

LSI CORP
Form 10-Q
November 10, 2011
Table of Contents

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 October 2, 2011

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: 1-10317

LSI CORPORATION

(Exact name of registrant as specified in its charter)

Delaware
(State of Incorporation)

94-2712976
(I.R.S. Employer Identification Number)

1621 Barber Lane

Milpitas, California 95035

(Address of principal executive offices)

(Zip code)

Edgar Filing: LSI CORP - Form 10-Q

(408) 433-8000

(Registrant's telephone number, including area code)

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

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

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

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

(Do not check if a smaller reporting company.)

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

As of November 4, 2011, there were 563,488,950 shares of the registrant's Common Stock, \$.01 par value, outstanding.

Table of Contents

LSI CORPORATION

FORM 10-Q

For the Quarter Ended October 2, 2011

INDEX

	Page
	No.
<u>PART I. FINANCIAL INFORMATION</u>	
<u>Item 1. Financial Statements (Unaudited)</u>	3
<u>Condensed Consolidated Balance Sheets as of October 2, 2011 and December 31, 2010</u>	3
<u>Condensed Consolidated Statements of Operations for the three and nine months ended October 2, 2011 and October 3, 2010</u>	4
<u>Condensed Consolidated Statements of Cash Flows for the nine months ended October 2, 2011 and October 3, 2010</u>	5
<u>Notes to Condensed Consolidated Financial Statements</u>	6
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	19
<u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u>	28
<u>Item 4. Controls and Procedures</u>	28
<u>PART II. OTHER INFORMATION</u>	
<u>Item 1. Legal Proceedings</u>	29
<u>Item 1A. Risk Factors</u>	29
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	30
<u>Item 6. Exhibits</u>	30
<u>Signatures</u>	31
<u>Exhibit Index</u>	32
<u>EX-31.1</u>	
<u>EX-31.2</u>	
<u>EX-32.1</u>	
<u>EX-32.2</u>	
<u>EX-101 INSTANCE DOCUMENT</u>	
<u>EX-101 SCHEMA DOCUMENT</u>	
<u>EX-101 CALCULATION LINKBASE DOCUMENT</u>	
<u>EX-101 DEFINITION LINKBASE DOCUMENT</u>	
<u>EX-101 LABELS LINKBASE DOCUMENT</u>	
<u>EX-101 PRESENTATION LINKBASE DOCUMENT</u>	

FORWARD-LOOKING STATEMENTS

This Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. The words estimate, plan, intend, expect, anticipate, believe and similar words are intended to identify forward-looking statements. Although we believe our expectations are based on reasonable assumptions, our actual results could differ materially from those projected in the forward-looking statements. We have described in Part II, Item 1A. Risk Factors a number of factors that could cause our actual results to differ from our projections or estimates. Except where otherwise indicated, the statements made in this report are made as of the date we filed this report with the Securities and Exchange Commission and should not be relied upon as of any subsequent date. We expressly disclaim any obligation to update the information in this report, except as may otherwise be required by law.

Table of Contents**PART I FINANCIAL INFORMATION****Item 1. Financial Statements****LSI CORPORATION****CONDENSED CONSOLIDATED BALANCE SHEETS****(In thousands, except per share amounts)****(Unaudited)**

	October 2, 2011	December 31, 2010
ASSETS		
Cash and cash equivalents	\$ 725,150	\$ 521,786
Short-term investments	153,719	154,880
Accounts receivable, less allowances of \$7,208 and \$9,701, respectively	248,389	326,604
Inventories	210,434	186,772
Prepaid expenses and other current assets	74,761	73,314
Assets held for sale	16,619	464
Total current assets	1,429,072	1,263,820
Property and equipment, net	176,669	223,181
Identified intangible assets, net	462,463	561,137
Goodwill	72,377	188,698
Other assets	132,499	188,076
Total assets	\$ 2,273,080	\$ 2,424,912
LIABILITIES AND STOCKHOLDERS EQUITY		
Accounts payable	\$ 173,753	\$ 173,919
Accrued salaries, wages and benefits	108,700	126,307
Other accrued liabilities	181,961	184,402
Total current liabilities	464,414	484,628
Pension and post-retirement benefit obligations	409,692	463,119
Income taxes payable non-current	86,684	85,717
Other non-current liabilities	37,311	73,946
Total liabilities	998,101	1,107,410
Commitments and contingencies (Note 14)		
Stockholders' equity:		
Preferred stock, \$.01 par value: 2,000 shares authorized; none outstanding		
Common stock, \$.01 par value: 1,300,000 shares authorized; 563,347 and 615,191 shares outstanding, respectively	5,633	6,152
Additional paid-in capital	5,623,920	5,998,137
Accumulated deficit	(4,035,245)	(4,368,522)
Accumulated other comprehensive loss	(319,329)	(318,265)
Total stockholders' equity	1,274,979	1,317,502

Edgar Filing: LSI CORP - Form 10-Q

Total liabilities and stockholders' equity	\$ 2,273,080	\$ 2,424,912
--	--------------	--------------

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

Table of Contents**LSI CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS****(In thousands, except per share amounts)****(Unaudited)**

	Three Months Ended		Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
Revenues	\$ 546,910	\$ 452,878	\$ 1,520,818	\$ 1,398,997
Cost of revenues	283,065	234,658	795,179	741,215
Gross profit	263,845	218,220	725,639	657,782
Research and development	143,347	140,517	431,567	422,250
Selling, general and administrative	77,874	69,205	218,534	209,720
Restructuring of operations and other items, net	10,784	3,538	2,686	10,244
Income from operations	31,840	4,960	72,852	15,568
Interest expense				(5,601)
Interest income and other, net	7,610	10,315	18,348	6,147
Income from continuing operations before income taxes	39,450	15,275	91,200	16,114
Provision for/(benefit from) income taxes	7,800	2,456	12,596	(13,735)
Income from continuing operations	31,650	12,819	78,604	29,849
(Loss)/income from discontinued operations (including a gain on disposal of \$260,066 for the nine months ended October 2, 2011), net of taxes	(2,311)	10,602	254,673	23,524
Net income	\$ 29,339	\$ 23,421	\$ 333,277	\$ 53,373
Basic income per share:				
Income from continuing operations	\$ 0.05	\$ 0.02	\$ 0.13	\$ 0.04
(Loss)/income from discontinued operations	\$ (0.00)	\$ 0.02	\$ 0.43	\$ 0.04
Net income	\$ 0.05	\$ 0.04	\$ 0.56	\$ 0.08
Diluted income per share:				
Income from continuing operations	\$ 0.05	\$ 0.02	\$ 0.13	\$ 0.04
(Loss)/income from discontinued operations	\$ (0.00)	\$ 0.02	\$ 0.42	\$ 0.04
Net income	\$ 0.05	\$ 0.04	\$ 0.55	\$ 0.08
Shares used in computing per share amounts:				
Basic	567,790	629,852	592,898	646,167
Diluted	581,483	633,731	608,743	653,685

Edgar Filing: LSI CORP - Form 10-Q

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

Table of Contents**LSI CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(In thousands)****(Unaudited)**

	Nine Months Ended	
	October 2, 2011	October 3, 2010
Operating activities:		
Net income	\$ 333,277	\$ 53,373
Adjustments:		
Depreciation and amortization	145,843	200,718
Stock-based compensation expense	38,480	51,884
Non-cash restructuring of operations and other items, net	30,535	(41)
Write-down of investments, net of gain on sale		6,779
Gain on sale of business	(260,066)	
(Gain)/loss on sale of property and equipment	(543)	153
Unrealized foreign exchange loss	200	6,374
Deferred taxes	(18,944)	34
Changes in assets and liabilities:		
Accounts receivable, net	78,215	25,094
Inventories	(60,203)	(50,785)
Prepaid expenses, assets held for sale and other assets	(10,256)	13,898
Accounts payable	(1,700)	(23,541)
Accrued and other liabilities	(83,479)	(28,405)
Net cash provided by operating activities	191,359	255,535
Investing activities:		
Purchases of debt securities available-for-sale	(38,683)	(24,218)
Proceeds from maturities and sales of debt securities available-for-sale	31,988	36,209
Purchases of other investments	(4,000)	(316)
Proceeds from sale of other investments		9,795
Purchases of property and equipment	(46,841)	(67,262)
Proceeds from sale of property and equipment	939	559
Proceeds from sale of business, net of transaction costs	475,150	
Net cash provided by/(used in) investing activities	418,553	(45,233)
Financing activities:		
Redemption of convertible subordinated notes		(349,999)
Issuances of common stock	66,060	22,057
Purchase of common stock under repurchase programs	(471,787)	(217,743)
Net cash used in financing activities	(405,727)	(545,685)
Effect of exchange rate changes on cash and cash equivalents	(821)	(3,927)
Net change in cash and cash equivalents	203,364	(339,310)
Cash and cash equivalents at beginning of period	521,786	778,291

Edgar Filing: LSI CORP - Form 10-Q

Cash and cash equivalents at end of period	\$ 725,150	\$ 438,981
--	------------	------------

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

Table of Contents

LSI CORPORATION

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1 Basis of Presentation

For financial reporting purposes, LSI Corporation (LSI or the Company) reports on a 13- or 14-week quarter with the year ending December 31. The third quarter of 2011 and 2010 consisted of 13 weeks each and ended on October 2, 2011 and on October 3, 2010, respectively. The first nine months of 2011 and 2010 consisted of approximately 39 weeks each. The results of operations for the three and nine months ended October 2, 2011 are not necessarily indicative of the results to be expected for the full year.

On May 6, 2011, the Company completed the sale of substantially all of its external storage systems business to NetApp, Inc. (NetApp). The results of the external storage systems business are presented as discontinued operations in the Company s statements of operations and, as such, have been excluded from all line items other than income from discontinued operations for all periods presented. Since the first quarter of 2011, the Company operates in one reportable segment. Before it was sold, the external storage systems business was part of the Storage Systems segment. The results of the redundant array of independent disks (RAID) adapter business, which were formerly included in the Storage Systems segment, are now included in the Company s remaining reportable segment.

The preparation of financial statements in conformity with generally accepted accounting principles (GAAP) in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ significantly from these estimates.

In management s opinion, the accompanying unaudited condensed consolidated financial statements contain all normal recurring adjustments necessary for a fair statement of the Company s financial position, results of operations, and cash flows for the interim periods presented. While the Company believes that the disclosures are adequate to make the information not misleading, these financial statements should be read in conjunction with the audited consolidated financial statements and accompanying notes included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010.

