

LAM RESEARCH CORP  
Form 10-Q  
November 03, 2010  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended September 26, 2010

or

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

For the transition period from            to

Commission file number 0-12933

**LAM RESEARCH CORPORATION**

(Exact name of registrant as specified in its charter)

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|   |  |
|---|--|
| <b>Delaware</b><br>(State or other jurisdiction of<br>incorporation or organization)        | <b>94-2634797</b><br>(I.R.S. Employer<br>Identification No.) |
| <b>4650 Cushing Parkway Fremont, California</b><br>(Address of principal executive offices) | <b>94538</b><br>(Zip Code)                                   |
| <b>(510) 572-0200</b><br>(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 (§ 232.405 of this chapter) 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 the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act:

|  |  |
|--|--|
| Large accelerated filer <input checked="" type="checkbox"/>                                  | Accelerated filer <input type="checkbox"/>         |
| Non-accelerated filer <input type="checkbox"/> (Do not check if a smaller reporting company) | Smaller reporting company <input type="checkbox"/> |

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

As of October 29, 2010, there were 122,978,708 shares of registrant's common stock outstanding.

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**LAM RESEARCH CORPORATION**

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**Table of Contents****PART I. FINANCIAL INFORMATION****ITEM 1. Financial Statements****LAM RESEARCH CORPORATION****CONSOLIDATED BALANCE SHEETS****(in thousands, except per share data)**

|   | <b>September 26,<br/>2010<br/>(unaudited)</b> | <b>June 27,<br/>2010<br/>(1)</b> |
|---|---|----------------------------------|
| <b>ASSETS</b>   |   |                                  |
| Cash and cash equivalents   | \$ 628,281                                    | \$ 545,767                       |
| Short-term investments  | 304,992                                       | 280,690                          |
| Accounts receivable, less allowance for doubtful accounts of \$10,223 as of September 26, 2010 and \$10,609 as of June 27, 2010   | 526,904                                       | 499,890                          |
| Inventories   | 338,335                                       | 318,479                          |
| Deferred income taxes   | 46,191  | 46,158                           |
| Prepaid expenses and other current assets   | 74,728  | 65,677                           |
| <b>Total current assets</b>   | <b>1,919,431</b>                              | <b>1,756,661</b>                 |
| Property and equipment, net   | 206,238                                       | 200,336                          |
| Restricted cash and investments   | 165,244                                       | 165,234                          |
| Deferred income taxes   | 26,968  | 26,218                           |
| Goodwill  | 169,182                                       | 169,182                          |
| Intangible assets, net  | 62,506  | 67,724                           |
| Other assets  | 102,727                                       | 102,037                          |
| <b>Total assets</b>   | <b>\$ 2,652,296</b>                           | <b>\$ 2,487,392</b>              |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>   |   |                                  |
| Trade accounts payable  | \$ 143,454                                    | \$ 121,099                       |
| Accrued expenses and other current liabilities  | 331,456                                       | 309,397                          |
| Deferred profit   | 132,261                                       | 123,194                          |
| Current portion of long-term debt and capital leases  | 5,226   | 4,967                            |
| <b>Total current liabilities</b>  | <b>612,397</b>                                | <b>558,657</b>                   |
| Long-term debt and capital leases   | 15,077  | 17,645                           |
| Income taxes payable  | 114,946                                       | 110,462                          |
| Other long-term liabilities   | 23,248  | 32,493                           |
| <b>Total liabilities</b>  | <b>765,668</b>                                | <b>719,257</b>                   |
| Commitments and contingencies   |   |                                  |
| Stockholders' equity:   |   |                                  |
| Preferred stock, at par value of \$0.001 per share; authorized 5,000 shares; none outstanding   |   |                                  |
| Common stock, at par value of \$0.001 per share; authorized 400,000 shares; issued and outstanding 122,869 shares at September 26, 2010 and 125,946 shares at June 27, 2010 | 123   | 126                              |
| Additional paid-in capital  | 1,472,760                                     | 1,452,939                        |

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|   |              |              |
|---|--------------|--------------|
| Treasury stock, at cost; 40,058 shares at September 26, 2010 and 36,884 shares at June 27, 2010 | (1,706,449)  | (1,581,417)  |
| Accumulated other comprehensive loss  | (39,866)     | (69,849)     |
| Retained earnings   | 2,160,060    | 1,966,336    |
| Total stockholders' equity  | 1,886,628    | 1,768,135    |
| Total liabilities and stockholders' equity  | \$ 2,652,296 | \$ 2,487,392 |

(1) Derived from audited financial statements

See Notes to Condensed Consolidated Financial Statements

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**LAM RESEARCH CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

(in thousands, except per share data)

(unaudited)

|  | Three Months Ended    |                       |
|--|-----------------------|-----------------------|
|  | September 26,<br>2010 | September 27,<br>2009 |
| Revenue  | \$ 805,874            | \$ 318,548            |
| Cost of goods sold                               | 428,548               | 187,233               |
| Cost of goods sold 409A expense                  |                       | (3,120)               |
| Total costs of goods sold                        | 428,548               | 184,113               |
| Gross margin                                     | 377,326               | 134,435               |
| Research and development                         | 86,353                | 71,199                |
| Selling, general and administrative              | 72,142                | 52,119                |
| Restructuring and asset impairments              | (5,163)               | 2,093                 |
| 409A expense                                     |                       | (20,228)              |
| Total operating expenses                         | 153,332               | 105,183               |
| Operating income                                 | 223,994               | 29,252                |
| Other expense, net                               | (979)                 | (368)                 |
| Income before income taxes                       | 223,015               | 28,884                |
| Income tax expense                               | 29,291                | 12,087                |
| Net income                                       | \$ 193,724            | \$ 16,797             |
| Net income per share:                            |                       |                       |
| Basic net income per share                       | \$ 1.57               | \$ 0.13               |
| Diluted net income per share                     | \$ 1.55               | \$ 0.13               |
| Number of shares used in per share calculations: |                       |                       |
| Basic  | 123,665               | 126,774               |
| Diluted  | 125,202               | 127,890               |

See Notes to Condensed Consolidated Financial Statements

**Table of Contents****LAM RESEARCH CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(in thousands)****(unaudited)**

|   | <b>Three Months Ended</b>     |                               |
|---|-------------------------------|-------------------------------|
|   | <b>September 26,<br/>2010</b> | <b>September 27,<br/>2009</b> |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>                                      |                               |                               |
| Net income  | \$ 193,724                    | \$ 16,797                     |
| Adjustments to reconcile net income to net cash provided by operating activities: |                               |                               |
| Depreciation and amortization   | 17,948                        | 17,681                        |
| Deferred income taxes   | (783)                         | 12,482                        |
| Restructuring charges   | (5,163)                       | 2,093                         |
| Equity-based compensation expense   | 13,009                        | 13,958                        |
| Income tax benefit on equity-based compensation plans                             | 5,083                         | (89)                          |
| Excess tax benefit on equity-based compensation plans                             | (3,939)                       | (368)                         |
| Other, net  | (1,964)                       | 1,159                         |
| Changes in operating assets and liabilities                                       | 37,829                        | (61,009)                      |
| Net cash provided by operating activities   | 255,744                       | 2,704                         |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>                                      |                               |                               |
| Capital expenditures and intangible assets  | (19,130)                      | (5,832)                       |
| Purchases of available-for-sale securities  | (50,958)                      | (29,638)                      |
| Sales and maturities of available-for-sale securities                             | 26,452                        | 19,863                        |
| Purchase of other investments   |                               | (961)                         |
| Transfer of restricted cash and investments                                       | (10)                          | (6,571)                       |
| Net cash used for investing activities  | (43,646)                      | (23,139)                      |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>                                      |                               |                               |
| Principal payments on long-term debt and capital lease obligations                | (3,333)                       | (1,915)                       |
| Net proceeds from issuance of long-term debt                                      |                               | 284                           |
| Excess tax benefit on equity-based compensation plans                             | 3,939                         | 368                           |
| Treasury stock purchases  | (144,795)                     | (2,356)                       |
| Reissuances of treasury stock   | 7,155                         | 5,761                         |
| Proceeds from issuance of common stock  | 835                           | 2,256                         |
| Net cash provided by (used for) financing activities                              | (136,199)                     | 4,398                         |
| Effect of exchange rate changes on cash   | 6,615                         | 3,033                         |
| Net increase (decrease) in cash and cash equivalents                              | 82,514                        | (13,004)                      |
| Cash and cash equivalents at beginning of period                                  | 545,767                       | 374,167                       |
| Cash and cash equivalents at end of period  | \$ 628,281                    | \$ 361,163                    |

See Notes to Condensed Consolidated Financial Statements





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**LAM RESEARCH CORPORATION**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**September 26, 2010**

**(Unaudited)**

**NOTE 1 BASIS OF PRESENTATION**

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ( GAAP ) for interim financial information and the instructions to Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation have been included. The accompanying unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements of Lam Research Corporation ( Lam Research or the Company ) for the fiscal year ended June 27, 2010, which are included in the Annual Report on Form 10-K as of and for the year ended June 27, 2010 (the 2010 Form 10-K ). The Company s Forms 10-K, Forms 10-Q and Forms 8-K are available online at the Securities and Exchange Commission website on the Internet. The address of that site is [www.sec.gov](http://www.sec.gov). The Company also posts its Forms 10-K, Forms 10-Q and Forms 8-K on its corporate website at <http://investor.lamresearch.com>.

The Company s reporting period is a 52/53-week fiscal year. The Company s current fiscal year will end June 26, 2011 and includes 52 weeks. The quarters ended September 26, 2010 (the September 2010 quarter ) and September 27, 2009 (the September 2009 quarter ) each included 13 weeks.

Certain amounts presented in the comparative financial statements for the prior year have been reclassified to conform to the fiscal year 2011 presentation.

**NOTE 2 RECENT ACCOUNTING PRONOUNCEMENTS**

In September 2009, the FASB ratified guidance from the Emerging Issues Task Force ( EITF ) regarding revenue arrangements with multiple deliverables. This guidance addresses criteria for separating the consideration in multiple-element arrangements and requires companies to allocate the overall consideration to each deliverable by using a best estimate of the selling price of individual deliverables in the arrangement in the absence of vendor-specific objective evidence or other third-party evidence of the selling price. The Company adopted this guidance on June 28, 2010, on a prospective basis, and the adoption did not have a significant impact on its results of operations or financial condition.

In September 2009, the FASB also ratified guidance from the EITF regarding certain revenue arrangements that include software elements. This guidance modifies the scope of the software revenue recognition rules to exclude (a) non-software components of tangible products and (b) software components of tangible products that are sold, licensed, or leased with tangible products when the software components and non-software components of the tangible product function together to deliver the tangible product s essential functionality. The Company adopted this guidance on June 28, 2010, on a prospective basis, and the adoption did not have a significant impact on its results of operations or financial condition.

**NOTE 3 EQUITY-BASED COMPENSATION PLANS**

The Company has adopted stock plans that provide for grants of equity-based awards to eligible participants, including stock options and restricted stock units, of Lam Research common stock ( Common Stock ). The Company also has an employee stock purchase plan ( ESPP ) that allows employees to purchase its Common Stock at a discount through payroll deductions.

The Company recognized the following equity-based compensation expense and related income tax benefit in the consolidated statements of operations:

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|   | Three Months Ended    |                       |
|---|-----------------------|-----------------------|
|   | September 26,<br>2010 | September 27,<br>2009 |
|   | (in millions)         |                       |
| Equity-based compensation expense                               | \$ 13.0               | \$ 14.0               |
| Income tax benefit related to equity-based compensation expense | \$ 2.2                | \$ 1.5                |

The estimated fair value of the Company's stock-based awards, less expected forfeitures, is amortized over the awards' vesting periods on a straight-line basis.

***Stock Options and Restricted Stock Units***

The 2007 Stock Incentive Plan provides for grants of equity-based awards to eligible participants. Additional shares are reserved for issuance under the Company's 1997 Stock Incentive Plan and its 1999 Stock Option Plan pursuant to awards previously granted under those plans (together with the 2007 Stock Incentive Plan, the Plans). As of September 26, 2010, there were a total of 3,581,018 shares reserved to cover options and restricted stock units issued and outstanding under the Plans. As of September 26, 2010, there were an additional 9,477,009 shares reserved and available for future equity-based awards under the 2007 Stock Incentive Plan.

**Table of Contents****LAM RESEARCH CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****September 26, 2010****(Unaudited)**

A summary of stock option activity under the Plans as of September 26, 2010 and changes during the three months then ended is presented below:

| <b>Options</b>                    | <b>Shares<br/>(in<br/>thousands)</b> | <b>Weighted-<br/>Average<br/>Exercise<br/>Price</b> | <b>Weighted-Average<br/>Remaining<br/>Contractual<br/>Term<br/>(years)</b> | <b>Aggregate Intrinsic<br/>Value as of<br/>September 26, 2010<br/>(in thousands)</b> |
|-----------------------------------|--------------------------------------|---|--|--|
| Outstanding at June 27, 2010      | 885                                  | \$ 21.61  | 2.76   |  |
| Exercised                         | (38)                                 | \$ 22.08  |  |  |
| Forfeited or expired              | (2)                                  | \$ 23.86  |  |  |
| Outstanding at September 26, 2010 | 845                                  | \$ 21.59  | 2.60   | \$ 16,876  |
| Exercisable at September 26, 2010 | 369                                  | \$ 23.36  | 1.55   | \$ 6,716   |

The total intrinsic value of options exercised during the three months ended September 26, 2010 and September 27, 2009 was \$0.7 million and \$2.2 million respectively.

As of September 26, 2010, there was approximately \$0.8 million of total unrecognized compensation expense related to unvested stock options granted and outstanding; that expense is expected to be recognized over a remaining period of 0.4 years.

A summary of the Company's restricted stock units as of September 26, 2010 and changes during the three months then ended is presented below:

| <b>Unvested Restricted Stock Units</b> | <b>Shares<br/>(in<br/>thousands)</b> | <b>Average Grant-<br/>Date Fair Value</b> |
|--|--------------------------------------|---|
| Unvested at June 27, 2010              | 2,741                                | \$ 30.50                                  |
| Granted                                | 62                                   | \$ 39.19                                  |
| Vested                                 | (53)                                 | \$ 36.08                                  |
| Forfeited                              | (14)                                 | \$ 30.69                                  |
| Unvested as of September 26, 2010      | 2,736                                | \$ 30.59                                  |

The fair value of the Company's restricted stock units was calculated based upon the fair market value of the Company's stock at the date of grant. As of September 26, 2010, there was \$51.6 million of total unrecognized compensation expense related to unvested restricted stock units granted; that expense is expected to be recognized over a weighted average remaining period of 1.5 years.

***ESPP***

The 1999 Employee Stock Purchase Plan (as amended and restated, the 1999 ESPP ) allows employees to designate a portion of their base compensation to be withheld through payroll deductions and used to purchase the Company's Common Stock at a purchase price per share equal to the lower of 85% of the fair market value of the Company's Common Stock on the first or last day of the applicable purchase period. Each offering period generally lasts up to 12 months and includes up to three interim purchase dates. As of September 26, 2010, there were a total of 8,265,932 shares available for issuance under the 1999 ESPP.

**Table of Contents****LAM RESEARCH CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****September 26, 2010****(Unaudited)**

Purchase rights under the 1999 ESPP were valued using the Black-Scholes model assuming no expected dividends and the following weighted-average assumptions for the three months ended September 26, 2010:

|                                 | <b>Three Months Ended<br/>September 26,<br/>2010</b> |
|---------------------------------|--|
| Expected term (years)           | 0.68   |
| Expected stock price volatility | 41.94%   |
| Risk-free interest rate         | 0.61%  |

As of September 26, 2010, there was \$7.1 million of unrecognized compensation expense related to the 1999 ESPP which is expected to be recognized over the next 0.9 years.

**NOTE 4 FINANCIAL INSTRUMENTS**

The Company maintains an investment portfolio of various holdings, types, and maturities. The Company's mutual funds are classified as trading securities. Investments classified as trading securities are recorded at fair value based upon quoted market prices. Any material differences between the cost and fair value of trading securities is recognized as Other income (expense) in the Consolidated Statement of Operations. All of the Company's other short-term investments are classified as available-for-sale and consequently are recorded in the Consolidated Balance Sheets at fair value with unrealized gains or losses reported as a separate component of accumulated other comprehensive income, net of tax.

***Fair Value***

Pursuant to the accounting guidance for fair value measurement, the Company defines fair value as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities required or permitted to be recorded at fair value, the Company considers the principal or most advantageous market in which it would transact, and it considers assumptions that market participants would use when pricing the asset or liability.

The FASB has established a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. An asset or liability's level in the hierarchy is based on the lowest level of input that is significant to the fair value measurement. Assets and liabilities carried at fair value are classified and disclosed in one of the following three categories:

Level 1: Valuations based on quoted prices in active markets for identical assets or liabilities with sufficient volume and frequency of transactions.

Level 2: Valuations based on observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or model-derived valuations techniques for which all significant inputs are observable in the market or can be corroborated by, observable market data for substantially the full term of the assets or liabilities.

Level 3: Valuations based on unobservable inputs to the valuation methodology that are significant to the measurement of fair value of assets or liabilities and based on non-binding, broker-provided price quotes and may not have been corroborated by observable market data.



