CIRRUS LOGIC INC
Form 10-K
May 25, 2006

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K
þ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For The Fiscal Year Ended March 25, 2006
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the Transition Period from _____ to _____

Commission File Number 0-17795
CIRRUS LOGIC, INC.

DELAWARE	**77-0024818**
(State of incorporation)	**(I.R.S. ID)**

2901 Via Fortuna, Austin, TX 78746
(512) 851-4000
Securities registered pursuant to Section 12(b) of the Act:
None
Securities registered pursuant to Section 12(g) of the Act:
Common Stock, $0.001 Par Value

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Act. YES þ NO o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. YES o NO þ

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 þ NO o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

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

Large accelerated filer o Accelerated filer þ Non-accelerated filer o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). YES o NO þ

The aggregate market value of the registrant s voting and non-voting stock held by non-affiliates was approximately $410 million based upon the closing price reported on the NASDAQ National Market as of September 24, 2005.

As of May 19, 2006, the number of outstanding shares of the registrant s Common Stock, $0.001 par value, was 87,454,555.

DOCUMENTS INCORPORATED BY REFERENCE

Certain information contained in the registrant s proxy statement for its annual meeting of stockholders to be held July 28, 2006 is incorporated by reference in Part III of this Annual Report on Form 10-K.

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For The Fiscal Year Ended March 25, 2006
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PART I

ITEM 1. *Business*

Cirrus Logic, Inc. (Cirrus Logic, Cirrus, We, Us, Our, or the Company) develops high-precision, analog a mixed-signal integrated circuits (ICs) for a broad range of consumer and industrial markets. Building on our diverse analog mixed-signal patent portfolio, Cirrus Logic delivers highly optimized products for consumer and commercial audio, automotive entertainment and industrial applications. We develop and market ICs and embedded software used by original equipment manufacturers. We also provide complete system reference designs based on our technology that enable our customers to bring products to market in a timely and cost-effective manner.

We were founded in 1984 and were reincorporated in the State of Delaware in February 1999. Our headquarters are in Austin, Texas with design centers in Boulder, Colorado and Beijing, China and sales locations throughout the United States. We also serve customers from international offices in Europe and Asia, including the People s Republic of China, Hong Kong, Korea, Japan, Singapore and Taiwan. Our common stock, which has been publicly traded since 1989, is listed on the NASDAQ National Market under the symbol CRUS.

We maintain a Web site with the address www.cirrus.com. We are not including the information contained on our Web site as a part of, or incorporating it by reference into, this Annual Report on Form 10-K. We make available free of charge through our Web site our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K and amendments to these reports, as soon as reasonably practicable after we electronically file such material with, or furnish such material to, the Securities and Exchange Commission (SEC). To receive a free copy of this Form 10-K, please forward your written request to Cirrus Logic, Inc., Attn: Investor Relations, 2901 Via Fortuna, Austin, Texas 78746, or via email at InvestorRelations@cirrus.com.

Background of the Semiconductor Industry

In general, the semiconductor industry produces three types of products: analog, digital and mixed-signal. Analog semiconductors process a continuous range of values that can regulate functions such as temperature, speed, sound, video images and electrical current. Digital semiconductors process discrete values, for example, two values, such as 0s and 1s, used by computers. Mixed-signal semiconductors combine analog and digital functions in a single product.

In the consumer electronics industry, audio soundtracks and video images were transmitted, edited and stored almost exclusively using analog formats. Given advances in technology, audio and video now can be stored in digital format. This format allows for the manipulation of audio and video signals through digital signal processors (DSPs). With digital signal processors, digital audio and digital video signals can be compressed, improving storage and efficiencies in transmissions and they can be transmitted and reproduced without degradation in the sound or images. The digital format also allows for greater security from unauthorized copying, better editing capabilities and random access to data.

In addition, increasing advances in semiconductor technology are resulting in the convergence of consumer electronics products, which means cost savings and added convenience and functionality for consumers. For example, compact disc (CD) players were introduced to play audio content in the CD format only. Later, digital video disc (DVD) players were introduced, combining audio with video. These consumer electronics products now support additional audio and video formats, such as MP3 audio and MPEG-4 video. As these digital home entertainment systems have converged and have become increasingly complex, a need has arisen among makers of these systems for sophisticated IC chips that have many features and are cost-effective.

Manufacturers of consumer electronics products also face expedited time-to-market demands. In addition, because analog or mixed-signal IC design is a specialized field of IC design, manufacturers increasingly are asking third parties to provide advanced, analog or mixed-signal ICs. The design of the analog component of a mixed-signal IC is complex and difficult, and requires engineers to optimize speed, power and resolution within standard manufacturing processes.

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Markets and Products

We are focused on becoming a leader in high-precision analog and mixed-signal ICs for a broad range of consumer and industrial markets. During fiscal year 2006, Cirrus Logic sold its digital video product line assets to Magnum Semiconductor, a privately held company formed by an investment group led by Investcorp and August Capital. By selling these assets, Cirrus Logic re-aligned its business focus around its core analog, mixed-signal and embedded integrated circuit product lines for audio and industrial markets. Our primary product lines include:

Mixed-Signal Audio Products: High-precision analog and mixed-signal products for consumer, professional, and automotive entertainment markets.

