

LSI CORP
Form 10-Q
May 09, 2013
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 March 31, 2013

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)

1320 Ridder Park Drive

San Jose, California 95131

(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 May 2, 2013, there were 549,559,114 shares of the registrant's Common Stock, \$.01 par value, outstanding.

Table of Contents

LSI CORPORATION

FORM 10-Q

For the Quarter Ended March 31, 2013

INDEX

	Page No.
<u>PART I. FINANCIAL INFORMATION</u>	
<u>Item 1. Financial Statements (Unaudited)</u>	3
<u>Condensed Consolidated Balance Sheets as of March 31, 2013 and December 31, 2012</u>	3
<u>Condensed Consolidated Statements of Operations for the three months ended March 31, 2013 and April 1, 2012</u>	4
<u>Condensed Consolidated Statements of Comprehensive Income for the three months ended March 31, 2013 and April 1, 2012</u>	5
<u>Condensed Consolidated Statements of Cash Flows for the three months ended March 31, 2013 and April 1, 2012</u>	6
<u>Notes to Condensed Consolidated Financial Statements</u>	7
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	16
<u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u>	23
<u>Item 4. Controls and Procedures</u>	23
<u>PART II. OTHER INFORMATION</u>	
<u>Item 1. Legal Proceedings</u>	23
<u>Item 1A. Risk Factors</u>	23
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	24
<u>Item 6. Exhibits</u>	24
<u>Signatures</u>	25
<u>Exhibit Index</u>	26

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 materially 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)**

	March 31, 2013	December 31, 2012
ASSETS		
Cash and cash equivalents	\$ 425,225	\$ 471,528
Short-term investments	233,305	204,457
Accounts receivable, less allowances of \$4,620 and \$6,770, respectively	223,185	264,112
Inventories	181,071	206,323
Prepaid expenses and other current assets	70,046	80,372
Total current assets	1,132,832	1,226,792
Property and equipment, net	277,995	269,747
Identified intangible assets, net	456,490	486,119
Goodwill	255,005	255,005
Other assets	118,573	118,502
Total assets	\$ 2,240,895	\$ 2,356,165
LIABILITIES AND STOCKHOLDERS EQUITY		
Accounts payable	\$ 170,334	\$ 209,699
Accrued salaries, wages and benefits	104,703	129,533
Other accrued liabilities	166,491	177,662
Total current liabilities	441,528	516,894
Pension and post-retirement benefit obligations	541,397	559,252
Income taxes payable non-current	99,102	102,246
Other non-current liabilities	17,898	18,149
Total liabilities	1,099,925	1,196,541
Commitments and contingencies (Note 12)		
Stockholders' equity:		
Preferred stock, \$.01 par value: 2,000 shares authorized; none outstanding		
Common stock, \$.01 par value: 1,300,000 shares authorized; 548,826 and 550,894 shares outstanding, respectively	5,488	5,509
Additional paid-in capital	5,530,418	5,573,248
Accumulated deficit	(3,822,371)	(3,840,803)
Accumulated other comprehensive loss	(572,565)	(578,330)
Total stockholders' equity	1,140,970	1,159,624
Total liabilities and stockholders' equity	\$ 2,240,895	\$ 2,356,165

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 OPERATIONS

(In thousands, except per share amounts)

(Unaudited)

	Three Months Ended	
	March 31, 2013	April 1, 2012
Revenues	\$ 568,636	\$ 622,424
Cost of revenues	279,132	335,512
Gross profit	289,504	286,912
Research and development	171,305	169,871
Selling, general and administrative	89,495	90,100
Restructuring of operations and other items, net	20,452	15,462
Income from operations	8,252	11,479
Interest income and other, net	7,880	14,656
Income before income taxes	16,132	26,135
Benefit from income taxes	(2,300)	(49,062)
Net income	\$ 18,432	\$ 75,197
Net income per share:		
Basic	\$ 0.03	\$ 0.13
Diluted	\$ 0.03	\$ 0.13
Shares used in computing per share amounts:		
Basic	550,227	566,709
Diluted	567,092	590,556

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

Table of Contents**LSI CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME****(In thousands)****(Unaudited)**

	Three Months Ended	
	March 31, 2013	April 1, 2012
Net income	\$ 18,432	\$ 75,197
Other comprehensive income before tax:		
Foreign currency translation adjustments	(342)	1,447
Available-for-sale securities:		
Unrealized gain on investments	1,980	338
Reclassification of net realized loss/(gain) on investments to net income	17	(142)
Derivative financial instruments:		
Unrealized (loss)/gain on derivatives	(32)	640
Reclassification of net realized (gain)/loss on derivatives to net income	(162)	673
Amortization of transition asset, prior service cost and net actuarial loss on defined benefit pension and post-retirement plans	5,044	3,969
Other comprehensive income before tax	6,505	6,925
Income tax expense on unrealized gain on investments	740	
Other comprehensive income, net of tax	5,765	6,925
Comprehensive income	\$ 24,197	\$ 82,122

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)**

	Three Months Ended	
	March 31, 2013	April 1, 2012
Operating activities:		
Net income	\$ 18,432	\$ 75,197
Adjustments:		
Depreciation and amortization	44,285	45,368
Stock-based compensation expense	25,546	30,834
Non-cash restructuring of operations and other items, net	6,596	2,140
Gain on re-measurement of a pre-acquisition equity interest to fair value		(5,765)
(Gain)/loss on sale of property and equipment	(4)	25
Unrealized foreign exchange loss	589	1,461
Deferred taxes	(26)	(43,202)
Changes in assets and liabilities, net of assets acquired and liabilities assumed in business combination:		
Accounts receivable, net	40,652	(44,845)
Inventories	25,123	3,453
Prepaid expenses and other assets	(7,955)	(2,290)
Accounts payable	(33,054)	47,119
Accrued and other liabilities	(57,354)	(59,270)
Net cash provided by operating activities	62,830	50,225
Investing activities:		
Purchases of debt securities available-for-sale	(53,345)	(21,263)
Proceeds from maturities and sales of debt securities available-for-sale	24,117	9,506
Purchases of other investments	(750)	
Purchases of property and equipment	(25,075)	(64,982)
Proceeds from sale of property and equipment	27	21
Acquisition of business, net of cash acquired		(319,231)
Net cash used in investing activities	(55,026)	(395,949)
Financing activities:		
Issuances of common stock	8,165	65,274
Purchases of common stock under repurchase programs	(60,765)	(38,206)
Net cash (used in)/provided by financing activities	(52,600)	27,068
Effect of exchange rate changes on cash and cash equivalents	(1,507)	(495)
Net change in cash and cash equivalents	(46,303)	(319,151)
Cash and cash equivalents at beginning of period	471,528	779,811
Cash and cash equivalents at end of period	\$ 425,225	\$ 460,660

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****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 first quarters of 2013 and 2012 consisted of 13 weeks each and ended on March 31, 2013 and April 1, 2012, respectively. The results of operations for the quarter ended March 31, 2013 are not necessarily indicative of the results to be expected for the full year.

