

AUSPEX ANNUAL REPORT

Nasdaq: ASPX

edition #1/☆☆☆☆

YEAR ENDED JUNE 30, 1997

<http://www.auspex.com>

It's All About Data

Auspex's Continuous Data Access Focus Gives CIOs New Solutions for Managing Network Data

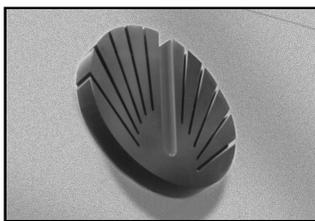
By Bruce N. Moore

President and Chief Executive Officer

There's a big problem just appearing on the radar screen of most Chief Information Officers today, and it's a problem that threatens the very productivity and profitability of the enterprise.

If the challenge was only that of providing hundreds or thousands of users with shared

access to critical information, it would be big enough. But it's far more substantial than that. The type of data residing on the network of any given enterprise is vastly more complex than just a few years ago, and there's a lot more of it. From megabytes, to gigabytes, to terabytes needing to be stored, managed and protected on one or many networked servers.



The networks themselves are no longer simple to manage, with UNIX and a growing number of Windows NT clients all demanding access to network data as if it were on the desktop. And, given the reality of global business, the information must be available to anyone, from anywhere 'round the clock—24 x 365.

No time for downtime. No time for backups. No tolerance for anything less than **continuous data access**.

The issues surrounding data management for the enterprise are numerous, and at Auspex we've been fortunate enough to have visibility to these key problems. We have taken

advantage of this valuable lead time to develop a strategy that is aligned with the objectives of our customers. And if managing enterprise data more effectively is not an issue for them today, it probably will be tomorrow. We're focused on the solutions our customers—the Chief Information Officers and Information Systems Managers of leading global enterprises—have come to rely on us to provide.

Managing the NT Migration— "It's Not Just UNIX Anymore"

For customers faced with the challenge of managing data that is shared by UNIX and NT clients, or for those who are considering an eventual shift from UNIX to NT, Auspex is committed to providing the products and support they need to make that transition a safe and successful one. NetServices, our bilingual server, will allow UNIX and NT clients to share files on the same platform with the kind of reliability, performance and scalability they have come to expect in a UNIX-only environment.

Auspex also has under development a native NT server that will, we believe, bring a new level of performance to the NT server market. This product will enhance the performance and extend the scalability of NT through a powerful application of our patented Functional Multiprocessing (FMP) architecture. We believe the NT market presents an attractive opportunity for Auspex to apply our FMP architecture in much the same way as we did in the UNIX market.

Server Consolidation— "NT Is Heading the Way of UNIX"

What was once common wisdom, that more users, more applications, and more data meant the need for more file servers, has been dispelled. Network performance slows under the weight of its own complexity. Systems administrators spend their days reacting to problems, instead of proactively managing their systems for optimal performance. And, as organizations increasingly must support both UNIX and NT clients seeking to share data, server consolidation is becoming a critical issue.

Whether the customer's environment is UNIX, a combination of UNIX and NT, or NT alone, we believe that data consolidation offers many benefits over the life cycle of the data and the underlying infrastructure. But consolidation only works if a server has the performance, reliability and scalability to meet the challenge of continuous data access. Fortunately, that's where Auspex excels. By leveraging our FMP architecture, we will bring the same value proposition to NT—improved scalability and networking performance—in order to reduce the complexity and overall cost associated with managing multiple NT servers.

High Availability— "Information Is Only Useful if It's Available"

High availability is where Auspex has made its mark, and with good reason. We know that all the network information in the world means nothing if it is not accessible. And the price of downtime is incredibly high. In the world of system availability, 99% uptime equates to 88 hours of unplanned downtime per year.

At Auspex, our aim is considerably higher. For the year ended June 30, 1997,

Auspex servers at customer production sites had measured uptime of 99.989%—about one hour of unplanned downtime per year. For customers using Auspex ServerGuard, measured uptime exceeded 99.999%—that's about six minutes of unplanned downtime.

Auspex's emphasis on high availability—in both our hardware and our software products—complements our focus on continuous data access.

Enterprise Data Management— "The 500 Pound Gorilla in the Data Center"

The explosive growth in network storage and the need for 'round-the-clock access to information has effectively eliminated the available window in which to backup and protect enterprise data. We believe that this will be one of the most pressing issues for CIOs and IS Managers within the next few years.

Enabling continuous access to enterprise data is a major strategic focus for Auspex. The acquisition of Alphasat, Inc. in June 1997 is a key component in this strategy. The acquisition of Alphasat will significantly speed implementation of Auspex's new enterprise-class data management solutions that complement the company's multi-terabyte servers and current high-availability software products. Our strategy in the coming year will be to continue to develop innovative solutions for enterprise data management and, specifically, products that will safeguard and provide our customers with continuous and transparent access to their data. We believe it's a strategy that offers Auspex tremendous opportunity for long-term growth.

FINANCIAL HIGHLIGHTS

Auspex's Revenues Up 24% — Top \$200 Million for Fiscal 1997

Company to Continue Strategic Investments in NT and Enterprise Data Management in Fiscal 1998

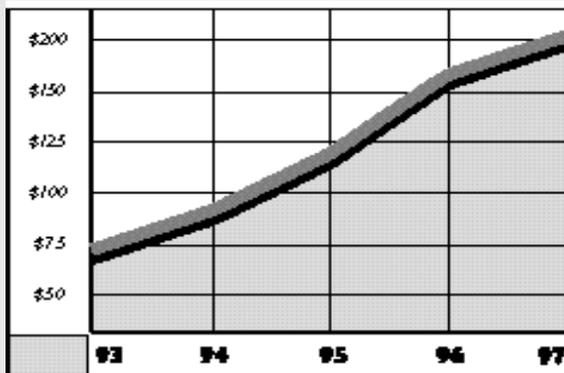


By Kent L. Robertson
Chief Financial Officer

For the year ended June 30, 1997, Auspex's revenues totaled \$202.5 million, up 24% over fiscal 1996. The company's financial results for 1997 include the impact of a one-time charge of \$7.4 million, or \$0.29 per share, related to the acquisition of Alphatronix, Inc. Excluding this charge for in-process R&D, Auspex's net income was \$20.8 million, or \$0.81 per share, for fiscal 1997 compared with net income of \$19.8 million, or \$0.77 per share, for fiscal 1996. Including the one-time charge, fiscal 1997 net income totaled \$13.4 million, or \$0.52 per share.

Auspex made significant investments in fiscal 1997 to support planned new product introductions in the company's primary UNIX-based market, as well as NT and enterprise data management. While we anticipate modest revenue growth in the first half of fiscal 1998, Auspex will continue to ramp its investments in all parts of the business. These investments will dampen short-term earnings, but we believe they are essential to the strategic repositioning of the company.

REVENUE IN MILLIONS



Auspex ended fiscal 1997 with a strong balance sheet, no debt and \$60.9 million in cash and short-term investments with which to fund its continued growth.

—Kent L. Robertson
Chief Financial Officer

FINANCIAL HIGHLIGHTS

in thousands, except per share amounts



AUSPEX SYSTEMS, INC.

Fiscal Year 1997

FISCAL YEAR (JUNE 30)	1997	1996	1995	1994	1993
Revenues	\$ 202,486	\$ 162,640	\$ 115,625	\$ 83,280	\$ 73,508
Net Income	\$ 13,420*	\$ 19,830	\$ 12,411	\$ 8,318	\$ 8,126
Net Income per Share	\$ 0.52*	\$ 0.77	\$ 0.51	\$ 0.34	\$ 0.36

* Includes the impact of a one-time charge of \$7.4 million, or \$0.29 per share, related to the acquisition of Alphatronix, Inc.

~ Special Note ~

This document includes forward-looking statements relating to anticipated revenue growth, anticipated product introductions and performance in the Japanese market.

Actual results could differ materially from those contemplated by any such forward-looking statements due to a number of factors, including the Company's ability to develop and deliver new products on schedule, market acceptance of such products, the impact of competitive products and pricing, general economic conditions, and the factors set forth starting on page A17 of this annual report.

NT STRATEGY

NT and the Enterprise

By Paul R. Gifford

Vice President of Product Development

When it comes to Windows NT and UNIX, today's business technology environment is not an either/or world. It is both.

Today's CIO typically views the corporate Information Technology infrastructure as needing to support three distinct "tiers" or levels in their organization—the desktop, workgroup or departmental-level applications, and the enterprise-level application. With such a networked computing environment, UNIX servers are seen as delivering

benefits, NeTservices provides enterprise-level consolidation for UNIX and NT data; streamlined systems administration; secure, flexible file sharing among UNIX and NT users; and high-performance, native shared file services. We believe NeTservices will offer a premier solution for deploying enterprise-level shared file services for mixed UNIX and NT environments.

Beyond addressing the needs of organizations that are managing a complete or partial migration to NT, the larger dedicated NT market offers another significant opportunity.



The challenge for supporting both UNIX and NT clients seeking to share data is finding a solution that offers seamless integration without compromising system performance, availability of data, or increasing system administrative costs.

the requisite degree of performance, high availability and scalability for enterprise-level application and file services. At the same time, Microsoft Windows is the *de facto* standard operating environment for the desktop, and as companies network their Windows desktop systems, the natural choice for the workgroup server platform is rapidly becoming Windows NT.

For companies that have traditionally utilized UNIX clients to support their applications, the challenge for supporting both UNIX and NT clients seeking to share data is finding a solution that offers seamless integration without compromising system performance, availability of data, or increasing system administrative costs.

NeTservices for Mixed UNIX and NT Environments

In response to this need, Auspex has introduced NeTservices, which will deliver enterprise-class file services that allow data consolidation and file sharing in a mixed UNIX and NT environment. Among its many

The UNIX network file server market is approximately \$4 billion today and growing, as companies continue to invest in support of their UNIX technology infrastructure. At the same time, the Windows NT file server market is expected to grow at a rapid rate, reaching \$4 billion by the year 2000, according to independent industry research. By embracing NT, Auspex has doubled its potential available market.

Dedicated NT Server

NT is also expected to experience a pattern of server consolidation similar to the UNIX market as more organizations realize the benefits of improved systems administration, greater network efficiencies, higher levels of system availability, improved productivity and lower costs. Auspex's dedicated NT product will enable the company to provide the same high-performance, high-availability solutions for continuous data access in NT as it has done so successfully in the UNIX market.



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—Paul R. Gifford

Vice President of Product Development

TO OUR STOCKHOLDERS

* * *

"The past year has been one of growth, and of change, at Auspex. Fiscal 1997 marked a year when we strategically repositioned the company and realigned our goals to reflect the critical need of our customers — who seek nothing less than comprehensive solutions that give them continuous, shared access to their network data. I believe that the direction we have charted, and the investments we are making, position Auspex very well going forward."

Bruce N. Moore
Auspex President and Chief Executive Officer

Revenues Top \$200 Million, Level of Investment Increases

For the fiscal year ended June 30, 1997, Auspex's revenues totaled \$202.5 million, up 24% over fiscal 1996. The company sharply increased its level of investments in order to support major new product introductions scheduled for fiscal 1998 and beyond, and acquired Alphantronix, Inc., a key component in the company's new focus on continuous data access and enterprise data management.

Excluding a one-time charge related to the Alphantronix



creation of a new Auspex K.K. subsidiary, and the hiring of a seasoned executive to expand the company's Asia/Pacific operations.

The emphasis in fiscal 1997 was on strategically repositioning the company to take advantage of the explosive growth in NT and the growing demand for solutions to manage increasingly complex network data.

acquisition, net income was \$20.8 million, or \$0.81 per share, for fiscal 1997 compared with net income of \$19.8 million, or \$0.77 per share for fiscal 1996. Including the one-time charge, fiscal 1997 net income totaled \$13.4 million, or \$0.52 per share.

Strong performance in North America and Europe drove revenue growth in fiscal 1997. Japan was weak, with results impacted by the major reorganization of our OEM partner. However, we took a number of steps in the fourth quarter of fiscal 1997 that should position Japan for improved performance, including the realignment of distribution channels,

We anticipate that the revenue contribution from Japan should return to more normal levels in the second half of fiscal 1998.

Strategic Repositioning

The emphasis in fiscal 1997 was on strategically repositioning the company to take advantage of the explosive growth in NT and the growing demand for solutions to manage increasingly complex network data. During the year, we not only invested in our core UNIX-based product line, we embarked on concurrent product development initiatives in these new areas. The product development efforts that we are pursuing

extend beyond the immediate horizon. In fact, for the first time, the company has significant traction on projects beyond the 12-month window, with almost 50% of research and development dollars allocated to technologies

version of our system software. Further product innovations are planned for fiscal 1998.

Focus on NT

Auspex made NT product development a priority in fiscal 1997,

Everything we are doing as a company is guided by our focus on providing the customer with continuous, shared access to multiple terabytes of data, whether the platform is UNIX or NT. We believe this path holds tremendous opportunity for Auspex because of the demand from our large base of Fortune 1000 companies.

and products that are expected to ship in volume in the 12- to 18-month timeframe.

Investing more aggressively in research and product development is essential to meeting our long-term objectives, despite the impact to near-term earnings. In fiscal 1998, the company plans to continue to ramp its level of investment across all functional areas of the organization. We have chosen to increase our investment levels significantly over fiscal 1997 to take advantage of the windows of opportunity we see in the marketplace, which we believe is in the best long-term interest of our stockholders and our customers. By focusing on solutions-oriented initiatives that solve critical problems faced by Chief Information Officers today, we can significantly enhance our value to customers and become a more strategic partner in their success.

Product Initiatives Provide More Comprehensive Solutions, Extend Auspex Franchise

In fiscal 1997, we made good progress within all three initiatives.

Auspex Enhances Core UNIX-Based Systems

Auspex continued to enhance the performance of its core products. During the year, we introduced our new flagship model NS 7000/700, with optional software products aimed at data protection and backup, and an improved

in response to the growing number of customers looking for solutions that enable them to seamlessly share files among UNIX and NT clients, and manage and protect multi-terabytes of on-line data. Subsequent to the close of the year ended June 30, we announced NeTservices, an NT 4.0-compatible solution that we believe will be a best-of-class product offering for UNIX users migrating to NT. Auspex also has a scalable native NT server under development, aimed at the NT data consolidation market, which will be an entirely new market opportunity for the company.

Auspex Acquires Alphantronix

The company's emphasis on value-added software reflects our belief that to be a truly strategic partner with our customers, we have got to think beyond "the box" by providing a total solutions approach to network data management.

The June 30, 1997 acquisition of Alphantronix reflects Auspex's commitment to enterprise data management solutions for UNIX and NT. The acquisition has strengthened our focus in this area by accelerating our ability to develop innovative software solutions for managing and delivering enterprise data. We believe it has enhanced by 18 to 24 months the time-to-market of new Auspex enterprise-class data management solutions. The acquisition of Alphantronix has not only given

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Stockholders Letter

continued from A4

the company significant software assets and key enabling technologies, it has provided a dedicated software development center in Research Triangle Park, North Carolina devoted solely to developing value-added software products that will provide continuous access to network data. While the acquisition of Alphatronix will be dilutive in fiscal 1998, we expect to introduce a suite of software products that will represent an incremental revenue stream in fiscal 1999.

Customer Demand Drives New Focus

Everything we are doing as a company in these three areas is guided by our focus on providing the customer with continuous, shared access to multiple terabytes of data, whether the platform is UNIX or NT.

We believe this path holds tremendous opportunity for Auspex because of the demand from our large base of Fortune 1000 companies. Our customers are fast approaching an era where they have no backup window because the data on their networks must be accessible 24 hours a day, 365 days a year. And, increasingly, they must contend with managing data that must be shared by UNIX and NT clients. Auspex has had visibility to the growing complexity of enterprise data management because of the large amounts of data stored on our servers, and our expertise in helping customers design global information technology infrastructures that support network-based applications.

