated, for disclosure purposes under SFAS 123, using a Black-Scholes option pricing model which was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. The Company believes that the binomial model provides a better estimate of the fair value of stock option awards because it considers the contractual term of the option, the probability that the option will be exercised prior to the end of its contractual life, and the probability of termination or retirement of the option holder in computing the value of the option. Both models require the input of highly subjective assumptions including the expected stock price volatility and expected life.

The Company's estimates of expected volatilities are based on a weighted historical and market-based implied volatility. The Company uses historical data to estimate option exercises and employee terminations within the valuation model; separate groups of employees that have similar historical exercise behavior are considered separately for valuation purposes. The

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expected term of options granted is derived from the output of the stock option valuation model and represents the period of time that granted options are expected to be outstanding. The risk-free rate for periods within the contractual life of the stock option is based on the U.S. Treasury yield curve in effect at the time of the grant.

The fair values of the Company's stock option and ESPP awards were estimated using the following weighted average assumptions:

Stock Options:

	December 30, 2007	December 31, 2006	December 31, 2005
Expected life (years)	4.1	3.9	3.8
Expected volatility	61%	58%	60%
Risk-free interest rate	4.5%	4.8%	3.9%

Employee Share Purchase Plan:

	December 30, 2007	December 31, 2006	December 31, 2005
Expected life (years)	1.3	1.3	1.3
Expected volatility	50%	50%	53%
Risk-free interest rate	4.7%	4.9%	3.5%

Stock Option Plans

The Company issues its common stock under the provisions of various stock option plans. Stock option awards are granted with an exercise price equal to the closing market price of the Company's common stock at the grant date. The options generally expire within five to ten years and vest over four years.

In 2001, the Company simplified its plan structure. The 2001 Stock Option Plan (the "2001 Plan") was created to replace a number of stock option plans the Company had assumed in connection with mergers and acquisitions completed prior to 2001. The number of shares available for issuance under the 1994 Incentive Stock Plan ("1994 Plan") were approved by stockholders. New stock options or other equity incentives may only be issued under the 1994 Plan and the 2001 Plan. In the second quarter of 2006 the Company assumed the stock option plans and all outstanding stock options of Passave as part of the merger consideration.

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Activity under the option plans during the year ended December 30, 2007 was as follows:

	Number of Options	Weighted average price per share	Weighted average remaining contractual term per share - Years	Aggregate intrinsic value per share
Outstanding, Dec 31, 2006	32,995,994	\$ 9.55		
Granted	4,274,427	\$ 6.67		
Exercised	(4,847,215)	\$ 4.87		
Cancelled, Forfeited	(2,889,217)	\$ 10.77		
Expired	(2,212,484)	\$ 14.01		
Outstanding, December 30, 2007	27,321,505	\$ 9.74	6.67	\$ 0.47
Vested & Expected to Vest, December 30, 2007	25,099,305	\$ 9.85	6.52	\$ 0.51
Exercisable, December 30, 2007	17,559,272	\$ 10.85	5.76	\$ 0.51

No adjustment has been recorded for fully vested options that expired during the year ended December 30, 2007. A reversal of \$5.4 million was recorded for pre-vesting forfeitures.

The following table summarizes information on options outstanding and exercisable for the combined option plans at December 30, 2007:

Range of Exercise Prices	Options Outstanding	Weighted Average Remaining Contractual Life (years)	Weighted Average Exercise Price per Share	Options Exercisable	Weighted Average Exercise Price per Share
\$0.05 - \$5.95	6,968,919	5.94	\$ 4.84	5,818,999	\$ 5.08
\$6.01 - \$7.87	8,439,582	8.17	\$ 7.26	3,019,938	\$ 7.73
\$7.89 - \$10.82	2,964,563	6.29	\$ 9.17	2,031,965	\$ 9.21
\$10.97 - \$15.25	4,468,029	7.65	\$ 11.17	2,209,670	\$ 11.33
<u>\$15.98 - \$189.94</u>	<u>4,480,412</u>	<u>4.26</u>	<u>\$ 20.97</u>	<u>4,478,700</u>	<u>\$ 20.97</u>
<u>\$0.05 - \$189.94</u>	<u>27,321,505</u>	<u>6.67</u>	<u>\$ 9.74</u>	<u>17,559,272</u>	<u>\$ 10.85</u>

The weighted-average estimated fair values of employee stock options granted during fiscal 2007, 2006, and 2005 were \$3.22, \$4.60, and \$3.34, per share, respectively.

Restricted Stock Units

On February 1, 2007, the Company amended its stock award plans to allow for the issuance of RSUs to employees and directors. The first grant of RSUs occurred on May 25, 2007. The grants vest over varying terms, to a maximum of four years from the date of grant.

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A summary of RSU activity during the year ended December 30, 2007 is as follows:

	Restricted Stock Units	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value at December 30, 2007
Unvested shares at December 31, 2006	—	—	—
Awarded	901,125	—	—
Released	—	—	—
Forfeited	(69,374)	—	—
End of Period	831,751	2.04	\$ 5,489,557
Restricted Stock Units vested and expected to vest, December 30, 2007	612,619	1.89	\$ 4,043,287

The weighted-average estimated fair value of RSU's awarded in fiscal 2007 was \$7.49.

Employee Stock Purchase Plan

In 1991, the Company adopted an Employee Stock Purchase Plan ("ESPP") under Section 423 of the Internal Revenue Code. The ESPP allows eligible participants to purchase shares of the Company's common stock through payroll deductions at a purchase price of 85% of the lower of the fair market value of the Company's stock on the close of the first trading day or last trading day of the six-month purchase period. Under the ESPP, the number of shares authorized to be available for issuance under the plan are increased automatically on January 1 of each year until the expiration of the plan. The increase will be limited to the lesser of (i) 1% of the outstanding shares on January 1 of each year, (ii) 2,000,000 shares (after adjusting for stock dividends), or (iii) an amount to be determined by the Board of Directors.

During 2007, 1,753,447 shares were issued under the Plan at a weighted-average price of \$4.78 per share. As of December 30, 2007, 8,149,940 shares were available for future issuance under the ESPP (December 31, 2006—7,903,387).

The weighted-average estimated fair values of Employee Stock Purchase Plan awards during fiscal years 2007, 2006, and 2005, were \$2.59, \$3.27 and \$3.18 per share, respectively.

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NOTE 5. Restructuring and Other Costs

The activity related to excess facility and severance accruals under the Company's restructuring plans during the three years ended December 30, 2007, by year of plan, were as follows:

Excess facility and contract termination costs

<i>(in thousands)</i>	By Year of Plan					
	2007	2006	2005	2003	2001	Total
Balance at December 26, 2004	\$ —	\$ —	\$ —	\$ 3,895	\$ 9,840	\$ 13,735
New charges	—	—	5,288	—	—	5,288
Cash payments	—	—	(417)	(884)	(2,974)	(4,275)
Balance at December 31, 2005	—	—	4,871	3,011	6,866	14,748
Reversals and adjustments	—	—	776	(2,300)	776	(748)
New charges	—	2,338	—	—	—	2,338
Cash payments	—	(227)	(1,379)	(162)	(2,546)	(4,314)
Balance at December 31, 2006	—	2,111	4,268	549	5,096	12,024
Reversals and adjustments	23	(441)	450	(549)	978	(461)
New charges	2,768	—	—	—	—	2,768
Cash payments	(860)	(1,081)	(1,389)	—	(2,130)	(5,460)
Balance at December 30, 2007	\$ 1,931	\$ 589	\$ 3,329	\$ —	\$ 3,944	\$ 9,793

Severance costs

<i>(in thousands)</i>	By Year of Plan			
	2007	2006	2005	Total
Balance at December 26, 2004	\$ —	\$ —	\$ —	\$ —
New charges	—	—	7,675	7,675
Cash payments	—	—	(7,190)	(7,190)
Balance at December 31, 2005	—	—	485	485
Reversals and adjustments	—	—	(350)	(350)
New charges	—	2,968	1,562	4,530
Cash payments	—	(2,432)	(1,600)	(4,032)
Balance at December 31, 2006	—	536	97	633
Reversals and adjustments	144	(409)	(59)	(324)
New charges	9,863	—	—	9,863
Cash payments	(8,889)	(127)	(38)	(9,054)
Balance at December 30, 2007	<u>\$ 1,118</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 1,118</u>

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2007

In the first quarter of 2007, the Company initiated a cost-reduction plan that involved staff reductions of 175 employees at various sites and the closure of design centers in Saskatoon, Saskatchewan and Winnipeg, Manitoba. The Company also vacated excess office space at its Santa Clara facility. PMC continued to rationalize costs in the fourth quarter of 2007 by reducing headcount by 18 employees primarily at the Burnaby facility.

To date, the Company has incurred \$9.9 million in termination and relocation costs, \$2.8 million for excess facilities and contract termination costs and \$2.5 million in asset impairment charges.

The Company has made payments of \$9.7 million in connection with this plan. As of December 30, 2007, \$1.1 million in severance costs remained to be paid and payments related to the excess facilities may extend until 2011.

2006

In the third quarter of 2006, the Company closed its Ottawa development site in order to reduce operating expenses and the space was vacated by the end of the fourth quarter of 2006. Approximately 35 positions were eliminated, primarily from research and development, resulting in one-time termination benefit and relocation costs of \$2.2 million, and \$2.0 million for excess facilities. The Company also eliminated 10 positions from research and development in the Company's Portland development site, resulting in restructuring charges of \$1.4 million, comprised of \$0.8 million in severance, \$0.3 million for excess facilities, \$0.1 million for contract termination and \$0.2 million in asset impairment.

During the fourth quarter of 2007 the Company reduced its estimated severance accrual by \$0.3 million and its accrual for excess facilities by \$0.4 million as the Company fulfilled a portion of these obligations. The Company has made \$3.9 million in payments relating to the 2006 plan. As of December 30, 2007, all severance costs have been paid and payments related to the excess facilities will extend to 2010.