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 the 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, comprehensive income 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, 2012.

Recent Accounting Pronouncement

In February 2013, the Financial Accounting Standards Board (FASB) issued additional guidance regarding the presentation of comprehensive income. The guidance requires an entity to present the effects on net income line items of significant amounts reclassified out of accumulated other comprehensive income, but only if the item reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same reporting period. An entity shall provide this information either on the face of the financial statements or in the notes to the financial statements. The guidance is effective for fiscal years beginning after December 15, 2012. The Company adopted this guidance in the first quarter of 2013. The adoption did not impact the Company's results of operations or financial position.

Note 2 Stock-Based Compensation Expense

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 by expense category was as follows:

	Three Months Ended	
	March 31, 2013	April 1, 2012
	(In thousands)	
Cost of revenues	\$ 2,875	\$ 3,512
Research and development	12,409	12,308
Selling, general and administrative	10,262	15,014
Total stock-based compensation expense	\$ 25,546	\$ 30,834

The income tax benefit that the Company realized for the tax deduction from option exercises and other awards was not material for any periods presented.

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:

Edgar Filing: LSI CORP - Form 10-Q

	Three Months Ended	
	March 31, 2013	April 1, 2012
Estimated grant date fair value per share	\$ 2.33	\$ 2.86
Expected life (years)	4.38	4.46
Risk-free interest rate	1%	1%
Volatility	49%	47%

The following table summarizes changes in stock options outstanding:

Table of Contents

	Number of Shares (In thousands)	Weighted-Average Exercise Price Per Share	Weighted-Average Remaining Contractual Term (In years)	Aggregate Intrinsic Value (In thousands)
Options outstanding at December 31, 2012	56,042	\$ 5.75		
Granted	6,247	\$ 6.89		
Exercised	(2,192)	\$ 3.72		
Canceled	(1,006)	\$ 8.24		
Options outstanding at March 31, 2013	59,091	\$ 5.90	3.86	\$ 85,227
Options exercisable at March 31, 2013	39,726	\$ 5.87	2.72	\$ 62,059

As of March 31, 2013, the total unrecognized compensation expense related to unvested stock options, net of estimated forfeitures, was \$41.8 million and is expected to be recognized over the next 2.6 years on a weighted-average basis.

Restricted Stock Units (RSUs)

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

Service-based:

The vesting of service-based RSUs requires that the employees remain employed by the Company for a specified period of time.

The following table summarizes changes in service-based RSUs outstanding:

	Number of Units (In thousands)	Weighted-Average Grant Date Fair Value per Share
Unvested service-based RSUs outstanding at December 31, 2012	17,655	\$ 6.99
Granted	7,227	\$ 6.90
Vested	(4,461)	\$ 6.84
Forfeited	(309)	\$ 6.77
Unvested service-based RSUs outstanding at March 31, 2013	20,112	\$ 7.00

As of March 31, 2013, the total unrecognized compensation expense related to the service-based RSUs, net of estimated forfeitures, was \$124.0 million and will be recognized over the next 3 years on a weighted-average basis.

Performance-based:

The vesting of performance-based RSUs is contingent upon the Company meeting specified performance criteria and requires that the employees remain employed by the Company for a specified period of time.

The following table summarizes changes in performance-based RSUs outstanding:

Number of Units	Weighted-Average Grant Date Fair Value per Share
-----------------	--

Edgar Filing: LSI CORP - Form 10-Q

	(In thousands)		
Unvested performance-based RSUs outstanding at December 31, 2012	5,634	\$	7.29
Granted	1,441	\$	6.89
Vested	(2,324)	\$	7.87
Forfeited	(330)	\$	6.40
Unvested performance-based RSUs outstanding at March 31, 2013	4,421	\$	6.93

As of March 31, 2013, the total unrecognized compensation expense related to the performance-based RSUs, net of estimated forfeitures, was \$17.2 million and, if the performance conditions are fully met, will be recognized over the next 3 years.

Table of Contents**Employee Stock Purchase Plan**

Compensation expense for the 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. No shares related to the ESPP were issued during the three months ended March 31, 2013 or April 1, 2012.

Note 3 Common Stock Repurchases

On August 1, 2012, the Company's board of directors authorized a common stock repurchase program of up to \$500.0 million of its common stock. As of March 31, 2013, \$417.9 million remained available for repurchases under this program.

During the three months ended March 31, 2013, the Company repurchased 8.6 million shares for \$60.8 million. During the three months ended April 1, 2012, the Company repurchased 4.6 million shares for \$38.2 million. Repurchased shares are retired immediately after the repurchases are completed. Retirement of repurchased shares is recorded as a reduction of common stock and additional paid-in capital.

Note 4 Restructuring and Other Items

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

	Three Months Ended	
	March 31, 2013	April 1, 2012
	(In thousands)	
Lease and contract terminations	\$ 1,768(a)	\$ 1,634(a)
Employee severance and benefits	4,386	431
Total restructuring expense	6,154	2,065
Other items, net	14,298(b)	13,397(c)
Total restructuring of operations and other items, net	\$ 20,452	\$ 15,462

(a) Includes lease obligation costs for facilities that the Company ceased to use, changes in estimates, changes in time value and on-going expenditures related to previously vacated facilities.

(b) Primarily consists of \$12.6 million of costs related to litigation settlements.

(c) Primarily consists of \$8.3 million of SandForce, Inc. (SandForce) acquisition-related costs and \$4.6 million of costs related to the transition service agreement associated with the sale of the external storage systems business.