Execution Is Key

Given the growing need for continuous access to network data and the market demand for more comprehensive data management solutions, I am optimistic about Auspex's prospects for continued long-term growth.

Making the shift from a UNIX-only company to one that also embraces NT and enterprise data management is not an easy one. Nevertheless, I believe that the direction we have charted, and the investments we are making, position Auspex very well going forward. We have a significant opportunity to become a strategic solutions partner for organizations managing an explosion of network data. The key for fiscal 1998 is execution.



BRUCE N. MOORE
President and
Chief Executive Officer

THE COMPETITIVE ADVANTAGE

Auspex's Value Proposition

At Auspex, we believe the criticality of the file server to the network should not be underestimated. In a business climate where time-to-market pressures continue to grow, maximizing network performance is vital to the competitive strength of every organization.

Auspex's Expertise in Network Infrastructures and Network-Based Applications Is a Key Competitive Advantage

In today's information-driven enterprise, data is the common currency of the corporate network. At the center of the network is the enterprise file server. The file server — more than any other single point on the network — speeds the delivery of information to everyone throughout the organization. And information is what drives business today.

Well beyond the more straightforward functions of storage subsystems and network routers and switches, file servers must comprehend and be intelligent about the entire network infrastructure,

At Auspex, we bring a thorough understanding of network-based applications — whether it is ECAD, MCAD, data analysis or e-mail — and our expertise in designing network infrastructures that support these applications in order to help customers achieve continuous, shared access to network data.

Simultaneous Access to Shared Information — The Critical Distinction

While a sophisticated storage subsystem is essential for storing multiple terabytes of data, the real complexity lies in the networking capabilities of the file server, which processes network requests for data. The network file server must seamlessly manage the movement and exchange of data, enabling it to be shared simultaneously — by anyone, from anywhere — around the world.

Whether there are 100 or 1,000 engineers collaborating on a new product, the need for simultaneous access to the same information characterizes today's

Sharing information globally presents a significant challenge for our customers. As networks continue to grow in complexity, as the demand for 'round-the-clock access to information shrinks the available time for backups to near-zero, and as NT clients increasingly require

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including the relationship between the data and user, whether the data is being delivered over a local or wide area network, the type of data being requested (for example, whether it is text or images), and the size of the data. The file server must take all these factors into account, and optimize the delivery of network data.

global enterprise. It's not about sharing storage, it's about enabling users to have simultaneous access to the same files. To share that information intelligently. To work smart and productively. To make critical decisions. To create the new ideas that will drive their future growth.

simultaneous access to shared files, network and data management has become a monumental challenge for even the best-staffed IT departments.

We add value to our customers' business by understanding the applications on the desktop and the network infrastructure required to support those applications. It is an expertise that distinguishes Auspex, and a fundamental element of the company's value proposition.

BUSINESS NEWS

STRENGTH IN U.S. AND EUROPE, REORGANIZATION IN JAPAN

Auspex's 24% year-over-year revenue growth in fiscal 1997 was the result of continued strong demand for the company's high-performance NetServer product line in North America and Europe. While our operations in the Pacific Rim were impacted by the reorganization of a major OEM distribution partner in Japan, we took several steps that should position the region for improved performance in the second half of fiscal 1998.

By Joseph G. Brown
Vice President of Worldwide Field Operations

North America: Healthy Demand in Key Market Segments

At \$142.5 million, North American operations comprised 70% of Auspex's total revenues in fiscal 1997. The semiconductor industry remained Auspex's single largest market segment, accounting for approximately 27% of North American revenues in fiscal 1997. The internet service provider market also had a significant impact on the company's performance, with direct sales of products and services to one such customer totaling 15% of total company revenues in fiscal 1997. Strong sales to the oil and gas industry included sizable orders from such customers as Conoco, Unocal, Minerals Management Service, Petro-Canada, Phillips Petroleum and Anadarko Petroleum. Auspex's strong relationships with such leading inde-

At \$142.5 million, North American operations comprised 70% of Auspex's total revenues in fiscal 1997. For the coming year, we plan to continue to increase our sales force in order to take advantage of opportunities in the North American market.

pendent software vendors as Landmark Graphics were instrumental in the company's continued success in the oil and gas business. The company also focused its attention on aerospace and automotive manufacturers, which led to significant orders from leading organizations including Boeing,

Pratt & Whitney, and Lockheed Martin. During the year, Auspex and EDS Unigraphics announced a joint marketing agreement, which will promote Auspex's servers and software to EDS Unigraphics' large customer base, and EDS Unigraphics itself was a major customer for Auspex. In the fast-growing communication industry, Nortel and Bell Northern Research were among Auspex's largest customers in fiscal 1997. For the coming year, we plan to continue to increase our sales force in order to take advantage of opportunities in the North American market.

Europe: Revenues Up 74%

Revenues from the company's European operations were up a robust 74% from year-ago levels, as the major investments we made in sales capacity in fiscal 1996 yielded results. A very strong performance in the

United Kingdom included significant orders from Shell U.K., British Aerospace, News International, Linklaters & Paines, the British government, and Horizon/AT&T. In Germany, Mannesmann Mobilfunk, FAW Forschungsinstitut and Swiss Bank were among the largest

customers. In France, the company made continued progress, with orders from Total SA, Snecma Villaroche, Caisse des Depots and Dassault Systems. We were very gratified with the performance of our European operations in fiscal 1997, which we believe reflects the positive impact of a strengthened sales force together with a competitive line of high-performance products.

Japan: Positioned for Improved Performance in Fiscal 1998

While performance in Japan was disappointing in fiscal 1997 due to the reorganization of a major OEM partner, we also took a number of steps to improve our performance in this region. We anticipate that comparisons in the first half of fiscal 1998 will be difficult, with Japan's contribution to revenues returning to more normal levels in the second half of the year.

In fiscal 1997, Auspex realigned its channel distribution strategy in order to expand market opportunities in Japan. As the first step in this expansion, Auspex signed a Master Value Added Distributor (MVAD) agreement with Fuji Xerox and redefined Auspex's relationship with Nissho Electronics Corp. in the fourth quarter of fiscal 1997. Under the new MVAD contract, Fuji Xerox, formerly Auspex's OEM partner in Japan, will act as a non-exclusive supplier of the company's products to leading resellers in Japan. As Auspex moves to increase brand awareness in Japan, the company's line of network file servers and high-availability software will also be sold under the Auspex name for the first time by Fuji Xerox.



Subsequent to the close of the year, Auspex announced the formation of a new subsidiary—Auspex K.K.—and hired Mikio Kamimura as Managing Director, Asia/Pacific Operations of the new

With the formation of Auspex K.K. and the hiring of Mikio Kamimura, we believe Auspex will strengthen its ability to provide better support to the company's distribution partners and increase market penetration.

organization. The former Nihon Sun Microsystems Senior Director of Sales brings extensive management expertise to the new entity. With the formation of Auspex K.K. and the hiring of Mikio Kamimura, we believe Auspex will strengthen its ability to provide better support to the company's distribution partners and increase market penetration.

BUSINESS NEWS

New VP Accelerates Auspex Product Development

Paul Gifford Drives Product Development Roadmap in NT and Enterprise Data Management

What a difference a year makes

The accelerated rate of product introductions in support of Auspex's new strategic direction can, in large measure, be dated to the hiring of Paul Gifford as Vice President of Product Development in October, 1996.

Gifford is the chief architect of new product development efforts for the company's UNIX-based systems, as well as its NT-based systems currently under development. According to Bruce N. Moore, Auspex President and Chief Executive Officer, "We hired Paul because of his experience with complex systems and his expertise in NT, but he has brought much more to the table. He has brought the vision and technical capabilities to our engineering organization that I believe will drive this company's long-term growth."

Paul Gifford is more unassuming about his role, crediting his



engineering organization with turning on a dime as the company's new strategic direction was defined. "There is incredible engineering talent here at Auspex, and we've had a very productive 12 months. Auspex has a deserved reputation for technical excellence and for customer support that goes above and beyond what's required. I'm confident that — with our new NT products and enterprise data management software initiatives — the next twelve months will be just as exciting and productive."

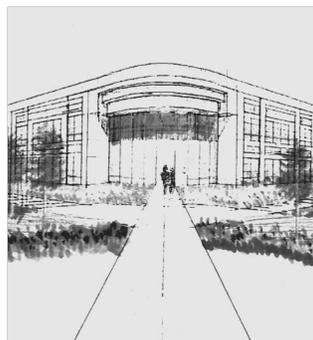
Auspex Systems Breaks Ground On New Headquarters

Leased Complex Designed to Accommodate Growth

Santa Clara, CA – March 10, 1997 – Auspex has broken ground on a new 269,000 square foot headquarters. The complex will be leased in order to provide the most cost-effective method of accommodating company growth. The new four-building complex will be located in the heart of Silicon Valley at the corner of San Tomas and Central Expressways in Santa Clara.

"We continue to attract very talented individuals to join the company and consequently will soon out-grow our current facility," said Bruce N. Moore, Chief Executive Officer of Auspex Systems. "Moving to this new complex gives us an opportunity to design in workspace efficiencies, and to create a more open and synergistic atmosphere for employees to work."

Auspex's total worldwide organization is approximately 600 employees, of which 450 will be initially



housed in the new facility. Auspex plans to move to the new campus during the first quarter of calendar 1998. Design and construction are being coordinated by South Bay Development Company with Gordon-Prill, Inc. as the interior architect.

Auspex Installs Its 2,000th System

NetServer Delivered to State-of-the-Art Fabrication Facility at Advanced Micro Devices

Santa Clara, CA – November 25, 1996 – In an important company milestone, Auspex shipped and installed its 2,000th system in the second quarter of fiscal 1997. The system, part of a ServerGuarded pair of NS 7000/700 NetServers, was delivered to Advanced Micro Devices (AMD), a leading supplier of integrated circuits, at its newest semiconductor manufacturing facility located in Austin, Texas.

The NetServers were installed at AMD's fully automated Fab 25, AMD's first wafer fabrication facility where applications are built strictly on client-server open systems. The NetServers with ServerGuard provide continuous availability of data required for automated production processes. Auspex's ServerGuard is an innovative software solution that mirrors the NetServers and automatically delivers



for our needs and ServerGuard gave us the disaster recovery component that we were looking for."

Prior to installing the two NS 7000/700 servers at its innovative Fab 25, AMD relied on Auspex servers at design and engineering analysis facilities. "We felt confident about using Auspex servers because they had established a proven track record elsewhere within our company and we were very impressed with Auspex's technical support services," said O'Donnell.

"We needed a system that could stay up 24 hours a day, 365 days a year, because in our environment, every minute of downtime is extremely expensive. We were also looking to implement a disaster recovery scenario so that we could ensure continuous access to data if a disaster occurred. Auspex's servers provided the most reliable solution for our needs and ServerGuard gave us the disaster recovery component that we were looking for."

—Mike O'Donnell
Senior Technical Systems Analyst
Advanced Micro Devices

failover file service, even in the event of a catastrophic system failure.

"We needed a system that could stay up 24 hours a day, 365 days a year, because in our environment, every minute of downtime is extremely expensive," said Mike O'Donnell, Senior Technical Systems Analyst at AMD. "We were also looking to implement a disaster recovery scenario so that we could ensure continuous access to data if a disaster occurred. Auspex's servers provided the most reliable solution

"Auspex is now protecting, distributing and managing over 300 terabytes of network data in mission-critical environments," said Bruce N. Moore, Auspex President and Chief Executive Officer. "We are pleased that semiconductor industry leaders such as AMD are taking full advantage of the demonstrated reliability and quality that our products deliver in manufacturing environments where continuous access to data is critical."

BUSINESS NEWS

EDS Unigraphics/Auspex Joint Marketing Agreement

Strategic Relationship Promotes Auspex NetServers and Software

Santa Clara, CA – June 6, 1997 – Auspex today announced it has signed a joint marketing agreement with EDS Unigraphics. The strategic relationship will promote Auspex's proven, high-performance network file servers and high-availability software to EDS Unigraphics' customers. Auspex is the only EDS Unigraphics partner exclusively dedicated to delivering high-performance, high-availability network file servers.

EDS Unigraphics' products enable data-intensive, collaborative engineering processes for product design, development, and manufacturing. "EDS Unigraphics and Auspex serve large, global manufacturing industries,"



widely distributed over inefficient network infrastructures. The agreement between Auspex and EDS Unigraphics will make it easier for our customers to break out of their data impasse," said Bruce N. Moore, President and CEO at Auspex.

EDS Unigraphics has been a long-time customer of Auspex, and uses Auspex NetServers in all three of its global development environments, both to manage Unigraphics and Information Manager (IMAN) code libraries, and to deliver large model files for quality assurance and testing cycles. "During the quality assurance phase of our IMAN development process, we simulate a very rigorous production environment, putting extremely high data loads on our Auspex server," says Dave Mitchell, IMAN Business Unit Director, EDS Unigraphics. "IMAN is uniquely architected to take advantage of network file servers, and we have mandated their use in all IMAN implementations. This agreement with Auspex will be extremely beneficial to all our IMAN customers." EDS Unigraphics will offer Auspex solutions to its installed base in the United States, Canada, Europe and Asia.

commented John Mazzola, President of EDS Unigraphics. "To meet their critical, time-to-market goals, these customers require uninterrupted, fast access to large volumes of design and manufacturing data. Our joint marketing agreement with Auspex will ensure that more of the EDS Unigraphics customer base will benefit from Auspex's technological expertise for managing, storing and serving their mission-critical data."

"Today's engineering design customers must contend with an explosion of data that is often

Auspex is the only EDS Unigraphics partner exclusively dedicated to delivering high-performance, high-availability network file servers.

Auspex Systems Acquires Alpatronix

Strengthens Focus on Integrated, High-Availability Data Management Solutions

Santa Clara, CA – July 1, 1997 – Auspex Systems today announced it has acquired Alpatronix, Inc. of Research Triangle Park, NC. The acquisition of Alpatronix accelerates Auspex's ongoing strategic initiatives to complement its multi-terabyte servers with innovative software solutions that make it much easier to manage and deliver enterprise data in mission-critical, 7x24 environments.

implementation of Auspex's new enterprise-class data management solutions."

"Network storage is growing at over 100 percent annually," said Dr. Paul Mason, Vice President of Infrastructure Software Research at International Data Corporation. "This growth in storage, coupled with the need for 7x24 operations at most large corporations, has reduced the time available to back-

"Network storage is growing at over 100 percent annually. This growth in storage, coupled with the need for 7x24 operations at most large corporations, has reduced the time available to backup and protect enterprise data to virtually zero. Auspex is looking to solve this problem – one of the most strategically critical problems IS managers face today – by ensuring around-the-clock continuous data access."

—Dr. Paul Mason
Vice President of Infrastructure Software Research
International Data Corporation

Auspex purchased Alpatronix in a cash transaction for a total consideration of approximately \$7.7 million. The acquisition resulted in a one-time charge to Auspex's income statement in the fourth quarter of fiscal 1997 of approximately \$7.4 million, related to the purchase of in-process technology. Alpatronix will operate as a wholly owned subsidiary based in Research Triangle Park, NC.

"Enabling continuous access to enterprise data is a major strategic focus for Auspex," said Bruce N. Moore, Auspex's President and Chief Executive Officer. "Alpatronix's expertise in developing a scalable, high-availability data management software architecture will significantly speed

up and protect enterprise data to virtually zero. Auspex is looking to solve this problem – one of the most strategically critical problems IS managers face today – by ensuring around-the-clock continuous data access."

