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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 29, 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 0-12933

LAM RESEARCH CORPORATION

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

94-2634797
(I.R.S. Employer
Identification No.)

4650 Cushing Parkway
Fremont, California
(Address of principal executive offices)

94538
(Zip Code)

(510) 572-0200
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

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

As of November 1, 2013, the Registrant had 162,391,905 shares of common stock outstanding.

[Table of Contents](#)

LAM RESEARCH CORPORATION

TABLE OF CONTENTS

	<u>Page No.</u>
<u>PART I. Financial Information</u>	
<u>Item 1. Financial Statements (Unaudited):</u>	3
<u>Consolidated Balance Sheets as of September 29, 2013 and June 30, 2013</u>	3
<u>Condensed Consolidated Statements of Operations for the three months ended September 29, 2013 and September 23, 2012</u>	4
<u>Condensed Consolidated Statements of Comprehensive Income for the three months ended September 29, 2013 and September 23, 2012</u>	5
<u>Condensed Consolidated Statements of Cash Flows for the three months ended September 29, 2013 and September 23, 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>	24
<u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u>	32
<u>Item 4. Controls and Procedures</u>	33
<u>PART II. Other Information</u>	
<u>Item 1. Legal Proceedings</u>	34
<u>Item 1A. Risk Factors</u>	34
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	43
<u>Item 3. Defaults Upon Senior Securities</u>	44
<u>Item 4. Mine Safety Disclosures</u>	44
<u>Item 5. Other Information</u>	44
<u>Item 6. Exhibits</u>	44
<u>Signatures</u>	45
<u>Exhibit Index</u>	46
EX-31.1	
EX-31.2	
EX-32.1	
EX-32.2	
EX-101.INS	
EX-101.SCH	
EX-101.CAL	
EX-101.DEF	
EX-101.LAB	
EX-101.PRE	

PART I. FINANCIAL INFORMATION

ITEM 1. Financial Statements

**LAM RESEARCH CORPORATION
CONSOLIDATED BALANCE SHEETS
(in thousands, except per share data)**

	September 29, 2013	June 30, 2013
	(unaudited)	(1)
ASSETS		
Cash and cash equivalents	\$ 1,156,184	\$ 1,162,473
Short-term investments	1,300,031	1,334,745
Accounts receivable, less allowance for doubtful accounts of \$5,583 as of September 29, 2013 and \$5,448 as of June 30, 2013	713,524	602,624
Inventories	614,790	559,317
Deferred income taxes	29,090	27,674
Prepaid expenses and other current assets	110,633	106,996
Total current assets	3,924,252	3,793,829
Property and equipment, net	564,845	603,910
Restricted cash and investments	166,385	166,536
Goodwill	1,452,196	1,452,196
Intangible assets, net	1,032,704	1,074,345
Other assets	149,963	159,499
Total assets	<u>\$ 7,290,345</u>	<u>\$ 7,250,315</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Trade accounts payable	\$ 206,072	\$ 200,254
Accrued expenses and other current liabilities	492,860	464,528
Deferred profit	188,420	225,038
Current portion of long-term debt, convertible notes, and capital leases	515,538	514,655
Total current liabilities	1,402,890	1,404,475
Long-term debt, convertible notes, and capital leases	796,373	789,256
Income taxes payable	248,462	246,479
Other long-term liabilities	129,306	134,313
Total liabilities	2,577,031	2,574,523
Commitments and contingencies		
Senior convertible notes	186,042	186,920
Stockholders' equity:		
Preferred stock, at par value of \$0.001 per share; authorized - 5,000 shares; none outstanding	—	—
Common stock, at par value of \$0.001 per share; authorized - 400,000 shares; issued and outstanding - 162,217 shares as of September 29, 2013 and 162,873 shares as of June 30, 2013	162	163
Additional paid-in capital	5,121,032	5,084,544
Treasury stock, at cost; 90,797 shares as of September 29, 2013 and 89,205 shares as of June 30, 2013	(3,628,761)	(3,539,830)
Accumulated other comprehensive loss	(23,355)	(28,693)
Retained earnings	3,058,194	2,972,688
Total stockholders' equity	4,527,272	4,488,872
Total liabilities and stockholders' equity	<u>\$ 7,290,345</u>	<u>\$ 7,250,315</u>

(1) Derived from audited financial statements

See Notes to Condensed Consolidated Financial Statements

[Table of Contents](#)

LAM RESEARCH CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data)
(unaudited)

	Three Months Ended	
	September 29, 2013	September 23, 2012
Revenue	\$ 1,015,059	\$ 906,888
Cost of goods sold	583,201	573,002
Gross margin	431,858	333,886
Research and development	170,567	163,311
Selling, general and administrative	155,883	153,863
Total operating expenses	326,450	317,174
Operating income	105,408	16,712
Other expense, net	(14,262)	(9,938)
Income before income taxes	91,146	6,774
Income tax expense	5,640	4,006
Net income	<u>\$ 85,506</u>	<u>\$ 2,768</u>
Net income per share:		
Basic	<u>\$ 0.52</u>	<u>\$ 0.02</u>
Diluted	<u>\$ 0.50</u>	<u>\$ 0.02</u>
Number of shares used in per share calculations:		
Basic	<u>162,896</u>	<u>179,928</u>
Diluted	<u>171,363</u>	<u>181,926</u>

See Notes to Condensed Consolidated Financial Statements

[Table of Contents](#)

LAM RESEARCH CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(in thousands)
(unaudited)

	Three Months Ended	
	September 29, 2013	September 23, 2012
Net income	<u>\$ 85,506</u>	<u>\$ 2,768</u>
Other comprehensive income (loss), net of tax:		
Foreign currency translation adjustment	3,559	(4,125)
Cash flow hedges:		
Net unrealized gains (losses) during the period	4,507	(719)
Net losses (gains) reclassified into earnings	<u>(3,802)</u>	<u>1,926</u>
	705	1,207
Available-for-sale investments:		
Net unrealized gains during the period	686	3,005
Net losses (gains) reclassified into earnings	<u>74</u>	<u>(334)</u>
	760	2,671
Defined benefit plan, net change in unrealized component	<u>314</u>	<u>158</u>
Other comprehensive income (loss), net of tax	<u>5,338</u>	<u>(89)</u>
Comprehensive income	<u>\$ 90,844</u>	<u>\$ 2,679</u>

See Notes to Condensed Consolidated Financial Statements

LAM RESEARCH CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(unaudited)

	Three Months Ended	
	September 29,	September 23,
	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 85,506	\$ 2,768
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	74,331	74,816
Deferred income taxes	—	(12,017)
Impairment of long-lived asset	7,004	—
Equity-based compensation expense	23,235	24,414
Amortization of convertible note discount	8,122	7,752
Other, net	4,115	8,406
Changes in operating assets and liabilities	(150,388)	143,123
Net cash provided by operating activities	<u>51,925</u>	<u>249,262</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditures and intangible assets	(23,778)	(43,965)
Purchases of available-for-sale securities	(156,409)	(222,187)
Sales and maturities of available-for-sale securities	198,976	205,549
Transfer of restricted cash and investments	150	146
Net cash provided by (used for) investing activities	<u>18,939</u>	<u>(60,457)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Principal payments on long-term debt and capital lease obligations	(88)	(665)
Treasury stock purchases	(104,285)	(355,079)
Reissuances of treasury stock related to employee stock purchase plan	15,154	9,925
Proceeds from issuance of common stock	12,574	951
Net cash used for financing activities	<u>(76,645)</u>	<u>(344,868)</u>
Effect of exchange rate changes on cash	(508)	2,777
Net decrease in cash and cash equivalents	(6,289)	(153,286)
Cash and cash equivalents at beginning of period	<u>1,162,473</u>	<u>1,564,752</u>
Cash and cash equivalents at end of period	<u>\$ 1,156,184</u>	<u>\$ 1,411,466</u>

See Notes to Condensed Consolidated Financial Statements

LAM RESEARCH CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
September 29, 2013
(Unaudited)

NOTE 1 — BASIS OF PRESENTATION

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) for interim financial information and the instructions to Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation have been included. The accompanying unaudited Condensed Consolidated Financial Statements should be read in conjunction with the audited Consolidated Financial Statements of Lam Research Corporation (“Lam Research” or the “Company”) for the fiscal year ended June 30, 2013, which are included in the Annual Report on Form 10-K as of and for the year ended June 30, 2013 (the “2013 Form 10-K”). The Company’s Forms 10-K, Forms 10-Q and Forms 8-K are available online at the Securities and Exchange Commission website on the Internet. The address of that site is www.sec.gov. The Company also posts its Forms 10-K, Forms 10-Q and Forms 8-K on its corporate website at <http://investor.lamresearch.com>.

The consolidated financial statements include the accounts of Lam Research and its wholly owned subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation. We use the equity method to account for equity investments in instances in which we own common stock or similar interests and have the ability to exercise significant influence, but not control, over the investee. The Company’s reporting period is a 52/53-week fiscal year. The Company’s current fiscal year (the “2014 fiscal year”) will end June 29, 2014 and includes 52 weeks. The quarters ended September 29, 2013 (the “September 2013 quarter”) and September 23, 2012 (the “September 2012 quarter”) both included 13 weeks.

NOTE 2 — RECENT ACCOUNTING PRONOUNCEMENTS

In July 2013, the FASB released Accounting Standards Update 2013-11, “Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists.” The new standard requires that an unrecognized tax benefit should be presented as a reduction of a deferred tax asset for a net operating loss carryforward or other tax credit carryforward when settlement in this manner is available under the tax law. We are required to adopt this standard starting fiscal year 2015 and are currently in the process of determining the impact, if any, on our financial position.

NOTE 3 — EQUITY-BASED COMPENSATION PLANS

The Company has stock plans that provide for grants of equity-based awards to eligible participants, including stock options and restricted stock units (“RSUs”), of Lam Research common stock (“Common Stock”). An option is a right to purchase the Company’s stock at a set price. An RSU award is an agreement to issue shares of the Company’s stock at the time of vesting. The Company’s options and RSU awards typically vest over a period of three years or less, although awards assumed in connection with the acquisition of Novellus Systems, Inc. (“Novellus”), have vesting terms up to four years. The Company also has an employee stock purchase plan that allows employees to purchase its Common Stock at a discount through payroll deductions.

The Company recognized the following equity-based compensation expense and related income tax benefit in the Condensed Consolidated Statements of Operations:

	Three Months Ended	
	September 29, 2013	September 23, 2012
	(in millions)	
Equity-based compensation expense	\$ 23.2	\$ 24.4
Income tax benefit related to equity-based compensation expense	\$ 3.9	\$ 5.7

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

[Table of Contents](#)**Stock Options and RSUs**

The Lam Research Corporation 2007 Stock Incentive Plan and 2011 Stock Incentive Plan (collectively the “Stock Plans”) provide for the grant of non-qualified equity-based awards to eligible employees, consultants and advisors, and non-employee directors of the Company and its subsidiaries. As of September 29, 2013, there were a total of 6,418,827 shares reserved to cover options and RSUs issued and outstanding under the Plans. As of September 29, 2013, there were an additional 13,343,330 shares reserved and available for future equity-based awards under the Plans.

A summary of stock option activity under the Plans as of September 29, 2013 and changes during the three months then ended is presented below:

Options	Shares (in thousands)	Weighted- Average Exercise Price	Weighted-Average Remaining Contractual Term (years)	Aggregate Intrinsic Value as of September 29, 2013 (in thousands)
Outstanding at June 30, 2013	2,571	\$ 26.87	4.48	
Exercised	(534)	\$ 23.56		
Outstanding at September 29, 2013	<u>2,037</u>	\$ 27.73	4.72	\$ 47,674
Exercisable at September 29, 2013	<u>1,339</u>	\$ 24.89	3.69	\$ 35,134

The fair value of the Company’s stock options was estimated using a Black-Scholes option valuation model. The total intrinsic value of options exercised during the three months ended September 29, 2013 and September 23, 2012 was \$14.2 million and \$0.6 million, respectively. As of September 29, 2013, there was \$5.8 million of total unrecognized compensation cost related to unvested stock options granted and outstanding; that cost is expected to be recognized over a weighted-average remaining vesting period of 1.3 years.

A summary of the Company’s RSUs as of September 29, 2013 and changes during the three months then ended is presented below:

Unvested Restricted Stock Units	Shares (in thousands)	Average Grant- Date Fair Value
Unvested at June 30, 2013	4,842	\$ 39.32
Granted	32	\$ 48.09
Vested	(403)	\$ 38.90
Forfeited	(89)	\$ 39.46
Unvested at September 29, 2013	<u>4,382</u>	\$ 39.42

The fair value of the Company’s RSUs was calculated based upon the fair market value of the Common Stock at the date of grant. As of September 29, 2013, there was \$105.7 million of total unrecognized compensation expense related to unvested RSUs granted; that expense is expected to be recognized over a weighted-average remaining period of 1.7 years.

ESPP

The 1999 Employee Stock Purchase Plan, as amended and restated (the “1999 ESPP”), allows employees to designate a portion of their base compensation to be withheld through payroll deductions and used to purchase the Company’s Common Stock at a purchase price per share equal to the lower of 85% of the fair market value of the Company’s Common Stock on the first or last day of the applicable purchase period. Each offering period generally lasts up to 12 months and includes up to three interim purchase dates. As of September 29, 2013, there were a total of 9,073,882 shares available for issuance under the 1999 ESPP.

Purchase rights under the 1999 ESPP were valued using the Black-Scholes option valuation model assuming no expected dividends and the following weighted-average assumptions for the three months ended September 29, 2013:

	Three Months Ended September 29, 2013
Expected term (years)	0.66
Expected stock price volatility	31.43%
Risk-free interest rate	0.11%

[Table of Contents](#)

As of September 29, 2013, there was \$11.9 million of unrecognized compensation expense related to the 1999 ESPP, which is expected to be recognized over a remaining period of approximately 11 months.