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

	Lease and Contract Terminations	Employee Severance and Benefits (In thousands)	Total
Balance at December 31, 2012	\$ 12,991	\$ 5,003	\$ 17,994
Expense	1,768	4,386	6,154
Utilized	(6,441)(a)	(4,970)(a)	(11,411)

Edgar Filing: LSI CORP - Form 10-Q

Balance at March 31, 2013	\$ 8,318(b)	\$ 4,419(b)	\$ 12,737
---------------------------	-------------	-------------	-----------

(a) Represents cash payments.

(b) The balance remaining for the lease terminations is expected to be paid during the remaining terms of the leases, which extend through 2014. The majority of the balance remaining for employee severance and benefits is expected to be paid by the end of 2013.

Note 5 Benefit Obligations

The Company provides retirement benefits to certain current and former U.S. employees under defined benefit pension plans, which include a management plan and a represented plan. Benefits under the management plan are based on an adjusted career-average-pay formula or a cash-balance program. Benefits under the represented plan are based on a dollar-per-month formula. Benefit accruals under the management plan were frozen in 2009. Participants in the adjusted career-average-pay program no longer earn service accruals. Participants in the cash-balance program no longer earn service accruals, but continue to earn 4% interest per year on their cash-balance accounts. There are 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 the management plan. In addition, the Company provides post-retirement life insurance coverage under a group life insurance plan for certain U.S. employees. The Company also has pension plans covering certain international employees.

Table of Contents

The following table summarizes the components of the net periodic benefit cost:

	Three Months Ended			
	March 31, 2013	March 31, 2013		April 1, 2012
	Pension Benefits	Post-retirement Benefits	Pension Benefits	Post-retirement Benefits
	(In thousands)			
Service cost	\$ 123	\$ 25	\$ 109	\$ 25
Interest cost	14,270	600	15,252	650
Expected return on plan assets	(16,581)	(875)	(17,023)	(1,050)
Amortization of net actuarial loss, prior service cost and transition asset	4,669	375	3,469	500
Total benefit cost	\$ 2,481	\$ 125	\$ 1,807	\$ 125

During the three months ended March 31, 2013, the Company contributed \$15.3 million to its pension plans. The Company expects to contribute an additional \$36.4 million to its pension plans during the remainder of 2013. The Company does not expect to contribute to its post-retirement benefit plan in 2013.

Note 6 Cash Equivalents and Investments

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

	Fair Value Measurements as of March 31, 2013		
	Level 1	Level 2	Total
	(In thousands)		
Cash equivalents:			
Money-market funds	\$ 325,927(a)	\$	\$ 325,927
Government and agency securities		8,547(b)	8,547
Commercial paper		2,500(b)	2,500
Total cash equivalents	\$ 325,927	\$ 11,047	\$ 336,974

Available-for-sale debt securities:

Asset-backed and mortgage-backed securities:

Agency securities	\$	\$ 145,150(b)	\$ 145,150
Non-agency securities		1,116(b)	1,116
Government and agency securities	15,003(a)	58,032(b)	73,035
Corporate debt securities		10,006(b)	10,006
Commercial paper		3,998(b)	3,998
Total short-term investments	\$ 15,003	\$ 218,302	\$ 233,305

Long-term investments in equity securities:

Marketable available-for-sale equity securities	\$ 1,952(c)	\$	\$ 1,952
---	-------------	----	----------

	Fair Value Measurements as of December 31, 2012		
	Level 1	Level 2	Total
	(In thousands)		
Cash equivalents:			
Money-market funds	\$ 364,596(a)	\$	\$ 364,596

Edgar Filing: LSI CORP - Form 10-Q

Government and agency securities		6,479(b)	6,479
Total cash equivalents	\$ 364,596	\$ 6,479	\$ 371,075
Available-for-sale debt securities:			
Asset-backed and mortgage-backed securities:			
Agency securities	\$	\$ 129,463(b)	\$ 129,463
Non-agency securities		1,393(b)	1,393
Government and agency securities	17,042(a)	49,658(b)	66,700
Corporate debt securities		6,001(b)	6,001
Commercial paper		900(b)	900
Total short-term investments	\$ 17,042	\$ 187,415	\$ 204,457
Long-term investments in equity securities:			
Marketable available-for-sale equity securities	\$ 1,689(c)	\$	\$ 1,689

Table of Contents

- (a) The fair value of money-market funds is determined using unadjusted prices in active markets. The fair value of Level 1 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 prices in active markets. These amounts are included within other assets in the condensed consolidated balance sheets.

As of March 31, 2013 and December 31, 2012, the aggregate carrying value of the Company's non-marketable securities was \$42.8 million and \$42.1 million, respectively.

Upon the acquisition of SandForce in January 2012, the Company recognized a gain of \$5.8 million as a result of re-measuring its pre-acquisition equity interest in SandForce to estimated fair value. There were no other non-marketable securities fair-valued during the three months ended March 31, 2013 or April 1, 2012.

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

	Amortized Cost	March 31, 2013		Fair Value
		Gross Unrealized Gain	Gross Unrealized Loss	
(In thousands)				
Short-term debt securities:				
Asset-backed and mortgage-backed securities	\$ 139,611	\$ 7,484	\$ (829)	\$ 146,266
Government and agency securities	72,194	843	(2)	73,035
Corporate debt securities	9,885	124	(3)	10,006
Commercial paper	3,998			3,998
Total short-term debt securities	\$ 225,688	\$ 8,451	\$ (834)	\$ 233,305
Long-term marketable equity securities	\$ 669	\$ 1,283	\$	\$ 1,952

	Amortized Cost	December 31, 2012		Fair Value
		Gross Unrealized Gain	Gross Unrealized Loss	
(In thousands)				
Short-term debt securities:				
Asset-backed and mortgage-backed securities	\$ 125,563	\$ 6,390	\$ (1,097)	\$ 130,856
Government and agency securities	65,904	802	(6)	66,700
Corporate debt securities	5,864	137		6,001
Commercial paper	900			900
Total short-term debt securities	\$ 198,231	\$ 7,329	\$ (1,103)	\$ 204,457
Long-term marketable equity securities	\$ 669	\$ 1,020	\$	\$ 1,689

As of March 31, 2013, there were 107 investments in an unrealized loss position. 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:

	March 31, 2013	
	Less than 12 Months	Greater than 12 Months

Edgar Filing: LSI CORP - Form 10-Q

	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
		(In thousands)		
Asset-backed and mortgage-backed securities	\$ 47,476	\$ (749)	\$ 3,728	\$ (80)
Government and agency securities	4,910	(2)		
Corporate debt securities	2,956	(3)		
Total	\$ 55,342	\$ (754)	\$ 3,728	\$ (80)

Table of Contents

	December 31, 2012			
	Less than 12 Months		Greater than 12 Months	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(In thousands)			
Asset-backed and mortgage-backed securities	\$ 38,280	\$ (1,018)	\$ 4,141	\$ (79)
Government and agency securities	18,301	(6)		
Total	\$ 56,581	\$ (1,024)	\$ 4,141	\$ (79)

Net realized losses and gains on sales of available-for-sale securities were not material for the three months ended March 31, 2013 or April 1, 2012.

