

CYPRESS SEMICONDUCTOR CORP /DE/

Form 10-Q

August 03, 2012

[Table of Contents](#)

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended July 1, 2012

OR

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

Commission file number 1-10079

CYPRESS SEMICONDUCTOR CORPORATION

(Exact name of registrant as specified in its charter)

Edgar Filing: CYPRESS SEMICONDUCTOR CORP /DE/ - Form 10-Q

Delaware
(State or other jurisdiction of
incorporation or organization)
94-2885898
(I.R.S. Employer
Identification No.)
198 Champion Court, San Jose, California 95134
(Address of principal executive offices and zip code)
(408) 943-2600
(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer ☒ Accelerated filer ☐
Non-accelerated filer ☐ (Do not check if a smaller reporting company) Smaller reporting company ☐
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

The total number of outstanding shares of the registrant's common stock as of July 29, 2012 was 148,557,309.

Table of Contents

INDEX

	Page
<u>PART I FINANCIAL INFORMATION</u>	
<u>Forward-Looking Statements</u>	3
Item 1. <u>Financial Statements</u>	4
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	31
Item 3. <u>Quantitative and Qualitative Disclosures about Market Risk</u>	40
Item 4. <u>Controls and Procedures</u>	40
<u>PART II OTHER INFORMATION</u>	
Item 1. <u>Legal Proceedings</u>	41
Item 1A. <u>Risk Factors</u>	41
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	41
Item 3. <u>Defaults Upon Senior Securities</u>	41
Item 4. <u>Mine Safety Disclosures</u>	41
Item 5. <u>Other Information</u>	42
Item 6. <u>Exhibits</u>	43
<u>Signatures</u>	44

Table of Contents

PART I FINANCIAL INFORMATION

Forward-Looking Statements

The discussion in this Quarterly Report on Form 10-Q contains statements that are not historical in nature, but are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, that involve risks and uncertainties, including, but not limited to, statements related to our manufacturing strategy, our expectation regarding dividends and stock repurchases, the application of our 2011 prepayments to Grace, our expectations regarding future technology transfers and other licensing arrangements, our expectations regarding the timing of our restructuring liabilities, expected payments from IV, our expectations regarding our active litigation matters and our intent to defend ourselves in those matters; our foreign currency exposure and the impact exchange rates could have on our operating margins, the adequacy of our cash and working capital positions, the value and liquidity of our investments, including auction rate securities and our other debt investments, our ability to recognize certain unrecognized tax benefits within the next twelve months as well as the resolution of agreements with various foreign tax authorities, our investment strategy, our belief that liquidity provided by existing cash, cash equivalents and investments and our borrowing arrangements will provide sufficient capital to meet our requirements for at least the next twelve months, our expectations regarding our outstanding warranty liability, the impact of interest rate fluctuations on our investments, the volatility of our stock price and the impact of new accounting standards on our financial statements. We use words such as plan, anticipate, believe, expect, future, intend and similar expressions to identify forward-looking statements. Such forward-looking statements are made as of the date hereof and are based on our current expectations, beliefs and intentions regarding future events or our financial performance and the information available to management as of the date hereof. Except as required by law, we assume no responsibility to update any such forward-looking statements. Our actual results could differ materially from those expected, discussed or projected in the forward-looking statements contained in this Quarterly Report on Form 10-Q for any number of reasons, including, but not limited to, the state and future of the general economy and its impact on the markets and consumers we serve and our investments; the current credit conditions; our ability to expand our customer base, our ability to transform our business with a leading portfolio of programmable products; the number and nature of our competitors; the changing environment and/or cycles of the semiconductor industry; foreign currency exchange rates; our ability to efficiently manage our manufacturing facilities and achieve our cost goals emanating from our flexible manufacturing strategy; our ability to achieve our goals related to our restructuring activities; our success in our pending litigation matters, our ability to manage our investments and interest rate and exchange rate exposure; our ability to achieve liquidity in our investments, the failure or success of our Emerging Technology division and/or the materialization of one or more of the risks set forth above or in Part II, Item 1A (*Risk Factors*) in this Quarterly Report on Form 10-Q and in Part I, Item 1A (*Risk Factors*) in our Annual Report on Form 10-K for the fiscal year ended January 1, 2012.

Table of Contents**ITEM 1. FINANCIAL STATEMENTS****CYPRESS SEMICONDUCTOR CORPORATION****CONDENSED CONSOLIDATED BALANCE SHEETS***

	July 1, 2012 (In thousands, except	January 1, 2012 (In thousands, except
	per-share amounts)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 118,262	\$ 99,717
Short-term investments	92,542	66,613
Accounts receivable, net	126,190	103,524
Inventories	91,376	92,304
Other current assets	53,246	43,492
Total current assets	481,616	405,650
Property, plant and equipment, net	276,063	284,979
Goodwill	31,836	31,836
Intangible assets, net	6,086	8,626
Other long-term assets	85,806	78,999
Total assets	\$ 881,407	\$ 810,090
LIABILITIES AND EQUITY		
Current liabilities:		
Accounts payable	\$ 55,901	\$ 52,868
Accrued compensation and employee benefits	44,620	41,679
Deferred margin on sales to distributors	148,570	150,568
Dividends payable	16,661	13,786
Income taxes payable	5,349	4,629
Other current liabilities	79,149	62,930
Total current liabilities	350,250	326,460
Deferred income taxes and other tax liabilities	39,023	38,610
Loan payable	153,000	
Other long-term liabilities	44,466	47,178
Total liabilities	586,739	412,248
Commitments and contingencies (Note 8)		
Equity:		
Preferred stock, \$.01 par value, 5,000 shares authorized; none issued and outstanding		
Common stock, \$.01 par value, 650,000 and 650,000 shares authorized; 283,726 and 278,812 shares issued; 151,494 and 154,174 shares outstanding at July 1, 2012 and January 1, 2012, respectively	2,837	2,780
Additional paid-in-capital	2,608,144	2,579,348
Accumulated other comprehensive income (loss)	588	(1,940)
Accumulated deficit	(340,646)	(326,163)
Stockholders' equity before treasury stock, total	2,270,923	2,254,025
Less: shares of common stock held in treasury, at cost; 132,232 and 124,638 shares at July 1, 2012 and January 1, 2012, respectively	(1,971,605)	(1,853,758)

Edgar Filing: CYPRESS SEMICONDUCTOR CORP /DE/ - Form 10-Q

Total Cypress stockholders' equity	299,318	400,267
Noncontrolling interest	(4,650)	(2,425)
Total equity	294,668	397,842
Total liabilities and equity	\$ 881,407	\$ 810,090

* Amounts as of July 1, 2012 are unaudited. Amounts as of January 1, 2012 were derived from the January 1, 2012 audited consolidated financial statements.

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

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS****(Unaudited)**

	Three Months Ended		Six Months Ended	
	July 1, 2012	July 3, 2011	July 1, 2012	July 3, 2011
	(In thousands, except per-share amounts)			
Revenues	\$ 201,300	\$ 254,978	\$ 386,390	\$ 488,088
Costs and expenses (credits):				
Cost of revenues	94,531	115,958	187,840	220,292
Research and development	47,946	49,278	95,914	97,143
Selling, general and administrative	51,955	58,482	112,448	117,134
Amortization of acquisition-related intangible assets	731	731	1,463	1,429
Restructuring costs	989	3,798	1,217	4,532
Gain on divestiture				(34,291)
Total costs and expenses, net	196,152	228,247	398,882	406,239
Operating income (loss)	5,148	26,731	(12,492)	81,849
Interest and other income (expense), net	1	(522)	335	900
Income (loss) before income taxes and noncontrolling interest	5,149	26,209	(12,157)	82,749
Income tax provision (benefit)	517	(14,433)	2,982	(13,083)
Income (loss), net of taxes	4,632	40,642	(15,139)	95,832
Adjust for net loss attributable to noncontrolling interest	345	181	655	365
Net income (loss) attributable to Cypress	\$ 4,977	\$ 40,823	\$ (14,484)	\$ 96,197
Net income (loss) per share attributable to Cypress:				
Basic	\$ 0.03	\$ 0.24	\$ (0.09)	\$ 0.57
Diluted	\$ 0.03	\$ 0.21	\$ (0.09)	\$ 0.49
Cash dividend declared per share	\$ 0.11	\$ 0.09	\$ 0.22	\$ 0.09
Shares used in net income (loss) per share calculation:				
Basic	151,765	168,723	152,894	170,034
Diluted	164,605	192,276	152,894	196,110

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

Table of Contents

CYPRESS SEMICONDUCTOR CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(Unaudited)

	Three Months Ended		Six Months Ended	
	July 1,	July 3,	July 1,	July 3,
	2012	2011	2012	2011
	(In thousands)			
Net income (loss)	\$ 4,632	\$ 40,642	\$ (15,139)	\$ 95,832
Other comprehensive income (loss), net of tax:				
Change in net unrealized gains on available-for-sale investments	2,326	(42)	2,528	921
Other		150		300
Other comprehensive income	2,326	108	2,528	1,221
Comprehensive income (loss)	6,958	40,750	(12,611)	97,053
Adjust for net loss attributable to noncontrolling interest	345	181	655	365
Comprehensive income (loss) attributable to Cypress	\$ 7,303	\$ 40,931	\$ (11,956)	\$ 97,418

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

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(Unaudited)**

	Six Months Ended	
	July 1, 2012	July 3, 2011
	(In thousands)	
Cash flows from operating activities:		
Net income (loss)	\$ (15,139)	\$ 95,832
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Stock-based compensation expense	50,967	50,577
Depreciation and amortization	24,890	28,240
Deferred income taxes and other tax liabilities	477	(13,288)
Restructuring costs	1,216	4,532
Loss on sale or retirement of property and equipment, net	818	1,350
Contribution of asset		4,000
Gain on divestiture		(34,291)
Other	1,612	
Changes in operating assets and liabilities, net of effects of a divestiture:		
Accounts receivable	(22,666)	(52,990)
Inventories	647	(8,185)
Other current and long-term assets	(3,974)	(27,407)
Accounts payable and other liabilities	22,780	3,600
Deferred margin on sales to distributors	(1,998)	60,243
Net cash provided by operating activities	59,630	112,213
Cash flows from investing activities:		
Proceeds from sales or maturities of available-for-sale investments	60,448	170,097
Purchases of available-for-sale investments	(81,798)	(72,385)
Net contributions of deferred compensation plan	277	975
Acquisition of property, plant and equipment	(19,716)	(53,591)
Proceeds from sales of property, plant and equipment	8	1,176
Proceeds from divestiture		34,025
Cash paid for other investments	(7,203)	(2,962)
Net cash provided by (used in) investing activities	(47,984)	77,335
Cash flows from financing activities:		
Repurchase of common shares	(97,864)	(101,470)
Loan payable proceeds	203,000	
Withholding of common shares for tax obligations on vested restricted shares	(19,984)	(41,442)
Payment of dividends	(30,510)	
Proceeds from issuance of common shares under employee stock plan	9,982	48,240
Payments of equipment leases and loans, net	(57,725)	
Yield enhancement structured agreements settled in stock		(127,833)
Yield enhancement structured agreements settled in cash, net		49,927
Net cash provided by (used in) financing activities	6,899	(172,578)
Net increase in cash and cash equivalents	18,545	16,970

Edgar Filing: CYPRESS SEMICONDUCTOR CORP /DE/ - Form 10-Q

Cash and cash equivalents, beginning of period	99,717	263,183
Cash and cash equivalents, end of period	\$ 118,262	\$ 280,153

Supplemental disclosures:

Dividends payable	\$ 16,661	\$ 15,262
-------------------	-----------	-----------

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

Table of Contents

CYPRESS SEMICONDUCTOR CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Fiscal Years

Cypress Semiconductor Corporation (Cypress or the Company) reports on a fiscal-year basis. We end our quarters on the Sunday closest to the end of the applicable calendar quarter, except in a 53-week fiscal year, in which case the additional week falls into the fourth quarter of that fiscal year. Fiscal 2012 has 52 weeks and fiscal 2011 had 52 weeks. The second quarter of fiscal 2012 ended on July 1, 2012 and the second quarter of fiscal 2011 ended on July 3, 2011.

Basis of Presentation

In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments, consisting of only normal recurring items, which are necessary to state fairly the financial information included therein. The financial data should be read in conjunction with the audited consolidated financial statements and related notes thereto included in our Annual Report on Form 10-K for the fiscal year ended January 1, 2012.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

The condensed consolidated results of operations for the three and six months ended July 1, 2012 are not necessarily indicative of the results to be expected for the full fiscal year.

Recently Adopted Accounting Standards

In June 2011, Financial Accounting Standards Board (FASB) issued authoritative guidance on the presentation of comprehensive income to require an entity to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The authoritative guidance also required presentation of adjustments for items that are reclassified from other comprehensive income in the statement where the components of net income and the components of other compressive income are presented, which was indefinitely deferred by the FASB in December 2011. We adopted this guidance in the first quarter of fiscal 2012 and we now present condensed consolidated statements of comprehensive income (loss) in a separate statement following the condensed consolidated statements of operations. The implementation of this authoritative guidance did not have any impact on our financial position or results of operations as it only required separate presentation of total comprehensive income (loss).