Auspex's strategy is to develop innovative solutions for enterprise data management and specifically products that will provide the customer with continuous and shared access to their data. The Alpatronix Inspire suite of object-oriented software and GUI libraries will provide the basic enabling technologies required to implement these new products. They will allow Auspex to build upon its leadership position in delivering continuous

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BUSINESS NEWS

Auspex Systems Acquires Alphatronix

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data access, which today is based upon its popular DataGuard, ServerGuard, DriveGuard and FastBackup software products.

"Alphatronix has an outstanding engineering team with demonstrated expertise in solving large enterprise data management problems," Moore continued. "By utilizing open application programming interfaces and adhering to industry standards, Auspex will offer data management software solutions that can be tightly integrated with existing third-party data management products. We will continue to work closely with third-party independent software vendor partners to integrate our complementary systems products with their software to tailor an overall solution that is optimized for continuous data access," he said.

"We are very pleased to be able to expand our presence in the Research Triangle Park area." Moore explained further, "A year ago, we established a technical support group in Cary, NC. Alphatronix represents our first remote product development center outside of the San Francisco Bay Area and gives us immediate access to a very talented high-tech work force."

"By combining our high-availability data management expertise with Auspex's unique Functional Multiprocessing server architecture, we can provide customers with continuous data access and protection, without degradation in performance for mission-critical applications in both UNIX and UNIX/NT environments," said Brian Ritchie, President of Alphatronix.

"We've already consolidated our NFS data onto an Auspex server, and are planning to do the same with NT. By investing in technology that enables both our UNIX and NT clients to share files and have 'round-the-clock access to data, we improve their productivity and enhance our time to market. We are confident in Auspex's ability to extend the reliability, performance and ease of administration of its systems, and carry that forward to NT."

—Steve Butler, Information Systems Manager
FUJIFILM Electronic Imaging Ltd.

FUJIFILM

"EDS Unigraphics and Auspex serve large, global manufacturing industries. To meet their critical time-to-market goals, these customers require uninterrupted, fast access to large volumes of design and manufacturing data. Our joint marketing agreement with Auspex will ensure that more of the EDS Unigraphics customer base will benefit from Auspex's technological expertise for managing, storing and serving their mission-critical data."

—John Mazzola, President
EDS Unigraphics



"A one-minute failover sounds simple, but a minute can be a lifetime during a shuttle launch when you're going from ground to orbit in eight minutes, and from 0 to 18,000 miles per hour. Auspex's ServerGuard provided an automatic two-second failover which we tested and retested. It proved to be a key factor in this very successful mission."

—Stan Hutchison
NASA Platform and Systems Services Group



HIGH-PERFORMANCE, HIGH-AVAILABILITY SOLUTIONS

Customers Gain Dramatic Advantage Through Server Consolidation

99.989% Measured Uptime Underscores Company's Position as High-Availability Leader

If customers want to know just how reliable Auspex NetServers are, all they have to do is ask. For the year ended June 30, 1997, Auspex's installed base of over 2,000 systems reported uptime of 99.989%—an outstanding result in the client/server industry. This enviable uptime record is allowing many Auspex customers to adopt and realize the benefits of a data consolidation strategy.

"Our customers measure server downtime in minutes or even seconds per year rather than hours," said Bruce Moore, President and Chief Executive Officer of Auspex. "These outstanding reliability results demonstrate the proven technology advantage that Auspex provides its customers day in and day out. It's an advantage that is enabling a growing number of Auspex customers to replace difficult-to-manage and costly distributed file servers with one highly scalable, high-performance server."

Tom Bain, Principal and Director of Technology at BlackRock Financial Management, commented on the complexity of maintaining reliable data delivery in a distributed file server environment. "Over time, it's very difficult to keep interdepen-

dencies between servers from creeping in. So, in reality, when one server fails because another mounts off of it, then that one stops and then another mount hangs, pretty soon, none of your servers are working. Instead of reducing the impact of failure, you actually have a less stable environment." By eliminating multiple servers and consolidating that data on a single Auspex server, BlackRock realized dramatically improved data availability. Bain states, "With Auspex, we are confident we'll have access to the information we need to analyze market and risk conditions. We can accurately say that the Auspex solution is critical to our continued earnings growth."

Moore commented, "Our customers compete in the most data-intensive industries in the world, including internet services, communications, financial services, automotive and aircraft design, and semiconductor manufacturing. They require the ease of management, increased reliability and lower IT cost of operations that consolidated file servers provide. Our high-availability products deliver the performance, reliability and scalability to make consolidation a viable tactic in their competitive strategy."

Meeting the Data Consolidation Opportunity

Auspex Selected by Boeing North American Aircraft Division to Implement Its Data Consolidation Strategy

Santa Clara, CA – June 18, 1997 – As part of a major centralization of its file services in the Los Angeles area, the North American Aircraft Division (NAAD) of Boeing North American, Inc. has chosen Auspex to implement its data consolidation and backup strategy. Boeing North American, Inc. is a subsidiary of The Boeing Company, the world's leading manufacturer of commercial airplanes and a major U.S. government contractor. Boeing acquired Rockwell's aerospace and defense business, including NAAD, on December 6, 1996.

NAAD purchased an Auspex NetServer NS 7000/700 with 290 gigabytes of storage capacity, which will house all the data for their major UNIX Systems. The single NetServer will supply file services for engineering design users, engineering analysis users, finance users and vehicle management system software developers. In addition to consolidating the division's CATIA software data, the Auspex NetServer will be used to consolidate all the division's analysis data and act as a hub for an entire major UNIX Systems backup strategy.

The move signals the first major infrastructure change at North American Aircraft Division in consolidating data and backup. "NAAD has made a strategic decision to streamline our information technology infrastructure by providing centralized file services for all our major UNIX Systems," said Richard L. (Dick) Dement, acting director of the division's Southern California Information Systems. "We chose Auspex because of their products' record of reliability and performance, and their ability to provide NAAD with a level of data availability we demand." The division also will be consolidating their NT data onto the Auspex server.

According to Bruce N. Moore, Auspex President and Chief Executive Officer, "The consolidation of the commercial and defense aerospace industries has generated significant challenges to the merged companies from an



information management and productivity perspective, which presents Auspex with continued opportunities. Auspex NetServers and high-availability software are optimally designed to assist companies consolidate data from disparate and often under-performing servers to a single-point source of information management. Boeing NAAD joins the ranks of many large manufacturers who depend on Auspex technology to respond to ever-increasing time-to-market pressures." The Auspex NetServer at the division will be used to consolidate the data that formerly resided on 40 workstations and network file server systems.



HIGH-PERFORMANCE, HIGH-AVAILABILITY SOLUTIONS

PRODUCT INTRODUCTIONS

Auspex Introduces New High-Performance Model NS 7000/700 NetServer

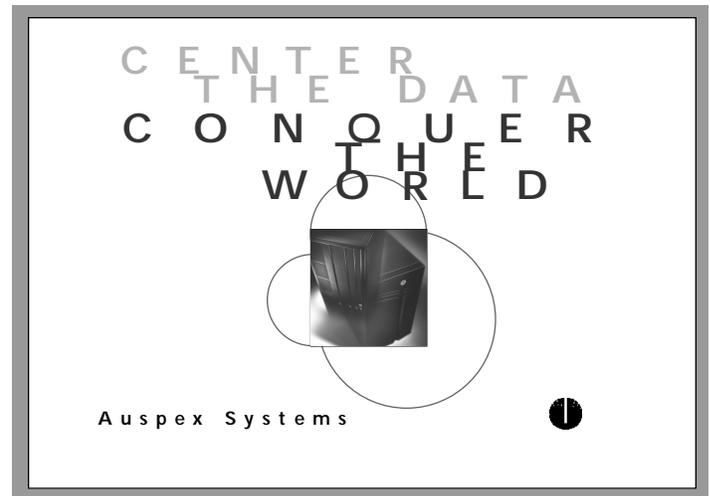
New Flagship Model Increases Throughput 25% and Doubles Number of Network Connections

Santa Clara, CA - October 26, 1996 - Auspex Systems began shipping its new enterprise-class network data server model NS 7000/700 that nearly doubles the number of network connections and increases network file system (NFS) throughput by an average of 25%.

The company's new flagship network data server features a double-wide backplane that accommodates up to five independent network processors and five independent storage processors, which accelerates NetServer throughput. Network connectivity is nearly doubled to as many as 30 Ethernets, or 15 Fast Ethernets, FDDI and ATM links, which dramatically increases throughput

measured as NFS input/output operations per second. This gives customers a simplified single point of system administration and delivers high-speed network application response, even when supporting hundreds of users.

"The driving force behind Auspex's product development strategy is responding to our customers' need for continuous data access. Because we are committed to increasing system performance while maintaining the highest standards of reliability, customers find meaningful value in Auspex products and support," said Bruce N. Moore, Auspex President and Chief Executive Officer. Moore stated further that the capabilities of the



NS 7000/700 are available to Auspex's customer base through upgrades, preserving their investment in server technology while providing expanded performance. "The Auspex NetServer has been the most reliable server that we've had during the last four years and we actually exceeded Auspex's

uptime statistics," said Steve McCarthy, Manager of Data Center Operations, Phibro Energy, Inc. "We can't risk our entire business on a server that isn't reliable. If something goes bump in the night, the Auspex server is the server we want."

PRODUCT INTRODUCTIONS

DriveGuard Software Lowers Disk Protection Costs up to 45 Percent

Santa Clara, CA - March 26, 1997 - When it comes to protecting important data, companies gained a high-performance, cost-effective solution in fiscal 1997 with the introduction of Auspex's DriveGuard.

DriveGuard, an embedded RAID 5 solution for Auspex's NetServers, provides mission-critical data security, while saving customers up to 45 percent of the cost of fully mirrored configurations. Through its performance, flexibility and unique hot-move features, DriveGuard sets new implementation standards for RAID 5, as compared to traditional software-based solutions.

"DriveGuard offers customers a cost-effective alternative to mirroring," said Paul Gifford, Vice President of Product Development at Auspex. "Customers now have the flexibility

to prioritize their data and select the most cost-effective method for protecting mission-critical information. DriveGuard's economical disk protection eliminates the expense associated with mirrored disks while providing robust protection customers can trust for most of their important data."

"For our most critical data, we would prefer to mirror drives or utilize Auspex's ServerGuard for maximum data protection," said John Cooper, UNIX Senior Systems Administrator at LSI Logic, Inc. "DriveGuard gives us an additional storage protection option for important data that we want to protect but can't justify the expense of disk mirroring. This gives us an economical way to ensure continuous availability of information."

DriveGuard delivers dramatically higher performance than typical software RAID 5 implementations by off-loading parity calculations and rebuilds to a hardware-assisted disk controller level. The resulting performance is nearly identical to mirrored disks and rebuilds take as little as 90 minutes. Customers can use automatic rebuild or schedule rebuild times and priority to maximize continuous data access and performance.

DriveGuard's flexibility allows customers to prioritize protection on a file system basis or with special system-wide hot-spare pooling. This offers more economical protection for their most sensitive business data. Finally, DriveGuard offers a unique feature, called hot-move, that allows reconstructed hot-spares to be physically moved to the failed drive's location while the system is running and without requiring a second rebuild. This simplifies physical administration

of RAID 5 arrays without affecting data availability. As a result, customers can grow storage capacity and know that it is completely protected, while DriveGuard meets the most discriminating continuous operation and administrative demands.

"The addition of RAID 5 to Auspex's RAID offerings lets customers optimize for performance, availability and cost on a per file system basis," stated Gifford. "File system flexibility means customers can tailor their storage configurations to meet their continuous data access needs. In addition to Auspex's DataGuard and ServerGuard software, DriveGuard represents another example of our commitment to deliver comprehensive solutions for high-availability data protection."

HIGH-PERFORMANCE, HIGH-AVAILABILITY SOLUTIONS

PRODUCT INTRODUCTIONS

FastBackup Sets New Backup and Restore Performance Standard

Santa Clara, CA – March 14, 1997 – Today Auspex announced FastBackup, the highly scalable network data management software,

100 gigabytes per hour cost-effectively. Superior performance such as this will help businesses seamlessly protect corporate information.

FastBackup leverages Auspex's unique Functional Multiprocessing architecture, and yields best-of-class backup and restore performance with the most cost-effective tape library technology.

which sets a new best-of-class backup and restore performance standard for network file servers with DLT-based backup library technology. Users can now achieve backup and restore throughput of up to

"Our challenge is not only to provide the industry with powerful, large-capacity servers," said Paul Gifford, Vice President of Product Development at Auspex, "but also to offer storage management solutions like

FastBackup, AXXiON NetBackup, and DLT libraries that effectively address our customers' network data management requirements. FastBackup is another reflection of our commitment to continuous data access."

FastBackup leverages Auspex's unique Functional Multiprocessing (FMP) architecture that distributes NFS workload to multiple, dedicated processors. Traditional NFS server architectures experience backup performance degradation through congested CPUs or backplanes that manage disk, tape and network data traffic. FastBackup is FMP-embedded software that overcomes these issues by offering parallel data transfers from disk controller to tape without moving data across the backplane. This yields best-of-class backup and restore performance with the most cost-effective tape library technology.

"As network data volume continues exponential growth, enter-

prise environments and continuous operation environments, in particular, demand comprehensive, high-speed storage management," said Steve Colman, Director of OEM Relationships for OpenVision Technologies. "Integrating AXXiON NetBackup with Auspex's FastBackup results in a flexible, powerful and fast storage management solution to protect large amounts of data in the least amount of time. This gives customers protected data with maximized continuous data availability."

"DLT libraries are the overwhelming market leader in price-performance and reliability," said Chet Baffa, Vice President of Sales and Marketing for ATL, a leading provider of DLT tape library systems. "Auspex FastBackup enables impressive performance, driving up to 10 DLT drives virtually at performance capacity. This maximized library utilization lets customers get the most out of their ATL library products."

Auspex Introduces New NetServer Configuration Optimized For High Availability

NetServer Model 7000/700 HA Bundles Auspex's Unique Software Products for Industry-Leading Continuous Data Access

Santa Clara, CA – April 15, 1997 – Reflecting the company's commitment to provide cost-effective network data management solutions that ensure continuous data access, Auspex introduced the new NS 7000/700 HA NetServer. Bundled with the company's

Auspex's flagship network data server delivers industry-leading continuous data access.

"Auspex has been a premier provider of high-availability solutions," said Joe Brown, Vice President of Worldwide Field Operations at Auspex. "The

forefront of providing technology designed to meet our customers' need for continuous data access."

Robert Johnson, Manager, Exploration and Production Technology, Apache Corporation, one of the country's largest independent oil and gas exploration and production companies, commented on the decision to purchase an Auspex NS 7000/700 HA system. "Aligning networking technology with business strategy is key to our company's competitiveness. Staying competitive directly impacts Apache's financial success," Johnson said. "Our ability to make decisions quickly depends upon high system reliability and availability of data. Data drives our business decisions and system downtime is money lost."

"We were looking to expand and optimize our computing environment," remarked Johnson. "We selected Auspex because their systems offer the best price-performance server technology available in the market today. NetServers have an excellent record of availability, and the 7000/700 HA with Auspex's high-availability software and RAID 5 configuration provided Apache with



a higher level of system resource availability."

Auspex's unique software offering, DataGuard, is a fundamental differentiator because it protects file storage and transfer against UNIX or application failure. In the event of a UNIX failure, DataGuard allows the host processor in

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"The NS 7000/700 HA NetServer demonstrates our intent to remain at the forefront of providing technology designed to meet our customers' need for continuous data access."