2005

During 2005, the Company completed various restructuring activities aimed at streamlining production and reducing operating expenses. In the first quarter of 2005, the Company recorded restructuring charges of \$0.9 million in severance costs related to the termination of 24 employees across all business functions. In the second quarter of 2005, the company expanded the workforce reduction activities initiated during the first quarter and terminated 63 employees from research and development located in the Santa Clara facility. In addition, the Company consolidated two manufacturing facilities (Santa Clara, California and Burnaby, British Columbia) into one facility (Burnaby), which involved the termination of 26 employees from production control, quality assurance, and product engineering. As a result, the Company recorded total second quarter restructuring charges of \$7.6 million, including \$6.7 million for termination benefits and a \$0.9 million write-down of equipment and software assets whose value was impaired as a result of these plans. In the third quarter of 2005, the Company

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consolidated its facilities and vacated excess office space in the Santa Clara location, and recorded a restructuring charge of \$5.3 million for excess facilities and an additional \$0.1 million in severance costs.

In the first quarter of 2006, the Company continued the workforce reduction plans initiated in 2005 and recorded \$1.6 million in restructuring charges related to the termination of 19 employees, primarily from research and development, in the Santa Clara facility. During the third quarter of 2006 the Company reduced its estimated severance accrual related to the 2005 workforce reduction activities by \$0.4 million, and increased the accrual for excess facilities related to the 2005 restructuring by \$0.8 million. The Company further increased its accrual for excess facilities by \$0.5 million in the fourth quarter of 2007. To date, the Company has made payments relating to these activities of \$12.0 million. As of December 30, 2007, all severance costs have been paid. Payments related to the excess facilities will extend to 2011.

2003 and 2001

In 2003 and 2001, the Company implemented three restructuring plans aimed at focusing development efforts on key projects and reducing operating costs in response to the severe and prolonged economic downturn in the semiconductor industry. PMC's assessment of the market demand for its products, and the development efforts necessary to meet this demand, were key factors in the decisions to implement these restructuring plans. As end markets for the Company's products had contracted, certain projects were curtailed in an effort to cut costs. Cost reductions in all other functional areas were also implemented, as fewer resources were required to support the reduced level of development and sales activities during these periods.

The January 2003 restructuring included the termination of 175 employees and the closure of design centers in Maryland, Ireland and India, and vacating office space in the Santa Clara facility. To date, PMC has recorded restructuring charges of \$18.3 million in accordance with SFAS 146, "Accounting for Costs Associated with Exit or Disposal Activities", including \$1.5 million for asset write-downs. These charges related to workforce reduction, lease and contract settlement costs, and the write-down of certain property, equipment and software assets whose value was impaired as a result of this restructuring plan. PMC has disposed of the property improvements and computer equipment, and software licenses have been cancelled or are no longer being used. In 2006, the Company reversed \$2.3 million of this restructuring accrual because certain floors in the Santa Clara facility that had been vacated in 2003 were re-occupied in 2006 due to the addition of personnel that occurred with the acquisition of the Storage Semiconductor Business. The Company reversed a further \$0.5 million in 2007 as it completed a portion of the lease obligation at this site.

The October 2001 restructuring plan included the termination of 341 employees, the consolidation of excess facilities, and the curtailment of certain research and development projects, resulting in a restructuring charge of \$175.3 million, including \$12.2 million of asset write-downs. Due to the continued downturn in real estate markets, the Company recorded additional provisions for abandoned office facilities of \$1.3 million in the fourth quarter of 2004.

In the first quarter of 2001, PMC recorded a charge of \$19.9 million for a restructuring plan that included the termination of 223 employees across all business functions, the consolidation of a number of facilities and the curtailment of certain research and development projects. Due to the continued downturn in real estate markets, the Company recorded additional provisions for abandoned office facilities of \$2.2 million in the fourth quarter of 2004, \$0.8 million in the third quarter of 2006, and \$0.9 million in the fourth quarter of 2007.

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To date, PMC has made cash payments of \$12.7 million and \$176.6 million related to the 2003 and 2001 plans, respectively. The Company has completed the activities contemplated in these restructuring plans, but has not yet terminated the leases on all of its surplus facilities. Efforts to exit these sites are ongoing, but the payments related to these facilities could extend to 2011.

NOTE 6. Investments in Debt Securities

At December 30, 2007, we held \$35.1 million (2006—\$153.2 million) in U.S. Government Treasury and Agency notes, which were classified as available-for-sale investments. These investments are included in cash and cash equivalents in the Consolidated Balance Sheet and have maturities of three months or less.

NOTE 7. Investments and Other Assets

The components of other investments and assets are as follows:

<i>(in thousands)</i>	December 30, 2007	December 31, 2006
Investments in private entities	\$ 2,000	\$ 2,000
Deferred debt issue costs (Note 9)	4,677	5,645
Other assets	4,070	7,008
	<u>\$ 10,747</u>	<u>\$ 14,653</u>

During 2006, the Company recorded a \$3.2 million impairment loss on its investment in a private company, which was its carrying value. This was offset by a \$0.1 million gain on sale of another investment. In addition, the Company sold its investment in Ikanos Communications Inc. (Ikanos) in 2006 for proceeds of \$5.1 million and recorded a gain of \$3.1 million, included in Gain on investments on the Statement of Operations.

The Company monitors the value of its investments for impairment and records an impairment charge to reflect any decline in value below its cost basis, if that decline is considered to be other than temporary. The assessment of impairment in carrying value is based on the market value trends of similar public companies, the current business performance of the entities in which we have invested, and if available, the estimated future market potential of the companies and venture funds.

As of December 30, 2007 the Company had deposits of \$4 million related to long-term design tool contracts. These costs are recorded as other assets and are being amortized according to usage over the contract term, which ends in 2010.

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NOTE 8. Lines of credit

At December 30, 2007, the Company had available a revolving line of credit with a bank under which the Company may borrow up to \$0.8 million with interest at the bank's alternate base rate (annual rate of 7.75% at December 30, 2007) as long as the Company maintains eligible investments with the bank in an amount equal to its drawings. This agreement will expire in July 2008. At December 30, 2007, \$0.8 million cash was deposited with the bank to offset the amount committed under letters of credit used as security for a facility lease.

NOTE 9. Long-term debt

2.25% Senior convertible notes

On October 26, 2005, the Company issued \$225 million aggregate principal amount of 2.25% senior convertible notes due 2025. The Company has recorded these Notes as long-term debt and issuance costs of \$6.8 million have been deferred and will be amortized over seven years, which is the Company's earliest call date. This approximates the effective interest method.

The notes rank equal in right of payment with our other unsecured senior indebtedness and mature on October 15, 2025 unless earlier redeemed by the Company at its option, or converted or put to the Company at the option of the holders. Interest is payable semi-annually in arrears on April 15 and October 15 of each year, commencing on April 15, 2006. The Company may redeem all or a portion of the notes at par on and after October 20, 2012. The holders may require that the Company repurchase notes on October 15, 2012, 2015 and 2020 respectively.

Holders may convert the notes into the right to receive the conversion value (i) when the Company's stock price exceeds 120% of the approximately \$8.80 per share initial conversion price for a specified period, (ii) in certain change in control transactions, and (iii) when the trading price of the notes does not exceed a minimum price level. For each \$1,000 principal amount of notes, the conversion value represents the amount equal to 113.6687 shares multiplied by the per share price of the Company's common stock at the time of conversion. If the conversion value exceeds \$1,000 per \$1,000 in principal of notes, the Company will pay \$1,000 in cash and may pay the amount exceeding \$1,000 in cash, stock or a combination of cash and stock, at the Company's election.

The Company entered into a Registration Rights Agreement with the holders of the notes, under which the Company is required to keep the shelf registration statement effective until the earlier of (i) the sale pursuant to the shelf registration statement of all of the notes and/or shares of common stock issuable upon conversion of the notes, and (ii) the expiration of the holding period applicable to such securities held by non-affiliates under Rule 144(k) under the Securities Act, or any successor provision, subject to certain permitted exceptions.

The Company will be required to pay liquidated damages, subject to some limitations, to the holders of the notes if the Company fails to comply with its obligations to register the notes and the common stock issuable upon conversion of the notes or the registration statement does not become effective within the specified time periods. In no event will liquidated damages accrue

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after the second anniversary of the date of issuance of the notes or at a rate exceeding 0.50% of the issue price of the notes. The Company will have no other liabilities or monetary damages with respect to any registration default. If the holder has converted some or all of its notes into common stock, the holder will not be entitled to receive any liquidated damages with respect to such common stock or the principal amount of the notes converted.

3.75% Convertible subordinated notes

In August 2001, the Company issued \$275 million of convertible subordinated notes maturing on August 15, 2006.

During the third fiscal quarter of 2003, the Company repurchased \$100 million principal amount of these notes for \$96.7 million and expensed \$1.6 million of related unamortized debt issue costs, resulting in a net gain of \$1.7 million. On January 6, 2004, the Company repurchased \$106.9 million of these notes pursuant to a tender offer, at par value. The Company expensed approximately \$1.6 million of debt issue costs related to the repurchased notes. The remaining \$68.1 million of these notes were redeemed by the Company on January 18, 2005 for a total of \$70.2 million in cash, which included \$1.1 million in accrued interest and a \$1.0 million call premium.

These notes bore interest at 3.75% payable semi-annually and were convertible into an aggregate of approximately 6.5 million shares of PMC's common stock at any time prior to maturity at a conversion price of approximately \$42.43 per share.

NOTE 10. Commitments and Contingencies

Legal Matters:

SEC Informal Inquiry

On August 18, 2006, PMC received an informal confidential request from the SEC advising that the SEC commenced an informal inquiry into the Company's historical stock option-granting practices. The Company engaged outside counsel to represent it in the inquiry. On December 6, 2006, a meeting took place at the SEC in San Francisco during which the Audit Committee and its special counsel summarized the results of its investigation into the Company's historical option-granting practices. In February 2007, the Company completed all the SEC's requests for information related to its inquiry. On October 26, 2007, the SEC staff formally notified the Company that its inquiry was terminated and that no enforcement action against the Company had been recommended to the SEC.