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## LAM RESEARCH CORPORATION

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

September 26, 2010

(Unaudited)

The following table sets forth the Company's financial assets and liabilities measured at fair value on a recurring basis as of September 26, 2010:

|  | Total               | Fair Value Measurement at September 26, 2010                               |   |  |
|--|---------------------|--|---|--|
|  |                     | Quoted Prices in<br>Active Markets for<br>Identical<br>Assets<br>(Level 1) | Significant Other<br>Observable Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |
| (In thousands)                         |                     |  |   |  |
| <b>Assets</b>                          |                     |  |   |  |
| <b>Fixed Income</b>                    |                     |  |   |  |
| Money Market Funds                     | \$ 534,179          | \$ 534,179   | \$  | \$   |
| Municipal Notes and Bonds              | 103,805             |  | 103,805   |  |
| US Treasury & Agencies                 | 53                  | 53   |   |  |
| Government-Sponsored Enterprises       | 9,274               |  | 9,274   |  |
| Foreign Government Bond                | 1,004               |  | 1,004   |  |
| Corporate Notes and Bonds              | 311,802             | 168,854  | 142,948   |  |
| Mortgage Backed Securities Residential | 5,156               |  | 5,156   |  |
| Mortgage Backed Securities Commercial  | 42,752              |  | 42,752  |  |
| <b>Total Fixed Income</b>              | <b>\$ 1,008,025</b> | <b>\$ 703,086</b>  | <b>\$ 304,939</b>                                   | <b>\$</b>  |
| <b>Equities</b>                        | 6,369               | 6,369  |   |  |
| <b>Mutual Funds</b>                    | 18,441              | 18,441   |   |  |
| <b>Derivatives Assets</b>              | 78                  |  | 78  |  |
| <b>Total</b>                           | <b>\$ 1,032,913</b> | <b>\$ 727,896</b>  | <b>\$ 305,017</b>                                   | <b>\$</b>  |
| <b>Liabilities</b>                     |                     |  |   |  |
| Derivative Liabilities                 | \$ 1,969            | \$   | \$ 1,969  | \$   |

The amounts in the table above are reported in the consolidated balance sheet as of September 26, 2010 as follows:

|   | Total      | (Level 1)  | (Level 2) | (Level 3) |
|---|------------|------------|-----------|-----------|
| (In thousands)                            |            |            |           |           |
| <b>Reported As:</b>                       |            |            |           |           |
| Cash Equivalents                          | \$ 538,148 | \$ 538,148 | \$        | \$        |
| Short-Term Investments                    | 304,992    | 53         | 304,939   |           |
| Restricted Cash and Investments           | 164,885    | 164,885    |           |           |
| Prepaid Expenses and Other Current Assets | 78         |            | 78        |           |
| Other Assets                              | 24,810     | 24,810     |           |           |

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|  |                     |                   |                   |           |
|--|---------------------|-------------------|-------------------|-----------|
|  | <b>\$ 1,032,913</b> | <b>\$ 727,896</b> | <b>\$ 305,017</b> | <b>\$</b> |
| Accrued Expenses and Other Current Liabilities | \$ 1,969            | \$                | \$ 1,969          | \$        |



**Table of Contents****LAM RESEARCH CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

September 26, 2010

(Unaudited)

The following table sets forth the Company's financial assets and liabilities measured at fair value on a recurring basis as of June 27, 2010.

|  | Total             | Fair Value Measurement at June 27, 2010                                    |   |  |
|--|-------------------|--|---|--|
|  |                   | Quoted Prices in<br>Active Markets for<br>Identical<br>Assets<br>(Level 1) | Significant Other<br>Observable Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |
| (In thousands)                         |                   |  |   |  |
| <b>Assets</b>                          |                   |  |   |  |
| <b>Fixed Income</b>                    |                   |  |   |  |
| Money Market Funds                     | \$ 470,936        | \$ 470,936   | \$  | \$   |
| Municipal Notes and Bonds              | 103,903           |  | 103,903   |  |
| US Treasury & Agencies                 | 3,447             |  | 3,447   |  |
| Government-Sponsored Enterprises       | 6,060             | 6,060  |   |  |
| Foreign Government Bond                | 1,008             |  | 1,008   |  |
| Corporate Notes and Bonds              | 289,437           | 169,723  | 119,636   | 78   |
| Mortgage Backed Securities Residential | 6,106             |  | 6,106   |  |
| Mortgage Backed Securities Commercial  | 42,964            |  | 42,964  |  |
| <b>Total Fixed Income</b>              | <b>\$ 923,861</b> | <b>\$ 646,719</b>  | <b>\$ 277,064</b>                                   | <b>\$ 78</b>                                       |
| <b>Equities</b>                        | 7,636             | 7,636  |   |  |
| <b>Mutual Funds</b>                    | 18,124            | 18,124   |   |  |
| <b>Derivatives Assets</b>              | 2,063             |  | 2,063   |  |
| <b>Total</b>                           | <b>\$ 951,684</b> | <b>\$ 672,479</b>  | <b>\$ 279,127</b>                                   | <b>\$ 78</b>                                       |
| <b>Liabilities</b>                     |                   |  |   |  |
| Derivative Liabilities                 | \$ 470            | \$   | \$ 470  | \$   |

The amounts in the table above are reported in the consolidated balance sheet as of June 27, 2010 as follows:

|   | Total      | (Level 1)  | (Level 2) | (Level 3) |
|---|------------|------------|-----------|-----------|
| (In thousands)                            |            |            |           |           |
| <b>Reported As:</b>                       |            |            |           |           |
| Cash Equivalents                          | \$ 478,286 | \$ 477,279 | \$ 1,007  | \$        |
| Short-Term Investments                    | 280,690    | 4,555      | 276,057   | 78        |
| Restricted Cash and Investments           | 164,885    | 164,885    |           |           |
| Prepaid Expenses and Other Current Assets | 2,063      |            | 2,063     |           |

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|  |                   |                   |                   |              |
|--|-------------------|-------------------|-------------------|--------------|
| Other Assets                                   | 25,760            | 25,760            |                   |              |
|  | <b>\$ 951,684</b> | <b>\$ 672,479</b> | <b>\$ 279,127</b> | <b>\$ 78</b> |
| Accrued Expenses and Other Current Liabilities | \$ 470            | \$                | \$ 470            | \$           |

**Table of Contents****LAM RESEARCH CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****September 26, 2010****(Unaudited)****Investments**

The following tables summarize the Company's investments (in thousands):

|  | <b>September 26, 2010</b> |                            |                              |                     | <b>June 27, 2010</b> |                            |                              |                     |
|--|---------------------------|----------------------------|------------------------------|---------------------|----------------------|----------------------------|------------------------------|---------------------|
|  | <b>Cost</b>               | <b>Unrealized<br/>Gain</b> | <b>Unrealized<br/>(Loss)</b> | <b>Fair Value</b>   | <b>Cost</b>          | <b>Unrealized<br/>Gain</b> | <b>Unrealized<br/>(Loss)</b> | <b>Fair Value</b>   |
| Cash   | \$ 90,492                 | \$                         | \$                           | \$ 90,492           | \$ 67,830            | \$                         | \$                           | \$ 67,830           |
| Fixed Income Money Market Funds                  | 534,179                   |                            |                              | 534,179             | 470,936              |                            |                              | 470,936             |
| Municipal Notes and Bonds                        | 101,946                   | 1,889                      | (30)                         | 103,805             | 102,130              | 1,784                      | (11)                         | 103,903             |
| US Treasury & Agencies                           | 52                        | 1                          |                              | 53                  | 3,437                | 10                         |                              | 3,447               |
| Government-Sponsored Enterprises                 | 9,144                     | 130                        |                              | 9,274               | 5,976                | 84                         |                              | 6,060               |
| Foreign Government Bond                          | 1,006                     |                            | (2)                          | 1,004               | 1,007                | 1                          |                              | 1,008               |
| Corporate Notes and Bonds                        | 309,594                   | 2,219                      | (11)                         | 311,802             | 287,922              | 1,608                      | (93)                         | 289,437             |
| Mortgage Backed Securities                       |                           |                            |                              |                     |                      |                            |                              |                     |
| Residential                                      | 4,900                     | 286                        | (30)                         | 5,156               | 5,825                | 323                        | (42)                         | 6,106               |
| Mortgage Backed Securities                       |                           |                            |                              |                     |                      |                            |                              |                     |
| Commercial                                       | 42,407                    | 391                        | (46)                         | 42,752              | 42,765               | 275                        | (76)                         | 42,964              |
| <b>Total Cash and Short-Term<br/>Investments</b> | <b>\$ 1,093,720</b>       | <b>\$ 4,916</b>            | <b>\$ (119)</b>              | <b>\$ 1,098,517</b> | <b>\$ 987,828</b>    | <b>\$ 4,085</b>            | <b>\$ (222)</b>              | <b>\$ 991,691</b>   |
| Publicly Traded Equity Securities                | \$ 9,471                  | \$                         | \$ (3,102)                   | \$ 6,369            | \$ 9,471             | \$                         | \$ (1,835)                   | \$ 7,636            |
| Mutual Funds                                     | 18,530                    | 404                        | (493)                        | 18,441              | 19,043               |                            | (919)                        | 18,124              |
| <b>Total Financial Instruments</b>               | <b>\$ 1,121,721</b>       | <b>\$ 5,320</b>            | <b>\$ (3,714)</b>            | <b>\$ 1,123,327</b> | <b>\$ 1,016,342</b>  | <b>\$ 4,085</b>            | <b>\$ (2,976)</b>            | <b>\$ 1,017,451</b> |
| <b>As Reported</b>                               |                           |                            |                              |                     |                      |                            |                              |                     |
| Cash and Cash Equivalents                        | \$ 628,281                | \$                         | \$                           | \$ 628,281          | \$ 545,766           | \$ 1                       | \$                           | \$ 545,767          |
| Short-Term Investments                           | 300,195                   | 4,916                      | (119)                        | 304,992             | 276,828              | 4,084                      | (222)                        | 280,690             |
| Restricted Cash and Investments                  | 165,244                   |                            |                              | 165,244             | 165,234              |                            |                              | 165,234             |
| Other Assets                                     | 28,001                    | 404                        | (3,595)                      | 24,810              | 28,514               |                            | (2,754)                      | 25,760              |
| <b>Total</b>                                     | <b>\$ 1,121,721</b>       | <b>\$ 5,320</b>            | <b>\$ (3,714)</b>            | <b>\$ 1,123,327</b> | <b>\$ 1,016,342</b>  | <b>\$ 4,085</b>            | <b>\$ (2,976)</b>            | <b>\$ 1,017,451</b> |

The Company accounts for its investment portfolio at fair value. Realized gains (losses) for investments sold are specifically identified. Management assesses the fair value of investments in debt securities that are not actively traded through consideration of interest rates and their impact on the present value of the cash flows to be received from the investments. The Company also considers whether changes in the credit ratings of the issuer could impact the assessment of fair value. The Company did not recognize any realized losses on investments due to other-than-temporary impairment charges during the three months ended September 26, 2010 and September 27, 2009. The Company realized losses from sales of investments of less than \$0.1 million in each of the three months ended September 26, 2010 and September 27, 2009.

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The following is an analysis of the Company's fixed income securities in unrealized loss positions as of September 26, 2010 (in thousands):

|  | UNREALIZED LOSSES<br>LESS THAN 12 MONTHS |                    | September 26, 2010<br>UNREALIZED LOSSES<br>12 MONTHS OR GREATER |                    | TOTAL            |                    |
|--|--|--------------------|---|--------------------|------------------|--------------------|
|  | Gross                                    |                    | Gross   |                    | Gross            |                    |
|  | Fair<br>Value                            | Unrealized<br>Loss | Fair<br>Value   | Unrealized<br>Loss | Fair<br>Value    | Unrealized<br>Loss |
| <b>Fixed Income Securities</b>         |  |                    |   |                    |                  |                    |
| Municipal Notes and Bonds              | \$ 6,087                                 | \$ (30)            | \$  | \$                 | \$ 6,087         | \$ (30)            |
| Foreign Government Bond                | 1,004                                    | (2)                |   |                    | 1,004            | (2)                |
| Corporate Notes and Bonds              | 9,380                                    | (11)               |   |                    | 9,380            | (11)               |
| Mortgage Backed Securities Residential |  |                    | 372   | (30)               | 372              | (30)               |
| Mortgage Backed Securities Commercial  | 10,906                                   | (46)               |   |                    | 10,906           | (46)               |
| <b>Total Fixed Income</b>              | <b>\$ 27,377</b>                         | <b>\$ (89)</b>     | <b>\$ 372</b>   | <b>\$ (30)</b>     | <b>\$ 27,749</b> | <b>\$ (119)</b>    |

**Table of Contents****LAM RESEARCH CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****September 26, 2010****(Unaudited)**

The amortized cost and fair value of cash equivalents, short-term investments, and restricted cash and investments with contractual maturities are as follows:

|                           | <b>September 26, 2010</b> |                                 | <b>June 27, 2010</b> |                                     |
|---------------------------|---------------------------|---------------------------------|----------------------|-------------------------------------|
|                           | <b>Cost</b>               | <b>Estimated<br/>Fair Value</b> | <b>Cost</b>          | <b>Estimated<br/>Fair<br/>Value</b> |
|                           | <b>(in thousands)</b>     |                                 |                      |                                     |
| Due in less than one year | \$ 791,031                | \$ 791,621                      | \$ 723,143           | \$ 723,707                          |
| Due in more than one year | 212,198                   | 216,404                         | 196,855              | 200,154                             |
|                           | \$ 1,003,229              | \$ 1,008,025                    | \$ 919,998           | \$ 923,861                          |

Management has the ability, if necessary, to liquidate any of its investments in order to meet the Company's liquidity needs in the next 12 months. Accordingly, those investments with contractual maturities greater than one year from the date of purchase nonetheless are classified as short-term on the accompanying consolidated balance sheets.

***Derivative Instruments and Hedging***

The Company carries derivative financial instruments ( derivatives ) on its consolidated balance sheets at their fair values. The Company enters into foreign exchange forward contracts with financial institutions with the primary objective of reducing volatility of earnings and cash flows related to foreign currency exchange rate fluctuations. The counterparties to these foreign exchange forward contracts are creditworthy multinational financial institutions; therefore, we do not consider the risk of counterparty nonperformance to be material.

***Cash Flow Hedges***

The Company's policy is to attempt to minimize short-term business exposure to foreign currency exchange rate fluctuations using an effective and efficient method to eliminate or reduce such exposures. In the normal course of business, the Company's financial position is routinely subjected to market risk associated with foreign currency exchange rate fluctuations. To protect against a reduction in value of forecasted Japanese yen-denominated revenues and forecasted Euro denominated operating expenses, the Company has instituted a foreign currency cash flow hedging program. The Company enters into foreign exchange forward contracts that generally expire within 12 months and no later than 24 months. These foreign exchange forward contracts are designated as cash flow hedges and are carried on the Company's balance sheet at fair value with the effective portion of the contracts' gains or losses included in accumulated other comprehensive income (loss) and subsequently recognized in revenue in the same period the hedged revenue is recognized.

At inception and at each quarter end, hedges are tested for effectiveness using regression testing. Changes in the fair value of foreign exchange forward contracts due to changes in time value are excluded from the assessment of effectiveness and are recognized in revenue and operating expenses in the current period. The change in forward time value was not material for all reported periods. There were no gains or losses during either the three months ended September 26, 2010 or September 27, 2009 associated with ineffectiveness or forecasted transactions that failed to occur. To qualify for hedge accounting, the hedge relationship must meet criteria relating both to the derivative instrument and the hedged item. These criteria include identification of the hedging instrument, the hedged item, the nature of the risk being hedged and how the hedging

instrument's effectiveness in offsetting the exposure to changes in the hedged item's fair value or cash flows will be measured.

To receive hedge accounting treatment, all hedging relationships are formally documented at the inception of the hedge, and the hedges must be highly effective in offsetting changes to future cash flows on hedged transactions. When derivative instruments are designated and qualify as effective cash flow hedges, the Company is able to defer effective changes in the fair value of the hedging instrument within accumulated other comprehensive income (loss) until the hedged exposure is realized. Consequently, with the exception of excluded time value and hedge ineffectiveness recognized, the Company's results of operations are not subject to fluctuation as a result of changes in the fair value of the derivative instruments. If hedges are not highly effective or if the Company does not believe that the underlying hedged forecasted transactions will occur, the Company may not be able to account for its derivative instruments as cash flow hedges. If this were to occur, future changes in the fair values of the Company's derivative instruments would be recognized in earnings without the benefits of offsets or deferrals of changes in fair value arising from hedge accounting treatment. At September 26, 2010, the Company expects to reclassify the entire amount associated with the \$1.4 million of losses accumulated in other comprehensive income to earnings during the next 12 months due to the recognition in earnings of the hedged forecasted transactions.

***Balance Sheet Hedges***

The Company also enters into foreign exchange forward contracts to hedge the effects of foreign currency fluctuations associated with foreign currency denominated assets and liabilities, primarily intercompany receivables and payables. These foreign exchange forward contracts are not designated for hedge accounting treatment. Therefore, the change in fair value of these derivatives is recorded as a component of other income (expense) and offsets the change in fair value of the foreign currency denominated assets and liabilities, recorded in other income (expense).