Contractual maturities of available-for-sale debt securities as of March 31, 2013 were as follows:

	Available-For-Sale Debt Securities (In thousands)
Due within one year	\$ 29,424
Due in 1-5 years	59,264
Due in 5-10 years	10,497
Due after 10 years	134,120
Total	\$ 233,305

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

Note 7 Supplemental Financial Information**Inventories**

	March 31, 2013	December 31, 2012
	(In thousands)	
Raw materials	\$ 71	\$ 176
Work-in-process	39,281	52,003
Finished goods	141,719	154,144
Total inventories	\$ 181,071	\$ 206,323

Accumulated Other Comprehensive Loss

The following table presents the components of, and changes in, accumulated other comprehensive loss, net of taxes:

Balance at December 31, 2012	Other Comprehensive Income before Reclassifications	Amounts Reclassified from Accumulated Other Comprehensive Loss (a)	Net Current Period Other Comprehensive Income	Balance at March 31, 2013
---------------------------------	---	---	--	------------------------------

Edgar Filing: LSI CORP - Form 10-Q

	(In thousands)				
Foreign currency translation adjustments	\$ 39,881	\$ (342)	\$	\$ (342)	\$ 39,539
Net unrealized gain on investments	4,484	1,240	17	1,257	5,741
Net unrealized gain on derivatives	224	(32)	(162)	(194)	30
Defined benefit pension and post-retirement plans	(622,919)		5,044	5,044	(617,875)
Total accumulated other comprehensive loss	\$ (578,330)	\$ 866	\$ 4,899	\$ 5,765	\$ (572,565)

- (a) The reclassified components of defined benefit pension and post-retirement plans were included in the computation of net periodic benefit cost (see Note 5). All other reclassified amounts were insignificant.

Reconciliation of Basic and Diluted Shares

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

Table of Contents

	Three Months Ended	
	March 31, 2013	April 1, 2012
	(In thousands)	
Basic shares	550,227	566,709
Dilutive effect of stock options, employee stock purchase rights and restricted stock unit awards	16,865	23,847
Diluted shares	567,092	590,556

The weighted-average common share equivalents that were excluded from the computation of diluted shares because their inclusion would have had an anti-dilutive effect on net income per share were as follows:

	Three Months Ended	
	March 31, 2013	April 1, 2012
	(In thousands)	
Anti-dilutive securities:		
Stock options	29,420	15,929
Restricted stock unit awards	1,632	4,710

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 assets and liabilities 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

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, when the hedged expense is recognized, is subsequently reclassified into earnings within the same line item in the statement of operations as the impact of the hedged transaction. The ineffective portion of the gain or loss is reported in earnings immediately. As of March 31, 2013 and December 31, 2012, the total notional value of the Company's outstanding forward contracts, designated as foreign-currency cash-flow hedges, was \$40.3 million and \$39.8 million, respectively.

Other Foreign-Currency Hedges

The Company enters into foreign-exchange forward contracts that are used to hedge certain assets or liabilities denominated in non-functional currencies 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 March 31, 2013 and December 31, 2012, the total notional value of the Company's outstanding forward contracts, not designated as hedges under hedge accounting, was \$40.4 million and \$31.6 million, respectively. For the three months ended March 31, 2013 and April 1, 2012, the Company recognized a loss of \$1.2 million and a gain of \$1.1 million on other foreign-currency hedges, respectively. These amounts are included in interest income and other, net in the Company's condensed consolidated statements of operations and were substantially offset by the gain and loss on the underlying foreign-currency-denominated assets or liabilities.

Fair Value of Derivative Instruments

The total fair value of derivative assets and liabilities was recorded in prepaid expenses and other current assets and in other accrued liabilities, respectively, in the condensed consolidated balance sheets. As of March 31, 2013 and December 31, 2012, the total fair value of derivative assets and liabilities was immaterial.

Note 9 Segment, Geographic and Product Information

Edgar Filing: LSI CORP - Form 10-Q

The Company operates in one reportable segment – the Semiconductor segment. The Company’s chief executive officer is the chief operating decision maker (CODM). The Company’s CODM bears ultimate responsibility for, and is actively engaged in, the allocation of resources and the evaluation of the Company’s operating and financial results.

Table of Contents**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, revenues by geography as presented below may not accurately reflect geographic end-user demand for its products.

	Three Months Ended	
	March 31, 2013	April 1, 2012
	(In thousands)	
North America*	\$ 146,650	\$ 158,969
Asia	373,933	414,022
Europe and the Middle East	48,053	49,433
Total	\$ 568,636	\$ 622,424

* Primarily the United States.

Information about Product Groups

The following table presents the Company's revenues by product groups:

	Three Months Ended	
	March 31, 2013	April 1, 2012
	(In thousands)	
Storage products	\$ 437,901	\$ 488,469
Networking products	92,603	107,022
Other	38,132	26,933
Total	\$ 568,636	\$ 622,424

Note 10 Income Taxes

The Company recorded income tax benefits of \$2.3 million and \$49.1 million for the three months ended March 31, 2013 and April 1, 2012, respectively.

The income tax benefit for the three months ended March 31, 2013 included a reversal of \$8.6 million of liabilities for uncertain tax positions, which included previously unrecognized tax benefits of \$3.8 million and interest and penalties of \$4.8 million, as a result of the expiration of statutes of limitations in multiple jurisdictions.