—Joe Brown
Vice President of Worldwide
Field Operations

distinctive DataGuard and NS 7000/700 HA NetServer demonstrates our intent to remain at the DriveGuard software products,

HIGH-PERFORMANCE, HIGH-AVAILABILITY SOLUTIONS

Auspex Launches NeTservices — New High-Performance “Bilingual” Server

Windows NT 4.0—Compatible Product Enables Enterprise Customers to Share Terabytes of Data in Mixed UNIX and NT Environments

Santa Clara, CA - July 16, 1997 - Auspex today announced NeTservices, the first product to provide the scalability and reliability customers require to manage and share terabytes of NT and UNIX data on the same file server. With the introduction of NeTservices, Auspex undertakes a major strategic initiative to embrace NT for enterprise file serving and extend its high-availability network data access and management solutions into the enterprise Microsoft Windows NT marketplace.

He explained, “NeTservices avoids the performance degradation which characterizes competitive, emulation-based offerings. And, NeTservices provides a fully implemented, NT 4.0 network environment. For the first time, NT and UNIX clients will enjoy native performance levels while sharing the same data files on a single, scalable, high-availability, and highly reliable server.”

Enterprise-class customers with a mixed UNIX/NT environment to manage will benefit from NeTservices’ performance and

“Current offerings in the marketplace force customers with UNIX and NT data management requirements to make trade-offs,” commented Paul Gifford, Vice President of Product Development at Auspex. “NeTservices’ native implementation of NT’s CIFS file service protocol doesn’t suffer from the performance degradation which is typical of emulation-based products.”

“NeTservices delivers a complete, NT Server 4.0 network environment, including directory services, file security, and the remote administration features that are essential for easy, transparent deployment into existing Windows corporate

networks,” Gifford continued. “And, NeTservices relieves significant overhead burden for the enterprise customer by eliminating the need for duplicate servers and for per-client administrative burdens such as PC-NFS installation and maintenance.”

Tom Bain, Principal and Director of Technology at BlackRock Financial Management, commented, “NeTservices will give us the reliability and scalability we need, and decrease the complexity of our environment by allowing us to manage our UNIX and NT data on one consolidated file server. That’s why we are in the process of placing an order for the product.”

NeTservices Product Feature Overview

NeTservices adds support for the Windows NT 4.0 networking environment, allowing Auspex’s NetServer product family to be fully integrated into NT-based corporate network environments. These features include:

- High-performance, scalable, and high-availability network file services for MS Windows NT, Windows 95, MS Windows for Workgroups, MS Windows 3.x, and MS-DOS clients.
- Interoperability with MS Windows NT servers as primary or backup servers for NT client log-on validation and for file access across trusted domains.
- Administration based on MS Windows NT Server Tools, such as Server Manager, User Manager, and Event Viewer.
- Windows NT security at the user/group level, file/directory access control, and network auditing.

“NeTservices represents a significant milestone in enterprise computing,” said Bruce N. Moore, President and Chief Executive Officer of Auspex. “Until now, network file servers for mixed UNIX and NT environments forced the enterprise customer to compromise on performance. Auspex’s introduction of NeTservices reverses this trend.”

ease of management while realizing significant reductions in cost and administrative burden, according to Moore. “NeTservices provides our customers with an unbeatable combination: better total cost of ownership, and the ability to easily manage terabytes of data, regardless of the desktop client type — UNIX or Microsoft Windows 3.x/95/NT,” Moore said.

Auspex Introduces New Configuration

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the NetServer to automatically reboot UNIX while the Auspex NetServer continues to deliver data and file services to its clients.

“Our NetServers are the only systems in the world to deliver primary network data services when the host operating system fails,”

protection, is Auspex’s most cost-effective form of data security. It provides customers with the flexibility necessary to prioritize their stored files so mission-critical data is always protected. DriveGuard provides data security while saving customers 45 percent of the cost of fully mirrored configurations.

The NS 7000/700 HA is backed by a full range of support services, including 24-hour, 365-day toll-free telephone assistance by technical support engineers, a single-step resolution process, and

“We were looking to expand and optimize our computing environment. We selected Auspex because their systems offer the best price-performance server technology available in the market today. NetServers have an excellent record of availability, and the 7000/700 HA with Auspex’s high-availability software and RAID 5 configuration provided Apache with a higher level of system resource availability.”

— Robert Johnson
Manager, Exploration and Production Technology
Apache Corporation

states Brown. Customers can also run host-based applications on the NetServer with the assurance that in the event of an application failure, data services continue uninterrupted.

DriveGuard, an innovative RAID 5 solution for high-availability data

comprehensive software media and documentation updates. “Our commitment to service and support ensures that our customers realize the maximum benefit from their investment in Auspex products,” said Brown.

AUSPEX CUSTOMERS: AN ONGOING SUCCESS STORY

Auspex Targets Oil & Gas Market

Shell U.K. One of Several Major New Oil & Gas Customers

When Auspex turns its attention to a market, it means business. A case in point in fiscal 1997 was the seismic interpretation area of the oil and gas exploration industry. Two years ago, oil and gas was not a significant portion of Auspex revenues. But Auspex identified it as one where the company's value proposition would be especially persuasive. By the close of fiscal 1997, oil and gas grew to approximately 6% of total company revenues.

Auspex's customer list now reads like a "Who's Who" in the oil and gas industry. In fiscal 1997, Shell U.K., Conoco, Unocal, Minerals Management Service, Petro-Canada, Total SA and Apache Corp. were among a long list of new customers that joined BP Exploration, Phillips Petroleum Co., Western Geophysical, Shell Expro and Anadarko Petroleum

as Auspex customers. Shell U.K. was the single largest customer in the oil and gas business for Auspex in fiscal 1997.

According to Auspex President and Chief Executive Officer Bruce N. Moore, the company's association with leading exploration and production companies is the result of a natural fit of customer requirements and Auspex technology. "Seismic exploration requires massive on-line storage capacity and demands very high-speed input/output during data interpretation. Auspex NetServers are optimally designed to manage and store data of this complexity and size," he said.

"For oil and gas customers, the key to long-term growth and profitability is quickly and accurately interpreting complex seismic data. Auspex NetServers significantly enhance data



access, which directly impacts their ability to make critical judgments on the productive potential of a given site," Moore said.

NetServers Bring More Strength to Nortel's Power Networks

Santa Clara, CA – May 22, 1997 – Auspex today announced that it will provide advanced server technology to support Nortel's Power Networks, which will deliver an integrated networks environment incorporating voice, data, internet/intranet, wireless, fax and video. Auspex's high-performance, high-availability servers are crucial in rigorous enterprise network environments such as those served by Power Networks.

"The Power Networks infrastructure often will require the high-performance and scalability that our products provide," said Bruce N. Moore, President and Chief Executive Officer of Auspex. "Power Networks will

Auspex Ships First 2-Terabyte System

Santa Clara, CA – April 8, 1997 – Confirming the company's view that data consolidation will continue to translate into the need for highly scalable, high-performance servers, Auspex today shipped its first server with over 2 terabytes of storage capacity.

The Gulf Region Division of Conoco Inc., a subsidiary of DuPont, selected Auspex to store and manage its seismic interpretation and exploration data, along with system implementation services from Landmark Graphics Corporation. Two Auspex NetServer model NS 7000/700 systems, protected by Auspex's DataGuard and DriveGuard (RAID 5) high-availability software, have a total of 2.25 terabytes of storage capacity. With over 1.5 terabytes of total additional storage capacity, the systems also have considerable untapped capacity to accommodate the division's anticipated growth.

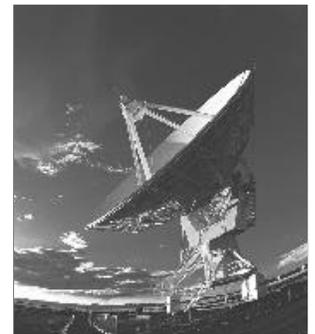
The NetServers, located in Lafayette Louisiana, will provide data services for complex 3-D seismic interpretation using Landmark Graphic's suite of geoscience applications. In an

effort to improve data access and availability to approximately 80 client workstations, and accommodate planned workstation and data volume growth, Conoco is migrating from an existing data server to a high-performance and fail-safe centralized Auspex solution.

Robert Moyer of Conoco said, "Auspex's NetServer was evaluated against other competitive systems being used in our application environment. It not only had the proven scalability, performance and reliability that would immediately improve our ability to access and interpret the data, but had the storage capacity to meet our future growth requirements as well." Moyer also cited an endorsement from an existing Auspex customer in the oil and gas market as instrumental in Conoco's decision to place the order with Auspex.

Landmark Professional Services will team with Auspex to offer a complete solution designed to optimize the Gulf Region Division's geocomputing infrastructure, data and applications.

"Landmark and Auspex are partnering to offer a highly reliable solution centered around the Auspex NetServer," said Keith J. Johnston, Landmark Vice President of Professional Services. "Conoco will not only derive the benefit of an environment in which applications, databases, networks, operating and system software, and hardware have been optimized for maximum end-user productivity; they will also realize a cost-effective IT model offering the scalability to address their future requirements." In addition to implementation services, Landmark will provide and configure the "Common Access Interface" (CAI) tool. This tool will provide easy and uniform access to geoscience projects and applications. A single graphical user interface will allow users to select the application and project of interest without incurring the burden of performing application-specific environment setups or requiring knowledge of where on the network a particular project dataset may reside.



demand very high reliability, and Auspex network file servers are ideally suited to this type of demanding environment." Auspex currently measures availability at 99.989%, the highest in the client/server industry.

F. William Conner, Executive Vice President, Nortel Enterprise Networks, commented, "Our goal is to provide the integrated information infrastructure that is essential in today's enterprises, in which customers can use rapidly emerging technologies and applications. Auspex's advanced file server delivers the power, performance and reliability required by our customers."

AUSPEX CUSTOMERS: AN ONGOING SUCCESS STORY

NASA Deploys Auspex's Fault Resilient Solution in Atlantis Space Shuttle Launch

Auspex's ServerGuard Ensures NASA Mission Controllers Have Critical Access to Data

Santa Clara, CA – November 11, 1996 – Auspex's NetServer with ServerGuard is providing a high-availability, high-performance solution for NASA's space program.

At the Mission Control Center in the Johnson Space Center in Houston, a multitude of mission-critical operations are performed. Every second counts and manual intervention to recover from system failures must be minimized. In this environment, Auspex NetServers are combined with ServerGuard to ensure continu-



photo: Professor Andrew Davidhazy

ous availability of data required for a successful space mission. ServerGuard is an innovative software solution that mirrors the NetServers and automatically delivers failover file service even in the event of a catastrophic system failure.

area, approximately 100 mission controllers have shared access to these file systems, even if one server fails entirely. The Atlantis Space Shuttle's recent rendezvous with Shannon Lucid and the Russian Mir Space Station was the first launch to use Auspex's ServerGuard.

"A one-minute failover sounds simple, but a minute can be a lifetime during a shuttle launch when you're going from ground to orbit in eight minutes, and from 0 to 18,000 miles per hour. Auspex's ServerGuard provided an automatic two-second failover which we tested and retested. It proved to be a key factor in this very successful mission."

—Stan Hutchison
NASA Platform and Systems Services Group

"In designing the new Mission Control Center, we faced the challenge of reducing costs while delivering a system that would be flexible, safe and meet the demands of high-risk human space adventure. Auspex's servers and ServerGuard gave us the tools to meet this challenge," said Stan Hutchison of NASA's Platform and Systems Services Group.

ous availability of data required for a successful space mission. ServerGuard is an innovative software solution that mirrors the NetServers and automatically delivers failover file service even in the event of a catastrophic system failure.

With ServerGuard, the Mission Control Center has multiple file systems mirrored between independent Auspex servers. Working from over 250 workstations in the operations

"A one-minute failover sounds simple, but a minute can be a lifetime during a shuttle launch when you're going from ground to orbit in eight minutes, and from 0 to 18,000 miles per hour," said Hutchison. "Auspex's ServerGuard provided an automatic two-second failover which we tested and retested. It proved to be a key factor in this very successful mission."

"Auspex is committed to working with our customers to ensure the development of technology solutions and their applicability to real-life situations. The use of ServerGuard in NASA's Mission Control Center reflects the outstanding quality and reliability that our products deliver in mission-critical environments," said Bruce N. Moore, President and CEO of Auspex Systems.

ServerGuard Proves Its Worth at Fuji Capital

NetServer with ServerGuard Provides Dramatic Failover Solution for Critical Financial Trading Operations

Santa Clara, CA – April 28, 1997 – An incident in London dramatically demonstrated the value of Auspex's NetServer with ServerGuard to Fuji Capital Markets Corporation (FCMC).

"ServerGuard saved the day," said Mark Maxwell, Vice President and Global Systems Manager at FCMC in New York. "A basic human error caused a power interruption to our NetServer 7000/700 located

As an industry leader in managing market and credit risks, FCMC is committed to employing leading-edge technology to sustain its ability to provide competitive pricing and responsive support to its customers. According to Maxwell, "Auspex is an integral part of the systems technology that we rely on to conduct our trading operations. With Auspex, we've realized

"With Auspex, we've realized greater performance, higher availability, simplified systems administration and increased expandability"

—Mark Maxwell
Vice President and Global Systems Manager
Fuji Capital Markets Corporation

on the ground floor of the datacenter. The NetServer was forced off line, but a second NetServer stationed in the basement took over immediately," Maxwell continued, "In fact, this is the second time our London office has been served well by ServerGuard. In January it was a street power interruption that could have caused us problems, but ServerGuard performed well and we were back up immediately."

"In a trading floor environment like ours, time is money and we can't afford for our traders to lose access to information," said Maxwell. "The derivatives market experiences market surges during certain hours of the month. During these windows of opportunity we may generate a large portion of our monthly revenue. Our Auspex servers give us the high performance, and ServerGuard provides us with the failover protection we need."

greater performance, higher availability, simplified systems administration and increased expandability. The NetServers have provided us with the built-in capacity to better manage growth."

"Auspex's systems provide state-of-the-art server availability and reliability to our customers," says Joe Brown, Vice President of Worldwide Field Operations at Auspex. "Auspex's NetServer with ServerGuard ensures timely and continuous access to mission-critical data. By mirroring data at the file system level, ServerGuard provides high availability and disaster recovery with minimal network impact. Customers, like FCMC, now have an extra level of protection against catastrophic system and site failures."

AUSPEX CUSTOMERS: AN ONGOING SUCCESS STORY

Auspex Systems Receives Vehicle Design Center Certification from Major U.S. Automotive Manufacturer

Auspex Designated the Preferred Network File Server in Auto Company's Vehicle Design Centers Worldwide

Santa Clara, CA – August 7, 1996 – Auspex Systems today reported that its complete NetServer 7000 product family has been certified as the preferred Network File Serving system in the vehicle design centers of a major U.S. automotive manufacturer.

The vehicle design center (VDC) certification refers to a rigorous technical certification process, not only of the qualifying company's product, but of its operations and financial condition. A VDC certification means that a product has been determined to be the best of its class and is to be considered the product of choice based upon its clear technological advantages for a given application. The NetServer 7000 family has been designated as the NFS server of choice where demonstrated availability and throughput is critical. The automotive manufacturer granting VDC certification currently has 15 Auspex systems with over 5 terabytes of storage capacity deployed worldwide. This includes



9 systems at the vehicle design centers in the metropolitan Detroit area, one of which is the largest Mechanical Computer-Aided Design (MCAD) site in the automotive industry, with 5,000 employees and approximately 1,200 engineering workstations.

In a large distributed computing environment such as mechanical computer-aided design, Auspex NetServers improve network throughput and availability while consolidating data and simplifying network management. "The outstanding availability and performance of Auspex NetServers was critical to our success in achieving vehicle design center certification," said Bruce N. Moore, Auspex President and Chief Executive Officer. "We are the first new vendor to receive VDC certification from this particular company since 1987 and consider it a positive reflection, both on our product and Auspex's financial strength and prospects for growth."