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## LAM RESEARCH CORPORATION

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

September 26, 2010

(Unaudited)

As of September 26, 2010, the Company had the following outstanding foreign currency forward contracts that were entered into to hedge forecasted revenues and purchases:

|   | Derivatives Designated<br>as<br>Hedging<br>Instruments: | Derivatives Not Designated<br>as<br>Hedging Instruments:<br>(in thousands) |
|---|---|--|
| <b>Foreign Currency Forward Contracts</b> |   |  |
| Sell JPY                                  | \$ 38,439   | \$   |
| Sell JPY                                  |   | 109,775  |
| Buy CHF                                   |   | 209,204  |
| Buy TWD                                   |   | 69,427   |
| Buy EUR                                   | 9,017   |  |
| Buy EUR                                   |   | 42,913   |
|   | \$ 47,456   | \$ 431,319   |

The fair value of derivatives instruments in the Company's condensed consolidated balance sheets as of September 26, 2010 was as follows:

|   | Fair Value of Derivative Instruments |              |  |                   |
|---|--------------------------------------|--------------|--|-------------------|
|   | Asset Derivatives<br>Balance Sheet   |              | Liability Derivatives<br>Balance Sheet |                   |
|   | Location                             | Fair Value   | Location                               | Fair Value        |
| (in thousands)  |                                      |              |  |                   |
| <b>Derivatives designated as hedging instruments:</b>     |                                      |              |  |                   |
| Foreign exchange forward contracts                        | Prepaid expense and other assets     | \$ 68        | Accrued liabilities                    | (\$ 1,517)        |
| <b>Derivatives not designated as hedging instruments:</b> |                                      |              |  |                   |
| Foreign exchange forward contracts                        | Prepaid expense and other assets     | \$ 10        | Accrued liabilities                    | (\$ 452)          |
| <b>Total derivatives</b>                                  |                                      | <b>\$ 78</b> |  | <b>(\$ 1,969)</b> |

The fair value of derivatives instruments in the Company's condensed consolidated balance sheets as of June 27, 2010 was as follows:

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| Fair Value of Derivative Instruments                      |                                  |                 |                       |                 |
|---|----------------------------------|-----------------|-----------------------|-----------------|
| Asset Derivatives   |                                  |                 | Liability Derivatives |                 |
| Balance Sheet   | Fair Value                       |                 | Balance Sheet         | Fair Value      |
| Location  | (in thousands)                   |                 | Location              | (in thousands)  |
| <b>Derivatives designated as hedging instruments:</b>     |                                  |                 |                       |                 |
| Foreign exchange forward contracts                        | Prepaid expense and other assets | \$ 30           | Accrued liabilities   | (\$ 52)         |
| <b>Derivatives not designated as hedging instruments:</b> |                                  |                 |                       |                 |
| Foreign exchange forward contracts                        | Prepaid expense and other assets | \$ 2,033        | Accrued liabilities   | (\$ 418)        |
| <b>Total derivatives</b>                                  |                                  | <b>\$ 2,063</b> |                       | <b>(\$ 470)</b> |



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## LAM RESEARCH CORPORATION

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

September 26, 2010

(Unaudited)

The effect of derivative instruments designated as cash flow hedges on the Company's condensed consolidated statements of operations for the three months ended September 26, 2010 and September 27, 2009 were as follows:

|   | Three Months Ended September 26, 2010                      |   |  | Gain (Loss)<br>Recognized<br>(Excluded<br>from<br>Effectiveness<br>Testing) (4) |
|---|--|---|--|---|
|   | Gain (Loss)<br>Recognized<br>(Effective<br>Portion)<br>(1) | Gain (Loss)<br>Recognized<br>(Effective<br>Portion) (2) | Gain (Loss)<br>Recognized<br>(Ineffective<br>Portion)<br>(3) |   |
|   | (in thousands)   |   |  |   |
| <b>Derivatives Designated as Hedging Instruments:</b> |  |   |  |   |
| Foreign exchange forward contracts                    | \$ (5,094)   | \$ (3,610)  | \$   | \$ 114  |
|   | Three Months Ended September 27, 2009                      |   |  | Gain (Loss)<br>Recognized<br>(Excluded<br>from<br>Effectiveness<br>Testing) (4) |
|   | Gain (Loss)<br>Recognized<br>(Effective<br>Portion)<br>(1) | Gain (Loss)<br>Recognized<br>(Effective<br>Portion) (2) | Gain (Loss)<br>Recognized<br>(Ineffective<br>Portion)<br>(3) |   |
|   | (in thousands)   |   |  |   |
| <b>Derivatives Designated as Hedging Instruments:</b> |  |   |  |   |
| Foreign exchange forward contracts                    | \$ (707)   | \$ 5  | \$   | \$ 36   |

- (1) Amount recognized in other comprehensive income (effective portion).
- (2) Amount of gain (loss) reclassified from accumulated other comprehensive income into income (effective portion) located in revenue and operating expenses.
- (3) Amount of gain (loss) recognized in income on derivative (ineffective portion) located in other income (expense), net.
- (4) Amount of gain (loss) recognized in income on derivative (amount excluded from effectiveness testing) located in other income (expense), net.

The effect of derivative instruments not designated as cash flow hedges on the Company's condensed consolidated statement of operations for the three months ended September 26, 2010 and September 27, 2009 were as follows:

|   | Three Months Ended                  |                               |
|---|-------------------------------------|-------------------------------|
|   | September 26, 2010                  | September 27, 2009            |
|   | Gain<br>(Loss)<br>Recognized<br>(5) | Gain (Loss)<br>Recognized (5) |
|   | (in thousands)                      |                               |
| <b>Derivatives Not Designated as Hedging Instruments:</b> |                                     |                               |
| Foreign exchange forward contracts                        | \$ 8,380                            | \$ 7,253                      |

(5) Amount of gain (loss) recognized in income located in other income (expense), net.

***Concentrations of Credit Risk***

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash equivalents, short term investments, restricted cash and investments, trade accounts receivable, and derivative financial instruments used in hedging activities. Cash is placed on deposit in major financial institutions in various countries throughout the world. Such deposits may be in excess of insured limits. Management believes that the financial institutions that hold the Company's cash are financially sound and, accordingly, minimal credit risk exists with respect to these balances.

The Company's available-for-sale securities, which are invested in taxable financial instruments, must have a minimum rating of A2 / A at the time of original purchase, as rated by two of the following three rating agencies: Moody's, Standard & Poor's (S&P), or Fitch. Available-for-sale securities that are invested in tax-exempt financial instruments must have a minimum rating of A2 / A, as rated by any one of the same three rating agencies. The Company's policy limits the amount of credit exposure with any one financial institution or commercial issuer.

The Company is exposed to credit losses in the event of nonperformance by counterparties on the foreign currency forward contracts that are used to mitigate the effect of exchange rate changes. These counterparties are large international financial institutions and to date, no such counterparty has failed to meet its financial obligations to the Company.

**Table of Contents****LAM RESEARCH CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****September 26, 2010****(Unaudited)**

Credit risk evaluations, including trade references, bank references and Dun & Bradstreet ratings, are performed on all new customers and the Company monitors its customers' financial statements and payment performance. In general, the Company does not require collateral on sales.

**NOTE 5 INVENTORIES**

Inventories are stated at the lower of cost (first-in, first-out method) or market. Shipments to Japanese customers, to whom title does not transfer until customer acceptance, are classified as inventory and carried at cost until title transfers. Inventories consist of the following:

|                 | <b>September 26,<br/>2010</b> | <b>June 27,<br/>2010</b> |
|-----------------|-------------------------------|--------------------------|
|                 | <b>(in thousands)</b>         |                          |
| Raw materials   | \$ 164,759                    | \$ 159,574               |
| Work-in-process | 77,527                        | 67,114                   |
| Finished goods  | 96,049                        | 91,791                   |
|                 | \$ 338,335                    | \$ 318,479               |

**NOTE 6 PROPERTY AND EQUIPMENT, NET**

Property and equipment, net, consists of the following:

|   | <b>September 26,<br/>2010</b> | <b>June 27,<br/>2010</b> |
|---|-------------------------------|--------------------------|
|   | <b>(in thousands)</b>         |                          |
| Manufacturing, engineering and office equipment | \$ 269,194                    | \$ 253,925               |
| Computer equipment and software                 | 81,246                        | 77,249                   |
| Land  | 15,574                        | 15,574                   |
| Buildings                                       | 61,233                        | 61,145                   |
| Leasehold improvements                          | 50,310                        | 55,300                   |
| Furniture and fixtures                          | 14,226                        | 14,095                   |
|   | 491,783                       | 477,288                  |
| Less: accumulated depreciation and amortization | (285,545)                     | (276,952)                |
|   | \$ 206,238                    | \$ 200,336               |

**NOTE 7 GOODWILL AND INTANGIBLE ASSETS**

**Goodwill**

The balance of goodwill was \$169.2 million as of September 26, 2010 and June 27, 2010. Goodwill attributable to the SEZ acquisition of approximately \$104 million is not tax deductible due to applicable foreign law. The remaining goodwill balance of approximately \$65 million is tax deductible.

**Intangible Assets**

The following table provides details of the Company's intangible assets subject to amortization as of September 26, 2010 (in thousands, except years):

|                         | Gross      | Accumulated Amortization | Net       | Weighted-Average Useful Life (years) |
|-------------------------|------------|--------------------------|-----------|--------------------------------------|
| Customer relationships  | \$ 35,226  | \$ (19,751)              | \$ 15,475 | 6.90                                 |
| Existing technology     | 61,941     | (29,138)                 | 32,803    | 6.68                                 |
| Other intangible assets | 35,216     | (29,687)                 | 5,529     | 4.10                                 |
| Patents                 | 20,670     | (11,971)                 | 8,699     | 6.11                                 |
|                         | \$ 153,053 | \$ (90,547)              | \$ 62,506 | 6.06                                 |

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## LAM RESEARCH CORPORATION

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

September 26, 2010

(Unaudited)

The following table provides details of the Company's intangible assets subject to amortization as of June 27, 2010 (in thousands, except years):

|                         | Gross      | Accumulated<br>Amortization | Net       | Weighted-<br>Average<br>Useful Life<br>(years) |
|-------------------------|------------|-----------------------------|-----------|--|
| Customer relationships  | \$ 35,226  | \$ (18,512)                 | \$ 16,714 | 6.90   |
| Existing technology     | 61,598     | (27,084)                    | 34,514    | 6.70   |
| Other intangible assets | 35,216     | (27,783)                    | 7,433     | 4.10   |
| Patents                 | 20,270     | (11,207)                    | 9,063     | 6.13   |
|                         | \$ 152,310 | \$ (84,586)                 | \$ 67,724 | 6.07   |

The Company recognized \$6.0 million and \$5.9 million in intangible asset amortization expense during the three months ended September 26, 2010 and September 27, 2009, respectively.

The estimated future amortization expense of purchased intangible assets as of September 26, 2010 is as follows (in thousands):

| Fiscal Year     | Amount    |
|-----------------|-----------|
| 2011 (9 months) | 15,084    |
| 2012            | 17,997    |
| 2013            | 16,350    |
| 2014            | 10,377    |
| 2015            | 2,154     |
| Thereafter      | 544       |
|                 | \$ 62,506 |

**NOTE 8 ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES**

Accrued expenses and other current liabilities consist of the following:

|                      | September 26,<br>2010 | June 27,<br>2010 |
|----------------------|-----------------------|------------------|
|                      | (in thousands)        |                  |
| Accrued compensation | \$ 173,807            | \$ 164,579       |

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|                                |            |            |
|--------------------------------|------------|------------|
| Warranty reserves              | 35,612     | 31,756     |
| Income and other taxes payable | 60,783     | 54,874     |
| Other                          | 61,254     | 58,188     |
|                                | \$ 331,456 | \$ 309,397 |

**NOTE 9 OTHER INCOME (EXPENSE), NET**

The significant components of other income (expense), net, are as follows:

|                                 | Three Months Ended    |                       |
|---------------------------------|-----------------------|-----------------------|
|                                 | September 26,<br>2010 | September 27,<br>2009 |
|                                 | (in thousands)        |                       |
| Interest income                 | \$ 3,076              | \$ 2,048              |
| Interest expense                | (101)                 | (189)                 |
| Foreign exchange gains (losses) | (3,179)               | (1,794)               |
| Other, net                      | (775)                 | (433)                 |
|                                 | \$ (979)              | \$ (368)              |

**NOTE 10 INCOME TAX EXPENSE**

The Company's effective tax rate for the quarter ended September 26, 2010 is approximately 13.1%. The difference between the U.S. federal statutory tax rate of 35% and the Company's effective tax rate is primarily due to the geographical mix of income partially offset by the tax effect of non-deductible stock-based compensation. The effective tax rate recorded during the quarter includes the tax impact of discrete items, which are recorded during the quarter in which they occur. During the September 2010 quarter, discrete items primarily consisted of: (1) a tax expense of \$2.1 million related to the reversal of accrued restructuring expenses and (2) a tax expense of \$1.0 million of interest related to uncertain tax positions.

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## LAM RESEARCH CORPORATION

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

September 26, 2010

(Unaudited)

The total gross unrecognized tax benefits as of each date noted below were as follows:

|                                       | September 26,<br>2010 | June 27,<br>2010 |
|---------------------------------------|-----------------------|------------------|
|                                       | (in millions)         |                  |
| Total gross unrecognized tax benefits | \$ 196.9              | \$ 190.5         |

As of September 26, 2010, the total gross unrecognized tax benefits were \$196.9 million compared to \$190.5 million as of June 27, 2010, representing an increase of approximately \$6.4 million for the quarter. If the gross unrecognized tax benefits were recognized in a future period, it would result in a net tax benefit of \$160.2 million and a reduction of the effective tax rate. The Company does not anticipate that the total unrecognized tax benefits will significantly change due to the expiration of statutes of limitations in the next 12 months.

The Company recognizes interest expense and penalties related to the above unrecognized tax benefits within income tax expense. As of September 26, 2010, the Company had accrued approximately \$19.6 million for the payment of gross interest and penalties, relating to unrecognized tax benefits, compared to \$18.5 million as of June 27, 2010.

The Company files U.S. federal, U.S. state, and foreign income tax returns. As of September 26, 2010, tax years 2001-2010 remain subject to examination in certain jurisdictions where the Company operates.

The Internal Revenue Service ( IRS ) is examining the Company's U.S. income tax return for fiscal year 2007. The California Franchise Tax Board ( FTB ) is examining the Company's tax returns for fiscal years 2005 and 2006. As of September 26, 2010, no significant adjustments have been proposed by the IRS or FTB. The Company is unable to make a reasonable estimate as to when cash settlements, if any, with the relevant taxing authorities will occur.

The Company believes it has made adequate tax payments and accrued adequate amounts such that the outcome of these audits will have no material adverse effects on its results of operations or financial condition. It is reasonably possible that certain examinations may be concluded in the next twelve months. Until these examinations are effectively settled, the Company cannot estimate if there will be a material change to the total unrecognized tax benefits within the next twelve months.

Realization of the Company's net deferred tax assets is based upon the weight of available evidence, including such factors as the recent earnings history and expected future taxable income. The Company believes it is more likely than not that such assets will be realized with the exception of \$37.0 million related to certain California and foreign deferred tax assets. However, ultimate realization could be negatively impacted by market conditions and other variables not known or anticipated at this time. If the valuation allowance related to deferred tax assets were released as of September 26, 2010, approximately \$37.0 million would be credited to the statement of operations.