The income tax benefit for the three months ended April 1, 2012 included a tax benefit of approximately \$43.2 million due to the release of valuation allowance resulting from the net deferred tax liabilities recorded as part of the SandForce purchase price allocation. The income tax benefit for the three months ended April 1, 2012 also included a reversal of \$10.2 million of liabilities for uncertain tax positions, which included previously unrecognized tax benefits of \$5.2 million and interest and penalties of \$5.0 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. Historically, the Company has sustained losses from its U.S. operations and, as a result, has maintained a full valuation allowance against U.S. net deferred tax assets. The Company recently achieved profitability in the U.S., however, management does not believe there is sufficient positive evidence to reach a conclusion that it is more likely than not that the Company will generate sufficient future taxable income in the U.S. to realize the benefits of its deferred tax assets.

Edgar Filing: LSI CORP - Form 10-Q

Depending on future results and projected trends, it is reasonably possible that Company may determine in the foreseeable future that it is more likely than not that a significant portion of its U.S. deferred tax assets will be realized, resulting in a release of a significant portion of the valuation allowance.

As of March 31, 2013, the Company had \$195.3 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 \$23.8 million.

Note 11 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 \$153.7 million and \$207.0 million for the three months ended March 31, 2013 and April 1, 2012, respectively. The Company had accounts receivable from Seagate of \$86.7 million and \$94.0 million as of March 31, 2013 and December 31, 2012, respectively.

Table of Contents

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 \$9.4 million and \$12.2 million of inventory from SMP during the three months ended March 31, 2013 and April 1, 2012, respectively. As of March 31, 2013 and December 31, 2012, the amounts payable to SMP were \$6.2 million and \$9.2 million, respectively.

Note 12 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 March 31, 2013, the Company had purchase commitments of \$350.4 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 following table sets forth a summary of changes in product warranties:

	Accrued Warranties (In thousands)
Balance as of December 31, 2012	\$ 5,426
Accruals for warranties issued during the period	107
Adjustments to pre-existing accruals (including changes in estimates)	395
Settlements made during the period (in cash or in kind)	(295)
Balance as of March 31, 2013	\$ 5,633

Standby Letters of Credit:

The Company had outstanding obligations relating to standby letters of credit of \$4.2 million and \$4.1 million, respectively, as of March 31, 2013 and December 31, 2012. 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

Edgar Filing: LSI CORP - Form 10-Q

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, license agreements or agreements for 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.

Table of Contents**Legal Matters**

On December 6, 2006, Sony Ericsson Mobile Communications USA Inc. (Sony Ericsson) filed a lawsuit against Agere Systems Inc. (Agere), which LSI acquired in 2007, 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 August 4, 2011, the court granted LSI s motion for summary judgment in this matter and ordered the dismissal of all of Sony Ericsson s claims. Sony Ericsson appealed this decision. On January 24, 2013, the New York Appellate Division unanimously affirmed the lower court s ruling. On April 2, 2013, the New York Court of Appeals denied Sony Ericsson s motion seeking to appeal this ruling.

On March 23, 2007, CIF Licensing, LLC, d/b/a GE Licensing (GE) filed a lawsuit against Agere Systems, which is now a subsidiary of LSI, in the United States District Court for the District of Delaware, asserting that Agere products infringed patents in a portfolio of patents GE acquired from Motorola. GE asserted that four of the patents cover inventions relating to modems. The court postponed hearing motions based on Agere s defenses until after the trial, and did not allow Agere to present evidence on its 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 have increased the amount of damages up to three times the original amount. If the jury s verdict had been entered by the court, Agere expected to be required to pay interest from the date of infringing sales. 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. On December 3, 2012, the court affirmed its prior grant of GE s summary judgment motions seeking to bar Agere s defenses of laches and license, but ordered that a trial go forward regarding Agere s exhaustion defense. On April 24, 2013, following a court-ordered mediation, LSI and GE settled this lawsuit. The settlement did not have a material impact on LSI s results of operations or financial condition.

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 any liabilities arising from the matters described above will not have a material adverse effect on the Company s consolidated results of operations, financial position or cash flows.

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 I, 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 offer a broad portfolio of capabilities including custom and standard product integrated circuits that are used in hard disk drives, solid state drives, high-speed communications

Edgar Filing: LSI CORP - Form 10-Q

systems, computer servers, storage systems and personal computers. We deliver our products to our customers as stand-alone integrated circuits as well as incorporated onto circuit boards that offer additional functionality. We also license our intellectual property to other entities.

Table of Contents

On January 3, 2012, we acquired SandForce, Inc., a provider of flash storage processors for enterprise and client flash solutions and solid state drives, for total consideration of approximately \$346.4 million, net of cash acquired. We acquired SandForce to enhance our competitive position in the PCIe® flash adapter space where LSI's products already used SandForce flash storage processors. Additionally, the combination of LSI's custom capability and SandForce's standard product offerings allows us to offer a full range of products aimed at the growing flash storage processor market for ultrabook, notebook and enterprise solid state drives and other flash memory-based solutions.

We derive the majority of our revenues from sales of products for the hard disk and solid state drive, server and networking equipment end markets and our revenues depend on market demand for these types of products. We believe that these markets offer us attractive opportunities because of the growing demand to create, store, manage and move digital content efficiently.

Our products are sold primarily to original equipment manufacturers, or OEMs, in the server, storage and networking industries. We also sell some of our products through a network of resellers and distributors.

The markets in which we operate are highly competitive and our revenues depend on our ability to compete successfully. We face competition not only from makers of products similar to ours, but also from competing technologies.

During the first quarter of 2013, we reported revenues of \$568.6 million, compared to \$622.4 million for the first quarter of 2012. For the first quarter of 2013, we reported net income of \$18.4 million, or \$0.03 per diluted share, compared to \$75.2 million, or \$0.13 per diluted share, for the first quarter of 2012.

Our board of directors authorized a stock repurchase program of up to \$500.0 million on August 1, 2012. During the first quarter of 2013, we repurchased 8.6 million shares for \$60.8 million under this program. As of March 31, 2013, \$417.9 million remained available for stock repurchases. Future purchases under the stock repurchase program are expected to be funded with available cash, cash equivalents and short-term investments. We ended the first quarter of 2013 with cash and cash equivalents, together with short-term investments, of \$658.5 million, compared to \$676.0 million at the end of 2012.