NetServer Delivers Multimedia Excitement to Indy 500 Web Site

Santa Clara, CA – May 9, 1997 – Racing fans from around the world will enjoy multimedia presentations of race coverage and historic Indy 500 moments on the Auspex-based, Indy Racing League (IRL) web site. A high-performance, high-availability Auspex NetServer model NS 7000/700 is the network data server supporting the IRL's new web site and will enable the Indy site to house multimedia applications and other information.

"The Auspex NetServer is at the heart of the new Indy web site, bringing race enthusiasts up-to-the-minute information and the kind of multimedia excitement the web does so well," said Bruce N. Moore, President and CEO of Auspex. "Because hundreds of thousands of people will access this web site; reliable, continuous data access is critical. Our unmatched level of reliability uniquely qualifies Auspex as the server of choice for this application. The high-performance and scalability of our product makes it an excellent fit for delivering the large data files associated with such a complex, multimedia site."



"We're delighted to be involved with Auspex in the implementation of the IRL's web site," said F. William Conner, Executive Vice President at Nortel Enterprise Networks. "This project allowed the IRL to take advantage of the power of the internet. To do that, we needed Auspex's advanced data server to enable the site to deliver its extensive content and provide the multimedia excitement of the Indy racing experience. The Auspex NetServer has lived up to the IRL's site requirements."

Nortel Enterprise Networks played a critical role in the launch of the IRL's web site. Nortel is providing high-capacity, digital communications technology integration for the IRL.

FORTUNE 1000 AND WORLDWIDE LEADERS

Representative Customer List

AEROSPACE AND AUTOMOTIVE
 Allied Signal, Inc.
 BMW Rolls Royce Aero Engines
 Boeing Defense and Space Boeing North
 American Aircraft Division
 General Motors
 EDS Allison Transmission
 Honeywell Commercial Flight Systems
 Hughes Aircraft Company
 Lockheed Missiles & Space Co.
 NASA
 Pratt & Whitney Canada, Inc.
 SAAB Aircraft
 SAAB Automotive
 Siemens Automotive
 Snecma Villaroche

Ellemtel
 Ericsson Telecom
 Fujitsu Telecommunications
 Mannesmann Mobilfunk
 Northern Telecom
 Tellabs
 US West

COMPUTER MANUFACTURERS
 Amdahl Corporation
 Compaq Computer
 Dell Computer Corporation
 Hitachi Computer Products, Inc.
 IBM Corporation
 Stratus Computer, Inc.
 Tandem Computers, Inc.
 Xerox Corporation

ENTERTAINMENT AND GAMES
 Industrial Light & Magic
 Sega
 Walt Disney Imagineering
 Warner Bros.

FINANCE AND BANKING
 Barclays Bank
 Bear Stearns & Co. Inc.
 BlackRock Financial Mgmt. L.P.
 Caisse des Depots
 Chrysler Financial Corp.
 Credit Suisse First Boston
 Dow Jones & Company, Inc.
 Fidelity Investments
 First Union
 Fuji Capital Markets Corp.
 Great-West Life Assurance Co.
 Merrill Lynch
 NationsBanc
 Capital Markets, Inc.
 Paine Webber
 Swiss Bank Corporation
 Union Bank of Switzerland

INTERNET AND ON-LINE SERVICE PROVIDERS
 CERFnet
 Demon Internet Ltd.

Digital Express Group, Inc.
 France Telecom Interactive
 Flashnet Communications
 Internet America
 Network Solutions

NETWORKING
 3Com Corporation
 Bay Networks, Inc.
 Cabletron Systems, Inc.
 Cisco Systems, Inc.
 Network Express

OIL AND GAS
 Amerada Hess Corporation
 Anadarko Petroleum Corporation
 Apache Corporation
 BP Exploration
 Coastal Natural Gas
 Conoco Inc.
 Enserch Exploration
 Geco-Prakla
 Minerals Management Service
 Petro-Canada

Phibro Energy, Inc.
 Phillips Petroleum Co.
 Shell
 Total SA
 Union Pacific Resources
 Unocal
 Western Geophysical
 Zilkha Energy Company

RESEARCH
 FAW Forschungsinstitut
 Fraunhofer Institute
 Lawrence Livermore National Laboratories
 Los Alamos National Laboratory
 Sandia National Laboratories

SEMICONDUCTORS
 Advanced Micro Devices, Inc.
 Advanced RISC Machines
 LSI Logic Corporation
 Microchip Technology
 Micron Technology, Inc.
 Motorola, Incorporated

NEC USA, Inc.
 Rockwell Telecommunications
 Silicon Systems
 Xilinx

SOFTWARE PRODUCTS
 Adobe Systems, Inc.
 Avanti
 Cadence Design Systems
 ComputerVision Corp.
 Dassault Systems
 EDS Unigraphics
 iXOS
 Mentor Graphics Corporation
 MicroCADAM
 NeXT Computer, Inc.
 Progress Software
 Schlumberger Technologies
 Sybase, Inc.

SELECTED FINANCIAL DATA

(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

<i>Fiscal Year Ended,</i>	<i>June 30, 1997</i>	<i>June 30, 1996</i>	<i>June 30, 1995</i>	<i>June 30, 1994</i>	<i>June 30, 1993</i>
Net revenues	\$202,486	\$162,640	\$115,625	\$83,280	\$73,508
Income before income taxes	24,362	29,597	15,912	9,786	10,046
Net income	13,420	19,830	12,411	8,318	8,126
Net income per share	0.52 ⁽¹⁾	0.77	0.51	0.34	0.36
Total assets	157,152	135,844	106,526	85,433	76,728
Long-term obligations	—	—	159	399	799

(1) Includes the costs associated with the acquisition of Alphatronix, Inc. in the fourth quarter of fiscal 1997. Exclusive of these acquisition costs, earnings per share for fiscal 1997 would have been \$0.81.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

RESULTS OF OPERATIONS

Revenues for the fiscal year ended June 30, 1997 of \$202.5 million increased 24.5% over fiscal year 1996 revenues of \$162.6 million. To date, the Company has shipped approximately 2,100 data servers.

The following table sets forth, for the fiscal years indicated, the percentage of total revenues represented by certain line items in the Company's statement of operations:

<i>Years Ended June 30,</i>	<i>1997</i>	<i>1996</i>	<i>1995</i>
Revenues	100%	100%	100%
Costs of Revenues	46	44	46
Gross margin	54	56	54
Operating Expenses			
Sales and marketing	24	23	24
Research and development	12	11	13
General and administrative	4	5	5
In-process research and development	3	-	-
Income from operations	11	17	12
Other Income	1	1	2
Income before income taxes	12	18	14
Provision for Income Taxes	5	6	3
Net Income	<u>7%</u>	<u>12%</u>	<u>11%</u>

REVENUES

Product revenue includes hardware sales of systems and upgrades as well as software license fees. The Company recognizes revenues from sales of data servers to end users only when the product has been shipped, installed, and the customer has indicated a level of satisfaction with the product's performance that meets or exceeds predefined Company standards. Revenues from sales of data servers to distributors, integrators and OEMs, as well as product upgrade revenues, are generally recognized when the product has been shipped. Revenues earned under software license agreements with end users are generally recognized when the software has been shipped and there are no significant obligations remaining. Service revenue includes installation, maintenance and training and is recognized ratably over the contractual period or as the services are provided. Beginning with the first quarter of fiscal 1998, the Company will change its revenue recognition policy such that revenues from systems sales will generally be recognized when the equipment has been shipped. The reason for this change is to better conform its policies with industry practices.

The following table sets forth the principal components of the Company's revenue (in thousands):

<i>Years Ended June 30,</i>	<i>1997</i>	<i>1996</i>	<i>1995</i>
Product revenue	\$182,533	\$146,913	\$104,102
Service and other revenue	19,953	15,727	11,523
Total revenues	<u>\$202,486</u>	<u>\$162,640</u>	<u>\$115,625</u>

Product revenue increased \$35.6 million or 24% in fiscal 1997 as compared to fiscal 1996 and \$42.8 million, or 41%, in fiscal 1996 as compared to fiscal 1995. These increases were attributable to higher average system prices and increased sales of upgrades to the Company's installed base. Revenue from product upgrades, which primarily consists of additional processors (or upgrades of existing processors), and memory and disk and tape drives, increased from the prior year as a percentage of total revenues to 41% in fiscal 1997 from 39% in fiscal 1996 and decreased to 39% in fiscal 1996 from 44% in fiscal 1995. The increase in product upgrade revenue as a percentage of total revenues compared to fiscal 1996 is primarily due to the expansion of the Company's installed base, demand from customers for increased storage capacity and the Company's periodic product enhancements. There can be no assurance, however, that the Company's product revenue will continue to increase in absolute dollar amounts or at the rate at which it has grown in recent fiscal years.

The Company provides ongoing support and maintenance to its end user customers, distributors and OEMs generally under annual service agreements. Service revenue as a percentage of total revenues remained constant in fiscal 1997, 1996, and 1995 at 10%.

The following table sets forth the Company's revenue by geographic area (in thousands):

<i>Years Ended June 30,</i>	<i>1997</i>		<i>1996</i>		<i>1995</i>	
North America	\$142,536	70%	\$110,163	68%	\$85,251	74%
Pacific Rim	31,759	16%	36,229	22%	21,390	18%
Europe	28,191	14%	16,248	10%	8,984	8%
	<u>\$202,486</u>	<u>100%</u>	<u>\$162,640</u>	<u>100%</u>	<u>\$115,625</u>	<u>100%</u>

Revenue from North America increased \$32.4 million in fiscal 1997 as compared to fiscal 1996 and \$24.9 million in fiscal 1996 as compared to fiscal 1995. Revenue from Pacific Rim decreased \$4.5 million in fiscal 1997 as compared to fiscal 1996 and increased \$14.8 million in fiscal 1996 as compared to fiscal 1995. The decrease in Pacific Rim revenue as a percentage of total revenue and in absolute dollars in fiscal 1997 as compared to fiscal 1996 was primarily due to the reorganization of a major OEM partner, a delay in the introduction of Auspex's model NS 7000/700 NetServer by that partner in Japan and weakness in the Japanese economy.

Sales of products and services to Intel Corporation ("Intel") accounted for 10%, 10% and 15% of total revenues for the fiscal years ended June 30, 1997, 1996 and 1995, respectively. Sales to America Online ("AOL") accounted for 15% of total revenues for the fiscal year ended June 30, 1997. Additionally, sales to Fuji Xerox accounted for 13% of total revenues for the fiscal year ended June 30, 1996. No other customer accounted for 10% or more of total revenues for any of the three years in the period ended June 30, 1997. In addition to direct purchases from the Company, Intel or its affiliates have from time to time made significant purchases of the Company's products through indirect channels. Intel, AOL and Fuji Xerox are not obligated to purchase any minimum level of products from the Company. Accordingly, there can be no assurance that sales of products and services to Intel, AOL and Fuji Xerox will not decline, either in absolute dollar amounts or as a percentage of total revenues, in future periods and that any such declines will not have a material adverse effect on the Company's results of operations.

GROSS MARGIN

The Company's gross margin was 54%, 56% and 54% in fiscal 1997, 1996 and 1995, respectively. Costs of revenues include material costs, manufacturing and service overhead costs, installation and warranty expenses, obsolescence, the cost of spare parts and other related costs. The decrease in gross margins in fiscal 1997 as compared to fiscal 1996 was due to pricing on systems sales and lower margins on service. This was partially offset by a significant increase in software revenue. The improvement in margin in fiscal 1996 was attributable to engineering-related cost reductions in successive new product designs, increased production volumes, and improved manufacturing and service-related efficiencies.

OPERATING EXPENSES

Marketing and sales expenses increased \$10.4 million in fiscal 1997 as compared to fiscal 1996 and increased \$9.6 million in fiscal 1996 as compared to fiscal 1995, and were 24%, 23% and 24% of total revenues in fiscal 1997, 1996 and 1995, respectively. The increase in absolute dollars is the result of additional headcount in the North American direct sales operations and the growth of direct sales operations of the Company's international subsidiaries.

Research and development expenses, net of capitalized software development costs, increased \$6.6 million in fiscal 1997 as compared to fiscal 1996 and increased \$3.2 million in fiscal 1996 as compared to fiscal 1995, and represented 12%, 11% and 13% of total revenues in fiscal 1997, 1996 and 1995, respectively. The increase in net research and development expenses both in absolute dollars and as a percentage of total revenues in fiscal 1997 as compared to fiscal 1996 was due to the addition of employees and related project costs to support the Company's new product development efforts. The decrease in net research and development as a percent of total revenue in fiscal 1996 as compared to fiscal 1995 relates primarily to the increase in revenues. Software development expenses have been accounted for in accordance with Statement of Financial Accounting Standards No. 86, under which the Company is required to capitalize software development costs after "technological feasibility" is established. In the fourth quarter of fiscal 1994, the Company initiated several software development projects which resulted in the capitalization of \$0.7 million in fiscal 1995 and \$0.3 million in fiscal 1996. No amounts were capitalized in fiscal 1997. The amount of capitalized software development costs in any given period may vary depending on the exact nature of the development performed. The Company believes that in order to remain competitive, it will need to continue to make substantial investments in new and enhanced products, and anticipates that research and development expenses will increase in both absolute amounts and as a percentage of total revenues from current levels.

General and administrative expenses increased \$0.2 million in fiscal 1997 as compared to fiscal 1996 and increased \$1.9 million in fiscal 1996 as compared to fiscal 1995 and represented 4%, 5% and 5% of total revenues in fiscal 1997, 1996 and 1995, respectively. Although general and administrative expenses remained generally flat in absolute dollars in fiscal 1997 as compared to fiscal 1996, the Company anticipates that the cost of expanding infrastructure including new facilities will increase in fiscal 1998 to support the Company's growth.

On June 30, 1997, the Company acquired all of the outstanding shares of Alpatronix, Inc. ("Alpatronix"), a market leader in the development and marketing of open-systems based storage management solutions for a total purchase price of \$7.7 million. The acquisition was accounted for using the purchase method of accounting. A portion of the purchase price was allocated to assets acquired and liabilities assumed based on their estimated fair value. The fair value of tangible assets acquired and liabilities assumed was \$0.3 million and \$0.3 million, respectively. In addition, \$7.4 million of the purchase price was allocated to in-process research and development projects that had not reached technological feasibility and had no probable alternative future uses, which the Company expensed at the date of the acquisition as a one-time non-recurring charge. The remainder of the purchase price, \$0.3 million, was allocated to goodwill and will be amortized over five years on a straight-line basis. See Note 3 of Notes to the Consolidated Financial Statements.

Alphatronix's in-process research and development projects relate primarily to developing significant enhancements to the current product offering as well as introducing advanced new products. The incomplete projects include a new user interface, enterprise management support, a hierarchical storage management function, database journalizing, database insertion, differential dataset recovery, and on-demand restore ability. Given the uniqueness of the tasks and the technologies involved, alternative future uses for these projects, apart from the objectives and economies of the projects for which they are intended, do not exist.

The Company believes that the efforts to complete the acquired in-process research and development projects will consist of internally staffed engineering costs over the next one to two years. These costs are estimated to be approximately \$3,000,000 to complete the research and development. There can be no assurance that the Company will succeed in making commercially viable products from the Alphatronix research and development.

OTHER INCOME

Other income and expense resulted in income of \$2.4 million, \$1.8 million and \$2.0 million in fiscal 1997, 1996 and 1995, respectively. Other income and expense includes interest income, interest expense and foreign exchange gains and losses. Interest income was \$2.3 million, \$1.8 million and \$1.7 million in fiscal 1997, 1996 and 1995, respectively. The increase in interest income in fiscal 1997 as compared to fiscal 1996 primarily relates to an increase in the cash and short-term investments balances.