NOTE 4 — FINANCIAL INSTRUMENTS

The Company maintains an investment portfolio of various holdings, types, and maturities. The Company's mutual funds, which are related to the Company's obligations under the deferred compensation plan, are classified as trading securities. Investments classified as trading securities are recorded at fair value based upon quoted market prices. Differences between the cost and fair value of trading securities are recognized as other income (expense) in the Condensed Consolidated Statements of Operations. All of the Company's other short-term investments are classified as available-for-sale and consequently are recorded in the Consolidated Balance Sheets at fair value with unrealized gains or losses reported as a separate component of accumulated other comprehensive income (loss), net of tax.

Fair Value

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

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

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

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

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

The following table sets forth the Company's financial assets and liabilities measured at fair value on a recurring basis:

	Fair Value Measurement at September 29, 2013			
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(In thousands)			
Assets				
Short-Term Investments				
Money Market Funds	\$ 926,971	\$ 926,971	\$ —	\$ —
Municipal Notes and Bonds	247,864	—	247,864	—
US Treasury and Agencies	154,401	154,401	—	—
Government-Sponsored Enterprises	54,713	—	54,713	—
Foreign Government Bonds	23,699	—	23,699	—
Corporate Notes and Bonds	845,095	164,885	680,210	—
Mortgage Backed Securities - Residential	25,218	—	25,218	—
Mortgage Backed Securities - Commercial	103,092	—	103,092	—
Equities	5,834	5,834	—	—
Total Short-Term Investments	\$2,386,887	\$ 1,252,091	\$ 1,134,796	\$ —
Mutual Funds	19,235	19,235	—	—
Derivative Assets	4,184	—	4,184	—
Total Assets	\$2,410,306	\$ 1,271,326	\$ 1,138,980	\$ —
Liabilities				
Derivative Liabilities	\$ 542	\$ —	\$ 367	\$ 175

[Table of Contents](#)

The amounts in the table above are reported in the Consolidated Balance Sheet as of September 29, 2013 as follows:

	Total	Level 1	Level 2	Level 3
	(In thousands)			
Reported Within:				
Cash Equivalents	\$ 926,971	\$ 926,971	\$ —	\$ —
Short-Term Investments	1,295,031	160,235	1,134,796	—
Restricted Cash and Investments	164,885	164,885	—	—
Prepaid Expenses and Other Current Assets	4,184	—	4,184	—
Other Assets	19,235	19,235	—	—
Total Assets	\$2,410,306	\$1,271,326	\$1,138,980	\$ —
Accrued Expenses and Other Current Liabilities	\$ 367	\$ —	\$ 367	\$ —
Other Non-current Liabilities	175	—	—	175
Total Liabilities	\$ 542	\$ —	\$ 367	\$ 175

The following table sets forth the Company's financial assets and liabilities measured at fair value on a recurring basis:

	Fair Value Measurement at June 30, 2013			
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(In thousands)			
Assets				
Short-Term Investments				
Money Market Funds	\$ 725,311	\$ 725,311	\$ —	\$ —
Municipal Notes and Bonds	268,746	—	268,746	—
US Treasury and Agencies	155,293	155,293	—	—
Government-Sponsored Enterprises	54,805	—	54,805	—
Foreign Government Bond	24,972	—	24,972	—
Corporate Notes and Bonds	860,492	164,885	695,607	—
Mortgage Backed Securities - Residential	27,365	—	27,365	—
Mortgage Backed Securities - Commercial	107,958	—	107,958	—
Total Short-Term Investments	\$2,224,942	\$ 1,045,489	\$ 1,179,453	\$ —
Equities	7,096	7,096	—	—
Mutual Funds	18,216	18,216	—	—
Derivative Assets	4,929	—	4,929	—
Total Assets	\$2,255,183	\$ 1,070,801	\$ 1,184,382	\$ —
Liabilities				
Derivative Liabilities	\$ 1,815	\$ —	\$ 1,620	\$ 195

The amounts in the table above are reported in the Consolidated Balance Sheet as of June 30, 2013 as follows:

	Total	Level 1	Level 2	Level 3
	(In thousands)			
Reported Within:				
Cash Equivalents	\$ 725,311	\$ 725,311	\$ —	\$ —
Short-Term Investments	1,334,746	155,293	1,179,453	—
Restricted Cash and Investments	164,885	164,885	—	—
Prepaid Expenses and Other Current Assets	4,929	—	4,929	—
Other Assets	25,312	25,312	—	—
Total Assets	\$2,255,183	\$1,070,801	\$1,184,382	\$ —
Accrued Expenses and Other Current Liabilities	\$ 1,620	\$ —	\$ 1,620	\$ —
Other Non-current Liabilities	195	—	—	195
Total Liabilities	\$ 1,815	\$ —	\$ 1,620	\$ 195

Table of Contents

The Company's primary financial instruments include its cash, cash equivalents, short-term investments, restricted cash and investments, long-term investments, accounts receivable, accounts payable, long-term debt and capital leases, and foreign currency related derivatives. The estimated fair value of cash, accounts receivable and accounts payable approximates their carrying value due to the short period of time to their maturities. The estimated fair values of capital lease obligations approximate their carrying value as the substantial majority of these obligations have interest rates that adjust to market rates on a periodic basis. Refer to Note 13 for additional information regarding the fair value of the Company's convertible notes.

Investments

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

	September 29, 2013				June 30, 2013			
	Cost	Unrealized Gain	Unrealized (Loss)	Fair Value	Cost	Unrealized Gain	Unrealized (Loss)	Fair Value
Cash	\$ 230,713	\$ —	\$ —	\$ 230,713	\$ 438,813	\$ —	\$ —	\$ 438,813
Fixed Income Money Market Funds	926,971	—	—	926,971	725,311	—	—	725,311
Municipal Notes and Bonds	247,111	894	(141)	247,864	268,390	805	(449)	268,746
US Treasury and Agencies	154,440	77	(116)	154,401	155,648	18	(373)	155,293
Government-Sponsored Enterprises	54,674	79	(40)	54,713	54,835	65	(95)	54,805
Foreign Government Bonds	23,628	79	(8)	23,699	24,950	47	(25)	24,972
Corporate Notes and Bonds	844,524	1,568	(997)	845,095	861,109	1,328	(1,945)	860,492
Mortgage Backed Securities - Residential	25,522	18	(322)	25,218	27,618	29	(282)	27,365
Mortgage Backed Securities - Commercial	103,407	344	(659)	103,092	108,204	426	(672)	107,958
Publicly Traded Equity Security	5,584	250	—	5,834	—	—	—	—
Private Equity Security	5,000	—	—	5,000	—	—	—	—
Total Cash and Short-Term Investments	\$2,621,574	\$ 3,309	\$ (2,283)	\$2,622,600	\$2,664,878	\$ 2,718	\$ (3,841)	\$2,663,755
Publicly Traded Equity Security	\$ —	\$ —	\$ —	\$ —	\$ 5,610	\$ 1,486	\$ —	\$ 7,096
Private Equity Security	—	—	—	—	5,000	—	—	5,000
Mutual Funds	17,804	1,523	(92)	19,235	16,611	1,619	(14)	18,216
Total Financial Instruments	\$2,639,378	\$ 4,832	\$ (2,375)	\$2,641,835	\$2,692,099	\$ 5,823	\$ (3,855)	\$2,694,067
Reported Within								
Cash and Cash Equivalents	\$1,156,184	\$ —	\$ —	\$1,156,184	\$1,162,473	\$ —	\$ —	\$1,162,473
Short-Term Investments	1,299,005	3,309	(2,283)	1,300,031	1,335,868	2,718	(3,841)	1,334,745
Restricted Cash and Investments	166,385	—	—	166,385	166,536	—	—	166,536
Other assets	17,804	1,523	(92)	19,235	27,222	3,105	(14)	30,313
Total	\$2,639,378	\$ 4,832	\$ (2,375)	\$2,641,835	\$2,692,099	\$ 5,823	\$ (3,855)	\$2,694,067

The Company accounts for its investment portfolio at fair value. Realized gains (losses) for investment sales are specifically identified. Management assesses the fair value of investments in debt securities that are not actively traded through consideration of interest rates and their impact on the present value of the cash flows to be received from the investments. The Company also considers whether changes in the credit ratings of the issuer could impact the assessment of fair value. The Company did not recognize any losses on investments due to other-than-temporary impairments during the three months ended September 29, 2013 or September 23, 2012. Additionally, gross realized gains and gross realized (losses) from sales of investments were approximately \$0.2 million and \$(0.6) million, respectively, in the three months ended September 29, 2013 and \$0.3 million and \$(0.4) million, respectively, in the three months ended September 23, 2012.

[Table of Contents](#)

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

	September 29, 2013					
	Unrealized Losses Less Than 12 Months		Unrealized Losses 12 Months or Greater		Total	
	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss
Short-Term Investments						
Municipal Notes and Bonds	\$ 38,907	\$ (141)	\$ —	\$ —	\$ 38,907	\$ (141)
US Treasury and Agencies	58,400	(116)	—	—	58,400	(116)
Government-Sponsored Enterprises	14,988	(40)	—	—	14,988	(40)
Foreign Government Bonds	8,162	(8)	—	—	8,162	(8)
Corporate Notes and Bonds	302,417	(977)	715	(20)	303,132	(997)
Mortgage Backed Securities - Residential	25,013	(322)	—	—	25,013	(322)
Mortgage Backed Securities - Commercial	62,157	(498)	6,555	(161)	68,712	(659)
Total Short-Term Investments	\$510,044	\$ (2,102)	\$7,270	\$ (181)	\$517,314	\$ (2,283)

The amortized cost and fair value of cash equivalents, short-term investments, and restricted cash and investments with contractual maturities are as follows as of September 29, 2013:

	Cost	Estimated Fair Value
	(in thousands)	
Due in one year or less	\$1,372,583	\$ 1,373,071
Due after one year through five years	851,648	852,550
Due in more than five years	156,046	155,432
No Single Maturity Date	10,584	10,834
	<u>\$2,390,861</u>	<u>\$ 2,391,887</u>

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

Derivative Instruments and Hedging

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

Cash Flow Hedges

The Company's financial position is routinely subjected to market risk associated with foreign currency exchange rate fluctuations on non-US dollar transactions or cash flows, primarily from Japanese yen-denominated revenues and euro-denominated expenses. The Company's policy is to mitigate the foreign exchange risk arising from the fluctuations in the value of these non-U.S. dollar denominated transactions or cash flows through a foreign currency cash flow hedging program, using forward contracts that generally expire within 12 months and no later than 24 months. These foreign currency forward contracts are designated as cash flow hedges and are carried on the Company's balance sheet at fair value with the effective portion of the contracts' gains or losses included in accumulated other comprehensive income (loss) and subsequently recognized in revenue/expense in the same period the hedged items are recognized.

At inception and at each quarter end, hedges are tested prospectively and retrospectively for effectiveness using regression analysis. Changes in the fair value of the forward contracts due to changes in time value are excluded from the assessment of effectiveness and are recognized in revenue or expense in the current period. The change in time value related to these contracts was not material for all reported periods. To qualify for hedge accounting, the hedge relationship must meet criteria relating both to the derivative instrument and the hedged item. These criteria include identification of the hedging instrument, the hedged item, the nature of the risk being hedged and how the hedging instrument's effectiveness in offsetting the exposure to changes in the hedged item's fair value or cash flows will be measured. There were no gains or losses during the three months ended September 29, 2013 or September 23, 2012 associated with ineffectiveness or forecasted transactions that failed to occur.

[Table of Contents](#)

To receive hedge accounting treatment, all hedging relationships are formally documented at the inception of the hedge and the hedges must be tested to demonstrate an expectation of providing highly effective offsetting changes to future cash flows on hedged transactions. When derivative instruments are designated and qualify as effective cash flow hedges, the Company recognizes effective changes in the fair value of the hedging instrument within accumulated other comprehensive income (loss) until the hedged exposure is realized. Consequently, with the exception of excluded time value and hedge ineffectiveness recognized, the Company's results of operations are not subject to fluctuation as a result of changes in the fair value of the derivative instruments. If hedges are not highly effective or if the Company does not believe that the underlying hedged forecasted transactions will occur, the Company may not be able to account for its derivative instruments as cash flow hedges. If this were to occur, future changes in the fair values of the Company's derivative instruments would be recognized in earnings. Additionally, related amounts previously recorded in other comprehensive income would be reclassified to income immediately. At September 29, 2013, the Company had gains of \$3.5 million accumulated in other comprehensive income, which it expects to reclassify from other comprehensive income into earnings over the next 12 months.