Stockholder Derivative Lawsuits

Three derivative actions have been filed against the Company, as a nominal defendant, and various current and former officers and/or directors: (1) *Meissner v. Bailey, et al.*, Santa Clara Superior Court Case No. 1-06-CV-071329 (filed September 18, 2006); (2) *Beiser v. Bailey, et al.*, United States District Court for the Northern District of California Case No. 5:06-CV-05330-RS (filed August 29, 2006); and (3) *Barone v. Bailey, et al.*, United States District Court for the Northern District of California Case No. 4:06-CV-06473-SBA (filed October 16, 2006). On

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November 21, 2006, the Beiser and Barone actions were consolidated into one case. On January 18, 2007, the Santa Clara County Superior Court in California ordered that the Meissner action be stayed pending the outcome of the consolidated, federal Beiser/Baron action. A consolidated complaint in the Beiser/Baron action was filed on January 29, 2007 (the "Consolidated Complaint").

The Consolidated Complaint generally alleged that various current and former Company directors and/or officers breached their duty of loyalty and/or duty of care to the Company and its shareholders, that these purported breaches of fiduciary duties caused harm to the Company and the plaintiffs seek to recover damages on behalf of the Company. The Consolidated Complaint also alleged violations of federal securities laws. The Company is a nominal defendant in the cases, but any recovery in the litigation would be paid to the Company, rather than to its shareholders. The defendants have entered into joint defense arrangements.

On March 15, 2007, the Company filed three separate motions aimed at having the federal lawsuit dismissed on various legal grounds. One of these motions was on the basis that plaintiffs failed to plead with particularity facts establishing that a litigation demand on the board of directors of the Company would have been futile at the time they commenced the derivative lawsuit. On June 20, 2007, the Court heard the motion to dismiss plaintiffs' complaint for failure to plead demand futility with particularity. The Court ruled on the motion to dismiss on August 22, 2007 finding that the plaintiffs' Consolidated Complaint had not met the pleading burden and gave plaintiffs leave to amend. The plaintiffs filed their Amended Consolidated Complaint on October 2, 2007. While the plaintiffs' claims are substantially similar, they have reduced the scope of their allegations. The Company filed motions to dismiss the Amended Consolidated Complaint consistent with its previous motions which were argued before the Court on January 30, 2008. The Court also took argument on a motion to compel the production of certain documents filed by the plaintiffs December 26, 2007. The Court has not yet ruled on the motions.

At December 30, 2007, the Company has not accrued costs for potential losses related to the Amended Consolidated Complaint.

Operating leases:

The Company leases its facilities under operating lease agreements, which expire at various dates through September 30, 2013.

Rent expense including operating costs for the years ended December 30, 2007, December 31, 2006, and 2005 was \$10.8 million, \$10.5 million, and \$9.1 million, respectively. Excluded from rent expense for 2007 was additional rent and operating costs of \$4.6 million (2006—\$4.2 million; 2005—\$4.2 million) related to excess facilities, which were accrued as part of the restructuring programs.

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Minimum future rental payments under operating leases are as follows:

<u>Year Ending December 31 (in thousands)</u>	
2007	\$11,742
2008	12,583
2009	7,604
2010	4,682
2011 and thereafter	98
Total minimum future rental payments under operating leases	<u>\$36,709</u>

Supply agreements. The Company has supply agreements with both Chartered and TSMC that were renewed during 2006. These renewed agreements are in effect until December 31, 2008. The Company made deposits to secure access to wafer fabrication capacity of \$5.1 million at December 31, 2006 and 2005. Under these agreements, the foundries must supply certain quantities of wafers per year. Neither of these agreements have minimum unit volume requirements but the Company is obliged under one of the agreements to purchase a minimum percentage of the Company's total annual wafer requirements provided that the foundry is able to continue to offer competitive technology, pricing, quality and delivery. The agreements may be terminated if either party does not comply with the terms.

Contingencies. In the normal course of business, the Company receives and makes inquiries with regard to possible patent infringements. Where deemed advisable, the Company may seek or extend licenses or negotiate settlements. Outcomes of such negotiations may not be determinable at any point in time; however, management does not believe that such licenses or settlements will, individually or in the aggregate, have a material adverse effect on the Company's financial position, results of operations or cash flows.

NOTE 11. Special Shares

At December 30, 2007 and December 31, 2006, the Company maintained a reserve of 2,065,000 and 2,099,000 shares, respectively, of PMC common stock to be issued to holders of PMC-Sierra, Ltd. (LTD) special shares.

The special shares of LTD, the Company's principal Canadian subsidiary, are redeemable or exchangeable for PMC common stock. Special shares do not vote on matters presented to the Company's stockholders, but in all other respects represent the economic and functional equivalent of PMC common stock for which they can be redeemed or exchanged at the option of the holders. The special shares have class voting rights with respect to transactions that affect the rights of the special shares as a class and for certain extraordinary corporate transactions involving LTD. If LTD files for bankruptcy, is liquidated or dissolved, the special shares receive as a preference the number of shares of PMC common stock issuable on conversion plus a nominal amount per share plus unpaid dividends, or at the holder's option convert into LTD ordinary shares, which are the functional equivalent of voting common stock. If the Company files for bankruptcy, is liquidated, or dissolved, special shares of LTD receive the cash equivalent of the value of PMC common stock into which the special shares could be converted, plus unpaid dividends, or at the holder's option convert into LTD ordinary shares. If the Company materially breaches its obligations to special shareholders of LTD (primarily to permit conversion of special shares into PMC common stock), the special shareholders may convert their shares into LTD ordinary shares.

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These special shares of LTD are classified outside of stockholders' equity until such shares are exchanged for PMC common stock. Upon exchange, amounts will be transferred from the LTD special shares account to the Company's common stock and additional paid-in capital on the consolidated balance sheet.

NOTE 12. Stockholders' Equity

Authorized capital stock of PMC. At December 30, 2007 and December 31, 2006, the Company had an authorized capital of 905,000,000 shares, 900,000,000 of which are designated "Common Stock", \$0.001 par value, and 5,000,000 of which are designated "Preferred Stock", \$0.001 par value.

Stockholders' Rights Plan. The Company adopted a stockholder rights plan in 2001, pursuant to which the Company declared a dividend of one share purchase right for each outstanding share of common stock. If certain events occur, including if an investor tenders for or acquires more than 15% of the Company's outstanding common stock, stockholders (other than the acquirer) may exercise their rights and receive \$650 worth of our common stock in exchange for \$325 per right, or the Company may, at the Company's option, issue one share of common stock in exchange for each right, or the Company may redeem the rights for \$0.001 per right.

NOTE 13. Employee Benefit Plans

Post-retirement Health Care Benefits. Our unfunded post retirement benefit plan, which was assumed in connection with the acquisition of the Storage Semiconductor Business, provides retiree medical benefits to eligible United States employees who meet certain age and service requirements upon retirement from the Company. These benefits are provided from the date of retirement until the employee qualifies for Medicare coverage. The amount of the retiree medical benefit obligation assumed by the Company was \$1.1 million at the time of the acquisition.

At December 30, 2007, the accumulated postretirement benefit obligation was \$1.4 million, with no unrecognized gain/loss or unrecognized prior service cost. The net period benefit cost was \$0.2 million during 2007. No distributions were made from the plan during the period. The Company includes accrued benefit costs for its post-retirement program in Accrued liabilities on the Company's Consolidated Balance Sheet.

The health care accumulated postretirement benefit obligations were determined at December 30, 2007 using a discount rate of 6% and a current year health care trend of 9% decreasing to an ultimate trend rate of 5.0% in 2011.

Employee Retirement Savings Plans. The Company sponsors a 401(k) retirement plan for its employees in the United States and similar plans for its employees in Canada and other countries. Employees can contribute a percentage of their annual compensation to the plans, limited to maximum annual amounts set by local taxation authorities. The Company contributed \$3.7 million, \$4.3 million, and \$3.8 million to the plans in fiscal years 2007, 2006, and 2005, respectively.

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NOTE 14. Income Taxes

The income tax provision, calculated under Statement of Financial Accounting Standard No. 109 (SFAS 109), consists of the following:

<i>(in thousands)</i>	December 30, 2007	December 31, 2006	December 31, 2005
Current:			
Federal	\$ (258)	\$ 2,248	\$ 263
State	4	4	3
Foreign	25,864	43,140	1,842
	<u>25,610</u>	<u>45,392</u>	<u>2,108</u>
Deferred:			
Federal	3,549	3,845	—
Foreign	(12,311)	—	—
	<u>(8,762)</u>	<u>3,845</u>	<u>—</u>
Provision for income taxes	<u>\$ 16,848</u>	<u>\$ 49,237</u>	<u>\$ 2,108</u>

Reconciliation between the Company's effective tax rate and the U.S. Federal statutory rate is as follows:

<i>(in thousands)</i>	Year ended		
	December 30, 2007	December 31, 2006	December 31, 2005
Income (loss) before provision for income taxes	\$ (32,256)	\$ (50,655)	\$ 30,094
Federal statutory tax rate	35%	35%	35%
Income taxes at U.S. Federal statutory rate	(11,290)	(17,729)	10,533
Tax on intercompany dividend	—	45,727	19,871
Adjustment of prior years due to change in estimate	—	29,889	—
Change in liability for unrecognized tax benefit	28,296	—	—
Non-deductible intangible asset amortization and in-process research and development	11,059	12,221	—
Non-deductible stock-based compensation	9,409	9,299	75
Non-deductible items and other	(215)	5,875	(81)
Adjustment of prior year taxes and excess tax credits	23,628	(673)	(3,924)
Incremental recovery on foreign earnings and other rate differentials and investment tax credits	(33,357)	(8,530)	(35,677)
Valuation allowance	(10,682)	(26,842)	11,311
Provision for income taxes	<u>\$ 16,848</u>	<u>\$ 49,237</u>	<u>\$ 2,108</u>

Despite the net loss for 2007, income taxes were incurred primarily from a \$28 million additional accrual relating to an ongoing FIN 48 liability arising from the examination of our historic transfer pricing policies and practices of certain companies within the PMC Group by a certain tax authority. Of the \$28 million increase in our FIN 48 liability, \$13.1 million is related to arrears interest. Our FIN 48 liability is partially offset by available investment tax credits earned in the year of \$18 million. The remainder of the provision for income taxes primarily relates to \$6 million of deferred taxes recorded with respect to a past acquisition and net \$1 million due to various items, including revisions of prior estimates.

