

LATTICE SEMICONDUCTOR CORP

Form 10-Q

November 04, 2011

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

FOR THE QUARTERLY PERIOD ENDED October 1, 2011

OR

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

FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_

Commission file number 000-18032

LATTICE SEMICONDUCTOR CORPORATION

(Exact name of Registrant as specified in its charter)

State of Delaware

93-0835214

(State or other jurisdiction of incorporation or  
organization)

(I.R.S. Employer Identification No.)

5555 N.E. Moore Court, Hillsboro, Oregon

97124-6421

(Address of principal executive offices)

(Zip Code)

(503) 268-8000

(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

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

Number of shares of common stock outstanding as of November 3, 2011

117,382,731

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Forward-Looking Statements

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Any statements about our expectations, beliefs, plans, objectives, assumptions or future events or performance are not historical facts and may be forward-looking. We use words or phrases such as “anticipates,” “believes,” “could,” “estimates,” “expects,” “intends,” “plans,” “predicts,” “projects,” “may,” “will,” “should,” “continue,” “ongoing,” “future,” “potential” and phrases to identify forward-looking statements. Examples of forward-looking statements include, but are not limited to, statements about: programmable logic products being expected to simplify board management design and reduce development costs; customers using both PLD and FPGA architectures; our plan to introduce new FPGA, PLD and associated software design tool products; our existing facilities being suitable and adequate for our future needs; the majority of our revenue being through our sell-through distributors; changes to our unrecognized tax benefits and expectations regarding taxes and tax adjustments; our expectations that a significant portion of our revenue will continue to be dependent on the communications end market and the growth of our revenue from this end market; the Asia Pacific market being the primary source of our revenue; our ability to continue to serve our customers after the termination of our relationship with Avnet; the benefits of our purchase of APAC IC; our plans to sell our auction rate securities; the costs and benefits of our restructuring plans; the impact of new accounting pronouncements; our making significant future investments in research and development; and our beliefs concerning the adequacy of our liquidity and ability to meet our operating and capital requirements and obligations.

Forward-looking statements involve estimates, assumptions, risks and uncertainties that could cause actual results to differ materially from those expressed in the forward-looking statements. The key factors that could cause our actual results to differ materially from the forward-looking statements include global economic conditions and uncertainty, the concentration and growth of our sales in the communications equipment end market, particularly as it relates to the concentration of our sales in the Asia Pacific region, market acceptance and demand for our new products, any disruption of our distribution channels, unexpected charges relating to our restructuring plans, the effect of the downturn in the economy on capital markets and credit markets, the impact of competitive products and pricing, unanticipated taxation requirements, or positions of the IRS, unexpected impacts of recent accounting guidance and the other risks that are described herein and that are otherwise described from time to time in our filings with the Securities and Exchange Commission, including, but not limited to, the items discussed in “Risk Factors” in Item 1A of Part II of this Report. You should not unduly rely on forward-looking statements because our actual results could differ materially from those expressed in any forward-looking statements made by us. In addition, any forward-looking statement applies only as of the date on which it is made. We do not plan to, and undertake no obligation to, update any forward-looking statements to reflect events or circumstances that occur after the date on which such statements are made or to reflect the occurrence of unanticipated events.

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## PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

LATTICE SEMICONDUCTOR CORPORATION  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

(unaudited)

|  | Three Months Ended |                    | Nine Months Ended  |                    |
|--|--------------------|--------------------|--------------------|--------------------|
|  | October 1,<br>2011 | October 2,<br>2010 | October 1,<br>2011 | October 2,<br>2010 |
| Revenue  | \$81,720           | \$77,137           | \$248,196          | \$224,688          |
| Costs and expenses:                                |                    |                    |                    |                    |
| Cost of products sold                              | 33,866             | 31,551             | 100,062            | 90,704             |
| Research and development                           | 16,999             | 14,814             | 55,770             | 44,654             |
| Selling, general and administrative                | 16,809             | 15,818             | 51,717             | 47,621             |
| Restructuring charges                              | 1,760              | 79                 | 4,982              | 41                 |
|  | 69,434             | 62,262             | 212,531            | 183,020            |
| Income from operations                             | 12,286             | 14,875             | 35,665             | 41,668             |
| Other income, net                                  | 248                | 669                | 1,179              | 1,916              |
| Income before (benefit) provision for income taxes | 12,534             | 15,544             | 36,844             | 43,584             |
| (Benefit) provision for income taxes               | (803 )             | 176                | (443 )             | 391                |
| Net income   | \$13,337           | \$15,368           | \$37,287           | \$43,193           |
| Net income per share:                              |                    |                    |                    |                    |
| Basic  | \$0.11             | \$0.13             | \$0.32             | \$0.37             |
| Diluted  | \$0.11             | \$0.13             | \$0.31             | \$0.36             |
| Shares used in per share calculations:             |                    |                    |                    |                    |
| Basic  | 117,926            | 117,257            | 117,990            | 116,332            |
| Diluted  | 120,627            | 121,052            | 121,343            | 119,624            |

See Accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

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CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except share and par value data)

(unaudited)

|  | October 1,<br>2011 | January 1,<br>2011 |
|--|--------------------|--------------------|
| Assets   |                    |                    |
| Current assets:  |                    |                    |
| Cash and cash equivalents  | \$204,920          | \$174,384          |
| Short-term marketable securities   | 62,316             | 63,836             |
| Accounts receivable, net   | 53,482             | 41,188             |
| Inventories  | 35,121             | 37,333             |
| Prepaid expenses and other current assets  | 10,659             | 8,648              |
| Total current assets   | 366,498            | 325,389            |
| Property and equipment, less accumulated depreciation  | 38,735             | 39,322             |
| Long-term marketable securities  | 7,389              | 10,232             |
| Other long-term assets   | 11,790             | 2,744              |
| Goodwill   | 897                | —                  |
| Total assets   | \$425,309          | \$377,687          |
| Liabilities and Stockholders' Equity   |                    |                    |
| Current liabilities:   |                    |                    |
| Accounts payable and accrued expenses  | \$35,498           | \$26,994           |
| Accrued payroll obligations  | 10,265             | 11,654             |
| Deferred income and allowances on sales to sell-through distributors   | 19,081             | 15,692             |
| Total current liabilities  | 64,844             | 54,340             |
| Long-term liabilities  | 8,492              | 4,625              |
| Total liabilities  | 73,336             | 58,965             |
| Commitments and contingencies  |                    |                    |
| Stockholders' equity:  |                    |                    |
| Preferred stock, \$.01 par value, 10,000,000 shares authorized, none issued and outstanding  | —                  | —                  |
| Common stock, \$.01 par value, 300,000,000 shares authorized, 117,542,000 and 117,971,000 shares issued and outstanding, excluding 371,000 shares of treasury stock 1,175 at January 1, 2011 |                    | 1,179              |
| Paid-in capital  | 626,354            | 630,184            |
| Accumulated other comprehensive income   | 297                | 499                |
| Accumulated deficit  | (275,853           | ) (313,140         |
| Total stockholders' equity   | 351,973            | 318,722            |
| Total liabilities and stockholders' equity   | \$425,309          | \$377,687          |
| See Accompanying Notes to Unaudited Condensed Consolidated Financial Statements.   |                    |                    |

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CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(unaudited)

|  | Nine Months Ended  |                    |
|--|--------------------|--------------------|
|  | October 1,<br>2011 | October 2,<br>2010 |
| Cash flows from operating activities:  |                    |                    |
| Net income   | \$37,287           | \$43,193           |
| Adjustments to reconcile net income to net cash provided by operating activities:                                |                    |                    |
| Depreciation and amortization  | 12,598             | 10,642             |
| Gain on sale or maturity of marketable securities, net   | (385 )             | (416 )             |
| Gain on sale of land   | —                  | (720 )             |
| Stock-based compensation   | 4,768              | 3,505              |
| Changes in assets and liabilities:   |                    |                    |
| Accounts receivable, net   | (12,294 )          | (15,666 )          |
| Inventories  | 2,212              | (5,756 )           |
| Prepaid expenses and other assets  | (14,659 )          | (3,525 )           |
| Foundry advances (includes advance credits)  | —                  | 11,446             |
| Accounts payable and accrued expenses (includes restructuring)   | 8,056              | 6,488              |
| Accrued payroll obligations  | (1,389 )           | 6,743              |
| Deferred income and allowances on sales to sell-through distributors   | 3,389              | 8,017              |
| Other liabilities  | 4,536              | 337                |
| Net cash provided by operating activities  | 44,119             | 64,288             |
| Cash flows from investing activities:  |                    |                    |
| Proceeds from sales or maturities of marketable securities   | 74,312             | 40,813             |
| Purchase of marketable securities  | (69,706 )          | (91,150 )          |
| Proceeds from sale of excess real estate   | —                  | 874                |
| Capital expenditures   | (8,690 )           | (8,531 )           |
| Acquisition of business - Goodwill   | (897 )             | —                  |
| Net cash used in investing activities  | (4,981 )           | (57,994 )          |
| Cash flows from financing activities:  |                    |                    |
| Net share settlement upon issuance of RSUs   | (597 )             | (655 )             |
| Purchase of treasury stock   | (12,789 )          | —                  |
| Net proceeds from issuance of common stock   | 4,784              | 4,926              |
| Net cash (used in) provided by financing activities  | (8,602 )           | 4,271              |
| Net increase in cash and cash equivalents  | 30,536             | 10,565             |
| Beginning cash and cash equivalents  | 174,384            | 156,069            |
| Ending cash and cash equivalents   | \$204,920          | \$166,634          |
| Supplemental disclosures of non-cash investing and financing activities:   |                    |                    |
| Unrealized (loss) gain on assets measured at fair value, net, included in Accumulated other comprehensive income | \$(8 )             | \$4                |
| Distribution of deferred compensation from trust assets  | \$277              | \$227              |
| Retirement of treasury stock   | \$(12,789 )        | \$(326 )           |
| See Accompanying Notes to Unaudited Condensed Consolidated Financial Statements.                                 |                    |                    |



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LATTICE SEMICONDUCTOR CORPORATION  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)

Note 1 - Basis of Presentation and Significant Accounting Policies:

The accompanying Condensed Consolidated Financial Statements are unaudited and have been prepared by Lattice Semiconductor Corporation (“Lattice”, the “Company”, “we”, “us” or “our”) pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) and in our opinion include all adjustments, consisting of normal recurring adjustments, necessary for the fair statement of results for the interim periods. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. These Condensed Consolidated Financial Statements should be read in conjunction with our audited financial statements and notes thereto included in our Annual Report on Form 10-K for the fiscal year ended January 1, 2011.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts and classification of assets, such as marketable securities, accounts receivable, inventory, auction rate securities, goodwill, deferred income taxes and liabilities, accrued expenses (including restructuring charges and accrual for bonus arrangements), income taxes, deferred income and allowances on sales to certain sell-through distributors, forward exchange contracts, and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the fiscal periods presented. Actual results could differ from these estimates.

We report based on a 52 or 53-week fiscal year ending on the Saturday closest to December 31. Our third quarter of fiscal 2011 and third quarter of fiscal 2010 ended on October 1, 2011 and October 2, 2010, respectively. All references to quarterly or three and nine months ended financial results are references to the results for the relevant fiscal period.

Cash Equivalents and Marketable Securities

We consider all investments that are readily convertible into cash and have original maturities of three months or less, to be cash equivalents. Cash equivalents consist primarily of highly liquid investments in time deposits or money market accounts and are carried at cost. We account for marketable securities as available for sale with unrealized gains or losses recorded as Accumulated other comprehensive income, unless losses are considered other-than-temporary, in which case, losses are charged to the Condensed Consolidated Statements of Operations.

Derivative Financial Instruments

We have international subsidiary and branch operations. A portion of our silicon wafer and other purchases are denominated in Japanese yen and we bill our Japanese customers in yen. We mitigate the resulting foreign currency exchange rate exposure by entering into foreign currency forward exchange contracts for Japanese yen. Although such hedges mitigate our foreign currency exchange rate exposure from an economic perspective they were not designated as “effective” hedges for accounting purposes and are adjusted to fair value through Net income. We do not hold or issue derivative financial instruments for trading or speculative purposes.

Concentration Risk

Potential exposure to concentration risk consists primarily of cash and cash equivalents, marketable securities, trade receivables and supply of wafers for our new products. We place our investments primarily through four financial



institutions and mitigate the concentration of credit risk by placing percentage limits on the maximum portion of the investment portfolio which may be invested in any one investment instrument. The Company's investment policy defines approved credit ratings for investment securities. Investments consisted primarily of money market instruments, "AA" or better corporate notes and bonds, "A-1" or better for commercial paper, "AA" or better rated U.S. municipal notes, and U.S. government agency obligations. See Note 5 for a discussion of the liquidity attributes of our marketable securities.

Concentration of credit risk with respect to trade receivables is mitigated by a diverse customer base and our credit and collection process. Accounts receivable are recorded at the invoice amount, do not bear interest, and are shown net of allowances for doubtful accounts of \$0.9 million at both October 1, 2011 and January 1, 2011. We perform credit evaluations for essentially all customers and secure transactions with letters of credit or advance payments where appropriate. We regularly review our allowance for doubtful accounts and the aging of our accounts receivable. Write-offs for uncollected trade

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receivables have not been significant to date.

We rely on Fujitsu Limited (“Fujitsu”) for essentially all wafer purchases for our new products.

## Revenue Recognition and Deferred Income

Revenue from sales to customers is recognized upon shipment, or in the case of sales by our sell-through distributors, at the time of reported resale, provided that persuasive evidence of an arrangement exists, the price is fixed or determinable, title has transferred, collection of resulting receivables is reasonably assured, there are no remaining customer acceptance requirements and no remaining significant obligations. We sell our products directly to end customers or through a network of independent manufacturers' representatives and indirectly through a network of independent sell-in and sell-through distributors. Distributors provide us periodic data regarding the product, price, quantity and end customer when products are resold as well as the quantities of our products they still have in stock. We must use estimates and apply judgment to reconcile sell-through distributors' reported inventories to their activities. Any differences between our estimates and actual results could lead to inaccurate reporting of our Revenue, Cost of products sold, Deferred income and allowances on sales to sell-through distributors, and Net income.