A number of hard disk drive manufacturers have production facilities in Thailand. In the fall of 2011, flooding there forced many of these facilities to stop production. As the industry recovered in early 2012, our revenues benefited. Since late 2012, sales of personal computers have been weak and we expect this to continue in the near term, affecting sales of hard disk and solid state drives and our revenues from semiconductors for hard disk and solid state drives. We also believe that general economic conditions remain weak, and are resulting in reduced spending on information technology products in general, which is also affecting our revenues. Our networking revenues are closely tied to capital spending by wireless telecommunications carriers who have been limiting their capital expenditures in recent quarters. Some large carriers have indicated that they may increase their expenditures later in 2013.

In light of this environment, we are working to manage our operating expenses while at the same time continuing work on products under development. We are focusing our research and development operations on products that we believe provide favorable growth opportunities for our business. We are also working to expand our sales of products in newer areas such as flash memory-based server adapter cards, where we are working directly with large, internet-based datacenter operators, in addition to our more traditional customer base of OEMs and distributors.

RESULTS OF OPERATIONS

Revenues

	Three Months Ended	
	March 31, 2013	April 1, 2012
	(In millions)	
Revenues	\$ 568.6	\$ 622.4

Revenues decreased by \$53.8 million, or 8.6%, for the three months ended March 31, 2013 as compared to the three months ended April 1, 2012. The decrease reflected lower unit sales of semiconductors used in hard disk drives and our older networking products in the first quarter of 2013. In addition, revenues in the first quarter of 2012 reflected temporarily higher unit sales of semiconductors used in hard disk drives as a result of the recovery from the Thailand flooding, which had adversely impacted the hard disk drive industry in late 2011. These decreases were partially offset by increased unit sales from the ramping of flash memory-based storage products and higher intellectual property licensing revenues in the first quarter of 2013.

Table of Contents**Significant Customers:**

The following table provides information about sales to Seagate, which was our only customer that accounted for 10% or more of our revenues in the first quarter of each of 2013 and 2012:

	Three Months Ended	
	March 31, 2013	April 1, 2012
Percentage of revenues	27%	33%

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-user demand for our products.

	Three Months Ended	
	March 31, 2013	April 1, 2012
	(In millions)	
North America*	\$ 146.6	\$ 159.0
Asia	373.9	414.0
Europe and the Middle East	48.1	49.4
Total	\$ 568.6	\$ 622.4

* Primarily the United States.

Revenues in Asia and North America decreased by \$40.1 million, or 9.7%, and \$12.4 million, or 7.8%, respectively for the three months ended March 31, 2013 as compared to the three months ended April 1, 2012. The decreases in both regions were primarily attributable to lower unit sales of semiconductors used in hard disk drives and our older networking products in the first quarter of 2013. In addition, revenues in the first quarter of 2012 reflected temporarily higher unit sales of semiconductors used in hard disk drives as a result of the recovery from the Thailand flooding, which had adversely impacted the hard disk drive industry in late 2011. These decreases were partially offset by increased unit sales from the ramping of flash memory-based storage products and higher intellectual property licensing revenues in the first quarter of 2013.

Revenues by Product Groups:

The following table presents our revenues by product groups:

	Three Months Ended	
	March 31, 2013	April 1, 2012
	(In millions)	
Storage products	\$ 437.9	\$ 488.5
Networking products	92.6	107.0
Other	38.1	26.9
Total	\$ 568.6	\$ 622.4

Revenues from storage products decreased by \$50.6 million, or 10.4%, for the three months ended March 31, 2013 as compared to the three months ended April 1, 2012. This was attributable to lower unit sales of semiconductors used in hard disk drives in the first quarter of 2013 and temporarily higher unit sales of semiconductors used in hard disk drives in the first quarter of 2012 as a result of the recovery from the Thailand

Edgar Filing: LSI CORP - Form 10-Q

flooding, which had adversely impacted the hard disk drive industry in late 2011. These decreases were partially offset by increased unit sales from the ramping of flash memory-based storage products in the first quarter of 2013.

Revenues from networking products decreased by \$14.4 million, or 13.5%, for the three months ended March 31, 2013 as compared to the three months ended April 1, 2012. The decrease was primarily the result of lower unit sales of semiconductors used in our older networking products.

Other revenues increased by \$11.2 million, or 41.6%, for the three months ended March 31, 2013 as compared to the three months ended April 1, 2012. The increase primarily resulted from higher intellectual property licensing revenues in the first quarter of 2013.

Table of Contents**Gross Profit Margin**

	Three Months Ended	
	March 31, 2013	April 1, 2012
	(Dollars in millions)	
Gross profit margin	\$ 289.5	\$ 286.9
Percentage of revenues	50.9%	46.1%

Various factors affect and may continue to affect our product gross margin. These factors include, but are not limited to, changes in our production mix and volume of product sales, the timing of production ramps and margin structures of new products, the positions of our products in their respective life cycles, the effects of competition, the price of commodities used in our products, provisions for excess and obsolete inventories, changes in the costs charged by foundry, assembly and test subcontractors, and amortization of acquired intangible assets.

Gross profit margin as a percentage of revenues increased by 4.8% for the three months ended March 31, 2013 as compared to the three months ended April 1, 2012. The increase was primarily attributable to sales of higher margin products, offset in part by decreased revenues with a similar level of fixed costs in the first quarter of 2013 as compared to the first quarter of 2012.

Research and Development

	Three Months Ended	
	March 31, 2013	April 1, 2012
	(Dollars in millions)	
Research and development	\$ 171.3	\$ 169.9
Percentage of revenues	30.1%	27.3%

R&D expense increased by \$1.4 million, or 0.8%, for the three months ended March 31, 2013 as compared to the three months ended April 1, 2012. The increase was primarily attributable to higher compensation-related expense and increased spending to support our new product development projects.

Selling, General and Administrative

	Three Months Ended	
	March 31, 2013	April 1, 2012
	(Dollars in millions)	
Selling, general and administrative	\$ 89.5	\$ 90.1
Percentage of revenues	15.7%	14.5%

SG&A expense decreased by \$0.6 million, or 0.7%, for the three months ended March 31, 2013 as compared to the three months ended April 1, 2012. The decrease was primarily attributable to lower stock-based compensation expense as a result of a \$4.5 million charge in the first quarter of 2012 related to the accelerated vesting of stock options and restricted stock units for certain SandForce employees. The decrease was offset in part by an increase in litigation costs and higher sales and marketing expenses, including higher compensation-related expenses to support future revenue growth.