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The Company's estimated tax provision rate increased significantly at the end of 2006 due to an increase in its estimated tax liability following receipt in 2007 of a written communication from a tax authority examining the historic transfer pricing policies and practices of certain companies within the PMC-Sierra group. As a result, in 2006, the Company increased its provision for periods prior to 2006 by \$29.9 million.

Significant components of the Company's deferred tax assets and liabilities are as follows:

<i>(in thousands)</i>	December 30, 2007	December 31, 2006
Deferred tax assets:		
Net operating loss carryforwards	\$ 210,718	\$ 215,547
Capital loss	38,780	42,043
Credit carryforwards	68,238	25,216
Reserves and accrued expenses	13,681	16,988
Intangible assets	11,347	8,683
Depreciation and amortization	9,332	8,694
Restructuring and other charges	5,680	6,896
State tax loss carryforwards	8,200	6,439
Deferred income	2,700	2,927
Total deferred tax assets	368,676	333,433
Valuation allowance	(322,750)	(333,433)
Deferred tax liabilities:		
Acquired intangible assets and goodwill	(15,924)	(12,095)
Capitalized technology and other	(355)	(74)
Unrealized gain on investments	(744)	—
Total net deferred taxes	\$ 28,903	\$ (12,169)
Presented on the Consolidated Balance Sheet in the following components:		
Deferred tax assets	\$ 54,676	\$ —
Deferred income taxes	(2,787)	(2,042)
Deferred taxes and other liabilities	(22,986)	(10,127)
	\$ 28,903	\$ (12,169)

At December 30, 2007, the Company has approximately \$599.9 million of federal net operating losses, which will expire through 2027. The Company also has approximately \$273.3 million of state tax loss carryforwards, which expire through 2017. A portion of our net operating losses were used in 2005 and 2006 to reduce the taxes otherwise payable on intercompany dividends. The utilization of a portion of these net operating losses is also subject to ownership change limitations provided by federal and specific state income tax legislation.

Included in the credit carry-forwards are \$37.7 million of investment tax credits, \$16.7 million of federal research and development credits which expire through 2025, \$1.8 million of federal AMT credits which carryforward indefinitely, \$11.5 million of state research and development credits which do not expire, and \$0.5 million of state manufacturer's investment credits which expire through 2011.

Included in the above net operating loss carryforwards are \$23.8 million and \$3.9 million of U.S. federal and state net operating losses related to acquisitions accounted for under the purchase method of accounting. The benefit of such losses, if and when realized, will be credited first to reduce to zero any goodwill related to the respective acquisition, second to reduce to zero other non-current intangible assets related to the respective acquisition, and third to reduce income tax expense.

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Included in the deferred tax assets before valuation allowance are approximately \$145.9 million of cumulative tax benefits related to equity transactions, which will be credited to stockholder's equity if and when realized.

The pretax income from foreign operations was \$30.4 million, \$48.2 million, and \$65.7 million in 2007, 2006, and 2005, respectively. The Company recorded \$7.1 million tax expense related to earnings it repatriated in 2006 to fund the purchase of the Storage Semiconductor Business in 2006. This distribution does not change the Company's intent to indefinitely reinvest undistributed earnings of the Company's foreign subsidiaries and accordingly, no additional provision for federal and state income taxes has been provided thereon. It is not practical to estimate the income tax liability that might be incurred on the remittance of such earnings.

The Company had \$92.5 million of gross unrecognized tax benefits as of January 1, 2007. The total amount of net unrecognized tax benefits that, if recognized, would affect the effective tax rate was \$92.5 million as of January 1, 2007. The Company accrues interest and penalties related to unrecognized tax benefits in its provision for income taxes. As of January 1, 2007, the company had accrued interest and penalties related to unrecognized tax benefits of \$32.6 million. See Note 1 to the consolidated financial statements for additional disclosures related to the adoption of FIN 48.

A reconciliation of the beginning and ending balances of the total amounts of gross unrecognized tax benefits is as follows (in millions):

Gross unrecognized tax benefits at January 1, 2007	\$ 92.5
Increases in tax positions for prior years	15.0
Decreases in tax positions for prior years	(1.3)
Lapse in statute of limitations	(0.7)
Effect of foreign currency loss on translation	20.1
Gross unrecognized tax benefits at December 30, 2007	<u>\$125.6</u>

The total amount of gross unrecognized tax benefits that, if recognized, would affect the effective tax rate was \$125.6 million at December 30, 2007. The Company accrues interest and penalties related to unrecognized tax benefits in its provision for income taxes. At December 30, 2007, the Company had accrued interest and penalties related to unrecognized tax benefits of \$46.8 million.

The Company and its subsidiaries file income tax returns in the U.S. and in various states, local and foreign jurisdictions. The 2004 through 2007 tax years generally remain subject to examination by federal and most state tax authorities. In significant foreign jurisdictions, the 2000 through 2007 tax years generally remain subject to examination by their respective tax authorities. The Company does not reasonably estimate that the unrecognized tax benefit will change significantly within the next 12 months.

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NOTE 15. Segment Information

The Company operates in one segment: networking products. The networking segment consists of internetworking semiconductor devices and related technical service and support to equipment manufacturers for use in their communications and networking equipment.

Enterprise-wide information is provided below in accordance with SFAS 131. Geographic revenue information is based on the location of the customer invoiced. Long-lived assets include property and equipment, goodwill and other intangible assets and other long-term assets. Geographic information about long-lived assets is based on the physical location of the assets.

	Year ended		
	December 30, 2007	December 31, 2006	December 31, 2005
<i>(in thousands)</i>			
Net revenues			
United States	\$ 91,307	\$ 103,144	\$ 98,619
China	89,027	63,797	54,324
Japan	71,941	79,009	40,790
Asia, other	45,890	43,331	20,067
Taiwan	43,754	31,377	19,590
Singapore	42,969	25,195	11,363
Europe and Middle East	40,874	46,922	23,866
Other foreign	23,619	32,217	22,792
Total	<u>\$ 449,381</u>	<u>\$ 424,992</u>	<u>\$ 291,411</u>
	December 30, 2007	December 31, 2006	December 31, 2005
Long-lived assets			
Canada	\$ 18,207	\$ 16,749	\$ 15,990
United States	588,036	629,102	16,603
Other	6,724	5,219	175
Total	<u>\$ 612,967</u>	<u>\$ 651,070</u>	<u>\$ 32,768</u>

During 2007, the Company had two customers whose purchases represented a significant portion of net revenues, based on billing, including contract manufacturers and distributors. Net revenues from one customer represented approximately 12% of net revenues in 2007, 12% in 2006, and 14% in 2005. Net revenues from a second customer were 11% in 2007, and 12% in 2006 and 2005. In 2007 and 2006, the Company had two end customers, Cisco Systems and EMC Corporation, whose purchases represented greater than 10% of our total net revenues (2005 – Cisco Systems).

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NOTE 16. Net Income (Loss) Per Share

The following table sets forth the computation of basic and diluted net (loss) income per share:

<i>(in thousands, except per share amounts)</i>	December 30, 2007	December 31, 2006	December 31, 2005
Numerator:			
Net (loss) income	\$ (49,104)	\$ (99,892)	\$ 27,986
Denominator:			
Basic weighted average common shares outstanding ⁽¹⁾	216,330	203,470	184,098
Effect of dilutive securities:			
Stock options	—	—	5,034
Basic and diluted weighted average common shares outstanding	216,330	203,470	189,132
Basic net (loss) income per share	\$ (0.23)	\$ (0.49)	\$ 0.15
Diluted net (loss) income per share	\$ (0.23)	\$ (0.49)	\$ 0.15

(1) PMC-Sierra, Ltd. Special Shares are included in the calculation of basic weighted average common shares outstanding.

In 2007, the Company had approximately 5.5 million options that were not included in diluted net loss per share because they would be antidilutive.

NOTE 17. Comprehensive (Loss) Income

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

<i>(in thousands)</i>	December 30, 2007	December 31, 2006	December 31, 2005
Net (loss) income	\$ (49,104)	\$ (99,892)	\$ 27,986
Other comprehensive (loss) income:			
Change in net unrealized (losses) gains on investments, net of tax of (2006—\$91 and 2005—\$246)	—	(12)	929
Change in fair value of derivatives, net of tax of \$1,328 in 2007 (2006—\$1,530 and 2005—\$727)	2,564	(2,838)	444
Total	\$ (46,540)	\$ (102,742)	\$ 29,359

ITEM 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.

None.

ITEM 9A. Controls and Procedures.

In evaluating the effectiveness of our internal control over financial reporting as of December 30, 2007, we considered the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”) in *Internal Control-Integrated Framework*. Internal control over financial reporting cannot provide absolute assurance of achieving financial reporting objectives because of its inherent limitations. Internal control over financial reporting is a process that involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failures. Internal control over financial reporting also can be circumvented by collusion or improper management override. Because of such limitations, there is a risk that material misstatements may not be prevented or detected on a timely basis by internal control over financial reporting. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

A material weakness is a control deficiency, or combination of control deficiencies, that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected.

Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures

Our chief executive officer and our chief financial officer evaluated our “disclosure controls and procedures” as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934 as amended (the “Exchange Act”) as of December 30, 2007. They concluded that as of the evaluation date, our disclosure controls and procedures are effective to ensure that information we are required to disclose in reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure, and that such information is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission rules and forms.