In May 2011, the FASB issued a new standard amending U.S. generally accepted accounting principles (GAAP) fair value measurements and disclosures for the purpose of ensuring that fair value measurement and disclosure requirements are the same across both U.S. GAAP and International Financial Reporting Standards (IFRS). The standard contains amendments changing the wording used to describe many of the requirements in U.S. GAAP for measuring fair value and for disclosing information about fair value measurements, clarifying the application of existing fair value measurement requirements and changing a particular principle for measuring fair value or for disclosing information about fair value measurements. This guidance is effective for our interim and annual periods beginning January 2, 2012. Additionally, the standard expands certain disclosure requirements, including qualitative disclosures selected to level 3 fair value measurements. We adopted this authoritative guidance in the first quarter of fiscal 2012 and our implementation of this authoritative guidance did not have any impact on our financial position or results of operations as it only required additional disclosures related to fair value measurements.

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 2. GOODWILL AND INTANGIBLE ASSETS*****Goodwill***

Goodwill represents the excess of the purchase price over the estimated fair value of the net tangible and identifiable intangible assets acquired in a business combination. The carrying amount of goodwill at July 1, 2012 was \$31.8 million in the Programmable Systems Division (PSD) and was unchanged from the balance at January 1, 2012. PSD is the only reportable business segment with goodwill.

Goodwill is not amortized, but is reviewed for impairment annually during the fourth quarter of each fiscal year and whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. In fiscal 2011, we adopted the authoritative guidance which allows us to use a qualitative approach to test goodwill for impairment. This authoritative guidance permits us to first perform a qualitative assessment to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying value. If it is concluded that this is the case, it is necessary to perform the two-step goodwill impairment test. Otherwise, the two-step goodwill impairment test is not required. The process of evaluating the potential impairment of goodwill and intangible assets requires significant judgment. We regularly monitor current business conditions and other factors including, but not limited to (i) change in the industry and competitive environment; (ii) market capitalization; (iii) stock price; and (iv) overall financial performance such as negative or declining cash flows or a decline in actual or planned revenue or earnings compared with actual and projected results of relevant prior periods.

Intangible Assets

The following table presents details of our intangible assets:

	As of July 1, 2012			As of January 1, 2012		
	Gross	Accumulated Amortization	Net	Gross	Accumulated Amortization	Net
	(In thousands)					
Acquisition-related intangible assets	\$ 95,134	\$ (90,244)	\$ 4,890	\$ 95,134	\$ (88,782)	\$ 6,352
Non-acquisition related intangible assets	10,648	(9,452)	1,196	10,648	(8,374)	2,274
Total intangible assets	\$ 105,782	\$ (99,696)	\$ 6,086	\$ 105,782	\$ (97,156)	\$ 8,626

As of July 1, 2012, the estimated future amortization expense of intangible assets was as follows:

	(In thousands)
2012 (remaining six months)	\$ 2,148
2013	3,435
2014	503
Total future amortization expense	\$ 6,086

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 3. RESTRUCTURING**

For the three and six months ended July 1, 2012, we recorded restructuring charges of \$1.0 million and \$1.2 million, respectively. For the three and six months ended July 3, 2011, we recorded restructuring charges of \$3.8 million and \$4.5 million, respectively. The determination of when we accrue for severance and benefits costs, and which accounting standard applies, depends on whether the termination benefits are provided under a one-time benefit arrangement or under an on-going benefit arrangement.

Fiscal 2011 Restructuring Plan

In fiscal 2011, we initiated a restructuring plan which allows us to continue to allocate and align our resources to the business units that we expect will drive future development and revenue growth (Fiscal 2011 Restructuring Plan). To date, we have recorded total restructuring charges of \$5.8 million under the Fiscal 2011 Restructuring Plan, which was all related to personnel costs. The restructuring activities related to personnel costs, which are primarily in the U.S., are summarized as follows:

	(In thousands)
Balance as of January 1, 2012	\$ 1,955
Cash payments	(372)
Balance as of April 1, 2012	1,583
Provision	725
Cash payments	(185)
Balance as of July 1, 2012	\$ 2,123

The restructuring liability as of July 1, 2012 under the Fiscal 2011 Restructuring Plan related primarily to personnel costs and is expected to be paid out within the next twelve months.

Fiscal 2010 Restructuring Plan

During the third quarter of fiscal 2010, we implemented a restructuring plan to exit certain of our back-end manufacturing operations located in the Philippines (Fiscal 2010 Restructuring Plan). These actions were intended to reduce the cost of our back-end manufacturing by selling our labor intensive assembly operations to a lower cost third-party subcontractor in China and by the continued shifting of these operations to our fully automated back-end processes.

To date, we have recorded total restructuring charges of \$4.1 million under the Fiscal 2010 Restructuring Plan, which was all related to personnel costs. As of July 1, 2012, the outstanding restructuring liability under the Fiscal 2010 Restructuring Plan was primarily related to severance and benefits of our employees. We expect to substantially complete the activities and fully pay out the remaining restructuring liability under this program within the next twelve months.

The restructuring activities related to personnel costs are summarized as follows:

(In thousands)

Edgar Filing: CYPRESS SEMICONDUCTOR CORP /DE/ - Form 10-Q

Balance as of January 1, 2012	\$	1,885
Provision		100
Cash payments		(1,291)
Balance as of April 1, 2012		694
Provision		200
Cash payments		(127)
Balance as of July 1, 2012	\$	767

Assets Held For Sale:

The Texas facility ceased operations in the fourth quarter of fiscal 2008. As our management has committed to a plan to sell the assets associated with the facility, we have classified the assets as held for sale and recorded the assets at the lower of their carrying amount or estimated fair value less cost to sell. Fair value was determined by an analysis of market prices for similar assets.

The net book value of the remaining restructured assets that were classified as held for sale and included in Other current assets in the Condensed Consolidated Balance Sheets was \$6.9 million as of July 1, 2012 and January 1, 2012.

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 4. BALANCE SHEET COMPONENTS***Accounts Receivable, Net*

	As of July 1, 2012	January 1, 2012
	(In thousands)	
Accounts receivable, gross	\$ 130,017	\$ 107,433
Allowance for doubtful accounts receivable and sales returns	(3,827)	(3,909)
Total accounts receivable, net	\$ 126,190	\$ 103,524

Inventories

	As of July 1, 2012	January 1, 2012
	(In thousands)	
Raw materials	\$ 6,190	\$ 4,474
Work-in-process	62,926	63,552
Finished goods	22,260	24,278
Total inventories	\$ 91,376	\$ 92,304

Other Current Assets

	As of July 1, 2012	January 1, 2012
	(In thousands)	
Prepaid expenses	\$ 27,660	\$ 24,664
Prepayment to Grace	8,367	2,164
Assets held for sale	6,913	6,913
Other current assets	10,306	9,751
Total other current assets	\$ 53,246	\$ 43,492

Prepayment to Grace

Edgar Filing: CYPRESS SEMICONDUCTOR CORP /DE/ - Form 10-Q

In fiscal 2011, we made certain pre-payments to Grace Semiconductor Manufacturing Corporations (Grace), a strategic foundry partner, to secure a certain supply of wafers. The pre-payments made in fiscal 2011 are expected to be applied to purchases of wafers from Grace. At July 1, 2012, the unapplied pre-payment balance was approximately \$8.4 million and was recorded as part of Other current assets in the Condensed Consolidated Balance Sheet because if we do not use all the pre-payment against our purchases of wafers from Grace within the next twelve months from the second quarter ended July 1, 2012, Grace will return to us any portion of the unused pre-payment.

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)*****Other Long-Term Assets***

	July 1, 2012	As of January 1, 2012
	(In thousands)	
Employee deferred compensation plan	\$ 34,910	\$ 32,976
Investments:		
Debt securities	14,580	19,004
Equity securities	14,598	6,213
Prepayment to Grace-long-term portion	1,200	5,957
Prepaid patent license	5,868	
Other assets	14,650	14,849
 Total other long-term assets	 \$ 85,806	 \$ 78,999

Other Current Liabilities

	July 1, 2012	As of January 1, 2012
	(In thousands)	
Employee deferred compensation plan	\$ 34,480	\$ 32,485
Patent license liability (see Note 8)	14,009	
Restructuring accrual (see Note 3)	3,110	4,061
Capital lease-current portion (see Note 8)	2,257	2,257
Equipment loan-current portion (see Note 9)	2,725	2,725
Other current liabilities	22,568	21,402
 Total other current liabilities	 \$ 79,149	 \$ 62,930

Deferred Income Taxes and Other Tax Liabilities

	July 1, 2012	As of January 1, 2012
	(In thousands)	
Deferred income taxes	\$ 112	\$ 165
Non-current tax liabilities	38,911	38,445
 Total deferred income taxes and other tax liabilities	 \$ 39,023	 \$ 38,610

Other Long-term Liabilities

	July 1, 2012	As of January 1, 2012
	(In thousands)	
Advances received from the sale of Auction Rate Securities (ARS) (see Note 5)	\$ 11,662	\$ 16,390
Capital lease long term portion (see Note 8)	14,052	12,982
Equipment loan long term portion (see Note 9)	10,091	11,413
Other long term liabilities	8,661	6,393
Total other long-term liabilities	\$ 44,466	\$ 47,178

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 5. FAIR VALUE MEASUREMENTS*****Assets/Liabilities Measured at Fair Value on a Recurring Basis***

The following tables present the fair value hierarchy for our financial assets and liabilities measured at fair value on a recurring basis:

	Level 1	As of July 1, 2012		Total	Level 1	As of January 1, 2012		Total
		Level 2	Level 3			Level 2	Level 3	
<u>Financial Assets</u>								
Cash equivalents:								
Money market funds	\$ 50,097	\$	\$	\$ 50,097	\$ 77,952	\$	\$	\$ 77,952
Corporate notes/bonds						1,340		1,340
Total cash equivalents	50,097			50,097	77,952	1,340		79,292
Short-term investments:								
U.S. treasuries	10,047			10,047	10,072			10,072
Corporate notes/bonds		24,816		24,816		33,028		33,028
Federal agency		4,011		4,011		15,524		15,524
Commercial paper		52,865		52,865		7,189		7,189
Certificates of deposit		803		803		800		800
Total short-term investments	10,047	82,495		92,542	10,072	56,541		66,613
Long-term investments:								
Auction rate securities			14,580	14,580			19,004	19,004
Marketable equity securities	6,218			6,218	3,013			3,013
Non-marketable equity securities			1,200	1,200			1,200	1,200
Total long-term investments	6,218		15,780	21,998	3,013		20,204	23,217
Employee deferred compensation plan:								
Mutual funds	20,226			20,226	18,046			18,046
Equity securities	4,806			4,806	5,448			5,448
Fixed income	3,731			3,731	3,799			3,799
Cash equivalents	2,433			2,433	1,960			1,960
Money market funds	3,714			3,714	3,723			3,723
Total employee deferred compensation plan	34,910			34,910	32,976			32,976
Total financial assets	\$ 101,272	\$ 82,495	\$ 15,780	\$ 199,547	\$ 124,013	\$ 57,881	\$ 20,204	\$ 202,098
<u>Financial Liabilities</u>								
Employee deferred compensation plan	\$	\$ 34,480	\$	\$ 34,480		\$ 32,485	\$	\$ 32,485

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****Valuation Techniques:**

Level 1 includes instruments for which quoted prices in active markets for identical assets or liabilities that we have the ability to access. Our financial assets utilizing Level 1 inputs include U.S. treasuries, money market funds, marketable equity securities and our employee deferred compensation plan assets.

Level 2 includes instruments for which the valuations are based on quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable data for substantially the full term of the assets or liabilities. Level 2 assets consist of certain marketable debt instruments for which values are determined using inputs that are observable in the market or can be derived principally from or corroborated by observable market data. Our Level 2 instruments include certain U.S. government securities, commercial paper, corporate notes and bonds and employee deferred compensation plan liabilities.

Level 3 Valuations based on inputs that are unobservable and significant to the overall fair value measurement. Financial assets utilizing Level 3 inputs primarily include auction rate securities. We use an income approach valuation model to estimate the exit price of the auction rate securities, which is derived as the weighted-average present value of expected cash flows over various periods of illiquidity, using a risk adjusted discount rate that is based on the credit risk and liquidity risk of the securities.

Sale of Auction Rate Securities

In December 2011, we entered into a settlement and securities purchase agreement (the "Securities Agreement") with a certain financial institution. Pursuant to the terms of the Securities Agreement, we agreed to sell to the financial institution certain of our ARS investments with an aggregate par value of approximately \$19.1 million and carrying value of approximately \$17.3 million at the time of sale for an aggregate sale price of approximately \$16.4 million. Under the terms of the Securities Agreement, we have the option to repurchase from the financial institution any of the ARS we sold to them until November 30, 2013 for the amount at which the related ARS were sold plus agreed upon funding costs. Because of our ability to repurchase the ARS from the date of sale through November 30, 2013, we maintain effective control of these ARS. As such, we did not account for the transaction as a sale and recognized the \$16.4 million sale consideration we received as Advances received for the sale of ARS under Other long-term liabilities in the Condensed Consolidated Balance Sheets. We will continue to account for these ARS as a financing arrangement until they are called or the expiration of our call option under the Securities Agreement.