Industrial Products: High-precision analog and mixed-signal components for industrial and medical measurement applications.

Embedded Products: High-precision processors and software for consumer audio, professional audio and industrial applications.

We offer more than 600 products to over 2,500 customers worldwide through both direct and indirect sales channels. Our major customers are among the world s leading electronics manufacturers. We target both large existing and emerging growth consumer electronic markets that derive value from our expertise in advanced analog and mixed-signal design processing, systems-level integrated circuit engineering and embedded software development. We derive our revenue both domestically and from a variety of locations across the globe, including the People s Republic of China, Hong Kong, Taiwan, Korea, Japan, the European Union, and the United Kingdom.

The following table summarizes sales to customers that represent more than 10 percent of our consolidated net sales:

	March 25, 2006	March 26, 2005	March 27, 2004
Avnet, Inc. (formerly Memec Holdings Group)	25%	27%	20%

MIXED-SIGNAL AUDIO PRODUCTS

We are a recognized leader in analog and mixed-signal audio converter technologies that enable today s new consumer, professional and automotive entertainment products. Our products include analog-to-digital converters (ADCs), digital-to-analog converters (DACs), chips that integrate ADCs and DACs into a single IC, otherwise known as coder-decoders (CODECs), digital interface ICs, and volume and digital amplifiers controllers. Our broad portfolio of approximately 275 active proprietary products includes the following products, which have been added in the past fiscal year:

the CS42L51 low-power stereo audio CODEC for portable consumer applications;

the CS52L21 low-power stereo ADC for portable consumer applications;

the CS4361 entry-level six channel audio DAC for consumer and automotive audio applications;

the CS4270 stereo audio CODEC for entry and mid-tier consumer and automotive audio applications;

the CS4364/84 six- and eight-channel DACs for consumer and automotive audio applications;

the CS5364/66/68 multi channel ADC for professional audio applications;

the CS5343/44 stereo ADC for consumer and automotive audio applications; and

the CS3308/18 analog volume control for professional and high-end consumer audio applications.

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Our products are used in a wide array of consumer applications, including audio/video receivers (AVRs), DVD players and recorders, complete home theater systems, set-top boxes, MP3 players, gaming devices, sound cards and digital televisions. Applications for products within professional markets include digital mixing consoles, multi-track digital recorders and effects processors. Applications for products within automotive markets include amplifiers, satellite radio systems and multi-speaker car-audio systems.

Our analog and mixed-signal audio converters support a customer base featuring such leading companies as Apple, BBK, Bose, Creative, Harman Kardon, iRiver, Korg, LG Electronics, Marantz, Panasonic, Philips, Sony, Samsung and Scientific-Atlanta. Key competitors to Cirrus Logic in this product line include Wolfson Microelectronics, AKM, Texas Instruments/ Burr Brown, Analog Devices and Maxim.

INDUSTRIAL PRODUCTS

We provide high-precision analog and mixed-signal ICs for industrial measurement applications. We have more than 150 active proprietary products which include ADCs, DACs, successive approximation register (SAR) converters and amplifier ICs. Our products are used in a wide array of high-precision, industrial measurement applications including industrial process control, analytical and medical instruments, consumer utility, digital power meters and seismic systems. New additions to our proprietary product portfolio in the past fiscal year include:

- the CS5373A seismic IC, which integrates a high-precision Delta Sigma modulator and a seismic test DAC into a single IC;
- the CS5461A and CS5463 power meter ICs for digital power measurement applications for emerging global markets; and
- the CS5464 and CS5467 power meter ICs targeting market-specific requirements in India and Japan, respectively.

We have a wide-ranging industrial customer base including Actaris, Elymer, Hydroscience, Input/ Output, Itron Electric Metering, Mettler-Toledo, National Instruments, and Schlumberger. Our key competitors in industrial applications include Analog Devices, Texas Instruments/ Burr Brown, Maxim and Linear Technologies.

EMBEDDED PRODUCTS

We provide a wide variety of embedded processor technologies for consumer and industrial markets. These embedded processors include audio DSPs primarily targeted at consumer audio applications, ARM7- and ARM9-based embedded processors focused on industrial applications, CobraNet™-enabled controller and audio system processor ICs for commercial and professional audio markets, and Ethernet MACs and T1/ E1 line interface units. We offer advanced ICs combined with innovation in software solutions, providing our customers features that differentiate their products against their competitors. We offer a family of 24- and 32-bit audio DSPs targeted at a wide range of applications such as audio/video receivers, automotive entertainment, set-top boxes, digital televisions and DVD receivers. In addition, we provide our customers standard audio algorithms, as well as proprietary audio enhancement algorithms, such as Intelligent Room Calibration software.