Recent Accounting Pronouncements

Pronouncements not yet effective:

In May 2011, the Financial Accounting Standards Board (FASB) issued additional guidance on fair value measurements and related disclosures. The new guidance clarifies the application of existing guidance on fair value measurement for non-financial assets and requires the disclosure of quantitative information about the unobservable inputs used in a fair value measurement. This guidance is effective on a prospective basis for interim and annual periods beginning after December 15, 2011. The adoption of this guidance is not expected to have any impact on the Company s results of operations or financial position.

In June 2011, the FASB issued amended guidance regarding the presentation of comprehensive income. The amended guidance gives an entity the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The amended guidance eliminates the option to present the components of other comprehensive income as part of the statement of changes in stockholders equity. This guidance is effective on a retrospective basis for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2011. The adoption of this guidance is not expected to have any impact on the Company s results of operations or financial position.

In September 2011, the FASB amended the goodwill impairment guidance to provide an option for entities to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. After assessing the totality of events and circumstances, if an entity determines that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, performance of the two-step impairment test is no longer required. This guidance is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011, with early adoption permitted. The adoption of this guidance is not expected to have any impact on the Company s results of operations or financial position.

Table of Contents***Pronouncements adopted during the nine months ended October 2, 2011:***

In October 2009, the FASB amended revenue recognition guidance on multiple-deliverable arrangements to address how to separate deliverables and how to measure and allocate arrangement consideration. The new guidance requires the use of management's best estimate of selling price for the deliverables in an arrangement when a vendor does not have specific objective evidence of selling price or third party evidence of selling price. In addition, excluding specific software revenue guidance, the residual method of allocating arrangement consideration is no longer permitted, and an entity is required to allocate arrangement consideration using the relative selling price method. This guidance also expands the disclosure requirements to include both quantitative and qualitative information. The Company adopted this guidance in the first quarter of 2011. The adoption did not impact the Company's results of operations or financial position.

In October 2009, the FASB issued guidance to clarify that tangible products containing software components and non-software components that function together to deliver a product's essential functionality will be considered non-software deliverables and will be scoped out of the software revenue recognition guidance. The Company adopted this guidance in the first quarter of 2011. The adoption did not impact the Company's results of operations or financial position.

In December 2010, the FASB issued guidance to clarify that, when presenting comparative financial statements for business combinations that occurred during the current year, a public entity should disclose revenue and earnings of the combined entity as though the business combinations had occurred as of the beginning of the comparable prior annual reporting period. The update also expands the supplemental pro forma disclosures to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. The Company adopted this guidance in the first quarter of 2011. The adoption did not impact the Company's results of operations or financial position.

Note 2 Stock-Based Compensation**Stock-Based Compensation Expense**

The following table summarizes stock-based compensation expense, net of estimated forfeitures, related to the Company's stock options, Employee Stock Purchase Plan (ESPP) and restricted stock unit awards:

Stock-Based Compensation Expense Included In:	Three Months Ended		Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
	(In thousands)			
Cost of revenues	\$ 1,460	\$ 1,822	\$ 5,324	\$ 5,223
Research and development	5,410	6,047	18,286	18,817
Selling, general and administrative	4,883	6,135	15,462	18,261
Total stock-based compensation expense	\$ 11,753	\$ 14,004	\$ 39,072	\$ 42,301

Stock Options:

The fair value of each option grant is estimated as of the date of grant using a reduced-form calibrated binomial lattice model (lattice model). The following table summarizes the weighted-average assumptions that the Company applied in the lattice model:

	Three Months Ended		Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
Estimated grant date fair value per share	\$ 2.37	\$ 1.60	\$ 2.14	\$ 1.95
Expected life (years)	4.48	4.48	4.51	4.29
Risk-free interest rate	1%	1%	2%	2%
Volatility	50%	49%	47%	51%

The following table summarizes changes in stock options outstanding:

Edgar Filing: LSI CORP - Form 10-Q

	Number of Shares (In thousands)	Weighted-Average Exercise Price Per Share
Options outstanding at December 31, 2010	71,224	\$ 6.98
Options granted	8,954	6.36
Options exercised	(6,736)	5.04
Options canceled	(6,405)	15.32
Options outstanding at October 2, 2011	67,037	\$ 6.29
Options exercisable at October 2, 2011	43,449	\$ 6.97

Table of Contents

For options outstanding and options exercisable as of October 2, 2011, the weighted-average remaining contractual term was 3.47 years and 2.51 years, respectively, and the aggregate intrinsic value was \$30.3 million and \$13.5 million, respectively.

Employee Stock Purchase Plan:

Compensation expense for the Company's ESPP is calculated using the fair value of the employees' purchase rights under the Black-Scholes model. Under the ESPP, rights to purchase shares are granted during the second and fourth quarters of each year. A total of 2.9 million shares and 3.3 million shares were issued under the ESPP during the three months ended July 3, 2011 and July 4, 2010, respectively. No shares related to the ESPP were issued during the three months ended October 2, 2011 or October 3, 2010. The following table summarizes the weighted-average assumptions that went into the calculation of the fair value for the May 2011 and May 2010 grants:

	Three Months Ended	
	July 3, 2011	July 4, 2010
Estimated grant date fair value per share	\$ 2.10	\$ 1.74
Expected life (years)	0.8	0.8
Risk-free interest rate	0.02%	0.3%
Volatility	37%	48%

Restricted Stock Awards:

The cost of service-based and performance-based restricted stock unit awards is determined using the fair value of the Company's common stock on the date of grant. For performance-based restricted stock unit awards, the Company also considers the probability that those restricted stock units will vest.

Service-based:

The vesting requirements for service-based restricted stock units are determined at the time of grant and require that the employee remain employed by the Company for a specified period of time. As of October 2, 2011, the total unrecognized compensation expense related to these restricted stock units, net of estimated forfeitures, was \$55.7 million and is expected to be recognized over the next 3.1 years on a weighted-average basis. The fair value of the shares that were issued upon the vesting of service-based restricted stock units during the three and nine months ended October 2, 2011 was \$1.0 million and \$12.0 million, respectively.

The following table summarizes changes in service-based restricted stock units outstanding:

	Service-Based Restricted Stock Units (In thousands)
Unvested service-based restricted stock units at December 31, 2010	7,027
Granted	7,493
Vested	(1,907)
Forfeited	(680)
Unvested service-based restricted stock units at October 2, 2011	11,933

Performance-based:

The vesting of performance-based restricted stock units is contingent upon the Company meeting specified performance criteria and requires that the employee remain employed by the Company for a specified period of time. As of October 2, 2011, the total unrecognized compensation expense related to performance-based restricted stock units was \$15.9 million and, if the contingencies are fully met, is expected to be recognized over the next 3 years.

Table of Contents

The following table summarizes changes in performance-based restricted stock units outstanding:

	Performance-Based Restricted Stock Units (In thousands)
Unvested performance-based restricted stock units at December 31, 2010	2,313
Granted	3,516
Vested	(815)
Forfeited	(224)
Unvested performance-based restricted stock units at October 2, 2011	4,790

Note 3 Common Stock Repurchases

On March 9, 2011, the Company's Board of Directors authorized a stock repurchase program of up to \$750.0 million of its common stock. The repurchases under this program are funded from the proceeds of the sale of the external storage systems business, available cash and short-term investments. Under this program, the Company repurchased 11.2 million shares for \$75.0 million during the three months ended October 2, 2011 and 67.5 million shares for \$471.8 million during the nine months ended October 2, 2011. The repurchased shares were retired immediately after the repurchases were completed. Retirement of the repurchased shares is recorded as a reduction of common stock and additional paid-in capital. As of October 2, 2011, \$278.2 million remained available under this stock repurchase program.

Note 4 Restructuring, Asset Impairment Charges and Other Items

The following table summarizes items included in restructuring of operations and other items, net from continuing operations:

	Three Months Ended		Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
	(In thousands)			
Lease and contract terminations	\$ 311(a)	\$ 1,867	\$ 3,864(a)	\$ 2,838
Employee severance and benefits	482(b)	2,071	2,414(b)	7,375
Asset impairment and other exit charges	6,019(c)		6,019(c)	
Total restructuring expenses	6,812	3,938	12,297	10,213
Other items	3,972(d)	(400)	(9,611)(e)	31
Total restructuring of operations and other items, net	\$ 10,784	\$ 3,538	\$ 2,686	\$ 10,244

(a) Primarily relates to changes in estimates and changes in time value of accruals for previously accrued facility lease exit costs.

(b) Primarily relates to cost saving actions taken during 2011 with the Company's ongoing initiatives to streamline operations.

(c) Primarily relates to the write-off of intellectual property and software which are no longer in use.

Edgar Filing: LSI CORP - Form 10-Q

- (d) Primarily relates to the costs associated with the transition service agreements entered into with NetApp in connection with the sale of the external storage systems business.
- (e) Primarily relates to the reversal of a \$14.5 million sales and use tax related liability as a result of concluding various audits, partially offset by \$5.3 million of costs associated with the transition service agreements entered into with NetApp in connection with the sale of the external storage systems business.

In connection with the sale of the external storage systems business and other exit-related activities, the Company initiated certain restructuring actions. The results of those actions are included in discontinued operations and are summarized below:

	Three Months Ended		Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
	(In thousands)			
Lease and contract terminations	\$ (133)	\$ 95	\$ 2,446	\$ 76
Employee severance and benefits	1,033(a)	60	15,206(a)	60
Asset impairment and other exit charges	2,140(b)		23,278(b)	
Total	\$ 3,040	\$ 155	\$ 40,930	\$ 136

- (a) Primarily represents severance accruals for the restructuring actions taken in connection with the sale of the external storage systems business.
- (b) Primarily represents the write-down of certain assets related to discontinued operations.

Table of Contents

The following table summarizes the significant activity within, and components of, the Company's restructuring obligations from continuing operations and discontinued operations:

	Asset Impairment and Other Exit Costs	Lease and Contract Terminations	Employee Severance and Benefits	Total
	(In thousands)			
Beginning balance at December 31, 2010	\$	\$ 20,905	\$ 4,951	\$ 25,856
Expense	29,297	6,310	17,620	53,227
Utilized	(29,297)	(11,744)(a)	(19,853)(a)	(60,894)
Ending balance at October 2, 2011	\$	\$ 15,471(b)	\$ 2,718(b)	\$ 18,189

(a) The amounts utilized represent cash payments.

(b) The balance remaining for lease and contract terminations is expected to be paid during the remaining terms of the leases, which extend through 2015. The balance remaining for employee severance and benefits is expected to be paid by the first quarter of 2012.