Restructuring of Operations and Other Items, net

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

	Three Months Ended	
	March 31, 2013	April 1, 2012
	(In millions)	
Lease and contract terminations	\$ 1.8(a)	\$ 1.6(a)

Edgar Filing: LSI CORP - Form 10-Q

Employee severance and benefits	4.4	0.5
Total restructuring expense	6.2	2.1
Other items, net	14.3(b)	13.4(c)
Total restructuring of operations and other items, net	\$ 20.5	\$ 15.5

- (a) Includes lease obligation costs for facilities that we ceased to use, changes in estimates, changes in time value and on-going expenditures related to previously vacated facilities.
- (b) Primarily consists of \$12.6 million of costs related to litigation settlements.
- (c) Primarily consists of \$8.3 million of SandForce acquisition-related costs and \$4.6 million of costs related to the transition service agreement associated with the sale of the external storage systems business.

Table of Contents**Interest Income and Other, net**

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

	Three Months Ended	
	March 31, 2013	April 1, 2012
	(In millions)	
Interest income	\$ 0.3	\$ 1.6
Other income, net	7.6	13.1
Total	\$ 7.9	\$ 14.7

The \$1.3 million decrease in interest income for the three months ended March 31, 2013 as compared to the three months ended April 1, 2012 primarily resulted from lower returns on investments in the first quarter of 2013 as compared to the first quarter of 2012.

Other income, net, for the three months ended March 31, 2013 primarily included \$6.1 million of insurance proceeds for covered losses from the 2011 Thailand flooding. We do not expect any further insurance recoveries related to the Thailand flooding. Other income, net, for the three months ended April 1, 2012 primarily included a \$5.8 million gain as a result of re-measuring our pre-acquisition equity interest in SandForce to estimated fair value and \$4.5 million of income for services provided under the transition service agreements entered into in connection with the sale of the external storage systems business.

Benefit from Income Taxes

We recorded income tax benefits of \$2.3 million and \$49.1 million for the three months ended March 31, 2013 and April 1, 2012, respectively.

The income tax benefit for the three months ended March 31, 2013 included a reversal of \$8.6 million of liabilities for uncertain tax positions, which included previously unrecognized tax benefits of \$3.8 million and interest and penalties of \$4.8 million, as a result of the expiration of statutes of limitations in multiple jurisdictions.

The income tax benefit for the three months ended April 1, 2012 included a tax benefit of approximately \$43.2 million due to the release of valuation allowance resulting from the net deferred tax liabilities recorded as part of the SandForce purchase price allocation. The income tax benefit for the three months ended April 1, 2012 also included a reversal of \$10.2 million of liabilities for uncertain tax positions, which included previously unrecognized tax benefits of \$5.2 million and interest and penalties of \$5.0 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. Historically, we have sustained losses from our U.S. operations and, as a result, have maintained a full valuation allowance against U.S. net deferred tax assets. We recently achieved profitability in the U.S., however, we do not believe there is sufficient positive evidence to reach a conclusion that it is more likely than not that we will generate sufficient future taxable income in the U.S. to realize the benefits of our deferred tax assets. Depending on future results and projected trends, it is reasonably possible that we may determine in the foreseeable future that it is more likely than not that a significant portion of our U.S. deferred tax assets will be realized, resulting in a release of a significant portion of the valuation allowance.

FINANCIAL CONDITION, CAPITAL RESOURCES AND LIQUIDITY

Cash, cash equivalents, short-term investments and cash generated from our operations are our primary source of liquidity. Short-term investments consist primarily of U.S. government and agency securities. 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.

Cash, cash equivalents and short-term investments decreased to \$658.5 million as of March 31, 2013 from \$676.0 million as of December 31, 2012. The decrease was mainly due to cash outflows for investing and financing activities, offset in part by cash inflows generated from

operating activities as described below.

Working Capital

Working capital decreased by \$18.6 million to \$691.3 million as of March 31, 2013 from \$709.9 million as of December 31, 2012. The decrease was attributable to the following:

Accounts receivable decreased by \$40.9 million primarily as a result of decreased revenues in the first quarter of 2013 as compared to the fourth quarter of 2012;

Inventories decreased by \$25.3 million, which primarily reflects our continued proactive management of inventory levels;

Cash, cash equivalents and short-term investments decreased by \$17.5 million primarily due to \$60.8 million used to repurchase our common stock, \$30.0 million used for purchases of investments, net of proceeds from maturities and sales and \$25.0 million used for purchases of property and equipment, net of proceeds from sales, offset in part by net cash provided by operating activities of \$62.8 million and proceeds from issuances of common stock of \$8.2 million; and

Table of Contents

Prepaid expenses and other current assets decreased by \$10.3 million primarily as a result of decreases in prepaid software maintenance. These decreases in working capital were offset in part by the following:

Accounts payable decreased by \$39.4 million primarily due to a decrease in inventory purchases and the timing of invoice receipts and payments;

Accrued salaries, wages and benefits decreased by \$24.8 million primarily as a result of the timing of payments for salaries, benefits and performance-based compensation; and

Other accrued liabilities decreased by \$11.2 million primarily due to the utilization of restructuring reserves, and decreases in tax and other accruals.

Working capital decreased by \$243.7 million to \$718.1 million as of April 1, 2012 from \$961.8 million as of December 31, 2011. The decrease was primarily attributable to the following:

Cash, cash equivalents and short-term investments decreased by \$312.4 million primarily due to \$319.2 million used in connection with the acquisition of SandForce in January 2012, net of cash acquired, \$65.0 million used for purchases of property and equipment, net of proceeds from sales, and \$38.2 million used to repurchase our common stock, offset in part by proceeds from issuances of common stock of \$65.3 million and net cash provided by operating activities of \$50.2 million; and

Accounts payable increased by \$47.1 million primarily due to an increase in inventory purchases to support new product introductions and expected increases in product demand in future quarters and, to a lesser extent, due to the normal timing of invoice receipts and payments.

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

Accounts receivable increased by \$55.6 million primarily as a result of increased revenues in the first quarter of 2012 as compared to the fourth quarter of 2011;

Other accrued liabilities decreased by \$32.7 million primarily due to the utilization of restructuring reserves, payments of taxes and decreases in other accruals related to our operations;

Inventories increased by \$20.8 million as a result of increased inventory purchases to support new product introductions and expected increases in product demand in future quarters; and

Accrued salaries, wages and benefits decreased by \$5.0 million primarily as a result of the timing of payments for salaries, benefits and performance-based compensation.