In the second quarter of 2012, ARS with a par value of \$5.0 million were called for redemption at par, which resulted in the reversal of an unrealized loss of \$0.1 million.

The fair value of our investments in ARS was approximately \$14.6 million and \$19.0 million as of July 1, 2012 and January 1, 2012, respectively.

In the second quarter of fiscal 2012 and during the fourth quarter of fiscal 2011, we performed an analysis to assess the fair value of the ARS using a valuation model based on discounted cash flows. The assumptions used were the following:

	Q2-2012	Q4-2011
Years to liquidity	7	7

Edgar Filing: CYPRESS SEMICONDUCTOR CORP /DE/ - Form 10-Q

Discount rates *	1.29% -3.30%	1.75% -3.95%
Continued receipt of contractual interest which provides a premium spread for failed auctions	Yes	Yes

* *Discount rates incorporate a spread for both credit and liquidity risk.*

Based on these assumptions, we estimated that the ARS were valued at approximately 91.7% and 90.9% of their stated par value as of July 1, 2012 and January 1, 2012, respectively, representing a decline in value of approximately \$1.3 million and \$1.9 million, respectively. These amounts were recorded as an unrealized loss in accumulated other comprehensive loss as of July 1, 2012 and January 1, 2012.

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)*****Level 3 Investments Measured Fair Value on a Recurring Basis***

The following table presents a summary of changes in our Level 3 investments measured at fair value on a recurring basis:

	Auction Rate Securities	Non-marketable Equity Securities
	(In thousands)	
Balance as of January 1, 2012	\$ 19,004	\$ 1,200
Unrealized gain recorded in Other comprehensive income (loss)	576	
Amount settled at par	(5,000)	
Balance as of July 1, 2012	\$ 14,580	\$ 1,200

Level 3 Assets Measured at Fair Value on a Nonrecurring Basis

Certain of our assets, including intangible assets, goodwill and cost-method investments, are measured at fair value on a nonrecurring basis if impairment is indicated.

Investments in Equity Securities

Our investments in equity securities included long-term investments in non-marketable equity securities (investments in privately-held companies) of approximately \$8.4 million and marketable equity securities (investments in publicly traded companies) of approximately \$6.2 million as of July 1, 2012 (\$3.2 million investments in non-marketable equity securities and \$3.0 million investments in marketable equity securities as of January 1, 2012). Our privately-held equity investments are accounted for under the cost method as we have less than 20% ownership interest and we do not have the ability to exercise significant influence over the operations of the privately-held companies. These investments are periodically reviewed for other-than-temporary declines in fair value by considering available evidence, including general market conditions, financial condition, pricing in recent rounds of financing, if any, earnings and cash flow forecasts, recent operational performance and any other readily available market data. As a result of our recent evaluation, we determined that our investment in a certain privately-held company with an original carrying value of \$2.0 million was impaired (fair value of \$1.2 million). As such, we recognized an impairment loss of approximately \$0.8 million in Interest and other income, net during six months ended July 1, 2012 and we classified the investment as Level 3 asset due to the absence of quoted market prices and inherent lack of liquidity. We had no impairment charges against our privately-held equity investments in the first and second quarters of fiscal 2011.

In February 2012, we entered into a Stock Purchase Agreement (the Agreement) with a company that designs, develops and manufactures products in the area of advanced battery storage for mobile consumer devices. Pursuant to the terms of the Agreement, we purchased approximately \$6 million of preferred stock from the company and have committed to purchase additional preferred stock in a series of subsequent closings subject to certain performance milestones that must be fulfilled within a defined and agreed upon timeline. Our future commitment to purchase additional preferred stock is approximately \$0.6 million in fiscal 2012, \$60.8 million in fiscal 2013 and \$17.8 million in fiscal 2014 subject to the attainment of certain milestones and the timing of additional capital requests which could vary substantially. As of July 1, 2012, we own less than 10% of the company. If our future commitments are fully funded, we could become their majority shareholder. As of July 1, 2012, our initial investment of \$6.0 million was recorded as part of our investments in non-marketable equity securities.

There were no significant transfers between Level 1, Level 2 and Level 3 fair value hierarchies during the first six months of fiscal 2012.

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 6. INVESTMENTS AND EMPLOYEE DEFERRED COMPENSATION PLAN*****Available-For-Sale Securities***

The following tables summarize our available-for-sale and other investments:

	Cost	As of July 1, 2012 Gross Unrealized Gains	Gross Unrealized Losses	Fair Value (In thousands)	Cost	As of January 1, 2012 Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Reported as cash equivalents:								
Money market funds	\$ 50,097	\$	\$	\$ 50,097	\$ 77,952	\$	\$	\$ 77,952
Corporate notes/bonds					1,341		(1)	1,340
Total cash equivalents	50,097			50,097	79,293		(1)	79,292
Reported as short-term investments:								
Corporate notes/bonds	24,795	25	(4)	24,816	33,010	33	(15)	33,028
U.S. treasuries	10,011	36		10,047	10,004	68		10,072
Federal agency	4,010	1		4,011	15,526	4	(6)	15,524
Commercial paper	52,864	1		52,865	7,189	1	(1)	7,189
Certificates of deposit	803			803	801		(1)	800
Total short-term investments	92,483	63	(4)	92,542	66,530	106	(23)	66,613
Reported as long-term investments:								
Auction rate securities	15,901		(1,321)	14,580	20,900		(1,896)	19,004
Marketable equity securities	4,455	2,003	(240)	6,218	3,253		(240)	3,013
Total long-term investments	20,356	2,003	(1,561)	20,798	24,153		(2,136)	22,017
Total available-for-sale securities and other	\$ 162,936	\$ 2,066	\$ (1,565)	\$ 163,437	\$ 169,976	\$ 106	\$ (2,160)	\$ 167,922

As of July 1, 2012, \$1.3 million of the \$1.6 million gross unrealized losses were related to ARS that had been in a continuous loss position for 12 months or more. As of January 1, 2012, \$1.9 million of the \$2.2 million gross unrealized losses were related to ARS that had been in a continuous loss position for 12 months or more. For individual marketable equity securities with unrealized losses, we evaluated the near-term prospects in relation to the severity and duration of the impairment. Based on that evaluation and our ability and intent to hold these investments for a reasonable period of time, we did not consider these investments to be other-than-temporarily impaired as of July 1, 2012 or January 1, 2012.

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)**

As of July 1, 2012, the contractual maturities of our available-for-sale investments and certificates of deposit were as follows (the table below does not include our investments in marketable equity securities):

	Cost	Fair Value
	(in thousands)	
Maturing within one year	\$ 139,815	\$ 139,874
Maturing in one to three years	2,765	2,765
Maturing in more than three years	15,901	14,580
Total	\$ 158,481	\$ 157,219

Realized gains and realized losses from sales of available-for-sale investments were not material for all periods presented.

Proceeds from sales or maturities of available-for-sale investments were \$23.4 million and \$60.4 million for the three and six months ended July 1, 2012, respectively, and \$91.8 million and \$170.1 million for the three and six months ended July 3, 2011, respectively.

Employee Deferred Compensation Plan

We have a deferred compensation plan which provides certain key employees, including our executive management, with the ability to defer the receipt of compensation in order to accumulate funds for retirement on a tax-deferred basis. We do not make contributions to the deferred compensation plan or guarantee returns on the investments. Participant deferrals and investment gains and losses remain as our liabilities and the underlying assets are subject to claims of general creditors.

Under the deferred compensation plan, the assets are recorded at fair value in each reporting period with the offset being recorded in Interest and other income, net. The liabilities are recorded at fair value in each reporting period with the offset being recorded as an operating expense or income. As of July 1, 2012 and January 1, 2012, the fair value of the assets was \$34.9 million and \$33.0 million, respectively, and the fair value of the liabilities was \$34.5 million and \$32.5 million, respectively.

All non-cash expense and income recorded under the deferred compensation plan were included in the following line items in the Condensed Consolidated Statements of Operations:

	Three Months Ended		Six Months Ended	
	July 1, 2012	July 3, 2011	July 1, 2012	July 3, 2011
	(In thousands)			
Changes in fair value of assets recorded in:				
Interest and other income, net	\$ (842)	\$ 6	\$ 1,652	\$ 1,480
Changes in fair value of liabilities recorded in:				
Cost of revenues	40	2	(222)	(202)
Research and development expenses	89	(58)	(334)	(567)
Selling, general and administrative expenses	183	4	(1,071)	(919)
Total income (expense)	\$ (530)	\$ (46)	\$ 25	\$ (208)

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 7. STOCK-BASED COMPENSATION**

Our equity incentive plans are broad-based, long-term programs intended to attract and retain talented employees and align stockholder and employee interests.

The following table summarizes the stock-based compensation expense, by line item recorded in the Condensed Consolidated Statements of Operations:

	Three Months Ended		Six Months Ended	
	July 1, 2012	July 3, 2011	July 1, 2012	July 3, 2011
	(In thousands)			
Cost of revenues	\$ 7,759	\$ 6,714	\$ 11,798	\$ 13,224
Research and development	5,480	6,941	12,393	12,414
Selling, general and administrative	8,991	16,085	26,776	24,939
Total stock-based compensation	\$ 22,230	\$ 29,740	\$ 50,967	\$ 50,577

As stock-based compensation expense recognized in the Condensed Consolidated Statements of Operations is based on awards ultimately expected to vest, it has been reduced for estimated forfeitures. The accounting guidance requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates.

Consolidated cash proceeds from the issuance of shares under the employee stock plans were approximately \$3.8 million and \$10.0 million for the three and six months ended July 1, 2012, respectively, and \$24.3 million and \$48.2 million for the three and six months ended July 3, 2011, respectively. We did not recognize a tax benefit from stock option exercises for the three and six months ended July 1, 2012 or July 3, 2011.

As of July 1, 2012 and January 1, 2012, stock-based compensation capitalized in inventories totaled \$4.3 million and \$4.6 million, respectively.

The following table summarizes the stock-based compensation expense by type of awards:

	Three Months Ended		Six Months Ended	
	July 1, 2012	July 3, 2011	July 1, 2012	July 3, 2011
	(In thousands)			
Stock options	\$ 2,272	\$ 4,041	\$ 3,923	\$ 7,560
Restricted stock units and restricted stock awards	17,029	23,933	41,897	39,275
Employee Stock Purchase Plan (ESPP)	2,929	1,766	5,147	3,742
Total stock-based compensation expense	\$ 22,230	\$ 29,740	\$ 50,967	\$ 50,577

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)**

The following table summarizes the unrecognized stock-based compensation expense, net of estimated forfeitures, by type of awards as of July 1, 2012:

	As of July 1, 2012 (In thousands)	Weighted- Average Amortization Period (In years)
Stock options	\$ 12,641	1.43
Restricted stock units and restricted stock awards	58,384	1.44
ESPP	3,651	1.03
Total unrecognized stock-based compensation balance	\$ 74,676	1.41

Valuation Assumptions

We estimated the fair value of the stock options and ESPP using the Black-Scholes valuation model with the following assumptions:

	Three Months Ended		Six Months Ended	
	July 1, 2012	July 3, 2011	July 1, 2012	July 3, 2011
Expected life	2.2-6.2 years	0.5-7.3 years	1.2-6.2 years	0.5-7.3 years
Volatility	45.8%-49.6%	37.6%-43.8%	42.9%-49.6%	37.6%-50.3%
Risk-free interest rate	0.3%-1.0%	0.1%-2.5%	0.2%-1.5%	0.1%-2.9%
Dividend yield	3.3%	1.7%	2.8%-3.3%	0%-1.7%

The fair value of the restricted stock units and the restricted stock awards was based on our stock price on the date of grant.

Equity Incentive Program

As of July 1, 2012, approximately 19.0 million stock options or 10.1 million restricted stock units and restricted stock awards were available for grant under the Amended and Restated 1994 Stock Plan.

Stock Options:

The following table summarizes our stock option activities:

Shares	Weighted- Average Exercise Price Per Share
--------	--

Edgar Filing: CYPRESS SEMICONDUCTOR CORP /DE/ - Form 10-Q

	(In thousands, except per-share amounts)	
Options outstanding as of January 1, 2012	23,363	\$ 6.49
Granted	3	\$ 18.33
Exercised	(1,144)	\$ 5.42
Forfeited or expired	(288)	\$ 10.32
Options outstanding as of April 1, 2012	21,934	\$ 6.50
Granted	18	\$ 13.64
Exercised	(889)	\$ 4.25
Forfeited or expired	(266)	\$ 10.83
Options outstanding as of July 1, 2012	20,797	\$ 6.55
Options exercisable as of July 1, 2012	15,310	\$ 5.17

The weighted-average grant-date fair value of the options granted during the six months ended July 1, 2012 and July 3, 2011 was \$4.02 and \$7.14.