Balance Sheet Hedges

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

As of September 29, 2013, the Company had the following outstanding foreign currency forward contracts that were entered into under its cash flow and balance sheet hedge program:

Foreign Currency Forward Contracts	Derivatives Designated as Hedging Instruments:		Derivatives Not Designated as Hedging Instruments:	
	(in thousands)			
	Buy Contracts	Sell Contracts	Buy Contracts	Sell Contracts
Japanese Yen	\$ —	\$ 110,274	\$ —	\$ 93,945
Swiss Francs	—	—	18,692	1,621
Euro	58,281	—	5,081	18,452
Korean Won	—	—	14,771	—
Taiwan Dollar	—	—	121,742	—
	<u>\$ 58,281</u>	<u>\$ 110,274</u>	<u>\$ 160,286</u>	<u>\$ 114,018</u>

The fair value of derivative instruments in the Company's Consolidated Balance Sheets as of September 29, 2013 and June 30, 2013 were as follows:

	September 29, 2013				June 30, 2013			
	Fair Value of Derivative Instruments				Fair Value of Derivative Instruments			
	Asset Derivatives		Liability Derivatives		Asset Derivatives		Liability Derivatives	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
(in thousands)								
Derivatives designated as hedging instruments:								
Foreign exchange forward contracts	Prepaid expense and other assets	\$ 4,169	Accrued liabilities	\$ 130	Prepaid expense and other assets	\$ 4,858	Accrued liabilities	\$ 1,577
Derivatives not designated as hedging instruments:								
Foreign exchange forward contracts	Prepaid expense and other assets	15	Accrued liabilities	237	Prepaid expense and other assets	71	Accrued liabilities	43
Total derivatives		<u>\$ 4,184</u>		<u>\$ 367</u>		<u>\$ 4,929</u>		<u>\$ 1,620</u>

Under the master netting agreements with the respective counterparties to our foreign exchange contracts, subject to applicable requirements, we are allowed to net settle transactions of the same currency with a single net amount payable by one party to the other. However, we have elected to present the derivative assets and derivative liabilities on a gross basis in our balance sheet. As of September 29, 2013, the potential effect of rights of set-off associated with the above foreign exchange contracts would be an offset to both assets and liabilities by \$0.4 million, resulting in a net derivative asset of \$3.8 million. As of June 30, 2013, the potential effect of rights of set-off associated with the above foreign exchange contracts would be an offset to both assets and liabilities by \$1.6 million, resulting in a net derivative asset of \$3.3 million. We are not required to pledge, nor are we entitled to receive, cash collateral related to these derivative transactions.

[Table of Contents](#)

The effect of derivative instruments designated as cash flow hedges on the Company's Consolidated Statements of Operations was as follows:

Location of Gain (Loss) Recognized in or Reclassified into Income	Three Months Ended September 29, 2013			Three Months Ended September 23, 2012			
	Effective Portion		Ineffective Portion and Amount Excluded from Effectiveness Testing	Effective Portion		Ineffective Portion and Amount Excluded from Effectiveness Testing	
	Gain (Loss) Recognized in AOCI	Gain (Loss) Reclassified from AOCI into Income (in thousands)		Gain (Loss) Recognized in AOCI	Gain (Loss) Reclassified from AOCI into Income (in thousands)		
Derivatives Designated as Hedging Instruments							
Foreign Exchange Contracts	Revenue	\$ 4,878	\$ 3,383	\$ 93	\$ (2,726)	\$ 857	\$ —
Foreign Exchange Contracts	Cost of goods sold	149	651	(32)	1,251	(2,024)	—
Foreign Exchange Contracts	Selling, general, and administrative	48	317	(15)	756	(759)	—
Foreign Exchange Contracts	Other income (expense)	—	—	—	—	—	(22)
		<u>\$ 5,075</u>	<u>\$ 4,351</u>	<u>\$ 46</u>	<u>\$ (719)</u>	<u>\$ (1,926)</u>	<u>\$ (22)</u>

The effect of derivative instruments not designated as cash flow hedges on the Company's Condensed Consolidated Statements of Operations was as follows:

Derivatives Not Designated as Hedging Instruments:	Location of Gain (Loss) Recognized in Income	Three Months Ended	
		September 29, 2013 Gain Recognized in Income	September 23, 2012 Loss Recognized in Income
Foreign Exchange Contracts	Other income (expense)	\$ 6,027	\$ (5,382)

(in thousands)

Concentrations of Credit Risk

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

The Company's overall portfolio of available-for-sale securities must maintain an average minimum rating of "AA-" or "Aa3" as rated by Standard and Poor's or Moody's Investor Services, respectively. To ensure diversification and minimize concentration, the Company's policy limits the amount of credit exposure with any one financial institution or commercial issuer.

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

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

[Table of Contents](#)

NOTE 5 — INVENTORIES

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

	September 29, 2013	June 30, 2013
	(in thousands)	
Raw materials	\$ 350,770	\$312,484
Work-in-process	90,916	101,530
Finished goods	173,104	145,303
	<u>\$ 614,790</u>	<u>\$559,317</u>

NOTE 6 — PROPERTY AND EQUIPMENT, NET

Property and equipment, net, consists of the following:

	September 29, 2013	June 30, 2013
	(in thousands)	
Manufacturing, engineering and office equipment	\$ 530,276	\$ 521,047
Computer equipment and software	120,046	120,144
Land	50,394	65,360
Buildings	232,102	249,126
Leasehold improvements	86,747	76,225
Furniture and fixtures	22,764	21,110
	<u>1,042,329</u>	<u>1,053,012</u>
Less: accumulated depreciation and amortization	<u>(477,484)</u>	<u>(449,102)</u>
	<u>\$ 564,845</u>	<u>\$ 603,910</u>

NOTE 7 — GOODWILL AND INTANGIBLE ASSETS

Goodwill

There was no change in the goodwill balance during the three months ended September 29, 2013. Of the \$1.5 billion goodwill balance as of September 29, 2013, \$61 million is tax deductible and the remaining balance is not tax deductible due to purchase accounting and applicable foreign law.

The Company's goodwill is measured at fair value when an impairment exists. Goodwill is assessed at least annually for impairment. The Company did not record impairments of goodwill during the three months ended September 29, 2013 or September 23, 2012.

Table of Contents**Intangible Assets**

The following table provides details of the Company's intangible assets, including the impact of foreign currency translation adjustments, as of September 29, 2013 (in thousands, except years):

	<u>Gross</u>	<u>Accumulated Amortization</u>	<u>Net</u>	<u>Weighted-Average Useful Life (years)</u>
Customer relationships	\$ 624,656	\$ (121,706)	\$ 502,950	9.01
Existing technology	653,564	(162,444)	491,120	6.97
Patents	32,053	(22,627)	9,426	6.09
Other intangible assets	35,216	(35,108)	108	4.10
Intangible assets subject to amortization	1,345,489	(341,885)	1,003,604	
In process research and development	20,000		20,000	
Development rights	9,100		9,100	
Intangible assets not subject to amortization	29,100		29,100	
Total intangible assets	<u>\$1,374,589</u>	<u>\$ (341,885)</u>	<u>\$1,032,704</u>	

The following table provides details of the Company's intangible assets, including the impact of foreign currency translation adjustments, as of June 30, 2013 (in thousands, except years):

	<u>Gross</u>	<u>Accumulated Amortization</u>	<u>Net</u>	<u>Weighted- Average Useful Life (years)</u>
Customer relationships	\$ 624,686	\$ (103,519)	\$ 521,167	9.01
Existing technology	653,628	(139,894)	513,734	6.97
Patents	32,053	(22,036)	10,017	6.09
Backlog	10,000	(10,000)	—	1.00
Other intangible assets	35,216	(34,889)	327	4.10
Intangible assets subject to amortization	1,355,583	(310,338)	1,045,245	
In process research and development	20,000		20,000	
Development rights	9,100		9,100	
Intangible assets not subject to amortization	29,100		29,100	
Total intangible assets	<u>\$1,384,683</u>	<u>\$ (310,338)</u>	<u>\$1,074,345</u>	

The Company recognized \$41.6 million and \$44.6 million in intangible asset amortization expense during the three months ended September 29, 2013 and September 23, 2012, respectively.

The estimated future amortization expense of purchased intangible assets as of September 29, 2013 is as follows (in thousands):

<u>Fiscal Year</u>	<u>Amount</u>
2014 (9 months)	\$ 120,759
2015	159,102
2016	156,885
2017	155,144
2018	153,958
Thereafter	257,756
	<u>\$1,003,604</u>

NOTE 8 — ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES

Accrued expenses and other current liabilities consist of the following:

	September 29, 2013	June 30, 2013
	(in thousands)	
Accrued compensation	\$ 275,589	\$254,795
Warranty reserves	58,983	52,252
Income and other taxes payable	32,894	39,420
Other	125,394	118,061
	<u>\$ 492,860</u>	<u>\$464,528</u>

NOTE 9 — OTHER EXPENSE, NET

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

	Three Months Ended	
	September 29, 2013	September 23, 2012
	(in thousands)	
Interest income	\$ 2,723	\$ 3,800
Interest expense	(15,302)	(15,144)
Gains (losses) on deferred compensation plan related assets	37	2,741
Foreign exchange losses	(222)	(368)
Other, net	(1,498)	(967)
	<u>\$ (14,262)</u>	<u>\$ (9,938)</u>

NOTE 10 — INCOME TAX EXPENSE

The Company recorded an income tax provision of \$5.6 million, which yielded an effective tax rate for the quarter ended September 29, 2013 of approximately 6.2%. The difference between the U.S. federal statutory tax rate of 35% and the Company's effective tax rate for the three months ended September 29, 2013 is primarily due to the geographic mix of income, the treatment of discrete items in determining the effective tax rate, and the tax effect of non-deductible stock-based compensation.

NOTE 11 — NET INCOME PER SHARE

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

	Three Months Ended	
	September 29, 2013	September 23, 2012
	(in thousands, except per share data)	
Numerator:		
Net income	<u>\$ 85,506</u>	<u>\$ 2,768</u>
Denominator:		
Basic average shares outstanding	162,896	179,928
Effect of potential dilutive securities:		
Employee stock plans	2,868	1,998
Convertible notes	5,599	—
Diluted average shares outstanding	<u>171,363</u>	<u>181,926</u>
Net income per share - basic	<u>\$ 0.52</u>	<u>\$ 0.02</u>
Net income per share - diluted	<u>\$ 0.50</u>	<u>\$ 0.02</u>

[Table of Contents](#)

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

	Three Months Ended	
	September 29, 2013	September 23, 2012
	(in thousands)	
Number of potential dilutive securities excluded	290	2,147

Dilutive shares outstanding include only the effect of the 2041 Notes. Diluted shares outstanding do not include any effect resulting from warrants, assumed conversion of the notes, or note hedges associated with the Company's 2016 or 2018 Notes (as described in Note 13) as their impact would have been anti-dilutive.

NOTE 12 — ACCUMULATED OTHER COMPREHENSIVE LOSS

The components of accumulated other comprehensive income (loss), net of tax at the end of the period, as well as the activity during the period, were as follows:

	Accumulated foreign currency translation adjustment	Accumulated unrealized holding gain (loss) on cash flow hedges	Accumulated unrealized holding gain (loss) on available-for- sale investments	Accumulated unrealized components of defined benefit plans	Total
	(in thousands)				
Balance as of June 30, 2013	\$ (17,178)	\$ 2,822	\$ (15)	\$ (14,322)	\$(28,693)
Other comprehensive income (loss) before reclassifications	3,559	4,507	686	314	9,066
Losses (gains) reclassified from accumulated other comprehensive income to net income	—	(3,802) ⁽¹⁾	74 ⁽²⁾	—	(3,728)
Net current-period other comprehensive income (loss)	\$ 3,559	\$ 705	\$ 760	\$ 314	\$ 5,338
Balance as of September 29, 2013	\$ (13,619)	\$ 3,527	\$ 745	\$ (14,008)	\$(23,355)

- (1) Amount of gain (loss) reclassified from accumulated other comprehensive income into net income (loss) located in revenue: (\$3,010), cost of goods sold: (\$554) and selling, general and administrative expenses: (\$238).
- (2) Amount of loss reclassified from accumulated other comprehensive income into net income located in other expense, net

NOTE 13 — LONG-TERM DEBT

The following table reflects the carrying value of the Company's convertible senior notes and other long-term debt as of September 29, 2013 and June 30, 2013:

	September 29, 2013	June 30, 2013
	(in millions)	
0.50% Notes due 2016	\$ 450.0	\$ 450.0
Less: Unamortized interest discount	(42.0)	(45.7)
Net carrying amount of 0.50% Notes due 2016	408.0	404.3
1.25% Notes due 2018	450.0	450.0
Less: Unamortized interest discount	(73.4)	(76.9)
Net carrying amount of 1.25% Notes due 2018	376.6	373.1
2.625% Notes due 2041	699.9	699.9
Less: Unamortized interest discount	(186.0)	(186.9)
Net carrying amount of 2.625% Notes due 2041	513.9	513.0
Total debt	1,298.5	1,290.4
Less: current portion of debt	(513.9)	(513.0)
Long-term debt	\$ 784.6	\$ 777.4

[Table of Contents](#)

Convertible Senior Notes

In May 2011, the Company issued and sold \$450.0 million in aggregate principal amount of 0.50% Convertible Senior Notes due May 2016 (the “2016 Notes”) at par. At the same time, the Company issued and sold \$450.0 million in aggregate principal amount of 1.25% Convertible Senior Notes due May 2018 (the “2018 Notes”) at par. The 2016 Notes and the 2018 Notes may be converted, under certain circumstances, based on an initial conversion rate of 15.8687 shares of Common Stock per \$1,000 principal amount of notes (which represents an initial conversion price of approximately \$63.02 per share of Common Stock). The net proceeds to the Company from the sale of the 2016 Notes and the 2018 Notes were \$835.5 million. The Company pays cash interest at an annual rate of 0.5% and 1.25%, respectively, on the 2016 Notes and the 2018 Notes, on a semi-annual basis on May 15 and November 15 of each year.

In June 2012, with the acquisition of Novellus, the Company assumed \$700.0 million in aggregate principal amount of 2.625% Convertible Senior Notes due May 2041 (the “2041 Notes,” and collectively with the 2016 Notes and the 2018 Notes, the “Notes”). The 2041 Notes may be converted, under certain circumstances, based on an initial conversion rate of 28.4781 shares of Common Stock per \$1,000 principal amount of notes (which represents an initial conversion price of approximately \$35.11 per share of Common Stock). The Company pays cash interest at an annual rate of 2.625%, on a semi-annual basis on May 15 and November 15 of each year. The 2041 Notes also have a contingent interest payment provision that may require the Company to pay additional interest based on certain thresholds, beginning with the semi-annual interest payment commencing on May 15, 2021, and upon the occurrence of certain events, as outlined in the indenture governing the 2041 Notes. The maximum amount of the contingent interest will accrue at a rate of 2.1% per annum, excluding any potential impact from dividends deemed payable to holders of the 2041 Notes. The contingent interest payment provision has been identified as an embedded derivative, to be accounted for separately, and is recorded at fair value at the end of each reporting period in other non-current liabilities, with any gains and losses recorded in interest expense, within the Condensed Consolidated Statements of Operations.