Cash Provided by Operating Activities

During the three months ended March 31, 2013, we generated \$62.8 million of cash from operating activities as a result of the following:

Edgar Filing: LSI CORP - Form 10-Q

Net income adjusted for non-cash items and other non-operating adjustments, which are quantified in our statements of cash flows included in Item 1;

Offset in part by a net decrease of \$32.6 million in assets and liabilities, including changes in working capital components, from December 31, 2012 to March 31, 2013, as discussed above.

During the three months ended April 1, 2012, we generated \$50.2 million of cash from operating activities as a result of the following:

Net income adjusted for non-cash items and other non-operating adjustments, which are quantified in our statements of cash flows included in Item 1;

Offset in part by a net decrease of \$55.8 million in assets and liabilities, including changes in working capital components, from December 31, 2011 to April 1, 2012, as discussed above.

Cash Used in Investing Activities

Cash used in investing activities for the three months ended March 31, 2013 was \$55.0 million. Our investing activities during the three months ended March 31, 2013 were the following:

Purchases of available-for-sale debt securities and other investments, net of proceeds from maturities and sales, of \$30.0 million; and

Purchases of property and equipment, net of proceeds from sales, totaling \$25.0 million.

Table of Contents

Cash used in investing activities for the three months ended April 1, 2012 was \$395.9 million. Our investing activities during the three months ended April 1, 2012 were the following:

\$319.2 million of cash used in connection with the acquisition of SandForce;

Purchases of property and equipment, net of proceeds from sales, totaling \$65.0 million, including \$45.5 million for our new headquarters; and

Purchases of available-for-sale debt securities, net of proceeds from maturities and sales, of \$11.7 million.

We expect capital expenditures to be approximately \$85 million in 2013. We use semiconductor foundries and outside assembly and test companies to manufacture products, which enables us to have access to advanced manufacturing capacity without having to increase our capital spending requirements.

Cash Used in/Provided by Financing Activities

Cash used in financing activities for the three months ended March 31, 2013 was \$52.6 million. This amount included \$60.8 million used to repurchase our common stock, offset in part by \$8.2 million of cash received from issuances of common stock under our employee stock plans.

Cash provided by financing activities for the three months ended April 1, 2012 was \$27.1 million. This amount included \$65.3 million of cash received from issuances of common stock under our employee stock plans, offset in part by \$38.2 million used to repurchase our common stock.

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

CONTRACTUAL OBLIGATIONS

The following table summarizes our contractual obligations as of March 31, 2013:

	Payments Due by Period					Total
	Less Than 1 Year	1-3 Years	4-5 Years	After 5 Years	Other	
	(In millions)					
Operating lease obligations	\$ 38.8	\$ 33.1	\$ 10.1	\$ 4.8	\$	\$ 86.8
Purchase commitments	322.4	22.6	5.4			350.4
Pension contributions	36.4	*	*	*	*	36.4
Uncertain tax positions					99.1**	99.1
Total	\$ 397.6	\$ 55.7	\$ 15.5	\$ 4.8	\$ 99.1	\$ 572.7

* We have pension plans covering certain U.S. employees and 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, legislation changes and the amount of voluntary contributions to the plans. The amount shown in the table represents our planned contributions to our pension plans during the remainder of 2013. Because any contributions for 2014 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 2014 and beyond in the above table.

**

Edgar Filing: LSI CORP - Form 10-Q

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.

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 March 31, 2013, we had \$195.3 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 \$23.8 million.

Table of Contents

Standby Letters of Credit

We had outstanding obligations relating to standby letters of credit of \$4.2 million and \$4.1 million, respectively, as of March 31, 2013 and December 31, 2012. 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 amounts. 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 three months ended March 31, 2013 as compared to the discussion in Part II, Item 7 and in Note 2 to our financial statements in Part II, Item 8 of our Annual Report on Form 10-K for the year ended December 31, 2012.

RECENT ACCOUNTING PRONOUNCEMENTS

The information contained in Note 1 to our financial statements in Item 1 under the heading *Recent Accounting Pronouncement* 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 three months ended March 31, 2013 as compared to the discussion in Part II, Item 7A of our Annual Report on Form 10-K for the year ended December 31, 2012.

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 furnishes 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 first quarter of 2013, there were no changes in our internal control over financial reporting that materially affected or are reasonably likely to materially affect our internal control over financial reporting.

PART II OTHER INFORMATION

Item 1. *Legal Proceedings*

This information is included under the caption *Legal Matters* in Note 12 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, 2012, 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 revenues from, any of these customers would harm our results of operations.

Edgar Filing: LSI CORP - Form 10-Q

A significant portion of our revenues is derived from the sale of products for use in hard disk drives and dynamics in that industry as well as competing technologies could have an adverse impact on our revenues.

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.

Table of Contents

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

We are seeking to expand our business by selling to new types of customers and may be unsuccessful in doing so, which could have a negative impact on 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.

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.

Volatility in the price of commodities used in the production of our products or lack of availability of these materials could negatively impact our results of operations.

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 have engaged, and will likely continue to engage, in acquisitions and strategic alliances, which may disrupt our business or 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.

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

Edgar Filing: LSI CORP - Form 10-Q

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.

Laws and regulations to which we are subject, as well as customer requirements in the area of environmental protection and social responsibility, could impose substantial costs on us and may adversely affect our business.

We rely on our information technology systems to run our business and any failure of these systems or any malicious intrusion into those systems could result in harm to our business, results of operations and financial condition.

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 March 31, 2013.

Issuer Purchases of Equity Securities

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs
January 1 - January 31, 2013	202,824	\$ 7.40	202,824	\$ 477,128,738
February 1 - February 28, 2013	4,385,582	\$ 7.16	4,385,582	\$ 445,736,108
March 1 - March 31, 2013	4,046,400	\$ 6.89	4,046,400	\$ 417,864,085
Total	8,634,806	\$ 7.04	8,634,806	

On August 1, 2012, our board of directors authorized the repurchase of up to \$500.0 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.

Date: May 8, 2013

LSI CORPORATION
(Registrant)

By /s/ Bryon Look

Bryon Look
Executive Vice President, Chief Financial Officer
and Chief Administrative Officer

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