In the general-purpose processor segment, our ARM family of processors offers a highly integrated 32-bit System-On-A-Chip solution with a wide array of price-performance-integration points for industrial applications. These embedded processors support popular third-party software such as Linux and WinCE Net™.

In networked digital audio applications, our proprietary CobraNet controller ICs enable delivery of uncompressed digital audio over Ethernet networks. In doing so, the distributed audio co-exists with standard Ethernet network data traffic. In December 2005, we announced an agreement with Gibson® USA to develop next-generation digital audio networking products beginning in calendar year 2006. Building upon CobraNet technology and Gibson s MaGIC® technology, the new products will provide high-channel count media transport solutions for professional markets, while enabling secure multiroom distribution of media content in consumer markets.

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New embedded products introduced in the last fiscal year include:

DSP Conductor, a unique software tool designed to streamline audio features programming for users of the CS496XXX family of audio systems processors featuring CobraNet technology; and

A reference design in collaboration with Genesis Microchip for high-definition audio/video receivers, featuring Cirrus Logic s CS495XX family of audio DSPs.

Our embedded product customers include Bose, eTronics, Harman Kardon, Hitachi, Kenwood, Logitech, Marantz, Onkyo, Panasonic, Pioneer, RCA/ Thomson S.A., Sharp and Sony. Our competitors in embedded product solutions include Analog Devices, Texas Instruments/ Burr Brown, Freescale Semiconductor, Samsung, Realtek, ATMEL and IDT.

With the sale of the digital video product line assets, we have reclassified a product previously reported as part of the digital video products as part of the embedded product line. We retained the rights to sell this specific product as part of the digital video product line divestiture.

Manufacturing

We contract with third parties for all of our wafer fabrication, assembly, and test services. Our fabless manufacturing strategy allows us to concentrate on our design strengths, minimize fixed costs and capital expenditures, access advanced manufacturing facilities and provide flexibility to source multiple leading-edge technologies through strategic relationships. After wafer fabrication by the foundry, third-party assembly vendors package the wafer die. The finished products are then sent for testing before shipment to our customers. Our supply chain management organization is responsible for the management of all aspects of the manufacturing and testing of our products, including process and package development, test program development, and production testing of products in accordance with our ISO-certified quality management system. We use multiple foundries, assembly and test houses.

Patents, Licenses and Trademarks

We rely on trade secret, patent, copyright and trademark laws to protect our intellectual property products and technology. We intend to continue this practice in the future to protect our products and technologies. As of March 25, 2006, we held 933 U.S. patents, 148 U.S. patent applications pending and various corresponding international patents and applications. Our U.S. patents expire in years 2006 through 2025.

We have obtained U.S. federal registrations for the CIRRUS LOGIC®, CIRRUS® and CRYSTAL® trademarks as well as our Cirrus Logic logo trademark. These U.S. registrations may be renewed as long as the marks continue to be used in interstate commerce. We have also filed or obtained foreign registration for these marks in other countries or jurisdictions where we conduct, or anticipate conducting, international business.

To complement our own research and development efforts, we have also licensed and expect to continue to license, a variety of intellectual property and technologies important to our business from third parties.

Research and Development

We concentrate our research and development efforts on the design and development of new products for each of our principal markets. We also fund certain advanced-process technology development, as well as other emerging product opportunities. Expenditures for research and development in fiscal years 2006, 2005, and 2004, were $45.1 million, $80.5 million, and $90.6 million, respectively. These amounts include amortization of acquired intangibles of $1.4 million, $13.7 million, and $14.4 million, in fiscal years 2006, 2005, and 2004, respectively. Our future success is highly dependent upon our ability to develop complex new products, to transfer new products to volume production in a timely fashion, to introduce them to the marketplace ahead of the competition and to have them selected for design into products of systems manufacturers. Our future success may also depend on assisting our

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customers with integration of our components into their new products, including providing support from the concept stage through design, launch and production ramp.

Competition

Markets for our products are highly competitive and we expect that competition will continue to increase. We compete with other semiconductor suppliers that offer standard semiconductors, application-specific standard product and fully customized ICs, including embedded software, chip and board-level products. A few customers also develop ICs that compete with our products. Our strategy involves providing lower-cost versions of existing products and new, more advanced products for customers new designs.

While no single company competes with us in all of our product lines, we face significant competition in each of our major product lines, as detailed above in our product line discussions. We expect to face additional competition from new entrants in our markets, which may include both large domestic and international IC manufacturers and smaller, emerging companies.

The principal competitive factors in our markets include time to market; quality of hardware/ software design and end-market systems expertise; price; product benefits that are characterized by performance, features, quality and compatibility with standards; access to advanced process and packaging technologies at competitive prices; and sales and technical support, including assisting our customers with integration of our components into their new products and providing support from the concept stage through design, launch and production ramp.

Competition typically occurs at the design stage, where the customer evaluates alternative design approaches that require ICs. Many of our products have not been available from second sources, thus, once our ICs have been designed into a customer s system, we generally do not face direct competition in selling our products.