Revenue and cost of products sold to sell-through distributors are deferred until either the product is resold by the distributor or, in certain cases, return privileges terminate, at which time Revenue and Cost of products sold are reflected in Net income. Amounts invoiced are recorded in Accounts receivable, net and inventory is transferred from Inventories to Deferred income and allowances on sales to sell-through distributors. Backlog and shipments to sell-through distributors are valued at list price, which is significantly higher than the amount recognized as revenue when resale occurs.

The components of Deferred income and allowances on sales to sell-through distributors are presented in the following table (in thousands):

|   | October 1,<br>2011 | January 1,<br>2011 |
|---|--------------------|--------------------|
| Inventory valued at published list price and held by sell-through distributors with right of return | \$48,169           | \$50,085           |
| Allowance for distributor advances  | (21,660 )          | (26,830 )          |
| Deferred cost of sales related to inventory held by sell-through distributors                       | (7,428 )           | (7,563 )           |
| Total deferred income and allowances on sales to sell-through distributors                          | \$19,081           | \$15,692           |

We expect the majority of our revenue in fiscal 2011 will be from reported resale from our sell-through distributors. Resale of product by sell-through distributors as a percentage of our total revenue was 61% and 60% for the three and nine months ended October 1, 2011, respectively, and 55% and 56% for the three and nine months ended October 2, 2010, respectively.

Revenue from software licensing was not material for the periods presented.

## Note 2 - New Accounting Pronouncements

In June 2011, the Financial Accounting Standards Board (“FASB”) issued changes to the presentation of comprehensive income. These changes give an entity the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements; the option to present components of other comprehensive income as part of the statement of changes in stockholders' equity was eliminated. The items that must be reported in

other comprehensive income or when an item of other comprehensive income must be reclassified to net income were not changed. Additionally, no changes were made to the calculation and presentation of earnings per share. These changes become effective for the Company on January 1, 2012. We are currently evaluating these changes to determine which option will be chosen for the presentation of comprehensive income.

In May 2011, the FASB issued amended guidance on fair value measurement and related disclosures. The new guidance clarified the concepts applicable for fair value measurement of non-financial assets and requires the disclosure of quantitative information about the unobservable inputs used in a fair value measurement. This guidance will be effective for reporting periods beginning after December 15, 2011, and will be applied prospectively. We are in the process of evaluating the financial

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and disclosure impact of this guidance. We do not anticipate a material impact on our Consolidated Financial Statements as a result of the adoption of this amended guidance.

In September 2011, the FASB issued amended guidance on testing goodwill for impairment. The new guidance provides an entity the option to first perform a qualitative assessment to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If an entity determines that this is the case, it is required to perform the currently prescribed two-step goodwill impairment test to identify potential goodwill impairment and measure the amount of goodwill impairment loss to be recognized for that reporting unit (if any). If an entity determines that the fair value of a reporting unit is more than its carrying amount, the two-step goodwill impairment test is not required. This guidance will be effective for reporting periods beginning after December 15, 2011. We are in the process of evaluating the financial and disclosure impact of this guidance. We do not anticipate a material impact on our Consolidated Financial Statements as a result of the adoption of this amended guidance.

## Note 3 - Net Income Per Share:

Net income per share is computed based on the weighted average number of shares of common stock and potentially dilutive securities assumed to be outstanding during the period using the treasury stock method. Potentially dilutive securities consist of stock options, restricted stock units ("RSUs") and employee stock purchase plan ("ESPP") shares.

A reconciliation of basic and diluted Net income per share is presented below (in thousands, except per share data):

|  | Three Months Ended |                    | Nine Months Ended  |                 |
|--|--------------------|--------------------|--------------------|-----------------|
|  | October 1,<br>2011 | October 2,<br>2010 | October 1,<br>2011 | October 2, 2010 |
| Net income   | \$13,337           | \$15,368           | \$37,287           | \$43,193        |
| Shares used in basic Net income per share              | 117,926            | 117,257            | 117,990            | 116,332         |
| Dilutive effect of stock options, RSUs and ESPP shares | 2,701              | 3,795              | 3,353              | 3,292           |
| Shares used in diluted Net income per share            | 120,627            | 121,052            | 121,343            | 119,624         |
| Basic Net income per share                             | \$0.11             | \$0.13             | \$0.32             | \$0.37          |
| Diluted Net income per share                           | \$0.11             | \$0.13             | \$0.31             | \$0.36          |

The computation of Diluted Net income per share for the three and nine months ended October 1, 2011, excludes the effects of stock options, RSUs and ESPP shares aggregating 4.4 million and 3.9 million shares, respectively, as they are antidilutive. The computation of diluted net income per share for the three and nine months ended October 2, 2010, excludes the effects of stock options, RSUs and ESPP shares aggregating 2.0 million and 3.1 million shares, respectively, as they are antidilutive. Stock options, RSUs and ESPP shares are considered antidilutive when the aggregate of exercise price, unrecognized stock-based compensation expense and excess tax benefit are greater than the average market price for our common stock during the period or when the Company is in a net loss position. Stock options and RSUs that are antidilutive in the third quarter of fiscal 2011 could become dilutive in the future.

## Note 4 - Marketable Securities:

The following table summarizes the contractual maturities of our marketable securities (at fair value and in thousands):

|                                    | October 1,<br>2011 | January 1,<br>2011 |
|------------------------------------|--------------------|--------------------|
| Short-term marketable securities:  |                    |                    |
| Maturities of less than five years | \$62,316           | \$63,836           |

|                                   |          |          |
|-----------------------------------|----------|----------|
| Long-term marketable securities:  |          |          |
| Maturities of more than ten years | 7,389    | 10,232   |
| Total marketable securities       | \$69,705 | \$74,068 |

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The following table summarizes the composition of our marketable securities (at fair value and in thousands):

|   | October 1,<br>2011 | January 1,<br>2011 |
|---|--------------------|--------------------|
| Short-term marketable securities:                             |                    |                    |
| Corporate and government bonds and notes and commercial paper | \$62,316           | \$63,836           |
| Long-term marketable securities:                              |                    |                    |
| Federally-insured or FFELP guaranteed student loans           | 7,389              | 10,232             |
| Total marketable securities                                   | \$69,705           | \$74,068           |

The following table summarizes the composition of our auction rate securities (in thousands):

|  | October 1, 2011 |            |                         | January 1, 2011 |            |                         |
|--|-----------------|------------|-------------------------|-----------------|------------|-------------------------|
|  | Par Value       | Fair Value | S&P<br>Credit<br>rating | Par Value       | Fair Value | S&P<br>Credit<br>rating |
| Long-term marketable securities:                       |                 |            |                         |                 |            |                         |
| Federally-insured or FFELP<br>guaranteed student loans | \$8,300         | \$7,389    | AAA                     | \$11,600        | \$10,232   | AAA                     |
| Total auction rate securities                          | \$8,300         | \$7,389    |                         | \$11,600        | \$10,232   |                         |

On March 29, 2011, the Company sold student loan auction rate securities, with a par value of \$3.3 million and an estimated fair value of \$2.8 million, for \$3.3 million, reported a gain of \$0.6 million and relieved \$0.1 million of previously unrecognized gain in Accumulated other comprehensive income, in the first quarter of fiscal 2011. At October 1, 2011, due to continued multiple failed auctions and a determination of illiquidity, the auction rate securities held by the Company are classified as Long-term marketable securities. These auction rate securities are exposed to risks associated with student loan asset-backed notes. Such loans are insured by the federal government or guaranteed by the Federal Family Educational Loan Program ("FFELP"). The Company intends to sell its auction rate securities as markets for these securities resume or reasonable offers become available.

Note 5 - Fair Value of Financial Instruments (in thousands):

|  | Fair value measurements as of October<br>1, 2011 |          |         |         | Fair value measurements as of January<br>1, 2011 |          |         |          |
|--|--|----------|---------|---------|--|----------|---------|----------|
|  | Total  | Level 1  | Level 2 | Level 3 | Total  | Level 1  | Level 2 | Level 3  |
| Short-term marketable securities               | \$62,316   | \$62,316 | \$—     | \$—     | \$63,836   | \$63,836 | \$—     | \$—      |
| Long-term marketable securities                | 7,389  | —        | —       | 7,389   | 10,232   | —        | —       | 10,232   |
| Foreign currency forward<br>exchange contracts | 9  | —        | 9       | —       | —  | —        | —       | —        |
| Total fair value of financial<br>instruments   | \$69,714   | \$62,316 | \$9     | \$7,389 | \$74,068   | \$63,836 | \$—     | \$10,232 |

We invest in various financial instruments including corporate and government bonds and notes, commercial paper and auction rate securities. In addition, we enter into foreign currency forward exchange contracts to mitigate our foreign currency exchange rate exposure. The Company carries these instruments at their fair value in accordance with Financial Accounting Standards Board Accounting Standards Codification ("ASC") 820, "Fair Value Measurements and Disclosures" ("ASC 820"). The framework under the provisions of ASC 820 establishes three levels of inputs that may be used to measure fair value. Each level of input has different levels of subjectivity and difficulty involved in determining fair value.

Level 1 instruments generally represent quoted prices in active markets. Therefore, determining fair value for Level 1 instruments generally does not require significant management judgment, and the estimation is not difficult. Our Level 1 instruments consist of federal agency, municipal or corporate notes and bonds that are traded in active markets and are classified as Short-term marketable securities on our Condensed Consolidated Balance Sheet.

Level 2 instruments include inputs other than Level 1 that are observable, either directly or indirectly, such as quoted

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prices for similar assets or liabilities; quoted prices for identical instruments in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Our Level 2 instruments include foreign currency forward exchange contracts.

Level 3 instruments include unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Our auction rate securities are classified as Level 3 instruments. Management uses a combination of the market and the income approach to derive the fair value of auction rate securities, which includes third party valuation results, investment broker provided market information and available information on the credit quality of the underlying collateral. As a result, the determination of fair value for Level 3 instruments requires significant management judgment and subjectivity. Our Level 3 instruments are classified as Long-term marketable securities on our Condensed Consolidated Balance Sheet.

During the nine months ended October 1, 2011 and October 2, 2010, the following changes occurred in our Level 3 instruments (in thousands):

|   | Nine Months Ended  |                    |
|---|--------------------|--------------------|
|   | October 1,<br>2011 | October 2,<br>2010 |
| Beginning fair value of Long-term marketable securities | \$10,232           | \$12,939           |
| Fair value of securities sold or redeemed               | (2,843             | ) (3,220           |
| Ending fair value of Long-term marketable securities    | \$7,389            | \$9,719            |

In accordance with ASC 320, "Investments-Debt and Equity Securities," the Company recorded an unrealized loss of less than \$0.1 million during the nine months ended October 1, 2011 on certain Short-term marketable securities (Level 1 instruments), which has been recorded in Accumulated other comprehensive income. Future fluctuations in fair value related to these instruments that the Company deems to be temporary, including any recoveries of previous write-downs, would be recorded to Accumulated other comprehensive income. In addition, during the nine months ended October 1, 2011, the Company realized a gain of \$0.6 million related to the sale of a portion of its Long-term marketable securities portfolio. If the Company were to determine in the future that any further decline in fair value is other-than-temporary, we would record an impairment charge, which could have a materially detrimental impact on our operating results. If we were to liquidate our position in these securities, it is likely that the amount of any future realized gain or loss would be different from the unrealized gain or loss reported in Accumulated other comprehensive income or the previously reported other-than-temporary impairment charge.

Note 6 - Inventories (in thousands):

|                   | October 1,<br>2011 | January 1,<br>2011 |
|-------------------|--------------------|--------------------|
| Work in progress  | \$24,721           | \$25,516           |
| Finished goods    | 10,400             | 11,817             |
| Total inventories | \$35,121           | \$37,333           |



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## Note 7 - Goodwill:

Goodwill is recorded when consideration paid under an acquisition accounted for as a business combination exceeds the fair value of the net tangible and intangible assets acquired. We do not amortize goodwill, but instead test for impairment annually or more frequently if certain triggering events or changes in circumstances indicate that the carrying value may not be recoverable.

As of October 1, 2011, Goodwill was \$0.9 million, all of which resulted from the acquisition of substantially all of the assets of Rise Technology Development Limited ("Rise"), a Hong Kong company, and its subsidiary, APAC IC Layout Consultants, Inc. ("APAC IC"), a Manila, Philippines based company engaged in engineering layout and design services. The acquisition of Rise and APAC IC, which was completed on July 15, 2011, is part of the Company's effort to improve its research and development and operations activities, reduce costs and streamline its supply chain for improved predictability and flexibility. The Company allocated the purchase price of the acquisition in accordance with the guidance of ASC 820, "Business Combinations", which resulted in recording the majority of the purchase price to Goodwill. The Company has not disclosed the purchase price allocation or proforma information as the acquisition was immaterial to the Condensed Consolidated Financial Statements.