The Company separately accounts for the liability and equity components of the Notes. The initial debt components of the 2016 Notes, the 2018 Notes, and the 2041 Notes were valued at \$373.8 million, \$345.1 million, and \$509.5 million, respectively, based on the present value of the future cash flows using discount rates of 4.29%, 5.27%, and 4.28%, respectively, the Company’s borrowing rate at the date of the issuance or assumption for similar debt instruments without the conversion feature. The carrying values of the equity components of the 2016 Notes, the 2018 Notes, and the 2041 Notes were \$76.2 million, \$104.9 million, and \$328.1 million, respectively as of September 29, 2013. The effective interest rates on the liability components of the 2016 Notes, the 2018 Notes, and the 2041 Notes for the three months ended September 29, 2013 were 4.29%, 5.27%, and 4.28% respectively. The following table presents the amount of interest cost recognized relating to both the contractual interest coupon and amortization of the discount on the liability component of the Notes during the three months ended September 29, 2013 and September 23, 2012.

	Three Months Ended	
	September 29, 2013	September 23, 2012
	<i>(in millions)</i>	
Contractual interest coupon	\$ 6.6	\$ 6.6
Amortization of interest discount	8.1	7.8
Amortization of issuance costs	0.6	0.6
Total interest cost recognized	<u>\$ 15.3</u>	<u>\$ 15.0</u>

The remaining bond discount of the 2016 Notes, the 2018 Notes, and the 2041 Notes of \$42.0 million, \$73.4 million, and \$186.0 million, respectively, as of September 29, 2013 will be amortized over their respective remaining lives of approximately 2.6 years, 4.6 years, and 27.6 years. As of September 29, 2013, the if-converted value of the 2016 Notes and 2018 Notes did not exceed the aggregate principal amount. As of September 29, 2013, the if-converted value of the 2041 Notes exceeded the aggregate principal amount by \$320 million.

Convertible Note Hedges and Warrants

Concurrently with the issuance of the 2016 Notes and the 2018 Notes, the Company purchased convertible note hedges and sold warrants. The separate convertible note hedge and warrant transactions are collectively structured to reduce the potential future economic dilution associated with the conversion of the 2016 Notes and the 2018 Notes and to increase the effective initial conversion price to \$71.34 and \$76.10 per share, respectively. Each of these components is discussed below:

[Table of Contents](#)

Concurrent with the issuance of the 2016 Notes, the Company sold warrants to purchase up to approximately 7.1 million shares of Common Stock at an exercise price of \$71.34 per share. The warrants expire on a series of dates between August 15, 2016 and October 21, 2016. At expiration, the Company may, at its option, elect to settle the warrants on a net share basis. As of September 29, 2013, the warrants had not been exercised and remained outstanding. In addition, counterparties agreed to sell to the Company up to approximately 7.1 million shares of the Company's common stock, which is the number of shares initially issuable upon conversion of the 2016 Notes in full, at a price of \$63.02 per share. The convertible note hedge transaction will be settled in net shares and will terminate upon the earlier of the maturity date of the 2016 Notes or the first day none of the 2016 Notes remains outstanding due to conversion or otherwise. Settlement of the convertible note hedge in net shares, based on the number of shares issued upon conversion of the 2016 Notes, on the expiration date would result in the Company receiving net shares equivalent to the number of shares issuable by the Company upon conversion of the 2016 Notes.

Concurrent with the issuance of the 2018 Notes, the Company sold warrants to purchase up to approximately 7.1 million shares of Common Stock at an exercise price of \$76.10 per share. The warrants expire on a series of dates between August 15, 2018 and October 23, 2018. At expiration, the Company may, at its option, elect to settle the warrants on a net share basis. As of September 29, 2013, the warrants had not been exercised and remained outstanding. In addition, counterparties agreed to sell to the Company up to approximately 7.1 million shares of the Company's common stock, which is the number of shares initially issuable upon conversion of the 2018 Notes in full, at a price of \$63.02 per share. The convertible note hedge transaction will be settled in net shares and will terminate upon the earlier of the maturity date of the 2018 Notes or the first day none of the 2018 Notes remains outstanding due to conversion or otherwise. Settlement of the convertible note hedge in net shares, based on the number of shares issued upon conversion of the 2018 Notes, on the expiration date would result in the Company receiving net shares equivalent to the number of shares issuable by the Company upon conversion of the 2018 Notes.

Conversion Period

During the fiscal quarters ended June 30, 2013 and September 29, 2013 the Company's common stock for 20 or more trading days of the 30 consecutive trading days preceding the quarter end was greater than or equal to 130% of the 2041 Note conversion price. As a result, the 2041 Notes became convertible at the option of the holder anytime during the fiscal quarters ending September 29, 2013 and December 29, 2013. However, there were no conversions of the 2041 Notes during the September 2013 quarter or the December 2013 quarter as of November 7, 2013.

As a result of the open conversion period, the carrying amount of the 2041 Notes was classified in current liabilities in our Consolidated Balance Sheets as of September 29, 2013 and June 30, 2013. The excess of the amount of cash payable, if converted, over the carrying amount of the 2041 Notes was classified as temporary equity as of September 29, 2013 and June 30, 2013. Upon closure of a conversion period, all 2041 Notes not converted will be reclassified back to noncurrent liabilities and the temporary equity is reclassified to permanent equity.

Fair Value of Notes

As of September 29, 2013, the face values of the 2016 Notes, the 2018 Notes, and the 2041 Notes were \$450.0 million, \$450.0 million, and \$699.9 million, respectively. As of September 29, 2013, the fair values of the 2016 Notes, the 2018 Notes, and the 2041 Notes, which includes the debt and equity components, were approximately \$516.4 million, \$544.5 million, and \$1,110.6 million respectively, based on quoted market prices (Level 1 inputs within the fair value hierarchy).

NOTE 14 — COMMITMENTS

Operating Leases and Related Guarantees

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

On December 18, 2007, the Company entered into two operating leases regarding certain improved properties in Livermore, California. These leases were amended on April 3, 2008 and July 9, 2008 (as so amended, the "Livermore Leases"). On December 21, 2007, the Company entered into a series of four amended and restated operating leases (the "New Fremont Leases," and collectively with the Livermore Leases, the "Operating Leases") with regard to certain improved properties at the Company's headquarters in Fremont, California.

The Operating Leases have a term of approximately seven years ending on the first business day in January 2015. The Company may, at its discretion and with 30 days' notice, elect to purchase the property that is the subject of the Operating Leases for an amount approximating the sum required to pay the amount of the lessor's investment in the property and any accrued but unpaid rent.

[Table of Contents](#)

The Company is required, pursuant to the terms of the Operating Leases, to maintain collateral in an aggregate of approximately \$164.9 million in separate interest-bearing accounts as security for the Company's obligations under the Operating Leases. This amount is recorded as restricted cash in the Company's Consolidated Balance Sheet as of September 29, 2013.

When the terms of the Operating Leases expire, the property subject to those Operating Leases may be remarketed. The Company has guaranteed to the lessor that each property will have a certain minimum residual value. The aggregate guarantee made by the Company under the Operating Leases is generally no more than approximately \$141.7 million; however, under certain default circumstances, the guarantee with regard to an Operating Lease may be 100% of the lessor's aggregate investment in the applicable property, which in no case will exceed \$164.9 million, in the aggregate.

In prior fiscal years, the Company recognized aggregate restructuring charges of \$26.7 million related to the reassessment of the residual value guarantee for such lease. This amount has been recorded in other long-term liabilities as of September 29, 2013.

Other Guarantees

The Company has issued certain indemnifications to its lessors for taxes and general liability under some of its agreements. The Company has entered into certain insurance contracts that may limit its exposure to such indemnifications. As of September 29, 2013, the Company had not recorded any liability in connection with these indemnifications, as it does not believe, based on information available, that it is probable that any amounts will be paid under these guarantees.

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

The Company provides guarantees and standby letters of credit to certain parties as required for certain transactions initiated during the ordinary course of business. As of September 29, 2013, the maximum potential amount of future payments that we could be required to make under these arrangements and letters of credit was \$20.0 million. We do not believe, based on historical experience and information currently available, that it is probable that any amounts will be required to be paid.

Warranties

The Company provides standard warranties on its systems. The liability amount is based on actual historical warranty spending activity by type of system, customer, and geographic region, modified for any known differences such as the impact of system reliability improvements.

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

	Three Months Ended	
	September 29, 2013	September 23, 2012
	(in thousands)	
Balance at beginning of period	\$ 58,078	\$ 70,161
Warranties issued during the period	16,753	19,692
Settlements made during the period	(14,305)	(24,375)
Changes in liability for pre-existing warranties	(655)	2,358
Balance at end of period	<u>\$ 59,871</u>	<u>\$ 67,836</u>

NOTE 15 — RESTRUCTURING AND IMPAIRMENTS

From time to time, Lam initiates restructuring activities to appropriately align its cost structure relative to prevailing economic and industry conditions and associated customer demand as well as in connection with certain acquisitions. Costs associated with restructuring actions can include termination benefits and related charges in addition to facility closure, contract termination and other related activities.

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

[Table of Contents](#)

March 2009 Plan

Beginning in the March 2009 quarter, the Company incurred restructuring expenses designed to align the Company's cost structure with its outlook for the economic environment and business opportunities. The remaining liability under this plan of \$26.7 million relates to the residual value guarantee under certain of the Company's unoccupied operating leases. See Note 14 to the Condensed Consolidated Financial Statements for additional information regarding residual value guarantees.

Acquired Restructuring Liabilities

In addition to restructuring plans initiated by the Company, a restructuring liability related to future rent obligations on unoccupied facilities was assumed in the Novellus acquisition. The associated liability balance of \$12.3 million, as of September 29, 2013, is expected to be paid by the end of fiscal year 2017.

NOTE 16 — STOCK REPURCHASE PROGRAM

On April 22, 2013, the Board of Directors authorized the repurchase of up to \$250 million of Common Stock. These repurchases can be conducted on the open market or as private purchases and may include the use of derivative contracts with large financial institutions, in all cases subject to compliance with applicable law. Repurchases will be funded using the Company's on-shore cash and on-shore cash generation. This repurchase program has no termination date and may be suspended or discontinued at any time.

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

<u>Period</u>	<u>Total Number of Shares Repurchased</u>	<u>Total Cost of Repurchase</u>	<u>Average Price Paid Per Share*</u>	<u>Amount Available Under Repurchase Program</u>
		<u>(in thousands, except per share data)</u>		
Available balance as of June 30, 2013				\$ 250,000
Quarter ended September 29, 2013	1,935	\$ 96,462	\$ 48.06	\$ 153,538

* Average price paid per share excludes accelerated share repurchases for which cost was incurred during the September 2013 quarter, but that had not settled as of quarter end and for which final price per share information was not yet known. See *Collared Accelerated Share Repurchases* section below for details regarding average price associated with these transactions.

In addition to shares repurchased under the Board-authorized repurchase program shown above, during the three months ended September 29, 2013, the Company acquired 159,000 shares at a total cost of \$7.8 million, which the Company withheld through net share settlements to cover minimum tax withholding obligations upon the vesting of restricted stock unit awards granted under the Company's equity compensation plans. The shares retained by the Company through these net share settlements are not a part of the Board-authorized repurchase program but instead are authorized under the Company's equity compensation plans.

As part of its share repurchase program, the Company may from time-to-time enter into structured share repurchase arrangements with financial institutions using general corporate funds. Such arrangements entered into or settled during the three months ended September 29, 2013 included the following:

Collared Accelerated Share Repurchases

During the three months ended September 29, 2013, the Company entered into a collared accelerated share repurchase ("ASR") transaction under a master repurchase arrangement. Under the ASR, the Company made an up-front cash payment of \$75 million, in exchange for an initial delivery of 1.2 million shares of its Common Stock and a subsequent delivery of 0.3 million shares following the initial hedge period.

The number of shares to ultimately be repurchased by the Company is based generally on the volume-weighted average price ("VWAP") of the Common Stock during the term of the ASR minus a pre-determined discount set at inception of the ASR, subject to collar provisions that provide a minimum and maximum number of shares that the Company could repurchase under the agreements. The minimum and maximum thresholds for the transaction were established based on the average of the VWAP prices for the Common Stock during an initial hedge period. The ASR was scheduled to end at any time after September 27, 2013 and on or before November 27, 2013. At the conclusion of the ASR, the Company may receive additional shares based on the VWAP of the Common Stock during the term of the agreement minus the pre-determined fixed discount, however, the total number of shares received under the ASR would not exceed the maximum of 1.7 million shares.

The counterparty designated October 28, 2013 as the termination date, at which time the Company settled the ASR. No additional shares were received at final settlement, which represented a weighted average share price of approximately \$50.40 for the transaction period.

[Table of Contents](#)

The Company accounted for the ASR as two separate transactions: (a) as shares of common stock acquired in a treasury stock transaction recorded on the acquisition date and (b) as a forward contract indexed to the Company's own common stock and classified in stockholders' equity. As such, the Company accounted for the shares that it received under the ASR as a repurchase of its Common Stock for the purpose of calculating earnings per common share. The Company has determined that the forward contract indexed to the Common Stock met all of the applicable criteria for equity classification in accordance with the Derivatives and Hedging topic of the FASB Accounting Standards Codification, and, therefore, the ASR was not accounted for as a derivative instrument. As of September 29, 2013, the aggregate repurchase price of \$75 million was reflected as Treasury stock, at cost, in the Consolidated Balance Sheet.