Product life cycles vary greatly by product category. For example, many consumer electronic devices have shorter design-in cycles; therefore, our competitors have increasingly frequent opportunities to achieve design wins in next-generation systems. Conversely, this also provides us more frequent opportunities to displace competitors in products we have previously not been designed in. The industrial and automotive markets typically have longer life cycles, which provide longer revenue streams. In the event that competitors succeed in supplanting our products, our market share may not be sustainable and net sales, gross margins and earnings could be adversely affected.

Sales, Marketing and Technical Support

Although we sell our products worldwide, we sell our products principally in Asia. Export sales, which include sales to customers with manufacturing plants outside the United States, were 66 percent, 67 percent, and 72 percent in fiscal years 2006, 2005, and 2004, respectively. We maintain a worldwide sales force, which is intended to provide geographically specific selling support to our customers and specialized selling of product lines with unique customer bases.

Our domestic sales force includes a network of regional direct sales offices located in California, Colorado, Massachusetts, Nevada, Oregon and Texas. International sales offices and staff are located in Hong Kong, Japan, Shanghai and Shenzen in the People s Republic of China, Singapore, South Korea, Taiwan and the United Kingdom. We supplement our direct sales force with external sales representatives and distributors. Our technical support staff is located in Colorado, Texas, and Beijing in the People s Republic of China.

Backlog

Sales are made primarily pursuant to standard short-term purchase orders for delivery of standard products. The quantity actually ordered by the customer, as well as the shipment schedules, are frequently revised, without significant penalty, to reflect changes in the customer s needs. We utilize backlog as an indicator to assist us in production planning. However, backlog is influenced by several factors including market demand, pricing and customer order patterns in reaction to product lead times. Quantities actually purchased by customers, as well as

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prices, are subject to variations between booking and delivery to reflect changes in customer needs or industry conditions. As a result, we believe that our backlog at any given time is not a reliable indicator of future revenues.

Employees

As of March 25, 2006, we had 424 full-time employees, of whom 54 percent were engaged in research and product development activities, 40 percent in sales, marketing, general and administrative activities and 6 percent in manufacturing-related activities. Our future success depends, in part, on our ability to continue to attract, retain and motivate highly qualified technical, marketing, engineering and administrative personnel.

Due to the highly competitive nature of the marketplace that we operate in, we may from time-to-time lose key employees to our competitors. We have been able to hire qualified personnel in the past to fill open positions created by these occurrences, although there can be no assurance that we will be able to do this in the future. None of our employees are represented by collective bargaining agreements.

ITEM 1A. ***Risk Factors Affecting Our Business and Prospects***

Our business faces significant risks. The risk factors set forth below may not be the only risks that we face. Additional risks that we are not aware of yet or that currently are not significant may adversely affect our business operations. You should read the following cautionary statements in conjunction with the factors discussed elsewhere in this and other of Cirrus Logic s filings with the SEC. These cautionary statements are intended to highlight certain factors that may affect the financial condition and results of operations of Cirrus Logic and are not meant to be an exhaustive discussion of risks that apply to companies such as ours.

Our results may be affected by the fluctuation in sales in the consumer entertainment market.

Because we sell products in the consumer entertainment market, we are likely to be affected by seasonality in the sales of our products. In particular, a significant portion of consumer electronics products are sold worldwide during the third calendar quarter in preparation for the fourth calendar quarter holiday seasons. As a result, we expect stronger sales of ICs into the consumer entertainment market to occur in our second and third fiscal quarters in anticipation of these seasons.

Further, a decline in consumer confidence and consumer spending relating to economic conditions, terrorist attacks, armed conflicts, oil prices, global health conditions and/or the political stability of countries in which we operate or sell into could have a material adverse effect on our business.

The highly cyclical and volatile nature of our industry may affect our operating results.

We are subject to business cycles and it is difficult to predict the timing, length or volatility of these cycles. During downturns, customers usually reduce purchases, delay delivery of products, shorten lead times on orders and/or cancel orders. During upturns, our third party suppliers and contract manufacturers may have capacity or supply constraints that result in higher costs, longer lead times, and/or an inability to meet customer demand. These business cycles may create pressure on our sales, gross margins and/or operating results.

We cannot assure that any future downturn or upturn will not have a material adverse effect on our business and results of operations. We cannot assure that we will not experience substantial period-to-period fluctuations in revenue due to general semiconductor industry conditions or other factors.

Our failure to develop and timely introduce new products that gain market acceptance could harm our operating results.

Our success depends upon our ability to develop new products for new and existing markets, to introduce these products in a timely and cost-effective manner, and to have these products gain market acceptance. New product

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introductions involve significant risks. For example, delays in new product introductions or less-than-anticipated market acceptance of our new products are possible and would have an adverse effect on our revenue and earnings. The development of new products is highly complex and, from time-to-time, we have experienced delays in developing and introducing these new products. Successful product development and introduction depend on a number of factors, including:

proper new product definition,

timely completion of design and testing of new products,

assisting our customers with integration of our components into their new products, including providing support from the concept stage through design, launch and production ramp,

successfully developing and implementing the software necessary to integrate our products into our customers products,

achievement of acceptable manufacturing yields,

availability of wafer, assembly and test capacity,

market acceptance of our products and the products of our customers, and

obtaining and retaining industry certification requirements.