Note 5 Benefit Obligations

The Company has pension plans covering substantially all former Agere Systems Inc. (Agere) U.S. employees, excluding management employees hired after June 30, 2003. Retirement benefits are offered under defined benefit pension plans, which include a management plan and a represented plan. The payments under the management plan are based on an adjusted career-average-pay formula or a cash-balance program. The cash-balance program provides for annual company contributions based on a participant's age, compensation and interest on existing balances. It covers employees of certain companies acquired by Agere since 1996 and management employees hired after January 1, 1999 and before July 1, 2003. The payments under the represented plan are based on a dollar-per-month formula. Since February 2009, there have been no active participants under the represented plan. The Company also has a non-qualified supplemental pension plan in the U.S. that principally provides benefits based on compensation in excess of amounts that can be considered under a tax qualified plan. The Company also provides post-retirement life insurance coverage under a group life insurance plan for former Agere employees excluding participants in the cash-balance program and management employees hired after June 30, 2003. The Company also has pension plans covering certain international employees.

Effective April 6, 2009, the Company froze the U.S. management defined benefit pension plan. Participants in the adjusted career-average-pay program will not earn any future service accruals after that date. Participants in the cash-balance program will not earn any future service accruals, but will continue to earn 4% interest per year on their cash-balance accounts.

The following table summarizes the components of the net periodic benefit cost/(credit):

	Three Months Ended			
	October 2, 2011		October 3, 2010	
	Pension Benefits	Post-retirement Benefits	Pension Benefits	Post-retirement Benefits
	(In thousands)			
Service cost	\$ 141	\$ 19	\$ 112	\$ 20
Interest cost	16,891	702	17,577	610
Expected return on plan assets	(16,999)	(1,032)	(17,864)	(1,149)
Amortization of transition asset	(5)			

Edgar Filing: LSI CORP - Form 10-Q

Amortization of prior service cost	10		9	
Amortization of net actuarial loss	1,688	237	540	
Total benefit cost/(credit)	\$ 1,726	\$ (74)	\$ 374	\$ (519)

Table of Contents

	Nine Months Ended			
	October 2, 2011		October 3, 2010	
	Pension Benefits	Post-retirement Benefits	Pension Benefits	Post-retirement Benefits
	(In thousands)			
Service cost	\$ 416	\$ 57	\$ 343	\$ 61
Interest cost	50,670	1,948	52,747	1,830
Expected return on plan assets	(50,998)	(3,097)	(53,597)	(3,447)
Amortization of transition asset	(15)			
Amortization of prior service cost	31		29	
Amortization of net actuarial loss	5,064	414	1,614	
Total benefit cost/(credit)	\$ 5,168	\$ (678)	\$ 1,136	\$ (1,556)

During the nine months ended October 2, 2011, the Company contributed \$53.9 million to its pension plans. The Company expects to contribute an additional \$11.5 million to its pension plans for the remainder of 2011. The Company does not expect to contribute to its post-retirement benefit plan in 2011.

Note 6 Balance Sheet Details

Inventories were comprised of the following:

	October 2, 2011	December 31, 2010
	(In thousands)	
Raw materials	\$ 1,213	\$ 30,691
Work-in-process	66,095	33,513
Finished goods	143,126	122,568
Total inventories	\$ 210,434	\$ 186,772

During the nine months ended October 2, 2011, the Company reclassified \$16.2 million of land in Gresham, Oregon from held and used to held for sale.

Note 7 Cash Equivalents and Investments

The following tables summarize the Company's cash equivalents and investments measured at fair value:

	Fair Value Measurements as of October 2, 2011			
	Level 1	Level 2	Level 3	Total
	(In thousands)			
Cash equivalents:				
Money-market funds	\$ 632,707(a)	\$ 785(b)	\$	\$ 632,707
U.S. government and agency securities				785
Total cash equivalents	\$ 632,707	\$ 785	\$	\$ 633,492
Available-for-sale debt securities:				
Asset-backed and mortgage-backed securities	\$	\$ 108,970(b)	\$	\$ 108,970
U.S. government and agency securities	4,830(a)	26,187(b)		31,017

Edgar Filing: LSI CORP - Form 10-Q

Corporate debt securities		13,732(b)		13,732
Total short-term investments	\$ 4,830	\$ 148,889	\$	\$ 153,719

Long-term investments in equity securities:

Marketable available-for-sale equity securities	\$ 1,382(c)	\$	\$	\$ 1,382
---	-------------	----	----	----------

	Fair Value Measurements as of December 31, 2010			Total
	Level 1	Level 2	Level 3	
	(In thousands)			
Cash equivalents:				
Money-market funds	\$ 378,382(a)	\$	\$	\$ 378,382
U.S. government and agency securities	2,000(a)			2,000
Total cash equivalents	\$ 380,382	\$	\$	\$ 380,382
Available-for-sale debt securities:				
Asset-backed and mortgage-backed securities	\$	\$ 116,552(b)	\$	\$ 116,552
U.S. government and agency securities	1,496(a)	24,502(b)		25,998
Corporate debt securities		12,330(b)		12,330
Total short-term investments	\$ 1,496	\$ 153,384	\$	\$ 154,880

Long-term investments in equity securities:

Marketable available-for-sale equity securities	\$ 1,681(c)	\$	\$	\$ 1,681
---	-------------	----	----	----------

Table of Contents

- (a) The fair value of money-market funds is determined using unadjusted prices in active markets. The fair value of these U.S. government and agency securities is determined using quoted prices in active markets.
- (b) These investments are traded less frequently than Level 1 securities and are valued using inputs that include quoted prices for similar assets in active markets and inputs other than quoted prices that are observable for the asset, such as interest rates, yield curves, prepayment speeds, collateral performance, broker/dealer quotes and indices that are observable at commonly quoted intervals.
- (c) The fair value of marketable equity securities is determined using quoted market prices in active markets. These amounts are included within other assets in the condensed consolidated balance sheets.

Investments in Non-Marketable Securities

The Company does not estimate the fair value of non-marketable securities unless there are identified events or changes in circumstances that may have a significant adverse effect on the investment. There were no non-marketable securities fair-valued during the three and nine months ended October 2, 2011. The following table summarizes the Company's non-marketable securities measured and recorded at fair value on a non-recurring basis during the nine months ended October 3, 2010:

	Carrying Value as of October 3, 2010	Fair Value Measurements			Losses for the	Losses for the
		During the Nine Months Ended October 3, 2010			Three Months Ended	Nine Months Ended
		Level 1	Level 2	Level 3	October 3, 2010	October 3, 2010
Non-marketable securities	\$ *	\$	\$	\$ 1,900	\$	\$ 11,600

* The carrying value was zero as the related investment was sold during the three months ended October 3, 2010. As of October 2, 2011 and December 31, 2010, the aggregate carrying value of the Company's non-marketable securities was \$43.9 million and \$39.9 million, respectively. The Company recognized a pre-tax gain of \$4.8 million associated with the sale of certain non-marketable securities during the three and nine months ended October 3, 2010. There were no sales of non-marketable securities during the three or nine months ended October 2, 2011.

Investments in Available-for-Sale Securities

The following tables summarize the Company's available-for-sale securities:

	Amortized Cost	October 2, 2011		Fair Value
		Gross Unrealized Gain	Gross Unrealized Loss*	
		(In thousands)		
Short-term debt securities:				
Asset-backed and mortgage-backed securities	\$ 100,627	\$ 8,560	\$ (217)	\$ 108,970
U.S. government and agency securities	30,181	836		31,017
Corporate debt securities	13,617	161	(46)	13,732
Total short-term debt securities	\$ 144,425	\$ 9,557	\$ (263)	\$ 153,719

Edgar Filing: LSI CORP - Form 10-Q

Long-term marketable equity securities	\$ 852	\$ 687	\$ (157)	\$ 1,382
--	--------	--------	----------	----------

* As of October 2, 2011, there were 51 investments in an unrealized loss position.

	Amortized Cost	December 31, 2010		Fair Value
		Gross Unrealized Gain	Gross Unrealized Loss	
(In thousands)				
Short-term debt securities:				
Asset-backed and mortgage-backed securities	\$ 107,891	\$ 9,012	\$ (351)	\$ 116,552
U.S. government and agency securities	25,313	812	(127)	25,998
Corporate debt securities	12,226	176	(72)	12,330
Total short-term debt securities	\$ 145,430	\$ 10,000	\$ (550)	\$ 154,880
Long-term marketable equity securities	\$ 852	\$ 868	\$ (39)	\$ 1,681

Table of Contents

The following tables summarize the gross unrealized losses and fair values of the Company's short-term investments that have been in a continuous unrealized loss position for less than and greater than 12 months, aggregated by investment category:

	October 2, 2011			
	Less than 12 Months		Greater than 12 Months	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(In thousands)			
Asset-backed and mortgage-backed securities	\$ 7,654	\$ (170)	\$ 575	\$ (47)
U.S. government and agency securities	1,037			
Corporate debt securities	4,614	(46)		
Total	\$ 13,305	\$ (216)	\$ 575	\$ (47)

	December 31, 2010			
	Less than 12 Months		Greater than 12 Months	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(In thousands)			
Asset-backed and mortgage-backed securities	\$ 11,807	\$ (179)	\$ 2,469	\$ (172)
U.S. government and agency securities	13,969	(127)		
Corporate debt securities	6,527	(72)		
Total	\$ 32,303	\$ (378)	\$ 2,469	\$ (172)

There were no impairment charges for available-for-sale debt or equity securities for the three or nine months ended October 2, 2011 and October 3, 2010. There were no material other than temporary impairment losses recorded in other comprehensive income for the three or nine months ended October 2, 2011 and October 3, 2010. Net realized gain or loss on sales of available-for-sale debt and equity securities for the three and nine months ended October 2, 2011 and October 3, 2010 was not significant.

Contractual maturities of available-for-sale debt securities as of October 2, 2011 were as follows:

	Available-For-Sale Debt Securities (In thousands)
Due within one year	\$ 10,211
Due in 1-5 years	40,572
Due in 5-10 years	10,826
Due after 10 years	92,110
Total	\$ 153,719

The maturities of asset-backed and mortgage-backed securities were allocated based on contractual principal maturities assuming no prepayments.

Note 8 Derivative Instruments

The Company has foreign subsidiaries that operate and sell the Company's products in various markets around the world. As a result, the Company is exposed to changes in foreign-currency exchange rates. The Company utilizes forward contracts to manage its exposure associated with net asset and liability positions denominated in non-functional currencies and to reduce the volatility of earnings and cash flows related to forecasted foreign-currency transactions. The Company does not hold derivative financial instruments for speculative or trading purposes.