NOTE 17 — LEGAL PROCEEDINGS

The Company is either a defendant or plaintiff in various actions that have arisen from time to time in the normal course of business, including intellectual property claims. The Company accrues for a liability when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. Significant judgment is required in both the determination of probability and the determination as to whether a loss is reasonably estimable. To the extent there is a reasonable possibility that the losses could exceed the amounts already accrued, the Company believes that the amount of any such additional loss would be immaterial to the Company's business, financial condition, and results of operations.

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

CAUTIONARY STATEMENT REGARDING FORWARD LOOKING STATEMENTS

With the exception of historical facts, the statements contained in this discussion are forward-looking statements, which are subject to the safe harbor provisions created by the Private Securities Litigation Reform Act of 1995. Certain, but not all, of the forward-looking statements in this report are specifically identified as forward-looking, by use of phrases and words such as “we believe,” “we anticipate,” “we expect,” “may,” “should,” “could” and other future-oriented terms. The identification of certain statements as “forward-looking” is not intended to mean that other statements not specifically identified are not forward-looking. Forward-looking statements include, but are not limited to, statements that relate to: trends in the global economic environment and the semiconductor industry; the anticipated levels of, and rates of change in, future shipments, margins, market share, capital expenditures, revenue and operating expenses generally; management’s plans and objectives for our current and future operations and business focus; volatility in our quarterly results; customer requirements and our ability to satisfy those requirements; customer capital spending and their demand for our products, and the reliability of indicators of change in customer spending and demand; our ability to defend our market share and to gain new market share; factors that affect our tax rates; anticipated growth in the industry and the total market for wafer-fabrication equipment and our growth relative to such growth; levels of research and development (“R&D”) expenditures; outsourced activities; the estimates we make, and the accruals we record, in order to implement our critical accounting policies (including but not limited to the adequacy of prior tax payments, future tax liabilities and the adequacy of our accruals relating to them); our access to capital markets; our ability to manage and grow our cash position; and the sufficiency of our financial resources to support future business activities (including but not limited to operations, investments, debt service requirements and capital expenditures). Such statements are based on current expectations and are subject to risks, uncertainties, and changes in condition, significance, value, and effect, including without limitation those discussed below under the heading “Risk Factors” within Part II Item 1A and elsewhere in this report and other documents we file from time to time with the Securities and Exchange Commission (“SEC”), such as our annual report on Form 10-K for the year ended June 30, 2013 (our “2013 Form 10-K”) and our current reports on Form 8-K. Such risks, uncertainties and changes in condition, significance, value, and effect could cause our actual results to differ materially from those expressed in this report and in ways not readily foreseeable. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof and are based on information currently and reasonably known to us. We do not undertake any obligation to release the results of any revisions to these forward-looking statements, which may be made to reflect events or circumstances that occur after the date of this report or to reflect the occurrence or effect of anticipated or unanticipated events.

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

For a full understanding of our financial position and results of operations for the three months ended September 29, 2013, and the related Management’s Discussion and Analysis of Financial Condition and Results of Operations below, you should also read the Condensed Consolidated Financial Statements and notes presented in this Form 10-Q and the financial statements and notes in our 2013 Form 10-K.

Overview

Management’s Discussion and Analysis of Financial Condition and Results of Operations consist of the following sections:

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

Results of Operations provides an analysis of operating results

Critical Accounting Policies and Estimates discusses accounting policies that reflect the more significant judgments and estimates we use to prepare our Condensed Consolidated Financial Statements

Liquidity and Capital Resources provides an analysis of cash flows and financial position

EXECUTIVE SUMMARY

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

[Table of Contents](#)

The semiconductor capital equipment industry has been highly competitive and subject to business cycles that historically have been characterized by rapid changes in demand that necessitate adjusting spending and managing capital allocation prudently across business cycles. Today's leading indicators of change in customer investment patterns, such as electronics demand, memory pricing, and foundry utilization rates, may not be any more reliable than in prior years. Demand for our equipment can vary significantly from period to period as a result of various factors, including, but not limited to, economic conditions (both general and in the semiconductor and electronics industries), industry supply and demand, prices for semiconductors, customer capacity requirements, and our ability to develop, acquire, and market competitive products. For these and other reasons, our results of operations during any particular period are not necessarily indicative of future operating results.

Industry conditions have improved since the beginning of calendar year 2013, and accordingly our September 2013 quarter represents our second consecutive quarter of revenue growth as customers increased their investments in semiconductor equipment to support their business. We believe that, over the long term, demand for our products will increase as customers' capital expenditures rise to meet growing demand for semiconductor devices and to address the increasing complexity of semiconductor manufacturing.

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

	Three Months Ended		
	September 29, 2013	June 30, 2013	September 23, 2012
Revenue	\$ 1,015,059	\$986,214	\$ 906,888
Gross margin	\$ 431,858	\$413,927	\$ 333,886
Gross margin as a percent of revenue	42.5%	42.0%	36.8%
Total operating expenses	\$ 326,450	\$327,429	\$ 317,174
Net income	\$ 85,506	\$ 85,707	\$ 2,768
Diluted net income per share	\$ 0.50	\$ 0.50	\$ 0.02

In the September 2013 quarter, revenue increased compared to the quarter ended June 30, 2013 (the "June 2013 quarter"), reflecting increased investments by our customers. Gross margin as a percent of revenues increased as compared to the June 2013 quarter due to a more favorable business mix combined with factory and manufacturing savings including integration cost synergies. Operating expenses in the September 2013 quarter remained relatively flat as compared to the June 2013 quarter.

Our cash and cash equivalents, short-term investments, and restricted cash and investments balances totaled approximately \$2.6 billion as of September 29, 2013 compared to \$2.7 billion as of June 30, 2013. Cash generated by operations was approximately \$52 million during the September 2013 quarter. We used cash during the September 2013 quarter to repurchase \$104 million of our shares and purchase \$24 million of property and equipment. Employee headcount decreased slightly as of September 29, 2013 as compared to June 30, 2013 to approximately 6,500 people.

RESULTS OF OPERATIONS

Shipments

	Three Months Ended		
	September 29, 2013	June 30, 2013	September 23, 2012
Shipments (in millions)	\$ 987	\$ 1,080	\$ 935
Taiwan	21%	32%	29%
Asia Pacific	19%	15%	22%
Korea	18%	20%	16%
North America	17%	13%	18%
Japan	17%	13%	8%
Europe	8%	7%	7%

Table of Contents

Shipments for the September 2013 quarter decreased 9% compared to the June 2013 quarter, primarily due to a delay in shipments resulting from a change in the timing of investments by certain foundry and memory customers, and increased 6% compared to the September 2012 quarter as customer demand for semiconductor equipment increased. The percentage of total system shipments to each of the market segments we serve were as follows for the periods presented:

	Three Months Ended		
	September 29, 2013	June 30, 2013	September 23, 2012
Memory	48%	46%	42%
Foundry	36%	43%	48%
Logic/integrated device manufacturing	16%	11%	10%

Revenue

	Three Months Ended		
	September 29, 2013	June 30, 2013	September 23, 2012
Revenue (in millions)	\$ 1,015	\$ 986	\$ 907
Taiwan	24%	33%	28%
Korea	23%	17%	24%
Asia Pacific	17%	16%	15%
North America	14%	15%	18%
Japan	13%	11%	8%
Europe	9%	8%	7%

Revenue for the September 2013 quarter increased 3% compared to the June 2013 quarter and 12% as compared to the September 2012 quarter, reflecting increased customer demand. Our deferred revenue balance decreased to \$334 million as of September 29, 2013 compared to \$389 million as of June 30, 2013. Our deferred revenue balance does not include shipments to Japanese customers, to whom title does not transfer until customer acceptance. Shipments to Japanese customers are classified as inventory at cost until the time of acceptance. The anticipated future revenue value from shipments to Japanese customers was approximately \$84 million as of September 29, 2013 compared to \$70 million as of June 30, 2013.

Gross Margin

	Three Months Ended		
	September 29, 2013	June 30, 2013	September 23, 2012
	(in thousands, except percentages)		
Gross margin	\$ 431,858	\$ 413,927	\$ 333,886
Percent of revenue	42.5%	42.0%	36.8%

The increase in gross margin as a percentage of revenue during the September 2013 quarter as compared to the June 2013 quarter is primarily due to a more favorable business mix combined with factory and manufacturing savings including integration cost synergies.

The increase in gross margin as a percentage of revenue during the September 2013 quarter as compared to the September 2012 quarter is primarily due to improved factory savings, as well as a more favorable product mix. Additionally, the acquisition-related inventory fair value impact decreased by \$42 million in the September 2013 quarter as compared to the same quarter last year.

Research and Development

	Three Months Ended		
	September 29, 2013	June 30, 2013	September 23, 2012
	(in thousands, except percentages)		
Research and development ("R&D")	\$ 170,567	\$ 180,220	\$ 163,311
Percent of revenue	16.8%	18.3%	18.0%

[Table of Contents](#)

We continue to make significant R&D investments focused on leading-edge plasma etch, deposition, single-wafer clean and other semiconductor manufacturing requirements. The decrease in R&D expenses during the September 2013 quarter compared to the June 2013 quarter was primarily due to an \$8.5 million decrease associated with the timing of certain equipment development projects.

The increase in R&D expenses during the September 2013 quarter compared to the same period in the prior year was primarily due to a \$5 million increase in salaries and benefits, as well as additional supply purchases.

Selling, General and Administrative

	Three Months Ended		
	September 29, 2013	June 30, 2013	September 23, 2012
	(in thousands, except percentages)		
Selling, general and administrative ("SG&A")	\$ 155,883	\$ 147,209	\$ 153,863
Percent of revenue	15.4%	14.9%	17.0%

The increase in SG&A expenses during the September 2013 quarter compared to the June 2013 quarter was primarily due to a \$7 million impairment of a long-lived asset.

The increase in SG&A expenses in the September 2013 quarter compared to the same period in the prior year was primarily due to a \$7 million impairment of a long-lived asset offset by a \$5 million decrease in integration costs.

Other Expense, Net

Other expense, net consisted of the following:

	Three Months Ended		
	September 29, 2013	June 30, 2013	September 23, 2012
	(in thousands)		
Interest income	\$ 2,723	\$ 3,326	\$ 3,800
Interest expense	(15,302)	(15,114)	(15,144)
Gains (losses) on deferred compensation plan related assets	37	2,677	2,741
Foreign exchange losses	(222)	(1,872)	(368)
Other, net	(1,498)	(1,268)	(967)
	<u>\$ (14,262)</u>	<u>\$ (12,251)</u>	<u>\$ (9,938)</u>

Interest income decreased in the three months ended September 29, 2013 as compared to each of the three months ending June 30, 2013 and September 23, 2012 as a result of lower interest rate yields.

We incurred insignificant foreign exchange losses in the three months ended September 29, 2013 and the three months ended September 23, 2012. Foreign exchange losses in the three months ended June 30, 2013 were related to un-hedged portions of the balance sheet exposures.

In the three months ended June 30, 2013 and September 23, 2012, we recognized gains on assets which are related to obligations under our deferred compensation plan, due to changes in the market value of securities in this portfolio.

Income Tax Expense

Our provision for income taxes and effective tax rate for the periods indicated were as follows:

	Three Months Ended	
	September 29, 2013	September 23, 2012
	(in millions, except percentages)	
Provision for income taxes	\$ 5.6	\$ 4.0
Effective tax rate	6.2%	59.1%

[Table of Contents](#)

The decrease in the effective tax rate for the three months ended September 29, 2013 compared to the three months ended September 23, 2012 was primarily due to the level of income and the treatment of integration and impairment expenses as a discrete event in determining the effective tax rate. In addition, the U.S. federal research and development credit is available through December 31, 2013 for the calculation of the tax provision for the quarter ended September 29, 2013. The credit was not available for the quarter ended September 23, 2012 and therefore no tax benefit was included in the calculation of the tax provision for that quarter.

The effective tax rate of 6.2% for the three months ended September 29, 2013 includes \$4.1 million of tax benefit related to the tax impact of integration, restructuring, and impairment expenses of \$18.9 million. The effective tax rate of 59.1% for the three months ended September 23, 2012 included the tax impact of discrete items that primarily consisted of the effective tax rate impact of \$17.0 million of integration expenses for which little tax benefit was derived due to expenses incurred in low tax jurisdictions.

International revenues account for a significant portion of our total revenues, such that a material portion of our pre-tax income is earned and taxed outside the United States at rates that are generally lower than in the United States. Please refer to Note 10 of the Notes to Condensed Consolidated Financial Statements.

Uncertain Tax Positions

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

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

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

We believe that the following critical accounting policies reflect the more significant judgments and estimates used in the preparation of our consolidated financial statements.

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

[Table of Contents](#)

Inventory Valuation: Inventories are stated at the lower of cost or market using standard costs that generally approximate actual costs on a first-in, first-out basis. We maintain a perpetual inventory system and continuously record the quantity on-hand and standard cost for each product, including purchased components, subassemblies, and finished goods. We maintain the integrity of perpetual inventory records through periodic physical counts of quantities on hand. Finished goods are reported as inventories until the point of title transfer to the customer. Unless specified in the terms of sale, title generally transfers when we complete physical transfer of the products to the freight carrier. Transfer of title for shipments to Japanese customers generally occurs at the time of customer acceptance.