Although we seek to design products that have the potential to become industry standard products, we cannot assure that market leaders will adopt any products introduced by us, or that any products initially accepted by our customers who are market leaders will become industry standard products. Both revenues and margins may be materially affected if new product introductions are delayed, or if our products are not designed into successive generations of our customers products. We cannot assure that we will be able to meet these challenges, or adjust to changing market conditions as quickly and cost-effectively as necessary to compete successfully. Our failure to develop and introduce new products successfully could harm our business and operating results.

Successful product design and development is dependent on our ability to attract, retain and motivate qualified design engineers, of which there is a limited number. Due to the complexity and variety of analog and high-precision analog and mixed-signal circuits, the limited number of qualified integrated circuit designers and the limited effectiveness of computer-aided design systems in the design of analog and mixed-signal ICs, we cannot assure that we will be able to successfully develop and introduce new products on a timely basis.

Our products are complex and could contain defects, which could result in material costs to us.

Product development in the markets we serve is becoming more focused on the integration of multiple functions on individual devices. There is a general trend towards increasingly complex products. The greater integration of functions and complexity of operations of our products increases the risk that our customers or end users could discover latent defects or subtle faults after volumes of product have been shipped. This could result in:

damage to our reputation,

a material recall and replacement costs for product warranty and support,

payments to our customer related to such recall claims as a result of various industry or business practices, or in order to maintain good customer relationships,

an adverse impact to our customer relationships by the occurrence of significant defects,

a delay in recognition or loss of revenues, loss of market share, or failure to achieve market acceptance, and

a diversion of the attention of our engineering personnel from our product development efforts.

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In addition, any defects or other problems with our products could result in financial or other damages to our customers who could seek damages from us for their losses. A product liability claim brought against us, even if unsuccessful, would likely be time consuming and costly to defend. In particular, the sale of systems and components into certain applications for the automotive industry involves a high degree of risk that such claims may be made.

While we believe that we are reasonably insured against these risks and contractually limit our financial exposure, we cannot assure that we will be able to obtain sufficient insurance, in terms of amounts or scope, to provide us with adequate coverage against all potential liability.

We have historically experienced fluctuations in our operating results and expect these fluctuations to continue in future periods.

Our quarterly and annual operating results are affected by a wide variety of factors that could materially and adversely affect our net sales, gross margins and operating results. These factors include:

the volume and timing of orders received,

changes in the mix of our products sold,

market acceptance of our products and the products of our customers,

competitive pricing pressures,

our ability to introduce new products on a timely basis,

the timing and extent of our research and development expenses,

the failure to anticipate changing customer product requirements,

disruption in the supply of wafers, assembly or test services,

certain production and other risks associated with using independent manufacturers, assembly houses and testers, and

product obsolescence, price erosion, competitive developments, and other competitive factors.

We may face increased risks and uncertainties related to our non-marketable securities.

On occasion, we may invest in non-marketable securities of private companies. As of March 25, 2006, the carrying value of our investments in non-marketable securities totaled $7.9 million.

Investments in non-marketable securities are inherently risky, and some of these companies are likely to fail. Their success (or lack thereof) is dependent on these companies product development, market acceptance, operational efficiency and other key business success factors. In addition, depending on these companies future prospects, they may not be able to raise additional funds when needed or they may receive lower valuations, with less favorable investment terms than in previous financings, and our investments in them would likely become impaired.

Shifts in industry-wide capacity and our practice of purchasing our products based on sales forecasts may result in significant fluctuations in our quarterly and annual operating results.

As a fabless semiconductor developer, we rely on independent foundries and assembly and test houses to manufacture our products. Our reliance on these third parties involves certain risks and uncertainties. For example, shifts in industry-wide capacity from shortages to oversupply, or from oversupply to shortages, may result in significant fluctuations in our quarterly and annual operating results. We may order wafers and build inventory in advance of receiving purchase orders. Because our industry is highly cyclical and is subject to significant downturns resulting from

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excess capacity, overproduction, reduced demand, order cancellations, or technological obsolescence, there is a risk that we will forecast inaccurately and produce excess inventories of particular products.

In addition, we generally order our products through non-cancelable purchase orders from third-party foundries based on our sales forecasts and our customers can generally cancel or reschedule orders they place with us without significant penalties. If we do not receive orders as anticipated by our forecasts, or our customers cancel orders that are placed, we may experience increased inventory levels.

Due to the product manufacturing cycle characteristic of IC manufacturing and the inherent imprecision by our customers to accurately forecast their demand, product inventories may not always correspond to product demand, leading to shortages or surpluses of certain products. As a result of such inventory imbalances, future inventory write-downs and charges to gross margin may occur due to lower of cost or market accounting, excess inventory, and inventory obsolescence.