Management’s Annual Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) and 15d-15(f) of the Securities Exchange Act of 1934 as amended).

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Our management assessed the effectiveness of our internal control over financial reporting using the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”) in Internal Control – Integrated Framework. Based on our assessment and those criteria, management believes that we maintained effective control over financial reporting as of December 30, 2007.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Deloitte and Touche LLP, the independent registered public accounting firm that audited the financial statements included in this Annual Report, has issued an attestation report on the registrant’s internal control over financial reporting. The report is included herein.

Changes in Internal Controls over Financial Reporting

There were no changes in our internal controls during our last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of PMC-Sierra, Inc.

We have audited the internal control over financial reporting of PMC-Sierra, Inc. and subsidiaries (the “Company”) as of December 30, 2007, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company’s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management’s Annual Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company’s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company’s internal control over financial reporting is a process designed by, or under the supervision of, the company’s principal executive and principal financial officers, or persons performing similar functions, and effected by the company’s board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company’s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company’s assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 30, 2007, based on the criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

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We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements and financial statement schedules as of and for the year ended December 30, 2007 of the Company and our report dated February 22, 2008 expressed an unqualified opinion on those financial statements and financial statement schedules and included an explanatory paragraph regarding the Company's adoption of Financial Accounting Standards Board Interpretation No. 48 "Accounting for Uncertainty in Income Taxes".

/s/ DELOITTE & TOUCHE LLP
Independent Registered Public Accountants
Vancouver, Canada
February 22, 2008

ITEM 9B. Other Information.

None.

PART III

ITEM 10. Directors, Executive Officers and Corporate Governance.

The information concerning our directors and executive officers required by this Item is incorporated by reference from the information set forth in the sections entitled “Election of Directors”, “Code of Business Conduct and Ethics”, “Executive Officers”, and “Section 16(a) Beneficial Ownership Reporting Compliance” in our Proxy Statement for the 2008 Annual Stockholder Meeting.

ITEM 11. Executive Compensation.

The information required by this Item is incorporated by reference from the information set forth in the sections entitled “Director Compensation,” “Executive Compensation,” “Compensation Committee Interlocks and Insider Participation,” and “Compensation Committee Report” in our Proxy Statement for the 2008 Annual Stockholder Meeting.

ITEM 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

The information concerning security ownership of certain beneficial owners that is required by this Item is incorporated by reference from the information set forth in the section entitled “Common Stock Ownership of Certain Beneficial Owners and Management” in our Proxy Statement for the 2008 Annual Stockholder Meeting.

Equity Compensation Plan Information:

The following table provides information as of December 30, 2007 with respect to the shares of our common stock that may be issued under our existing equity compensation plans.

	Number of Securities to be issued upon exercise of outstanding options	Weighted-average exercise price of outstanding options	Number of securities remaining available for future issuance under equity compensation plans
Equity compensation plans approved by security holders (1)	23,440,427	\$ 9.89	22,470,831 (2)
Equity compensation plans not approved by security holders (3)	3,881,078	\$ 8.89	11,251,845
Balance at December 30, 2007	27,321,505	\$ 9.74	33,342,292

- (1) Consists of the 1994 Incentive Stock Plan (the “1994 Plan”) and the 1991 Employee Stock Purchase Plan (the “1991 Plan”).
- (2) Includes 13,940,507 shares available for issuance in the 1994 plan and 8,149,940 shares available for issuance in the 1991 Plan.

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- (3) Consists of the 2001 Stock Option Plan (the “2001 Plan”), which was created to replace a number of stock option plans assumed by us in connection with mergers and acquisitions we completed prior to 2001. The number of options that may be granted under the 2001 Plan equals (i) the number of shares reserved under the assumed stock option plans that were not subject to outstanding or exercised options plus (ii) the number of options that were outstanding at the time the plans were assumed but that have subsequently been cancelled plus (iii) 10 million shares that were added to the plan in 2003. Also includes Passave Inc. 2003 Israeli Option Plan (the “2003 Plan”) and the Passave, Inc 2005 U.S. Stock Incentive Plan (the “2005 Plan”), which were assumed through the Passave acquisition.

In accordance with the term of the 1991 Plan, on January 1, 2008 an additional 2,000,000 options were automatically available for issuance under such plan.

ITEM 13. Certain Relationships and Related Transactions, and Director Independence.

The information required by this Item is incorporated by reference from the information set forth in the section entitled “Executive Compensation Change of Control and Severance Agreements” in our Proxy Statement for the 2008 Annual Stockholder Meeting.

ITEM 14. Principal Accountant Fees and Services

The information required by this Item is incorporated by reference from our Proxy Statement for the 2008 Annual Stockholder Meeting.

PART IV

ITEM 15. Exhibits and Financial Statement Schedules.

(a) 1. Consolidated Financial Statements

The financial statements (including the notes thereto) listed in the accompanying index to financial statements and financial statement schedules are filed within this Annual Report on Form 10-K.

2. Financial Statement Schedules

Financial Statement Schedules required by this item are listed on page 106 of this Annual Report on Form 10-K.

3. Exhibits

The exhibits listed under Item 15(c) are filed as part of this Form 10-K Annual Report.

Table of Contents**(b) Exhibits pursuant to Item 601 of Regulation S-K.**

Incorporated by Reference

<u>Exhibit Number</u>	<u>Description</u>	<u>Form</u>	<u>Date</u>	<u>Number</u>	<u>Filed herewith</u>
3.1	Restated Certificate of Incorporation of the Registrant, as amended on May 11, 2001	10-Q	05/16/2001	3.2	
3.2	Certificate of Designation of Rights, Preferences and Privileges of Series A Participating Preferred Stock of the Registrant	S-3	11/08/2001	3.2	
3.3	Bylaws of the Registrant, as amended	10-Q	11/14/2001	3.2	
4.1	Specimen of Common Stock Certificate of the Registrant	S-3	08/27/1997	4.4	
4.2	Exchange Agreement dated September 2, 1994 by and between the Registrant and PMC-Sierra, Ltd.	8-K	02/19/1994	2.1	
4.3	Amendment to Exchange Agreement effective August 9, 1995	8-K	09/06/1995	2.1	
4.4	Terms of PMC-Sierra, Ltd. Special Shares	S-3	09/19/1995	4.3	
4.5	Preferred Stock Rights Agreement, as amended and restated as of July 27, 2001, by and between the Registrant and American Stock Transfer and Trust Company	10-Q	11/14/2001	4.3	
4.6	Purchase and Sale Agreement dated October 28, 2005, between PMC-Sierra, Inc. and Avago Technologies Pte. Limited	8-K	11/03/2005	2.1	
4.7	Indenture Agreement dated October 26, 2005, between the Company and U.S. Bank National Association, as trustee	8-K	10/26/2005	2.1	
4.8	Agreement and Plan of Merger dated April 4, 2006, between PMC-Sierra, Inc. and Passave Inc.	8-K	04/04/2006	2.1	

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<u>Exhibit Number</u>	<u>Description</u>	<u>Form</u>	<u>Date</u>	<u>Number</u>	<u>Filed herewith</u>
10.1^	1991 Employee Stock Purchase Plan, as amended	10-K	03/01/2007	10.1	
10.2^	1994 Incentive Stock Plan, as amended	10-K	03/01/2007	10.2	
10.3^	2001 Stock Option Plan, as amended	10-K	03/01/2007	10.3	
10.4^	Form of Indemnification Agreement between the Registrant and its directors and officers, as amended and restated	10-K	03/28/03	10.4	
10.5^	Form of Change of Control Agreement by and between the Registrant and the executive officers				X
10.6	Net Building Lease dated May 15, 1996 by and between PMC-Sierra, Ltd. and Pilot Pacific Developments Inc.	10-K	04/14/1997	10.20	
10.7	Building Lease Agreements between WHTS Freedom Circle Partners, LLC and the Registrant	10-Q	08/08/2000	10.36	
10.7	First Amendment to Building Lease Agreements between WHTS Freedom Circle Partners, LLC and the Registrant	10-Q	11/14/2001	10.46	
10.8	Building Lease Agreement between Kanata Research Park Corporation and PMC-Sierra, Ltd.	10-K	04/02/2001	10.44	
10.9	Building Lease Agreement between Transwestern – Robinson I, LLC and PMC-Sierra US, Inc.	10-K	04/02/2001	10.45	
10.10*	Forecast and Option Agreement by and among the Registrant, PMC-Sierra, Ltd., and Taiwan Semiconductor Manufacturing Corporation	10-K	03/20/2000	10.31	
10.11*	Deposit agreement dated January 31, 2000 by and between Chartered Semiconductor Manufacturing Ltd. and the Registrant	10-Q	05/10/2000	10.35	

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<u>Exhibit Number</u>	<u>Description</u>	<u>Form</u>	<u>Date</u>	<u>Number</u>	<u>Filed herewith</u>
10.13*	Technology License Agreement, by and between Weitek Corporation and MIPS Computer Systems, Inc. Assignment Agreement, by and between Weitek Corporation and PMC-Sierra US, Inc. (formerly Quantum Effect Design, Inc.) Amendment No. 1 to the Technology License Agreement, by and between MIPS Technologies, Inc. and PMC-Sierra US, Inc. (formerly Quantum Effect Design, Inc.) dated March 31, 1997	S-3	01/04/2002	10.47	
10.14	Sixth Amendment to Building Lease Agreement between PMC-Sierra, Ltd. and Production Court Property Holdings Inc.	10-Q	11/10/2003	10.1	
10.15	Amendment for Purchase and Sale of Real Property between WHTS Freedom Circle Partners II, L.L.C. and PMC-Sierra, Inc.	10-Q	11/10/2003	10.2	
10.16	Amendment for Purchase and Sale of Real Property between PMC-Sierra, Inc. and WB Mission Towers, L.L.C.	10-Q	11/10/2003	10.3	
11.1	Calculation of earnings per share (1)				X
12.1	Statement of Computation of Ratio of Earnings to Fixed Charges				X
21.1	Subsidiaries of the Registrant				X
23.1	Consent of Deloitte & Touche LLP, Independent Registered Public Accountants				X
24.1	Power of Attorney (2)				X
31.1	Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (Chief Executive Officer)				X
31.2	Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (Chief Financial Officer)				X

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<u>Exhibit Number</u>	<u>Description</u>	<u>Form</u>	<u>Date</u>	<u>Number</u>	<u>Filed herewith</u>
32.1	Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Chief Executive Officer) (furnished, not filed)				X
32.2	Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Chief Financial Officer) (furnished, not filed)				X

* Confidential portions of this exhibit have been omitted and filed separately with the Commission.