Management evaluates the need to record adjustments for impairment of inventory at least quarterly. Our policy is to assess the valuation of all inventories including manufacturing raw materials, work-in-process, finished goods, and spare parts in each reporting period. Obsolete inventory or inventory in excess of management's estimated usage requirements over the next 12 to 36 months is written down to its estimated market value if less than cost. Estimates of market value include, but are not limited to, management's forecasts related to our future manufacturing schedules, customer demand, technological and/or market obsolescence, general semiconductor market conditions, and possible alternative uses. If future customer demand or market conditions are less favorable than our projections, additional inventory write-downs may be required and would be reflected in cost of goods sold in the period in which we make the revision.

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

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

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

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

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

We recognize the benefit from a tax position only if it is more-likely-than-not that the position would be sustained upon audit based solely on the technical merits of the tax position. Our policy is to include interest and penalties related to unrecognized tax benefits as a component of income tax expense.

[Table of Contents](#)

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

Goodwill and Intangible Assets: The valuation of intangible assets acquired in a business combination requires the use of management estimates including but not limited to estimating future expected cash flows from assets acquired and determining discount rates. Management's estimates of fair value are based upon assumptions believed to be reasonable, but which are inherently uncertain and unpredictable and, as a result, actual results may differ from estimates. Estimates associated with the accounting for acquisitions may change as additional information becomes available.

Goodwill represents the amount by which the purchase price in each business combination exceeds the fair value of the net tangible and identifiable intangible assets acquired. Each component of the Company for which discrete financial information is available and for which segment management regularly reviews the results of operations is considered a reporting unit. All goodwill acquired in a business combination is assigned to one or more reporting units as of the acquisition date. Goodwill is assigned to the Company's reporting units that are expected to benefit from the synergies of the combination. The goodwill assigned to a reporting unit is the difference between the acquisition consideration assigned to the reporting unit on a relative fair value basis and the fair value of acquired assets and liabilities that can be specifically attributed to the reporting unit. We test goodwill and identifiable intangible assets with indefinite useful lives for impairment at least annually. We amortize intangible assets with estimable useful lives over their respective estimated useful lives, and we review for impairment whenever events or changes in circumstances indicate that the carrying amount of the intangible asset may not be recoverable and the carrying amount exceeds its fair value.

We review goodwill at least annually for impairment. If certain events or indicators of impairment occur between annual impairment tests, we would perform an impairment test of goodwill at that date. In testing for a potential impairment of goodwill, we: (1) allocate goodwill to our reporting units to which the acquired goodwill relates; (2) estimate the fair value of our reporting units; and (3) determine the carrying value (book value) of those reporting units, as some of the assets and liabilities related to those reporting units are not held by those reporting units but by a corporate function. Prior to this allocation of the assets to the reporting units, we are required to assess long-lived assets for impairment. Furthermore, if the estimated fair value of a reporting unit is less than the carrying value, we must estimate the fair value of all identifiable assets and liabilities of that reporting unit, in a manner similar to a purchase price allocation for an acquired business. This can require independent valuations of certain internally generated and unrecognized intangible assets such as in-process R&D and developed technology. Only after this process is completed can the amount of goodwill impairment, if any, be determined. Beginning with our fiscal year 2012 goodwill impairment analysis, we adopted new accounting guidance that allowed us to first assess qualitative factors to determine whether it was necessary to perform a quantitative analysis. Under the revised guidance, an entity is no longer required to calculate the fair value of a reporting unit unless the entity determines, based on a qualitative assessment, that it is more-likely-than-not that its fair value is less than its carrying amount. Our most recent annual goodwill impairment analysis, which was performed as of April 1, 2013, did not result in a goodwill impairment charge, nor did we record any goodwill impairment in fiscal 2012 or 2011. As a result of historical performance and growth potential, our Clean systems reporting unit may be at greater risk for goodwill impairment than our other reporting units if our actual results for this reporting unit differ from our projections.

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

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

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

[Table of Contents](#)

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

Recent Accounting Pronouncements

In July 2013, the FASB released Accounting Standards Update 2013-11, "Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists." The new standard requires that an unrecognized tax benefit should be presented as a reduction of a deferred tax asset for a net operating loss carryforward or other tax credit carryforward when settlement in this manner is available under the tax law. We are required to adopt this standard starting fiscal year 2015 and are currently in the process of determining the impact, if any, on our financial position.

LIQUIDITY AND CAPITAL RESOURCES

As of September 29, 2013, we had \$2.6 billion in gross cash and cash equivalents, short-term investments, and restricted cash and investments (total cash and investments) compared to \$2.7 billion as of June 30, 2013. Approximately \$2.0 billion of our total cash and investments as of September 29, 2013 is held outside the U.S. in our foreign subsidiaries, of which substantially all would be subject to tax at U.S. rates if it were to be repatriated.

Cash Flows from Operating Activities

Net cash provided by operating activities of \$52 million during the three months ended September 29, 2013 consisted of (in millions):

Net income	\$ 85.5
Non-cash charges:	
Depreciation and amortization	74.3
Equity-based compensation	23.2
Amortization of convertible note discount	8.1
Impairment of long lived assets	7.0
Changes in operating asset and liability accounts	(150.3)
Other	4.1
	<u>\$ 51.9</u>

Changes in operating asset and liability accounts, net of foreign exchange impact, included the following uses of cash: increases in accounts receivable of \$109.2 million and inventories of \$55.1 million and a decrease in deferred profit of \$36.6 million, partially offset by sources of cash resulting from decreases in prepaid expenses of \$22.0 million and increases in accrued liabilities of \$22.7 million and trade accounts payable of \$5.8 million.

Cash Flows from Investing Activities

Net cash provided by investing activities during the three months ended September 29, 2013 was \$18.9 million, primarily consisting of net sales of available-for-sale securities of \$42.6 million partially offset by capital expenditures of \$23.8 million.

Cash Flows from Financing Activities

Net cash used for financing activities during the three months ended September 29, 2013 was \$76.6 million, primarily consisting of \$104.3 million in treasury stock repurchases partially offset by net proceeds from issuance of Lam Research common stock ("Common Stock") related to employee equity-based plans of \$27.7 million.

[Table of Contents](#)

Liquidity

Given the cyclical nature of the semiconductor equipment industry, we believe that maintaining sufficient liquidity reserves is important to support sustaining levels of investment in R&D and capital infrastructure. Anticipated cash flows from operations based on our current business outlook, combined with our current levels of cash, cash equivalents, and short term investments at September 29, 2013 are expected to be sufficient to support our anticipated levels of operations, investments, debt service requirements, and capital expenditures, through at least the next 12 months. However, uncertainty in the global economy and the semiconductor industry, as well as disruptions in credit markets have in the past, and could in the future, impact customer demand for our products, as well as our ability to manage normal commercial relationships with our customers, suppliers, and creditors.

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

ITEM 3. Quantitative and Qualitative Disclosures about Market Risk

For financial market risks related to changes in interest rates, marketable equity security prices, and foreign currency exchange rates, refer to Part II, Item 7A, “Quantitative and Qualitative Disclosures About Market Risk”, in our 2013 Form 10-K. Other than noted below, our exposure related to market risk has not changed materially since June 30, 2013. All of the potential changes noted below are based on sensitivity analyses performed on our financial position as of September 29, 2013. Actual results may differ materially.

Fixed Income Securities

Our investments in various interest earning securities carry a degree of market risk for changes in interest rates. At any time, a sharp rise in interest rates could have a material adverse impact on the fair value of our fixed income investment portfolio. Conversely, declines in interest rates could have a material adverse impact on interest income for our investment portfolio. We target to maintain a conservative investment policy, which focuses on the safety and preservation of our capital by limiting default risk, market risk, reinvestment risk, and concentration risk. The following table presents the hypothetical fair values of fixed income securities that would result from selected potential decreases and increases in interest rates. Market changes reflect immediate hypothetical parallel shifts in the yield curve of plus or minus 50 basis points (“BPS”), 100 BPS, and 150 BPS. The hypothetical fair values as of September 29, 2013 were as follows:

	Valuation of Securities Given an Interest Rate Decrease of X Basis Points			Fair Value as of September 29, 2013		Valuation of Securities Given an Interest Rate Increase of X Basis Points	
	(150 BPS)	(100 BPS)	(50 BPS)	0.00%	50 BPS	100 BPS	150 BPS
	(in thousands)						
Municipal Notes and Bonds	\$ 252,192	\$ 250,750	\$ 249,307	\$ 247,864	\$ 246,421	\$ 244,978	\$ 243,536
US Treasury & Agencies	158,741	157,294	155,847	154,401	152,953	151,506	150,059
Government-Sponsored Enterprises	55,908	55,510	55,112	54,713	54,315	53,917	53,519
Foreign Government Bond	24,156	24,004	23,851	23,699	23,546	23,394	23,241
Corporate Notes and Bonds	858,165	853,809	849,452	845,095	840,739	836,382	832,026
Mortgage Backed Securities - Residential	26,313	25,948	25,583	25,218	24,854	24,489	24,124
Mortgage Backed Securities - Commercial	104,580	103,955	103,331	103,092	102,082	101,457	100,833
Total	<u>\$1,480,055</u>	<u>\$1,471,270</u>	<u>\$1,462,483</u>	<u>\$1,454,082</u>	<u>\$1,444,910</u>	<u>\$1,436,123</u>	<u>\$1,427,338</u>

We mitigate default risk by investing in high credit quality securities and by positioning our portfolio to respond appropriately to a significant reduction in a credit rating of any investment issuer or guarantor. The portfolio includes only marketable securities with active secondary or resale markets to achieve portfolio liquidity and maintain a prudent amount of diversification.

ITEM 4. Controls and Procedures

Design of Disclosure Controls and Procedures and Internal Control over Financial Reporting

We maintain disclosure controls and procedures and internal control over financial reporting that are designed to comply with Rule 13a-15 of the Exchange Act. In designing and evaluating the controls and procedures associated with each, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and that the effectiveness of controls cannot be absolute because the cost to design and implement a control to identify errors or mitigate the risk of errors occurring should not outweigh the potential loss caused by the errors that would likely be detected by the control. Moreover, we believe that a control system cannot be guaranteed to be 100% effective all of the time. Accordingly, a control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met.

Disclosure Controls and Procedures

As required by Exchange Act Rule 13a-15(b), as of September 29, 2013, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and our Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as defined in Rule 13a-15(e). Based upon that evaluation, our Chief Executive Officer, along with our Chief Financial Officer, concluded that our disclosure controls and procedures are effective at the reasonable assurance level.

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

Changes in Internal Control over Financial Reporting

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

Effectiveness of Controls

While we believe the present design of our disclosure controls and procedures and internal control over financial reporting is effective, future events affecting our business may cause us to modify our disclosure controls and procedures or internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

The Company is either a defendant or plaintiff in various actions that have arisen from time to time in the normal course of business, including intellectual property claims. The Company accrues for a liability when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. Significant judgment is required in both the determination of probability and the determination as to whether a loss is reasonably estimable. To the extent there is a reasonable possibility that the losses could exceed the amounts already accrued, the Company believes that the amount of any such additional loss would be immaterial to the Company's business, financial condition, and results of operations.

ITEM 1A. Risk Factors

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

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

The business cycle in the semiconductor equipment industry has historically been characterized by frequent periods of rapid change in demand that challenge our management to adjust spending and other resources allocated to operating activities. During periods of rapid growth or decline in demand for our products and services, we face significant challenges in maintaining adequate financial and business controls, management processes, information systems, procedures for training and managing our work force, and in appropriately sizing our supply chain infrastructure, work force, and other components of our business on a timely basis. If we do not adequately meet these challenges during periods of demand decline, our gross margins and earnings may be negatively impacted.

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

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

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

Our business depends on the capital equipment expenditures of semiconductor manufacturers, which in turn depend on the current and anticipated market demand for integrated circuits. The semiconductor industry is cyclical in nature and experiences periodic downturns. Global economic and business conditions, which are often unpredictable, have historically impacted customer demand for our products and normal commercial relationships with our customers, suppliers, and creditors. Additionally, in times of economic uncertainty our customers' budgets for our products, or their ability to access credit to purchase them, could be adversely affected. This would limit their ability to purchase our products and services. As a result, economic downturns can cause material adverse changes to our results of operations and financial condition including, but not limited to:

- a decline in demand for our products or services;
- an increase in reserves on accounts receivable due to our customers' inability to pay us;
- an increase in reserves on inventory balances due to excess or obsolete inventory as a result of our inability to sell such inventory;
- valuation allowances on deferred tax assets;
- restructuring charges;
- asset impairments including the potential impairment of goodwill and other intangible assets;
- a decline in the value of our investments;

[Table of Contents](#)

- exposure to claims from our suppliers for payment on inventory that is ordered in anticipation of customer purchases that do not come to fruition;
- a decline in the value of certain facilities we lease to less than our residual value guarantee with the lessor; and
- challenges maintaining reliable and uninterrupted sources of supply.

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

Our Long-term Success, Results of Operations and the Value of Our Common Stock Depend on Our Ability to Successfully Combine the Novellus Business With Our Pre-existing Business, Which May Be More Difficult, Costly or Time-consuming Than Expected

On June 4, 2012, we acquired Novellus Systems, Inc. (“Novellus”), and we are in the process of completing the combination of Novellus’ business with our pre-existing business. Our future success, results of operations and the value of our common stock depend, in part, on our ability to realize the anticipated benefits of the acquisition. For us to fully realize these anticipated benefits, we must successfully combine our businesses in an efficient and effective manner and communicate the impact that the business combination will have on our financial statements. If we are not able to achieve and clearly communicate these objectives within the anticipated time frame, or at all, the anticipated benefits and cost savings of the acquisition may not be realized fully, or at all, or may take longer than expected to realize, and our results of operations and the value of our common stock may be adversely affected.