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## LAM RESEARCH CORPORATION

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

September 26, 2010

(Unaudited)

**NOTE 11 NET INCOME PER SHARE**

Basic net income per share is computed by dividing net income by the weighted-average number of common shares outstanding during the period. Diluted net income per share is computed, using the treasury stock method, for dilutive stock options and restricted stock units. The following table reconciles the numerators and denominators of the basic and diluted computations for net income per share.

|   | <b>Three Months Ended</b>                    |                               |
|---|--|-------------------------------|
|   | <b>September 26,<br/>2010</b>                | <b>September 27,<br/>2009</b> |
|   | <b>(in thousands, except per share data)</b> |                               |
| <b>Numerator:</b>                               |  |                               |
| Net income                                      | \$ 193,724                                   | \$ 16,797                     |
| <b>Denominator:</b>                             |  |                               |
| Basic average shares outstanding                | 123,665                                      | 126,774                       |
| <b>Effect of potential dilutive securities:</b> |  |                               |
| Employee stock plans                            | 1,537  | 1,116                         |
| <b>Diluted average shares outstanding</b>       | <b>125,202</b>                               | <b>127,890</b>                |
| Net income per share basic                      | \$ 1.57                                      | \$ 0.13                       |
| Net income per share diluted                    | \$ 1.55                                      | \$ 0.13                       |

For purposes of computing diluted net income per share, weighted-average common shares do not include potentially dilutive securities that are anti-dilutive under the treasury stock method. The following potentially dilutive securities were excluded:

|  | <b>Three Months Ended</b>     |                               |
|--|-------------------------------|-------------------------------|
|  | <b>September 26,<br/>2010</b> | <b>September 27,<br/>2009</b> |
|  | <b>(in thousands)</b>         |                               |
| Number of potential dilutive securities excluded | 30                            | 136                           |

**NOTE 12 COMPREHENSIVE INCOME**

The components of comprehensive income, on an after-tax basis where applicable, are as follows:



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|   | Three Months Ended    |                       |
|---|-----------------------|-----------------------|
|   | September 26,<br>2010 | September 27,<br>2009 |
|   | (in thousands)        |                       |
| Net income  | \$ 193,724            | \$ 16,797             |
| Foreign currency translation adjustment                                       | 30,673                | 13,800                |
| Unrealized gain (loss) on fair value of derivative financial instruments, net | 2,161                 | (715)                 |
| Unrealized gain (loss) on financial instruments, net                          | (77)                  | 1,280                 |
| Reclassification adjustment for gain included in earnings                     | (3,769)               | (72)                  |
| Postretirement benefit plan adjustment  | 995                   | 51                    |
| <b>Comprehensive income</b>   | <b>\$ 223,707</b>     | <b>\$ 31,141</b>      |

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## LAM RESEARCH CORPORATION

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

September 26, 2010

(Unaudited)

The balance of accumulated other comprehensive loss, on an after-tax basis where applicable, is as follows:

|   | September 26,<br>2010 | June 27,<br>2010 |
|---|-----------------------|------------------|
|   | (in thousands)        |                  |
| Accumulated foreign currency translation adjustment             | \$ (35,170)           | \$ (65,843)      |
| Accumulated unrealized gain on derivative financial instruments | (1,485)               | (1)              |
| Accumulated unrealized gain on financial instruments            | 1,024                 | 1,225            |
| Postretirement benefit plan adjustment                          | (4,235)               | (5,230)          |
| Accumulated other comprehensive loss                            | \$ (39,866)           | \$ (69,849)      |

**NOTE 13 LONG-TERM DEBT AND GUARANTEES**

The Company's contractual cash obligations relating to its existing capital leases and debt as of September 26, 2010 are as follows:

|  | Capital<br>Leases | Long-term<br>Debt<br>(in thousands) | Total     |
|--|-------------------|-------------------------------------|-----------|
| Payments due by period:                              |                   |                                     |           |
| One year   | \$ 1,742          | \$ 3,792                            | \$ 5,534  |
| Two years  | 1,752             | 134                                 | 1,886     |
| Three years  | 1,649             |                                     | 1,649     |
| Four years   | 1,443             |                                     | 1,443     |
| Five years   | 1,445             |                                     | 1,445     |
| Over 5 years   | 9,651             |                                     | 9,651     |
| Total  | 17,682            | 3,926                               | 21,608    |
| Interest on capital leases                           | 1,305             |                                     | 1,305     |
| Total less interest on capital leases                | 16,377            | 3,926                               | 20,303    |
| Current portion of long-term debt and capital leases | 1,434             | 3,792                               | 5,226     |
| Long-term debt and capital leases                    | \$ 14,943         | \$ 134                              | \$ 15,077 |

*Capital Leases*

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Capital leases reflect building and office equipment lease obligations. The amounts in the table above include the interest portion of payment obligations.

### ***Long-Term Debt***

The Company's total long-term debt of \$3.9 million as of September 26, 2010 consists of various bank loans and government subsidized technology loans supporting operating needs.

### ***Operating Leases and Related Guarantees***

The Company leases most of its administrative, R&D and manufacturing facilities, regional sales/service offices and certain equipment under non-cancelable operating leases, which expire at various dates through fiscal year 2016. Certain of the Company's facility leases for buildings located at its Fremont, California headquarters and certain other facility leases provide the Company with options to extend the leases for additional periods or to purchase the facilities. Certain of the Company's facility leases provide for periodic rent increases based on the general rate of inflation.

On December 18, 2007, the Company entered into two operating leases regarding certain improved properties in Livermore, California. These leases were amended on April 3, 2008 and July 9, 2008 (as so amended, the "Livermore Leases"). On December 21, 2007, the Company entered into a series of four amended and restated operating leases (the "New Fremont Leases," and collectively with the Livermore Leases, the "Operating Leases") with regard to certain improved properties at the Company's headquarters in Fremont, California. Each of the Operating Leases is an off-balance sheet arrangement. The Operating Leases (and associated documents for each Operating Lease) were entered into by the Company and BNP Paribas Leasing Corporation ("BNPPLC").

Each Operating Lease facility has a term of approximately seven years ending on the first business day in January 2015. Under each Operating Lease, the Company may, at its discretion and with 30 days' notice, elect to purchase the property that is the subject of the Operating Lease for an amount approximating the sum required to prepay the amount of BNPPLC's investment in the property and any accrued but unpaid rent. Any such amount may also include an additional make-whole amount for early redemption of the outstanding investment, which will vary depending on prevailing interest rates at the time of prepayment.

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**LAM RESEARCH CORPORATION**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**September 26, 2010**

**(Unaudited)**

The Company is required, pursuant to the terms of the Operating Leases and associated documents, to maintain collateral in an aggregate of approximately \$164.9 million in separate interest-bearing accounts as security for the Company's obligations under the Operating Leases. As of September 26, 2010, the Company had \$164.9 million recorded as restricted cash in its consolidated balance sheet as collateral required under the Operating Leases related to the amounts currently outstanding on the facilities.

When the term of an Operating Lease expires, the property subject to that Operating Lease may be remarketed. The Company has guaranteed to BNPPLC that each property will have a certain minimum residual value, as set forth in the applicable Operating Lease. The aggregate guarantee made by the Company under the Operating Leases is generally no more than approximately \$141.7 million; however, under certain default circumstances, the guarantee with regard to an Operating Lease may be 100% of BNPPLC's aggregate investment in the applicable property. The amounts payable under such guarantees will be no more than \$164.9 million plus related indemnification or other obligations.

The lessor under the Operating Leases is a substantive independent leasing company that does not have the characteristics of a variable interest entity (VIE) and is therefore not consolidated by the Company.

***Other Guarantees***

The Company has issued certain indemnifications to its lessors for taxes and general liability under some of its agreements. The Company has entered into certain insurance contracts which may limit its exposure to such indemnifications. As of September 26, 2010, the Company has not recorded any liability on its consolidated financial statements in connection with these indemnifications, as it does not believe, based on information available, that it is probable that any amounts will be paid under these guarantees.

Generally, the Company indemnifies, under pre-determined conditions and limitations, its customers for infringement of third-party intellectual property rights by the Company's products or services. The Company seeks to limit its liability for such indemnity to an amount not to exceed the sales price of the products or services subject to its indemnification obligations. The Company does not believe, based on information available, that it is probable that any material amounts will be paid under these guarantees.

The Company recognized at lease inception \$0.6 million in estimated liabilities related to the Operating Leases, which represents the fair value guarantee premium that would be required had the guarantee been issued in a standalone transaction. These liabilities are recorded in other long-term liabilities with the offsetting entry recorded as prepaid rent in other assets. The balances in prepaid rent and the guarantee liability are amortized to the statement of operations on a straight line basis over the life of the leases. If it becomes probable that the Company will be required to make a payment under the residual guarantee, the Company will increase its liability with a corresponding increase to prepaid rent and amortize the increased prepaid rent over the remaining lease term with no corresponding reduction in the liability. As of September 26, 2010, the unamortized portion of the fair value of the residual value guarantees remaining in other long-term liabilities and prepaid rent was \$0.3 million.

***Warranties***

The Company offers standard warranties on its systems that generally run for a period of 12 months from system acceptance. The liability amount is based on actual historical warranty spending by type of system, customer, and geographic region, modified for any known differences such as the impact of system reliability improvements.

Changes in the Company's product warranty reserves were as follows:

|   | Three Months Ended    |                       |
|---|-----------------------|-----------------------|
|   | September 26,<br>2010 | September 27,<br>2009 |
|   | (in thousands)        |                       |
| Balance at beginning of period  | \$ 31,756             | \$ 21,185             |
| Warranties issued during the period   | 11,416                | 4,943                 |
| Settlements made during the period  | (7,694)               | (4,626)               |
| Expirations and change in liability for pre-existing warranties during the period | (242)                 | (1,777)               |
| Changes in foreign currency exchange rates  | 376                   | 425                   |
| Balance at end of period  | \$ 35,612             | \$ 20,150             |

**NOTE 14 RESTRUCTURING AND ASSET IMPAIRMENTS**

Prior to incurring charges under the restructuring plans discussed below, management approved and announced the specific actions to be taken under each plan. Severance packages were communicated to affected employees in sufficient detail that the employees could determine

**Table of Contents****LAM RESEARCH CORPORATION****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****September 26, 2010****(Unaudited)**

their type and amount of benefit. The termination of the affected employees occurred as soon as practical after the restructuring plans were announced. The amount of remaining future lease payments for facilities the Company ceased to use and included in the restructuring charges is based on management's estimates using known prevailing real estate market conditions at that time based, in part, on the opinions of independent real estate experts. Leasehold improvements relating to the vacated buildings were written off, as these items will have no future economic benefit to the Company and have been abandoned.

Accounting for restructuring activities, as compared to regular operating cost management activities, requires an evaluation of formally committed and approved plans. Restructuring activities have comparatively greater strategic significance and materiality and may involve exit activities, whereas regular cost containment activities are more tactical in nature and are rarely characterized by formal and integrated action plans or exiting a particular product, facility, or service.

The following table summarizes restructuring and asset impairment charges and reversals during the three months ended September 26, 2010 and September 27, 2009 for each restructuring Plan. These amounts were recorded in operating expenses within the consolidated statements of operations for the respective periods.

|   | <b>Three Months Ended</b>     |                               |
|---|-------------------------------|-------------------------------|
|   | <b>September 26,<br/>2010</b> | <b>September 27,<br/>2009</b> |
|   | <b>(in thousands)</b>         |                               |
| December 2008 Plan                                      | \$                            | \$ 105                        |
| March 2009 Plan   | (5,163)                       | 1,988                         |
| <b>Total restructuring and asset impairment charges</b> | <b>\$ (5,163)</b>             | <b>\$ 2,093</b>               |

***December 2008 Plan***

During the December 2008 quarter the Company incurred restructuring expenses and asset impairment charges designed to better align the Company's cost structure with its business opportunities in consideration of market and economic uncertainties (December 2008 Plan). There were no restructuring and asset impairment charges incurred under the December 2008 Plan during the three months ended September 26, 2010. During the three months ended September 27, 2009 there were \$0.1 million of expenses incurred under the December 2008 Plan relating to severance and benefits. The remaining liabilities balance under the December 2008 Plan were \$0.3 million as of both September 26, 2010 and June 27, 2010 and relates to severance and benefits.

Total charges incurred through September 26, 2010 under the December 2008 Plan were \$17.9 million.

***March 2009 Plan***

During the March 2009 quarter the Company incurred restructuring expenses and asset impairment charges designed to align the Company's cost structure with its outlook for the current economic environment and future business opportunities (March 2009 Plan). During the September 2010 quarter, the Company reversed certain restructuring and asset impairment charges as a result of a decision to occupy previously restructured facilities. Restructuring and asset impairment charges (reversal) during the three months ended September 26, 2010 and September 27, 2009 were as follows:

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|  | Three Months Ended    |                       |
|--|-----------------------|-----------------------|
|  | September 26,<br>2010 | September 27,<br>2009 |
|  | (in thousands)        |                       |
| Severance and benefits                           | \$                    | \$ 478                |
| Facilities                                       | (5,163)               | 1,510                 |
| Total restructuring and asset impairment charges | \$ (5,163)            | \$ 1,988              |

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## LAM RESEARCH CORPORATION

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

September 26, 2010

(Unaudited)

Below is a table summarizing activity relating to the March 2009 Plan during the three months ended September 26, 2010:

|                                     | Severance and<br>Benefits<br>(in<br>thousands) | Facilities | Total     |
|-------------------------------------|--|------------|-----------|
| Balance at June 27, 2010            | \$ 265   | \$ 16,852  | \$ 17,117 |
| Fiscal year 2011 expense (reversal) |  | (5,163)    | (5,163)   |
| Cash payments                       | (79)   | (496)      | (575)     |
| Balance at September 26, 2010       | \$ 186   | \$ 11,193  | \$ 11,379 |

Total charges incurred through September 26, 2010 under the March 2009 Plan were \$44.3 million.

The severance and benefits-related balances are anticipated to be paid by the end of fiscal year 2011. The facilities balance consists primarily of lease payments, net of sublease income, on vacated buildings and is expected to be paid by the end of fiscal year 2015.

**NOTE 15 STOCK REPURCHASE PROGRAM**

On September 8, 2008, the Company announced that its Board of Directors had authorized the repurchase of up to \$250 million of Company common stock from the public market or in private purchases, using the Company's available cash. While the repurchase program does not have a defined termination date, it may be suspended or discontinued at any time. The Company temporarily suspended repurchases under the program during the December 2008 quarter. On February 2, 2010, the Board of Directors authorized the resumption of the repurchase program. The Company completed the repurchase of all amounts available under this share repurchase authorizations during the quarter ended September 26, 2010.

On September 10, 2010, the Company announced that its Board of Directors had authorized the repurchase of up to an additional \$250 million of Company common stock using the Company's available cash. These repurchases could be conducted on the open market or as private purchases and may include the use of derivative contracts with large financial institutions. The repurchase program does not have a defined termination date, and it may be suspended or discontinued at any time.

Repurchases under the repurchase program were as follows during the periods indicated:

| Period                                | Total Number of<br>Shares<br>Repurchased | Total Cost of<br>Repurchase<br>(in thousands, except per share data) | Average Price Paid<br>Per Share | Amount Available<br>Under Repurchase<br>Program |
|---------------------------------------|--|--|---------------------------------|---|
| Available balance as of June 27, 2010 |  |  |                                 | \$ 130,693                                      |
|                                       |  |  |                                 | \$ 380,693                                      |



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Authorization of up to \$250 million    September  
2010

|                                  |       |            |          |            |
|----------------------------------|-------|------------|----------|------------|
| Quarter ended September 26, 2010 | 3,389 | \$ 130,693 | \$ 38.56 | \$ 250,000 |
|----------------------------------|-------|------------|----------|------------|

During the three months ended September 26, 2010, the Company withheld approximately 18,000 shares through net share settlements to cover tax withholding obligations upon the vesting of restricted stock unit awards granted under the Company's equity compensation plans. The shares retained by the Company through these net share settlements are not a part of the Board-authorized repurchase program but instead are authorized under the Company's equity compensation plans.

### **NOTE 16    LEGAL PROCEEDINGS**

From time to time, the Company has received notices from third parties alleging infringement of such parties' patent or other intellectual property rights by the Company's products. In such cases, it is the Company's policy to defend the claims, or if considered appropriate, negotiate licenses on commercially reasonable terms. However, no assurance can be given that the Company will be able in the future to negotiate necessary licenses on commercially reasonable terms, or at all, or that any litigation resulting from such claims would not have a material adverse effect on the Company's consolidated financial position or operating results.

**Table of Contents****ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations  
CAUTIONARY STATEMENT REGARDING FORWARD LOOKING STATEMENTS**

*With the exception of historical facts, the statements contained in this discussion are forward-looking statements, which are subject to the safe harbor provisions created by the Private Securities Litigation Reform Act of 1995. Certain, but not all, of the forward-looking statements in this report are specifically identified as forward-looking, by use of phrases and words such as we believe, we anticipate, we expect, may, should, could and other future-oriented terms. The identification of certain statements as forward-looking is not intended to mean that other statements not specifically identified are not forward-looking. Forward-looking statements include, but are not limited to, statements that relate to: trends in the global economic environment and the semiconductor industry; the anticipated levels of, and rates of change in, future shipments, margins, market share, capital expenditures, revenue and operating expenses generally; volatility in our quarterly results; customer requirements and our ability to satisfy those requirements; customer capital spending and their demand for our products; our ability to defend our market share and to gain new market share; anticipated growth in the industry and the total market for wafer-fabrication equipment and our growth relative to such growth; levels of research and development( R&D ) expenditures; the estimates we make, and the accruals we record, in order to implement our critical accounting policies (including but not limited to the adequacy of prior tax payments, future tax liabilities and the adequacy of our accruals relating to them); our access to capital markets; our ability to manage and grow our cash position; and the sufficiency of our financial resources to support future business activities (including but not limited to operations, investments, debt service requirements and capital expenditures). Such statements are based on current expectations and are subject to risks, uncertainties, and changes in condition, significance, value, and effect, including without limitation those discussed below under the heading Risk Factors within Part II Item 1A and elsewhere in this report and other documents we file from time to time with the Securities and Exchange Commission ( SEC ), such as our annual reports on Form 10-K and our current reports on Form 8-K. Such risks, uncertainties and changes in condition, significance, value, and effect could cause our actual results to differ materially from those expressed in this report and in ways not readily foreseeable. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof and are based on information currently and reasonably known to us. We undertake no obligation to release the results of any revisions to these forward-looking statements, which may be made to reflect events or circumstances that occur after the date hereof or to reflect the occurrence or effect of anticipated or unanticipated events.*

**Documents To Review In Connection With Management's Discussion and Analysis Of Financial Condition and Results Of Operations**

For a full understanding of our financial position and results of operations for the three months ended September 26, 2010, and the related Management's Discussion and Analysis of Financial Condition and Results of Operations below, you should also read the condensed consolidated financial statements and notes presented in this Form 10-Q and the financial statements and notes in our 2010 Form 10-K.