Cash-Flow Hedges

Edgar Filing: LSI CORP - Form 10-Q

The Company enters into forward contracts that are designated as foreign-currency cash-flow hedges of selected forecasted payments denominated in currencies other than U.S. dollars. These forward contracts generally mature within twelve months. The Company evaluates and calculates the effectiveness of each hedge at least quarterly. Changes in fair value attributable to changes in time value are excluded from the assessment of effectiveness and are recognized in interest income and other, net. The effective portion of the forward contracts' gain or loss is recorded in other comprehensive income and is subsequently reclassified into earnings when the hedged expense is recognized within the same line item in the statements of operations as the impact of the hedged transaction. The ineffective portion of the gain or loss is reported in earnings immediately. As of October 2, 2011 and December 31, 2010, the total notional value of the Company's outstanding forward contracts, designated as foreign-currency cash-flow hedges, was \$42.2 million and \$41.7 million, respectively. For the three and nine months ended October 2, 2011 and October 3, 2010, the after-tax effect of foreign-exchange forward contract derivatives on other comprehensive income was not material.

Table of Contents**Other Foreign-Currency Hedges**

The Company enters into foreign-exchange forward contracts that are used to hedge certain foreign-currency-denominated assets or liabilities and that do not qualify for hedge accounting. These forward contracts generally mature within three months. Changes in the fair value of these forward contracts are recorded immediately in earnings to offset the changes in fair value of the assets or liabilities being hedged. As of October 2, 2011 and December 31, 2010, the total notional value of the Company's outstanding forward contracts, not designated as hedges under hedge accounting, was \$47.3 million and \$112.3 million, respectively. For the three and nine months ended October 2, 2011, losses of \$2.5 million and \$0.5 million, respectively, on other foreign-currency hedges were recognized in interest income and other, net. For the three and nine months ended October 3, 2010, gains of \$6.5 million and \$2.9 million, respectively, on other foreign-currency hedges were recognized in interest income and other, net. These gains and losses were substantially offset by the gain and loss on the underlying foreign-currency-denominated assets or liabilities.

Fair Value of Derivative Instruments

As of October 2, 2011 and December 31, 2010, the total fair value of derivative assets was \$2.2 million and \$0.8 million, respectively, and was recorded in prepaid expenses and other current assets in the condensed consolidated balance sheets. As of October 2, 2011 and December 31, 2010, the total fair value of derivative liabilities was \$5.2 million and \$0.3 million, respectively, and was recorded in other accrued liabilities in the condensed consolidated balance sheets.

Note 9 Reconciliation of Basic and Diluted Shares

The following table provides a reconciliation of basic and diluted shares:

	Three Months Ended		Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
	(In thousands)			
Basic shares	567,790	629,852	592,898	646,167
Dilutive effect of stock options, employee stock purchase rights and restricted stock unit awards	13,693	3,879	15,845	7,518
Diluted shares	581,483	633,731	608,743	653,685

The following table provides information about the weighted-average common share equivalents that were excluded from the computation of diluted shares because their inclusion would have an anti-dilutive effect on net income per share:

	Three Months Ended		Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
	(In thousands)			
Anti-dilutive securities:				
Stock options	39,924	75,234	42,978	70,893
Restricted stock unit awards	1,491	7,404	182	422
Convertible notes				12,946

Note 10 Segment and Geographic Information

Prior to the sale of the external storage systems business, the Company operated in two reportable segments—the Semiconductor segment and the Storage Systems segment. The Semiconductor segment designs, develops and markets highly complex integrated circuits for storage and networking applications. These solutions include both custom solutions and standard products. The Storage Systems segment offered external storage systems and RAID adapters for computer servers and associated software for attaching storage devices to computer servers. On March 9, 2011, the Company entered into a definitive agreement to sell its external storage systems business to NetApp and started to operate its RAID adapter business as part of its semiconductor business. Accordingly, the Company has one reportable segment. The change has been reflected in the Company's segment reporting for all periods presented.

Information about Geographic Areas

The following table summarizes the Company's revenues by geography based on the ordering location of the customer. Because the Company sells its products primarily to other sellers of technology products and not to end-users, the information in the table below may not accurately

reflect geographic end-demand for its products.

Table of Contents

	Three Months Ended		Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
	(In thousands)			
North America*	\$ 136,849	\$ 110,890	\$ 380,648	\$ 311,035
Asia:				
China	146,873	82,263	362,051	249,422
Singapore	75,652	65,813	193,773	218,214
Taiwan	60,450	68,272	212,087	229,587
Other	77,263	69,947	225,328	229,513
Total Asia	360,238	286,295	993,239	926,736
Europe and the Middle East	49,823	55,693	146,931	161,226
Total	\$ 546,910	\$ 452,878	\$ 1,520,818	\$ 1,398,997

* Primarily the United States.

Note 11 Comprehensive Income

Comprehensive income or loss is defined as a change in equity of a company during a period from transactions and other events and circumstances, excluding transactions resulting from investments by owners and distributions to owners. The following table summarizes the changes in total comprehensive income, net of taxes:

	Three Months Ended		Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
	(In thousands)			
Net income	\$ 29,339	\$ 23,421	\$ 333,277	\$ 53,373
Net unrealized (loss)/gain on investments	(689)	738	(781)	2,046
Net unrealized (loss)/gain on derivatives	(2,455)	2,019	(2,406)	767
Foreign currency translation adjustments	(3,104)	4,928	(1,516)	2,808
Net actuarial loss	(1,855)		(1,855)	
Amortization of transition asset, prior-service cost and net actuarial loss	1,930	549	5,494	1,643
Total comprehensive income	\$ 23,166	\$ 31,655	\$ 332,213	\$ 60,637

Note 12 Income Taxes

The Company recorded income tax provisions of \$7.8 million and \$12.6 million for the three and nine months ended October 2, 2011, respectively, and an income tax provision of \$2.5 million and an income tax benefit of \$13.7 million for the three and nine months ended October 3, 2010, respectively.

The income tax provision for the nine months ended October 2, 2011 included a reversal of \$9.6 million in liabilities for uncertain tax positions, which included previously unrecognized tax benefits of \$5.6 million and interest and penalties of \$4.0 million, as a result of the expiration of statutes of limitations in multiple jurisdictions.

The income tax benefit for the nine months ended October 3, 2010 included a reversal of \$28.0 million in liabilities for uncertain tax positions, which included previously unrecognized tax benefits of \$12.2 million and interest and penalties of \$15.8 million, as a result of the expiration of statutes of limitations in multiple jurisdictions.

The Company computes its tax provision using an estimated annual tax rate. The Company excludes certain loss jurisdictions from the computation of the estimated annual rate when no benefit can be realized on those losses. With the exception of certain foreign jurisdictions, the

Edgar Filing: LSI CORP - Form 10-Q

Company believes it is not more likely than not that the future benefit of the deferred tax assets will be realized.

As of October 2, 2011, the Company had \$142.9 million of unrecognized tax benefits, for which the Company is unable to make a reasonably reliable estimate as to when cash settlement with a taxing authority may occur. It is reasonably possible that the total amount of unrecognized tax benefits will increase or decrease in the next 12 months. Such changes could occur based on the normal expiration of statutes of limitations or the possible conclusion of ongoing tax audits in various jurisdictions around the world. If those events occur within the next 12 months, the Company estimates that the unrecognized tax benefits, plus accrued interest and penalties, could decrease by up to \$16.8 million.

Table of Contents**Note 13 Related Party Transactions**

A member of the Company's board of directors is also a member of the board of directors of Seagate Technology (Seagate). The Company sells semiconductors used in storage product applications to Seagate for prices comparable to those charged to an unrelated third party. Revenues from sales by the Company to Seagate were \$157.9 million and \$375.4 million for the three and nine months ended October 2, 2011, respectively. Revenues from sales by the Company to Seagate were \$78.6 million and \$263.5 million for the three and nine months ended October 3, 2010, respectively. The Company had accounts receivable from Seagate of \$93.4 million and \$55.0 million as of October 2, 2011 and December 31, 2010, respectively.

The Company has an equity interest in a joint venture, Silicon Manufacturing Partners Pte Ltd. (SMP), with GLOBALFOUNDRIES, a manufacturing foundry for integrated circuits. SMP operates an integrated circuit manufacturing facility in Singapore. The Company owns a 51% equity interest in this joint venture and accounts for its ownership position under the equity method of accounting. The Company is effectively precluded from unilaterally taking any significant action in the management of SMP due to GLOBALFOUNDRIES' significant participatory rights under the joint venture agreement. Because of GLOBALFOUNDRIES' approval rights, the Company cannot make any significant decisions regarding SMP without GLOBALFOUNDRIES' approval, despite the 51% equity interest. In addition, the General Manager, who is responsible for the day-to-day management of SMP, is appointed by GLOBALFOUNDRIES, and GLOBALFOUNDRIES provides day-to-day operational support to SMP.

The Company purchased \$12.9 million and \$38.5 million of inventory from SMP for the three and nine months ended October 2, 2011, respectively. The Company purchased \$9.9 million and \$33.9 million of inventory from SMP for the three and nine months ended October 3, 2010, respectively. As of October 2, 2011 and December 31, 2010, the amounts payable to SMP were \$11.6 million and \$1.2 million, respectively.

Note 14 Commitments, Contingencies and Legal Matters**Purchase Commitments**

The Company maintains purchase commitments with certain suppliers, primarily for raw materials and manufacturing services and for some non-production items. Purchase commitments for inventory materials are generally restricted to a forecasted time horizon as mutually agreed upon between the parties. This forecasted time horizon can vary for different suppliers. As of October 2, 2011, the Company had purchase commitments of \$390.6 million, which are due through 2016.

The Company has a take-or-pay agreement with SMP under which it has agreed to purchase 51% of the managed wafer capacity from SMP's integrated circuit manufacturing facility, and GLOBALFOUNDRIES has agreed to purchase the remaining managed wafer capacity. SMP determines its managed wafer capacity each year based on forecasts provided by the Company and GLOBALFOUNDRIES. If the Company fails to purchase its required commitments, it will be required to pay SMP for the fixed costs associated with the unpurchased wafers. GLOBALFOUNDRIES is similarly obligated with respect to the wafers allotted to it. The agreement may be terminated by either party upon two years written notice. The agreement may also be terminated for material breach, bankruptcy or insolvency.

Guarantees***Product Warranties:***

The Company warrants finished goods against defects in material and workmanship under normal use and service generally for periods of one to three years. A liability for estimated future costs under product warranties is recorded when products are shipped.