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)**

The aggregate intrinsic value of the options outstanding and options exercisable as of July 1, 2012 was approximately \$149.9 million and \$125.9 million, respectively. The aggregate intrinsic value represents the total pre-tax intrinsic value which would have been received by the option holders had all option holders exercised their options as of July 1, 2012 and do not include substantial tax payments.

The aggregate pre-tax intrinsic value of option exercises, which represents the difference between the exercise price and the value of Cypress common stock at the time of exercise, was \$8.9 million and \$23.1 million during three and six months ended July 1, 2012, respectively.

The total number of exercisable in-the-money options was approximately 14.8 million shares as of July 1, 2012.

As of July 1, 2012, stock options vested and expected to vest totaled approximately 20.1 million shares, with a weighted-average remaining contractual life of 4.2 years and a weighted-average exercise price of \$6.41 per share. The aggregate intrinsic value was approximately \$146.8 million.

Restricted Stock Units and Restricted Stock Awards:

The following table summarizes our restricted stock unit and restricted stock award activities:

	Shares (In thousands, except per-share amounts)	Weighted- Average Grant Date Fair Value Per Share
Balance as of January 1, 2012	9,005	\$ 4.90
Granted	3,904	\$ 16.07
Released	(3,372)	\$ 7.15
Forfeited	(1,353)	\$ 7.47
Balance as of April 1, 2012	8,184	\$ 14.96
Granted	306	\$ 13.62
Released	(439)	\$ 9.77
Forfeited	(121)	\$ 16.68
Balance as of July 1, 2012	7,930	\$ 15.17

In the first and second quarters of fiscal 2012, we released 3.8 million shares which included 0.5 million performance-based awards (PARS) incremental shares issued due to overachievement on the PSoC revenue milestone against the target. The said incremental shares were approved by the Compensation Committee. As these 0.5 million PARS were approved during the first quarter of fiscal 2012, they were treated as new awards for accounting purposes. As such, the related compensation cost of approximately \$9.0 million was included in our Condensed Consolidated Statement of Operations for the six months ended July 1, 2012.

Table of Contents

CYPRESS SEMICONDUCTOR CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

The 7.9 million outstanding restricted stock units and awards as of July 1, 2012 included approximately 3.8 million PARS granted under the Amended and Restated 1994 Stock Plan. These PARS were issued to certain senior-level employees in the first quarter of fiscal 2012 and can be earned ratably over a period of one to two years, subject to the achievement of certain performance milestones set by the Compensation Committee. These performance milestones include the following:

Core Grant a company-wide scorecard of various individual milestones focused on financial results, cost savings, gaining additional market share, introducing new products on specific schedules and implementing various operational and customer facing systems (Core Grant Scorecard). Each individual milestone is assigned a specific number of points and each milestone has specific accomplishments that are documented in advance in order to achieve 100% of the milestone and scales down to a specific 0% point. The maximum number of points that can be achieved is 100 and there is no discretionary component to the Core Grant Scorecard. In order for an executive to earn 100% of the shares underlying the Core Grant, the Company must obtain 90.0 points or greater under the Core Grant Scorecard and the achievement then scales down linearly to 0% of shares earned if the Core Grant Scorecard is less than 50 points.

Tier 1 Grant requires the Company to achieve an approved design win during calendar year 2012 at a certain large multi-national consumer electronics company utilizing certain of the Company s new products (Tier 1 Targeted Design Win). In order for an executive to earn 100% of the shares underlying the Tier 1 Grant, the Tier 1 Targeted Design Win dollar value must be greater than a specified multimillion dollar amount and achievement then scales down linearly to 0% of the shares earned if the Tier 1 Targeted Grant Design Win is less than a specified dollar amount.

Tier 2 Grant requires the Company to grow its 2012 annual revenue at a year-over-year percentage rate (Annual Revenue Growth Rate) greater than a group of peer companies that it directly competes with. There are ten (10) companies, including Cypress, that comprise the peer group and all companies have been agreed upon in advance by the Compensation Committee. To earn 100% of the shares underlying the Tier 2 Grant the Company would need to be ranked #1 out of 10 in the Annual Revenue Growth Rate. To earn 75%, 50% or 25% of the shares underlying the Tier 2 Grant, the Company would need to be ranked #2, #3, and #4, respectively, in the Annual Revenue Growth Rate. No shares can be earned if the Company is ranked #5 or below among the peer group or if the Company s 2012 annual revenue change rate is negative by 10% or more regardless of how the Company ranks compared to the group of peer companies.

In the event of overachievement in the Tier 1 and Tier 2 Grant milestones and at the discretion of the Compensation Committee, the number of shares that can be earned could exceed 100% of the shares underlying the Tier 1 and Tier 2 Grants. However, under all circumstances, the total number of shares that can be earned under all three milestones cannot exceed the maximum target shares under the 2012 PARS. As at the end of the second quarter of fiscal 2012, management has estimated that approximately 48% of the overall 2012 PARS are expected to vest, and has accordingly recorded the stock compensation expense based on the number of shares expected to vest.

Upon certification and confirmation by the Compensation Committee, the earned shares for the Core Grant and Tier 1 Grant shares will be 100% vested at the time of delivery. Tier 2 Grant shares will have a twelve-month cliff vest following certification of the milestone attainment.

If the milestones are not achieved, the shares are forfeited and cannot be earned in future periods.

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 8. COMMITMENTS AND CONTINGENCIES****Operating Lease Commitments**

We lease certain facilities and equipment under non-cancelable operating lease agreements that expire at various dates through fiscal 2018. Some leases include renewal options, which would permit extensions of the expiration dates at rates approximating fair market rental values at the time of the extension.

As of July 1, 2012, future minimum lease payments under non-cancelable operating leases were as follows:

Fiscal Year	(In thousands)
2012 (remaining six months)	\$ 4,561
2013	5,473
2014	4,236
2015	3,390
2016	2,317
2017 and thereafter	2,640
Total	\$ 22,617

Capital Lease

On July 19, 2011, we entered into a capital lease agreement which allows us to borrow up to \$35.0 million to finance the acquisition of certain manufacturing equipment. We have the option of purchasing the tools from the lessor at specified intervals during the lease term. The master lease contains standard covenants requiring us to insure and maintain the equipment in accordance with the manufacturers' recommendations and comply with other customary terms to protect the leased assets. In addition, the master lease agreement contains provisions in the event of default. Assets purchased under the capital lease are included in Property, plant and equipment, net as manufacturing equipment and the amortization is included in depreciation. As of July 1, 2012, the gross value and net book value of manufacturing equipment purchased under a capital lease was approximately \$20.5 million and \$19.0 million, respectively. As of July 1, 2012, the total minimum lease payments under our capital leases amounted to approximately \$17.5 million.

Future minimum payments, by year and in the aggregate, under the capitalized lease consist of the following:

Fiscal Year	(In thousands)
2012 (remaining six months)	\$ 1,468
2013	2,937
2014	2,936
2015	2,937
2016 and thereafter	7,181
Total minimum lease payments	17,459
Less: amount representing interest	1,150

Present value of net minimum lease payments	\$	16,309
---	----	--------

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****Equity Investment Commitments**

As disclosed in Note 5, we have committed to purchase additional preferred stock from a company in a series of subsequent closings which are subject to certain performance milestones that must be fulfilled within a defined and agreed-upon timeline. Our future commitment to purchase additional preferred stock is approximately \$0.6 million in fiscal 2012, \$60.8 million in fiscal 2013 and \$17.8 million in fiscal 2014 subject to the attainment of certain milestones and the timing of additional capital requests which could vary substantially.

Product Warranties

We generally warrant our products against defects in materials and workmanship for a period of one year and that product warranty is generally limited to a refund of the original purchase price of the product or a replacement part. We estimate our warranty costs based on historical warranty claim experience. Warranty returns are recorded as an allowance for sales returns. The allowance for sales returns is reviewed quarterly to verify that it properly reflects the remaining obligations based on the anticipated returns over the balance of the obligation period.

The following table presents our warranty reserve activities:

	Three Months Ended		Six Months Ended	
	July 1, 2012	July 3, 2011	July 1, 2012	July 3, 2011
	(In thousands)			
Beginning balance	\$ 3,056	\$ 3,466	\$ 3,085	\$ 3,347
Settlements made	(41)	(435)	(506)	(656)
Provisions	76	89	512	429
Ending Balance	\$ 3,091	\$ 3,120	\$ 3,091	\$ 3,120

Patent License Agreement

On April 30, 2012, we entered into a strategic Patent License Agreement (PLA) with IV Global Licensing LLC (IV) under which we and our majority-owned subsidiaries will receive a license to IV's substantial patent portfolio. This transaction will allow us and IV to continue to develop our strategic relationship regarding patent monetization and litigation defense. Under the terms of the PLA, we have agreed to pay a license fee of approximately \$14 million and to purchase certain litigation defense services from IV in the future. In addition, in a related agreement, IV is expected to make certain patent purchases from us in the near term. The exact terms and conditions of the PLA are subject to confidentiality provisions, and are the subject of an application for confidential treatment to be filed with the SEC.

One of the benefits that we received from the PLA was the avoidance of future litigation expenses as well as future customer disruption and based upon our analysis, using a relief from royalty method, we determined that a portion of the license fee that we will pay IV represents the cumulative cost relating to prior years. As such, we recorded approximately \$7.1 million charge to cost of revenues during the six months ended July 1, 2012 and we determined that the remaining \$6.9 million in licensing fees had future value and will be amortized over the remaining period of the agreement. We recorded a corresponding liability for the \$14.0 million which is part of Other current liabilities in the Condensed Consolidated Balance Sheet as of July 1, 2012. We paid one half of the liability in July 2012 and the remaining \$7.0 million is due to be paid by the end of fiscal 2012.

Litigation and Asserted Claims

Edgar Filing: CYPRESS SEMICONDUCTOR CORP /DE/ - Form 10-Q

On March 30, 2011, we filed a five patent infringement case against GSI Technology (GSI) in the U.S. District Court in Minnesota. The five patents at issue cover GSI's static random access memory (SRAM) technology, including GSI's Sigma DDR and SigmaQuad II and III families of memory products. We are seeking damages as well as injunctive relief from the court. On July 23, 2011, the International Trade Commission (ITC) instituted a formal action to enjoin the importation of GSI products that infringe four of our U.S. patents. Thereafter, we expanded the scope of the ITC action to include GSI's standard synchronous and ZBT SRAMs as well as a proprietary product made for GSI's largest customer. We successfully completed trial in this matter on March 14, 2012 and post-trial briefing was complete as of April 6, 2012. We are currently awaiting the initial determination from the ITC, which was expected on or around July 28, 2012 but has been delayed to late October 2012. We believe strongly in the merits of our ITC action, and intend to take the steps necessary to protect our intellectual property.

Table of Contents

CYPRESS SEMICONDUCTOR CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

In July 2011, GSI filed requests for re-examination of two of our asserted U.S. Patents (Nos. 7,142,477 and 6,534,805) with the U.S. Patent and Trademark Office (PTO). The PTO has completed its re-examination of our U.S. Patent No. 7,142,477 and confirmed its validity. The PTO confirmed without amendment both of the claims being asserted by Cypress in the ITC case. The PTO also expanded the scope of the patent by allowing 64 new claims added by us during the re-examination. GSI also filed a civil complaint with the Federal District Court in Northern California, accusing the QDR Consortium, of which we are a member, of certain anti-competitive activity. The case has been stayed until recently when the courts ruled that the case move forward. We expect the case schedule to be determined sometime in August 2012. Aside from injunctive relief, GSI has made no specific monetary demand in the anti-trust matter. Accordingly, the possible range of monetary loss in the matter, if any, is demanded in the future, is unknown at this time. We believe we have meritorious defenses to the allegations set forth in the GSI civil complaint and we will vigorously defend ourselves in that matter.

On June 28, 2012, the U.S. District Court in Delaware dismissed with prejudice the single patent infringement case filed against us by Commonwealth Resource Group, LLC (CRG). We made no payments of any kind nor did we admit to any infringement in connection with the dismissal.

On February 16, 2012, the bankruptcy trustee of the assets of Qimonda AG, a non-operating entity, filed a four-patent infringement case naming Cypress and four other defendants in the U.S. District Court of Eastern Virginia. On June 15, 2012, our motion to transfer the case to the Northern District of California was granted. We also filed a motion to dismiss the case, which will now be decided by the Northern California District court judge assigned to this matter. We continue to believe we have meritorious non-infringement and invalidity defenses in this case, and as such, we will defend ourselves vigorously. Qimonda is seeking injunctive relief as well as unspecified monetary damages. Because the case is at a very early stage and no specific monetary demand has been made, it is not possible for us to estimate the potential loss or range of potential losses.

We are currently a party to various other legal proceedings, claims, disputes and litigation arising in the ordinary course of business. Based on our own investigations, we believe the ultimate outcome of our current legal proceedings, individually and in the aggregate, will not have a material adverse effect on our financial position, results of operation or cash flows. However, because of the nature and inherent uncertainties of the litigation, should the outcome of these actions be unfavorable, our business, financial condition, results of operations or cash flows could be materially and adversely affected.