**Overview**

Management's Discussion and Analysis of Financial Condition and Results of Operations consists of the following sections:

*Executive Summary* provides an overview of the Company's operations and a summary of certain highlights of our results of operations

*Results of Operations* provides an analysis of operating results

*Critical Accounting Policies and Estimates* discusses accounting policies that reflect the more significant judgments and estimates we use to prepare our condensed consolidated financial statements

*Liquidity and Capital Resources* provides an analysis of cash flows, contractual obligations and financial position

**EXECUTIVE SUMMARY**

We design, manufacture, market, refurbish, and service semiconductor processing equipment used in the fabrication of integrated circuits and are recognized as a major provider of such equipment to the worldwide semiconductor industry. Our customers include semiconductor memory and foundry manufacturers that make DRAM, flash memory, and logic integrated circuits for a wide range of consumer and industrial electronics. Semiconductor wafers are subjected to a complex series of process and preparation steps that result in the simultaneous creation of many individual integrated circuits. We leverage our expertise in the areas of etch and single-wafer clean to develop processing solutions that typically benefit our customers through lower defect rates, enhanced yields, faster processing time, and/or reduced cost as well as by facilitating their ability to meet more stringent performance and design standards.

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The semiconductor industry is cyclical in nature and has historically experienced periodic and pronounced downturns and upturns. Today's leading indicators of change in customer investment patterns may not be any more reliable than in prior years. Demand for our equipment can vary significantly from period to period as a result of various factors, including, but not limited to, economic conditions (both general and in the semiconductor and electronics industries), supply, demand, prices for semiconductors, customer capacity requirements, and our ability to develop, acquire, and market competitive products. For these and other reasons, our results of operations during any particular fiscal period are not necessarily indicative of future operating results.

Adverse conditions in the global economy during 2008 and 2009 severely reduced customer demand for our products, resulting in reduced revenue and profits throughout fiscal 2009. Our shipments, revenue and net income increased significantly in the September 2010 quarter compared to the June 2010 quarter, in response to improved customer demand. We expect the same to be true for calendar year 2010 versus calendar year 2009 given our current view of wafer fabrication equipment spending.

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We believe that, over the long term, demand for our products will continue to increase as customers' capital expenditures increase to meet growing demand for semiconductor devices. However, historically, any improvement in demand for semiconductor manufacturing equipment occurs at an uneven pace. Accordingly, any forecasts about demand for wafer fabrication equipment in the near term are subject to uncertainty, and we could experience significant volatility in our quarterly results of operations over the next several quarters.

The following table summarizes certain key financial information for the periods indicated below (in thousands, except percentage and per share data):

|  | <b>Three Months Ended</b>     |                          |                               |
|--|-------------------------------|--------------------------|-------------------------------|
|  | <b>September 26,<br/>2010</b> | <b>June 27,<br/>2010</b> | <b>September 27,<br/>2009</b> |
| Revenue                                    | \$ 805,874                    | \$ 695,289               | \$ 318,548                    |
| Gross margin                               | \$ 377,326                    | \$ 321,442               | \$ 134,435                    |
| Gross margin as a percent of total revenue | 46.8%                         | 46.2%                    | 42.2%                         |
| Total operating expenses                   | \$ 153,332                    | \$ 165,725               | \$ 105,183                    |
| Net income                                 | \$ 193,724                    | \$ 139,997               | \$ 16,797                     |
| Diluted net income per share               | \$ 1.55                       | \$ 1.10                  | \$ 0.13                       |

Our results for the September 2010 quarter reflect continued improvement in the global business environment and in the semiconductor industry, improved foundry fabrication utilization and an increase in the rate of next-generation DRAM and NAND technology conversions by leading memory companies.

Throughout calendar year 2010, we have maintained our investments in new product R&D to defend our market share and win new application share. Our activities also focused on improving customer productivity in our installed base by delivering continuously improved performance and lower cost of ownership. We continued to develop the operational capability to rapidly respond to short lead-time customer orders. We believe that these activities will allow us to maintain and grow our cash position over time.

We continue to believe that the total market for wafer-fabrication equipment will increase substantially in calendar year 2010 as compared to 2009 and currently anticipate year-on-year growth in our customer shipments as a result of both expansion of the market as a whole and increases in our market share.

Conditions in our industry have clearly improved and we continue to anticipate industry and market share growth for calendar year 2010 as compared to calendar year 2009. However, we cannot predict the robustness or pace of any macroeconomic recovery; at present, customer input suggests that shipments may flatten or decline slightly in the first half of calendar year 2011. The electronics and semiconductor industries remain significantly linked to worldwide GDP and consumer spending.

In the quarter ended September 26, 2010, revenue increased by 16%, as compared to the quarter ended June 27, 2010, primarily reflecting increased system shipments driven by growth in customer demand. Gross margin as a percent of revenues for the September 2010 quarter was 46.8% as compared to 46.2% in the June 2010 quarter. Included in cost of goods sold during the June 2010 quarter were approximately \$3 million of restructuring and asset impairment charges.

Operating expenses in the September 2010 quarter decreased \$12 million as compared to the quarter ended June 27, 2010. This decrease was primarily due to a decrease in restructuring charges from a charge of approximately \$13 million in the June 2010 quarter to a reversal of approximately \$5 million in the September 2010 quarter. This decrease was partially offset by higher variable compensation associated with our higher revenue and profit levels, as well as increased R&D investments to support and grow our etch and clean market share.

Our cash and cash equivalents, short-term investments, and restricted cash and investments balances totaled approximately \$1.1 billion as of September 26, 2010 compared to \$992 million as of June 27, 2010. Cash generated by operations was approximately \$256 million during the September 2010 quarter. We used cash to repurchase approximately \$145 million of our shares, to repay \$3 million of outstanding loan amounts, and to purchase \$19 million of property, plant, and equipment. Employee headcount increased to approximately 3,300 as of September 26, 2010, from approximately 3,150 in the June 2010 quarter.



**Table of Contents****RESULTS OF OPERATIONS***Shipments*

|                         | Three Months Ended    |                  |                       |
|-------------------------|-----------------------|------------------|-----------------------|
|                         | September 26,<br>2010 | June 27,<br>2010 | September 27,<br>2009 |
| Shipments (in millions) | \$ 808                | \$ 694           | \$ 355                |
| North America           | 5%                    | 8%               | 10%                   |
| Europe                  | 11%                   | 10%              | 6%                    |
| Japan                   | 12%                   | 22%              | 18%                   |
| Korea                   | 29%                   | 29%              | 24%                   |
| Taiwan                  | 28%                   | 23%              | 31%                   |
| Asia Pacific            | 15%                   | 8%               | 11%                   |

Shipments for the September 2010 quarter increased 16% compared to the June 2010 quarter and 128% year over year. During the September 2010 quarter, applications at or below the 65 nanometer technology node were 89% of total systems shipments. The memory market segment was approximately 57% of shipments, with foundry at 33%, and integrated device manufacturers and logic at 10%.

*Revenue*

|                        | Three Months Ended    |                  |                       |
|------------------------|-----------------------|------------------|-----------------------|
|                        | September 26,<br>2010 | June 27,<br>2010 | September 27,<br>2009 |
| Revenue (in thousands) | \$ 805,874            | \$ 695,289       | \$ 318,548            |
| North America          | 5%                    | 8%               | 9%                    |
| Europe                 | 10%                   | 7%               | 7%                    |
| Japan                  | 12%                   | 17%              | 18%                   |
| Korea                  | 36%                   | 27%              | 23%                   |
| Taiwan                 | 21%                   | 33%              | 29%                   |
| Asia Pacific           | 16%                   | 8%               | 14%                   |

Revenue for the September 2010 quarter increased 16% compared to the June 2010 quarter and 153% year over year. Revenue increased in all product lines. Our revenue levels are generally correlated to our shipment, installation and acceptance timelines. The overall Asia region continues to account for a predominant portion of our revenues as a substantial amount of the worldwide capacity additions for semiconductor manufacturing continues to occur in this region. Our deferred revenue balance increased to \$217.3 million as of September 26, 2010 compared to \$207.4 million as of June 27, 2010. Our deferred revenue balance does not include shipments to Japanese customers, to whom title does not transfer until customer acceptance. Shipments to Japanese customers are classified as inventory at cost until the time of acceptance. The anticipated future revenue value from shipments to Japanese customers was approximately \$50 million as of September 26, 2010 compared to \$52 million as of June 27, 2010.

*Gross Margin*

|                          | Three Months Ended                 |                  |                       |
|--------------------------|------------------------------------|------------------|-----------------------|
|                          | September 26,<br>2010              | June 27,<br>2010 | September 27,<br>2009 |
|                          | (in thousands, except percentages) |                  |                       |
| Gross margin             | \$ 377,326                         | \$ 321,442       | \$ 134,435            |
| Percent of total revenue | 46.8%                              | 46.2%            | 42.2%                 |

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Gross margin during the September 2010 quarter increased slightly compared to the June 2010 quarter, which included \$3 million in restructuring and asset impairment charges.

The increase in gross margin during the September 2010 quarter as compared to the same period in the prior year was due primarily to increased revenues, favorable product mix and increased factory and field utilization.

**Table of Contents****Research and Development**

|                          | September 26,<br>2010              | Three Months Ended<br>June 27,<br>2010 | September 27,<br>2009 |
|--------------------------|------------------------------------|--|-----------------------|
|                          | (in thousands, except percentages) |  |                       |
| Research and development | \$ 86,353                          | \$ 85,644                              | \$ 71,199             |
| Percent of total revenue | 10.7%                              | 12.3%                                  | 22.4%                 |

We continue to make significant R&D investments focused on plasma etch, single-wafer clean and other semiconductor manufacturing requirements. The increase in R&D expenses during the September 2010 quarter compared to the June 2010 quarter is primarily due to higher variable compensation associated with higher revenue and profit levels.

The increase in R&D expenses during the September 2010 quarter compared to the same period in the prior year is due to \$7 million of higher variable compensation associated with higher revenue and profit levels, \$3 million of higher salaries and benefits related to annual merit increases and higher headcount, and \$2 million of increased costs for supplies and outside services.

**Selling, General and Administrative**

|  | September 26,<br>2010              | Three Months Ended<br>June 27,<br>2010 | September 27,<br>2009 |
|--|------------------------------------|--|-----------------------|
|  | (in thousands, except percentages) |  |                       |
| Selling, general and administrative ( SG&A ) | \$ 72,142                          | \$ 66,779                              | \$ 52,119             |
| Percent of total revenue                     | 9.0%                               | 9.6%                                   | 16.4%                 |

The sequential increase in SG&A expenses in the September 2010 quarter was primarily due to \$4 million of variable compensation associated with higher revenue and profit levels and \$2 million of increased costs for supplies and outside services.

The increase in SG&A expenses for the September 2010 quarter compared to the same period in the prior year was primarily due to \$13 million of higher variable compensation associated with higher revenue and profit levels, \$4 million of higher salaries and benefits related to annual merit increases and higher headcount, and \$1 million of increased costs for supplies and outside services.

**Restructuring and Asset Impairments**

The following table summarizes charges (recoveries/reversals) under each of the plans described below for the periods indicated:

|   | September 26,<br>2010 | Three Months Ended<br>June 27,<br>2010 | September 27,<br>2009 |
|---|-----------------------|--|-----------------------|
|   | (in thousands)        |  |                       |
| June 2008 Plan  | \$                    | \$ (2,217)                             | \$                    |
| December 2008 Plan  |                       | (13)                                   | 105                   |
| March 2009 Plan   | (5,163)               | 12,984                                 | 1,988                 |
| Total restructuring and asset impairment charges incurred under restructuring plans | \$ (5,163)            | \$ 10,754                              | \$ 2,093              |

During fiscal years 2008 and 2009, we incurred restructuring and asset impairment charges related to the integration of SEZ and overall streamlining of our combined Clean Product Group ( June 2008 Plan ). These charges included severance and related benefits costs, excess



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facilities-related costs and certain asset impairments associated with our initial product line integration road maps. During the quarter ended June 27, 2010, we recorded a recovery of \$2.2 million related primarily to inventory previously restructured in connection with our initial product line integration road maps.

During fiscal years 2009 and 2010, we incurred restructuring and asset impairment charges designed to better align our cost structure with our business opportunities in consideration of market and economic uncertainties ( December 2008 Plan ). These charges consisted primarily of severance and related benefits costs as well as certain facilities related costs and asset impairments.

During fiscal years 2009 and 2010, we also incurred restructuring and asset impairment charges designed to align our cost structure with our outlook for the economic environment and future business opportunities at that time ( March 2009 Plan ). These charges consisted primarily of severance and related benefits costs as well as certain facilities related costs and asset impairments. During the quarter ended June 27, 2010, the Company recognized a restructuring charge of \$13.0 million related to the residual value guarantee for previously restructured leases. During the quarter ended September 26, 2010, the Company recorded a reversal of \$5.2 million as a result of a decision to occupy certain previously restructured facilities.

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In addition to charges incurred under the specific restructuring plans, during the quarter ended June 27, 2010, we incurred \$6.0 million of asset impairment charges related to production efficiencies and shifts in product demands.

For further details related to restructuring and asset impairment, see Note 14 of the Notes to Consolidated Financial Statements.

**409A Expense**

Following the voluntary independent review of our historical employee stock option grant process in 2007, we considered whether Section 409A ( Section 409A ) of the Internal Revenue Code of 1986, as amended ( IRC ) and similar provisions of state law would apply to certain stock option grants that were found to have intrinsic value at the time of their respective measurement dates. If a stock option is not considered as issued with an exercise price of at least the fair market value of the underlying stock on the date of grant, it may be subject to penalty taxes under Section 409A and similar provisions of state law. Under those circumstances, taxes may be assessed not only on the intrinsic value increase, but on the entire stock option gain as measured at various times. On March 30, 2008, our Board of Directors authorized us to assume potential tax liabilities of certain employees, including our Chief Executive Officer and certain other executive officers, relating to options that might be subject to Section 409A and similar provisions of state law. Those liabilities totaled \$50.9 million; \$44.5 million was recorded in operating expenses and \$6.4 million in cost of goods sold in our consolidated statements of operations for fiscal year 2008. We incurred \$3.2 million of expense during fiscal year 2009 consisting of interest and legal fees.

During fiscal year 2010, we reached final settlement of matters associated with our Section 409A expenses with the Internal Revenue Service ( IRS ) and California Franchise Tax Board ( FTB ) resulting in a credit of \$44.4 million due to the reversal of Section 409A liabilities. Of this credit, \$23.3 million was recorded in the three months ended September 27, 2009. The determinations from the voluntary independent stock option review are more fully described in Note 3, Restatement of Consolidated Financial Statements to Consolidated Financial Statements and Management s Discussion and Analysis of Financial Condition and Results of Operations in Item 7 of our 2007 Form 10-K.

There were no expenses related to Section 409A in the September 2010 quarter.

**Other Income (Expense), Net**

Other income (expense), net consisted of the following:

|                              | <b>Three Months Ended</b>     |                          |                               |
|------------------------------|-------------------------------|--------------------------|-------------------------------|
|                              | <b>September 26,<br/>2010</b> | <b>June 27,<br/>2010</b> | <b>September 27,<br/>2009</b> |
|                              | <b>(in thousands)</b>         |                          |                               |
| Interest income              | \$ 3,076                      | \$ 1,679                 | \$ 2,048                      |
| Interest expense             | (101)                         | (126)                    | (189)                         |
| Foreign exchange gain (loss) | (3,179)                       | 1,236                    | (1,794)                       |
| Other, net                   | (775)                         | 752                      | (433)                         |
|                              | <b>\$ (979)</b>               | <b>\$ 3,541</b>          | <b>\$ (368)</b>               |

Interest income increased in the three months ended September 26, 2010 compared with the three months ending June 27, 2010 and September 27, 2009 primarily due to increases in our average cash and investment balances.

Foreign exchange losses increased during the three months ending September 26, 2010 as compared to the three months ending June 27, 2010 and September 27, 2009, as a result of changes in the value of our foreign currency denominated liabilities with non-U.S. dollar functional subsidiaries where the U.S. dollar weakened against certain currencies, primarily the Euro and Singapore dollar. Included in foreign exchange gain during the three months ended June 27, 2010 was \$1.2 million of gains associated with our foreign currency denominated liabilities with non U.S. dollar functional currency subsidiaries where the U.S. dollar strengthened against certain currencies, primarily the Euro and, to a lesser extent, the Korean Won. Included in foreign exchange loss during the three months ended September 27, 2009 was \$1.7 million of losses associated with our foreign currency denominated liabilities with non U.S. dollar functional currency subsidiaries where the U.S. dollar weakened against certain currencies, primarily the Swiss franc and, to a lesser extent, the Euro.

*Income Tax Expense*

Our effective tax rate for the three months ended September 26, 2010 was 13.1%. Our effective tax rate for the three months ended September 27, 2009 was 41.8%. The change in the effective tax rate for the three months ended September 26, 2010 compared to the three months ended September 27, 2009 was primarily due to the level of income and its geographical mix in higher and lower tax jurisdictions. The effective tax rate of 13.1% for the three months ended September 26, 2010 includes the tax impact of the following discrete items which are recorded in the period in which they occur: (1) a tax expense of \$2.1 million related to the reversal of accrued restructuring expenses and (2) a tax expense of \$1.0 million of interest related to uncertain tax positions. The effective tax rate of 41.8% for the three months ended September 27, 2009 includes the tax impact of the following discrete items which are recorded in the period in which they occur: (1) a tax expense of \$9.3 million related to a settlement of 409A liabilities, (2) a tax expense of \$1.5 million related to a change in valuation allowance with respect to a California R&D credit, (3) a tax expense of \$1.0 million for interest related to uncertain tax positions, and (4) a tax benefit of \$1.0 million for adjustments related to the filing of prior year foreign tax returns.