Table of Contents

The following table sets forth a summary of changes in product warranties:

	Accrued Warranties (In thousands)
Balance as of December 31, 2010	\$ 17,617
Accruals for warranties issued during the period	6,382
Accruals related to pre-existing warranties (including changes in estimates)	500
Settlements made during the period (in cash or in kind)	(5,983)
Balance as of October 2, 2011	\$ 18,516

Standby Letters of Credit:

As of October 2, 2011 and December 31, 2010, the Company had outstanding obligations relating to standby letters of credit of \$2.9 million and \$3.9 million, respectively. Standby letters of credit are financial guarantees provided by third parties for leases, customs and certain self-insured risks. If the guarantees are called, the Company must reimburse the provider of the guarantee. The fair value of the letters of credit approximates the contract amounts. The standby letters of credit generally renew annually.

Indemnifications

The Company is a party to a variety of agreements pursuant to which it may be obligated to indemnify the other party. These obligations arise primarily in connection with sales contracts and license agreements or the sale of assets, under which the Company customarily agrees to hold the other party harmless against losses arising from a breach of warranties, representations and covenants related to such matters as title to assets sold, validity of certain intellectual property rights, non-infringement of third-party rights, and certain income tax-related matters. In each of these circumstances, payment by the Company is typically subject to the other party making a claim to and cooperating with the Company pursuant to the procedures specified in the particular contract. This usually allows the Company to challenge the other party's claims or, in case of breach of intellectual property representations or covenants, to control the defense or settlement of any third-party claims brought against the other party. Further, the Company's obligations under these agreements may be limited in terms of activity (typically to replace or correct the products or terminate the agreement with a refund to the other party), duration and/or amounts. In some instances, the Company may have recourse against third parties covering certain payments made by the Company.

Legal Matters

On December 6, 2006, Sony Ericsson Mobile Communications USA Inc. (Sony Ericsson) filed a lawsuit against Agere in Wake County Superior Court in North Carolina, alleging unfair and deceptive trade practices, fraud and negligent misrepresentation in connection with Agere's engagement with Sony Ericsson to develop a wireless data card for personal computers. The complaint claimed an unspecified amount of damages and sought compensatory damages, treble damages and attorneys' fees. In August, 2007, the case was dismissed for improper venue. On October 22, 2007, Sony Ericsson filed a lawsuit in the Supreme Court of the State of New York, New York County against LSI, raising substantially the same allegations and seeking substantially the same relief as the North Carolina proceeding. In January 2010, Sony Ericsson amended its complaint by adding claims for fraudulent concealment and gross negligence. On September 10, 2010, LSI filed a motion for summary judgment. On August 4, 2011, the court granted LSI's motion and ordered the dismissal of all of Sony Ericsson's claims. Sony Ericsson has appealed this decision. The Company is unable to estimate the possible loss or range of loss, if any, that may be incurred with respect to this matter.

On March 23, 2007, CIF Licensing, LLC, d/b/a GE Licensing (GE) filed a lawsuit against Agere in the United States District Court for the District of Delaware, asserting that Agere products infringe patents in a portfolio of patents GE acquired from Motorola. GE has asserted that four of the patents cover inventions relating to modems. GE is seeking monetary damages. Agere believes it has a number of defenses to the infringement claims in this action, including laches, exhaustion and its belief that it has a license to the patents. The court postponed hearing motions based on these defenses until after the trial, and did not allow Agere to present evidence on these defenses at trial. On February 17, 2009, the jury in this case returned a verdict finding that three of the four patents were invalid and that Agere products infringed the one patent found to be valid and awarding GE \$7.6 million for infringement of that patent. The jury also found Agere's infringement was willful, which means that the judge could increase the amount of damages up to three times its original amount. The court has not scheduled hearings on Agere's post-trial motions related to its defenses. One of these motions seeks to have a mis-trial declared based on Agere's belief that GE withheld evidence in discovery, which affected Agere's ability to present evidence at trial. On October 6, 2010, a special master appointed by the court

Edgar Filing: LSI CORP - Form 10-Q

determined that GE's actions were not wrongful and that the evidence withheld by GE was not material to the jury's findings. Agere is challenging this determination. If the jury's verdict is entered by the court, Agere would also expect to be required to pay interest from the date of infringing sales. If the verdict is entered, Agere intends to appeal the matter. On February 17, 2010, the court issued an order granting GE's summary judgment motions seeking to bar Agere's defenses of laches, exhaustion, and license and denying Agere's summary judgment motions concerning the same defenses. On July 30, 2010, the court held that one of the patents found invalid by the jury was valid. The court also held that the February 17, 2010 order was not inconsistent with its previous ruling that Agere would be permitted to renew its laches, licensing, and exhaustion defenses, and that Agere has not been precluded from asserting them post-trial. The Company is unable to estimate the possible loss or range of loss, if any, that may be incurred with respect to this matter.

Table of Contents

On December 1, 2010, Rambus Inc. (Rambus) filed a lawsuit against LSI in the United States District Court for the Northern District of California alleging that LSI products infringe one or more of nineteen Rambus patents. These products contain either DDR-type memory controllers or certain high-speed SerDes peripheral interfaces, such as PCI Express interfaces and certain SATA and SAS interfaces. Rambus is seeking unspecified monetary damages, treble damages and costs, expenses and attorneys' fees due to alleged willfulness, interest, and permanent injunctive relief in this action. In addition, on December 1, 2010, Rambus filed an action with the International Trade Commission (ITC) against LSI and five of its customers alleging that LSI products infringe six of the nineteen patents in the California case. Rambus also named five other companies and a number of their customers in the ITC action. Rambus is seeking an exclusionary order against LSI and its customers in the ITC action, which, if granted, would preclude LSI and its customers from selling these products in the U.S. The ITC instituted its investigation on December 29, 2010. LSI has filed an answer in the ITC proceedings and has requested a stay in the California case. The Company is unable to estimate the possible loss or range of loss, if any, that may be incurred with respect to this matter.

In addition to the foregoing, the Company and its subsidiaries are parties to other litigation matters and claims in the normal course of business. The Company does not believe, based on currently available facts and circumstances, that the final outcome of these other matters, taken individually or as a whole, will have a material adverse effect on the Company's consolidated results of operations or financial position. However, the pending unsettled lawsuits may involve complex questions of fact and law and may require the expenditure of significant funds and the diversion of other resources to defend. From time to time, the Company may enter into confidential discussions regarding the potential settlement of such lawsuits. However, there can be no assurance that any such discussions will occur or will result in a settlement. Moreover, the settlement of any pending litigation could require the Company to incur substantial costs and, in the case of the settlement of any intellectual property proceeding against the Company, may require the Company to obtain a license to a third-party's intellectual property that could require royalty payments in the future and the Company to grant a license to certain of its intellectual property to a third party under a cross-license agreement. The results of litigation are inherently uncertain, and material adverse outcomes are possible.

The Company has not provided accruals for any legal matters in its financial statements as potential losses for such matters are not considered probable and reasonably estimable. However, because such matters are subject to many uncertainties, the ultimate outcomes are not predictable, and there can be no assurances that the actual amounts required to satisfy alleged liabilities from the matters described above will not have a material adverse effect on its consolidated results of operations, financial position or cash flows.

Note 15 Discontinued Operations

On May 6, 2011, the Company completed the sale of substantially all of its external storage systems business to NetApp pursuant to the terms of the asset purchase agreement and received cash consideration of \$480.0 million. The strategic decision to divest the external storage systems business was based on the Company's expectation that long-term shareholder value can be maximized by becoming a pure-play semiconductor company. Under the terms of the agreement, NetApp purchased substantially all the assets of the Company's external storage systems business, which developed and delivered external storage systems products and technology to a wide range of partners that provide storage solutions to end customers. As part of the asset purchase agreement, certain transitional services are provided to NetApp for a period of up to eighteen months. The purpose of these services is to provide short-term assistance to the buyer in assuming the operations of the external storage systems business.

Following is selected financial information included in (loss)/income from discontinued operations:

	Three Months Ended		Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
	(In thousands)			
Revenues	\$ 2,860	\$ 176,106	\$ 210,225	\$ 506,574
(Loss)/income before income taxes	\$ (2,366)	\$ 16,246	\$ (24,866)	\$ 35,659
Gain on sale of external storage systems business			260,066	
(Benefit from)/provision for income taxes	(55)	5,644	(19,473)	12,135
(Loss)/income from discontinued operations	\$ (2,311)	\$ 10,602	\$ 254,673	\$ 23,524

Table of Contents

During the three and nine months ended October 2, 2011, the Company recorded write-downs of \$2.6 million and \$23.0 million, respectively, related to assets associated with discontinued operations. Further, the Company released \$19.7 million of deferred tax liabilities related to tax deductible goodwill in connection with the sale of the external storage systems business during the nine months ended October 2, 2011.

Note 16 Subsequent Events

On October 26, 2011, the Company entered into a definitive agreement to acquire SandForce, Inc. (SandForce), a leading provider of flash storage processors for enterprise and client flash solutions and solid state drives. The acquisition is expected to enhance LSI s position in storage technology solutions.

Under the agreement, LSI will pay approximately \$322 million in cash, net of cash acquired, and assume approximately \$48 million of unvested stock options and restricted shares held by SandForce employees. The transaction is expected to close early in the first quarter of 2012 subject to customary closing conditions and regulatory approvals.

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

This management s discussion and analysis should be read in conjunction with the other sections of this Form 10-Q, including Part 1, Item 1. Financial Statements.

Where more than one significant factor contributed to changes in results from year to year, we have quantified these factors throughout Management s Discussion and Analysis of Financial Condition and Results of Operations where practicable and material to understanding the discussion.

OVERVIEW

We design, develop and market complex, high-performance storage and networking semiconductors. We provide silicon-to-system solutions that are used at the core of products that create, store, consume and transport digital information. We offer a broad portfolio of capabilities, including custom and standard product integrated circuits used in hard disk drives, solid state drives, high-speed communications systems, computer servers, storage systems and personal computers. We also offer redundant array of independent disks, or RAID, adapters for computer servers and RAID software applications.

We sell our integrated circuits for server and storage applications principally to makers of hard disk drives, solid state drives and computer servers. We sell our integrated circuits for networking applications principally to makers of devices used in computer and telecommunications networks and, to a lesser extent, to makers of personal computers. We also generate revenue by licensing other entities to use our intellectual property.