## Note 8 - Changes in Stockholders' Equity and Comprehensive Income (in thousands):

|   | Common<br>stock | Paid-in<br>capital | Treasury<br>stock | Accumu-<br>lated<br>deficit | Accumu-<br>lated<br>other<br>compre-<br>hensive<br>income | Total     |
|---|-----------------|--------------------|-------------------|-----------------------------|---|-----------|
| Balances, January 1, 2011   | \$ 1,179        | \$630,184          | \$—               | \$(313,140)                 | \$499   | \$318,722 |
| Net income for the nine months<br>ended October 1, 2011   | —               | —                  | —                 | 37,287                      | —   | 37,287    |
| Unrealized loss, net, related to<br>marketable securities   | —               | —                  | —                 | —                           | (8 )  | (8 )      |
| Recognized gain on redemption of<br>marketable securities, previously<br>unrealized                             | —               | —                  | —                 | —                           | (133 )  | (133 )    |
| Translation adjustments   | —               | —                  | —                 | —                           | (61 )   | (61 )     |
| Comprehensive income  | —               | —                  | —                 | —                           | —   | 37,085    |
| Common stock issued in connection<br>with the exercise of stock options,<br>ESPP and vested RSUs (net of taxes) | 18              | 4,169              | —                 | —                           | —   | 4,187     |
| Stock repurchase  | —               | —                  | (12,789 )         | —                           | —   | (12,789 ) |
| Retirement of treasury stock  | (22 )           | (12,767 )          | 12,789            | —                           | —   | —         |
| Stock-based compensation expense<br>related to stock options, ESPP and<br>RSUs                                  | —               | 4,768              | —                 | —                           | —   | 4,768     |
| Balances, October 1, 2011   | \$ 1,175        | \$626,354          | \$—               | \$(275,853)                 | \$297   | \$351,973 |

On October 21, 2010, the Company's Board of Directors approved a stock repurchase program pursuant to which up to \$20.0 million of outstanding common stock may be repurchased from time to time. The duration of the repurchase program is twelve months. In connection with this stock repurchase program, the Company entered into a 10b5-1 plan. During the three and nine months ended October 1, 2011 approximately 850,800 and 2,150,800 shares were

repurchased for \$4.8 million and \$12.8 million, respectively. During fiscal 2010, approximately 371,000 shares were repurchased for \$2.0 million. All shares repurchased under this program were retired by October 1, 2011. All repurchases have and will be open market transactions and funded from available working capital. The number of shares that will be repurchased in the future will depend on market conditions, including the price of the common stock. The program ended by its terms October 26, 2011.

Note 9 - Income Taxes:

We are subject to federal income tax as well as income tax of multiple state and foreign jurisdictions. We are no longer subject to federal, state and local, or foreign income tax examinations for years before 2008, 2002 and 2005, respectively. We have federal net operating loss carryforwards that expire at various dates between 2023 and 2029. We have state net operating

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loss carryforwards that expire at various dates from 2011 through 2030. We also have federal and state credit carryforwards, some of which do not expire, with the remainder expiring at various dates from 2011 through 2031. We have provided a valuation allowance equal to our net federal and state deferred tax assets as we have not met the more-likely-than-not realization threshold for deferred tax asset recognition. We evaluate both positive and negative evidence to determine if some or all of our deferred tax assets should be recognized on a quarterly basis. In future periods, if we determine that we are more-likely-than-not to realize some or all of our deferred tax assets, we will recognize a deferred tax asset and a benefit in the period in which such determination is made. As of October 1, 2011, the net deferred tax asset relates to foreign jurisdictions where we have concluded it is more-likely-than-not that we will realize the net deferred tax assets in future periods.

The Internal Revenue Service (“IRS”) examined our income tax returns for 2001 and 2002, and issued proposed adjustments of \$1.4 million, plus interest. These adjustments relate to the treatment of acquisition costs and a tax accounting method change for prepaid expenses. We reached an agreement regarding the acquisition costs during the three months ended March 29, 2008. We made a payment of \$0.3 million related to this settlement agreement. On May 23, 2008, the Company filed a petition with the Tax Court seeking a redetermination of the prepaid expense adjustment. On May 9, 2011 the United States Tax Court ruled that the IRS did not err in denying the Company's request to change its accounting method with respect to prepaid expenses and held that the Company was not allowed a deduction for prepaid expenses on its 2002 tax return. During the quarter ended October 1, 2011, the Company decided not to pursue further litigation with regard to the prepaid expense adjustment and settled with the IRS. As a result, the Company paid \$1.0 million in October 2011 related to disallowed prepaid expense deductions and the corresponding carry back of those deductions to the 1999 and 2000 tax returns through a net operating loss carry back. The amount paid was fully reserved. A benefit of approximately \$0.9 million has been recognized in the three months and nine months ended October 1, 2011 for the reversal of uncertain tax positions and related interest for the years effectively settled.

We are not currently under examination in any tax jurisdictions.

We believe that it is reasonably possible that \$0.4 million of unrecognized tax benefits and \$0.1 million of associated interest and penalties could significantly change during the next twelve months. The \$0.5 million potential change would represent a decrease in unrecognized tax benefits, comprised of items related to federal research and development credits and uncertain income tax positions related to foreign tax filings for years that will no longer be subject to examination under expiring statutes of limitations.

We are paying foreign income taxes, which are reflected in the (Benefit) provision for income taxes in our Condensed Consolidated Statements of Operations and are primarily related to the cost of operating an offshore research and development subsidiary and sales subsidiaries. We are not currently paying federal income taxes and do not expect to pay such taxes until the benefits of our tax net operating losses are fully utilized. We expect to pay a nominal amount of state income tax. We accrue interest and penalties related to uncertain tax positions in the (Benefit) provision for income taxes.

Note 10 - Restructuring:

During 2011, the Company's Board of Directors adopted a restructuring plan to more efficiently implement the Company's product development strategy and to better align the Company's corporate strategy with the Company's sales resources (the “2011 restructuring plan”). In connection with the 2011 restructuring plan, the Company will reduce and refocus its headcount at certain of its research and development facilities, including Pennsylvania and Shanghai, China, and streamline its supply chain activities at its headquarters for reduced operational costs, improved predictability and flexibility. Part of the 2011 restructuring plan includes extending silicon development capabilities, planning and logistics activities by locating personnel in Manila, Philippines. The 2011 restructuring plan will be

substantially implemented during 2011, with a total projected restructuring charge of approximately \$7.6 million through the first quarter of fiscal 2012, of which \$5.8 million was recorded in the first nine months of fiscal 2011.

During fiscal 2009, we initiated a restructuring plan ("2009 restructuring plan") to lower operating expenses primarily by reducing headcount, reducing occupancy in certain leased facilities and to transfer inventory management, order fulfillment, and direct sales logistics from our headquarters in Oregon to a third party contractor in Singapore. In addition, the Company established an operations center in Singapore to transfer some of its supply chain activities from the Company's headquarters in Oregon. As part of the 2011 restructuring plan, we updated our estimate of the remaining severance and lease loss reserve for the 2009 restructuring plan. This resulted in a credit to Restructuring charges in the first quarter of fiscal 2011 of \$0.8 million, primarily for re-occupying certain leased facilities.

At October 1, 2011, our Condensed Consolidated Balance Sheet included an accrual of \$1.9 million related to severance and related expenses under the provisions of the 2011 restructuring plan. In addition, our Condensed Consolidated Balance

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Sheet included an accrual of \$0.1 million related to operating lease commitments under the provisions of the restructuring plan we initiated in 2005.

The following table displays the activity related to all restructuring plans described above (in thousands):

|                             | Balance at<br>January 1,<br>2011 | Charged to<br>expense<br>during nine<br>months ended<br>October 1,<br>2011 | Paid or<br>settled | Adjustments<br>to reserve | Balance at<br>October 1,<br>2011 |
|-----------------------------|----------------------------------|--|--------------------|---------------------------|----------------------------------|
| Severance and related costs | \$175                            | \$5,497  | \$(3,279)          | ) \$(444)                 | ) \$1,949                        |
| Lease loss reserve          | 1,014                            | 6  | (170)              | ) (743)                   | ) 107                            |
| Other                       | 13                               | 691  | (679)              | ) (25)                    | ) —                              |
| Total restructuring plans   | \$1,202                          | \$6,194  | \$(4,128)          | ) \$(1,212)               | ) \$2,056                        |

Total Restructuring charges included in our Condensed Consolidated Statements of Operations were as follows (in thousands):

|                             | Three Months Ended |                    | Nine Months Ended  |                    |
|-----------------------------|--------------------|--------------------|--------------------|--------------------|
|                             | October 1,<br>2011 | October 2,<br>2010 | October 1,<br>2011 | October 2,<br>2010 |
| Severance and related costs | \$1,563            | \$67               | \$5,053            | \$3                |
| Lease loss reserve          | (109)              | ) 12               | (737)              | ) 38               |
| Other                       | 306                | —                  | 666                | —                  |
| Total restructuring charges | \$1,760            | \$79               | \$4,982            | \$41               |

We cannot be certain as to the actual amount of any remaining restructuring charges, changes in original estimates or the timing of their recognition for financial reporting purposes.

## Note 11 - Stock-Based Compensation:

Total stock-based compensation expense included in our Condensed Consolidated Statements of Operations was as follows (in thousands):

| Line item:                          | Three Months Ended |                    | Nine Months Ended  |                    |
|-------------------------------------|--------------------|--------------------|--------------------|--------------------|
|                                     | October 1,<br>2011 | October 2,<br>2010 | October 1,<br>2011 | October 2,<br>2010 |
| Cost of products sold               | \$128              | \$76               | \$341              | \$235              |
| Research and development            | 689                | 468                | 2,039              | 1,388              |
| Selling, general and administrative | 870                | 489                | 2,285              | 1,882              |
| Restructuring charges               | —                  | —                  | 103                | —                  |
| Total stock-based compensation      | \$1,687            | \$1,033            | \$4,768            | \$3,505            |

## Note 12 - Legal Matters:

On June 11, 2007, a patent infringement lawsuit was filed by Lizy K. John (“John”) against Lattice Semiconductor Corporation in the U.S. District Court for the Eastern District of Texas, Marshall Division. John seeks an injunction, unspecified damages, and attorneys' fees and expenses. The Company filed a request for re-examination of the patent by the United States Patent and Trademark Office (“PTO”), which was granted by the PTO, and the re-examination has

concluded. The litigation was stayed pending the results of the re-examination. At this stage of the proceedings, we do not have an estimate of the likelihood or the amount of any potential exposure to us. The Company believes it possesses defenses to these claims and intends to vigorously defend this litigation.

On July 20, 2010, Intellitech Corporation (“Intellitech”) filed a patent infringement lawsuit against the Company, Altera Corporation and Xilinx, Inc. in the U.S. District Court for the District of Delaware, seeking unspecified damages. On August

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27, 2011 the Company and Intellitech entered into an agreement to resolve this litigation.

On December 8, 2010, Intellectual Ventures I LLC and Intellectual Ventures II LLC ("Intellectual Ventures") filed a patent infringement lawsuit against the Company, Altera Corporation and Microsemi Corporation in the U.S. District Court for the District of Delaware, seeking unspecified damages. At this stage of the proceedings, we do not have an estimate of the likelihood or the amount of any potential exposure to us. The Company believes it possess defenses to these claims and intends to vigorously defend this litigation.

On September 16, 2011, Commonwealth Research Group, LLC ("Commonwealth") filed a patent infringement against the Company and nineteen other semiconductor companies in the U.S. District Court for the district of Delaware, seeking unspecified damages. At this stage of the proceedings, we do not have an estimate of the likelihood or the amount of any potential exposure to us. The Company believes it possess defenses to these claims and intends to vigorously defend this litigation.

We are also exposed to certain other asserted and unasserted potential claims. There can be no assurance that, with respect to potential claims made against us, we could resolve such claims under terms and conditions that would not have a material adverse effect on our business, our liquidity or our financial results.

## Note 13 - Segment and Geographic Information:

We operate in one industry segment comprising the design, development, manufacture and marketing of high performance programmable logic devices. Our revenue by major geographic area based on ship-to location was as follows (dollars in thousands):

|   | Three Months Ended |                 |   | Nine Months Ended |                 |   |           |     |   |           |     |   |
|---|--------------------|-----------------|---|-------------------|-----------------|---|-----------|-----|---|-----------|-----|---|
|   | October 1, 2011    | October 2, 2010 |   | October 1, 2011   | October 2, 2010 |   |           |     |   |           |     |   |
| United States:                            | \$11,038           | 14              | % | \$8,884           | 12              | % | \$34,255  | 14  | % | \$26,772  | 12  | % |
| Export revenue:                           |                    |                 |   |                   |                 |   |           |     |   |           |     |   |
| Asia Pacific (primarily China and Taiwan) | 40,431             | 50              |   | 42,118            | 55              |   | 128,210   | 52  |   | 122,036   | 54  |   |
| Europe                                    | 16,656             | 20              |   | 13,691            | 17              |   | 52,977    | 21  |   | 40,465    | 18  |   |
| Japan                                     | 11,826             | 14              |   | 10,876            | 14              |   | 28,350    | 11  |   | 30,264    | 14  |   |
| Other Americas                            | 1,769              | 2               |   | 1,568             | 2               |   | 4,404     | 2   |   | 5,151     | 2   |   |
| Total export revenue                      | 70,682             | 86              |   | 68,253            | 88              |   | 213,941   | 86  |   | 197,916   | 88  |   |
| Total revenue                             | \$81,720           | 100             | % | \$77,137          | 100             | % | \$248,196 | 100 | % | \$224,688 | 100 | % |

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ITEM MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF  
2. OPERATIONS

Overview

Lattice Semiconductor Corporation ("Lattice", the "Company", "we", "us", or "our") designs, develops and markets high performance programmable logic products and related software. Programmable logic products are widely used semiconductor components that can be configured by the end customer as specific logic circuits, and enable the end customer to shorten design cycle times and reduce development costs. Within the programmable logic market there are two groups of products - programmable logic devices ("PLD") and field programmable gate arrays ("FPGA") - each representing a distinct silicon architectural approach. Products based on the two alternative programmable logic architectures are generally optimal for different types of logic functions, although many logic functions can be implemented using either architecture. We believe that a substantial portion of programmable logic customers utilize both PLD and FPGA architectures. Our end customers are primarily original equipment manufacturers in the wired and wireless communications, computing, industrial, consumer, automotive, medical and military end markets.