PROVISION FOR INCOME TAXES

As of June 30, 1997, the Company had gross deferred tax assets of approximately \$5.9 million. Management has determined, based on the Company's history of prior operating earnings and its expectations for future years, that the deferred tax asset is realizable. However, no assurances can be given that sufficient taxable income will be generated in future years for the utilization of the deferred tax asset.

The provision for income taxes was approximately \$10.9 million in fiscal 1997, \$9.8 million in fiscal 1996, and \$3.5 million in fiscal 1995, representing effective tax rates of approximately 45%, 33% and 22%, respectively. The increase in the effective tax rate in fiscal 1997 as compared to fiscal 1996 is attributable to the fact that the Company has not provided any tax benefits related to the write-off of in-process research and development expenses of approximately \$7.4 million resulting from the acquisition of Alphatronix. Excluding the write-off of in-process research and development expenses which accounts for an increase of 10.5% in the effective tax rate in fiscal 1997, the Company's effective tax rate was 34.5%.

QUARTERLY RESULTS OF OPERATIONS

The following table sets forth selected unaudited quarterly financial information for the Company's last eight quarters. This unaudited information has been prepared on the same basis as the audited information and in management's opinion reflects all adjustments (which include only normal recurring adjustments) necessary for the fair presentation of the information for the periods presented. Based on the Company's operating history and factors that may cause fluctuations in the quarterly results, quarter-to-quarter comparisons should not be relied upon as indicators of future performance. Although the Company's revenues are not generally seasonal in nature, the Company has experienced decreases in first quarter revenue versus the preceding fourth quarter which is believed to result primarily from the capital asset purchase cycle of the Company's customers.

The level of the Company's operating expenses is partially based on its expectations of future revenue. The Company's results of operations may be adversely affected if revenue does not materialize in a period as expected. Since expense levels are usually committed in advance of revenues and because only a small portion of expenses vary with revenue, the Company's net income may be impacted significantly by lower revenue. The Company's revenue increased each quarter in fiscal 1997 as compared to the equivalent quarter in the prior year. This increase was due principally to increased sales volume or higher average selling prices of the Company's products.

1997 Summary by Quarter

<i>(In thousands, except per share amounts)</i>	<i>first</i>	<i>second</i>	<i>third</i>	<i>fourth</i>	<i>year</i>
Net revenues	\$ 43,012	\$ 49,082	\$ 55,602	\$ 54,790	\$ 202,486
Gross profit	23,912	26,645	30,458	28,463	109,478
Income before taxes	6,620	7,603	10,057	82	24,362
Net income (loss)	4,270	4,904	6,487	(2,241)	13,420
Net income (loss) per share	\$ 0.17	\$ 0.19	\$ 0.25	\$ (0.09) ⁽¹⁾	\$ 0.52 ⁽¹⁾

(1) Includes the costs associated with the acquisition of Alphatronix, Inc. in the fourth quarter of fiscal 1997. Exclusive of these acquisition costs, earnings per share for fiscal 1997 would have been \$0.81.

1996 Summary by Quarter

<i>(In thousands, except per share amounts)</i>	<i>first</i>	<i>second</i>	<i>third</i>	<i>fourth</i>	<i>year</i>
Net revenues	\$ 33,536	\$ 38,003	\$ 43,333	\$ 47,768	\$ 162,640
Gross profit	18,294	21,166	24,202	27,012	90,674
Income before taxes	5,276	6,996	8,046	9,279	29,597
Net income	3,535	4,687	5,391	6,217	19,830
Net income per share	\$ 0.14	\$ 0.18	\$ 0.21	\$ 0.24	\$ 0.77

FACTORS THAT MAY AFFECT FUTURE RESULTS

This document includes forward-looking statements relating to anticipated revenue growth, anticipated product introductions and performance in the Japanese market. Actual results could differ materially from those contemplated by any such forward-looking statements due to a number of factors, including the Company's ability to develop and deliver new products on schedule, market acceptance of such products, the impact of competitive products and pricing, general economic conditions, and the factors set forth below. The Company may also make oral and written forward-looking statements from time to time. Actual results may differ materially from those projected in any such forward-looking statements due to a number of factors, including those set forth below. The Company undertakes no obligation to update such information.

POTENTIAL SIGNIFICANT FLUCTUATIONS IN QUARTERLY RESULTS

The Company's operating results may fluctuate significantly from quarter to quarter due to a combination of factors. These factors include the timing of orders, the timing of new product introductions by the Company or its competitors and the mix of distribution channels through which the Company's products are sold. The Company generally realizes higher gross margins on sales of systems to end users and on single system sales than on systems sold through distributors and OEMs and on multiple system sales. In addition, given the Company's focus on highly configured enterprise-class systems, the loss or delay in a given quarter of a relatively limited number of system sales could adversely affect the Company's revenues. Historically, the Company has often recognized a substantial portion of its revenues in the last month of any given quarter. Because the Company's operating expenses are based on anticipated revenue levels and because a high percentage of the Company's expenses are relatively fixed, a small variation in the timing of the recognition of revenues could cause significant variations in operating results from quarter to quarter.

INTENSELY COMPETITIVE MARKET

The market for the Company's products is intensely competitive. The Company experiences substantial competition, principally from Sun Microsystems, Hewlett-Packard Company and Silicon Graphics, Inc. Also, EMC Corporation has recently introduced proprietary products to provide network attached storage. In addition, smaller companies such as Network Appliance, Inc. have introduced products at the low end of the Company's target markets. Most of the Company's competitors are better known and have substantially greater financial, technological, production and marketing resources than the Company. While the Company believes that the price/performance characteristics of its products are competitive, price competition in the markets for the Company's products is intense. Any material reduction in the price of the Company's products without corresponding decreases in manufacturing costs and increases in unit volume would negatively affect gross margins which could in turn have a material adverse effect on the Company's business, financial condition and results of operations. The Company also derives a significant portion of its revenues from sales of product upgrades to its installed base, including additional processors, and memory and disk and tape drives. Increased competition for the Company's products that result in lower product sales could also adversely impact the Company's upgrade sales. In addition, decisions by customers not to increase capacity to their current systems could adversely impact the Company's revenues and results of operations. The Company's ability to maintain its competitive position will depend, among other factors, upon its success in anticipating industry trends, investing in product research and development, developing new products with improved price/performance characteristics and effectively managing the introduction of new products into targeted markets.

DEPENDENCE ON KEY PERSONNEL

Competition for employees with highly technical, management and other skills is intense in the computer industry and is particularly intense in the San Francisco Bay Area. The Company has in the past encountered some difficulties in fulfilling its hiring needs and retaining key employees in this market, and there can be no assurance that the Company will be successful in hiring and retaining qualified employees in the future. The Company's failure to retain the services of key personnel or to attract additional qualified employees could have a material adverse effect on the Company's business, financial condition and results of operations.

SOFTWARE PRODUCT RISKS

With the release of its DriveGuard and FastBackup software products along with current software products ServerGuard and DataGuard, the Company now markets software products in addition to its line of network file servers. The Company also expects to release enhancements and new features for these products from time to time. Although the Company performs extensive testing prior to releasing software products, such products may contain undetected errors or bugs when first released. These may not be discovered until the product has been used by customers in different application environments. Failure to discover product deficiencies or bugs could delay product introductions, require design modifications to previously shipped products, cause unfavorable publicity or negatively impact system shipments, any of which could result in a material adverse effect on the Company's business, financial condition and results of operations.

NEW PRODUCTS

New product introductions by the Company or its competitors carry the risk that customers could delay or cancel orders for existing products pending shipment of the new products. The Company's strategy is to continue to introduce new products and upgrades to existing products on an ongoing basis. There can be no assurance that the Company will not experience difficulties that delay or prevent the successful development, introduction or marketing of these products and enhancements or that these new products and enhancements will adequately address market requirements and achieve market acceptance. Any delays in the launch or availability of new products could have a material adverse effect on the Company's business, financial condition and results of operations.

DEPENDENCE ON ESTABLISHED STANDARDS

The rapid emergence of new or alternate standards such as NT which replace or diminish the market acceptance of UNIX operating systems or NFS, on which the Company's products are currently based, could materially and adversely affect the Company's results of operations unless the Company is able to incorporate any such standards in the Company's products in a timely manner.

DEPENDENCE ON CERTAIN CUSTOMERS/DISTRIBUTORS

For fiscal year 1997 and 1996, direct sales of products and services to Intel represented approximately 10% and 15%, respectively, of the Company's revenues. In addition to direct purchases from the Company, Intel or its affiliates have from time to time made significant purchases of the Company's products through indirect channels. Also in fiscal year 1997, direct sales of products and services to AOL represented approximately 15% of the Company's revenues. For fiscal year 1996, sales to Fuji Xerox, the Company's non-exclusive master value added distributor in Japan, represented approximately 13% of the Company's revenues. Intel, AOL and Fuji Xerox are not obligated to purchase any minimum level of products from the Company. A significant reduction in product sales to Intel, AOL or Fuji Xerox would materially and adversely affect the Company's business, financial condition and results of operations.

DEPENDENCE ON CERTAIN SUPPLIERS

Certain of the Company's products contain critical components supplied by a single or a limited number of third parties. While the Company has an inventory of these critical components, any significant or prolonged shortage of these components or the failure of the third-party suppliers to maintain or enhance these components could materially adversely affect the Company's results of operations.

RISKS OF INTERNATIONAL SALES; EUROPEAN AND JAPANESE MARKET RISKS

During fiscal year 1997 and 1996, approximately 30% and 32%, respectively, of the Company's total revenues were derived from markets outside of North America. The Company expects that sales to the Pacific Rim and Europe will continue to represent a significant portion of its business. There can be no assurance that the Company's Pacific Rim or European operations will continue to be successful. The Company's international business may be affected by changes in demand resulting from localized economic and market conditions. In addition, the Company's international business may be affected by fluctuations in currency exchange rates and currency restrictions as well as by risks such as trade restrictions, increases in tariff and freight rates and difficulties in obtaining necessary export licenses and meeting appropriate local regulatory standards. For example, the Company has had to modify its products in minor respects in Japan to comply with local electromagnetic emissions standards, and must also comply with corresponding European Economic Community standards. In marketing its products to the European Economic Community, the Company also must face the challenges posed by a fragmented market complicated by local distribution channels and local cultural considerations. For international sales, the Company has largely relied on distributors or OEMs, most of whom are entitled to carry products of the Company's competitors.

INTELLECTUAL PROPERTY AND PROPRIETARY RIGHTS; PENDING LITIGATION

The Company currently relies on a combination of patent, copyright, trademark and trade secret laws and contractual provisions to protect its proprietary rights in its hardware and software products. The Company currently holds six United States patents and has filed applications for additional patents. The Company has also filed applications for counterpart patents in foreign countries, including Japan. There can be no assurance that the Company's present or future competitors will not independently develop technologies that are substantially equivalent or superior to the Company's technology. Further, there can be no assurance that the Company's patent applications will result in issued patents, or that the Company's issued patents will be upheld if challenged. Additionally, there can be no assurance that third parties will not assert intellectual property infringement claims against the Company in the future with respect to current or future projects or that any such assertions may not require the Company to refrain from the sale of its products, enter into royalty arrangements or undertake costly litigation.

The Company's adherence to industry standards with respect to its products limits the Company's opportunities to provide proprietary features which may be protected. In addition, the laws of various countries in which the Company's products may be sold may not protect the Company's products and intellectual property rights to the same extent as the laws of the United States.

The Company is a defendant in various lawsuits and is subject to various claims which arise in the normal course of business. In the opinion of management, the ultimate dispositions of these claims will not have a material adverse effect on the financial position, liquidity or results of operations of the Company.

LIQUIDITY AND CAPITAL RESOURCES

The Company's cash, cash equivalents and short-term investments increased \$10.4 million as of June 30, 1997, compared to June 30, 1996, and increased \$5.9 million as of June 30, 1996, compared to June 30, 1995. The Company generated approximately \$28.6 million, \$16.9 million and \$9.4 million in cash from operating activities in fiscal 1997, 1996 and 1995, respectively. The increase of cash from operating activities in each year was due primarily to an increase in net income in each year.

The Company's principal investing activities consisted of the purchase of property and equipment which were \$16.4 million, \$15.4 million and \$8.1 million in fiscal 1997, 1996 and 1995, respectively. These expenditures were primarily for leasehold improvements, equipment for research and development, manufacturing test equipment, office equipment and spare parts to support customer service contracts. The Company currently anticipates capital expenditures of approximately \$35 million to \$40 million in fiscal year 1998, primarily for leasehold improvements, engineering, manufacturing and office equipment and spare parts support. The Company also used cash of \$7.5 million, \$1.3 million and \$2.9 million for short-term investments in fiscal 1997, 1996 and 1995, respectively.

The Company's primary financing activities included proceeds from the sale of common stock pursuant to employee benefit plans of \$4.1 million, \$5.0 million and \$1.7 million in fiscal 1997, 1996 and 1995, respectively. In addition, the Company made principal payments on capital leases of \$0.1 million, \$0.4 million and \$0.6 million in fiscal 1997, 1996 and 1995, respectively.

As of June 30, 1997, working capital was \$105.4 million as compared with \$90.9 million as of June 30, 1996. The Company anticipates that its current cash and short-term investment balances and expected cash flow from operations will be sufficient to meet its working capital and capital expenditure requirements at least through fiscal 1998.