We derive the majority of our revenue from sales of products for the hard disk drive, server and networking equipment end markets. We believe that these markets offer us attractive opportunities because of the growing demand to create, store, manage and move digital content. We believe that this growth is occurring as a result of a number of trends, including:

The increasing popularity of mobile devices such as smart phones and media tablets, and the increasing use of the Internet for streaming media, such as videos and music, which are driving the need for more network capacity;

Consumer and business demand for hard disks to store increasing amounts of digital data, including music, video, pictures and medical and other business records; and

Enterprises refreshing their data centers to provide higher levels of business support and analytics, which drives demand for new servers and storage systems and associated equipment.

Our revenues depend on market demand for these types of products and our ability to compete in highly competitive markets. We face competition not only from makers of products similar to ours, but also from competing technologies. For example, we see the development of solid state drives based on flash memory rather than the spinning platters used in hard disk drives as a long-term potential competitor to certain

Edgar Filing: LSI CORP - Form 10-Q

types of hard disk drives, and we are focusing development efforts in that area. We have also entered into an agreement to acquire SandForce, a provider of technology for solid state drives.

Table of Contents

On May 6, 2011, we completed the sale of our external storage systems business to NetApp for \$480.0 million in cash. That business sold external storage systems, primarily to original equipment manufacturers, or OEMs, who resold these products to end customers under their own brand name. We have reflected the external storage systems business as discontinued operations in our statements of operations and, as such, the results of that business have been excluded from all line items other than (loss)/income from discontinued operations for all periods presented. We believe that as a result of this sale, we are seeing increasing interest in our products from other external storage systems OEMs who previously were reluctant to buy our products because they viewed us as a competitor.

On October 26, 2011, we entered into a definitive agreement to acquire SandForce, a provider of flash storage processors for enterprise and client flash solutions and solid state drives. The acquisition is expected to enhance our position in storage technology solutions. Under the agreement, we will pay approximately \$322 million in cash, net of cash acquired, and assume approximately \$48 million of unvested stock options and restricted shares held by SandForce employees. The transaction is expected to close early in the first quarter of 2012, subject to customary closing conditions and regulatory approvals.

During the third quarter of 2011, we reported revenue of \$546.9 million, compared to \$452.9 million for the third quarter of 2010. For the nine months ended October 2, 2011, we reported revenue of \$1,520.8 million, compared to \$1,399.0 million for the nine months ended October 3, 2010. We reported net income of \$29.3 million, or \$0.05 per diluted share, for the third quarter of 2011, compared to \$23.4 million, or \$0.04 per diluted share, for the third quarter of 2010. For the nine months ended October 2, 2011, we reported net income of \$333.3 million, or \$0.55 per diluted share, compared to \$53.4 million, or \$0.08 per diluted share, for the nine months ended October 3, 2010. Net income for the nine months ended October 2, 2011 included a \$260.1 million gain on the sale of our external storage systems business.

On March 9, 2011, our Board of Directors authorized a stock repurchase program of up to \$750.0 million of our common stock. Through October 2, 2011, we had repurchased 67.5 million shares for \$471.8 million under this program.

We ended the third quarter of 2011 with cash and cash equivalents, together with short-term investments, of \$878.9 million, an improvement of \$202.2 million from the end of 2010, primarily attributable to the cash we received from the sale of our external storage systems business.

Recently, Thailand has experienced flooding as a result of significant rains. The Thailand operations of a number of technology companies have been affected by this flooding. We have a supplier in Thailand that performs assembly and test functions for our semiconductor products and that supplier's facility has been affected by flooding. The flooding has had a significant impact on the hard disk drive industry, which we serve. To the extent that there is an extended period during which our supplier's assembly and test facility is not able to operate and we are unable to obtain alternate sources of supply, our ability to deliver products, particularly products used in hard disk drives, will be affected and we may not be able to supply all of our customers' demand. Further, if because of the flooding, our customers are unable to obtain sufficient parts from other suppliers or their operations will not support the level of production we are able to supply, their demand for our products may be reduced. We currently believe that the impact of the flooding will have an adverse impact on our revenue in the fourth quarter of 2011.

The price of commodities used in the production of semiconductors has been increasing this year and has had an adverse impact on our gross margins. For example, we use gold in the production of semiconductors and the market price of gold has increased significantly during 2011. We do not currently enter into hedging transactions to reduce income statement volatility due to changes in the prices of gold or other commodities, although we may choose to do so in the future. Further increases in commodity costs may also have an adverse impact on our gross margins.

As we look forward into the remainder of 2011 and 2012, we are focused on a number of key objectives, including:

Successfully completing the acquisition and integration of SandForce;

Attempting to mitigate the impact on our business of the flooding in Thailand;

Successfully delivering products to customers to support share gains and new product ramps we anticipate;

Improving our gross margins and controlling operating expenses to drive improved financial performance;

Meeting or exceeding our development, product quality and delivery commitments to our customers;

Table of Contents

Identifying attractive opportunities for future products, particularly in areas that are adjacent to technologies where we have strong capabilities;

Developing leading-edge new technologies; and

Developing the skills of our workforce.

RESULTS OF OPERATIONS**Revenues**

	Three Months Ended		\$ Change	% Change
	October 2, 2011	October 3, 2010		
Revenues	\$ 546.9	\$ 452.9	\$ 94.0	20.8%

The increase in revenues was primarily attributable to increased demand from existing customers for semiconductors used in storage product applications and increased demand for our server RAID adapters. These increases were offset in part by a decrease in unit sales from semiconductors used in networking product applications, primarily products used in wireless networking applications.

	Nine Months Ended		\$ Change	% Change
	October 2, 2011	October 3, 2010		
Revenues	\$ 1,520.8	\$ 1,399.0	\$ 121.8	8.7%

The increase in revenues was primarily attributable to increased demand from existing customers for semiconductors used in storage product applications, increased demand for our server RAID adapters and higher revenues from the licensing of our intellectual property. These increases were offset in part by a decrease in unit sales from semiconductors used in networking product applications, primarily products used in wireless networking applications.

Significant Customers:

The following table provides information about our one customer that accounted for 10% or more of consolidated revenues:

	Three Months Ended		Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
Revenues	29%	18%	25%	19%

Revenues by Geography

The following table summarizes our revenues by geography based on the ordering location of the customer. Because we sell our products primarily to other sellers of technology products and not to end-users, the information in the table below may not accurately reflect geographic end-demand for our products.

	Three Months Ended		\$ Change	% Change
	October 2, 2011	October 3, 2010		
North America*	\$ 136.9	\$ 110.9	\$ 26.0	23.4%

Asia:

Edgar Filing: LSI CORP - Form 10-Q

China	146.9	82.3	64.6	78.5%
Singapore	75.7	65.8	9.9	15.0%
Taiwan	60.4	68.3	(7.9)	(11.6)%
Other	77.2	69.9	7.3	10.4%
Total Asia	360.2	286.3	73.9	25.8%
Europe and the Middle East	49.8	55.7	(5.9)	(10.6)%
Total	\$ 546.9	\$ 452.9	\$ 94.0	20.8%

* Primarily the United States.

Table of Contents

The increase in North America was primarily attributable to increased demand for semiconductors used in networking applications and increased unit sales of server RAID adapters. The increase in Asia was primarily attributable to increased unit sales of semiconductors used in storage product applications. The decrease in Europe and the Middle East was primarily attributable to decreased unit sales of semiconductors used in storage product applications, offset in part by increased unit sales of server RAID adapters.

	Nine Months Ended		\$ Change	% Change
	October 2, 2011	October 3, 2010		
	(Dollars in millions)			
North America*	\$ 380.7	\$ 311.1	\$ 69.6	22.4%
Asia:				
China	362.0	249.4	112.6	45.1%
Singapore	193.8	218.2	(24.4)	(11.2)%
Taiwan	212.1	229.6	(17.5)	(7.6)%
Other	225.3	229.5	(4.2)	(1.8)%
Total Asia	993.2	926.7	66.5	7.2%
Europe and the Middle East	146.9	161.2	(14.3)	(8.9)%
Total	\$ 1,520.8	\$ 1,399.0	\$ 121.8	8.7%

* Primarily the United States.

The increase in North America was primarily attributable to increased demand for semiconductors used in networking applications, increased unit sales of server RAID adapters and higher revenues from the licensing of our intellectual property. The increase in Asia was primarily attributable to increased demand for semiconductors used in storage product applications, partially offset by a decrease in unit sales from semiconductors used in networking product applications, primarily products used in wireless networking applications. The decrease in Europe and the Middle East was primarily attributable to decreased unit sales of semiconductors used in storage product applications and decreased demand for custom products used in networking applications, offset in part by increased unit sales of server RAID adapters.

Gross Profit Margin

	Three Months Ended		\$ Change	% Change
	October 2, 2011	October 3, 2010		
	(Dollars in millions)			
Gross profit	\$ 263.8	\$ 218.2	\$ 45.6	20.9%
% of revenues	48.2%	48.2%		

Gross margin as a percentage of revenues remained flat as a result of lower amortization of identified intangible assets, offset in part by less favorable product mix and higher costs for commodities used in the manufacture of our products.

	Nine Months Ended		\$ Change	% Change
	October 2, 2011	October 3, 2010		
	(Dollars in millions)			
Gross profit	\$ 725.6	\$ 657.8	\$ 67.8	10.3%
% of revenues	47.7%	47.0%		

Gross margin as a percentage of revenues remained relatively flat as a result of lower amortization of identified intangible assets, offset in part by less favorable product mix and higher costs for commodities used in the manufacture of our products.

Research and Development

Table of Contents

R&D expenses increased primarily due to higher compensation-related expenses and facility costs as a result of headcount additions, offset in part by lower R&D costs for shared development engineering projects due to higher contributions from certain customers associated with existing R&D projects.

	Nine Months Ended		\$ Change	% Change
	October 2, 2011	October 3, 2010		
	(Dollars in millions)			
Research and development	\$ 431.6	\$ 422.3	\$ 9.3	2.2%
% of revenues	28.4%	30.2%		

R&D expenses increased primarily due to higher compensation-related expenses and facility costs as a result of headcount additions, offset in part by lower R&D costs for shared development engineering projects due to higher contributions from certain customers associated with existing R&D projects.

Selling, General and Administrative

	Three Months Ended		\$ Change	% Change
	October 2, 2011	October 3, 2010		
	(Dollars in millions)			
Selling, general and administrative	\$ 77.9	\$ 69.2	\$ 8.7	12.6%
% of revenues	14.2%	15.3%		

SG&A expenses increased primarily due to increases in litigation costs and compensation-related expenses as a result of headcount additions in marketing and sales to support operations.