Critical Accounting Policies and Estimates

Critical accounting policies are those that are both most important to the portrayal of a company's financial condition and results and require management's most difficult, subjective and complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. Management believes that there have been no significant changes during the nine months ended October 1, 2011 to the items that we disclosed as our critical accounting policies and estimates in Management's Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the fiscal year ended January 1, 2011.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts and classification of assets, such as marketable securities, accounts receivable, inventory, auction rate securities, goodwill, deferred income taxes and liabilities, accrued liabilities (including restructuring charges and accrual for bonus arrangements), income taxes, deferred income and allowances on sales to certain sell-through distributors, forward exchange contracts, and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the fiscal periods presented. Actual results could differ from those estimates.

New Accounting Pronouncements

In June 2011, the Financial Accounting Standards Board ("FASB") issued changes to the presentation of comprehensive income. These changes give an entity the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements; the option to present components of other comprehensive income as part of the statement of changes in stockholders' equity was eliminated. The items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income were not changed. Additionally, no changes were made to the calculation and presentation of earnings per share. These changes become effective for the Company on January 1, 2012. We are currently evaluating these changes to determine which option will be chosen for the presentation of comprehensive income.

In May 2011, the FASB issued amended guidance on fair value measurement and related disclosures. The new guidance clarified the concepts applicable for fair value measurement of non-financial assets and requires the disclosure of quantitative information about the unobservable inputs used in a fair value measurement. This guidance



will be effective for reporting periods beginning after December 15, 2011, and will be applied prospectively. We are in the process of evaluating the financial and disclosure impact of this guidance. We do not anticipate a material impact on our Consolidated Financial Statements as a result of the adoption of this amended guidance.

In September 2011, the FASB issued amended guidance on testing goodwill for impairment. The new guidance provides an entity the option to first perform a qualitative assessment to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If an entity determines that this is the case, it is required to perform the currently prescribed two-step goodwill impairment test to identify potential goodwill impairment and measure the amount of goodwill impairment loss to be recognized for that reporting unit (if any). If an entity determines that the fair value of a reporting unit is more than its carrying amount, the two-step goodwill impairment test is not required. This guidance will be

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effective for reporting periods beginning after December 15, 2011. We are in the process of evaluating the financial and disclosure impact of this guidance. We do not anticipate a material impact on our Consolidated Financial Statements as a result of the adoption of this amended guidance.

## Results of Operations

## Revenue

Key elements of our Condensed Consolidated Statements of Operations were as follows (dollars in thousands):

|                                     | Three Months Ended |         |                 |         |           | Nine Months Ended |           |                 |  |  |
|-------------------------------------|--------------------|---------|-----------------|---------|-----------|-------------------|-----------|-----------------|--|--|
|                                     | October 1, 2011    |         | October 2, 2010 |         |           | October 1, 2011   |           | October 2, 2010 |  |  |
| Revenue                             | \$81,720           | 100.0 % | \$77,137        | 100.0 % | \$248,196 | 100.0 %           | \$224,688 | 100.0 %         |  |  |
| Gross margin                        | 47,854             | 58.6    | 45,586          | 59.1    | 148,134   | 59.7              | 133,984   | 59.6            |  |  |
| Research and development            | 16,999             | 20.8    | 14,814          | 19.2    | 55,770    | 22.5              | 44,654    | 19.9            |  |  |
| Selling, general and administrative | 16,809             | 20.6    | 15,818          | 20.5    | 51,717    | 20.8              | 47,621    | 21.2            |  |  |
| Restructuring charges               | 1,760              | 2.2     | 79              | 0.1     | 4,982     | 2.0               | 41        | —               |  |  |
| Income from operations              | \$12,286           | 15.0 %  | \$14,875        | 19.3 %  | \$35,665  | 14.4 %            | \$41,668  | 18.5 %          |  |  |

Revenue for the three months and nine months ended October 1, 2011 increased to \$81.7 million and \$248.2 million, respectively, compared to \$77.1 million and \$224.7 million for the three months and nine months ended October 2, 2010, respectively. Revenue growth was primarily attributed to an increase in our New products and in the Industrial and other end market.

## Revenue by Product Line

FPGA and PLD revenue increased in the third quarter and first nine months of fiscal 2011 when compared to the third quarter and first nine months of fiscal 2010. There was a 10% increase in FPGA units sold and a 6% increase in revenue in the third quarter of fiscal 2011 when compared to the third quarter of fiscal 2010. There was a 10% increase in PLD units sold and a 6% increase in revenue in the third quarter of fiscal 2011 when compared to the third quarter of fiscal 2010.

The composition of our revenue by product line for the third quarter and first nine months of fiscal 2011 and 2010 was as follows (dollars in thousands):

|               | Three Months Ended |       |                 |       |           | Nine Months Ended |           |                 |  |  |
|---------------|--------------------|-------|-----------------|-------|-----------|-------------------|-----------|-----------------|--|--|
|               | October 1, 2011    |       | October 2, 2010 |       |           | October 1, 2011   |           | October 2, 2010 |  |  |
| FPGA          | \$26,180           | 32 %  | \$24,715        | 32 %  | \$85,261  | 34 %              | \$72,737  | 32 %            |  |  |
| PLD           | 55,540             | 68    | 52,422          | 68    | 162,935   | 66                | 151,951   | 68              |  |  |
| Total revenue | \$81,720           | 100 % | \$77,137        | 100 % | \$248,196 | 100 %             | \$224,688 | 100 %           |  |  |

## Revenue by End Market

Revenue from the Industrial and other end market increased 30% and 40% for the third quarter and first nine months of fiscal 2011, respectively, when compared to the third quarter and first nine months of fiscal 2010. Revenue from the Consumer end market increased 21% and 17% for the third quarter and first nine months of fiscal 2011, respectively, when compared to the third quarter and first nine months of fiscal 2010. By contrast, revenue in the Communications end market decreased 7% and 1% for the third quarter and first nine months of fiscal 2011,

respectively, when compared to the same periods in the prior year and accounted for approximately 44% and 50% of our total revenue for the quarters ended October 1, 2011 and October 2, 2010, respectively. We expect that a significant portion of our revenue will continue to be dependent on the health of the Communications end market, which is in the midst of a downtrend.

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The composition of our revenue by end market for the third quarter and first nine months of fiscal 2011 and 2010 was as follows (dollars in thousands):

|                      | Three Months Ended |       |                 |       | Nine Months Ended |       |                 |       |
|----------------------|--------------------|-------|-----------------|-------|-------------------|-------|-----------------|-------|
|                      | October 1, 2011    |       | October 2, 2010 |       | October 1, 2011   |       | October 2, 2010 |       |
| Communications       | \$36,288           | 44 %  | \$38,954        | 50 %  | \$111,824         | 45 %  | \$112,791       | 50 %  |
| Industrial and other | 25,432             | 31    | 19,575          | 26    | 76,307            | 31    | 54,668          | 24    |
| Computing            | 10,305             | 13    | 10,590          | 14    | 32,089            | 13    | 33,229          | 15    |
| Consumer             | 9,695              | 12    | 8,018           | 10    | 27,976            | 11    | 24,000          | 11    |
| Total revenue        | \$81,720           | 100 % | \$77,137        | 100 % | \$248,196         | 100 % | \$224,688       | 100 % |

## Revenue by Product Classification

Revenue for New products increased 11% and 23%, respectively, for the third quarter and first nine months of fiscal 2011, compared to the third quarter and first nine months of fiscal 2010. New product revenue increased primarily due to an increase in unit sales and an increase in average selling price. Revenue for Mainstream products decreased 13% and 7% for the third quarter and first nine months of fiscal 2011, respectively, when compared to the third quarter and first nine months of fiscal 2010. Mainstream product revenue decreased due to a decrease in both average selling price and in unit sales. The increase in average selling price for New products and the decrease in average selling price for Mainstream products resulted from changes in product mix and end customer mix. Mature product revenue increased 23% and 13% for the third quarter and first nine months of fiscal 2011, respectively, compared to the third quarter and first nine months of fiscal 2010. Mature product revenue increased primarily due to an increase in units sold partially offset by a decrease in average selling price.

The composition of our revenue by product classification for the third quarter and first nine months of fiscal 2011 and 2010 was as follows (dollars in thousands):

|               | Three Months Ended |       |                 |       | Nine Months Ended |       |                 |       |
|---------------|--------------------|-------|-----------------|-------|-------------------|-------|-----------------|-------|
|               | October 1, 2011    |       | October 2, 2010 |       | October 1, 2011   |       | October 2, 2010 |       |
| New *         | \$39,363           | 48 %  | \$35,304        | 46 %  | \$116,937         | 47 %  | \$95,174        | 42 %  |
| Mainstream *  | 21,830             | 27    | 25,099          | 32    | 71,230            | 29    | 76,284          | 34    |
| Mature *      | 20,527             | 25    | 16,734          | 22    | 60,029            | 24    | 53,230          | 24    |
| Total revenue | \$81,720           | 100 % | \$77,137        | 100 % | \$248,196         | 100 % | \$224,688       | 100 % |

## \* Product Classifications:

|             |   |
|-------------|---|
| New:        | LatticeECP3, LatticeXP2, LatticeECP2/M, MachXO, Power Manager II, ispClockA/D/S, ispMACH 4000ZE   |
| Mainstream: | ispXPLD, ispGDX2, ispMACH 4000/Z, ispXPGA, LatticeSC, LatticeECP, LatticeXP, ispClock, Power Manager I, Software and IP   |
| Mature:     | FPSC, ORCA 2, ORCA 3, ORCA 4, ispPAC, ispLSI 8000V, ispMACH 5000B, ispMACH 2LV, ispMACH 5LV, ispLSI 2000V, ispLSI 5000V, ispMACH 5000VG, all 5-volt CPLDs, GDX/V, ispMACH 4/LV, all SPLDs |

\* Product categories are modified as appropriate relative to our portfolio of products and the generation within each major product family. New products consist of our latest generation of products, while Mainstream and Mature are older or based on unique late stage customer-based production needs. Generally, product categories are adjusted every two to three years, at which time prior periods are reclassified to conform to the new categorization. No adjustments were made in the third quarter of fiscal 2011.



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## Revenue by Geography

Domestic revenue accounted for 14% of total revenue for the three and nine months ended October 1, 2011, whereas export revenue was 86% of total revenue. Domestic revenue accounted for 12% of total revenue for the three and nine months ended October 2, 2010, whereas export revenue was 88% of total revenue. We believe the export market to the Asia Pacific region will remain the primary source of our revenue due to more favorable business conditions and a continuing trend towards outsourcing of manufacturing by North American and European customers to the Asia Pacific region.

The composition of our revenue by geography, based on ship-to location, is as follows (dollars in thousands):

|   | Three Months Ended |       |                 |       | Nine Months Ended |       |                 |       |
|---|--------------------|-------|-----------------|-------|-------------------|-------|-----------------|-------|
|   | October 1, 2011    |       | October 2, 2010 |       | October 1, 2011   |       | October 2, 2010 |       |
| United States:                            | \$11,038           | 14 %  | \$8,884         | 12 %  | \$34,255          | 14 %  | \$26,772        | 12 %  |
| Export revenue:                           |                    |       |                 |       |                   |       |                 |       |
| Asia Pacific (primarily China and Taiwan) | 40,431             | 50    | 42,118          | 55    | 128,210           | 52    | 122,036         | 54    |
| Europe                                    | 16,656             | 20    | 13,691          | 17    | 52,977            | 21    | 40,465          | 18    |
| Japan                                     | 11,826             | 14    | 10,876          | 14    | 28,350            | 11    | 30,264          | 14    |
| Other Americas                            | 1,769              | 2     | 1,568           | 2     | 4,404             | 2     | 5,151           | 2     |
| Total export revenue                      | 70,682             | 86    | 68,253          | 88    | 213,941           | 86    | 197,916         | 88    |
| Total revenue                             | \$81,720           | 100 % | \$77,137        | 100 % | \$248,196         | 100 % | \$224,688       | 100 % |

## Termination of Avnet Inc. ("Avnet") global franchise agreement

On August 28, 2011, our global franchise agreement with Avnet terminated, however, we have mutually agreed to terms for the transition of inventory through December 31, 2011. Revenue from Avnet made up approximately 20% of our total revenue for the first nine months of fiscal 2011, and 17% of our total revenue for the year ended January 1, 2011. We do not expect a significant disruption in our ability to service customers as a result of this change. We continue to serve our end customers with a network that includes a global distributor, regional distributors, manufacturer's representatives, and our direct sales team.

## Gross Margin and Operating Expenses

Our gross margin percentage was 58.6% and 59.7% in the third quarter and first nine months of fiscal 2011, respectively, compared to 59.1% and 59.6% in the third quarter and first nine months of fiscal 2010, respectively. The decrease in gross margin percentage for the third quarter of 2011, as compared to the third quarter of 2010, was partly attributed to product mix as New products accounted for 48% of revenue in the third quarter of 2011 compared to 46% in the comparable quarter of 2010, and an increase in gold and yield related costs. The increase in gross margin percentage when the first nine months of 2011 is compared to the same period in 2010 was primarily attributed to product mix as revenue from the Industrial and other end market increased 40%. New products typically have lower gross margins than products in other product classifications.

Research and development expense was \$17.0 million and \$55.8 million in the third quarter and first nine months of fiscal 2011, respectively, compared to \$14.8 million and \$44.7 million in the third quarter and first nine months of fiscal 2010, respectively. Research and development expenses consist primarily of personnel, masks, engineering wafers, third-party design automation software, test equipment and tooling depreciation, and qualification expenses.