^ Indicates management compensatory plan or arrangement required to be filed as an exhibit pursuant to Item 15(c) of Form 10K.

(1) Refer to Note 16 of the consolidated financial statements included in Item 8 of Part II of this Annual Report.

(2) Refer to Signature page of this Annual Report.

(c) Financial Statement Schedules required by this item are listed on page 106 of this Annual Report on Form 10-K.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

PMC-SIERRA, INC.
(Registrant)

Date: February 22, 2008

/s/ Michael W. Zellner

Michael W. Zellner
Vice President, (duly authorized officer)
Chief Financial Officer and
Principal Accounting Officer

POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Robert L. Bailey and Michael W. Zellner, jointly and severally, his attorneys-in-fact, each with the power of substitution, for him in any and all capacities, to sign any amendments to this Report on Form 10-K, and to file the same, with exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, hereby ratifying and confirming all that each of said attorneys-in-fact, or his substitute or substitutes, may or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this Annual Report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

<u>Name</u>	<u>Title</u>	<u>Date</u>
<u>/s/ Robert L. Bailey</u> Robert L. Bailey	President, Chief Executive Officer (Principal Executive Officer) and Chairman of the Board of Directors	February 22, 2008
<u>/s/ Michael W. Zellner</u> Michael W. Zellner	Vice President, Chief Financial Officer (and Principal Accounting Officer)	February 22, 2008
<u>/s/ Richard E. Belluzzo</u> Richard E. Belluzzo	Director	February 21, 2008
<u>/s/ James V. Diller</u> James V. Diller	Director	February 21, 2008
<u>/s/ William H. Kurtz</u> William H. Kurtz	Director	February 21, 2008
<u>/s/ Frank J. Marshall</u> Frank J. Marshall	Director	February 20, 2008
<u>/s/ Jonathan J. Judge</u> Jonathan J. Judge	Director	February 21, 2008
<u>/s/ Michael R. Farese</u> Michael R. Farese	Director	February 21, 2008

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SCHEDULE II—Valuation and Qualifying Accounts

<u>(in thousands)</u>	<u>Balance at beginning of year</u>	<u>Charged to expenses or other accounts</u>	<u>Write-offs</u>	<u>Balance at end of year</u>
Allowance for doubtful accounts:				
December 30, 2007	\$ 1,768	\$ (222)	\$ —	\$ 1,546
December 31, 2006	\$ 1,768	\$ —	\$ —	\$ 1,768
December 31, 2005	\$ 2,665	\$ (897)	\$ —	\$ 1,768
Allowance for obsolete inventory and excess inventory:				
December 30, 2007	\$ 8,409	\$ 2,921	\$ (1,490)	\$ 9,840
December 31, 2006	\$ 8,454	\$ 2,276	\$ (2,321)	\$ 8,409
December 31, 2005	\$ 12,190	\$ (1,904)	\$ (1,832)	\$ 8,454
Allowance for warranty claims:				
December 30, 2007	\$ 4,331	\$ 2,492	\$ (584)	\$ 6,239
December 31, 2006	\$ 3,997	\$ 1,093	\$ (759)	\$ 4,331
December 31, 2005	\$ 3,492	\$ 712	\$ (207)	\$ 3,997

INDEX TO EXHIBITS

<u>Exhibit Number</u>	<u>Description</u>	<u>Page Number</u>
10.5	Form of Change of Control Agreement by and between the Registrant and the executive officers	
12.1	Statement of Computation of Ratio of Earnings to Fixed Charges	
21.1	Subsidiaries of the Registrant	
23.1	Consent of Deloitte & Touche LLP, Independent Registered Public Accountants	
31.1	Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (Chief Executive Officer)	
31.2	Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (Chief Financial Officer)	
32.1	Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Chief Executive Officer) (furnished, not filed)	
32.2	Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Chief Financial Officer) (furnished, not filed)	

**FORM OF
PMC-SIERRA, INC.**

CHANGE OF CONTROL AGREEMENT

THIS CHANGE OF CONTROL AGREEMENT (this “Agreement”), is made by and between PMC-Sierra, Inc. (hereinafter the “Company”), and [Executive Officer] (hereinafter “Executive”) and shall be effective as of [Effective Date] (the “Effective Date”).

WHEREAS, the Company and the Executive desire to enter into an employment agreement governing a constructive or actual termination connected with a change in control of the Company.

NOW, THEREFORE, the Company and Executive, in consideration of the mutual promises set forth herein, hereby agree as follows:

1. Termination Without Cause or Constructive Termination in Connection With a Change in Control. If the Company terminates Executive’s employment without Cause or Executive resigns under circumstances that constitute a Constructive Termination, and a Change in Control (or the signing of a binding agreement which could result in a Change in Control) is reasonably expected to occur within the next 60 days or has occurred in the past two years, then, provided that Executive executes a release in a form substantially similar to Exhibit A (the “Release”) and such Release becomes effective and enforceable in accordance with its terms following the expiration of any applicable revocation period under federal or state law 30 days following the Executive’s Separation from Service, the following will occur:

(i) Executive shall receive (in each case less applicable withholding):

(A) a cash payment equal to 4% of Executive’s then-current Base Salary for each full month during which Executive was employed by the Company or its affiliates (up to a maximum total payment equal to two times Executive’s then-current Base Salary) payable in a series of 12 equal monthly installments beginning on the first regular payday for the Company’s salaried employees on which the Release is effective within the 60-day period following the date of the Executive’s Separation from Service. Such cash payments shall be treated as a right to a series of separate payments for purposes of Section 409A of the Code, and each such payment made during the period commencing with the date of Executive’s Separation from Service and ending March 15 of the succeeding calendar year is hereby designated a “Short-Term Deferral Payment” for purposes of Section 5 of this Agreement and shall be paid during that period whether or not Executive is deemed to be a key employee under Section 5 at the time of Executive’s Separation from Service;

(B) a cash payment equal to 2% for every month the Executive was employed by the Company of the total of bonuses received by Executive for the last Short Term Incentive Plan (“STIP”) periods totaling 12 months, up to a maximum total payment equal to 100% of the amount of bonuses received by Executive under STIP for the last periods totaling 12 months. For example: if STIP bonuses are measured on a semi-annual

basis, and in August of a given year after 47 months of employment the Executive experiences a Separation of Service that triggers payout under this Agreement, then the total of bonuses considered are those paid for the STIP periods of July through December of the previous year and January through June of the current year. If the Company's performance targets for STIP were not met in the second half of the previous year resulting in no bonus payout for that period, but targets were exceeded for the January – June period, the calculation for purposes of this Section of the Agreement would be: $(2\% \times 47 = 94\%) \times [\$0 + (100\% \text{ of amount paid for second period})]$. This payment will be payable in a series of 12 equal monthly installments beginning on the first regular payday for the Company's salaried employees on which the Release is effective within the 60-day period following the date of the Executive's Separation from Service. Such cash payments shall be treated as a right to a series of separate payments for purposes of Section 409A of the Code, and each such payment made during the period commencing with the date of Executive's Separation from Service and ending March 15 of the succeeding calendar year is hereby designated a "Short-Term Deferral Payment" for purposes of Section 5 of this Agreement and shall be paid during that period whether or not Executive is deemed to be a key employee under Section 5 at the time of Executive's Separation from Service;

(C) upon the Separation from Service, acceleration in vesting by twelve (12) months of all equity awards (options and restricted stock units) that are unvested as of the Separation of Service; and

(D) twelve (12) months from the Separation from Service to exercise all vested options or the remaining term of the option, whichever is shorter.

(ii) As an executive employee, Executive will be extensively involved in high-level decisions related to the competitive design, development, marketing, positioning and sale of the Company's products and services. Executive acknowledges and agrees that such participation requires unlimited access to highly sensitive proprietary information (as described in the At Will Employment, Confidential Information, Invention Assignment, And Arbitration Agreement entered into by and between Executive and the Company, the "Confidentiality Agreement"), including confidential information and trade secrets related to the development of the Company's business model, competitive strategies, product and/or services positioning, marketing, and other information that would be highly injurious if divulged to or used by a Competitor of the Company. Accordingly, until one year after Executive's Separation from Service, Executive will not, as an employee, agent, consultant, advisor, independent contractor, general partner, officer, director, stockholder, investor or in any other capacity directly or indirectly, engage in, work for, provide services or assistance to, or own a more than 25% voting interest in any Competitor of the Company.

(iii) Until one year after Executive's Separation from Service, Executive will not directly or indirectly induce, encourage, solicit, influence or attempt to influence any employee, contractor or other service provider of the Company or its subsidiaries to cease providing services for the Company or its subsidiaries for any reason, or to employ, interview or arrange to have business opportunities offered to any such individual.

(iv) Executive's agreements in Sections 1(ii) and 1(iii) are severable, and each will still be enforceable even if another is not enforceable. If a court determines that any provision of this section exceeds the maximum scope, time period, or geographic area that the court deems enforceable, the scope, time period, or geographic area shall be deemed the maximum that the court considers reasonable.

2. Exclusive Remedy. This Agreement specifies all of Executive's compensation and benefits resulting from actual or Constructive Termination in connection with a Change of Control. Executive shall not be entitled to any other compensation and benefits from the Company except to the extent provided under any written Company benefit plan, stock option or other equity agreement or indemnification agreement, or as may be required under applicable law.

3. Definitions.

(i) "Base Salary" means Executive's then-current cash compensation paid on the Company's standard salary payment schedule, less applicable withholding.