Specific issues that we will have to continue to address in integrating the operations of Novellus into our pre-existing operations in order to realize the anticipated benefits of the acquisition include, among other things:

- integrating and optimizing the utilization of the properties, equipment, suppliers, distribution channels, manufacturing, service, marketing, promotion and sales activities and information technologies of the combined company;
- consolidating corporate and administrative infrastructures of the combined company;
- coordinating geographically dispersed organizations of the combined company;
- retaining and growing business at existing customers and attracting new customers to the combined company;
- managing our contractual and business relationships with common suppliers and customers to reduce inconsistent or inefficient effects;
- retaining key employees and utilizing their technical knowledge and business expertise;
- communicating the inherently complex factors that a business combination will have on our financial position and results of operations; and
- conforming standards, controls, procedures, policies, business cultures and compensation structures throughout the combined company.

In addition, integration efforts have diverted and will continue to divert management attention and resources, the actual integration may result in additional and unforeseen expenses, and the anticipated benefits of the integration plan may not be realized. Actual synergies may be lower than what we expect and may take longer to achieve than anticipated. If we are not able to adequately address these challenges, we may be unable to successfully integrate the combined company’s operations or to realize the anticipated benefits of the acquisition.

Our Quarterly Revenues and Operating Results Are Unpredictable

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

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

Table of Contents

- the size and timing of orders from customers;
- procurement shortages;
- the failure of our suppliers or outsource providers to perform their obligations in a manner consistent with our expectations;
- manufacturing difficulties;
- customer cancellations or delays in shipments, installations, and/or customer acceptances;
- the extent that customers continue to purchase and use our products and services in their business;
- changes in average selling prices, customer mix, and product mix;
- our ability in a timely manner to develop, introduce and market new, enhanced, and competitive products;
- our competitors' introduction of new products;
- legal or technical challenges to our products and technology;
- transportation, communication, demand, information technology or supply disruptions based on factors outside our control such as strikes, acts of God, wars, terrorist activities, and natural disasters;
- legal, tax, accounting, or regulatory changes (including but not limited to change in import/export regulations) or changes in the interpretation or enforcement of existing requirements;
- changes in our estimated effective tax rate;
- foreign currency exchange rate fluctuations; and
- the dilutive impact of our convertible notes and related warrants on our earnings per share.

Our Leverage and Debt Service Obligations and Potential Note Conversion or Related Hedging Activities May Adversely Affect Our Financial Condition, Results of Operations and Earnings Per Share

As a result of the sale of our 2016 and 2018 convertible notes and the assumption of the 2041 convertible notes in connection with the Novellus acquisition (collectively the "Notes"), we have a greater amount of debt than we have maintained in the past. Our maintenance of higher levels of indebtedness could have adverse consequences including:

- impacting our ability to satisfy our obligations;
- increasing the portion of our cash flows that may have to be dedicated to interest and principal payments and may not be available for operations, working capital, capital expenditures, expansion, acquisitions or general corporate or other purposes; and
- impairing our ability to obtain additional financing in the future.

Our ability to meet our expenses and debt obligations will depend on our future performance, which will be affected by financial, business, economic, regulatory and other factors. Furthermore, our operations may not generate sufficient cash flows to enable us to meet our expenses and service our debt. As a result, we may need to enter into new financing arrangements to obtain the necessary funds. If we determine it is necessary to seek additional funding for any reason, we may not be able to obtain such funding or, if funding is available, obtain it on acceptable terms. If we fail to make a payment on our debt, we could be in default on such debt, and this default could cause us to be in default on our other outstanding indebtedness.

Conversion of our Notes may cause dilution to our shareholders and to our earnings per share. Upon conversion of any Notes, we will deliver cash in the amount of the principal amount of the Notes and, with respect to any excess conversion value greater than the principal amount of the Notes, shares of our common stock, which would result in dilution to our shareholders. This dilution may be mitigated to some extent by the hedging transactions we entered into in connection with the sale of the 2016 and 2018 Notes or through share repurchases. Prior to the maturity of the Notes, if the price of our common stock exceeds the conversion price, U.S. GAAP requires that we report an increase in diluted share count, which would result in lower reported earnings per share. The price of our common stock could also be affected by sales of our common stock by investors who view the Notes as a more attractive means of equity participation in our company and by hedging activity that may develop involving our common stock by holders of the Notes.

We Have a Limited Number of Key Customers

Sales to a limited number of large customers constitute a significant portion of our overall revenue, shipments and profitability. As a result, the actions of even one customer may subject us to variability in those areas that are difficult to predict. In addition, large customers may be able to negotiate requirements that result in decreased pricing, increased costs and/or lower margins for us, such as regional manufacturing expectations, compliance to specific environmental, social and corporate governance standards, and limitations on our ability to share jointly developed technology with others. Similarly, significant portions of our credit risk may, at any given time, be concentrated among a limited number of customers, so that the failure of even one of these key customers to pay its obligations to us could significantly impact our financial results.

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

Rapid technological changes in semiconductor manufacturing processes subject us to increased pressure to develop technological advances that enable those processes. We believe that our future success depends in part upon our ability to develop and offer new products with improved capabilities and to continue to enhance our existing products. If new products have reliability, quality, or design problems, our performance may be impacted by reduced orders, higher manufacturing costs, delays in acceptance of and payment for new products, and additional service and warranty expenses. We may be unable to develop and manufacture new products successfully, or new products that we introduce may fail in the marketplace. The expected industry transition to a 450mm platform represents an emerging challenge for our business, and our failure to address that transition in a timely manner with productive and cost-effective products could adversely affect our business in a material way. Our failure to commercialize new products in a timely manner could result in loss of market share, unanticipated costs, and inventory obsolescence, which would adversely affect our financial results.

In order to develop new products and processes, we expect to continue to make significant investments in R&D and to pursue joint development relationships with customers, suppliers or other members of the industry. We must manage product transitions and joint development relationships successfully, as the introduction of new products could adversely affect our sales of existing products and certain jointly developed technologies may be subject to restrictions on our ability to share that technology with other customers, which could limit our market for products incorporating those technologies. Future technologies, processes or product developments may render our current product offerings obsolete, leaving us with non-competitive products, or obsolete inventory, or both. Moreover, customers may adopt new technologies or processes to address the complex challenges associated with next generation devices. This shift may result in a reduction in the size of our addressable markets or could increase the relative size of markets in which we either do not compete or have relatively low market share.

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

We derive a substantial percentage of our revenues from a limited number of products. System sales constitute a significant portion of our total revenue. Our systems are priced up to approximately \$9 million per unit, and our revenues in any given quarter are dependent upon the acceptance of a limited number of systems. As a result, the inability to recognize revenue on even a few systems can cause a significantly adverse impact on our revenues for a given quarter, and, in the longer term, the continued market acceptance of these products is critical to our future success. Our business, operating results, financial condition, and cash flows could therefore be adversely affected by:

- a decline in demand for even a limited number of our products;
- a failure to achieve continued market acceptance of our key products;
- export restrictions or other regulatory or legislative actions that could limit our ability to sell those products to key customer or market segments;
- an improved version of products being offered by a competitor in the market in which we participate;
- increased pressure from competitors that offer broader product lines;
- technological changes that we are unable to address with our products; or
- a failure to release new or enhanced versions of our products on a timely basis.

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

Strategic Alliances and Potential Customer Consolidation May Have Negative Effects on Our Business

Increasingly, semiconductor manufacturing companies are entering into strategic alliances or consolidating with one another to expedite the development of processes and other manufacturing technologies and/or achieve economies of scale. The outcomes of such an alliance can be the definition of a particular tool set for a certain function and/or the standardization of a series of process steps that use a specific set of manufacturing equipment; while the outcomes of consolidation can lead to an overall reduction in the market for semiconductor manufacturing equipment as customers' operations achieve economies of scale and/or increased purchasing power based on their higher volumes. While in certain instances this could work to our advantage, if our equipment becomes the basis for the function or process as the tool of choice for the larger consolidated customer or alliance, it could also work to our disadvantage if a competitor's tools or equipment become the standard equipment for such functions or processes.

Similarly, our customers may team with, or follow the lead of, educational or research institutions that establish processes for accomplishing various tasks or manufacturing steps. If those institutions utilize a competitor's equipment when they establish those processes, it is likely that customers will tend to use the same equipment in setting up their own manufacturing lines. Even if they select our equipment, the institutions and the customers that follow their lead could impose conditions on acceptance of that equipment, such as adherence to standards and requirements or limitations on how we license our proprietary rights, that increase our costs or require us to take on greater risk. These actions could adversely impact our market share and financial results.

We Depend On a Limited Number of Key Suppliers and Outsource Providers, and We Run the Risk That They Might Not Perform as We Expect

Outsource providers and component suppliers have played and will continue to play a key role in our manufacturing operations and in many of our transactional and administrative functions, such as information technology, facilities management, and certain elements of our finance organization. These providers and suppliers might suffer financial setbacks, be acquired by third parties, become subject to exclusivity arrangements that preclude further business with us or suffer *force majeure* events that could interrupt or impair their continued ability to perform as we expect.

Although we attempt to select reputable providers and suppliers, and we attempt to secure their performance on terms documented in written contracts, it is possible that one or more of these providers or suppliers could fail to perform as we expect, and such failure could have an adverse impact on our business. In some cases, the requirements of our business mandate that we obtain certain components and sub-assemblies included in our products from a single supplier or a limited group of suppliers. Where practical, we endeavor to establish alternative sources to mitigate the risk that the failure of any single provider or supplier will adversely affect our business, but this is not feasible in all circumstances. There is therefore a risk that a prolonged inability to obtain certain components or secure key services could impair our ability to manage operations, ship products and generate revenues, which could adversely affect our operating results and damage our customer relationships.

We Face Risks Related to the Disruption of Our Primary Manufacturing Facilities

Our manufacturing facilities are concentrated in just a few locations. These locations are subject to disruption for a variety of reasons such as natural disasters, terrorist attacks, disruptions of our information technology resources and utility interruptions. Such disruptions may cause delays in shipping our products which could result in the loss of business or customer trust, adversely affecting our business and operating results.

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

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

We Face a Challenging and Complex Competitive Environment

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

[Table of Contents](#)

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

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

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

Non-U.S. sales accounted for approximately 86% of total revenue in the three months ended September 29, 2013, 80% of total revenue in fiscal year 2013, and 83% of total revenue in fiscal year 2012. We expect that international sales will continue to account for a substantial majority of our total revenue in future years.

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

- trade balance issues;
- global economic and political conditions;
- changes in currency controls;
- differences in the enforcement of intellectual property and contract rights in varying jurisdictions;
- our ability to respond to customer and foreign government demands for locally sourced systems, spare parts and services and develop the necessary relationships with local suppliers;
- compliance with U.S. and international laws and regulations affecting foreign operations, including U.S. and international export restrictions and foreign labor laws;
- fluctuations in interest and foreign currency exchange rates;
- our ability to repatriate cash in a tax-efficient manner;
- the need for technical support resources in different locations; and
- our ability to secure and retain qualified people in all necessary locations for the successful operation of our business.

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

[Table of Contents](#)

We are potentially exposed to adverse as well as beneficial movements in foreign currency exchange rates. The majority of our sales and expenses are denominated in U.S. dollars. However, we are exposed to foreign currency exchange rate fluctuations primarily related to revenues denominated in Japanese yen and expenses denominated in euro. Currently, we enter into foreign currency forward contracts to minimize the short-term impact of the foreign currency exchange rate fluctuations on certain foreign currency monetary assets and liabilities, primarily third party accounts receivables, accounts payables and intercompany receivables and payables. In addition, we hedge certain anticipated foreign currency cash flows, primarily anticipated revenues denominated in Japanese yen and euro-denominated expenses. We believe these are our primary exposures to currency rate fluctuation. We expect to continue to enter into hedging transactions, for the purposes outlined, for the foreseeable future. However, these hedging transactions may not achieve their desired effect because differences between the actual timing of the underlying exposures and our forecasts of those exposures may leave us either over-or under-hedged on any given transaction. Moreover, by hedging these foreign currency denominated revenues, expenses, monetary assets and liabilities with foreign currency forward contracts, we may miss favorable currency trends that would have been advantageous to us but for the hedges. Additionally, we are exposed to short-term foreign currency exchange rate fluctuations on non-U.S. dollar-denominated monetary assets and liabilities (other than those currency exposures previously discussed) and currently we do not enter into foreign currency hedge contracts against these exposures. Therefore, we are subject to both favorable and unfavorable foreign currency exchange rate fluctuations to the extent that we transact business (including intercompany transactions) for these currencies.

The magnitude of our overseas business also affects where our cash is generated. Certain uses of cash, such as share repurchases or the repayment of our convertible notes, can usually only be made with cash balances and cash generated on-shore. Since the majority of our cash is generated outside of the United States, this may limit certain business decisions and adversely affect business outcomes.

Our Ability to Attract, Retain and Motivate Key Employees Is Critical to Our Success

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

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

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

In addition, we have recently merged the enterprise system used by Novellus prior to its acquisition by Lam with our global enterprise system. Combining these two systems was a complex process and there is possibility for error in the merger process. While we have exerted considerable efforts to ensure a fully operational system, should an error occur there could be a short-term adverse effect on our ability to conduct business in an efficient manner.

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

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

[Table of Contents](#)

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

We are subject to a variety of governmental regulations related to the handling, discharge, and disposal of toxic, volatile or otherwise hazardous chemicals. We believe that we are generally in compliance with these regulations and that we have obtained (or will obtain or are otherwise addressing the need for) all environmental permits necessary to conduct our business. These permits generally relate to the handling and disposal of hazardous wastes. Nevertheless, the failure to comply with present or future regulations could result in fines being imposed on us, require us to suspend production, or cease operations or cause our customers to not accept our products. These regulations could require us to alter our current operations, to acquire significant additional equipment or to incur substantial other expenses to comply with environmental regulations. Any failure to comply with regulations governing the use, handling, sale, transport or disposal of hazardous substances could subject us to future liabilities.