The increase in fiscal 2011 compared to fiscal 2010 was primarily a result of an increase in labor costs, engineering mask and wafer costs, purchased outside services, depreciation costs, and time based license costs. We believe that a continued commitment to research and development is essential to maintain product leadership and provide innovative new product offerings, and therefore we expect to continue to make significant future investments in research and development. As we continue to move to more advanced process technologies such as 65nm, mask and engineering wafer costs become increasingly more expensive and will therefore represent a greater proportion of total research and development expenses.

Selling, general and administrative expense was \$16.8 million and \$51.7 million for the third quarter and first nine months of fiscal 2011, respectively, compared to \$15.8 million and \$47.6 million in the third quarter and first nine months of fiscal 2010, respectively. This increase in fiscal 2011 compared to fiscal 2010 was a result of an increase in labor related costs, sales commission costs, legal costs and marketing related costs.

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During 2011, the Company's Board of Directors adopted a restructuring plan to more efficiently implement the Company's product development strategy and to better align the Company's corporate strategy with the Company's sales resources (the "2011 restructuring plan"). In connection with the 2011 restructuring plan, the Company will reduce and refocus its headcount at certain of its research and development facilities, including Pennsylvania and Shanghai, China, and streamline its supply chain activities at its headquarters for reduced operational costs, improved predictability and flexibility. Part of the 2011 restructuring plan includes extending silicon development capabilities, planning and logistics activities by locating personnel in Manila, Philippines, which is expected to initially increase certain supply chain and research and development costs, until transition is fully implemented. In addition, during the third quarter of 2011 the Company incurred restructuring costs related to outsourcing certain non-core information technology services. The 2011 restructuring plan will be substantially implemented during 2011, with a total projected restructuring charge of approximately \$7.6 million through the first quarter of fiscal 2012, of which \$5.8 million was recorded in the first nine months of fiscal 2011.

The Company also implemented restructuring plans during the fiscal years 2009 ("2009 restructuring plan") and 2005 ("2005 restructuring plan"). In connection with the 2009 restructuring plan, a credit of \$0.8 million was recorded in the first quarter of fiscal 2011, primarily due to a change in original estimates of lease and severance and related costs. In connection with the 2005 restructuring plan, a credit of \$0.1 million was recorded in the third quarter of fiscal 2011, primarily due to a change in original estimates of lease related costs.

## Other income, net

The following table summarizes the activity in Other income, net (in thousands):

|   | Three Months Ended |                    | Nine Months Ended  |                    |
|---|--------------------|--------------------|--------------------|--------------------|
|   | October 1,<br>2011 | October 2,<br>2010 | October 1,<br>2011 | October 2,<br>2010 |
| Interest income   | \$218              | \$300              | \$820              | \$751              |
| (Loss) gain primarily related to sale of marketable securities, net | (69                | ) 409              | 385                | 469                |
| Gain on sale of excess real estate                                  | —                  | —                  | —                  | 720                |
| Gain (loss) on foreign exchange transactions and other, net         | 99                 | (40                | ) (26              | ) (24              |
| Total other income, net   | \$248              | \$669              | \$1,179            | \$1,916            |

The decrease in Other income, net in the first nine months of fiscal 2011 as compared to the first nine months of fiscal 2010 resulted from a gain on the sale of excess real estate that was recorded in the second quarter of fiscal 2010 while no comparable transaction occurred in fiscal 2011. The decrease in Other income, net in the third quarter of fiscal 2011 as compared to the third quarter of fiscal 2010 resulted from a gain on the sale of auction rate securities that was recorded in the third quarter of fiscal 2010 while no comparable transaction occurred in the third quarter of fiscal 2011. Interest income increased in fiscal 2011 compared to fiscal 2010 primarily related larger invested balances. Interest income decreased in the third quarter of fiscal 2011 as compared to the third quarter of fiscal 2010 primarily due to lower yields on invested balances.

## (Benefit) provision for income taxes

We are paying foreign income taxes, which are reflected in the (Benefit) provision for income taxes in our Condensed Consolidated Statements of Operations and are primarily related to the cost of operating an offshore research and development subsidiary and sales subsidiaries. We are not currently paying federal income taxes and do not expect to



pay such taxes until the benefits of our tax net operating loss carryforwards are fully utilized. During the period ended October 1, 2011 the Company decided not to pursue further litigation with regards to the prepaid expense adjustment and settled with the IRS. As a result of this decision, the Company paid \$1.0 million in October 2011 related to disallowed prepaid expense deductions and the corresponding carry back of those deductions to the 1999 and 2000 tax returns through a net operating loss carry back. The amount paid was fully reserved. A benefit of approximately \$0.9 million has been recognized in the three months and nine months ended October 1, 2011 for the reversal of uncertain tax positions and related interest for the years effectively settled.

As a result of our recent positive operating results in 2010 and thus far in 2011, and our expectations for the future, we may release a portion or all of our allowance on our deferred tax assets in the near future. We expect to pay a nominal amount of state income tax. We accrue interest and penalties related to uncertain tax positions in the Provision for income taxes.

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## Liquidity and Capital Resources

## Financial Condition Sources and Uses of Cash (in thousands):

|   | Nine Months Ended  |                    |
|---|--------------------|--------------------|
|   | October 1,<br>2011 | October 2,<br>2010 |
| Net cash provided by operating activities           | \$44,119           | \$64,288           |
| Net cash used in investing activities               | (4,981 )           | (57,994 )          |
| Net cash (used in) provided by financing activities | (8,602 )           | 4,271              |
| Net increase in cash and cash equivalents           | \$30,536           | \$10,565           |

## Operating Activities

Net cash provided by operating activities was \$44.1 million in the first nine months of fiscal 2011, compared to \$64.3 million in the first nine months of fiscal 2010. The decrease in comparable periods is primarily the result of the decrease in Net income from operations from \$43.2 million in fiscal 2010 to \$37.3 million in fiscal 2011, and the use of foundry advances of \$11.4 million in fiscal 2010 and no such transaction in 2011. In addition, net cash was used for the increase of Inventory of \$5.8 million in the first nine months of fiscal 2010 compared to cash provided by a decrease in inventory of \$2.2 million in the first nine months of 2011. Finally, net cash was provided by an increase in Accounts payable and accrued expenses and Accrued payroll obligations in the first nine months of fiscal 2010 of \$13.2 million, whereas net cash was provided by an increase in Accounts payable and accrued expenses and Accrued payroll obligations in the first nine months of fiscal 2011 of \$6.7 million.

## Investing Activities

Net cash used in investing activities decreased by \$53.0 million in the first nine months of fiscal 2011, compared to the first nine months of fiscal 2010 primarily due to sales of Short-term marketable securities and Long-term marketable securities exceeding purchases of Short-term marketable securities in the first nine months of fiscal 2011, compared to the first nine months of fiscal 2010. The sale of Long-term marketable securities consisted of student loan auction rate securities with a par value of \$3.3 million and an estimated fair value of \$2.8 million for a gain of \$0.6 million in the first quarter of fiscal 2011. Capital expenditures increased from \$8.5 million in the first nine months of fiscal 2010, to \$8.7 million in first nine months of fiscal 2011.

## Financing Activities

Net cash used in financing activities increased by \$12.9 million for the first nine months of fiscal 2011 compared to the first nine months of fiscal 2010 due to the purchase of Treasury stock in the amount of \$12.8 million in the first nine months of fiscal 2011 while no such purchases took place in the first nine months of fiscal 2010.

## Liquidity

As of October 1, 2011, our principal source of liquidity was \$267.2 million of Cash and cash equivalents and Short-term marketable securities, which were approximately \$29.0 million more than the balance of \$238.2 million at January 1, 2011. Working capital increased to \$301.7 million at October 1, 2011 from \$271.0 million at January 1, 2011.

We believe that our existing liquid resources and cash expected to be generated from future operations will be adequate to meet our operating, capital requirements and obligations for at least the next twelve months.

At October 1, 2011 and January 1, 2011, the Company held auction rate securities with a par value of \$8.3 million and \$11.6 million, respectively. On March 29, 2011, the Company sold student loan auction rate securities, with a par value of \$3.3 million and an estimated fair value of \$2.8 million for \$3.3 million, reported a gain of \$0.6 million and relieved \$0.1 million of previously unrecognized gain in Accumulated other comprehensive income. The Company intends to sell its auction rate securities as markets for these securities resume or reasonable offers become available. At October 1, 2011, due to continued multiple failed auctions and a determination of illiquidity, the fair value of auction rate securities held by the Company and classified as Long-term marketable securities was \$7.4 million. These auction rate securities are exposed to risks associated with student loan asset-backed notes. Such loans are insured by the federal government or guaranteed by the Federal Family Educational Loan Program. If we were to liquidate our position in these securities, the amount realized could be materially

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different than the estimated fair value amounts at which we are carrying these securities and there could be a materially detrimental effect on our financial results.

In accordance with ASC 320, "Investments-Debt and Equity Securities," the Company recorded an unrealized loss of less than \$0.1 million during the nine months ended October 1, 2011 on certain Short-term marketable securities (Level 1 instruments), which has been recorded in Accumulated other comprehensive income. Future fluctuations in fair value related to these instruments that the Company deems to be temporary, including any recoveries of previous write-downs, would be recorded to Accumulated other comprehensive income. In addition, during the nine months ended October 1, 2011, the Company realized a gain of \$0.6 million related to the sale of a portion of its Long-term marketable securities portfolio.

If the Company were to determine in the future that any further decline in fair value is other-than-temporary, we would record an impairment charge, which could have a materially detrimental impact on our operating results. If we were to liquidate our position in these securities, it is likely that the amount of any future realized gain or loss would be different from the unrealized gain or loss reported in Accumulated other comprehensive income.

On October 21, 2010, the Company's Board of Directors approved a stock repurchase program pursuant to which up to \$20.0 million of outstanding common stock may be repurchased from time to time. The duration of the repurchase program was twelve months. In connection with this stock repurchase program, the Company entered into a 10b5-1 plan. During the first nine months of fiscal 2011, approximately 2.2 million shares were repurchased for \$12.8 million. During fiscal 2010, approximately 0.4 million shares were repurchased for \$2.0 million. All shares repurchased under this program were retired by October 1, 2011. All repurchases were open market transactions and funded from available working capital. The number of shares that will be repurchased in the future will depend on market conditions, including the price of the common stock. The program ended by its terms October 26, 2011.

We may in the future seek new or additional sources of funding. In addition, in order to secure additional wafer supply, we may from time to time consider various financial arrangements including equity investments, advance purchase payments, loans, or similar arrangements with independent wafer manufacturers in exchange for committed wafer capacity. To the extent that we pursue any such additional financing arrangements, additional debt or equity financing may be required. There can be no assurance that such additional financing will be available when needed or, if available, will be on favorable terms. Any future equity financing will decrease existing stockholders' equity percentage ownership and may, depending on the price at which the equity is sold, result in dilution.

## Contractual Obligations

There have been no significant changes to the Company's contractual obligations outside of the ordinary course of business in the first nine months of fiscal 2011 as summarized in Management's Discussion and Analysis of Financial Condition and Results of Operations in the Company's Annual Report on Form 10-K for the year ended January 1, 2011.

## Off-Balance Sheet Arrangements

As of October 1, 2011, we did not have any off-balance sheet arrangements, as defined in Item 303(a)(4)(ii) of SEC Regulation S-K.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Credit Market Risks

At October 1, 2011 and January 1, 2011, we held auction rate securities with a par value of \$8.3 million and \$11.6 million, respectively. At October 1, 2011, the auction rate securities held by us had an estimated fair value of \$7.4 million. At January 1, 2011, the auction rate securities had an estimated fair value of \$10.2 million. Our investments in auction rate securities are subject to interest rate and market risk. A hypothetical 10% movement in interest rates would not have a material impact on the fair value of the portfolio. If the market for our investment portfolio declines, our consolidated operating results may be negatively impacted.

Foreign Currency Exchange Rate Risk

We have international subsidiary and branch operations. In addition, a portion of our silicon wafer and other purchases are denominated in Japanese yen and we bill our Japanese customers in yen. We mitigate the resulting foreign currency exchange rate exposure by entering into foreign currency forward exchange contracts for Japanese yen. Although such hedges mitigate our foreign currency exchange rate exposure from an economic perspective they were not designated as "effective" hedges for accounting purposes and are adjusted to fair value through earnings. We do not hold or issue derivative financial instruments for trading or speculative purposes.

As a result of the use of derivative financial instruments, Lattice is exposed to the risk that counter-parties to derivative contracts will fail to meet their contractual obligations. To mitigate the counter-party credit risk, Lattice enters into contracts with carefully selected major financial institutions based upon their credit ratings and other factors.

On October 1, 2011, the Company had a forward contract to deliver 100 million yen by October 24, 2011. The contract was settled by that date.

Except for the above, there have been no material changes to the quantitative and qualitative disclosures about market risk reported in our Annual Report on Form 10-K for the year ended January 1, 2011.

ITEM 4. CONTROLS AND PROCEDURES

Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our principal executive officer and our principal financial officer, we conducted an evaluation of our disclosure controls and procedures, as such term is defined under Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended. Based on this evaluation, our principal executive officer and our principal financial officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this quarterly report.

Changes in Internal Control over Financial Reporting

There has been no change in our internal control over financial reporting that occurred during the period covered by this Quarterly Report on Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

We are in the process of implementing a new ERP system. The first phase of the implementation was completed during the fourth quarter of 2010 and included implementing new modules related to our general ledger, accounts

payable and elements of our cost accounting systems. Since the completion of the first phase of the implementation, we continued to develop and apply additional features of the new ERP system, which resulted in the modification of certain controls, procedures and processes. We follow a system implementation life cycle process that requires significant pre-implementation planning, design and testing. We plan to continue to replace our legacy systems with the new ERP system functionality over the next several years.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The information set forth above under Note 12 contained in the “Notes to Condensed Consolidated Financial Statements” is incorporated herein by reference.