(ii) "Cause" means (A) gross dereliction of duties which continues after at least two notices, each 30 days apart, from the Chief Executive Officer, specifying in reasonable detail the tasks which must be accomplished and a timeline for their accomplishment to avoid termination for Cause, (B) willful and gross misconduct which injures the Company, (C) willful and material violations of laws applicable to the Company, or (D) embezzlement or theft of Company property.

(iii) "Change of Control" means the occurrence of any of the following events:

(A) Any "person" or "group" as such terms are defined under Sections 13 and 14 of the Securities Exchange Act of 1934 ("Exchange Act") (other than the Company, a subsidiary of the Company, or a Company employee benefit plan) is or becomes the "beneficial owner" (as defined in Exchange Act Rule 13d-3), directly or indirectly, of Company securities representing 50% or more of the combined voting power of the Company's then outstanding securities.

(B) The closing of: (1) the sale of all or substantially all of the assets of the Company if the holders of Company securities representing all voting power for the election of directors before the transaction hold less than a majority of the total voting power for the election of directors of all entities which acquire such assets, or (2) the merger of the Company with or into another corporation if the holders of Company securities representing all voting power for the election of directors before the transaction hold less than a majority of the total voting power for the election of directors of the surviving entity.

(C) The issuance of securities, which would give a person or group beneficial ownership of Company securities representing 50% or more of all voting power for the election of directors.

(D) A change in the board of directors such that the incumbent directors and nominees of the incumbent directors are no longer a majority of the total number of directors.

(iv) "Competitor" means a business anywhere in the world which derives ten percent (10%) or more of its revenues from developing, manufacturing, marketing or selling any products which directly compete with the products manufactured, marketed or sold by the Company or its subsidiaries as at the date Executive's employment or consulting agreement (if applicable) terminates.

(v) "Constructive Termination" means Executive's resignation following the occurrence of any of the following events, without Executive's approval: (A) a material reduction in Executive's Base Salary, target bonus or benefits, other than a reduction that is implemented across-the-board to all employees at Executive's level; (B) a material reduction in Executive's title, authority or responsibilities, other than as a result of a transfer to a subsidiary of the Company; or (C) the requirement that Executive relocate to a place of employment more than 100 miles from both the then current Company Corporate Headquarters (currently located in Santa Clara, CA) and the then current Company Operation Headquarters (currently located in Burnaby, British Columbia)(for example, a requirement that the Executive relocate his place of employment from Company Corporate Headquarters in Santa Clara, CA to Company Operation Headquarters in Burnaby, British Columbia (or vice versa) would not allow the Executive to resign pursuant to a Constructive Termination, however, a requirement that the Executive relocate to Santa Barbara, CA from Company Corporate Headquarters in Santa Clara, CA would allow the Executive to resign pursuant to a Constructive Termination); provided, however, the Executive must provide written notice to the Company of the existence of a condition described in clause (A), B) or (C) within ninety (90) days of the initial existence of the condition, and if within thirty (30) days of the Company's receipt of such notice (or, if later, Executive's actual termination of employment) the Company remedies such condition, a Constructive Termination will not be deemed to have occurred.

(vi) "Separation from Service" means the cessation of Executive's status as an employee of the Company and shall be deemed to occur at such time as the level of the bona fide services Executive is to perform as an employee (or as a consultant or other independent contractor) permanently decreases to a level that is not more than 20% of the average level of services Executive rendered as an employee during the immediately preceding 36 months (or such shorter period for which the Executive may have rendered such service). Any such determination as to Separation from Service, however, shall be made in accordance with the applicable standards of the Treasury Regulations issued under Section 409A of the Code.

4. **Golden Parachute Excise Tax.** If the benefits provided for in this Agreement or otherwise payable to Executive constitute "parachute payments" within the meaning of Section 280G of the Code and will be subject to the excise tax imposed by Section 4999 of the Code (the "Excise Tax"), then Executive's severance benefits under Section 1 shall be (i) delivered in full, or (ii) delivered as to such lesser extent which would result in no portion of such severance benefits being subject to the Excise Tax, whichever of the foregoing amounts, taking into account the applicable federal, state and local income taxes and the Excise Tax, results in the receipt by Executive on an after-tax basis, of the greatest amount of severance benefits. Unless the Company and Executive otherwise agree in writing, any determination required under this Section 4 shall be made in writing in good faith by the accounting firm serving as the Company's independent public accountants immediately prior to the Change of Control (the "Accountants"). For purposes of making the calculations required by this Section 4, the Accountants may make reasonable assumptions and approximations concerning applicable taxes and may rely on reasonable, good faith interpretations concerning the application of Sections 280G and 4999 of the Code. The Company and Executive shall furnish to the Accountants such information and documents as the Accountants may reasonably request in order to make a determination under this Section. The Company shall bear all costs the Accountants may reasonably incur in connection with any calculations contemplated by this Section 4.

5. Section 409A. (i) Notwithstanding any provision to the contrary in this Agreement (other than Section 5 (ii) below), no payments or benefits to which the Executive becomes entitled under Section 1 of this Agreement shall be made or paid to the Executive prior to the *earlier* of (A) the expiration of the 6-month period measured from the date of his Separation from Service or (B) the date of the Executive's death, if the Executive is deemed at the time of such Separation from Service a "key employee" within the meaning of that term under Code Section 416(i) and such delayed commencement is otherwise required in order to avoid a prohibited distribution under Code Section 409A(a)(2). Upon the expiration of the applicable Code Section 409A(a)(2) deferral period, all payments deferred pursuant to this Section 5 shall be paid in a lump sum to the Executive, and any remaining payments due under this Agreement shall be paid in accordance with the normal payment dates specified for them herein.

(ii) The six month holdback set forth in Section 5(i) above shall not be applicable to (A) any severance payments under Section 1 that qualify as Short-Term Deferral Payments and (B) any remaining portion of the severance payments due Executive under Section 1 to the extent (1) the sum of the Executive's annualized compensation for the taxable year preceding the taxable year of Executive's Separation from Service and (2) the maximum amount that may be taken into account under a qualified plan pursuant to Section 401(a)(17) of the Code for the year in which Executive has a Separation from Service, provided such severance payments are paid no later than the last day of Executive's second taxable year following the taxable year in which the Separation from Service occurs.

6. Assignment. This Agreement shall bind and benefit (i) Executive's heirs, executors and legal representatives upon Executive's death to the extent the benefit is due and payable at the time of Executive's death and (ii) any successor of the Company. Any such successor of the Company shall be deemed substituted for the Company under the terms of this Agreement for all purposes. "Successor" shall include any person, firm, corporation or other business entity which at any time, whether by purchase, merger or otherwise, directly or indirectly acquires all or substantially all of the assets or business of the Company. Executive has no other right to assign this Agreement and any such attempted assignment is void.

7. Notices. All notices, requests, demands and other communications under this Agreement shall be in writing and shall be deemed given if: (i) delivered personally, (ii) one day after being sent by Federal Express or a similar commercial overnight service, or (iii) three days after being mailed by registered or certified mail, return receipt requested, prepaid and addressed to Company at its principal office, attention: Chief Executive Officer, or to Executive at his last principal residence known to the Company, or at such other addresses as the parties may designate by written notice.

8. Severability. In the event that any provision hereof becomes or is declared by a court of competent jurisdiction to be illegal, unenforceable or void, this Agreement shall continue in full force and effect without said provision.

9. Entire Agreement. This Agreement represents the entire agreement and understanding between the Company and Executive concerning payments to Executive in the event of a Change of Control and supersedes any and all prior change of control agreements between the Company and Executive, but does not supersede any other agreements between Company and Executive, including but not limited to, the Confidentiality Agreement, the Indemnification Agreement entered into by and between the Executive and the Company, and any restricted stock purchase

agreement, restricted stock unit agreement, stock option agreement or other equity award agreement entered into pursuant to the Company's stock plans, except as expressly provided herein. In case of conflict between any of the terms and conditions of this Agreement and the documents herein referred to, the terms and conditions of this Agreement shall control.

10. Arbitration and Equitable Relief.

(i) Any dispute or controversy arising out of, relating to, or in connection with this Agreement, or the interpretation, validity, construction, performance, breach, or termination thereof shall be settled by arbitration to be held in Santa Clara, California in accordance with the National Rules for the Resolution of Employment Disputes then in effect of the American Arbitration Association (the "Rules"). The arbitrator may grant injunctions or other relief in such dispute or controversy. The decision of the arbitrator shall be final, conclusive and binding on the parties to the arbitration. Judgment may be entered on the arbitrator's decision in any court having jurisdiction.

(ii) The arbitrator shall apply Delaware law to the merits of any dispute or claim, without reference to rules of conflict of law. The arbitration proceedings shall be governed by federal arbitration law and by the Rules, without reference to state arbitration law.

(iii) The Company shall pay the costs and expenses of such arbitration. Each party shall separately pay its counsel fees and expenses.

(iv) Executive understands that nothing in this Agreement modifies Executive's at-will status. Either the Company or Executive can terminate the employment relationship at any time, with or without cause.

11. No Oral Modification, Cancellation or Discharge. This Agreement may only be amended, canceled or discharged in writing signed by Executive and the Chairman and Chief Executive Officer of the Company.

12. Withholding. The Company shall be entitled to withhold, or cause to be withheld, from payment any amount of withholding taxes required by law with respect to payments made to Executive in connection with his employment hereunder.

13. Governing Law. This Agreement shall be governed by the laws of the State of Delaware (with the exception of its conflict of laws provisions).

[Remainder of Page Intentionally Left Blank]

14. Representations. Executive represents that he has had the opportunity to discuss this matter with and obtain advice from his private attorney, has had sufficient time to, and has carefully read and fully understands all the provisions of this agreement, and is knowingly and voluntarily entering into this Agreement.