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***Deferred Income Taxes***

We had gross deferred tax assets, related primarily to reserves and accruals that are not currently deductible and tax credit carryforwards, of \$138.2 million and \$137.4 million as of September 26, 2010, and June 27, 2010, respectively. The gross deferred tax assets were offset by deferred tax liabilities of \$36.3 million and a valuation allowance of \$37.0 million as of September 26, 2010. The gross deferred tax assets were offset by deferred tax liabilities of \$36.3 million and a valuation allowance of \$37.0 million as of June 27, 2010.

We record a valuation allowance to reduce our deferred tax assets to the amount that is more likely than not to be realized. Realization of our net deferred tax assets is dependent on future taxable income. We believe it is more likely than not that such assets will be realized; however, realization could be negatively impacted by market conditions and other variables not known or anticipated at this time. In the event that we determine that we would not be able to realize all or part of our net deferred tax assets, an adjustment would be charged to earnings in the period such determination is made. Likewise, if we later determine that it is more likely than not that the deferred tax assets would be realized, then the previously provided valuation allowance would be reversed. Our current valuation allowance of \$37.0 million relates to certain California and foreign deferred tax assets.

***Uncertain Tax Positions***

We reevaluate uncertain tax positions on a quarterly basis. This evaluation is based on factors including, but not limited to, changes in facts or circumstances, changes in tax law, effectively settled issues under audit, and new audit activity. Such a change in recognition or measurement would result in the recognition of a tax benefit or an additional charge to the tax provision.

**CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

A critical accounting policy is defined as one that has both a material impact on our financial condition and results of operations and requires us to make difficult, complex and/or subjective judgments, often as a result of the need to make estimates about matters that are inherently uncertain. The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make certain judgments, estimates and assumptions that could affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. We base our estimates and assumptions on historical experience and on various other assumptions we believe to be applicable and evaluate them on an ongoing basis to ensure they remain reasonable under current conditions. Actual results could differ significantly from those estimates, which could have a material impact on our business, results of operations, and financial condition.

We believe that the following critical accounting policies reflect the more significant judgments and estimates we use in preparing our consolidated financial statements.

***Revenue Recognition:*** We recognize all revenue when persuasive evidence of an arrangement exists, delivery has occurred and title has passed or services have been rendered, the selling price is fixed or determinable, collection of the receivable is reasonably assured, and we have completed our system installation obligations, received customer acceptance or are otherwise released from our installation or customer acceptance obligations. If terms of the sale provide for a lapsing customer acceptance period, we recognize revenue upon the expiration of the lapsing acceptance period or customer acceptance, whichever occurs first. If the practices of a customer do not provide for a written acceptance or the terms of sale do not include a lapsing acceptance provision, we recognize revenue when it can be reliably demonstrated that the delivered system meets all of the agreed-to customer specifications. In situations with multiple deliverables, we recognize revenue upon the delivery of the separate elements to the customer and when we receive customer acceptance or are otherwise released from our customer acceptance obligations. We allocate revenue from multiple-element arrangements among the separate elements based on their relative selling prices, provided the arrangement does not include a general right of return relative to the delivered item and delivery, or performance of the undelivered item(s) is considered probable and substantially in our control. The maximum revenue we recognize on a delivered element is limited to the amount that is not contingent upon the delivery of additional items. We generally recognize revenue related to sales of spare parts and system upgrade kits upon shipment. We generally recognize revenue related to services upon completion of the services requested by a customer order. We recognize revenue for extended maintenance service contracts with a fixed payment amount on a straight-line basis over the term of the contract.

***Inventory Valuation:*** Inventories are stated at the lower of cost or market using standard costs which generally approximate actual costs on a first-in, first-out basis. We maintain a perpetual inventory system and continuously record the quantity on-hand and standard cost for each product, including purchased components, subassemblies, and finished goods. We maintain the integrity of perpetual inventory records through

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periodic physical counts of quantities on hand. Finished goods are reported as inventories until the point of title transfer to the customer. Generally, title transfer is documented in the terms of sale. Unless specified in the terms of sale, title generally transfers when we complete physical transfer of the products to the freight carrier. Transfer of title for shipments to Japanese customers generally occurs at the time of customer acceptance.

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We reassess standard costs as needed but annually at a minimum, and reflect achievable acquisition costs. Acquisition costs are generally based on the most recent vendor contract prices for purchased parts, normalized assembly and test labor utilization levels, methods of manufacturing, and normalized overhead. Manufacturing labor and overhead costs are attributed to individual product standard costs at a level planned to absorb spending at average utilization volumes. We eliminate all intercompany profits related to the sales and purchases of inventory between our legal entities from our consolidated financial statements.

Management evaluates the need to record adjustments for impairment of inventory at least quarterly. Our policy is to assess the valuation of all inventories including manufacturing raw materials, work-in-process, finished goods, and spare parts in each reporting period. Obsolete inventory or inventory in excess of management's estimated usage requirements over the next 12 to 36 months is written down to its estimated

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market value if less than cost. Estimates of market value include, but are not limited to, management's forecasts related to our future manufacturing schedules, customer demand, technological and/or market obsolescence, general semiconductor market conditions, and possible alternative uses. If future customer demand or market conditions are less favorable than our projections, additional inventory write-downs may be required and would be reflected in cost of goods sold in the period in which we make the revision.

*Warranty:* Typically, the sale of semiconductor capital equipment includes providing parts and service warranty to customers as part of the overall price of the system. We provide standard warranties for our systems that generally run for a period of 12 months from system acceptance. When appropriate, we record a provision for estimated warranty expenses to cost of sales for each system when we recognize revenue. We do not maintain general or unspecified reserves; all warranty reserves are related to specific systems. The amount recorded is based on an analysis of historical activity which uses factors such as type of system, customer, geographic region, and any known factors such as tool reliability trends. All actual or estimated parts and labor costs incurred in subsequent periods are charged to those established reserves on a system-by-system basis.

Actual warranty expenses are accounted for on a system-by-system basis and may differ from our original estimates. While we periodically monitor the performance and cost of warranty activities, if actual costs incurred are different than our estimates, we may recognize adjustments to provisions in the period in which those differences arise or are identified. In addition to the provision of standard warranties, we offer customer-paid extended warranty services. Revenues for extended maintenance and warranty services with a fixed payment amount are recognized on a straight-line basis over the term of the contract. Related costs are recorded as incurred.

*Equity-based Compensation Employee Stock Purchase Plan ( ESPP ) and Employee Stock Plans:* GAAP requires us to recognize the fair value of equity-based compensation in net income. We determine the fair value of our restricted stock units based upon the fair market value of Company stock at the date of grant. We estimate the fair value of our stock options and ESPP awards using the Black-Scholes option valuation model. This model requires us to input highly subjective assumptions, including expected stock price volatility and the estimated life of each award. We amortize the fair value of equity-based awards over the vesting periods of the awards, and we have elected to use the straight-line method of amortization.

We make quarterly assessments of the adequacy of our tax credit pool related to equity-based compensation to determine if there are any deficiencies that we are required to recognize in our consolidated statements of operations. We will only recognize a benefit from stock-based compensation in paid-in-capital if we realize an incremental tax benefit after all other tax attributes currently available to us have been utilized. In addition, we have elected to account for the indirect benefits of stock-based compensation on the research tax credit through the income statement (continuing operations) rather than through paid-in-capital. We have also elected to net deferred tax assets and the associated valuation allowance related to net operating loss and tax credit carryforwards for the accumulated stock award tax benefits for income tax footnote disclosure purposes. We will track these stock award attributes separately and will only recognize these attributes through paid-in-capital.

*Income Taxes:* Deferred income taxes reflect the net tax effect of temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes, as well as the tax effect of carryforwards. We record a valuation allowance to reduce our deferred tax assets to the amount that is more likely than not to be realized. Realization of our net deferred tax assets is dependent on future taxable income. We believe it is more-likely-than-not that such assets will be realized; however, ultimate realization could be negatively impacted by market conditions and other variables not known or anticipated at the time. In the event that we determine that we would not be able to realize all or part of our net deferred tax assets, an adjustment would be charged to earnings in the period such determination is made. Likewise, if we later determine that it is more-likely-than-not that the deferred tax assets would be realized, then the previously provided valuation allowance would be reversed.

We calculate our current and deferred tax provision based on estimates and assumptions that can differ from the actual results reflected in income tax returns filed during the subsequent year. Adjustments based on filed returns are recorded when identified.

We recognize the benefit from a tax position only if it is more-likely-than-not that the position would be sustained upon audit based solely on the technical merits of the tax position. Our policy is to include interest and penalties related to unrecognized tax benefits as a component of income tax expense. Please refer to Note 10 of these Notes to the Consolidated Financial Statements for additional information.

In addition, the calculation of our tax liabilities involves dealing with uncertainties in the application of complex tax regulations. We recognize liabilities for uncertain tax positions based on the two-step process prescribed within the interpretation. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates that it is more-likely-than-not that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step requires us to estimate and measure the tax benefit as the largest amount that is more than 50% likely to be realized upon ultimate settlement. It is inherently difficult and subjective to estimate such amounts, as this requires us to determine the probability of various possible outcomes. We reevaluate these uncertain tax positions on a quarterly basis. This evaluation is based on factors including, but not limited to, changes in facts or circumstances, changes in tax law,

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effectively settled issues under audit, and new audit activity. Such a change in recognition or measurement would result in the recognition of a tax benefit or an additional charge to the tax provision in the period such determination is made.

*Goodwill and Intangible Assets:* Goodwill represents the amount by which the purchase price in each business combination exceeds the fair value of the net tangible and identifiable intangible assets acquired. We allocate the carrying value of goodwill to our reporting units. We test goodwill and identifiable intangible assets with indefinite useful lives for impairment at least annually. We amortize intangible assets with estimable useful lives over their respective estimated useful lives to their estimated residual values, and we review for impairment whenever events or changes in circumstances indicate that the carrying amount of the intangible asset may not be recoverable and the carrying amount exceeds its fair value.

We review goodwill at least annually for impairment. If certain events or indicators of impairment occur between annual impairment tests, we would perform an impairment test of goodwill at that date. In testing for a potential impairment of goodwill, we: (1) allocate goodwill to our



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reporting units to which the acquired goodwill relates; (2) estimate the fair value of our reporting units; and (3) determine the carrying value (book value) of those reporting units, as some of the assets and liabilities related to those reporting units are not held by those reporting units but by a corporate function. Prior to this allocation of the assets to the reporting units, we are required to assess long-lived assets for impairment. Furthermore, if the estimated fair value of a reporting unit is less than the carrying value, we must estimate the fair value of all identifiable assets and liabilities of that reporting unit, in a manner similar to a purchase price allocation for an acquired business. This can require independent valuations of certain internally generated and unrecognized intangible assets such as in-process R&D and developed technology. Only after this process is completed can the amount of goodwill impairment, if any, be determined.

The process of evaluating the potential impairment of goodwill is subjective and requires significant judgment at many points during the analysis. We determine the fair value of our reporting units by using a weighted combination of both market and an income approach, as this combination is deemed to be the most indicative of fair value in an orderly transaction between market participants.

Under the market approach, we use information regarding the reporting unit as well as publicly available industry information to determine various financial multiples to value our reporting units. Under the income approach, we determine fair value based on estimated future cash flows of each reporting unit, discounted by an estimated weighted-average cost of capital, which reflects the overall level of inherent risk of a reporting unit and the rate of return an outside investor would expect to earn.

In estimating the fair value of a reporting unit for the purposes of our annual or periodic analyses, we make estimates and judgments about the future cash flows of our reporting units, including estimated growth rates and assumptions about the economic environment. Although our cash flow forecasts are based on assumptions that are consistent with the plans and estimates we are using to manage the underlying businesses, there is significant judgment involved in determining the cash flows attributable to a reporting unit. In addition, we make certain judgments about allocating shared assets to the estimated balance sheets of our reporting units. We also consider our market capitalization and that of our competitors on the date we perform the analysis. Changes in judgment on these assumptions and estimates could result in a goodwill impairment charge.

As a result, several factors could result in impairment of a material amount of our goodwill balance in future periods, including, but not limited to: (1) weakening of the global economy, weakness in the semiconductor equipment industry, or failure of the Company to reach its internal forecasts, which could impact our ability to achieve our forecasted levels of cash flows and reduce the estimated discounted cash flow value of our reporting units; and (2) a decline in our stock price and resulting market capitalization, if we determine that the decline is sustained and indicates a reduction in the fair value of our reporting units below their carrying value. In addition, the value we assign to intangible assets, other than goodwill, is based on our estimates and judgments regarding expectations such as the success and life cycle of products and technology acquired. If actual product acceptance differs significantly from our estimates, we may be required to record an impairment charge to write down the asset to its realizable value.

### ***Recent Accounting Pronouncements***

In September 2009, the FASB ratified guidance from the Emerging Issues Task Force ( EITF ) regarding revenue arrangements with multiple deliverables. This guidance addresses criteria for separating the consideration in multiple-element arrangements and requires companies to allocate the overall consideration to each deliverable by using a best estimate of the selling price of individual deliverables in the arrangement in the absence of vendor-specific objective evidence or other third-party evidence of the selling price. We adopted this guidance on June 28, 2010, on a prospective basis, and the adoption did not have a significant impact on our results of operations or financial condition.

In September 2009, the FASB also ratified guidance from the EITF regarding certain revenue arrangements that include software elements. This guidance modifies the scope of the software revenue recognition rules to exclude (a) non-software components of tangible products and (b) software components of tangible products that are sold, licensed, or leased with tangible products when the software components and non-software components of the tangible product function together to deliver the tangible product s essential functionality. We adopted this guidance on June 28, 2010, on a prospective basis, and the adoption did not have a significant impact on our results of operations or financial condition.

### **LIQUIDITY AND CAPITAL RESOURCES**

As of September 26, 2010, we had \$1.1 billion in cash and cash equivalents, short-term investments, and restricted cash and investments (total cash and investments) compared to \$992 million as of June 27, 2010.



**Table of Contents*****Cash Flows from Operating Activities***

Net cash provided by operating activities of \$255.7 million during the three months ended September 26, 2010 consisted of (in millions):

|  |          |
|--|----------|
| Net income   | \$ 193.7 |
| Non-cash charges:                                  |          |
| Depreciation and amortization                      | 17.9     |
| Equity-based compensation                          | 13.0     |
| Restructuring charges, net                         | (5.2)    |
| Net tax benefit on equity-based compensation plans | 1.1      |
| Deferred income taxes                              | (0.8)    |
| Changes in operating asset and liability accounts  | 37.8     |
| Other  | (1.8)    |
|  | \$ 255.7 |

Changes in operating asset and liability accounts of \$37.8 million included the following sources of cash: decreases in prepaid and other assets of \$20.0 million, increases in accounts payable of \$22.2 million, increases in deferred profit of \$9.1 million, and increases in accrued expenses and other liabilities of \$35.2 million. These sources of cash were partially offset by the following uses of cash: increases in accounts receivable of \$22.2 million and inventory of \$19.8 million, and a \$6.6 million effect of foreign exchange rate changes on cash balances. These changes in overall cash were all consistent with increased business volumes.

***Cash Flows from Investing Activities***

Net cash used for investing activities during the three months ended September 26, 2010 was \$43.6 million, primarily consisting of capital expenditures of \$19.1 million and net purchases of available-for-sale securities of \$24.5 million.

***Cash Flows from Financing Activities***

Net cash used for financing activities during the three months ended September 26, 2010 was \$136.2 million, which included \$144.8 million in treasury stock purchases under a stock repurchase program authorized by our Board of Directors (see Note 15 of Notes to Consolidated Financial Statements) and \$3.3 million in principal payments on long-term debt and capital leases, partially offset by net proceeds from issuance of common stock related to employee equity-based plans of \$8.0 million and the effect of excess tax benefits on equity based compensation of \$3.9 million.

Given the cyclical nature of the semiconductor equipment industry, we believe that maintaining sufficient liquidity reserves is important to support sustaining levels of investment in R&D and capital infrastructure. Based upon our current business outlook, we expect that our levels of cash, cash equivalents, and short-term investments at September 26, 2010 will be sufficient to support our presently anticipated levels of operations, investments, debt service requirements, and capital expenditures, through at least the next 12 months.

In the longer term, liquidity will depend to a great extent on our future revenues and our ability to appropriately manage our costs based on demand for our products and services. If we require additional funding, we may need to raise the required funds through borrowings or public or private sales of debt or equity securities. We believe that, if necessary, we will be able to access the capital markets on terms and in amounts adequate to meet our objectives. However, given the possibility of changes in market conditions or other occurrences, there can be no certainty that such funding will be available in needed quantities or on terms favorable to us.