NOTE 9. DEBT AND EQUITY TRANSACTIONS

Line of Credit

On March 28, 2012, we amended our revolving line of credit with Silicon Valley Bank to increase the available borrowing from \$5 million to \$55 million and to extend the maturity date to March 27, 2013. On March 29, 2012, we borrowed \$50 million under this line of credit. On June 26, 2012 we repaid the outstanding balance of \$50 million and accrued interest and terminated the revolving line of credit, replacing it with a secured revolving credit facility.

Senior Secured Revolving Credit Facility

On June 26, 2012, we entered into a five-year senior secured revolving credit facility (Credit Facility) with a group of lenders led by Morgan Stanley Senior Funding, Inc. as administrative agent and collateral agent. The Credit Facility enables us to borrow up to \$430 million on a revolving basis. Borrowing terms vary based on the type of borrowing with all outstanding balances being due at the credit facility termination date, or June 25, 2017. Outstanding amounts may be repaid prior to maturity without penalty and are mandatory for certain asset sales and casualty events. For Eurodollar rate loans, the Credit Facility bears interest at LIBOR plus 2.25% on the drawn amount. There is a commitment fee payable of 0.375% per annum on any undrawn amounts. The Credit Facility contains customary affirmative, negative and financial covenants for similarly rated companies. The financial covenants include the following conditions: 1) maximum senior secured leverage ratio of 2.00 to 1.00, 2) maximum total leverage ratio of 3.50 to 1.00 through June 30, 2013 and 3.00 to 1.00 thereafter, 3) minimum fixed charge coverage ratio of 1.20 to 1.00, and 4) minimum liquidity of at least \$150 million. Borrowings are secured by substantially all assets of the

Edgar Filing: CYPRESS SEMICONDUCTOR CORP /DE/ - Form 10-Q

company. On June 27, 2012, we borrowed a Eurodollar rate loan of \$153.0 million at an interest rate of 2.5%. The borrowings were recorded as part of long-term liabilities and are presented as Loan payable in the Condensed Consolidated Balance Sheet as of July 1, 2012. As of July 1, 2012, we were in compliance with all of the financial covenants under the Credit Facility.

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)*****Equipment Loans***

In December 2011, we obtained equipment loans from a certain financial institution for an aggregate amount of approximately \$14.1 million. These loans are collateralized by certain of our manufacturing equipment and bear interest of 3.15% to 3.18% per annum and are payable in 60 equal installments with the first installments due in January 2012. The related master loan agreement includes a variety of standard covenants including restrictions on merger with another company without consent (which shall not be unreasonably withheld), liquidation or dissolution, and distribution, lease or transfer of our ownership interest in these properties or assets. During the first half of fiscal 2012, we repaid approximately \$1.3 million of the equipment loans. As of July 1, 2012, the outstanding balance of the equipment loans was approximately \$12.8 million, of which approximately \$2.7 million was recorded as part of Other current liabilities and \$10.1 million was recorded as part of Other long-term liabilities in the 2012 Condensed Consolidated Balance Sheet. At July 1, 2012, the fair value of the equipment loans approximated the carrying value. The fair value was estimated using discounted cash flow analysis using relevant factors that might affect the fair value, such as present value factors and risk-free interest rates based on the U.S. Treasury yield curve.

The schedule of principal payments under our equipment loans is as follows:

Fiscal Year	(In thousands)
2012 (remaining six months)	\$ 1,336
2013	2,737
2014	2,825
2015	2,915
2016	3,003
Total	\$ 12,816

Stock Buyback Program:***\$400 Million Program Authorized in Fiscal 2011***

On September 20, 2011, our Board of Directors authorized a new \$400 million stock buyback program. The program allows us to purchase our common stock or enter into equity derivative transactions related to our common stock. The timing and actual amount expended with the new authorized funds will depend on a variety of factors including the market price of our common stock, regulatory, legal, and contractual requirements, other uses of cash, and other market factors. The program does not obligate us to repurchase any particular amount of common stock and may be modified or suspended at any time at the discretion of our board of directors. For the three months ended July 1, 2012, we used approximately \$19.9 million from this program to repurchase approximately 1.5 million shares at an average share price of \$13.05. Since we announced our \$400 million stock buyback program in September 2011 through the end of the second quarter of fiscal 2012, we used approximately \$197.7 million from this program to repurchase approximately 12.7 million shares at an average share price of \$15.62. As of July 1, 2012, the remaining authorized amount that can be used to repurchase shares under the program was approximately \$202.3 million.

Dividends

On May 14, 2012, our Board approved a cash dividend of \$0.11 per share payable to holders of record of our common stock at the close of business day on June 28, 2012. This cash dividend was paid on July 19, 2012 and totaled approximately \$16.7 million which was accrued for in the second quarter of fiscal 2012 and shown as Dividends payable in the Condensed Consolidated Balance Sheet as of July 1, 2012.

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 10. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)**

The components of accumulated other comprehensive loss were as follows:

	As of	
	July 1, 2012	January 1, 2012
	(In thousands)	
Accumulated net unrealized loss on available-for-sale investments	\$ 588	\$ (1,551)
Other		(389)
Total accumulated other comprehensive income (loss)	\$ 588	\$ (1,940)

NOTE 11. FOREIGN CURRENCY DERIVATIVES

We operate and sell products in various global markets and purchase capital equipment using the U.S. dollar and foreign currencies. As a result, we are exposed to risks associated with changes in foreign currency exchange rates. We may use various hedge instruments from time to time to manage the exposures associated with purchases of foreign sourced equipment, net asset or liability positions of our subsidiaries and forecasted revenues and expenses. We do not enter into foreign currency derivative financial instruments for speculative or trading purposes. The counterparties to these hedging transactions are creditworthy multinational banks and the risk of counterparty nonperformance associated with these contracts is not considered to be material as of July 1, 2012. We estimate the fair value of our forward contracts based on spot and forward rates from published sources.

We record hedges of certain foreign currency denominated monetary assets and liabilities at fair value at the end of each reporting period with the related gains or losses recorded in Interest and other income, net in the Condensed Consolidated Statements of Operations. The gains or losses on these contracts are substantially offset by transaction gains or losses on the underlying balances being hedged. The aggregate notional value of outstanding forward contracts to hedge the risks associated with foreign currency denominated assets and liabilities as of July 1, 2012 and January 1, 2012 was not material.

NOTE 12. INCOME TAXES

Our income tax expense was \$0.5 million for the three months ended July 1, 2012 and tax benefit was \$14.4 million for the three months ended July 3, 2011. Our income tax expense was \$3.0 million and tax benefit was \$13.1 million for the six months ended July 1, 2012 and July 3, 2011, respectively. The tax provision for the second quarter of fiscal 2012 and first half of fiscal 2012 was primarily attributable to non-U.S. taxes on income earned in foreign jurisdictions. The tax benefit for the second quarter and first half of fiscal 2011 was primarily attributable to a release of previously accrued taxes and interest of \$18.4 million due to the completion of an income tax examination, and expired statutes of limitations in foreign jurisdictions, partially offset by non-U.S. taxes on income earned in foreign jurisdictions.

Unrecognized Tax Benefits

As of July 1, 2012 and January 1, 2012, the amount of unrecognized tax benefits that, if recognized, would affect our effective tax rate totaled \$27.5 million and \$27.5 million, respectively.

Management believes events that could occur in the next 12 months and cause a material change in unrecognized tax benefits include, but are not limited to, the following:

completion of examinations by the U.S. or foreign taxing authorities; and

expiration of statute of limitations on our tax returns.

The calculation of unrecognized tax benefits involves dealing with uncertainties in the application of complex global tax regulations. Management regularly assesses our tax positions in light of legislative, bilateral tax treaty, regulatory and judicial developments in the countries in which we do business. We believe it is possible that we may recognize approximately \$2.5 million to \$3.5 million of our existing unrecognized tax benefits within the next twelve months as a result of the lapse of statutes of limitations and the resolution of agreements with domestic and various foreign tax authorities.

Classification of Interest and Penalties

Our policy is to classify interest and penalties, if any, as components of the income tax provision in the Condensed Consolidated Statements of Operations. As of July 1, 2012 and January 1, 2012, the amount of accrued interest and penalties totaled \$10.7 million and \$9.8 million, respectively.

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 13. NET INCOME (LOSS) PER SHARE**

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

	Three Months Ended		Six Months Ended	
	July 1, 2012	July 3, 2011	July 1, 2012	July 3, 2011
	(In thousands, except per-share amounts)			
Net income (loss) attributable to Cypress	\$ 4,977	\$ 40,823	\$ (14,484)	\$ 96,197
Weighted-average common shares	151,765	168,723	152,894	170,034
Weighted-average diluted shares	164,605	192,276	152,894	196,110
Net income (loss) per share- basic	\$ 0.03	\$ 0.24	\$ (0.09)	\$ 0.57
Net income (loss) per share- diluted	\$ 0.03	\$ 0.21	\$ (0.09)	\$ 0.49

For the three and six months ended July 1, 2012, approximately 7.2 million and 18.5 million weighted common stock equivalents, respectively, were excluded in the computation of diluted net loss per share because their effect would have been anti-dilutive.

For the three and six months ended July 3, 2011, approximately 1.6 million and 1.5 million weighted common stock equivalents, respectively, were excluded from the calculation of diluted net income per share because their inclusion would have been anti-dilutive.

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)****NOTE 14. SEGMENT, GEOGRAPHICAL AND CUSTOMER INFORMATION*****Segment Information***

During the three months ended April 1, 2012, we realigned our operating segments as part of our continued efforts to better allocate key management resources and to focus on our core markets, such as our programmable products including our flagship programmable system-on-chip (PSoC®) solution and its derivatives, universal serial bus (USB), including the high performance West Bridge solutions, and our industry leading high performance static random access memory (SRAM) solutions. Accordingly, beginning with the three months ended April 1, 2012, we have reported our financial results under the following business segments:

Business Segments	Description
MPD: Memory Products Division	An existing division that will continue to focus on our four SRAM business units, general-purpose programmable clocks and process technology licensing.
DCD: Data Communications Division	An existing division realigned to focus solely on USB controllers, WirelessUSB and West Bridge® peripheral controllers for handsets, personal computers and tablets.
PSD: Programmable Systems Division	A new division focusing primarily on our PSoC® and PSoC-based products. This business segment focuses on (1) the PSoC platform family of devices including PSoC 1, PSoC 3 and PSoC 5 and all derivatives; (2) PSoC-based user interface products such as CapSense® touch-sensing and TrueTouch touchscreen products; (3) PSoC-based module solutions including Trackpad and Ovation Optical Navigation Sensors (ONS); (4) automotive products; and (5) certain legacy product lines.
ETD: Emerging Technologies Division	Our startup division, which includes Cypress EnviroSystems, AgigA Tech Inc. and Deca Technologies Inc., all majority-owned subsidiaries of Cypress. ETD also includes our foundry business and other development-stage activities.

As a result of the change in the structure of our operating segments, the financial results we reported in prior periods under the old business segment structure have been recast to conform to the new segment presentation. This reclassification did not impact our previously reported consolidated revenues, operating income, net income, or earnings per share. Also, the change in our business operating segments did not have any impact on the reporting units that we use for goodwill impairment purposes.

The following tables set forth certain information relating to our reportable business segments under the new reporting structure:

Revenue:

Three Months Ended		Six Months Ended	
July 1,	July 3,	July 1,	July 3,
2012	2011	2012	2011

Edgar Filing: CYPRESS SEMICONDUCTOR CORP /DE/ - Form 10-Q

	(In thousands)			
Programmable Systems Division	\$ 96,114	\$ 124,034	\$ 177,650	\$ 218,882
Memory Products Division	82,949	97,401	164,828	202,268
Data Communications Division	20,407	32,203	40,353	65,015
Emerging Technologies Division	1,830	1,340	3,559	1,923
Total revenue	\$ 201,300	\$ 254,978	\$ 386,390	\$ 488,088

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)*****Income (Loss) before Income Taxes:***

	Three Months Ended		Six Months Ended	
	July 1,	July 3,	July 1,	July 3,
	2012	2011	2012	2011
	(In thousands)			
Programmable Systems Division	\$ 3,486	\$ 24,317	\$ (649)	\$ 32,901
Memory Products Division	33,117	39,182	64,616	78,668
Data Communications Division	225	4,491	267	10,721
Emerging Technologies Division	(5,929)	(4,914)	(12,375)	(9,819)
Unallocated items:				
Stock-based compensation	(22,230)	(29,740)	(50,967)	(50,577)
Patent license fee			(7,100)	
Amortization of acquisition-related intangibles	(731)	(731)	(1,463)	(1,429)
Restructuring charges	(989)	(3,798)	(1,217)	(4,532)
Changes in value of deferred compensation plan	(530)	(46)	25	(208)
Gain on divestiture				34,291
Charitable donation of building				(4,125)
Impairment of assets and other	(1,270)	(2,552)	(3,294)	(3,142)
Income (loss) before income taxes	\$ 5,149	\$ 26,209	\$ (12,157)	\$ 82,749

Geographical Information

The following table presents our revenues by geographical locations:

	Three Months Ended		Six Months Ended	
	July 1,	July 3,	July 1,	July 3,
	2012	2011	2012	2011
	(In thousands)			
United States	\$ 27,846	\$ 28,185	\$ 55,034	\$ 59,306
Europe	18,933	30,405	42,306	65,825
Asia:				
China	68,723	100,208	128,100	179,594
South Korea	26,702	32,473	48,133	54,666
Rest of the World	59,096	63,707	112,817	128,697
Total revenue	\$ 201,300	\$ 254,978	\$ 386,390	\$ 488,088

Table of Contents**CYPRESS SEMICONDUCTOR CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)*****Depreciation:***

	Three Months Ended		Six Months Ended	
	July 1, 2012	July 3, 2011	July 1, 2012	July 3, 2011
	(In thousands)			
Programmable Systems Division	\$ 5,033	\$ 6,551	\$ 9,311	\$ 11,565
Memory Products Division	4,380	5,120	8,673	10,663
Data Communications Division	1,148	1,710	2,244	3,444
Emerging Technologies Division	1,107	112	2,122	194
Total depreciation	\$ 11,668	\$ 13,493	\$ 22,350	\$ 25,866

Property, plant and equipment, net, by geographic locations were as follows:

	July 1, 2012	As of January 1, 2012
	(In thousands)	
United States	\$ 181,523	\$ 187,438
Philippines	72,930	75,323
Other	21,610	22,218
Total property, plant and equipment, net	\$ 276,063	\$ 284,979

We track our assets by physical location. Although management reviews asset information on a corporate level and allocates depreciation expense by segment, our chief operating decision maker does not review asset information on a segment basis.