ITEM 1A. RISK FACTORS

The risk factors included herein include any material changes to and supersede the description of the risk factors associated with our business previously disclosed in Item 1A of our Annual Report on Form 10-K for the year ended January 1, 2011. The following risk factors and other information included in this Quarterly Report should be carefully considered. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties not presently known to us or that we currently deem immaterial also may impair our business operations. If any of the following risks occur, our business, financial condition, operating results and cash flows could be materially adversely affected.

We may be unsuccessful in defining, developing and identifying manufacturing processes for the new programmable logic products required to maintain or expand our business. Currently Fujitsu Semiconductor Limited ("Fujitsu") is our sole source supplier of wafers for our newest FPGA and PLD products.

As a semiconductor company, we operate in a dynamic environment marked by rapid product obsolescence. The programmable logic market is characterized by rapid technology and product evolution. Consequently, our future success depends on our ability to introduce new FPGA, PLD and associated software design tool products that meet evolving customer needs while achieving acceptable margins. We are presently shipping our latest generation product families that are critical to our ability to grow our overall revenue. We also plan to continue upgrading our customer design tool products and increase our offerings of intellectual property cores. If we fail to introduce new products in a timely manner, or if these products or future new products fail to achieve market acceptance, or if we fail in our ability to achieve acceptable margins our operating results could be adversely affected.

The Company and Fujitsu have entered into agreements pursuant to which Fujitsu manufactures most of our new products on its 130 nanometer, 90 nanometer and 65 nanometer CMOS process technologies, as well as on 130, 90 and 65 nanometer technologies with embedded flash memory that we have jointly developed with Fujitsu. Fujitsu is our sole source supplier of wafers for our newest FPGA and PLD products. The success of certain of our next generation products is dependent on our ability to successfully partner with Fujitsu or new foundry partners. If for any reason we are unsuccessful in establishing new foundry relationships for our next generation products, our future operating results could be adversely affected.

To develop new products and maintain the competitiveness of existing products, we need to migrate to more advanced wafer manufacturing processes that use smaller device geometries. We also may need to use additional foundry partners. Because we depend upon foundry partners to provide their facilities and support for our process technology development, we may experience delays in the availability of advanced wafer manufacturing process technologies at existing or new wafer fabrication facilities. As a result, volume production of our advanced process technologies at fabrication facilities may not be achieved. This could adversely affect our operating results.

The introduction of new silicon and software design tool products in a dynamic market environment presents significant business challenges. Product development commitments and expenditures must be made well in advance of product sales. The market acceptance of new products depends on accurate projections of long-term customer demand, which by their nature are uncertain. In order to secure new or additional wafer supply, we may from time to

time consider various financial arrangements including equity investments, advance purchase payments, loans, or similar arrangements with independent wafer manufacturers in exchange for committed wafer capacity. To the extent that we pursue any such additional financing arrangements, additional debt or equity financing may be required. There can be no assurance that such additional financing will be available when needed or, if available, will be on favorable terms. Any future equity financing will decrease existing stockholders' equity percentage ownership and may, depending on the price at which the equity is sold, result in dilution.

Our customer design-in activity, and thus, future revenue growth is dependent on market acceptance of our new silicon and software design tool products and the continued market acceptance of our current products. Future revenue is inherently uncertain and could impact our ability to manage production or our ability to forecast sales.

We face uncertainties relating to the potential impact of customer design-in activity because it is unknown whether any



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particular customer design-in will ultimately result in sales of significant volume. After a specific customer design-in is obtained, many factors can impact the timing and amount of sales that are ultimately realized. Changes in the competitive position of our technology, the customer's product competitiveness or product strategy, the financial position of the customer, and other factors can impact the timing and amount of sales ultimately realized from any specific customer design-in.

We are presently shipping our latest generation FPGA, PLD and Programmable Mixed Signal product families that are critical to our ability to grow our overall revenue. We also plan to continue upgrading our customer design tool products and increase our offerings of intellectual property cores. Our future revenue growth is dependent on customer design-in activity, market acceptance of our new silicon and software design tool products and the continued market acceptance of our current products. The success of these products is dependent on a variety of specific technical factors including:

- successful product definition;
- timely and efficient completion of product design;
- timely and efficient implementation of wafer manufacturing and assembly processes;
- product performance;
- product cost;
- the quality and reliability of the product; and
- ease of use.

If, due to these or other factors, our new silicon and software products do not achieve market acceptance, or our current products do not maintain market acceptance, our ability to manage production levels or accurately forecast the future revenue, our operating results may be adversely affected.

We depend on distributors, primarily those that use the sell-through distribution model, to generate a majority of our sales and complete order fulfillment. The failure of our distributors to sell our products and otherwise perform as expected could materially reduce our future sales.

We depend on our distribution partners to sell our products to end customers, generate a majority of our sales, complete order fulfillment and stock our products. Our distributors also help us to provide technical support and other value-added services to end customers.

We expect that the majority of our revenue in fiscal 2011 will be reported resale by our sell-through distributors. Our primary sell-through distributors, Arrow Electronics, Inc., including Nu Horizons Electronics Corp., (a wholly owned subsidiary of Arrow Electronics, Inc. USA), Avnet, Inc. ("Avnet"), and Weikeng (International and Industrial) Co. LTD made up approximately 49%, 34% and 28% of total revenue for fiscal years 2010, 2009 and 2008, respectively. We depend on the timeliness and accuracy of these resale reports from our distributors; late or inaccurate resale reports could have a detrimental effect on our ability to recognize revenue and our ability to predict future sales. In addition, our distribution channels recently have experienced consolidation due to merger and acquisition activity in that business sector. Consolidation may result in our distributors allocating fewer resources to the distribution and sale of our products, which could adversely affect our financial results.

On August 28, 2011, our global franchise agreement with Avnet will terminate, however, we have mutually agreed to terms for the transition of inventory through December 31, 2011. Revenue from Avnet made up approximately 20% of our total revenue for the nine months ended October 1, 2011, and 17% of our total revenue for the year ended January 1, 2011. We intend to serve the Avnet end customers through a network that includes a global distributor, regional distributors, manufacturer's representatives, and our direct sales team. If our end customers experience disruption in the supply of our products, or if our distributors and representatives are unable to provide technical support and other value-added service at least at historical levels, we may lose future sales and our financial results could be adversely affected.

At times, our sales are concentrated in a small number of distributors, which are in various international locations and of various financial strengths. Financial difficulties, inability to access capital markets, or other reasons, may affect our distributors' performance, which could materially harm our business and our operating results.

We rely on information technology systems and recently implemented a new enterprise-wide financial reporting system which may cause operating or reporting disruptions. The failure of these systems to function properly could result in business disruption.

We rely in part on various information technology ("IT") systems to manage our operations, including financial reporting,

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and we regularly make changes to improve them as necessary. Consequently, we periodically implement new, or enhance existing, operational and IT systems, procedures and controls. For example, the Company converted to a new enterprise-wide financial reporting ("ERP") system which includes cloud computing and off-site infrastructure to improve processes, enhance the access and timeliness of critical business information and strengthen controls throughout the Company. We converted to this new system in October 2010. At October 1, 2011, we have almost completed configuration of a new customer management software application. These systems are subject to power and telecommunications outages or other general system failures. During the third quarter of 2011, the Company incurred restructuring costs related to outsourcing certain non-core IT services. Failure of our IT systems or difficulties in managing them could result in business disruption. Many companies have experienced operating or reporting disruptions when converting to a new ERP system or integrating the new systems with legacy systems, including limitations on a company's ability to deliver and bill for customer shipments, maintain current and complete books and records, maintain an effective internal control environment, meet external reporting deadlines, or provide consistent and accurate analysis. While we have not yet experienced any significant disruptions to our business, we may encounter some unexpected aspects of the conversion, outsourcing, or new systems implementations that cause difficulty in the new reporting system which could adversely affect the Company's business, results of operations and cash flows.

We may experience a disruption of our business activities related to the successful execution of the 2011 restructuring plan.

During 2011, the Company's Board of Directors adopted a restructuring plan (the "2011 restructuring plan") to more efficiently implement the Company's product development strategy and to better align the Company's corporate strategy with the Company's sales resources to reduce development and operational costs and to streamline our supply chain for improved predictability and flexibility. Part of the 2011 restructuring plan includes extending silicon development capabilities, planning and logistics activities by locating personnel in Manila, Philippines, which is expected to initially increase certain supply chain and research and development costs, until transition is fully implemented. During the third quarter of 2011, the Company incurred restructuring costs related to outsourcing certain non-core IT services. We may experience disruption in our business activities as we execute our 2011 restructuring plan, and our relationships with employees, customers and suppliers could be adversely affected by these disruptions. Our business, financial condition and results of operations could be materially adversely affected by the loss of any of our key employees, by the failure of any key employee to perform in his or her current position, the effects of outsourcing certain non-core IT services, or by our inability to adequately maintain our relationships with customers and suppliers. In addition, we may not achieve the cost reductions and other benefits we anticipate from the 2011 restructuring plan.

Global economic conditions and uncertainty, as well as the highly cyclical nature of the semiconductor industry, could adversely affect our revenue, gross margin and expenses, collectability of accounts receivable and supplier relationships, and ability to access capital markets.

Our revenue and gross margin can fluctuate significantly due to downturns in the general economy or the semiconductor industry. These downturns are often severe and prolonged and can result in significant reductions in the demand for PLD and FPGA products in markets in which we compete. Global economic weakness or cyclical downturns have previously resulted from periods of economic recession, reduced access to credit markets, weakening or strengthening of the U.S. dollar relative to other currencies, weak end-user demand, excess industry capacity, political instability, Government fiscal policy, sovereign debt, terrorist activity, military actions, or general reductions in inventory levels by customers, and may cause a decrease in revenue, gross margin, earnings or growth rates and problems with our ability to manage inventory levels and collect customer receivables. Such economic conditions had a negative impact on our results of operations during much of 2009. Although business conditions improved in 2010 and the first half of 2011, that trend appears to be slowing down or reversing. In addition, our relationships with our

employees and suppliers and ability to access capital markets could be adversely affected. In addition, customer financial difficulties have previously resulted, and could result in the future, in increases in bad debt write-offs and additions to reserves in our accounts receivable. Global economic and cyclical downturns also may lead to restructuring actions and associated expenses. Uncertainty about future economic conditions makes it difficult for us to forecast operating results and to make decisions about future investments. Any or all of these factors could adversely affect our financial condition and results of operations in the future.

A downturn in the communications equipment end market could cause a reduction in demand for our products and limit our ability to maintain revenue levels and operating results.

Historically the largest percentage of our revenue (approximately 45% of the first nine months of fiscal 2011 revenue) has been derived from customers participating in the communications equipment end market. In addition, during fiscal year 2009, the Company participated in the China 3G telecommunications network build-out by selling products used by two large telecommunication equipment providers (one of which was supported through distribution), which accounted for a combined

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19% of our aggregate revenue. This is primarily due to strength in the wireless portion of the communications end market. For the 2010 fiscal year, the same two large telecommunication equipment providers accounted for a combined 12% of revenue. In the past, a general weakening in demand for programmable logic products from customers in the communications end market has adversely affected our revenue. In addition, telecommunication equipment providers are building networks for 4G networks in which we compete. Any deterioration in the communication end market, our ability to compete for new solutions in future telecommunications solutions (e.g. 4G networks) or reduction in capital spending to support this end market could lead to a reduction in demand for our products which could adversely affect our revenue and results of operations.

We may not be able to successfully compete in the highly competitive semiconductor industry.

The semiconductor industry is intensely competitive and many of our direct and indirect competitors have substantially greater financial, technological, manufacturing, marketing and sales resources. The current level of competition in the programmable logic market is high and may increase in the future. We currently compete directly with companies that have licensed our technology or have developed similar products, including Actel Corporation (acquired by Microsemi Corporation in November 2010), Altera Corporation, and Xilinx, Inc. We also compete indirectly with numerous semiconductor companies that offer products based on alternative solutions such as ASIC, ASSP, microcontroller, analog, and digital signal processing (DSP) technologies. These direct and indirect competitors are established, multinational semiconductor companies as well as emerging companies. If we are unable to compete successfully in this environment, our future results will be adversely affected.

Our revenue and gross margin, including quarter over quarter, are subject to fluctuations due to many factors which make our future financial results less predictable.

Our operating results, including quarter over quarter, have fluctuated in the past and may continue to fluctuate. Consequently, our operating results may fail to meet the expectations of analysts and investors. Our revenue and gross margin may fluctuate due to product mix, inventory fluctuations at our distributor end customers, market acceptance of new products, competitive pricing dynamics, geographical and market-segment pricing strategies, wafer, package and assembly prices and yields, overhead absorption, as well as provisions for warranty and excess and obsolete inventory.

We have limited ability to foresee changes or the pace of changes in sales by product classification. In the past we have also experienced periods of decline in sales of our mainstream and mature products. If, in any period, sales of our mature and mainstream products decline and sales of new products do not increase at a rate that is sufficient to counteract this decline, then our total revenue would decline. In addition, as mature products typically generate a higher gross margin than mainstream or new products, a faster than normal decline in sales of mature products could adversely impact our gross margins.

We also have experienced, and may experience in the future, gross margin declines in certain products or end-markets, reflecting the effect of competitive pricing pressures, inventory write-downs, charges associated with the cancellation of planned production lines, costs associated with our customers unplanned demand to build inventory, and increases in component and manufacturing costs resulting from higher labor and material costs borne by our manufacturers and suppliers that, as a result of competitive pricing pressures or other factors, we are unable to pass on to our customers.

Further, our ability to predict end customer demand, our customers' end customer demand, and resale of our products by our sell-through distributors is limited. Typically, a significant amount of our revenue comes from "turns orders," which are orders placed and filled within the same period. By definition, turns orders are not captured in a backlog measurement at the beginning of a quarter. Accordingly, we cannot use backlog as a reliable measure for predicting revenue.