**Table of Contents*****Off-Balance Sheet Arrangements and Contractual Obligations***

We have certain obligations to make future payments under various contracts, some of which are recorded on our balance sheet and some of which are not. Obligations are recorded on our balance sheet in accordance with GAAP and include our long-term debt which is outlined in the following table and noted below. Our off-balance sheet arrangements include contractual relationships and are presented as operating leases and purchase obligations in the table below. Our contractual cash obligations and commitments as of September 26, 2010, relating to these agreements and our guarantees are included in the following table. The amounts in the table below exclude \$114.9 million of liabilities related to uncertain tax benefits as we are unable to reasonably estimate the ultimate amount or time of settlement.

|                                | Operating<br>Leases | Capital<br>Leases | Purchase<br>Obligations<br>(in thousands) | Long-term<br>Debt and<br>Interest Expense | Total      |
|--------------------------------|---------------------|-------------------|---|---|------------|
| <b>Payments due by period:</b> |                     |                   |   |   |            |
| Less than 1 year               | \$ 9,945            | \$ 1,742          | \$ 143,819                                | \$ 3,861                                  | \$ 159,367 |
| 1-3 years                      | 15,552              | 3,402             | 72,376                                    | 148                                       | 91,478     |
| 3-5 years                      | 150,326             | 2,888             | 32,946                                    |   | 186,160    |
| Over 5 years                   | 1,011               | 9,650             | 5,853                                     |   | 16,514     |
| Total                          | \$ 176,834          | \$ 17,682         | \$ 254,994                                | \$ 4,009                                  | \$ 453,519 |

***Operating Leases and Related Guarantees***

We lease most of our administrative, R&D and manufacturing facilities, regional sales/service offices and certain equipment under non-cancelable operating leases, which expire at various dates through fiscal year 2016. Certain of our facility leases for buildings located at our Fremont, California headquarters and certain other facility leases provide us with options to extend the leases for additional periods or to purchase the facilities. Certain of our facility leases provide for periodic rent increases based on the general rate of inflation.

Included in the Operating Leases 3-5 years section of the table above is \$141.7 million in guaranteed residual values for lease agreements relating to certain properties at our Fremont, California campus and properties in Livermore, California. The remaining operating lease balances primarily relate to non-cancelable facility-related operating leases.

***Capital Leases***

Capital leases reflect building and office equipment lease obligations. The amounts in the table above include the interest portion of payment obligations.

***Purchase Obligations***

Purchase obligations consist of significant contractual obligations either on an annual basis or over multi-year periods related to our outsourcing activities or other material commitments, including vendor-consigned inventories. We continue to enter into new agreements and maintain existing agreements to outsource certain activities, including elements of our manufacturing, warehousing, logistics, facilities maintenance, certain information technology functions, and certain transactional general and administrative functions. The contractual cash obligations and commitments table presented above contains our obligations at September 26, 2010 under these arrangements and others. Actual expenditures will vary based on the volume of transactions and length of contractual service provided. In addition to these obligations, certain of these agreements include early termination provisions and/or cancellation penalties which could increase or decrease amounts actually paid.

***Long-Term Debt***

Our remaining total long-term debt, excluding interest, of \$3.9 million as of September 26, 2010 consisted of various bank loans and government subsidized technology loans supporting operating needs.

*Other Guarantees*

We have issued certain indemnifications to our lessors for taxes and general liability under some of our agreements. We have entered into certain insurance contracts that may limit our exposure to such indemnifications. As of September 26, 2010, we had not recorded any liability on our consolidated financial statements in connection with these indemnifications, as we do not believe, based on information available, that it is probable that we will pay any amounts under these guarantees.

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Generally, we indemnify, under pre-determined conditions and limitations, our customers for infringement of third-party intellectual property rights by our products or services. We seek to limit our liability for such indemnity to an amount not to exceed the sales price of the products or services subject to its indemnification obligations. We do not believe, based on information available, that it is probable that we will pay any material amounts under these guarantees.

### ***Warranties***

We offer standard warranties on its systems that run generally for a period of 12 months from system acceptance. The liability amount is based on actual historical warranty spending activity by type of system, customer, and geographic region, modified for any known differences such as the impact of system reliability improvements.

### **ITEM 3. Quantitative and Qualitative Disclosures about Market Risk**

For financial market risks related to changes in interest rates and foreign currency exchange rates, refer to Part II, Item 7A, Quantitative and Qualitative Disclosures About Market Risk, in our 2010 Form 10-K.

Our exposure to market risk for changes in interest rates relates primarily to our investment portfolio, long-term debt, and synthetic leases. We maintain a conservative investment policy, which focuses on the safety and preservation of our invested funds by limiting default risk, market risk, and reinvestment risk. We mitigate default risk by investing in high credit quality securities and by positioning our portfolio to respond appropriately to a significant reduction in a credit rating of any investment issuer or guarantor. The portfolio includes only marketable securities with active secondary or resale markets to achieve portfolio liquidity and maintain a prudent amount of diversification.

We believe that maintaining sufficient liquidity reserves is important to support sustaining levels of investment in our business activities. Anticipated cash flows from operations based on our current business outlook, combined with our current levels of cash, cash equivalents, and short-term investments at September 26, 2010 are expected to be sufficient to support our anticipated levels of operations, investments, debt service requirements, and capital expenditures, through at least the next 12 months. However, uncertainty in the global economy and the semiconductor industry, as well as disruptions in credit markets have in the past, and could in the future, impact customer demand for our products, as well as our ability to manage normal commercial relationships with our customers, suppliers, and creditors.

### **ITEM 4. Controls and Procedures**

#### ***Disclosure Controls and Procedures***

As required by Exchange Act Rule 13a-15(b), as of September 26, 2010, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and our Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as defined in Rule 13a-15(e). Based upon that evaluation, our Chief Executive Officer, along with our Chief Financial Officer, concluded that our disclosure controls and procedures are effective at the reasonable assurance level.

We intend to review and evaluate the design and effectiveness of our disclosure controls and procedures on an ongoing basis and to correct any material deficiencies that we may discover. Our goal is to ensure that our senior management has timely access to material information that could affect our business.

#### ***Changes in Internal Control over Financial Reporting***

There has been no change in our internal control over financial reporting during our most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

#### ***Effectiveness of Controls***

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While we believe the present design of our disclosure controls and procedures and internal control over financial reporting is effective, future events affecting our business may cause us to modify our disclosure controls and procedures or internal control over financial reporting. The effectiveness of controls cannot be absolute because the cost to design and implement a control to identify errors or mitigate the risk of errors occurring should not outweigh the potential loss caused by the errors that would likely be detected by the control. Moreover, we believe that a control system cannot be guaranteed to be 100% effective all of the time. Accordingly, a control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met.

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**PART II. OTHER INFORMATION**

**ITEM 1. Legal Proceedings**

From time to time, we have received notices from third parties alleging infringement of such parties' patent or other intellectual property rights by our products. In such cases it is our policy to defend the claims, or if considered appropriate, negotiate licenses on commercially reasonable terms. However, no assurance can be given that we will be able in the future to negotiate necessary licenses on commercially reasonable terms, or at all, or that any litigation resulting from such claims would not have a material adverse effect on our consolidated financial position or operating results.

**ITEM 1A. Risk Factors**

In addition to the other information in this Form 10-Q, the following risk factors should be carefully considered in evaluating the Company and its business because such factors may significantly impact our business, operating results, and financial condition. As a result of these risk factors, as well as other risks discussed in our other SEC filings, our actual results could differ materially from those projected in any forward-looking statements. No priority or significance is intended, nor should be attached, to the order in which the risk factors appear.

***The Semiconductor Equipment Industry is Subject to Major Fluctuations and, as a Result, We Face Risks Related to Our Strategic Resource Allocation Decisions***

The business cycle in the semiconductor equipment industry has historically been characterized by frequent periods of rapid change in demand that challenge our management to adjust spending and other resources allocated to operating activities. During periods of rapid growth or decline in demand for our products and services, we face significant challenges in maintaining adequate financial and business controls, management processes, information systems, procedures for training, managing, and appropriately sizing our supply chain, our work force, and other components of our business on a timely basis.

If we do not adequately meet these challenges during periods of demand decline, our gross margins and earnings may be impaired. In late 2008 and throughout 2009, the semiconductor industry experienced a general decline in demand, leading to a steep decline in demand for our products and services. In response to that industry demand decline and in an effort to minimize the disruptive effects of the deteriorating economic conditions on our business operating results, we made difficult resource allocation decisions, including layoffs and restructurings.

During fiscal year 2010 we transitioned into a period of demand growth, although the duration and intensity of the growth in fiscal 2011 is still uncertain. This demand growth has been fueled in large part by increased investment by customers who, during the downturn, reduced or eliminated their spending on our products.

We continuously reassess our strategic resource allocation choices in response to the changing business environment. If we do not adequately adapt to the changing business environment, we may lack the infrastructure and resources to scale up our business to meet customer expectations and compete successfully during this period of growth, or we may expand our capacity too rapidly and/or beyond what is appropriate for the actual demand environment.

Especially during transitional periods, resource allocation decisions can have a significant impact on our future performance, particularly if we have not accurately anticipated industry changes. Our success will depend, to a significant extent, on the ability of our executive officers and other members of our senior management to identify and respond to these challenges effectively.

***Future Declines in the Semiconductor Industry, and the Overall World Economic Conditions on Which it is Significantly Dependent, Could Have a Material Adverse Impact on Our Results of Operations and Financial Condition***

Our business depends on the capital equipment expenditures of semiconductor manufacturers, which in turn depend on the current and anticipated market demand for integrated circuits. The semiconductor industry is cyclical in nature and historically experiences periodic downturns. Global economic and business conditions, which are often unpredictable, have historically impacted customer demand for our products and normal commercial relationships with our customers, suppliers, and creditors. Additionally, in times of economic uncertainty, some



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of our customers' budgets for our products, or their ability to access credit to purchase them, could be adversely affected. This would limit their ability to purchase our products and services. As a result, economic downturns can cause material adverse changes to our results of operations and financial condition including, but not limited to:

a decline in demand for our products;

an increase in reserves on accounts receivable due to our customers' inability to pay us;

an increase in reserves on inventory balances due to excess or obsolete inventory as a result of our inability to sell such inventory;

valuation allowances on deferred tax assets;

restructuring charges;

asset impairments including the potential impairment of goodwill and other intangible assets;

a decline in the value of our investments;

exposure to claims from our suppliers for payment on inventory that is ordered in anticipation of customer purchases that do not come to fruition;

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a decline in value of certain facilities we lease to less than our residual value guarantee with the lessor; and

challenges maintaining reliable and uninterrupted sources of supply.

Fluctuating levels of investment by semiconductor manufacturers may materially affect our aggregate shipments, revenues and operating results. Where appropriate, we will attempt to respond to these fluctuations with cost management programs aimed at aligning our expenditures with anticipated revenue streams, which sometimes result in restructuring charges. Even during periods of reduced revenues, we must continue to invest in R&D and maintain extensive ongoing worldwide customer service and support capabilities to remain competitive, which may temporarily harm our profitability and other financial results.

***Our Quarterly Revenues and Operating Results Are Unpredictable***

Our revenues and operating results may fluctuate significantly from quarter to quarter due to a number of factors, not all of which are in our control. We manage our expense levels based in part on our expectations of future revenues. Because our operating expenses are based in part on anticipated future revenues, and a certain amount of those expenses are relatively fixed, a change in the timing of recognition of revenue and/or the level of gross profit from a small number of transactions can unfavorably affect operating results in a particular quarter. Factors that may cause our financial results to fluctuate unpredictably include, but are not limited to:

economic conditions in the electronics and semiconductor industries in general and specifically the equipment industry;

the size and timing of orders from customers;

procurement shortages;

the failure of our suppliers or outsource providers to perform their obligations in a manner consistent with our expectations;

manufacturing difficulties;

customer cancellations or delays in shipments, installations, and/or customer acceptances;

the extent that customers continue to purchase and use our products and services in their business;

changes in average selling prices, customer mix, and product mix;

our ability in a timely manner to develop, introduce and market new, enhanced, and competitive products;

our competitors' introduction of new products;

legal or technical challenges to our products and technology;

transportation, communication, demand, information technology or supply disruptions based on factors outside our control such as acts of God, wars, terrorist activities, and natural disasters;

natural, physical, logistical or other events or disruptions affecting our principal facilities (including labor disruptions, facility relocations or expansions, earthquakes, and power failures)

legal, tax, accounting, or regulatory changes (including but not limited to change in import/export regulations) or changes in the interpretation or enforcement of existing requirements;

changes in our estimated effective tax rate; and

foreign currency exchange rate fluctuations.

***We Derive Our Revenues Primarily from a Relatively Small Number of High-Priced Systems***

System sales constitute a significant portion of our total revenue. Our systems are priced up to approximately \$6 million per unit, and our revenues in any given quarter are dependent upon the acceptance of a limited number of systems. As a result, the inability to recognize revenue on even a few systems can cause a significantly adverse impact on our revenues for that quarter.

***We Have a Limited Number of Key Customers***

Sales to a limited number of large customers constitute a significant portion of our overall revenue, shipments and profitability. As a result, the actions of even one customer may subject us to variability in those areas that are difficult to predict. In addition, large customers may be able to negotiate requirements that result in increased costs and/or lower margins for us. Similarly, significant portions of our credit risk may, at any given time, be concentrated among a limited number of customers, so that the failure of even one of these key customers to pay its obligations to us could significantly impact our financial results.

***Variations in the Amount of Time it Takes for Our Customers to Accept Our Systems May Cause Fluctuation in Our Operating Results***

We generally recognize revenue for new system sales on the date of customer acceptance or the date the contractual customer acceptance provisions lapse. As a result, the fiscal period in which we are able to recognize new systems revenues is typically subject to the length of time that our customers require to evaluate the performance of our equipment after shipment and installation, which may vary from customer to customer and tool to tool. Such variations could cause our quarterly operating results to fluctuate.

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### ***We Depend on New Products and Processes for Our Success. Consequently, We are Subject to Risks Associated with Rapid Technological Change***

Rapid technological changes in semiconductor manufacturing processes subject us to increased pressure to develop technological advances that enable those processes. We believe that our future success depends in part upon our ability to develop and offer new products with improved capabilities and to continue to enhance our existing products. If new products have reliability, quality, or design problems, our performance may be impacted by reduced orders, higher manufacturing costs, delays in acceptance of and payment for new products, and additional service and warranty expenses. We may be unable to develop and manufacture new products successfully, or new products that we introduce may fail in the marketplace. Our failure to commercialize these new products in a timely manner could result in unanticipated costs and inventory obsolescence, which would adversely affect our financial results.

In order to develop new products and processes, we expect to continue to make significant investments in R&D and to pursue joint development relationships with customers, suppliers or other members of the industry. We must manage product transitions and joint development relationships successfully, as the introduction of new products could adversely affect our sales of existing products. Moreover, future technologies, processes or product developments may render our current product offerings obsolete, leaving us with non-competitive products, or obsolete inventory, or both.

### ***We are Subject to Risks Relating to Product Concentration and Lack of Product Revenue Diversification***

We derive a substantial percentage of our revenues from a limited number of products, and we expect our etch and clean products to continue to account for a large percentage of our revenues in the near term. Continued market acceptance of these products is, therefore, critical to our future success. Our business, operating results, financial condition, and cash flows could therefore be adversely affected by:

a decline in demand for even a limited number of our products;

a failure to achieve continued market acceptance of our key products;

export restrictions or other regulatory or legislative actions that could limit our ability to sell those products to key customer or market segments;

an improved version of products being offered by a competitor in the market in which we participate;

increased pressure from competitors that offer broader product lines;

technological changes that we are unable to address with our products; or

a failure to release new or enhanced versions of our products on a timely basis.

In addition, the fact that we offer limited product lines creates the risk that our customers may view us as less important to their business than our competitors that offer additional products as well. This may impact our ability to maintain or expand our business with certain customers. Such product concentration may also subject us to additional risks associated with technology changes. Since we are a provider of etch and clean equipment, our business is affected by our customers' use of etching and clean steps in their processes. Should technologies change so that the manufacture of semiconductor chips requires fewer etching or clean steps, this could have a larger impact on our business than it would on the business of our less concentrated competitors.

***Strategic Alliances May Have Negative Effects on Our Business***

Increasingly, semiconductor companies are entering into strategic alliances with one another to expedite the development of processes and other manufacturing technologies. Often, one of the outcomes of such an alliance is the definition of a particular tool set for a certain function or a series of process steps that use a specific set of manufacturing equipment. While this could work to our advantage if our equipment becomes the basis for the function or process, it could work to our disadvantage if a competitor's tools or equipment become the standard equipment for such function or process. In the latter case, even if our equipment was previously used by a customer, that equipment may be displaced in current and future applications by the tools standardized by the alliance.

Similarly, our customers may team with, or follow the lead of, educational or research institutions that establish processes for accomplishing various tasks or manufacturing steps. If those institutions utilize a competitor's equipment when they establish those processes, it is likely that customers will tend to use the same equipment in setting up their own manufacturing lines. These actions could adversely impact our market share and financial results.

***We are Dependent On a Limited Number of Key Suppliers***

We obtain certain components and sub-assemblies included in our products from a single supplier or a limited group of suppliers. We have established long-term contracts with many of these suppliers. These long-term contracts can take a variety of forms. We may renew these contracts periodically. In some cases, these suppliers have sold us products during at least the last five years, and we expect that we will continue to renew these contracts in the future or that we will otherwise replace them with competent alternative suppliers. However, certain of our suppliers are relatively new providers to us so that our experience with them and their performance is limited. Where practical, we intend to establish alternative sources to mitigate the risk that the failure of any single supplier will adversely affect our business. Nevertheless, a prolonged inability to obtain certain components could impair our ability to ship products and generate revenues, which could adversely affect our operating results and damage to our customer relationships.

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### ***Our Outsource Providers May Fail to Perform as We Expect***

Outsource providers have played and will continue to play a key role in our manufacturing operations and in many of our transactional and administrative functions, such as information technology, facilities management, and certain elements of our finance organization. Although we attempt to select reputable providers and secure their performance on terms documented in written contracts, it is possible that one or more of these providers could fail to perform as we expect and such failure could have an adverse impact on our business.