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

An important element of our management strategy is to review acquisition prospects that would complement our existing products, augment our market coverage and distribution ability, or enhance our technological capabilities. As a result, we may make acquisitions of complementary companies, products or technologies, or we may reduce or dispose of certain product lines or technologies that no longer fit our long-term strategies. Managing an acquired business, disposing of product technologies or reducing personnel entail numerous operational and financial risks, including difficulties in assimilating acquired operations and new personnel or separating existing business or product groups, diversion of management's attention away from other business concerns, amortization of acquired intangible assets, adverse customer reaction to our decision to cease support for a product, and potential loss of key employees or customers of acquired or disposed operations. There can be no assurance that we will be able to achieve and manage successfully any such integration of potential acquisitions, disposition of product lines or technologies, or reduction in personnel or that our management, personnel, or systems will be adequate to support continued operations. Any such inabilities or inadequacies could have a material adverse effect on our business, operating results, financial condition, and cash flows.

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

The Market for Our Common Stock is Volatile, Which May Affect Our Ability to Raise Capital, Make Acquisitions, or Subject Our Business to Additional Costs

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

- general market, semiconductor, or semiconductor equipment industry conditions;
- economic or political events and trends occurring globally or in any of our key sales regions;
- variations in our quarterly operating results and financial condition, including our liquidity;
- variations in our revenues, earnings or other business and financial metrics from forecasts by us or securities analysts, or from those experienced by other companies in our industry;
- announcements of restructurings, reductions in force, departure of key employees, and/or consolidations of operations;
- government regulations;
- developments in, or claims relating to, patent or other proprietary rights;
- technological innovations and the introduction of new products by us or our competitors;
- commercial success or failure of our new and existing products;
- disruptions of relationships with key customers or suppliers; or
- dilutive impacts of our Notes and related warrants.

In addition, the stock market experiences significant price and volume fluctuations. Historically, we have witnessed significant volatility in the price of our Common Stock due in part to the actual or anticipated movement in interest rates and the price of and markets for semiconductors. These broad market and industry factors have and may again adversely affect the price of our Common Stock, regardless of our actual operating performance. In the past, following volatile periods in the price of their stock, many companies became the object of securities class action litigation. If we are sued in a securities class action, we could incur substantial costs, and it could divert management's attention and resources and have an unfavorable impact on our financial performance and the price for our Common Stock.

[Table of Contents](#)

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

Third parties may assert infringement, unfair competition, product liability, breach of contract, or other claims against us. From time to time, other parties send us notices alleging that our products infringe their patent or other intellectual property rights. In addition, law enforcement authorities may seek criminal charges relating to intellectual property or other issues. We also face risks of claims arising from commercial and other relationships. In addition, our Bylaws and other indemnity obligations provide that we will indemnify officers and directors against losses that they may incur in legal proceedings resulting from their service to us. From time to time, in the normal course of business, we indemnify third parties with whom we enter into contractual relationships, including customers and suppliers, with respect to certain matters. We have agreed, under certain conditions, to hold these third parties harmless against specified losses, such as those arising from a breach of representations or covenants, other third party claims that our products when used for their intended purposes infringe the intellectual property rights of such other third parties, or other claims made against certain parties. In such cases, it is our policy either to defend the claims or to negotiate licenses or other settlements on commercially reasonable terms. However, we may be unable in the future to negotiate necessary licenses or reach agreement on other settlements on commercially reasonable terms, or at all, and any litigation resulting from these claims by other parties may materially adversely affect our business and financial results, and we may be subject to substantial damage awards and penalties. Moreover, although we have insurance to protect us from certain claims and cover certain losses to our property, such insurance may not cover us for the full amount of any losses, or at all, and may be subject to substantial exclusions and deductibles.

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

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

We May Incur Impairments to Goodwill or Long-Lived Assets

We review our long-lived assets, including goodwill and other intangible assets, for impairment annually or whenever events or changes in circumstances indicate that the carrying amount of these assets may not be recoverable. Negative industry or economic trends, including reduced market prices of our common stock, reduced estimates of future cash flows, disruptions to our business, slower growth rates, or lack of growth in our relevant business segments, could lead to impairment charges against our long-lived assets, including goodwill and other intangible assets. If, in any period, our stock price decreases to the point where our fair value, as determined by our market capitalization, is less than the book value of our assets, this could also indicate a potential impairment, and we may be required to record an impairment charge in that period, which could adversely affect our result of operations.

Our valuation methodology for assessing impairment requires management to make judgments and assumptions based on historical experience and to rely heavily on projections of future operating performance. We operate in a highly competitive environment and projections of future operating result and cash flows may vary significantly from actual results. Additionally, if our analysis indicates potential impairment to goodwill one or more of our business segments, we may be required to record additional charges to earnings in our financial statements, which could negatively affect our results of operations.

We Are Exposed to Various Risks from Our Regulatory Environment

We are subject to various risks related to (i) new, different, inconsistent or even conflicting laws, rules and regulations that may be enacted by legislative bodies and/or regulatory agencies in the countries that we operate; (ii) disagreements or disputes between national or regional regulatory agencies related to international trade; and (iii) the interpretation and application of laws, rules and regulations. As a public company with global operations, we are subject to the laws of multiple jurisdictions and the rules and regulations of various governing bodies, including those related to financial and other disclosures, corporate governance, privacy, anti-corruption, such as the Foreign Corrupt Practices Act and other local laws prohibiting corrupt payments to governmental officials, and antitrust regulations, among others. One of these laws imposes new disclosure requirements regarding the use of certain minerals, which may have originated from the Democratic Republic of the Congo and adjoining countries in our products. This new requirement could affect the pricing, sourcing and availability of minerals used in the manufacture of components we use in our products. In addition, there will be additional costs associated with complying with the disclosure requirements, such as costs related to determining the source of any of the covered minerals used in our products. Our supply chain is complex, and we may be unable to verify the origins for all metals used in our products. Financial reform legislation and the regulations enacted under such legislation have also added costs to our business by, among other things, requiring advisory votes on executive compensation and on severance packages upon a change in control.

To maintain high standards of corporate governance and public disclosure, we intend to invest all reasonably necessary resources to comply with all evolving standards. Changes in or ambiguous interpretations of laws, regulations and standards may create uncertainty regarding compliance matters. Efforts to comply with new and changing regulations have resulted in, and are likely to continue to result in, increased general and administrative expenses and a diversion of management's time and attention from revenue generating activities to compliance activities. If we are found by a court or regulatory agency not to be in compliance with the laws and regulations, our business, financial condition, and results of operations could be adversely affected.

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

Repurchases of Company Shares

On April 22, 2013, the Board of Directors authorized the repurchase of up to \$250 million of Common Stock. These repurchases can be conducted on the open market or as private purchases and may include the use of derivative contracts with large financial institutions, in all cases subject to compliance with applicable law. Repurchases will be funded using the Company's on-shore cash and on-shore cash generation. This repurchase program has no termination date and may be suspended or discontinued at any time.

As part of its share repurchase program, the Company may from time-to-time enter into structured share repurchase arrangements with financial institutions using general corporate funds. Such arrangements entered into or settled during the three months ended September 29, 2013 included the following:

Collared Accelerated Share Repurchases

During the three months ended September 29, 2013, the Company entered into a collared accelerated share repurchase ("ASR") transaction under a master repurchase arrangement. Under the ASR, the Company made an up-front cash payment of \$75 million, in exchange for an initial delivery of 1.2 million shares of its Common Stock and a subsequent delivery of 0.3 million shares following the initial hedge period.

The number of shares to ultimately be repurchased by the Company is based generally on the volume-weighted average price ("VWAP") of the Common Stock during the term of the ASR minus a pre-determined discount set at inception of the ASR, subject to collar provisions that provide a minimum and maximum number of shares that the Company could repurchase under the agreements. The minimum and maximum thresholds for the transaction were established based on the average of the VWAP prices for the Common Stock during an initial hedge period. The ASR was scheduled to end at any time after September 27, 2013 and on or before November 27, 2013. At the conclusion of the ASR, the Company may receive additional shares based on the VWAP of the Common Stock during the term of the agreement minus the pre-determined fixed discount, however the total number of shares received under the ASR would not exceed the maximum of 1.7 million shares.

The counterparty designated October 28, 2013 as the termination date, at which time the Company settled the ASR. No additional shares were received at final settlement, which represented a weighted average share price of approximately \$50.40 for the transaction period.

[Table of Contents](#)

The Company accounted for the ASR as two separate transactions: (a) as shares of common stock acquired in a treasury stock transaction recorded on the acquisition date and (b) as a forward contract indexed to the Company's own common stock and classified in stockholders' equity. As such, the Company accounted for the shares that it received under the ASR as a repurchase of its Common Stock for the purpose of calculating earnings per common share. The Company has determined that the forward contract indexed to the Common Stock met all of the applicable criteria for equity classification in accordance with the Derivatives and Hedging topic of the FASB Accounting Standards Codification, and, therefore, the ASR was not accounted for as a derivative instrument. As of September 29, 2013, the aggregate repurchase price of \$75 million was reflected as Treasury stock, at cost, in the Consolidated Balance Sheet.

Share repurchases, including those under the repurchase program, were as follows:

<u>Period</u>	<u>Total Number of Shares Repurchased (1)</u>	<u>Average Price Paid Per Share*</u>	<u>Total Number of Shares Purchased as Part of Publicly Announced Plan or Program</u>	<u>Amount Available Under Repurchase Program</u>
	(in thousands, except per share data)			
Amount available at June 30, 2013				\$ 250,000
July 1, 2013 - July 31, 2013	85	\$ 49.52	—	\$ 250,000
August 1, 2013 - August 31, 2013	476	\$ 48.15	434	\$ 229,129
September 1, 2013 - September 29, 2013	1,532	\$ 48.88	1,501	\$ 153,538
Total	2,093	\$ 48.39	1,935	

* Average price paid per share excludes accelerated share repurchases for which cost was incurred during the September 2013 quarter, but that had not settled as of quarter end and for which final price per share information was not yet known. See *Collared Accelerated Share Repurchases* section above for details regarding average price associated with these transactions.

(1) In addition to shares repurchased under the Board-authorized repurchase program (as described above), included in this column are 159,000 shares acquired at a total cost of \$7.8 million, which the Company withheld through net share settlements to cover minimum tax withholding obligations upon the vesting of restricted stock unit awards granted under the Company's equity compensation plans. The shares retained by the Company through these net share settlements are not a part of the Board-authorized repurchase program but instead are authorized under the Company's equity compensation plans.

ITEM 3. Defaults Upon Senior Securities

None.

ITEM 4. Mine Safety Disclosures

Not applicable.

ITEM 5. Other Information

None.

ITEM 6. Exhibits

See the Exhibit Index following the signature page to this Quarterly Report on Form 10-Q for a list of exhibits filed or furnished with this report, which Exhibit Index is incorporated herein by reference.

LAM RESEARCH CORPORATION

SIGNATURES

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

Date: November 7, 2013

LAM RESEARCH CORPORATION
(Registrant)

/s/ Douglas R. Bettinger

Douglas R. Bettinger
Executive Vice President, Chief Financial Officer
(Principal Financial Officer and Principal Accounting Officer)

EXHIBIT INDEX

<u>Exhibit Number</u>	<u>Description</u>
31.1	Rule 13a-14(a)/15d-14(a) Certification (Principal Executive Officer)
31.2	Rule 13a-14(a)/15d-14(a) Certification (Principal Financial Officer)
32.1	Section 1350 Certification (Principal Executive Officer)
32.2	Section 1350 Certification (Principal Financial Officer)
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

RULE 13a-14(a)/15d-14(a) CERTIFICATION (PRINCIPAL EXECUTIVE OFFICER)

I, Martin B. Anstice, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Lam Research Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

November 7, 2013

/s/ Martin B. Anstice

Martin B. Anstice
President and Chief Executive Officer

RULE 13a-14(a)/15d-14(a) CERTIFICATION (PRINCIPAL FINANCIAL OFFICER)

I, Douglas R. Bettinger, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Lam Research Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

November 7, 2013

/s/ Douglas R. Bettinger
Douglas R. Bettinger
Executive Vice President, Chief Financial Officer
(Principal Financial Officer and Principal Accounting Officer)

SECTION 1350 CERTIFICATION (PRINCIPAL EXECUTIVE OFFICER)

In connection with the Quarterly Report of Lam Research Corporation (the "Company") on Form 10-Q for the fiscal period ending September 29, 2013 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Martin B. Anstice, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to my knowledge, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) , as applicable, of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

November 7, 2013

/s/ Martin B. Anstice

Martin B. Anstice

President and Chief Executive Officer

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, and will not be deemed "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, as amended (the "Exchange Act") or otherwise subject to the liability of that section. Such certification will not be deemed incorporated by reference into any filing under the Securities Act of 1933, as amended, or the Exchange Act, except to the extent that the Company specifically incorporates it by reference.

SECTION 1350 CERTIFICATION (PRINCIPAL FINANCIAL OFFICER)

In connection with the Quarterly Report of Lam Research Corporation (the "Company") on Form 10-Q for the fiscal period ending September 29, 2013 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Douglas R. Bettinger, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to my knowledge, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) , as applicable, of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

November 7, 2013

/s/ Douglas R. Bettinger
Douglas R. Bettinger
Executive Vice President, Chief Financial Officer
(Principal Financial Officer and Principal Accounting Officer)

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, and will not be deemed "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, as amended (the "Exchange Act") or otherwise subject to the liability of that section. Such certification will not be deemed incorporated by reference into any filing under the Securities Act of 1933, as amended, or the Exchange Act, except to the extent that the Company specifically incorporates it by reference.