Strong competition in the semiconductor market may harm our business.

The IC industry is intensely competitive and is frequently characterized by rapid technological change, price erosion and design, technological obsolescence, and a push towards IC component integration. Because of shortened product life cycles and even shorter design-in cycles in a number of the markets that we serve, our competitors have increasingly frequent opportunities to achieve design wins in next-generation systems. In the event that competitors succeed in supplanting our products, our market share may not be sustainable and our net sales, gross margins and operating results would be adversely affected. Additionally, further component integration could eliminate the need for our products.

We compete in a number of fragmented markets. Our principal competitors in these markets include AKM Semiconductors, Analog Devices, Freescale Semiconductor, LSI Logic, Maxim, Micronas, Samsung Semiconductor, Texas Instruments, and Wolfson Microelectronics, many of whom have substantially greater financial, engineering, manufacturing, marketing, technical, distribution and other resources, broader product lines, greater intellectual property rights and longer relationships with customers. We also expect intensified competition from emerging companies and from customers who develop their own IC products. In addition, some of our current and future competitors maintain their own fabrication facilities, which could benefit them in connection with cost, capacity and technical issues.

Increased competition could adversely affect our business. We cannot assure that we will be able to compete successfully in the future or that competitive pressures will not adversely affect our financial condition and results of operations. Competitive pressures could reduce market acceptance of our products and result in price reductions and increases in expenses that could adversely affect our business and our financial condition.

We may be unable to protect our intellectual property rights.

Our success depends on our ability to obtain patents and licenses and to preserve our other intellectual property rights covering our products. We seek patent protection for those inventions and technologies for which we believe such protection is suitable and is likely to provide a competitive advantage to us. We also rely substantially on trade secrets, proprietary technology, non-disclosure and other contractual agreements, and technical measures to protect our technology and manufacturing knowledge. We work actively to foster continuing technological innovation to maintain and protect our competitive position. We cannot assure that steps taken by us to protect our intellectual property will be adequate, that our competitors will not independently develop or patent substantially equivalent or superior technologies or be able to design around our patents, or that our intellectual property will not be misappropriated. In addition, the laws of some non-U.S. countries may not protect our intellectual property as well as the laws of the United States.

Any of these events could materially adversely affect our business, operating results and financial condition. Policing infringement of our technology is difficult, and litigation may be necessary in the future to enforce our intellectual property rights. Any such litigation could be expensive, take significant time and divert management s attention from other business concerns.

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Potential intellectual property claims and litigation could subject us to significant liability for damages and could invalidate our proprietary rights.

The IC industry is characterized by frequent litigation regarding patent and other intellectual property rights. We may find it necessary to initiate a lawsuit to assert our patent or other intellectual property rights. These legal proceedings could be expensive, take significant time and divert management s attention from other business concerns. We cannot assure that we will ultimately be successful in any lawsuit, nor can we assure that any patent owned by us will not be invalidated, circumvented, or challenged. We cannot assure that rights granted under the patent will provide competitive advantages to us, or that any of our pending or future patent applications will be issued with the scope of the claims sought by us, if at all.

As is typical in the IC industry, we and our customers have from time to time received and may in the future receive, communications from third parties asserting patents, mask work rights, or copyrights. In the event third parties were to make a valid intellectual property claim and a license was not available on commercially reasonable terms, our operating results could be harmed. Litigation, which could result in substantial cost to us and diversion of our management, technical and financial resources, may also be necessary to defend us against claimed infringement of the rights of others. An unfavorable outcome in any such suit could have an adverse effect on our future operations and/or liquidity.

Our products may be subject to average selling prices that decline over short time periods. If we are unable to increase our volumes, introduce new or enhanced products with higher selling prices or reduce our costs, our business and operating results could be harmed.

Historically in the semiconductor industry, average selling prices of products have decreased over time. If the average selling price of any of our products declines and we are unable to increase our unit volumes, introduce new or enhanced products with higher margins and/or reduce manufacturing costs to offset anticipated decreases in the prices of our existing products, our operating results may be adversely affected. In addition, because of procurement lead times, we are limited in our ability to reduce total costs quickly in response to any revenue shortfalls. Because of these factors, we may experience material adverse fluctuations in our future operating results on a quarterly or annual basis.

We have significant international sales, and risks associated with these sales could harm our operating results.

Export sales, principally to Asia, include sales to U.S-based customers with manufacturing plants overseas and accounted for 66 percent, 67 percent, and 72 percent of our net sales in fiscal years 2006, 2005, and 2004, respectively. We expect export sales to continue to represent a significant portion of product sales. This reliance on international sales subjects us to the risks of conducting business internationally, including political and economic stability and global health conditions, especially in Asia. For example, the financial instability in a given region, such as Asia, may have an adverse impact on the financial position of end users in the region, which could affect future orders and harm our results of operations. Our international sales operations involve a number of other risks, including:

unexpected changes in government regulatory requirements,

changes to countries banking and credit requirements,

changes in diplomatic and trade relationships,

delays resulting from difficulty in obtaining export licenses for technology,

tariffs and other barriers and restrictions,

competition with non-U.S. companies or other domestic companies entering the non-U.S. markets in which we operate,

longer sales and payment cycles,

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problems in collecting accounts receivable,

political instability, and

the burdens of complying with a variety of non-U.S. laws.