Customer Information

Outstanding accounts receivable from Arkian, a distributor, accounted for 20% of our consolidated accounts receivable as of July 1, 2012. Outstanding accounts receivable from Arrow Electronics, Inc., Arkian and Avnet, Inc., three of our distributors, accounted for 14%, 14% and 11% of our consolidated accounts receivable as of January 1, 2012, respectively.

Revenue generated through Avnet, Inc., Macnica, Inc. and Arkian accounted for 12%, 12% and 12%, respectively, of our consolidated revenue for the three months ended July 1, 2012. Revenue generated through Avnet, Inc., Arkian and Macnica, Inc. accounted for 13%, 11% and 11%, respectively, of our consolidated revenue for the six months ended July 1, 2012. Samsung Electronics (Samsung), an end customer, purchases our products from certain of our distributors, primarily from Arkian. Shipments made by our distributors to Samsung during the three and six months ended July 1, 2012 accounted for 12% and 12% of our consolidated revenue, respectively.

For the three and six months ended July 3, 2011, two global distributors accounted for 26% and 24% of our total revenues. No one end customer accounted for more than 10% of our total revenues.

NOTE 15. SUBSEQUENT EVENTS

On July 26, 2012, we entered into a short-term yield enhancement structured agreement with a maturity of less than 45 days at an aggregate price of approximately \$14.5 million. Under this agreement, we can receive up to 1.5 million shares of our common stock or up to \$0.4 million in cash depending on the closing market price at the expiration of each agreement based on a pre-determined price.

We enter into yield enhanced structured agreements based upon a comparison of the yields available in the financial markets for similar maturities against the expected yield to be realized per the structured agreement and the related risks associated with this type of arrangement. We believe the risk associated with these types of agreements is no different than alternative investments available to us with equivalent counterparty credit ratings. All counterparties to a yield enhancement program have a credit rating of at least Aa2 or A as rated by major independent rating agencies.

Table of Contents**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The Management's Discussion and Analysis of Financial Condition and Results of Operations in this Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, that involve risks and uncertainties, which are discussed in the Forward-Looking Statements section under Part I of this Quarterly Report on Form 10-Q.

EXECUTIVE SUMMARY**General**

Cypress Semiconductor Corporation (Cypress) delivers high-performance, mixed-signal, programmable solutions that provide customers with rapid time-to-market and exceptional system value. Our offerings include the flagship PSoC® families and derivatives such as CapSense® touch sensing and TrueTouch solutions for touchscreens. We are the world leader in USB controllers, including the high-performance West Bridge® solution that enhances connectivity and performance in multimedia handsets. In addition we are the industry leader in the high-performance SRAM memory market and a market leader in programmable timing devices. We serve numerous markets including consumer, mobile handsets, computation, data communications, automotive, industrial and military. Cypress programmable products can be found in a wide array of the world's leading end products, including cell phones, tablets, PCs and PC peripherals, audio and gaming devices, household appliances, and communications devices.

As discussed in Note 14 of Notes to Condensed Consolidated Financial Statements under Part I, Item 1 *Financial Statements*, we have realigned our business segments as outlined below.

Business Segments	Description
MPD: Memory Products Division	An existing division that will continue to focus on our four SRAM business units, general-purpose programmable clocks and process technology licensing.
DCD: Data Communications Division	An existing division realigned to focus solely on USB controllers, WirelessUSB and West Bridge® peripheral controllers for handsets, PCs and tablets.
PSD: Programmable Systems Division	A new division focusing primarily on our PSoC® and PSoC-based products. This business segment focuses on (1) the PSoC platform family of devices including PSoC 1, PSoC 3 and PSoC 5 and all derivatives; (2) PSoC-based user interface products such as CapSense® touch-sensing and TrueTouch touchscreen products; (3) PSoC-based module solutions including Trackpad and Ovation Optical Navigation Sensors (ONS); (4) automotive products; and (5) certain legacy product lines.
ETD: Emerging Technologies Division	Our startup division, which includes Cypress EnviroSystems, AgigA Tech Inc. and Deca Technologies Inc., all majority-owned subsidiaries of Cypress. ETD also includes our foundry business and other development-stage activities.

Manufacturing Strategy

Our core manufacturing strategy flexible manufacturing combines capacity from foundries with output from our internal manufacturing facilities. This initiative is intended to allow us to meet rapid swings in customer demand while lessening the burden of high fixed costs, a capability that is particularly important in high-volume consumer markets that we serve with our leading programmable product portfolio.

Table of Contents***Results of Operations******Revenues***

The following table summarizes our consolidated revenues by segments under the new reporting structure:

	Three Months Ended		Six Months Ended	
	July 1, 2012	July 3, 2011	July 1, 2012	July 3, 2011
	(In thousands)			
Programmable Systems Division	\$ 96,114	\$ 124,034	\$ 177,650	\$ 218,882
Memory Products Division	82,949	97,401	164,828	202,268
Data Communications Division	20,407	32,203	40,353	65,015
Emerging Technologies Division	1,830	1,340	3,559	1,923
Total Revenues	\$ 201,300	\$ 254,978	\$ 386,390	\$ 488,088

Programmable Systems Division:

Revenues from the Programmable Systems Division decreased by \$27.9 million in the second quarter of fiscal 2012 and \$41.2 million in the first half of fiscal 2012, or approximately 22.5% and 18.8%, respectively, compared to the same prior-year periods. These decreases were primarily attributable to a decline in sales of our PSoC platform family of devices and a decline in sales of our TrueTouch® touchscreen products. The decrease in our TrueTouch® revenue stream was primarily due to a decrease in revenue from our handset and tablet customers and lower average selling prices.

Memory Products Division:

Revenues from the Memory Products Division decreased by approximately \$14.5 million in the second quarter of fiscal 2012 and \$37.4 million in the first half of fiscal 2012, or approximately 14.8% and 18.5%, respectively, compared to the same prior-year periods. The decrease in MPD revenue in the second quarter of fiscal 2012 and the first half of fiscal 2012 was primarily attributable to a \$11.7 million and \$20.2 million decrease in revenue of our SRAM products driven by the decreased demand from wireless and wireline end customers, a \$7.6 million decrease in revenue due to the divestiture of our Image Sensors business unit during the three months ended April 3, 2011, a \$1.6 million and \$3.6 million decrease in revenue of SPCM (dual-port memories) products, and a \$1.1 million and \$3.8 million decrease in revenue of our general-purpose programmable clocks.

Data Communications Division:

Revenues from the Data Communications Division decreased by \$11.8 million in the second quarter of fiscal 2012 and \$24.7 million in the first half of fiscal 2012, or approximately 36.6% and 37.9%, respectively, compared to the same prior-year periods primarily due to the decreases in sales of our West Bridge controllers and other USB-related products.

Emerging Technologies Division:

Revenues from Emerging Technologies Division increased by \$0.5 million in the second quarter of fiscal 2012 and \$1.6 million in the first half of fiscal 2012, respectively, compared to the same prior-year periods primarily due to the overall increase in demand as certain of our Emerging Technologies have begun initial production ramps.

Table of Contents*** Cost of Revenues/Gross Margins**

	Three Months Ended		Six Months Ended	
	July 1, 2012	July 3, 2011	July 1, 2012	July 3, 2011
	(In thousands)			
Cost of revenues	\$ 94,531	\$ 115,958	\$ 187,840	\$ 220,292
Gross Margin	53.0%	54.5%	51.4%	54.9%

Gross margin percentage decreased to 53.0% in the second quarter of fiscal 2012 from 54.5% in the second quarter of fiscal 2011 and decreased to 51.4% in the first half of fiscal 2012 from 54.9% in the first half of fiscal 2011. In the second quarter of fiscal 2012 gross margin decreased by 1.5 percentage points compared to the second quarter of fiscal 2011 primarily due to product mix and lower fixed cost absorption in our factories.

In the first half of fiscal 2012 gross margin decreased by 3.5 percentage points compared to the first half of fiscal 2011 primarily due to (i) \$7.1 million patent license fee recorded during the three months ended April 1, 2012 related to a Patent License Agreement discussed in Note 8 of Notes to Condensed Consolidated Financial Statements under Part I, Item 1 and (ii) the impact of the negative gross margins of our majority-owned subsidiaries (i.e., Emerging Technologies), particularly Deca Technologies, Inc. which has commenced revenue generating activities during the first half of fiscal 2012.

Research and Development (R&D) Expenses

	Three Months Ended		Six Months Ended	
	July 1, 2012	July 3, 2011	July 1, 2012	July 3, 2011
	(In thousands)			
R&D expenses	\$ 47,946	\$ 49,278	\$ 95,914	\$ 97,143
As a percentage of revenues	23.8%	19.3%	24.8%	19.9%

R&D expenditures decreased by \$1.3 million in the second quarter of fiscal 2012 compared to the same prior-year period. The decrease was primarily attributable to a decrease in variable bonus-related expenses of \$2.7 million and a decrease in stock-based compensation of \$1.4 million. These decreases were partially offset by an increase in purchased technology of \$1.0 million. As a percentage of revenues, R&D expenses were higher in the second quarter of fiscal 2012 driven by the decrease in total revenues in the same quarter.

R&D expenditures decreased by \$1.2 million in the first half of fiscal 2012 compared to the same prior-year period. The decrease was primarily attributable to a decrease in direct and indirect labor expenses, particularly variable bonus-related expenses. As a percentage of revenues, R&D expenses were higher in the first half of fiscal 2012 driven by the decrease in total revenues in the same period.

Our future operating results depend to a considerable extent on our ability to maintain a competitive advantage. Our research and development efforts are focused on the development and design of new semiconductor products, as well as the continued development of advanced software platforms primarily for our programmable solutions and investments in new products for our Emerging Technologies Division. Our goal is to increase efficiency in order to maintain our competitive advantage. We continue to make substantial investments in R&D to ensure the availability of innovative products that meet the current and projected requirements of our customers' most advanced designs.

Selling, General and Administrative (SG&A) Expenses

	Three Months Ended		Six Months Ended	
	July 1, 2012	July 3, 2011	July 1, 2012	July 3, 2011
	(In thousands)			
SG&A expenses	\$ 51,955	\$ 58,482	\$ 112,448	\$ 117,134
As a percentage of revenues	25.8%	22.9%	29.1%	24.0%

SG&A expenses decreased by \$6.5 million in the second quarter of fiscal 2012 compared to the same prior-year period. The decrease was primarily attributable to a \$7.2 million decrease in stock-based compensation, a \$3.3 million decrease in direct and

Table of Contents

indirect labor expenses, particularly a \$1.8 million decrease in variable bonus-related expenses, and a \$1.1 million decrease in marketing and advertising expenses primarily due to the annual sales conference which took place in the first quarter of fiscal 2011 and took place in the second quarter of fiscal 2012. These decreases were partially offset by a \$2.1 million increase in professional and legal fees due to the sale of certain patents in the first quarter of fiscal 2011 and a \$2.0 million increase for acquisition related costs.

SG&A expenses decreased by \$4.7 million in the first half of fiscal 2012 compared to the same prior-year period. The decrease was primarily attributable to \$5.4 million decrease in direct and indirect labor expenses, particularly a \$3.4 million decrease in variable bonus-related expenses and a \$4.0 million decrease in fixed asset write-offs from the donation of a building to a charitable organization in the first quarter of fiscal 2011. These decreases were partially offset by a \$3.3 million increase in professional and legal fees due to the sale of certain patents in the first quarter of fiscal 2011 and \$1.8 million increase in stock-based compensation which was primarily due to the additional compensation expense related to the vesting acceleration of certain performance-based awards discussed in Note 7 of Notes to Condensed Consolidated Financial Statements under Part I, Item 1.