Export sales, primarily to the Asia Pacific region, account for the majority of our revenue and may decline in the future due to economic and governmental uncertainties.

We derive the majority of our revenue from export sales. Accordingly, if we experience a decline in export sales, our operating results could be adversely affected. Our export sales are subject to numerous risks, including:

- changes in local economic conditions;
- exchange rate volatility;
- governmental stimulus packages, controls and trade restrictions;
- export license requirements and restrictions on the export of technology;
- political instability, war, terrorism or pandemic disease;
- changes in tax rates, tariffs or freight rates;
- reduced protection for intellectual property rights in some countries;

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longer receivable collection periods;  
natural or man-made disasters in the countries where we sell our products;  
interruptions in transportation;  
different labor regulations; and  
difficulties in staffing and managing foreign sales offices.

Product quality problems could lead to reduced revenue, gross margins and net income.

We generally warrant our products for varying lengths of time against non-conformance to our specifications and certain other defects. Because our products, including hardware, software and intellectual property cores, are highly complex and increasingly incorporate advanced technology, our quality assurance programs may not detect all defects, whether manufacturing defects in individual products or systematic defects that could affect numerous shipments. Inability to detect a defect could result in increased engineering expenses necessary to remediate the defect and also result in increased costs due to inventory impairment charges. On occasion we have also repaired or replaced certain components or made software fixes or refunded the purchase price or license fee paid by our customers due to product or software defects. If there are material increases in product defects, the costs to remediate such defects, net of reimbursed amounts from our vendors, if any, or to resolve warranty claims compared with our historical experience, may adversely affect our revenue, gross margins and net income.

If we are unable to adequately protect our intellectual property rights, our financial results and competitive position may suffer.

Our success depends in part on our proprietary technology. We intend to continue to protect our proprietary technology through patents, copyrights and trade secrets. Despite this intention, we may not be successful in achieving adequate protection. Claims allowed on any of our patents may not be sufficiently broad to protect our technology. Patents issued to us also may be challenged, invalidated or circumvented. Finally, our competitors may develop competing technologies. If any of these events occur, our competitive position could be adversely affected.

Companies in the semiconductor industry vigorously pursue and defend their intellectual property rights. We may be forced to pursue legal action to protect or enforce our intellectual property rights. If we become involved in protracted intellectual property disputes or litigation, we may be forced to use substantial financial and management resources, which could have an adverse effect on our operating results.

We face a number of patent infringement claims and may be subject to other intellectual property disputes, which could require us to spend a significant sum to defend and could cause losses.

Our industry is characterized by increasingly frequent claims regarding patents and other intellectual property rights of others. We have been, and from time to time expect to be, notified of claims that we are infringing upon the intellectual property rights of others. For instance, we are exposed to certain asserted and unasserted potential claims, including the pending patent litigation brought against us by Lizy K. John, Intellectual Ventures I LLC and Intellectual Ventures II LLC, and Commonwealth as described in Item 1. Legal Proceedings, above. If any third party makes a valid claim against us, we could face significant liability and could be required to make material changes to our products and processes. In response to claims of infringement, we have incurred legal costs and committed management resources, and there can be no assurance that we would be successful in our defense against the claims. Any such litigation could result in a substantial diversion of management and financial resources, including legal costs incurred to defend claims, which by itself could have a material adverse effect on our financial condition and operating results. We may seek licenses under patents that we are alleged to be infringing; however, we may not be able to obtain a license on favorable terms, or at all, which could have an adverse effect on our operating results.

If our foundry partners experience quality or yield problems, we may face a shortage of products available for sale and our revenue or gross margin could be adversely affected.

We depend on our foundry partners to deliver high quality silicon wafers with acceptable yields in a timely manner consistent with our safety stock inventory level and production plan. As is common in our industry, we have experienced wafer yield problems and delivery delays. The reliable manufacture of high performance programmable logic devices is a complicated and technically demanding process requiring:

- a high degree of technical skill;
- state-of-the-art equipment;



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- the availability of certain basic materials and supplies, such as chemicals, gases, polysilicon, silicon wafers and ultra-pure metals;
- the absence of defects in production wafers;
- the elimination of minute impurities and errors in each step of the fabrication process; and
- effective cooperation between the wafer supplier and us.

As a result, our foundry partners may periodically experience difficulties in achieving acceptable quality and yield levels when manufacturing our silicon wafers. If our foundry partners are unable for a prolonged period to produce silicon wafers that meet our specifications with acceptable yields, or we do not have adequate safety stock in times of delivery delays, our operating results could be adversely affected.

If our assembly and test supply contractors experience quality or yield problems, we may face a shortage of products available for sale.

We rely on contractors to assemble and test our devices with acceptable quality and yield levels. As is common in our industry, we have experienced quality and yield problems in the past. The majority of our revenue is derived from semiconductor devices assembled in advanced packages. The assembly of advanced packages is a complex process requiring:

- a high degree of technical skill;
- state-of-the-art equipment;
- the absence of defects in assembly and packaging manufacturing;
- the elimination of raw material impurities and errors in each step of the process; and
- effective cooperation between the assembly contractor and us.

As a result, our contractors may experience difficulties in achieving acceptable quality and yield levels when assembling and testing our semiconductor devices. If we experience prolonged quality or yield problems in the future and we do not have adequate levels of safety stock inventory on-hand, our operating results could be adversely affected.

Our wafer supply, which is sourced entirely from the Asia Pacific region, could be interrupted, could experience increased costs or could be reduced, which may result in a shortage of products available for sale or increased costs.

We do not manufacture finished silicon wafers and most of our products, including all of our newest products, are manufactured by a sole source. Currently, our silicon wafers are manufactured by Fujitsu in Japan, Seiko Epson Corporation in Japan, United Microelectronics Corporation in Taiwan and GLOBALFOUNDRIES in Singapore. If any of our current or future foundry partners significantly interrupts or reduces our wafer supply, increases wafer costs, or if any of our relationships with our partner suppliers are terminated, our operating results could be adversely affected.

In the past, we have experienced delays in obtaining wafers and in securing supply commitments from our foundry partners. At present, we anticipate that our supply commitments are adequate. However, these existing supply commitments may not be sufficient for us to satisfy customer demand in future periods. Additionally, notwithstanding our supply commitments, we may still have difficulty in obtaining wafer deliveries consistent with the supply commitments. We negotiate wafer prices and supply commitments from our suppliers on at least an annual basis. If any of our foundry partners were to reduce its supply commitment or increase its wafer prices, and we cannot find alternative sources of wafer supply, our operating results could be adversely affected.

Many other factors that could disrupt our wafer supply are beyond our control. Since worldwide manufacturing capacity (and that of Fujitsu) for silicon wafers is limited and inelastic, we could be harmed by significant industry-wide (or our own) increases in overall wafer demand or interruptions in wafer supply, or periods of increased wafer prices. During periods of economic uncertainty, our foundry partners may reduce or restructure their operations which may also affect the availability and price of wafers, and adversely affect our operating results. Additionally, a future disruption of any of our foundry partners' foundry operations as a result of a fire, earthquake, act of terrorism, political unrest, governmental uncertainty, war, disease or other natural disaster or catastrophic event could disrupt our wafer supply and could adversely affect our operating results.

Our supply of assembled and tested products, all from the Asia Pacific region, could be interrupted, could experience increased costs or could be reduced, which may result in a shortage of products available for sale or increased costs.

We do not assemble our finished products or perform all testing of our products. Our finished silicon wafers are assembled and tested by independent contractors located in Indonesia, Japan, Malaysia, the Philippines, Singapore and South Korea. Economic, financial, social and political conditions in Asia have historically been volatile. Financial difficulties, the

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effects of currency fluctuation, governmental actions or restrictions, prolonged work stoppages, political unrest, war, natural disaster, cost of assembly materials such as gold, disease or any other difficulties experienced by our suppliers may disrupt our supply and could adversely affect our operating results.

In the past, we have experienced delays in obtaining assembled and tested products and in securing assembly and test capacity commitments from our suppliers. At present, we anticipate that our assembly and test capacity commitments are adequate; however, these existing commitments may not be sufficient for us to satisfy customer demand in future periods. Additionally, notwithstanding our assembly and test capacity commitments, we may still have difficulty in obtaining deliveries of finished products consistent with the capacity commitments. We negotiate assembly and test prices and capacity commitments from our contractors on a periodic basis. If any of our assembly or test contractors were to reduce its capacity commitment or increase its prices, and we cannot find alternative sources, our operating results could be adversely affected.

Many other factors that could disrupt our supply of finished products are beyond our control. Because worldwide capacity for assembly and testing of semiconductor products is limited and inelastic, we could be harmed by significant industry-wide increases in overall demand or interruptions in supply. The assembly of complex packages requires a consistent supply of a variety of raw materials such as substrates, lead frames, gold and mold compound. The worldwide manufacturing capacity for these materials is also limited and inelastic. A significant industry-wide increase in demand, or interruptions in the supply of these materials to our assembly or test contractors, could adversely affect our operating results. Additionally, a future disruption of any of our assembly or test contractors' operations as a result of a fire, earthquake, flooding, act of terrorism, political unrest, governmental uncertainty, war, disease or other natural disaster or catastrophic event could disrupt our supply of assembled and tested devices and could adversely affect our operating results.

In addition, our quarterly revenue levels may be affected to a significant extent by our ability to match inventory and current production mix with the product mix required to fulfill orders. The large number of individual parts we sell and the large number of customers for our products, combined with limitations on our and our customers' ability to forecast orders accurately and our relatively lengthy manufacturing cycles, may make it difficult to achieve a match of inventory on hand, production units, and shippable orders sufficient to realize quarterly or annual revenue projections.

We may experience a disruption of our business activities due to the transition to a new Chief Executive Officer.

On October 12, 2010, the Company's Board of Directors announced the appointment of Darin G. Billerbeck as the Company's President and Chief Executive Officer, effective November 8, 2010. We may experience disruption in our business activities as we transition to a new chief executive officer, and our relationships with employees, customers and suppliers could be adversely affected by these disruptions. In addition, our competitors may seek to use this transition and the related potential disruptions to gain a competitive advantage over us. Our future operating results depend substantially upon the continued service of our key personnel, our ability to attract and retain qualified management personnel. Our business, financial condition and results of operations could be materially adversely affected by the loss of any of our key employees, by the failure of any key employee to perform in his or her current position, or by our inability to attract and retain skilled employees.

An acquisition may harm our business, financial condition or operating results.

We have made acquisitions in the past to execute on our business strategy which create uncertainty to our future operating results and cash flows. We may acquire products, technologies or businesses from third parties. An acquisition will require considerable management time, may divert time away from operations, require substantial cash resources, require us to incur or assume debt, and involve the issuance of the Company's equity securities. On July 15, 2011, the Company completed the purchase of Rise Technology Development Limited ("Rise"), a Hong Kong company, and its subsidiary, APAC IC Layout Consultants, Inc. ("APAC IC"), a Manila, Philippines based

company engaged in engineering layout and design services, for approximately \$1.0 million, which includes all assets and liabilities of the entity. The acquisition of Rise and APAC IC is part of the Company's effort to improve its research and development and operations activities, reduce costs and streamline its supply chain for improved predictability and flexibility. In addition, the Company recorded Goodwill of \$0.9 million in connection with the purchase of Rise and APAC IC. There is no assurance that Goodwill will be deemed recoverable as a result of an impairment test. The success of any acquisition, including Rise and APAC IC, requires the integration of products, technologies, personnel and administrative resources, and could result in departures of key personnel, equity dilution or acquisition of unknown liabilities. As a result, an acquisition could disrupt our operations and may have an adverse effect on our business, financial condition or operating results.

If our independent software and hardware developers and suppliers are unable or unwilling to meet our contractual requirements, we may face a delay or shortage of the introduction of new products, or the support of existing products.

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We rely on independent software and hardware developers for the design, development, supply and support of IP cores, design and development software, and certain elements of evaluation boards. As a result, failure or significant delay to complete software or hardware under contract to deliver could disrupt the release of or introduction of new products, which might be detrimental to the capability of our new products to win designs. Any of these delays or inability to complete the design or development could have an adverse effect on our business, financial condition, or operating results.

We depend upon a third party to provide inventory management, order fulfillment, and direct sales logistics.

We rely on a third party vendor located in Singapore to provide cost-effective and efficient supply chain services. Among other activities, these outsourced services relate to direct sales logistics, including order fulfillment, inventory management and warehousing, and distribution of inventory to third party distributors. If our third party supply chain partner were to discontinue services for us or its operations are disrupted as a result of a fire, earthquake, act of terrorism, political unrest, governmental uncertainty, war, disease or other natural disaster or catastrophic event, our ability to fulfill direct sales orders and distribute inventory timely, cost effectively, or at all, would be hindered, which could adversely affect our business.

We may have failed to adequately insure against certain risks, and, as a result, our financial condition and results may be adversely affected.

We carry insurance customary for companies in our industry, including, but not limited to, liability, property and casualty, worker's compensation and business interruption insurance. We also insure our employees for basic medical expenses. In addition, we have insurance contracts that provide director and officer liability coverage for our directors and officers. Other than the specific areas mentioned above, we are self-insured with respect to most other risks and exposures, and the insurance we carry in many cases is subject to a significant policy deductible or other limitation before coverage applies. Based on management's assessment and judgment, we have determined that it is more cost effective to self-insure against certain risks than to incur the insurance premium costs. The risks and exposures for which we self-insure include, but are not limited to, natural disasters, product defects, political risk, theft, patent infringement and some employment practice matters. Should there be a catastrophic loss due to an uninsured event such as an earthquake or a loss due to adverse occurrences in any area in which we are self-insured, our financial condition or operating results could be adversely affected.