In addition, our competitive position may be affected by the exchange rate of the U.S. dollar against other currencies. Consequently, increases in the value of the dollar would increase the price in local currencies of our products in non-U.S. markets and make our products relatively more expensive. Alternatively, decreases in the value of the dollar will increase the relative cost of our and our vendors operations that are based overseas. We cannot assure that regulatory, political and other factors will not adversely affect our operations in the future or require us to modify our current business practices.

Failure to manage our distribution channel relationships could adversely affect our business.

The future of our business, as well as the future growth of our business, will depend in part on our ability to manage our relationships with current and future distributors and external sales representatives and to develop additional channels for the distribution and sale of our products. The inability to successfully manage these relationships could adversely affect our business.

Our international operations subject our business to additional political and economic risks that could have an adverse impact on our business.

In addition to export sales constituting a majority of our net sales, we maintain significant international operations, including design, sales and technical support personnel. We are also using contract manufacturers in Asia for foundry, assembly and test operations. International expansion has required and will continue to require significant management attention and resources. There are risks inherent in expanding our presence into non-U.S. regions, including, but not limited to:

difficulties in staffing and managing non-U.S. operations,

failure of non-U.S. laws to adequately protect our U.S. intellectual property, patent, trademarks, copyrights, know-how and other proprietary rights,

global health conditions and potential natural disasters,

political and economic instability in international regions,

international currency controls and exchange rate fluctuations,

additional vulnerability from terrorist groups targeting American interests abroad, and

legal uncertainty regarding liability and compliance with non-U.S. laws and regulatory requirements.

If we fail to attract, hire and retain qualified personnel, we may not be able to develop, market, or sell our products or successfully manage our business.

Competition for personnel in our industry is intense. The number of technology companies in the geographic areas in which we operate is greater than it has been historically and we expect competition for qualified personnel to intensify. There are only a limited number of people in the job market with the requisite skills. Our Human Resources organization focuses significant efforts on attracting and retaining individuals in key technology positions. For example, start-up companies generally offer larger equity grants to attract individuals from more established companies. The loss of the services of key personnel or our inability to hire new personnel with the requisite skills could restrict our ability to develop new products or enhance existing products in a timely manner, sell products to our customers, or manage our business effectively.

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We will be required to expense share-based payments to our employees and we may have a significant material adverse charge to our financial statements.

On December 16, 2004, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standard No. 123R (SFAS No. 123(R)), *Share-Based Payment,* which is a revision of SFAS No. 123 and supersedes Accounting Principles Bulletin Opinion No. 25 (APB No. 25). SFAS No. 123(R) requires all share-based payments to employees, including grants of employee stock options, to be valued at fair value on the date of grant, and to be expensed over the applicable vesting period. Pro forma disclosure of the income statement effects of share-based payments is no longer an alternative. SFAS No. 123(R), as amended, is effective for all stock-based awards granted in fiscal years beginning after June 15, 2005. In addition, companies must also recognize compensation expense related to any awards that are not fully vested as of the effective date. Compensation expense for the unvested awards will be measured based on the fair value of the awards previously calculated in developing the pro forma disclosures in accordance with the provisions of SFAS No. 123.

We may be faced with increased risk due to the volatility of our stock price and our ability to predict the exercise patterns of our stock. In general, we view our volatility as greater than our competitors. As a result, our adoption of this standard may adversely impact our earnings disproportionately from our competitors. Further, we may have difficulty in predicting our operating profitability due to our stock option expense, which could affect future earnings or guidance.

Our adoption of this accounting standard on March 26, 2006, may result in a material adverse impact on our financial results. We will be required to expense stock options and other share-based payments to employees and directors, which will require us to record a significant charge to earnings. We continue to evaluate our stock-based compensation programs to determine what our alternatives may be to reduce this charge in the future. If we choose not to issue stock options at the levels we have in the past, or our shareholders do not approve the use of certain stock-based compensation programs, we believe we may face difficult challenges in attracting and retaining employees.

Because we depend on subcontractors primarily located in Asia to perform key manufacturing functions for us, we are subject to political and economic risks that could disrupt the assembly, packaging, or testing of our products.

We depend on third-party subcontractors, primarily in Asia, for the assembly, packaging and testing of our products. International operations and sales may be subject to political and economic risks, including changes in current tax laws, political instability, global health conditions, currency controls, exchange rate fluctuations and changes in import/export regulations, tariff and freight rates, as well as the risks of natural disaster. Although we seek to reduce our dependence on subcontractors, this concentration of subcontractors and manufacturing operations in Asia subjects us to the risks of conducting business internationally, including political and economic conditions in Asia. Disruption or termination of the assembly, packaging or testing of our products could occur and such disruptions could harm our business and operating results.