Gain on Divestiture

As part of our continued efforts to focus on programmable products including our flagship PSoC® programmable system-on-chip solutions and our TrueTouch touch-sensing controllers, we divested our image sensors product families by selling them to ON Semiconductor Corporation for a total cash consideration of \$34.0 million during the three months ended April 3, 2011. In connection with the divestiture, we recorded a gain of \$34.3 million in our Condensed Consolidated Statement of Operations for the three months ended April 3, 2011. We did not have any divestitures during the six months ended July 1, 2012.

Income Taxes

Our income tax expense was \$0.5 million for the three months ended July 1, 2012 and tax benefit was \$14.4 million for the three months ended July 3, 2011. Our income tax expense was \$3.0 million and tax benefit was \$13.1 million for the six months ended July 1, 2012 and July 3, 2011, respectively. The tax provision for the second quarter of fiscal 2012 and first half of fiscal 2012 was primarily attributable to non-U.S. taxes on income earned in foreign jurisdictions. The tax benefit for the second quarter and first half of fiscal 2011 was primarily attributable to a release of previously accrued taxes and interest of \$18.4 million due to the completion of an income tax examination, and expired statutes of limitations in foreign jurisdictions, partially offset by non-U.S. taxes on income earned in foreign jurisdictions.

LIQUIDITY AND CAPITAL RESOURCES

The following table summarizes information regarding our cash and investments and working capital:

	July 1, 2012	As of January 1, 2012
	(In thousands)	
Cash and cash equivalents	\$ 118,262	\$ 99,717
Short-term investments	92,542	66,613
Total cash, cash equivalents and short-term investments	\$ 210,804	\$ 166,330
 Total current assets	 \$ 481,616	 \$ 405,650
Total current liabilities	350,250	326,460
 Working capital	 \$ 131,366	 \$ 79,190

Key Components of Cash Flows

Six Months Ended

Edgar Filing: CYPRESS SEMICONDUCTOR CORP /DE/ - Form 10-Q

	July 1, 2012	July 3, 2011
	(In thousands)	
Net cash provided by operating activities	\$ 59,630	\$ 112,213
Net cash provided by (used in) investing activities	\$ (47,984)	\$ 77,335
Net cash provided by (used in) financing activities	\$ 6,899	\$ (172,578)

Six Months Ended July 1, 2012:

During the six months ended July 1, 2012, cash and cash equivalents increased by approximately \$18.5 million primarily due to the cash we generated from our operating and financing activities of approximately \$59.6 million and \$6.9 million, respectively. This increase was partially offset by the \$48.0 million cash we used in our financing activities, principally related to our purchase of available-for-sale investments and acquisition of property, plant and equipment.

Table of Contents

Operating Activities

The \$59.6 million cash generated from our operating activities during the six months ended July 1, 2012 was primarily due to \$80.0 million in net favorable non-cash adjustments to our net income, an increase in accounts payable and other liabilities, partially offset by the increase in accounts receivable, an increase in other current and long-term assets and a decrease in deferred income on sales to distributors.

The key changes in our working capital as of July 1, 2012 compared to January 1, 2012 were as follows:

Total cash, cash equivalents and short-term investments increased by \$44.5 million primarily due to the line of credit and Credit Facility proceeds.

Accounts receivable increased by \$22.7 million primarily due to an increase in distributor shipments.

Other current assets increased by \$9.8 million primarily due to an increase in miscellaneous receivables and prepaid expenses.

Net borrowings of \$153 million in the first half of fiscal 2012 from the Credit Facility.

Other current liabilities increased by \$16.2 million primarily due to the accrual of a patent license fee related to a Patent License Agreement discussed in Note 8 of Notes to Condensed Consolidated Financial Statements under Part I, Item 1.

Dividends payable increased by \$2.9 million due to the increase in dividend per share from \$0.09 to \$0.11.

Investing Activities

During the six months ended July 1, 2012, we used approximately \$48.0 million of cash from our investing activities primarily due to \$81.8 million of purchases of available-for-sale investments, \$19.7 million of cash used for property and equipment expenditures and \$7.2 million of cash was used for other investing activities, partially offset from net proceeds from the sales or maturities of investments totaling \$60.4 million.

Financing Activities

During the six months ended July 1, 2012, we generated approximately \$6.9 million of cash in our financing activities. The net cash provided by our financing activities was primarily due to \$203.0 million of cash we drew from our line of credit and Credit Facility and \$10.0 million of net proceeds from the issuance of common shares under our employee stock plans, partially offset by the \$97.9 million of cash we used to repurchase shares of our stock in the open market, \$57.7 million used to repay equipment leases and loans, \$20.0 million payments related to statutory income tax withholdings on vested restricted stock awards in lieu of issuing shares of stock (considered as part of our stock buyback program) and \$30.5 million dividends paid.

Six Months Ended July 3, 2011:

Operating Activities

During the six months ended July 3, 2011, net cash provided by operating activities was \$112.2 million which was primarily driven by higher net income adjusted for certain non-cash items including depreciation and amortization, stock-based compensation and partially offset by the gain on divestiture and changes in our working capital.

Investing Activities

Edgar Filing: CYPRESS SEMICONDUCTOR CORP /DE/ - Form 10-Q

During the six months ended July 3, 2011, we generated approximately \$77.3 million of cash from our investing activities which was primarily due to \$97.7 million of net proceeds from the sales or maturities and purchases of available-for-sale investments and \$34 million in proceeds from the sale of our Image Sensors business unit, partially offset by \$53.6 million of property and equipment expenditures.

Financing Activities

During the six months ended July 3, 2011, we used approximately \$172.6 million of cash in our financing activities. The net cash used in our financing activities was primarily due to \$101.5 million of cash we used to repurchase shares of our stock in the open market, \$127.8 million cash used for our yield enhancement structured agreements settling in our stock, and \$41.4 million payments related to statutory income tax withholdings on vested restricted stock awards in lieu of issuing shares of stock (considered as part of our stock buyback program), partially offset by \$49.9 million cash we received related to our yield enhancement structured agreements settling in cash and \$48.2 million net proceeds from the issuance of common shares under our employee stock plans.

Table of Contents**Liquidity and Contractual Obligations****Liquidity****Stock Buyback Programs:**

On September 20, 2011, our Board of Directors authorized a new \$400 million stock buyback program. The program allows us to purchase our common stock or enter into equity derivative transactions related to our common stock. The timing and actual amount expended with the new authorized funds will depend on a variety of factors including the market price of our common stock, regulatory, legal, and contractual requirements, other uses of cash, and other market factors. The program does not obligate us to repurchase any particular amount of common stock and may be modified or suspended at any time at the discretion of our board of directors. For the three months ended July 1, 2012, we used approximately \$19.9 million from this program to repurchase approximately 1.5 million shares at an average share price of \$13.05. Since we announced the new \$400 million stock buyback program in September 2012 through the end of the second quarter of fiscal 2012, we used approximately \$197.7 million from this program to repurchase approximately 12.7 million shares at an average share price of \$15.62. As of July 1, 2012, the remaining authorized amount that can be used to repurchase shares under the program was approximately \$202.3 million.

Contractual Obligations

The following table summarizes our contractual obligations as of July 1, 2012:

	Total	2012	2013 and 2014 (In thousands)	2015 and 2016	After 2016
Purchase obligations (1)	\$ 76,840	\$ 76,296	\$ 544	\$	\$
Operating lease commitments	22,617	4,561	9,709	5,707	2,640
Capital lease commitments	17,459	1,468	5,873	9,518	600
Patent license fee commitments (2)	19,809	14,009		5,800	
Total contractual obligations	\$ 136,725	\$ 96,334	\$ 16,126	\$ 21,025	\$ 3,240

(1) Purchase obligations primarily include non-cancelable purchase orders for materials, services, manufacturing equipment, building improvements and supplies in the ordinary course of business. Purchase obligations are defined as enforceable agreements that are legally binding on us and that specify all significant terms, including quantity, price and timing.

(2) On April 30, 2012, we entered into a patent license agreement whereby we have committed to pay a total patent license fee of \$14.0 million in fiscal 2012. We have also committed to pay another \$5.8 million on or before April 30, 2016 representing fees for future purchases of patents and patent related services.

As of July 1, 2012, our unrecognized tax benefits were \$27.5 million, which were classified as long-term liabilities. We believe it is possible that we may recognize approximately \$2.5 million to \$3.5 million of our existing unrecognized tax benefits within the next twelve months as a result of the lapse of statutes of limitations and the resolution of agreements with domestic and various foreign tax authorities.

Equity Investment Commitments

As disclosed in Note 5 of Notes to Condensed Consolidated Financial Statements under Part I, Item 1 *Financial Statements*, we have committed to purchase additional preferred stock from a company in a series of subsequent closings subject to certain performance milestones that must be fulfilled within a defined and agreed upon timeline. Our future commitment to purchase additional preferred stock is approximately \$0.6 million in fiscal 2012, \$60.8 million in fiscal 2013 and \$17.8 million in fiscal 2014 subject to the attainment of certain milestones and the timing of additional capital requests which could vary substantially.

Table of Contents

Capital Resources and Financial Condition

Our long-term strategy is to maintain a minimum amount of cash and cash equivalents for operational purposes and to invest the remaining cash in interest-bearing and highly liquid cash equivalents, debt securities and the purchase of our stock through our stock buyback program and payments of regularly scheduled cash dividends. As of July 1, 2012, in addition to \$118.3 million in cash and cash equivalents, we had \$92.5 million invested in short-term investments for a total cash and short-term investment position of \$210.8 million that is available for use in our current operations.

As of July 1, 2012, approximately 21% of our cash, cash equivalents and available-for-sale investments are funds held outside the United States. While these amounts are primarily invested in U.S. dollars, a portion is held in foreign currencies. All offshore balances are exposed to local, political, banking, currency control and other risks. In addition, these amounts, if repatriated may be subject to tax and other transfer restrictions.

We believe that liquidity provided by existing cash, cash equivalents and available-for-sale investments and our borrowing arrangements will provide sufficient capital to meet our requirements for at least the next twelve months. However, should prevailing economic conditions and/or financial, business and other factors beyond our control adversely affect the estimates of our future cash requirements, we could be required to fund our cash requirements by alternative financing. There can be no assurance that additional financing, if needed, would be available on terms acceptable to us or at all. We may choose at any time to raise additional capital or debt to strengthen our financial position, facilitate growth, enter into strategic initiatives including the acquisition of other companies and provide us with additional flexibility to take advantage of other business opportunities that arise.

Non-GAAP Financial Measures

Regulation G, conditions for use of Non-Generally Accepted Accounting Principles (Non-GAAP) financial measures, and other SEC regulations define and prescribe the conditions for use of certain Non-GAAP financial information. To supplement our condensed consolidated financial results presented in accordance with GAAP, we use Non-GAAP financial measures which are adjusted from the most directly comparable GAAP financial measures to exclude certain items, as described below. Management believes that these Non-GAAP financial measures reflect an additional and useful way of viewing aspects of our operations that, when viewed in conjunction with our GAAP results, provide a more comprehensive understanding of the various factors and trends affecting our business and operations. Non-GAAP financial measures used by us include gross margin, research and development expenses, selling, general and administrative expenses, operating income or loss, net income or loss and basic and diluted net income or loss per share.

Our Non-GAAP measures primarily exclude stock-based compensation, acquisition-related charges, impairments to goodwill, gain or losses on divestiture, investment-related gains and losses, discontinued operations, restructuring costs and other special charges and credits. Management believes these Non-GAAP financial measures provide meaningful supplemental information regarding our strategic and business decision making, internal budgeting, forecasting and resource allocation processes. In addition, these Non-GAAP financial measures facilitate management's internal comparisons to our historical operating results and comparisons to competitors' operating results.

We use each of these Non-GAAP financial measures for internal managerial purposes, when providing our financial results and business outlook to the public, to facilitate period-to-period comparisons and are used to formulate our formula driven cash bonus plan and any milestone based stock awards. Management believes that these Non-GAAP measures provide meaningful supplemental information regarding our operational and financial performance of current and historical results. Management uses these Non-GAAP measures for strategic and business decision making, internal budgeting, forecasting and resource allocation processes. In addition, these Non-GAAP financial measures facilitate management's internal comparisons to our historical operating results and comparisons to competitors' operating results.