PMC-SIERRA, INC.:

Robert L. Bailey
Chairman, President and CEO

Date

EXECUTIVE:

[Executive Officer]

Date

EXHIBIT A

FORM OF GENERAL RELEASE OF ALL CLAIMS

On behalf of myself, my heirs, executors, administrators and assigns, I hereby make the following agreements and acknowledgements in exchange for benefits to be received by me under my Change of Control Agreement (the "Agreement"):

1. I agree that I fully and forever release and discharge the Company and all of its parents, divisions, subsidiaries, affiliates, related entities, and their predecessors, successors, and past and present officers, directors, shareholders, employees, agents, partners, attorneys, benefit plans, insurers, and representatives, (hereinafter "Releasees") from any and all claims of whatever nature, except as noted below, whether known or unknown, which exist or may exist on my behalf against Releasees as of the date of this Agreement, including but not limited to any and all tort claims, contract claims, equitable claims, breach of fiduciary duty claims, ERISA claims, wrongful termination claims, public policy claims, retaliation claims, statutory claims, personal injury claims, emotional distress claims, invasion of privacy claims, defamation claims, fraud claims, quantum meruit claims, and any and all claims arising under any federal, state or other governmental statute, law, regulation or ordinance covering discrimination in employment, including but not limited to Title VII of the Civil Rights Act of 1964, as amended, the Americans with Disabilities Act, the Age Discrimination in Employment Act, and the California Fair Employment and Housing Act, including race, color, religious creed, national origin, ancestry, physical or mental disability, medical condition, marital status, sex, age, harassment, or retaliation. Notwithstanding any provisions and covenants in this paragraph, I am not waiving any claim I may have against Releasees to: (a) unemployment; (b) state disability and/or workers' compensation insurance benefits; (c) my vested rights upon termination in certain of the Company's group benefit plans pursuant to the federal law known as COBRA and the terms of the Company's benefit plans; and (d) any right to indemnification I may have under the Company's Bylaws or under that certain Indemnification Agreement dated as of February 1, 2007 between the Company and me.

2. I agree that I fully and forever waive any and all rights and benefits conferred upon me by the provisions of Section 1542 of the Civil Code of the State of California or any other similar state statute, which states as follows (parentheticals added):

A general release does not extend to claims which the creditor [i.e., me] does not know or suspect to exist in his favor at the time of executing the release, which if known by him must have materially affected his settlement with the debtor [i.e., the Company].

I understand and agree that this means that if, hereafter, I discover facts different from or in addition to those which I now know or believe to be true, that the waivers and releases of this General Release shall be and remain effective in all respects subject to the exceptions in Section 1, notwithstanding such different or additional facts or the discovery of such fact.

3. I agree that neither the fact nor any aspect of this General Release is intended, or should be construed at any time, to be an admission of liability or wrongdoing by either myself or by the Company.

4. I agree that if any provision, or portion of a provision, of this General Release is, for any reason, held to be unenforceable, that such unenforceability will not affect any other provision, or portion of a provision, and this General Release shall be construed as if such unenforceable provision or portion had never been contained herein.

5. I agree that if I am receiving benefits under Section 2 of the Agreement and am not separating from the Company at this time and that if I subsequently receive other separation benefits under the Agreement because of a subsequent Change of Control or for a different event under a subsequent agreement, I will again be required to sign a general release.

6. I understand that I may have twenty-one (21) days after receipt of this General Release within which I may review and consider it, and should discuss it with an attorney of my own choosing, and decide whether or not to sign this General Release. I also understand that, for the period of seven (7) days after I sign this General Release, I may revoke it by delivering a written notification of my revocation, no later than the seventh day, to:

General Counsel
3975 Freedom Circle, #100
Santa Clara, CA 95054
fax: 408-239-8166

I further understand that the Effective Date of this General Release will be the eighth day after I have signed it, *provided that* I have delivered it to the Company and have not revoked it during the seven days after I signed it.

7. This General Release, in all respects, shall be interpreted, enforced and governed by and under the laws of the State of Delaware.

8. This General Release contains the entire agreement between the Company and me with respect to any matters referred to herein.

I HAVE READ THIS GENERAL RELEASE; I UNDERSTAND IT AND KNOW THAT I AM GIVING UP IMPORTANT RIGHTS; I AM AWARE OF MY RIGHT TO CONSULT WITH AN ATTORNEY OF MY OWN CHOOSING BEFORE SIGNING IT AND I HAVE BEEN ENCOURAGED TO CONSULT WITH SUCH AN ATTORNEY; AND I SIGN IT VOLUNTARILY:

Signed: _____, 20__.

Employee's Signature:

Print Name:

PMC-SIERRA, INC.
COMPUTATION OF RATIO OF EARNINGS TO FIXED CHARGES

	Year Ended				
	December 30, 2007	December 31, 2006	December 31, 2005	December 26, 2004	December 28, 2003
Earnings:					
(Loss) income before income taxes and before income from equity investees	\$ (32,256)	\$ (50,655)	\$ 30,094	\$ 48,358	\$ (16,703)
Fixed charges:					
Interest expense and amortization of debt issuance costs	6,105	5,931	1,571	3,454	10,547
Rental expense interest factor ⁽¹⁾	3,601	3,503	3,047	3,083	4,122
Total fixed charges	9,706	9,434	4,618	6,537	14,669
Earnings (loss) available to cover fixed charges ⁽²⁾	\$ (22,550)	\$ (41,221)	\$ 34,712	\$ 54,895	\$ (2,034)
Ratio of earnings to fixed charges	—	—	7.5x	8.4x	—

The ratio of earnings to fixed charges was computed by dividing earnings by fixed charges for the periods indicated. Earnings consist of income (loss) before provision for income taxes less income from equity investees plus fixed charges. Fixed charges consist of interest charges, amortization of debt issuance costs, and that portion of rental expense that the Company believes to be a reasonable approximation of the interest factor included in rental expense.

- (1) The portion of operating lease rental expense that the Company believes to be a reasonable approximation of the interest factor is deemed to be one-third of total operating lease rental expense.
- (2) Earnings were inadequate to cover fixed charges by \$32.3 million, \$50.7 million and \$16.7 million for fiscal years ended December 30, 2007, December 31, 2006 and December 28, 2003 respectively.

PMC-SIERRA, INC.
LIST OF SUBSIDIARIES

1. PMC-Sierra Ltd., organized under the laws of British Columbia, doing business only under its official name, PMC-Sierra.
2. PMC-Sierra US, Inc., organized under the laws of Delaware, doing business only under its official name, PMC-Sierra, or under PMC-Sierra, Inc.
3. Palau Acquisition Corporation, organized under the laws of Delaware, doing business only under its official name, PMC-Sierra, or under PMC-Sierra, Inc.
4. Passave, Inc., organized under the laws of Delaware, doing business only under its official name, PMC-Sierra, or under PMC-Sierra, Inc.
5. PMC-Sierra International, Inc., organized under the laws of Barbados, doing business only under its official name, PMC-Sierra.

**CONSENT OF DELOITTE & TOUCHE LLP, INDEPENDENT
REGISTERED PUBLIC ACCOUNTANTS**

We consent to the incorporation by reference in the Registration Statements on Form S-3 (Nos. 333-44204, 333-34648, 33-86930, 33-90392, 33-96620, 33-97490, and 333-132447) and on Form S-8 (Nos. 333-45118, 333-40508, 333-44212, 33-41027, 333-142980, 333-13387, 333-13359, 333-13357, 33-80988, 333-56244, 333-48110, 333-35276, 333-34622, 333-94999, 333-92885, 333-87039, 333-55983, 333-55991, 333-34671, 333-81414, 333-102747, 33-80992, 33-94790, 333-133830, 333-115123 and 333-128427) of our report dated February 22, 2008 relating to the consolidated financial statements and financial statement schedules of PMC-Sierra Inc. (which report expressed an unqualified opinion and includes an explanatory paragraph relating to the Company's adoption of Statement of Financial Accounting Standard No. 123(R) "Share-Based Payment" and Financial Accounting Standards Board Interpretation No. 48 "Accounting for Uncertainty in Income Taxes") and the effectiveness of internal control over financial reporting appearing in the Annual Report on Form 10-K of PMC-Sierra Inc. for the year ended December 30, 2007.

/s/ DELOITTE & TOUCHE LLP
Independent Registered Public Accountants
Vancouver, Canada
February 22, 2008

CERTIFICATION

I, Robert L. Bailey, certify that:

1. I have reviewed this annual report on Form 10-K of PMC-Sierra, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13-a 15(f) and 15d-15(f)) 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) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - 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 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: February 21, 2008

/s/ Robert L. Bailey

Robert L. Bailey
President and Chief Executive Officer

CERTIFICATION

I, Michael W. Zellner, certify that:

1. I have reviewed this annual report on Form 10-K of PMC-Sierra, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - 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 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

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- 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: February 21, 2008

/s/ Michael W. Zellner
Michael W. Zellner
Vice President
Chief Financial Officer and
Principal Accounting Officer

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

I, Robert L. Bailey, hereby certify, in accordance with 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, in my capacity as an officer of PMC-Sierra, Inc. ("PMC"), that, to my knowledge, the Annual Report of PMC on Form 10-K for the annual period ended December 30, 2007, fully complies with the requirements of Section 13 (a) or 15(d) of the Securities Exchange Act of 1934 and that the information contained in such report fairly presents, in all material respects, the financial condition and results of operations of PMC.

Date: February 21, 2008

By: /s/ Robert L. Bailey
Robert L. Bailey
President and Chief Executive Officer

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

I, Michael W. Zellner, hereby certify, in accordance with 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, in my capacity as an officer of PMC-Sierra, Inc. ("PMC"), that, to my knowledge, the Annual Report of PMC on Form 10-K for the annual period ended December 30, 2007, fully complies with the requirements of Section 13 (a) or 15(d) of the Securities Exchange Act of 1934 and that the information contained in such report fairly presents, in all material respects, the financial condition and results of operations of PMC.

Date: February 21, 2008

By: /s/ Michael W. Zellner
Michael W. Zellner
Vice President
Chief Financial Officer and
Principal Accounting Officer

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