	Nine Months Ended		\$ Change	% Change
	October 2, 2011	October 3, 2010		
	(Dollars in millions)			
Selling, general and administrative	\$ 218.5	\$ 209.7	\$ 8.8	4.2%
% of revenues	14.4%	15.0%		

SG&A expenses increased primarily due to increases in litigation costs and compensation-related expenses as a result of headcount additions in marketing and sales to support operations, offset in part by decreases in general and administrative expenses as a result of our continuing focus on control of expenses.

Restructuring of Operations and Other Items, net

The following table summarizes items included in restructuring of operations and other items, net from continuing operations:

	Three Months Ended		Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
	(In millions)			
Lease and contract terminations	\$ 0.3(a)	\$ 1.9	\$ 3.9(a)	\$ 2.8
Employee severance and benefits	0.5(b)	2.0	2.4(b)	7.4
Asset impairment and other exit charges	6.0(c)		6.0(c)	
Total restructuring expenses	6.8	3.9	12.3	10.2
Other items	4.0(d)	(0.4)	(9.6)(e)	
Total restructuring of operations and other items, net	\$ 10.8	\$ 3.5	\$ 2.7	\$ 10.2

Edgar Filing: LSI CORP - Form 10-Q

- (a) Primarily relates to changes in estimates and changes in time value of accruals for previously accrued facility lease exit costs.
- (b) Primarily relates to cost saving actions taken during 2011 with our ongoing initiatives to streamline operations.
- (c) Primarily relates to the write-off of intellectual property and software which are no longer in use.
- (d) Primarily relates to the costs associated with the transition service agreements entered into with NetApp in connection with the sale of the external storage systems business.

Table of Contents

- (e) Primarily relates to the reversal of a \$14.5 million sales and use tax related liability as a result of concluding various audits, partially offset by \$5.3 million of costs associated with the transition service agreements entered into with NetApp in connection with the sale of the external storage systems business.

Interest Expense, Interest Income and Other, net

The following table summarizes interest expense and components of interest income and other, net:

	Three Months Ended		Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
	(In millions)			
Interest expense	\$	\$	\$	\$ (5.6)
Interest income	2.3	3.2	9.0	10.4
Other income/(expense), net	5.3	7.1	9.3	(4.3)
Total	\$ 7.6	\$ 10.3	\$ 18.3	\$ 0.5

Interest expense decreased by \$5.6 million for the nine months ended October 2, 2011 as compared to the nine months ended October 3, 2010, as a result of the repayment of our 4% Convertible Subordinated Notes in May 2010.

Interest income decreased by \$0.9 million for the three months ended October 2, 2011 as compared to the three months ended October 3, 2010, primarily as a result of lower interest rates in 2011. Interest income decreased by \$1.4 million for the nine months ended October 2, 2011 as compared to the nine months ended October 3, 2010, primarily as a result of lower interest rates, offset in part by higher cash balances in 2011.

Other income, net, for the three and nine months ended October 2, 2011, primarily included \$4.4 million and \$7.4 million, respectively, of income for services provided under the transition service agreements entered into with NetApp in connection with the sale of the external storage systems business. Other income, net, for the three months ended October 3, 2010, primarily included a \$4.8 million gain from the sale of investments. Other expense, net, for the nine months ended October 3, 2010, primarily included \$11.6 million of other than temporary impairment charges incurred during the first quarter of 2010 for certain non-marketable equity securities, offset in part by a \$4.8 million gain from the sale of investments and other.

Provision for/Benefit from Income Taxes

We recorded income tax provisions of \$7.8 million and \$12.6 million for the three and nine months ended October 2, 2011, respectively, and an income tax provision of \$2.5 million and an income tax benefit of \$13.7 million for the three and nine months ended October 3, 2010, respectively.

The income tax provision for the nine months ended October 2, 2011 is presented net of a reversal of \$9.6 million in liabilities for uncertain tax positions, which included previously unrecognized tax benefits of \$5.6 million and interest and penalties of \$4.0 million, as a result of the expiration of statutes of limitations in multiple jurisdictions.

The income tax benefit for the nine months ended October 3, 2010 included a reversal of \$28.0 million in liabilities for uncertain tax positions, which included previously unrecognized tax benefits of \$12.2 million and interest and penalties of \$15.8 million, as a result of the expiration of statutes of limitations in multiple jurisdictions.

We compute our tax provision using an estimated annual tax rate. We exclude certain loss jurisdictions from the computation of the estimated annual rate when no benefit can be realized on those losses. With the exception of certain foreign jurisdictions, we believe it is not more likely than not that the future benefit of the deferred tax assets will be realized.

Discontinued Operations

Following is selected financial information included in (loss)/income from discontinued operations:

Edgar Filing: LSI CORP - Form 10-Q

	Three Months Ended		Nine Months Ended	
	October 2, 2011	October 3, 2010	October 2, 2011	October 3, 2010
	(In millions)			
Revenues	\$ 2.9	\$ 176.1	\$ 210.2	\$ 506.6
(Loss)/income before income taxes	\$ (2.4)	\$ 16.2	\$ (24.9)	\$ 35.6
Gain on sale of external storage systems business			260.1	
(Benefit from)/provision for income taxes	(0.1)	5.6	(19.5)	12.1
(Loss)/income from discontinued operations	\$ (2.3)	\$ 10.6	\$ 254.7	\$ 23.5

Table of Contents

During the three and nine months ended October 2, 2011, we recorded write-downs of \$2.6 million and \$23.0 million, respectively, related to assets associated with discontinued operations. Further, we released \$19.7 million of deferred tax liabilities related to tax deductible goodwill in connection with the sale of the external storage systems business during the nine months ended October 2, 2011.

FINANCIAL CONDITION, CAPITAL RESOURCES AND LIQUIDITY

Cash, cash equivalents and short-term investments increased to \$878.9 million as of October 2, 2011 from \$676.7 million as of December 31, 2010. The increase was mainly due to proceeds from the sale of our external storage systems business and cash inflows generated from operating activities, offset in part by cash outflows for financing and other investing activities, as described below.

Under our agreement to acquire SandForce, we will pay approximately \$322 million in cash, net of cash acquired, and assume approximately \$48 million of unvested stock options and restricted shares held by SandForce employees. The cash consideration is expected to be funded from our existing cash, cash equivalents and short-term investments. We expect to complete the acquisition in early 2012.

Working Capital

Working capital increased by \$185.5 million to \$964.7 million as of October 2, 2011 from \$779.2 million as of December 31, 2010. The increase was primarily attributable to the following:

Cash, cash equivalents and short-term investments increased by \$202.2 million primarily due to the proceeds from the sale of our external storage systems business on May 6, 2011;

Inventories increased by \$23.7 million primarily due to increased inventory purchases during the third quarter of 2011 in anticipation of expected increases in product demand, offset in part by inventory sold to NetApp as part of the sale of the external storage systems business;

Accrued salaries, wages and benefits decreased by \$17.6 million primarily as a result of timing differences in the payment of salaries, benefits and performance-based compensation, and the payout of accrued compensation-related costs to employees transferred to NetApp as part of the sale of the external storage systems business; and

Assets held for sale increased by \$16.2 million primarily as a result of the reclassification of land in Gresham, Oregon from held and used to held for sale because the held for sale criteria were met during the second quarter of 2011.

These increases in working capital were offset in part by the following:

Accounts receivable decreased by \$78.2 million primarily as a result of lower revenues from discontinued operations due to the sale of the external storage systems business.

Working capital increased by \$7.8 million to \$738.9 million as of October 3, 2010 from \$731.1 million as of December 31, 2009. The increase was primarily attributable to the following:

Current portion of long-term debt decreased by \$350.0 million as a result of the repayment of our 4% Convertible Subordinated Notes upon their maturity in May 2010;

Inventories increased by \$50.8 million as a result of a slowdown in customer purchases in the last month of the third quarter of 2010;

Edgar Filing: LSI CORP - Form 10-Q

Accounts payable decreased by \$28.4 million primarily due to the normal timing of invoice receipts and payments; and

Other accrued liabilities decreased by \$26.4 million as a result of the utilization of restructuring reserves, payments of taxes and decreases in other accruals related to our operations.

Table of Contents

These increases in working capital were offset in part by the following:

Cash, cash equivalents and short-term investments decreased by \$361.2 million;

Accrued salaries, wages and benefits increased by \$49.8 million primarily as a result of timing differences in the payment of salaries and benefits and the restoration of performance-based compensation accruals, which we reduced in 2009 in response to the global economic downturn;

Accounts receivable decreased by \$25.1 million primarily as a result of an improvement in collections; and

Prepaid expenses and other current assets decreased by \$11.7 million primarily as a result of decreases in prepaid software maintenance and other receivables.

Cash Provided by Operating Activities

During the nine months ended October 2, 2011, we generated \$191.4 million of cash from operating activities as a result of the following:

Net income adjusted for non-cash items, primarily a \$260.1 million gain on the sale of our external storage systems business and \$145.8 million of depreciation and amortization. The non-cash items and other non-operating adjustments are quantified in our condensed consolidated statements of cash flows included in Item 1;

Offset in part by a net decrease of \$77.4 million in assets and liabilities, including changes in working capital components, from December 31, 2010 to October 2, 2011, as discussed above.

During the nine months ended October 3, 2010, we generated \$255.5 million of cash from operating activities as a result of the following:

Net income adjusted for non-cash items, including \$200.7 million of depreciation and amortization and \$51.9 million of stock-based compensation expense. The non-cash items and other non-operating adjustments are quantified in our condensed consolidated statements of cash flows included in Item 1;

Offset in part by a net decrease of \$63.7 million in assets and liabilities, including changes in working capital components, from December 31, 2009 to October 3, 2010, as discussed above.

Cash Provided by/Used in Investing Activities

Cash provided by investing activities for the nine months ended October 2, 2011 was \$418.6 million. The investing activities for the nine months ended October 2, 2011 were the following:

Proceeds from the sale of our external storage systems business, net of transaction fees, of \$475.2 million;

Purchases of property and equipment, net of proceeds from sales, totaling \$45.9 million; and

Edgar Filing: LSI CORP - Form 10-Q

Purchases of available-for-sale debt securities and other investments, net of proceeds from maturities and sales, of \$10.7 million. Cash used in investing activities for the nine months ended October 3, 2010 was \$45.2 million. The investing activities for the nine months ended October 3, 2010 were the following:

Purchases of property and equipment, net of proceeds from sales, totaling \$66.7 million; and

Proceeds from maturities and sales of available-for-sale debt and other investments, net of purchases, of \$21.5 million. We expect capital expenditures to be approximately \$12 million for the remainder of 2011. In recent years, we have reduced our level of capital expenditures as a result of our focus on establishing strategic supplier alliances with foundry semiconductor manufacturers and with third-party assembly and test operations, which enables us to have access to advanced manufacturing capacity while reducing our capital spending requirements.