Table of Contents

The following table shows our Non-GAAP financial measures:

	Three Months Ended	
	July 1, 2012	July 3, 2011
	(In thousands, except per share amounts)	
Non-GAAP gross margin	\$ 114,802	\$ 145,732
Non-GAAP research and development expenses	\$ 42,555	\$ 42,280
Non-GAAP selling, general and administrative expenses	\$ 41,144	\$ 40,677
Non-GAAP operating income	\$ 31,104	\$ 62,775
Non-GAAP net income attributable to Cypress	\$ 30,298	\$ 62,993
Non-GAAP net income per share attributable to Cypress- diluted	\$ 0.18	\$ 0.32

We believe that providing these Non-GAAP financial measures, in addition to the GAAP financial results, are useful to investors because they allow investors to see our results through the eyes of management as these Non-GAAP financial measures reflect our internal measurement processes. Management believes that these Non-GAAP financial measures enable investors to better assess changes in each key element of our operating results across different reporting periods on a consistent basis and provides investors with another method for assessing our operating results in a manner that is focused on the performance of our ongoing operations.

Table of Contents

CYPRESS SEMICONDUCTOR CORPORATION

RECONCILIATION OF GAAP FINANCIAL MEASURES TO NON-GAAP FINANCIAL MEASURES

(In thousands, except per-share data)

(Unaudited)

	Three Months Ended	
	July 1, 2012	July 3, 2011
	(In thousands, except per share amounts)	
GAAP gross margin	\$ 106,769	\$ 139,020
Stock-based compensation expense	7,759	6,714
Changes in value of deferred compensation plan	(40)	(2)
Impairment of assets and others	314	
Non-GAAP gross margin	\$ 114,802	\$ 145,732
GAAP research and development expenses	\$ 47,946	\$ 49,278
Stock-based compensation expense	(5,480)	(6,941)
Changes in value of deferred compensation plan	89	(57)
Non-GAAP research and development expenses	\$ 42,555	\$ 42,280
GAAP selling, general and administrative expenses	\$ 51,955	\$ 58,482
Stock-based compensation expense	(8,991)	(16,085)
Acquisition-related expense	(2,003)	
Changes in value of deferred compensation plan	183	3
Loss on sale of asset		(1,901)
Impairment of assets and other		178
Non-GAAP selling, general and administrative expenses	\$ 41,144	\$ 40,677
GAAP operating income (loss)	\$ 5,148	\$ 26,731
Stock-based compensation expense	22,230	29,740
Changes in value of deferred compensation plan	(312)	52
Acquisition-related expenses	2,734	731
Restructuring charges	989	3,798
Loss on sale of asset		1,901
Impairment of assets and others	315	(178)
Non-GAAP operating income	\$ 31,104	\$ 62,775
GAAP net income (loss) attributable to Cypress	\$ 4,977	\$ 40,823
Stock-based compensation	22,230	29,740
Impairment of assets and other	315	(178)
Acquisition-related expenses	2,734	731
Restructuring charges	989	3,798
Changes in value of deferred compensation plan	530	46
Investment-related gains/losses		(18)
Loss on sale of asset		1,901

Edgar Filing: CYPRESS SEMICONDUCTOR CORP /DE/ - Form 10-Q

Loss on foreign currency transactions	(1,049)	
Tax effects	(428)	(13,850)
Non-GAAP net income attributable to Cypress	\$ 30,298	\$ 62,993
GAAP net income (loss) per share attributable to Cypress-diluted	\$ 0.03	\$ 0.21
Stock-based compensation expense and other	0.14	0.15
Restructuring charges	0.01	0.02
Acquisition-related expenses	0.02	
Loss on sale of asset		0.01
Loss on foreign currency transactions	(0.01)	
Tax effects		(0.07)
Non-GAAP share count adjustment	(0.01)	
Non-GAAP net income attributable to Cypress- diluted	\$ 0.18	\$ 0.32

Table of Contents

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate Risks

Our investment portfolio consists of a variety of financial instruments that exposes us to interest rate risk, including, but not limited to, money market funds, commercial paper and corporate securities. These investments are generally classified as available-for-sale and, consequently, are recorded on our balance sheets at fair market value with their related unrealized gain or loss reflected as a component of accumulated other comprehensive income in stockholders' equity. Due to the relatively short-term nature of our investment portfolio, we do not believe that an immediate 10% increase in interest rates would have a material effect on the fair market value of our portfolio. Since we believe we have the ability to liquidate this portfolio, we do not expect our operating results or cash flows to be materially affected to any significant degree by a sudden change in market interest rates on our investment portfolio.

We are also exposed to interest rate risk related to our indebtedness, which includes our senior secured revolving credit facility. For further information, see Note 9 Debt and Equity Transactions in Part I, Item 1 of this Form 10-Q. A hypothetical increase in interest rates of 1.0% would result in a corresponding change in interest expense of approximately \$1.5 million per year.

Foreign Currency Exchange Risk

We operate and sell products in various global markets and purchase capital equipment using foreign currencies but predominantly the U.S. dollar. As a result, we are exposed to risks associated with changes in foreign currency exchange rates. Changes in exchange rates between foreign currencies and the U.S. dollar may adversely affect our operating margins. For example, when foreign currencies appreciate against the U.S. dollar, inventory and expenses denominated in foreign currencies become more expensive. An increase in the value of the U.S. dollar relative to foreign currencies could make our products more expensive for international customers, thus potentially leading to a reduction in demand, and therefore in our sales and profitability. Furthermore, many of our competitors are foreign companies that could benefit from such a currency fluctuation, making it more difficult for us to compete with those companies. We cannot predict the impact of future exchange rate fluctuations on our business and results of operations.

We analyzed our foreign currency exposure, including our hedging strategies, to identify assets and liabilities denominated in other currencies. For those assets and liabilities, we evaluated the effects of a 10% shift in exchange rates between those currencies and the U.S. dollar. We have determined that there would be an immaterial effect on our results of operations from such a shift.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures, as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act), that are designed to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating our disclosure controls and procedures, management recognized that disclosure controls and procedures, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the disclosure controls and procedures are met. Additionally, in designing disclosure controls and procedures, our management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible disclosure controls and procedures. The design of any disclosure controls and procedures also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

Based on their evaluation as of the end of the period covered by this Quarterly Report on Form 10-Q and subject to the foregoing, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were effective.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting that occurred during the three months ended July 1, 2012 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents**PART II OTHER INFORMATION****ITEM 1. LEGAL PROCEEDINGS**

The information required by this item is included in Note 8 of Notes to Condensed Consolidated Financial Statements under Item 1, Part 1 of this Quarterly Report on Form 10-Q and is incorporated herein by reference.

ITEM 1A. RISK FACTORS

Aside from the risk factors below, there have been no material changes to the risk factors set forth in our Annual Report on Form 10-K for the year ended January 1, 2012.

We utilize debt financing and such indebtedness could adversely affect our business, financial condition, results of operations, earnings per share and our ability to meet our payment obligations.

We routinely incur indebtedness to finance our operations and from time to time we have significant amounts of outstanding indebtedness and substantial debt service requirements. On June 26, 2012, we entered into a five-year senior secured revolving credit facility for up to \$430 million with a group of lenders led by Morgan Stanley Senior Funding, Inc. The credit facility contains customary affirmative, negative and financial covenants, including a maximum senior secured leverage ratio, a maximum total leverage ratio, minimum fixed charge coverage ratio, and a minimum liquidity of at least \$150 million. Our ability to meet our payment and other obligations and covenants under our indebtedness depends on our ability to generate significant cash flow. This, to some extent, is subject to general economic, financial, competitive, legislative and regulatory factors as well as other factors that are beyond our control. There is no assurance that our business will generate cash flow from operations, or that future borrowings will be available to us under our existing or any amended credit facilities or otherwise, in an amount sufficient to enable us to meet payment obligations under indebtedness we may under take from time to time. If we are not able to generate sufficient cash flow to service our debt obligations, we may need to refinance or restructure our debt, sell assets, reduce or delay capital investments, or seek to raise additional capital. If we are unable to implement one or more of these alternatives, we may not be able to meet our payment obligations under any indebtedness we owe. As of July 1, 2012, our outstanding debt included \$17.5 million in capital leases, \$12.8 million in equipment loans and \$153 million taken down from our recent credit facility. See Note 9 for more information on our new credit facility, Note 9 for more information on equipment loans, Note 8 for more information on capital leases and Note 5 for more information on advances received for the sale of auction rate securities.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**ISSUER PURCHASES OF EQUITY SECURITIES**

On September 20, 2011, our Board of Directors (the Board) authorized a new \$400 million stock buyback program. The program allows us to purchase our common stock or enter into equity derivative transactions related to our common stock. The timing and actual amount expended with the new authorized funds will depend on a variety of factors including the market price of our common stock, regulatory, legal, and contractual requirements, other uses of cash, and other market factors. The program does not obligate us to repurchase any particular amount of common stock and may be modified or suspended at any time at the discretion of our Board.

The table below sets forth information with respect to repurchases of our common stock made during the half of fiscal 2012 under this program:

	Total Number of Shares Purchased	Average Price Paid per Share (In thousands, except per-share amounts)	Total Shares Purchased as Part of Publicly Announced Programs	Total Dollar Value of Shares That May Yet Be Purchased Under the Plan or Program
Remaining balance available for purchases at the beginning of the period				\$ 320,189
<u>Repurchases during Q1-2012 (1):</u>				
January 2, 2012 January 29, 2012	97	\$ 16.90	97	\$ 318,543
January 30, 2012 February 26, 2012	1,087	\$ 17.87	1,087	\$ 299,124

Edgar Filing: CYPRESS SEMICONDUCTOR CORP /DE/ - Form 10-Q

February 27, 2012	April 1, 2012	4,887	\$ 15.75	4,887	\$ 222,160
Total repurchases during Q1-2012		6,071	\$ 16.15	6,071	\$ 222,160
Repurchases during Q2-2012 (1):					
April 2, 2012	April 29, 2012	6	\$ 15.14	6	\$ 222,077
April 30, 2012	May 27, 2012	1,402	\$ 13.09	1,402	\$ 203,715
May 28, 2012	July 1, 2012	115	\$ 12.44	115	\$ 202,282
Total repurchases during Q2-2012		1,523	\$ 13.05	1,523	\$ 202,282
Grand total repurchases during Q1 and Q2 2012		7,594		7,594	

(1) Monthly information is presented by reference to the Company's fiscal months during the first half of fiscal 2012.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable.

Table of Contents**PART II OTHER INFORMATION (Continued)****ITEM 5. OTHER INFORMATION****Quarterly Executive Incentive Payments**

On August 3, 2012, Cypress's Compensation Committee of the Board of Directors (the "Compensation Committee") approved incentive payments to our executive officers for the second quarter of fiscal 2012 performance incentive plans. These payments were earned in accordance with the terms of our Key Employee Bonus Plan (the "KEBP") and the Performance Bonus Plan (the "PBP").

The payments were determined based upon the financial performance of Cypress and each executive's performance. The performance measures under the KEBP include our non-GAAP profit-before-taxes percentage as well as individual strategic, operational and financial goals established for each executive. The following table sets forth the cash payments to our Named Executive Officers under the KEBP and the PBP in the second quarter of fiscal 2012:

Named Executive Officers	KEBP	PBP
T.J. Rodgers, President and Chief Executive Officer		\$ 2,787
Christopher Seams, Executive Vice President, Sales, Marketing and Operations	\$ 881	
Brad W. Buss, Executive Vice President, Finance & Administration and Chief Financial Officer	\$ 853	
Paul Keswick, Executive Vice President, New Product Development	\$ 312	
Cathal Phelan, Executive Vice President, Consumer and Computation Division		

Mr. Paul Keswick, our Executive Vice President of New Product Development, was paid an incentive payment amounting to \$8,967 in accordance with the terms of our Design Bonus Plan (the "DBP"). The payment amount was determined based upon the performance of Mr. Keswick during the second quarter of fiscal 2012. Mr. Keswick is the only named executive officer participant to the DBP as it is a bonus plan available to our design and certain product development engineers.

Additionally, there were incentive payments for the second quarter of fiscal 2012 under the KEBP, totaling \$2,768, to five other senior executive officers who are not Named Executive Officers.

Table of Contents**ITEM 6. EXHIBITS****Exhibit**

Number	Description
31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS*	XBRL Instance Document.
101.SCH*	XBRL Taxonomy Extension Schema Document.
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document.

* XBRL (Extensible Business Reporting Language) information is furnished and not filed or a part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, is deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, and otherwise is not subject to liability under these sections.

Table of Contents

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

CYPRESS SEMICONDUCTOR CORPORATION

Date: August 3, 2012

By: **/s/ BRAD W. BUSS**
Brad W. Buss
Executive Vice President, Finance and Administration
and Chief Financial Officer

Table of Contents**EXHIBIT INDEX**

Exhibit		Incorporated by References			Filed
		Form	Filing Date	File No.	Herewith
10.31	Credit and Guaranty Agreement - Revolving Credit Facility.	8-K	6/26/2012	001-10079	
10.32	Pledge and Security Agreement.	8-K	6/26/2012	001-10079	
31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.				X
31.2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.				X
32.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.				X
32.2	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.				X
101.INS*	XBRL Instance Document.				
101.SCH*	XBRL Taxonomy Extension Schema Document.				
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document.				
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document.				
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document.				
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document.				

* XBRL (Extensible Business Reporting Language) information is furnished and not filed or a part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, is deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, and otherwise is not subject to liability under these sections.
Furnished herewith.