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

## 2(c). Issuer Purchases of Equity Securities

| Period                                | Total Number of Shares Purchased | Average Price paid Per Share | Total Number of Shares Purchased as Part of Publicly Announced Program | Maximum Dollar Value of Shares That May Yet Be Purchased Under the Program |
|---------------------------------------|----------------------------------|------------------------------|--|--|
| Month #1                              |                                  |                              |  |  |
| July 3, 2011 through July 30, 2011    | 181,400                          | \$6.24                       | 181,400  | \$8,920,000  |
| Month #2                              |                                  |                              |  |  |
| July 31, 2011 through August 27, 2011 | 284,000                          | \$5.51                       | 284,000  | \$7,357,000  |

| Month #3                                |         |        |         |             |
|---|---------|--------|---------|-------------|
| August 28, 2011 through October 1, 2011 | 385,400 | \$5.49 | 385,400 | \$5,240,000 |
| Total                                   | 850,800 | \$5.66 | 850,800 | \$5,240,000 |

On October 21, 2010, the Company's Board of Directors approved a stock repurchase program pursuant to which up to \$20.0 million of outstanding common stock may be repurchased from time to time. The duration of the repurchase program was twelve months. In connection with this stock repurchase program, the Company entered into a 10b5-1 plan. During the third quarter and first nine months of fiscal 2011, approximately 850,800 and 2,150,800 shares were repurchased for \$4.8 million and \$12.8 million, respectively. All shares repurchased under this program were retired by October 1, 2011. All

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repurchases were open market transactions and funded from available working capital. The number of shares that will be repurchased will depend on market conditions, including the price of the common stock. The program ended by its terms October 26, 2011.

ITEM 5. OTHER INFORMATION

On August 31, 2011, Byron W. Milstead, the Company's Corporate Vice President, General Counsel and Secretary, established a rule 10b5-1 plan for shares of the Company's common stock as part of a personal investment diversification strategy. Rule 10b5-1 requires, among other things, that a trading plan be established only at a time when the officer is not aware of material, non-public information. The plan specifies the term of the plan, which will expire August 31, 2012, the number of shares to be sold, and the times and prices at which shares may be sold. If all conditions of the plan are met, up to 113,114 shares may be sold under the plan, which would equal approximately 55% of the aggregate number of shares, including vested and unvested equity awards, that Mr. Milstead holds as of October 31, 2011.

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ITEM 6. EXHIBITS

| Exhibit<br>Number | Description  |
|-------------------|--|
| 3.1               | The Company's Restated Certificate of Incorporation filed February 24, 2004 (Incorporated by reference to Exhibit 3.1 filed with the Company's Annual Report on Form 10-K for the year ended January 3, 2004).   |
| 3.2               | The Company's Bylaws, as amended and restated as of January 31, 2006 (Incorporated by reference to Exhibit 99.1 filed with the Company's Current Report on Form 8-K filed February 3, 2006).   |
| 4.4               | Indenture, dated as of June 20, 2003, between the Company and U.S. Bank National Association (Incorporated by reference to Exhibit 4.1 filed with the Company's Registration Statement on Form S-3 on August 13, 2003).  |
| 4.5               | Form of Note for the Company's Zero Coupon Convertible Subordinated Notes (Incorporated by reference to Exhibit 4.2 filed with the Company's Registration Statement on Form S-3 on August 13, 2003).   |
| 10.23             | Advance Production Payment Agreement dated March 17, 1997 among Lattice Semiconductor Corporation and Seiko Epson Corporation and S MOS Systems, Inc. (Incorporated by reference to Exhibit 10.23 filed with the Company's Annual Report on Form 10-K for the fiscal year ended January 1, 2005)(1).                   |
| 10.24*            | Lattice Semiconductor Corporation 1996 Stock Incentive Plan, as amended, and Related Form of Option Agreement (Incorporated by reference to Exhibits (d)(1) and (d)(2) to the Company's Schedule TO filed on February 13, 2003).   |
| 10.33*            | 2001 Outside Directors' Stock Option Plan, as amended and restated effective May 1, 2007 (Incorporated by reference to the Appendix A filed with the Company's 2007 Definitive Proxy Statement on Schedule 14A filed on April 5, 2007).  |
| 10.34*            | 2001 Stock Plan, as amended, and related Form of Option Agreement (Incorporated by reference to Exhibits (d)(3) and (d)(4) to the Company's Schedule TO filed on February 13, 2003).   |
| 10.35             | Intellectual Property Agreement by and between Agere Systems Inc. and Agere Systems Guardian Corporation and Lattice Semiconductor Corporation as Buyer, dated January 18, 2002 (Incorporated by reference to Exhibit 10.35 filed with the Company's Annual Report on Form 10-K for the year ended December 29, 2001). |
| 10.37*            | Lattice Semiconductor Corporation Executive Deferred Compensation Plan, as amended and restated effective as of August 11, 1997 (Incorporated by reference to Exhibit 99.3 filed with the Company's Registration Statement on Form S-3, as amended, dated October 17, 2002).   |
| 10.38*            | Amendment No. 1, to the Lattice Semiconductor Corporation Executive Deferred Compensation Plan, as amended, dated November 19, 1999 (Incorporated by reference to Exhibit 99.4 filed with the Company's Registration Statement on Form S-3, as amended, dated October 17, 2002).                                       |
| 10.39             |  |



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Registration Rights Agreement, dated as of June 20, 2003, between the Company and the initial purchaser named therein (Incorporated by reference to Exhibit 4.3 filed with the Company's Registration Statement on Form S-3 on August 13, 2003).

- 10.41\* Form of Indemnification Agreement executed by each director and executive officer of the Company and certain other officers and employees of the Company and its subsidiaries (Incorporated by reference to Exhibit 10.41 filed with the Company's Annual Report on Form 10-K for the year ended January 3, 2004).
- 10.42 Amendment dated March 25, 2004 to Advance Production Payment Agreement dated March 17, 1997, as amended, among Lattice Semiconductor Corporation and Seiko Epson Corporation and S MOS Systems, Inc. (Incorporated by reference to Exhibit 10.42 filed with the Company's Quarterly Report on Form 10-Q for the quarter ended April 3, 2004)(1).
- 10.43 Advance Payment and Purchase Agreement dated September 10, 2004 between Lattice Semiconductor Corporation and Fujitsu Limited (Incorporated by reference to Exhibit 10.1 filed with the Company's Quarterly Report on Form 10-Q for the quarter ended October 2, 2004)(1).
- 10.44\* Employment Agreement between Lattice Semiconductor Corporation and Stephen A. Skaggs dated August 9, 2005 (Incorporated by reference to Exhibit 99.1 filed with the Company's Current Report on Form 8-K filed on August 12, 2005).
- 10.45\* Compensation Arrangement between Lattice Semiconductor Corporation and Patrick S. Jones, Chairman of the Board of Directors (Incorporated by reference to Exhibit 99.2 filed with the Company's Current Report on Form 8-K filed on August 12, 2005).
- 10.46\* Employment Agreement between Lattice Semiconductor Corporation and Jan Johannessen dated November 1, 2005 (Incorporated by reference to Exhibit 10.1 filed with the Company's Quarterly Report on Form 10-Q filed on November 4, 2005).

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| Exhibit Number | Description   |
|----------------|---|
| 10.47*         | Employment Agreement between Lattice Semiconductor Corporation and Martin R. Baker dated November 1, 2005 (Incorporated by reference to Exhibit 10.2 filed with the Company's Quarterly Report on Form 10-Q filed on November 4, 2005).   |
| 10.48*         | Employment Agreement between Lattice Semiconductor Corporation and Stephen M. Donovan dated November 1, 2005 (Incorporated by reference to Exhibit 10.3 filed with the Company's Quarterly Report on Form 10-Q filed on November 4, 2005).  |
| 10.50*         | Compensation Arrangement between Lattice Semiconductor Corporation and Chairpersons for Committees of the Board of Directors (Incorporated by reference to Exhibit 99.1 filed with the Company's Current Report on Form 8-K filed on December 12, 2005).  |
| 10.51*         | Form of Amendment to Stock Option Agreements for 1996 Stock Incentive Plan, as amended, and 2001 Stock Plan, as amended (Incorporated by reference to Exhibit 99.3 filed with the Company's Current Report on Form 8-K filed on December 12, 2005).   |
| 10.52*         | 2006 Executive Bonus Plan (Incorporated by reference to Exhibit 99.4 filed with the Company's Current Report on Form 8-K filed on December 12, 2005).   |
| 10.53          | Addendum dated March 22, 2006 to the Advance Payment and Purchase Agreement dated September 10, 2004 between Lattice Semiconductor Corporation and Fujitsu Limited (Incorporated by reference to Exhibit 10.53 filed with the Company's Quarterly Report on Form 10-Q filed on November 7, 2006).                     |
| 10.54          | Addendum No. 2 dated effective October 1, 2006 to the Advance Payment and Purchase Agreement dated September 10, 2004 between Lattice Semiconductor Corporation and Fujitsu Limited (Incorporated by reference to Exhibit 10.54 filed with the Company's Quarterly Report on Form 10-Q filed on November 7, 2006)(1). |
| 10.55*         | 2007 Executive Variable Compensation Plan, as amended (Incorporated by reference to Exhibit 99.1 filed with the Company's Current Report on Form 8-K filed on December 7, 2006, as amended as described in the Company's Current Report on Form 8-K filed on February 8, 2007).                                       |
| 10.56*         | Form of Notice of Grant of Restricted Stock Units to Executive Officer (Incorporated by reference to Exhibit 99.1 filed with the Company's Current Report on Form 8-K filed on February 8, 2007).   |
| 10.57*         | 2008 Executive Variable Compensation Plan, as amended (Incorporated by reference to Exhibit 99.1 filed with the Company's Current Report on Form 8-K filed on December 7, 2007).  |
| 10.58*         | Letter Agreement between Lattice Semiconductor Corporation and Stephen A. Skaggs dated January 31, 2008 (Incorporated by reference to Exhibit 10.58 filed with the Company's Annual Report on Form 10-K filed on March 13, 2008).   |
| 10.59*         | Employment Agreement between Lattice Semiconductor Corporation and Bruno Guilmart dated May 14, 2008 (Incorporated by reference to Exhibit 99.1 filed with the Company's Current Report on Form 8-K filed on June 16, 2008).  |

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- 10.60\* Employment Agreement between Lattice Semiconductor Corporation and Byron Milstead dated May 14, 2008 (Incorporated by reference to Exhibit 10.60 filed with the Company's Current Report on Form 10-Q filed on August 8, 2008).
- 10.61\* Form of Inducement Stock Option Agreement (Incorporated by reference to Exhibit 10.61 filed with the Company's Current Report on Form 10-Q filed on November 5, 2008).
- 10.62\* Employment Agreement between Lattice Semiconductor Corporation and Michael G. Potter dated February 4, 2009 (Incorporated by reference to Exhibit 99.2 filed with the Company's Current Report on Form 8-K filed on February 4, 2009).
- 10.63\* 2009 Bonus Plan of Lattice Semiconductor Corporation (Incorporated by reference to Exhibit 10.63 filed with the Company's Annual Report on Form 10-K filed on March 13, 2009).
- 10.64 Addendum #4 dated effective December 18, 2009 to the Advanced Payment and Purchase Agreement dated September 10, 2004 between Lattice Semiconductor Corporation and Fujitsu Limited (Incorporated by reference to Exhibit 10.64 filed with the Company's Annual Report on Form 10-K filed on March 13, 2009).
- 10.65 Letter Agreement effective December 18, 2008 re Repayment of Advance Payment between Lattice Semiconductor Corporation and Fujitsu Microelectronics Limited and Fujitsu Microelectronics America, Inc. (Incorporated by reference to Exhibit 10.65 filed with the Company's Annual Report on Form 10-K filed on March 13, 2009).

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| Exhibit<br>Number | Description  |
|-------------------|--|
| 10.66*            | Employment Agreement between Lattice Semiconductor Corporation and Byron Milstead effective as of December 30, 2008 (Incorporated by reference to Exhibit 10.66 filed with the Company's Annual Report on Form 10-K filed on March 13, 2009).                  |
| 10.67*            | Employment Agreement between Lattice Semiconductor Corporation and Sean Riley dated September 22, 2008 (Incorporated by reference to Exhibit 10.67 filed with the Company's Current Report on Form 10-Q filed on May 8, 2009).                                 |
| 10.68*            | Employment Agreement between Lattice Semiconductor Corporation and Christopher M. Fanning amended and restated as of December 15, 2008 (Incorporated by reference to Exhibit 10.68 filed with the Company's Current Report on Form 10-Q filed on May 8, 2009). |
| 10.69*            | Lattice Semiconductor Corporation 2010 Cash Incentive Compensation Plan (Incorporated by reference to Exhibit 10.69 filed with the Company's Annual Report on Form 10-K filed on March 10, 2010).  |
| 10.70*            | Employment Agreement between Lattice Semiconductor Corporation and Darin G. Billerbeck dated as of November 8, 2010.   |
| 10.71*            | Employment Agreement between Lattice Semiconductor Corporation and Joe Bedewi dated as of April 11, 2011.  |
| 31.1              | Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.  |
| 31.2              | Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.  |
| 32.1              | Certification of Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.   |
| 32.2              | Certification of Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.   |
| 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 Labels Linkbase Document   |
| 101.PRE           | XBRL Taxonomy Extension Presentation Linkbase Document   |
| (1)               | Pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, confidential treatment has been granted to portions of this exhibit, which portions have been deleted and filed separately with the Securities and Exchange                                  |

Commission.

- \* Management contract or compensatory plan or arrangement required to be filed as an Exhibit to our Annual Report on Form 10-K pursuant to Item 15(b) thereof.

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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.

LATTICE SEMICONDUCTOR CORPORATION  
(Registrant)

/s/ JOE BEDEWI  
JOE BEDEWI  
Corporate Vice President and Chief Financial Officer  
(Duly Authorized Officer and Principal Financial  
and Accounting Officer)

Date: November 4, 2011