CONSOLIDATED STATEMENTS OF OPERATIONS

<i>Years Ended (In thousands, except per share amounts)</i>	<i>June 30, 1997</i>	<i>June 30, 1996</i>	<i>June 30, 1995</i>
Revenues			
Product revenue	\$ 182,533	\$146,913	\$ 104,102
Service revenue	<u>19,953</u>	<u>15,727</u>	<u>11,523</u>
Total revenues	<u>202,486</u>	<u>162,640</u>	<u>115,625</u>
Cost of Revenues			
Cost of product revenue	79,062	62,126	46,617
Cost of service revenue	<u>13,946</u>	<u>9,840</u>	<u>6,833</u>
Total cost of revenues	<u>93,008</u>	<u>71,966</u>	<u>53,450</u>
Gross profit	<u>109,478</u>	<u>90,674</u>	<u>62,175</u>
Operating Expenses			
Marketing and sales	48,047	37,647	28,069
Research and development	24,449	17,843	14,621
General and administrative	7,672	7,431	5,567
In-process research and development	<u>7,354</u>	<u>—</u>	<u>—</u>
Total operating expenses	<u>87,522</u>	<u>62,921</u>	<u>48,257</u>
Income from operations	<u>21,956</u>	<u>27,753</u>	<u>13,918</u>
Other Income			
Interest income	2,265	1,813	1,746
Interest expense	(20)	(81)	(55)
Other income	<u>161</u>	<u>112</u>	<u>303</u>
Total other income	<u>2,406</u>	<u>1,844</u>	<u>1,994</u>
Income before provision for income taxes	24,362	29,597	15,912
Provision for Income Taxes	<u>10,942</u>	<u>9,767</u>	<u>3,501</u>
Net Income	<u>\$ 13,420</u>	<u>\$ 19,830</u>	<u>\$ 12,411</u>
Net Income per Share	<u>\$ 0.52</u>	<u>\$ 0.77</u>	<u>\$ 0.51</u>
Weighted Average Common Shares and Equivalents	<u>25,658</u>	<u>25,702</u>	<u>24,371</u>

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

CONSOLIDATED BALANCE SHEETS

<i>(In thousands, except share and per share amounts)</i>	<i>June 30, 1997</i>	<i>June 30, 1996</i>
Assets		
Current Assets:		
Cash and cash equivalents	\$ 25,056	\$ 22,169
Short-term investments	35,830	28,349
Trade receivables, net of allowances of \$1,193 and \$1,535, respectively	43,130	37,848
Inventories	18,096	16,130
Prepaid expenses and other	12,158	12,447
Total current assets	134,270	116,943
Property and Equipment:		
Computer and manufacturing equipment	37,893	27,850
System spares	17,465	13,107
Furniture and fixtures	4,624	3,351
Leasehold improvements	3,006	2,573
Subtotal	62,988	46,881
Less—accumulated depreciation and amortization	(42,952)	(31,304)
Total property and equipment, net	20,036	15,577
Other Assets	2,846	3,324
Total assets	\$ 157,152	\$ 135,844
Liabilities and Stockholders' Equity		
Current Liabilities:		
Current portion of capital lease obligations	\$ 95	\$ 136
Accounts payable	6,906	6,165
Accrued liabilities	12,280	12,712
Income tax payable	64	440
Deferred revenue	9,491	6,578
Total current liabilities	28,836	26,031
Stockholders' Equity:		
Common stock, \$.001 par value—50,000,000 shares authorized; 25,004,965 and 24,527,188 shares issued, respectively; 25,004,965 and 24,360,507 shares outstanding, respectively	25	24
Additional paid-in capital	78,435	73,169
Notes receivable from sale of common stock	-	(49)
Retained earnings	50,261	36,841
Unrealized loss from available-for-sale securities	(5)	-
Cumulative translation adjustment	(400)	(172)
Total stockholders' equity	128,316	109,813
Total liabilities and stockholders' equity	\$ 157,152	\$ 135,844

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

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

For the three years ended June 30, 1997	Common Stock		Additional	Notes	Retained	Unrealized	Cumulative	
	Shares	Amount	Paid-in Capital	Receivable	Earnings	Loss on Available- For-Sale Securities	Translation Adjustment	Total
<i>(In thousands, except share amounts)</i>								
BALANCE, JUNE 30, 1994	22,897,816	\$23	\$62,332	(\$334)	\$4,600	\$ -	\$9	\$66,630
Issuance of common stock to employees	418,883	-	1,601	-	-	-	-	1,601
Repayment of notes receivable	-	-	-	67	-	-	-	67
Repurchase of previously exercised stock options	(15,573)	-	(4)	-	-	-	-	(4)
Translation adjustment	-	-	-	-	-	-	(6)	(6)
Net income	-	-	-	-	12,411	-	-	12,411
BALANCE, JUNE 30, 1995	23,301,126	23	63,929	(267)	17,011	-	3	80,699
Issuance of common stock to employees	1,065,632	1	4,829	-	-	-	-	4,830
Repayment of notes receivable	-	-	-	218	-	-	-	218
Repurchase of previously exercised stock options	(6,251)	-	(4)	-	-	-	-	(4)
Tax benefits related to exercise of stock options	-	-	4,415	-	-	-	-	4,415
Translation adjustment	-	-	-	-	-	-	(175)	(175)
Net income	-	-	-	-	19,830	-	-	19,830
BALANCE, JUNE 30, 1996	24,360,507	24	73,169	(49)	36,841	-	(172)	109,813
Issuance of common stock to employees	652,859	1	4,097	-	-	-	-	4,098
Repayment of notes receivable	-	-	-	49	-	-	-	49
Repurchase of previously exercised stock options	(8,401)	-	(10)	-	-	-	-	(10)
Tax benefits related to exercise of stock options	-	-	1,179	-	-	-	-	1,179
Unrealized loss on available for-sale securities	-	-	-	-	-	(5)	-	(5)
Translation adjustment	-	-	-	-	-	-	(228)	(228)
Net income	-	-	-	-	13,420	-	-	13,420
BALANCE, JUNE 30, 1997	25,004,965	\$25	\$78,435	-	\$50,261	(\$5)	(\$400)	\$128,316

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years Ended (In thousands)	June 30, 1997	June 30, 1996	June 30, 1995
Cash Flows from Operating Activities:			
Net income	\$ 13,420	\$ 19,830	\$ 12,411
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	12,435	8,885	8,030
In-process research and development	7,354	-	-
Changes in assets and liabilities:			
Increase in trade receivables	(5,282)	(10,295)	(10,628)
(Increase) decrease in inventories	(1,966)	1,014	(4,513)
(Increase) decrease in prepaid expenses and other	289	(8,174)	(161)
(Increase) decrease in other assets	(1,687)	579	(3,225)
Increase (decrease) in accounts payable	741	(1,248)	(874)
Increase (decrease) in accrued liabilities	(432)	5,343	1,576
Increase (decrease) in income tax payable	803	(354)	5,185
Increase in deferred revenue	2,913	1,285	1,647
Net cash provided by operating activities	<u>28,588</u>	<u>16,865</u>	<u>9,448</u>
Cash Flows from Investing Activities:			
Purchases of held-to-maturity short-term investments	-	(37,818)	(44,228)
Purchases of available-for-sale short-term investments	(38,220)	-	-
Proceeds from maturities of held-to-maturity short-term investments	-	30,858	41,348
Proceeds from sales of held-to-maturity short-term investments	-	4,591	-
Proceeds from sales/maturities of available-for-sale short-term investments	30,734	1,048	-
Payment for Alphatronix, Inc. acquisition, net of cash acquired	(5,600)	-	-
Purchases of property and equipment	<u>(16,385)</u>	<u>(15,405)</u>	<u>(8,052)</u>
Net cash used in investing activities	<u>(29,471)</u>	<u>(16,726)</u>	<u>(10,932)</u>
Cash Flows from Financing Activities:			
Principal payments on capital lease obligations	(139)	(407)	(571)
Proceeds from sale of common stock, net	4,147	5,048	1,668
Repurchase of common stock	(10)	(4)	(4)
Net cash provided by financing activities	<u>3,998</u>	<u>4,637</u>	<u>1,093</u>
Effect of Exchange Rate Changes on Cash	<u>(228)</u>	<u>(175)</u>	<u>(6)</u>
Net Increase (Decrease) in Cash and Cash Equivalents	2,887	4,601	(397)
Cash and Cash Equivalents, Beginning of Year	<u>22,169</u>	<u>17,568</u>	<u>17,965</u>
Cash and Cash Equivalents, End of Year	<u>\$ 25,056</u>	<u>\$ 22,169</u>	<u>\$ 17,568</u>

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1 | Organization

Auspex Systems, Inc. (the "Company") was incorporated in 1987 in California and reincorporated in Delaware in 1991 to develop, manufacture, market, sell and support a line of high-performance UNIX multi-protocol network file/data servers for the technical workstation market. The Company's markets are principally in North America, Pacific Rim and Europe and include customers in the technical and commercial computing market. See Note 9 for information on revenues by geographic area.

2 | Summary of Significant Accounting Policies

PRINCIPLES OF CONSOLIDATION. The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries after elimination of intercompany accounts and transactions.

ESTIMATES IN THE PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

FOREIGN CURRENCY TRANSLATIONS. The functional currency of the Company's foreign subsidiaries is the local currency. Accordingly, gains and losses resulting from the translation of the subsidiaries' financial statements are reported as a separate component of stockholders' equity.

REVENUE RECOGNITION. Product revenue includes hardware sales and software license fees. Revenues from system sales to end users are generally recognized when the equipment has been shipped, installed and accepted by the end user. Revenues from system sales to distributors, integrators and OEMs, as well as product upgrades, are generally recognized when the equipment has been shipped. Revenues earned under software license agreements with end users are generally recognized when the software has been shipped and there are no significant obligations remaining. Service revenue includes installation, maintenance and training and is recognized ratably over the contractual period or as the services are provided. Beginning with the first quarter of fiscal 1998, the Company will change its revenue recognition policy such that revenues from systems sales will generally be recognized when the equipment has been shipped. The reason for this change is to better conform its policies with industry practices.

CASH, CASH EQUIVALENTS AND SHORT-TERM INVESTMENTS. Substantially all cash equivalents consist of investments in certificates of deposit, money market deposits, and municipal bonds with original maturities of three months or less. Substantially all short-term investments consist of municipal bonds which the Company intends to hold between three and twelve months.

The Company classifies its investments in debt and equity securities as available-for-sale in accordance with Statement of Financial Accounting Standards (SFAS) No. 115, "Accounting for Certain Investments in Debt and Equity Securities." Securities classified as available-for-sale are reported at fair market value with the related unrealized gains and losses, net of tax, reported as a separate component of stockholders' equity. Realized gains and losses and declines in value judged to be other than temporary are included in other income.

At June 30, 1997, the Company's available-for-sale securities had contractual maturities that expire at various dates through August 1998. The fair value of available-for-sale securities was determined based on quoted market prices at the reporting date for those securities. At June 30, 1997 and 1996, the amortized cost basis, aggregate fair value and gross unrealized holding gains (losses) by major security type are as follows (in thousands):

<i>June 30, 1997</i>	Amortized Cost	Aggregate Fair Value	Unrealized Gains (Losses)
Available-for-Sale Securities:			
Municipal bonds	\$ 48,653	\$ 48,648	\$ (5)
<hr/>			
<i>June 30, 1996</i>			
Available-for-Sale Securities:			
Municipal bonds	\$ 35,137	\$ 35,098	\$ (39)
Certificate of deposit	61	61	-
	<hr/>		
Total investments in securities	\$ 35,198	\$ 35,159	\$ (39)

In fiscal year 1997, there were no significant gains or losses realized on the Company's cash equivalents or short-term investments. One available-for-sale security was sold in fiscal year 1996 with proceeds of \$1,048,000, providing a realized gain of \$1,000 (the realized gain was calculated using the 'specific identification' method).

In the fourth quarter of fiscal 1996, upon the Company's re-evaluation of its investment portfolio, all of the Company's securities were reclassified from held-to-maturity to available-for-sale for SFAS No. 115 purposes. During fiscal 1996, the Company sold, prior to maturity, securities previously classified as held-to-maturity with an amortized cost aggregating \$4,362,000. Total proceeds from these sales were \$4,591,000, with total interest and realized gain of \$229,000.

SUPPLEMENTAL STATEMENT OF CASH FLOWS DISCLOSURES. The Company acquired certain equipment under capital lease obligations at a cost of approximately \$61,000 in fiscal 1995. No equipment was acquired during fiscal 1997 and 1996 under capital lease obligations. Cash paid for interest during fiscal 1997, 1996 and 1995 was approximately \$20,000, \$81,000 and \$55,000, respectively. Cash paid for income taxes during fiscal 1997, 1996 and 1995 was approximately \$6,052,000, \$15,256,000 and \$1,073,000, respectively. In fiscal 1997 and 1996, non-cash activity consisted of \$1,179,000 and \$4,415,000, respectively from tax benefits related to exercise of stock options.

CONCENTRATIONS OF CREDIT RISK. Financial instruments which potentially subject the Company to concentrations of credit risk consist principally of cash investments and accounts receivables. The Company's cash investment policy limits the amount of credit exposure to any one issuer and restricts purchase of these investments to issuers evaluated as creditworthy. Concentrations of credit risk in trade receivables is limited as a result of the large number of customers comprising the Company's customer base and their dispersion across many different industries and geographies.

INVENTORIES. Inventories are stated at the lower of cost (first-in, first-out) or market, and include material, labor and manufacturing overhead. Inventories consisted of the following (in thousands):

	June 30, 1997	June 30, 1996
Purchased materials	\$ 6,382	\$ 4,366
Systems in process	7,885	7,082
Finished goods	3,829	4,682
	<u>\$ 18,096</u>	<u>\$ 16,130</u>

Inventories contained components and assemblies in excess of the Company's current estimated requirements and were fully reserved at June 30, 1997 and 1996. Due to competitive pressures, it is reasonably possible that these estimates could change in the near term.

Certain of the Company's products contain critical components supplied by a single or a limited number of third parties. While the Company has an inventory of these critical components, any significant or prolonged shortage of these components or the failure of the third-party suppliers to maintain or enhance these components could materially adversely affect the Company's results of operations.

PROPERTY AND EQUIPMENT. Property and equipment are stated at cost. Depreciation and amortization are computed using the straight-line method over the following estimated useful lives:

Computer and manufacturing equipment	1.5 to 2 years
System spares	2 to 3 years
Furniture and fixtures	3 years
Leasehold improvements	Shorter of the lease term or estimated useful life

SOFTWARE DEVELOPMENT COSTS. The Company capitalizes software development costs in compliance with SFAS No. 86, "Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed." Capitalization of software development costs begins upon the determination of technological feasibility. The determination of technological feasibility and the ongoing assessment of the recoverability of these costs require considerable judgment by management with respect to certain external factors including anticipated future gross product revenues, estimated economic life and changes in hardware and software technology. Software development costs capitalized during fiscal 1996 and 1995 amounted to \$274,000 and \$729,000, respectively. No amounts were capitalized in fiscal 1997.

Amortization of capitalized software development costs begins when the products are available for general release to customers and is computed on an individual product basis and is the greater of the amount computed on a units-sold basis or straight-line basis over the estimated economic life of the product. Amortization of software development costs amounted to \$411,000, \$220,000 and \$28,000 for the years ended June 30, 1997, 1996 and 1995, respectively.

ACCRUED LIABILITIES. Accrued liabilities consisted of the following (in thousands):

	June 30, 1997	June 30, 1996
Payroll, bonus and vacation	\$ 5,439	\$ 6,066
Other	6,841	6,646
	<u>\$ 12,280</u>	<u>\$ 12,712</u>

NET INCOME PER SHARE. Net income per share is computed using the weighted-average number of shares of common stock, and dilutive common equivalent shares from stock options using the treasury stock method. Fully diluted net income per share is substantially the same as primary net income per share.

In February 1997, the Financial Accounting Standards Board issued SFAS No. 128, "Earnings per Share," which is required to be adopted by the Company in its second quarter of fiscal 1998. At that time, the Company will be required to change the method currently used to compute net income per share and to restate all prior periods presented. Under the new requirements for calculating net income per share, primary net income per share will be replaced with basic net income per share and fully diluted net income per share will be replaced with diluted net income per share. Under basic net income per share, the dilutive effect of stock options will be excluded. The calculation of basic net income per share for the years ended June 30, 1997, 1996 and 1995 results in \$0.54, \$0.84 and \$0.54 per share, respectively. Diluted net income per share is substantially the same as the reported primary net income per share.

EMPLOYEE STOCK PLANS. Effective July 1, 1996, the Company adopted SFAS No. 123, "Accounting for Stock-Based Compensation." In accordance with the provisions of SFAS No. 123, the Company applies APB Opinion No. 25 and related interpretations to account for its employee stock option and stock purchase plans and, accordingly, does not recognize compensation expense. Note 7 of the Consolidated Financial Statements contains a summary of the pro forma effects to reported net income and earnings per share for 1997 and 1996 as if the Company had elected to recognize compensation expense based on the fair value of the options granted at grant date as prescribed by SFAS No. 123.

NEW ACCOUNTING PRONOUNCEMENTS. In June 1997, the Financial Accounting Standards Board issued SFAS No. 130, "Reporting Comprehensive Income," which establishes standards for disclosure and financial statement display for reporting total comprehensive income and its individual components. Comprehensive income as defined includes all changes in equity during a period from non-owner sources. The Company is required to adopt SFAS No. 130 in its first quarter of fiscal 1999. At that time, reclassification of financial statements for earlier periods for comparative purposes is required. The Company does not expect the adoption of SFAS No. 130 to have a material effect on the consolidated financial statements.

In June 1997, the Financial Accounting Standards Board issued SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information," which establishes annual and interim reporting standards for an enterprise's business segments and related disclosures about its products, services, geographic areas and major customers. The Company is required to adopt SFAS No. 131 in fiscal 1999 and does not expect such adoption to have a material effect on the consolidated financial statements.