In addition, the expansive role of our outsource providers has required and may continue to require us to implement changes to our existing operations and to adopt new procedures to deal with and manage the performance of these outsource providers. Any delay or failure in the implementation of our operational changes and new procedures could adversely affect our customer and/or employee relationships, which could have a negative effect on our operating results.

### ***Once a Semiconductor Manufacturer Commits to Purchase a Competitor's Semiconductor Manufacturing Equipment, the Manufacturer Typically Continues to Purchase that Competitor's Equipment, Making it More Difficult for Us to Sell Our Equipment to that Customer***

Semiconductor manufacturers must make a substantial investment to qualify and integrate wafer processing equipment into a semiconductor production line. We believe that once a semiconductor manufacturer selects a particular supplier's processing equipment, the manufacturer generally relies upon that equipment for that specific production line application for an extended period of time. Accordingly, we expect it to be more difficult to sell to a given customer if that customer initially selects a competitor's equipment.

### ***We Face a Challenging and Complex Competitive Environment***

We face significant competition from multiple competitors. Other companies continue to develop systems and products that are competitive to ours and may introduce new products, which may affect our ability to sell our existing products. We face a greater risk if our competitors enter into strategic relationships with leading semiconductor manufacturers covering products similar to those we sell or may develop, as this could adversely affect our ability to sell products to those manufacturers.

We believe that to remain competitive we must devote significant financial resources to offer a broad range of products, to maintain customer service and support centers worldwide, and to invest in product and process R&D. Certain of our competitors, especially those that are created and financially backed by foreign governments, have substantially greater financial resources and more extensive engineering, manufacturing, marketing, and customer service and support resources than we do and therefore have the potential to increasingly dominate the semiconductor equipment industry. These competitors may deeply discount or give away products similar to those that we sell, challenging or even exceeding our ability to make similar accommodations and threatening our ability to sell those products. We also face competition from our own customers, who in some instances have established affiliated entities that manufacture equipment similar to ours. For these reasons, we may fail to continue to compete successfully worldwide.

In addition, our competitors may be able to develop products comparable or superior to those we offer or may adapt more quickly to new technologies or evolving customer requirements. In particular, while we continue to develop product enhancements that we believe will address future customer requirements, we may fail in a timely manner to complete the development or introduction of these additional product enhancements successfully, or these product enhancements may not achieve market acceptance or be competitive. Accordingly, competition may intensify and we may be unable to continue to compete successfully in our markets, which could have a material adverse effect on our revenues, operating results, financial condition, and/or cash flows.

### ***Our Future Success Depends on International Sales and the Management of Global Operations***

Non-U.S. sales accounted for approximately 95% of total revenue in the September 2010 quarter, 91% of total revenue in fiscal year 2010, 85% of total revenue in fiscal year 2009, and 83% in fiscal year 2008. We expect that international sales will continue to account for a substantial portion of our total revenue in future years.

We are subject to various challenges related to international sales and the management of global operations including, but not limited to:

trade balance issues;

global economic and political conditions;

changes in currency controls;

differences in the enforcement of intellectual property and contract rights in varying jurisdictions;

our ability to respond to customer demands for locally sourced systems, spare parts and services and develop the necessary relationships with local suppliers;

compliance with U.S. and international laws and regulations affecting foreign operations, including U.S. export restrictions;

fluctuations in interest and foreign currency exchange rates;

the need for technical support resources in different locations; and

our ability to secure and retain qualified people in all necessary locations for the successful operation of our business.

Certain international sales depend on our ability to obtain export licenses from the U.S. government. Our failure or inability to obtain such licenses would substantially limit our markets and severely restrict our revenues. Many of the challenges noted above are applicable in China, which is a fast developing market for the semiconductor equipment industry and therefore an area of potential significant growth for our business. As the business volume between China and the rest of the world grows, there is inherent risk, based on the complex relationships among China, Taiwan, Japan, and the United States, that political and diplomatic influences might lead to trade disruptions; this would adversely affect our business with China and/or Taiwan and perhaps the entire Asia Pacific region. A significant trade disruption in these areas could have a materially adverse impact on our future revenue and profits.

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We are potentially exposed to adverse as well as beneficial movements in foreign currency exchange rates. The majority of our sales and expenses are denominated in U.S. dollars. However, we are exposed to foreign currency exchange rate fluctuations related to certain of our revenues denominated in Japanese yen and Euros, as well as certain of our spares and service contracts, Euro denominated expenses, and expenses related to our non-U.S. sales and support offices that are denominated in the related countries' local currency.

We currently enter into foreign exchange forward contracts to minimize the short-term impact of the foreign currency exchange rate fluctuations on Japanese yen-denominated revenue and monetary assets and liabilities, Euro-denominated operating expenses and monetary assets and liabilities, as well as monetary assets and liabilities denominated in Swiss francs and Taiwanese dollars. We currently believe these are our primary exposures to currency rate fluctuation. We expect to continue to enter into hedging transactions, for the purposes outlined, in the foreseeable future. However, these hedging transactions may not achieve their desired effect because differences between the actual timing of customer acceptances and our forecasts of those acceptances may leave us either over- or under-hedged on any given transaction. Moreover, by hedging these foreign currency denominated revenues, monetary assets and liabilities with foreign exchange forward contracts, we may miss favorable currency trends that would have been advantageous to us but for the hedges. Additionally, we are exposed to short-term foreign currency exchange rate fluctuations on non-U.S. dollar-denominated assets and liabilities (other than those currency exposures previously discussed) and currently we do not enter into foreign exchange forward contracts to hedge these other foreign currency exposures. Therefore, we are subject to both favorable and unfavorable foreign currency exchange rate fluctuations to the extent that we transact business (including intercompany transactions) in other currencies.

***Our Ability To Attract, Retain and Motivate Key Employees Is Critical To Our Success.***

Our ability to compete successfully depends in large part on our ability to attract, retain and motivate key employees. This is an ongoing challenge due to intense competition for top talent, as well as fluctuations in industry economic conditions that may require cycles of hiring activity and workforce reductions. Our success in hiring depends on a variety of factors, including the attractiveness of our compensation and benefit programs and our ability to offer a challenging and rewarding work environment. We periodically evaluate our overall compensation programs and make adjustments, as appropriate, to maintain or enhance their competitiveness. If we are not able to successfully attract, retain and motivate key employees, we may be unable to capitalize on market opportunities and our operating results may be materially and adversely affected.

***We Rely Upon Certain Critical Information Systems for the Operation of Our Business***

We maintain and rely upon certain critical information systems for the effective operation of our business. These information systems include telecommunications, the internet, our corporate intranet, various computer hardware and software applications, network communications, and e-mail. These information systems may be owned and maintained by us, our outsource providers or third parties such as vendors and contractors. These information systems are subject to attacks, failures, and access denials from a number of potential sources including viruses, destructive or inadequate code, power failures, and physical damage to computers, hard drives, communication lines, and networking equipment. To the extent that these information systems are under our control, we have implemented security procedures, such as virus protection software and emergency recovery processes, to mitigate the outlined risks. However, security procedures for information systems cannot be guaranteed to be failsafe and our inability to use or access these information systems at critical points in time could unfavorably impact the timely and efficient operation of our business.

***Our Financial Results May be Adversely Impacted by Higher Than Expected Tax Rates or Exposure to Additional Tax Liabilities***

As a global company, our effective tax rate is highly dependent upon the geographic composition of worldwide earnings and tax regulations governing each region. We are subject to income taxes in the United States and various foreign jurisdictions, and significant judgment is required to determine worldwide tax liabilities. Our effective tax rate could be adversely affected by changes in the split of earnings between countries with differing statutory tax rates, in the valuation of deferred tax assets, in tax laws, or by material audit assessments. These factors could affect our profitability. In particular, the carrying value of deferred tax assets, which are predominantly in the United States, is dependent on our ability to generate future taxable income in the United States. In addition, the amount of income taxes we pay is subject to ongoing audits in various jurisdictions, and a material assessment by a governing tax authority could affect our profitability.

***A Failure to Comply with Environmental Regulations May Adversely Affect Our Operating Results***

We are subject to a variety of governmental regulations related to the discharge or disposal of toxic, volatile or otherwise hazardous chemicals. We believe that we are generally in compliance with these regulations and that we have obtained (or will obtain or are otherwise addressing the



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need for) all environmental permits necessary to conduct our business. These permits generally relate to the disposal of hazardous wastes. Nevertheless, the failure to comply with present or future regulations could result in fines being imposed on us, require us to suspend production, or cease operations or cause our customers to not accept our products. These regulations could require us to alter our current operations, to acquire significant additional equipment or to incur substantial other expenses to comply with environmental regulations. Our failure to control the use, sale, transport or disposal of hazardous substances could subject us to future liabilities.

### ***If We Choose to Acquire or Dispose of Product Lines and Technologies, We May Encounter Unforeseen Costs and Difficulties That Could Impair Our Financial Performance***

An important element of our management strategy is to review acquisition prospects that would complement our existing products, augment our market coverage and distribution ability, or enhance our technological capabilities. As a result, we may make acquisitions of complementary

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companies, products or technologies, such as our March 2008 acquisition of SEZ Holding AG ( SEZ ), or we may reduce or dispose of certain product lines or technologies that no longer fit our long-term strategies. Managing an acquired business, disposing of product technologies or reducing personnel entail numerous operational and financial risks, including difficulties in assimilating acquired operations and new personnel or separating existing business or product groups, diversion of management's attention away from other business concerns, amortization of acquired intangible assets and potential loss of key employees or customers of acquired or disposed operations. There can be no assurance that we will be able to achieve and manage successfully any such integration of potential acquisitions, disposition of product lines or technologies, or reduction in personnel or that our management, personnel, or systems will be adequate to support continued operations. Any such inability or inadequacies could have a material adverse effect on our business, operating results, financial condition, and cash flows.

In addition, any acquisition could result in changes such as potentially dilutive issuances of equity securities, the incurrence of debt and contingent liabilities, the amortization of related intangible assets, and goodwill impairment charges, any of which could materially adversely affect our business, financial condition, and results of operations and/or the price of our Common Stock.

### ***The Market for Our Common Stock is Volatile, Which May Affect Our Ability to Raise Capital or Make Acquisitions***

The market price for our Common Stock is volatile and has fluctuated significantly over the past years. The trading price of our Common Stock could continue to be highly volatile and fluctuate widely in response to a variety of factors, many of which are not within our control or influence. These factors include but are not limited to the following:

general market, semiconductor, or semiconductor equipment industry conditions;

economic or political events and trends occurring globally or in any of our key sales regions;

variations in our quarterly operating results and financial condition, including our liquidity;

variations in our revenues, earnings or other business and financial metrics from forecasts by us or securities analysts, or from those experienced by other companies in our industry;

announcements of restructurings, reductions in force, departure of key employees, and/or consolidations of operations;

government regulations;

developments in, or claims relating to, patent or other proprietary rights;

technological innovations and the introduction of new products by us or our competitors;

commercial success or failure of our new and existing products; or

disruptions of relationships with key customers or suppliers.

In addition, the stock market experiences significant price and volume fluctuations. Historically, we have witnessed significant volatility in the price of our Common Stock due in part to the actual or anticipated movement in interest rates and the price of and markets for semiconductors. These broad market and industry factors have and may again adversely affect the price of our Common Stock, regardless of our actual operating

performance. In the past, following volatile periods in the price of their stock, many companies became the object of securities class action litigation. If we are sued in a securities class action, we could incur substantial costs, and it could divert management's attention and resources and have an unfavorable impact on our financial performance and the price for our Common Stock.

***Intellectual Property, Indemnity and Other Claims Against Us Can be Costly and We Could Lose Significant Rights That are Necessary to Our Continued Business and Profitability***

Third parties may assert infringement, unfair competition, product liability, breach of contract, or other claims against us. From time to time, other parties send us notices alleging that our products infringe their patent or other intellectual property rights. In addition, law enforcement authorities may seek criminal charges relating to intellectual property issues. We also face risks of claims from commercial and other relationships. In addition, our Bylaws and indemnity obligations provide that we will indemnify officers and directors against losses that they may incur in legal proceedings resulting from their service to Lam Research. In such cases, it is our policy either to defend the claims or to negotiate licenses or other settlements on commercially reasonable terms. However, we may be unable in the future to negotiate necessary licenses or reach agreement on other settlements on commercially reasonable terms, or at all, and any litigation resulting from these claims by other parties may materially adversely affect our business and financial results. Moreover, although we seek to obtain insurance to protect us from claims and cover losses to our property, there is no guarantee that such insurance will fully compensate us for any losses that we may incur.

***We May Fail to Protect Our Critical Proprietary Technology Rights, Which Could Affect Our Business***

Our success depends in part on our proprietary technology and our ability to protect key components of that technology through patents, copyrights and trade secret protection. Protecting our key proprietary technology helps us to achieve our goals of developing technological expertise and new products and systems that give us a competitive advantage; increasing market penetration and growth of our installed base; and providing comprehensive support and service to our customers. As part of our strategy to protect our technology we currently hold a number of United States and foreign patents and pending patent applications. However, other parties may challenge or attempt to invalidate or circumvent any patents the United States or foreign governments issue to us or these governments may fail to issue patents for pending applications. Additionally, even when patents are issued, the legal systems in certain of the countries in which we do business do not enforce patents and other intellectual property rights as rigorously as the United States. The rights granted or anticipated under any of our patents or pending patent applications may be narrower than we expect or, in fact, provide no competitive advantages. Any of these circumstances could have a material adverse impact on our business if they relate to critical technologies.

**Table of Contents*****Compliance with Federal Securities Laws, Rules and Regulations, as well As NASDAQ Requirements, has Become Increasingly Complex, and the Significant Attention and Expense We Must Devote to those Areas May Have an Adverse Impact on Our Business***

Federal securities laws, rules and regulations, as well as NASDAQ rules and regulations, require companies to maintain extensive corporate governance measures, impose comprehensive reporting and disclosure requirements, set strict independence and financial expertise standards for audit and other committee members and impose civil and criminal penalties for companies and their chief executive officers, chief financial officers and directors for securities law violations. These laws, rules and regulations have increased, and in the future are expected to continue to increase, the scope, complexity and cost of our corporate governance, reporting and disclosure practices, which could harm our results of operations and divert management's attention from business operations. A failure to comply with these regulations could also have a material adverse effect on our business.

**ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds**

(c) On September 8, 2008, the Company announced that its Board of Directors had authorized the repurchase of up to \$250 million of Company common stock from the public market or in private purchases. While the repurchase program does not have a defined termination date, it may be suspended or discontinued at any time and will be funded using the Company's available cash. The Company temporarily suspended repurchases under the program during the December 2008 quarter. On February 2, 2010, the Board of Directors authorized the resumption of the repurchase program. The Company completed the repurchase of all amounts available under this share repurchase authorizations during the quarter ended September 26, 2010.

On September 10, 2010, the Company announced that its Board of Directors had authorized the repurchase of up to an additional \$250 million of Company common stock using the Company's available cash. These repurchases could be conducted on the open market or as private purchases and may include the use of derivative contracts with large financial institutions. The repurchase program does not have a defined termination date, and it may be suspended or discontinued at any time.

Repurchases under the repurchase program and net share settlements were as follows during the periods indicated:

| Period  | Total Number of Shares Repurchased(1) | Average Price Paid Per Share<br>(in thousands, except per share data) | Total Number of Shares Purchased as Part of Publicly Announced Plan or Program | Amount Available Under Repurchase Program |
|---|---------------------------------------|---|--|---|
| Amount available at June 27, 2010                     |                                       |   |  | \$ 130,693                                |
| June 28, 2010 - August 4, 2010                        | 1,823                                 | \$ 38.66  | 1,821  | \$ 60,278                                 |
| August 5, 2010 - August 22, 2010                      | 1,569                                 | \$ 38.45  | 1,568  | \$  |
| Authorization of up to \$250 million - September 2010 |                                       |   |  | \$ 250,000                                |
| August 23, 2010 - September 26, 2010                  | 16                                    | \$ 36.82  |  | \$ 250,000                                |
| Total   | 3,408                                 | \$ 38.56  | 3,389  |   |

- (1) In addition to shares repurchased under Board authorized repurchase program and included in this column are 18,000 shares which the Company withheld through net share settlements during the three months ended September 26, 2010 to cover tax withholding obligations upon the vesting of restricted stock unit awards granted under the Company's equity compensation plans. The shares retained by the Company through these net share settlements are not a part of the Board-authorized repurchase program but instead are authorized under the Company's equity compensation plans.

**ITEM 3. Defaults Upon Senior Securities**

None

**ITEM 4. (Removed and Reserved)**

**ITEM 5. Other Information**

None

**ITEM 6. Exhibits**

(a) Exhibits

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**LAM RESEARCH CORPORATION**

**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.

Date: November 3, 2010

LAM RESEARCH CORPORATION

(Registrant)

/s/ ERNEST E. MADDOCK

**Ernest E. Maddock**  
**Senior Vice President, Chief Financial Officer**

**(Principal Financial Officer and Principal Accounting  
Officer)**

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**EXHIBIT INDEX**

| <b>Exhibit<br/>Number</b> | <b>Description</b>   |
|---------------------------|--|
| 31.1                      | Rule 13a-14(a)/15d-14(a) Certification (Principal Executive Officer) |
| 31.2                      | Rule 13a-14(a)/15d-14(a) Certification (Principal Financial Officer) |
| 32.1                      | Section 1350 Certification (Principal Executive Officer)             |
| 32.2                      | Section 1350 Certification (Principal Financial Officer)             |
| 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               |