We may acquire other companies or technologies, which may create additional risks associated with our ability to successfully integrate them into our business.

We continue to consider future acquisitions of other companies, or their technologies or products, to improve our market position, broaden our technological capabilities and expand our product offerings. However, we may not be able to acquire, or successfully identify, the companies, products or technologies that would enhance our business.

In addition, if we are able to acquire companies, products or technologies, we could experience difficulties in integrating them. Integrating acquired businesses involves a number of risks, including, but not limited to:

the potential disruption of our ongoing business,

unexpected costs or incurring unknown liabilities,

the diversion of management resources from other business concerns while involved in identifying, completing, and integrating acquisitions,

the inability to retain the employees of the acquired businesses,

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difficulties relating to integrating the operations and personnel of the acquired businesses,

adverse effects on the existing customer relationships of acquired companies,

the potential incompatibility of business cultures,

adverse effects associated with entering into markets and acquiring technologies in areas in which we have little experience, and

acquired intangible assets becoming impaired as a result of technological advancements, or worse-than-expected performance of the acquired company.

If we are unable to successfully address any of these risks, our business could be harmed.

Future transactions may limit our ability to use our net operating loss carryforwards.

As of March 25, 2006, we had U.S. federal tax net operating loss (NOL) carryforwards of approximately $465.8 million. These NOL carryforwards may be used to offset future taxable income and thereby reduce our U.S. federal income taxes otherwise payable. There is a risk we may not be able to generate taxable income in the future in the amount necessary to fully utilize all of these NOLs. Section 382 of the Internal Revenue Code of 1986 (the Code), as amended, imposes an annual limit on the ability of a corporation that undergoes an ownership change to use its NOL carry forwards to reduce its tax liability. Due in part to potential changes in our shareholder base, we may at some point in the future experience an ownership change as defined in Section 382 of the Code. Accordingly, our use of the net operating loss carryforwards and credit carryforwards may be limited by the annual limitations described in Sections 382 and 383 of the Code.

Our stock price may be volatile.

The market price of our common stock fluctuates significantly. This fluctuation is the result of numerous factors, including:

actual or anticipated fluctuations in our operating results,

announcements concerning our business or those of our competitors, customers or suppliers,

changes in financial estimates by securities analysts or our failure to perform as anticipated by the analysts,

announcements regarding technological innovations or new products by us or our competitors,

announcements by us of significant acquisitions, strategic partnerships, joint ventures, or capital commitment,

announcements by us of significant divestitures or sale of certain assets or intellectual property,

litigation arising out of a wide variety of matters, including, among others, employment matters and intellectual property matters,

departure of key personnel,

single significant shareholders selling for reasons unrelated to the business,

general assumptions made by securities analysts,

general conditions in the IC industry, and

general market conditions and interest rates.

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We have provisions in our charter, and are subject to certain provisions of Delaware law, which could prevent, delay or impede a change of control of our company. These provisions could affect the market price of our stock.

Certain provisions of our Certificate of Incorporation and By-Laws, and Delaware law could make it more difficult for a third party to acquire us, even if our stockholders support the acquisition. These provisions include:

the inability of stockholders to call a special meeting of stockholders;

a prohibition on stockholder action by written consent; and

a requirement that stockholders provide advance notice of any stockholder nominations of directors or any proposal of new business to be considered at any meeting of stockholders.

We are also subject to the anti-takeover laws of Delaware that may prevent, delay or impede a third party from acquiring or merging with us, which may adversely affect the market price of our common stock.

ITEM 1B. ***Unresolved Staff Comments***

None.

ITEM 2. ***Properties***

The company does not own any real estate. As of May 1, 2006, our principal leased facilities, located in Austin, Texas, consisted of approximately 214,000 square feet of office space, which have lease terms that extend through 2012, excluding renewal options. This leased space includes our headquarters and engineering facility, which has 197,000 square feet and 17,000 square feet of leased space at our failure analysis facility. We have subleased approximately 70,000 square feet of space at our Austin headquarters and engineering facilities. These subleases extend through 2012.

We also lease facilities in Fremont, California. These facilities consist of approximately 430,000 square feet of leased office and engineering space, which have leases that expire from fiscal year 2007 to fiscal year 2010, excluding renewal options. During fiscal year 2006, we sold all of our digital video product line assets, which were for the most part located in California, to Magnum Semiconductor, Inc. As a result of our facilities consolidation activities, which began in fiscal year 1999 concurrent with our move of headquarters from California to Texas, and the sale of our digital video product line assets, we no longer occupy any leased space in California. We have subleased approximately 263,000 square feet of our leased office space in California. We continue to actively pursue sublease tenants for these remaining facilities.

Below is a detailed schedule that identifies our occupied leased property locations as of May 1, 2006 with various lease terms through fiscal year 2013:

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