3 | Acquisition

On June 30, 1997, the Company acquired all of the outstanding shares of Alpatronix, Inc. ("Alpatronix"), a market leader in the development and marketing of open-systems based storage management solutions for a total purchase price of \$7.7 million. The acquisition was accounted for using the purchase method of accounting. A portion of the purchase price was allocated to assets acquired and liabilities assumed based on their estimated fair value. The fair value of tangible assets acquired and liabilities assumed was \$0.3 million and \$0.3 million, respectively. In addition, \$7.4 million of the purchase price was allocated to in-process research and development projects that had not reached technological feasibility and had no probable alternative future uses, which the Company expensed at the date of the acquisition as a one-time non-recurring charge. The remainder of the purchase price, \$0.3 million, was allocated to goodwill and will be amortized over five years on a straight-line basis. Comparative pro forma information has not been presented, as the results of operations for Alpatronix are not material to the Company's financial statements.



4 | Line of Credit

In November 1996, the Company entered into a revolving line of credit agreement with a bank under which it can borrow up to \$15,000,000. The line of credit bears interest at LIBOR plus 1.5% (7.3% at June 30, 1997) for increments in excess of \$250,000 and at the bank's reference rate on all other borrowings (8.5% at June 30, 1997) and expires on October 31, 1997. At June 30, 1997 there were no borrowings outstanding under the line of credit agreement. The line of credit agreement contains certain financial covenants determined on a quarterly basis.

5 | Commitments and Contingencies

Facilities and equipment are leased under various capital and operating leases. Rent expense was approximately \$3,197,000, \$2,564,000 and \$1,823,000, for fiscal 1997, 1996 and 1995, respectively. The Company did not enter into any new capital leases in fiscal 1997 and 1996. Also during fiscal 1997, the Company entered into lease agreements for four buildings under construction in Santa Clara, California. The leases for these facilities commence in March 1998 and expire in February 2010. In addition, the lease agreements contain three successive options to extend the lease terms for sixty months each.

As of June 30, 1997, future minimum lease payments under non-cancelable leases were as follows (in thousands):

Years Ending June 30,	Capital Leases	Operating Leases
1998	\$ 50	\$4,091
1999	46	5,431
2000	—	5,263
2001	—	5,119
2002	—	4,941
Thereafter	—	40,959
Total minimum lease payments	96	<u>\$ 65,804</u>
Less: Amount representing interest (8%)	<u>(1)</u>	
Present value of lease payments	<u>\$ 95</u>	

As of both June 30, 1997 and 1996, the cost of such leased equipment was approximately \$1,401,000 with accumulated amortization of \$1,401,000 and \$1,391,000, respectively.

The Company is a defendant in various lawsuits and is subject to various claims which arise in the normal course of business. In the opinion of management, the ultimate dispositions of these claims will not have a material adverse effect on the financial position, liquidity or results of operations of the Company.

6 | Capital Stock

During 1994, the Company repurchased approximately 600,000 shares of common stock for approximately \$3.8 million. As of June 30, 1997, the Company has reserved the following shares of authorized but unissued common stock:

Stock option plan	5,830,352
Directors' stock option plan	159,000
Employee stock purchase plan	<u>147,997</u>
	<u>6,137,349</u>

7 | Stock Option and Stock Purchase Plans

The Company has two stock option plans, the 1988 Employee Stock Option Plan (1988 Plan) and the Directors' Stock Option Plan (Directors' Plan), and an employee stock purchase plan (The 1993 Employee Stock Purchase Plan). The Company accounts for these plans under APB Opinion No. 25, under which no compensation cost has been recognized.

Had compensation cost for these plans been determined consistent with SFAS No. 123, the Company's net income and earnings per share would have been reduced to the following pro forma amounts (in thousands, except per share data):

<u>Net Income</u>	<u>1997</u>	<u>1996</u>
As Reported	\$ 13,420	\$ 19,830
Pro Forma	\$ 6,165	\$ 16,904
<u>Earnings Per Share</u>	<u>1997</u>	<u>1996</u>
As Reported	\$ 0.52	\$ 0.77
Pro Forma	\$ 0.24	\$ 0.66

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions used for grants in 1997 and 1996, respectively: risk-free interest rates of 6.0 and 5.8; expected volatility of 69 and 66 percent; no expected dividends, and an expected life of 0.4 years beyond the vest date for each year's vesting increment of an option.

Since the SFAS No. 123 method of accounting has not been applied to options granted prior to July 1, 1995, the resulting pro forma compensation cost may not be representative of that to be expected in future years.

In fiscal 1997, the Company offered its employees the option of exchanging and canceling stock options acquired from June 1995 through October 1996 for new options priced as of November 1, 1996. As a result, the Company canceled 1,933,592 options at prices ranging from \$10.75 to \$23.125 per share and reissued the same number of options at the then-current fair market value of \$10.25 per share. Employees who submitted their option grants for repricing had their vesting schedules amended by moving their vesting back three months or restarting the vesting as of the new grant date, depending on the date of the grant.

The Company may sell up to 800,000 shares of stock to its full-time employees under the 1993 Employee Stock Purchase Plan. The Company has sold 218,684, 146,175 and 222,646 shares in 1997, 1996 and 1995, respectively, and has sold 652,003 shares through June 30, 1997. The Company sells shares at 85% of the lower of the stock's closing market price on the first or last day of the six-month offering period. The weighted average fair value of shares sold in 1997 and 1996, respectively, was \$9.00 and \$11.70.

The Company may grant up to 10,000,000 shares under the 1988 Plan. The Company has granted options on 8,178,225 shares (net of lapsed and terminated options) through June 30, 1997. The option exercise price is not less than 100% of the fair value of the shares on the date of grant, except that non-statutory options may be granted at 85% of such fair value. The 1988 Plan options are fully vested after five years and expire after ten years.

The Company may grant options for up to 175,000 shares under the Directors' Plan. The Company granted options on 152,000 shares through June 30, 1997. The options' exercise price equals the closing price of the stock on the day of the grant. The options are fully vested after four years and expire after ten years.

A summary of the status of the Company's two stock option plans at June 30, 1997, 1996 and 1995 incorporating changes during the years then-ended is presented in the table and narrative below (share amounts in thousands):

Year Ended June 30 ,	1997		1996		1995	
	Shares	Weighted Avg. Exercise Price	Shares	Weighted Avg. Exercise Price	Shares	Weighted Avg. Exercise Price
Outstanding at beginning of year	4,088	\$10.56	3,914	\$ 5.86	3,011	\$ 4.11
Granted	3,574	\$10.86	1,679	\$16.83	1,572	\$8.63
Exercised	(434)	\$ 4.85	(918)	\$ 3.28	(196)	\$2.35
Cancelled	<u>(3,148)</u>	<u>\$13.66</u>	<u>(587)</u>	<u>\$ 8.47</u>	<u>(473)</u>	\$5.26
Outstanding at year end	<u>4,080</u>	<u>\$ 9.07</u>	<u>4,088</u>	<u>\$10.56</u>	<u>3,914</u>	\$5.86
Exercisable end of year	1,145	\$ 7.21	1,101	\$ 5.31	1,531	\$2.80
Weighted fair value per option granted	<u>\$3.50</u>		<u>\$8.46</u>			

Year Ended June 30, 1997 Range of Exercise Prices	OPTIONS OUTSTANDING			OPTIONS EXERCISABLE	
	Number	Weighted Average Remaining Years	Weighted Average Exercise Price	Number	Weighted Average Exercise Price
\$ 0.25-\$ 7.06	817	6.30	\$ 4.85	576	\$ 4.35
\$ 7.13-\$ 9.88	561	8.49	\$ 8.19	119	\$ 8.58
\$ 10.25-\$ 10.25	1,844	9.35	\$ 10.25	254	\$ 10.25
\$ 10.38-\$ 12.75	830	8.66	\$ 11.00	193	\$ 10.77
\$ 12.93-\$ 20.38	<u>28</u>	8.90	\$ 14.66	<u>3</u>	\$ 15.05
\$ 0.25-\$ 20.38	<u>4,080</u>	8.48	\$ 9.07	<u>1,145</u>	\$ 7.21

NOTES RECEIVABLE FROM EMPLOYEES. The Company had received as consideration from certain officers of the Company promissory notes in connection with the exercise of stock options. These notes bore interest at rates between 5.57% and 6.69% and matured at various dates through April 1998. As of June 30, 1997, all outstanding notes were repaid.

STOCKHOLDER RIGHTS PLAN. During 1995, the Company established a stock purchase rights plan (the Rights Plan), under which stockholders may be entitled to purchase stock in the Company, or in an acquirer of the Company at a discounted price in the event of certain efforts to acquire control of the Company. The rights expire on the earliest of (a) April 19, 2005, (b) exchange or redemption of the rights pursuant to the Rights Plan, or (c) consummation of a merger or consolidation.

8 | Income Taxes

The provision for income taxes consisted of the following (in thousands):

<i>Years Ended June 30,</i>	1997	1996	1995
Current:			
Federal	\$ 8,371	\$ 10,319	\$ 4,972
State	1,297	1,739	1,365
	<u>9,668</u>	<u>12,058</u>	<u>6,337</u>
Deferred (Prepaid):			
Federal	1,083	(2,039)	(2,281)
State	191	(252)	(555)
	<u>1,274</u>	<u>(2,291)</u>	<u>(2,836)</u>
Net tax provision	<u>\$ 10,942</u>	<u>\$ 9,767</u>	<u>\$ 3,501</u>

The provision for income taxes is reconciled with the Federal statutory rate as follows (in thousands):

<i>Years Ended June 30,</i>	1997	1996	1995
Provision computed at federal statutory rate	\$ 8,526	\$ 10,359	\$ 5,569
State taxes, net of federal tax benefit	1,078	1,487	1,059
Change in valuation allowance	—	—	(2,261)
Research and development and other credits	(650)	(700)	(655)
In-process research and development write-off	2,180	—	—
FSC commission	(746)	(871)	(381)
Foreign taxes and other	554	(508)	170
Net tax provision	<u>\$ 10,942</u>	<u>\$ 9,767</u>	<u>\$ 3,501</u>
Net effective tax rate	<u>45%</u>	<u>33%</u>	<u>22%</u>

The components of the net deferred income tax asset are as follows (in thousands):

	June 30, 1997	June 30, 1996
Depreciation and asset basis differences	\$ 1,739	\$ 2,030
Accrued vacation	728	629
Inventory reserves	1,806	2,041
Other reserves and accruals, not currently deductible for tax purposes	1,559	2,092
State taxes, not currently deductible for federal tax purposes	409	386
Other	(337)	7
Net deferred income tax asset	<u>\$ 5,904</u>	<u>\$ 7,185</u>

9 | Industry Segment, Geographic and Customer Information

The Company operates in a single industry segment, the design and manufacture of high-performance UNIX multi-protocol network file/data servers for the technical workstation market. Export revenues consisted of the following (in thousands):

<i>Years Ended June 30,</i>	1997	1996	1995
Pacific Rim	\$31,759	\$36,229	\$21,390
Europe	28,191	16,248	8,984
Canada	6,790	5,986	3,201
Total export revenues	\$66,740	\$58,463	\$33,575
Percentage of total revenues	33%	36%	29%

One customer accounted for 10%, 10% and 15% of total revenues in fiscal 1997, 1996 and 1995, respectively. One other customer accounted for 15% of total revenues in fiscal 1997. Another customer accounted for 13% of total revenues in fiscal 1996. No other customers accounted for 10% or more of total revenues in these years.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To Auspex Systems, Inc.:

We have audited the accompanying consolidated balance sheets of Auspex Systems, Inc. (a Delaware corporation) and subsidiaries as of June 30, 1997 and 1996, and the related statements of operations, stockholders' equity and cash flows for each of the three years in the period ended June 30, 1997. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. 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, the financial statements referred to above present fairly, in all material respects, the financial position of Auspex Systems, Inc. and subsidiaries as of June 30, 1997 and 1996, and the results of their operations and their cash flows for each of the three years in the period ended June 30, 1997 in conformity with generally accepted accounting principles.

ARTHUR ANDERSEN LLP

San Jose, California

July 28, 1997

CORPORATE INFORMATION

Profile

Auspex Systems helps customers speed the delivery of network data throughout the organization. The company's expertise in network infrastructures and network-based applications helps customers achieve continuous, shared access to network data.

As a market leader, Auspex provides high-performance network file servers and high-availability, enterprise data management software solutions for storing, serving and managing multiple terabytes of network data. The company's products offer robust, cost-effective solutions for client/server environments.

Auspex serves the Fortune 1000 and leading worldwide organizations, including customers in the software development, oil and gas, communication, semiconductor, aerospace, automotive, financial services and internet service industries.

Founded in 1987, Auspex is headquartered in Santa Clara, California. Auspex employs approximately 600 people, with sales and support offices worldwide.

On June 30, 1997, Auspex Systems acquired Alpatronix, Inc. of Research Triangle Park, North Carolina. Alpatronix, a wholly owned subsidiary of Auspex, has expertise in developing scalable, high-availability enterprise-class data management software solutions.

Auspex's Common Stock is quoted on the Nasdaq National Market System under the symbol ASPX.

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Board of Directors

Bruce N. Moore
President and Chief Executive Officer

R. Stephen Cheheyl
Director
Auspex Systems, Inc.

W. Frank King
President and Chief Executive Officer
PSW Technologies Inc.

David F. Marquardt
General Partner
August Capital

Corporate Officers

Bruce N. Moore
President and Chief Executive Officer

Joseph G. Brown
Vice President
Worldwide Field Operations

Dennis E. Daniels
Vice President
Customer Satisfaction

Paul R. Gifford
Vice President
Product Development

Dorothy Krier
Vice President
Human Resources

Russell M. Lait
Vice President
Operations

Frederick A. Nervo
Vice President and
General Counsel

Kent L. Robertson
Vice President, Finance and
Chief Financial Officer

Michael B. Stevens
Vice President
North American Sales

Transfer Agent and Registrar

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Accountants

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333 West San Carlos Street, San Jose, California 95110-2710

Corporate Headquarters

5200 Great America Parkway, Santa Clara, California 95054
Phone (408) 986-2000, Fax (408) 986-2020
www.auspex.com

Form 10-K

The company files an Annual Report with the Securities & Exchange Commission on Form 10-K, pursuant to the Securities Exchange Act of 1934. Stockholders may obtain a copy of this report without cost by writing to Investor Relations, Auspex Systems, Inc., 5200 Great America Parkway, Santa Clara, California 95054.

Annual Meeting

The annual meeting of stockholders will be held at 9:00 a.m., Thursday, November 20, 1997 at the Santa Clara Convention Center, Conference Room 207, 5001 Great America Parkway, Santa Clara, California.

Stock Information

Auspex Systems, Inc. Common Stock is quoted on the Nasdaq National Market System under the symbol ASPX. The following table sets forth the range of high and low closing sales prices for the quarters indicated. The Company had 698 stockholders of record as of September 10, 1997. The Company has not to date paid cash dividends on its capital stock. The Company currently intends to retain any earnings for use within its business and does not anticipate paying any cash dividends in the foreseeable future.

<i>Auspex Systems</i>	<i>Fiscal 1997</i>		<i>Fiscal 1996</i>	
	<i>high</i>	<i>low</i>	<i>high</i>	<i>low</i>
First Quarter	\$ 17.00	\$ 10.00	\$ 18.25	\$ 11.375
Second Quarter	\$ 15.50	\$ 10.125	\$ 18.25	\$ 13.375
Third Quarter	\$ 14.75	\$ 10.625	\$ 21.00	\$ 14.00
Fourth Quarter	\$ 13.125	\$ 7.50	\$ 24.625	\$ 14.75