Table of Contents

We also expect to pay approximately \$322 million in cash for the acquisition of SandForce in early 2012.

Cash Used in Financing Activities

Cash used in financing activities for the nine months ended October 2, 2011 was \$405.7 million, as compared to \$545.7 million for the nine months ended October 3, 2010. The primary financing activities during the nine months ended October 2, 2011 were the use of \$471.8 million to repurchase our common stock, offset in part by proceeds of \$66.1 million from issuances of common stock under our employee stock plans. On March 9, 2011, our Board of Directors authorized a stock repurchase program of up to \$750.0 million of our common stock. As of October 2, 2011, \$278.2 million remained available under this stock repurchase program.

The primary financing activities during the nine months ended October 3, 2010 were the use of \$350 million to repay all of our outstanding 4% Convertible Subordinated Notes upon their maturity on May 15, 2010 and the use of \$217.7 million to repurchase our common stock, which were offset in part by proceeds of \$22.0 million from issuances of common stock under our employee stock plans.

We do not currently pay any cash dividends to our stockholders.

Cash, cash equivalents and short-term investments are our primary source of liquidity. We believe that our existing liquid resources and cash generated from operations will be adequate to meet our operating and capital requirements and other obligations for more than the next 12 months. We may, however, find it desirable to obtain additional debt or equity financing. Such financing may not be available to us at all or on acceptable terms if we determine that it would be desirable to obtain additional financing.

CONTRACTUAL OBLIGATIONS

The following table summarizes our contractual obligations as of October 2, 2011:

	Payments Due by Period					Total
	Less Than 1 Year	1-3 Years	4-5 Years	After 5 Years	Other	
	(In millions)					
Operating lease obligations	\$ 45.3	\$ 52.9	\$ 10.8	\$ 2.0	\$	\$ 111.0
Purchase commitments	361.2	27.9	1.5			390.6
Pension contributions	11.5	*	*	*	*	11.5
Uncertain tax positions					86.7**	86.7
Total	\$ 418.0	\$ 80.8	\$ 12.3	\$ 2.0	\$ 86.7	\$ 599.8

* We have pension plans covering substantially all former Agere U.S. employees, excluding management employees hired after June 30, 2003. We also have pension plans covering certain international employees. Although additional future contributions will be required, the amount and timing of these contributions will be affected by actuarial assumptions, the actual rate of return on plan assets, the level of market interest rates, and the amount of voluntary contributions to the plans. The amount shown in the table represents our planned contributions to our pension plans for the remainder of 2011. Because any contributions for 2012 and later will depend on the value of the plan assets in the future and thus are uncertain, we have not included any amounts for 2012 and beyond in the above table.

** This amount represents the non-current tax payable obligation. We are unable to make a reasonably reliable estimate as to when cash settlement with a taxing authority may occur.

Operating Lease Obligations

We lease real estate and certain non-manufacturing equipment under non-cancellable operating leases. We also include non-cancellable obligations under certain software licensing arrangements in this category.

Table of Contents

Purchase Commitments

We maintain purchase commitments with certain suppliers, primarily for raw materials and manufacturing services and for some non-production items. Purchase commitments for inventory materials are generally restricted to a forecasted time horizon as mutually agreed upon between the parties. This forecasted time horizon can vary for different suppliers.

Uncertain Tax Positions

As of October 2, 2011, we had \$142.9 million of unrecognized tax benefits, for which we are unable to make a reasonably reliable estimate as to when cash settlement with a taxing authority may occur. It is reasonably possible that the total amount of unrecognized tax benefits will increase or decrease in the next 12 months. Such changes could occur based on the normal expiration of statutes of limitations or the possible conclusion of ongoing tax audits in various jurisdictions around the world. If those events occur within the next 12 months, we estimate that the unrecognized tax benefits, plus accrued interest and penalties, could decrease by up to \$16.8 million.

Standby Letters of Credit

As of October 2, 2011 and December 31, 2010, we had outstanding obligations relating to standby letters of credit of \$2.9 million and \$3.9 million, respectively. Standby letters of credit are financial guarantees provided by third parties for leases, customs and certain self-insured risks. If the guarantees are called, we must reimburse the provider of the guarantee. The fair value of the letters of credit approximates the contract amount. The standby letters of credit generally renew annually.

CRITICAL ACCOUNTING POLICIES

There have been no significant changes in our critical accounting estimates or significant accounting policies during the nine months ended October 2, 2011 as compared to the discussion in Part II, Item 7 and in Note 1 to our financial statements in Part II, Item 8 of our Annual Report on Form 10-K for the year ended December 31, 2010.

RECENT ACCOUNTING PRONOUNCEMENTS

The information contained in Note 1 to our financial statements in Item 1 under the heading *Recent Accounting Pronouncements* is incorporated by reference into this Item 2.

Item 3. *Quantitative and Qualitative Disclosures about Market Risk*

There have been no significant changes in the market risk disclosures during the nine months ended October 2, 2011 as compared to the discussion in Part II, Item 7A of our Annual Report on Form 10-K for the year ended December 31, 2010.

Item 4. *Controls and Procedures*

Evaluation of Disclosure Controls and Procedures: The Securities and Exchange Commission defines the term *disclosure controls and procedures* to mean a company's controls and other procedures that are designed to ensure that information required to be disclosed in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in our reports filed under the Securities Exchange Act is accumulated and communicated to management, including our chief executive officer and chief financial officer, as appropriate, to allow timely decisions regarding required or necessary disclosures. Our chief executive officer and chief financial officer have concluded, based on the evaluation of the effectiveness of the disclosure controls and procedures by our management with the participation of our chief executive officer and chief financial officer, as of the end of the period covered by this report, that our disclosure controls and procedures were effective for this purpose.

Changes in Internal Control: During the third quarter of 2011, we did not make any change in our internal control over financial reporting that materially affected or is reasonably likely to materially affect our internal control over financial reporting.

Table of Contents

PART II OTHER INFORMATION

Item 1. *Legal Proceedings*

This information is included under the caption "Legal Matters" in Note 14 to our financial statements in Item 1 of Part I.

Item 1A. *Risk Factors*

Set forth below are risks and uncertainties, many of which are discussed in greater detail in our Annual Report on Form 10-K for the year ended December 31, 2010, that, if they were to occur, could materially adversely affect our business or could cause our actual results to differ materially from the results contemplated by the forward-looking statements in this report and other public statements we make:

We depend on a small number of customers. The loss of, or a significant reduction in revenue from, any of these customers would harm our results of operations.

If we fail to keep pace with technological advances, or if we pursue technologies that do not become commercially accepted, customers may not buy our products and our results of operations may be harmed.

We operate in intensely competitive markets, and our failure to compete effectively would harm our results of operations.

Customer orders and ordering patterns can change quickly, making it difficult for us to predict our revenues and making it possible that our actual revenues may vary materially from our expectations, which could harm our results of operations and stock price.

We depend on outside suppliers to manufacture, assemble, package and test our products; accordingly, any failure to secure and maintain sufficient manufacturing capacity at attractive prices or to maintain the quality of our products could harm our business and results of operations.

Failure to qualify our products or our suppliers' manufacturing lines with key customers could harm our business and results of operations.

Any defects in our products could harm our reputation, customer relationships and results of operations.

Our pension plans are underfunded, and may require significant future contributions, which could have an adverse impact on our business.

We may be subject to intellectual property infringement claims and litigation, which could cause us to incur significant expenses or prevent us from selling our products.

If we are unable to protect or assert our intellectual property rights, our business and results of operations may be harmed.

If we are unable to reduce costs associated with the external storage systems business that we sold to NetApp, our results of operations may be adversely affected.

Following the sale of our external storage systems business, we are providing services and office space to NetApp on a temporary basis and are compensated for doing so by NetApp. Once we stop providing those services and office space to NetApp, we may have systems and office space that we must pay for but do not need for our business. If we are not able to eliminate these costs promptly, our results of operations may be adversely affected.

We are exposed to legal, business, political and economic risks associated with our international operations.

We use indirect channels of product distribution over which we have limited control.

We may engage in acquisitions and strategic alliances, which may not be successful and could harm our business and operating results.

The semiconductor industry is highly cyclical, which may cause our operating results to fluctuate.

Table of Contents

Our failure to attract, retain and motivate key employees could harm our business.

Our operations and our suppliers' operations are subject to natural disasters and other events outside of our control that may disrupt our business and harm our operating results.

Recently, Thailand has experienced flooding as a result of significant rains. We have a supplier in Thailand that performs assembly and test functions for our semiconductor products and that supplier's facility has been affected by flooding. Other semiconductor companies also have facilities in Thailand that may be affected by flooding. To the extent that there is an extended period during which our supplier's assembly and test facility is not able to function and we are unable to obtain alternate sources of supply, our ability to deliver products, particularly products used in hard disk drives, could be affected and we may not be able to supply all of our customers' demand. Further, if our customers are unable to obtain sufficient parts from other suppliers because of the flooding, their demand for our products may be reduced. We currently believe that the impact of the flooding will have an adverse impact on our revenue in the fourth quarter of 2011.

We are subject to various environmental laws and regulations that could impose substantial costs on us and may harm our business.

Our blank check preferred stock and Delaware law contain provisions that may inhibit potential acquisition bids, which may harm our stock price, discourage merger offers or prevent changes in our management.

Class action litigation due to stock price volatility or other factors could cause us to incur substantial costs and divert our management's attention and resources.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

The following table contains information about the repurchases of our common stock during the quarter ended October 2, 2011.

Issuer Purchases of Equity Securities

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Publicly Announced Plans or Programs	Dollar Value of Shares that May Yet Be Purchased Under the Programs
July 4 - August 3, 2011		\$		\$ 353,208,822
August 4 - September 3, 2011	10,383,417	\$ 6.71	10,383,417	\$ 283,512,868
September 4 - October 2, 2011	787,644	\$ 6.73	787,644	\$ 278,213,291
Total	11,171,061	\$ 6.71	11,171,061	

On March 9, 2011, our Board of Directors authorized the repurchase of up to \$750 million of our common stock. The repurchases reported in the table above were made pursuant to this authorization.

Item 6. Exhibits

See the Exhibit Index, which follows the signature page to this report.

Table of Contents

SIGNATURES

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

LSI CORPORATION
(Registrant)

Date: November 10, 2011

By /s/ Bryon Look
Bryon Look
Executive Vice President, Chief Financial Officer
and Chief Administrative Officer

31

Table of Contents

EXHIBIT INDEX

31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a)
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a)
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. 1350
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. 1350
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