

SILICON LABORATORIES INC
Form 10-Q
October 26, 2016
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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, 2016

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: 000-29823

SILICON LABORATORIES INC.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

74-2793174

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

400 West Cesar Chavez, Austin, Texas

(Address of principal executive offices)

78701

(Zip Code)

(512) 416-8500

(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

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

As of October 18, 2016, 41,747,783 shares of common stock of Silicon Laboratories Inc. were outstanding.

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Cautionary Statement

Except for the historical financial information contained herein, the matters discussed in this report on Form 10-Q (as well as documents incorporated herein by reference) may be considered 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. Such forward-looking statements include declarations regarding the intent, belief or current expectations of Silicon Laboratories Inc. and its management and may be signified by the words believe, estimate, expect, intend, anticipate, plan, project, will or similar language. You are cautioned that any such

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forward-looking statements are not guarantees of future performance and involve a number of risks and uncertainties. Actual results could differ materially from those indicated by such forward-looking statements. Factors that could cause or contribute to such differences include those discussed under Risk Factors and elsewhere in this report. Silicon Laboratories disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

Table of Contents**Part I. Financial Information****Item 1. Financial Statements****Silicon Laboratories Inc.****Condensed Consolidated Balance Sheets****(In thousands, except per share data)****(Unaudited)**

	October 1, 2016	January 2, 2016
Assets		
Current assets:		
Cash and cash equivalents	\$ 148,195	\$ 114,085
Short-term investments	131,139	128,901
Accounts receivable, net	84,923	73,601
Inventories	55,051	53,895
Prepaid expenses and other current assets	49,087	52,658
Total current assets	468,395	423,140
Long-term investments	6,980	7,126
Property and equipment, net	130,318	131,132
Goodwill	272,722	272,722
Other intangible assets, net	100,320	121,354
Other assets, net	51,481	55,989
Total assets	\$ 1,030,216	\$ 1,011,463
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	\$ 39,591	\$ 42,127
Current portion of long-term debt		10,000
Accrued expenses	51,561	52,131
Deferred income on shipments to distributors	47,057	35,448
Income taxes	5,638	2,615
Total current liabilities	143,847	142,321
Long-term debt	72,500	67,500
Other non-current liabilities	26,240	40,528
Total liabilities	242,587	250,349
Commitments and contingencies		
Stockholders equity:		
Preferred stock \$0.0001 par value; 10,000 shares authorized; no shares issued and outstanding		
Common stock \$0.0001 par value; 250,000 shares authorized; 41,651 and 41,727 shares issued and outstanding at October 1, 2016 and January 2, 2016, respectively	4	4
Additional paid-in capital	6,344	13,868
Retained earnings	781,890	747,749

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Accumulated other comprehensive loss	(609)	(507)
Total stockholders' equity	787,629	761,114
Total liabilities and stockholders' equity	\$ 1,030,216	\$ 1,011,463

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

Table of Contents**Silicon Laboratories Inc.****Condensed Consolidated Statements of Income****(In thousands, except per share data)****(Unaudited)**

	Three Months Ended		Nine Months Ended	
	October 1, 2016	October 3, 2015	October 1, 2016	October 3, 2015
Revenues	\$ 178,083	\$ 156,194	\$ 515,016	\$ 484,755
Cost of revenues	69,880	62,759	202,988	197,523
Gross margin	108,203	93,435	312,028	287,232
Operating expenses:				
Research and development	48,437	46,483	149,118	140,805
Selling, general and administrative	38,034	35,729	116,716	118,989
Operating expenses	86,471	82,212	265,834	259,794
Operating income	21,732	11,223	46,194	27,438
Other income (expense):				
Interest income	331	186	880	544
Interest expense	(643)	(687)	(1,939)	(2,160)
Other, net	(58)	(280)	(431)	218
Income before income taxes	21,362	10,442	44,704	26,040
Provision for income taxes	1,344	467	3,319	2,112
Net income	\$ 20,018	\$ 9,975	\$ 41,385	\$ 23,928
Earnings per share:				
Basic	\$ 0.48	\$ 0.24	\$ 0.99	\$ 0.56
Diluted	\$ 0.47	\$ 0.23	\$ 0.98	\$ 0.55
Weighted-average common shares outstanding:				
Basic	41,614	42,331	41,673	42,522
Diluted	42,307	42,795	42,263	43,135

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

Table of Contents**Silicon Laboratories Inc.****Condensed Consolidated Statements of Comprehensive Income****(In thousands)****(Unaudited)**

	Three Months Ended		Nine Months Ended	
	October 1, 2016	October 3, 2015	October 1, 2016	October 3, 2015
Net income	\$ 20,018	\$ 9,975	\$ 41,385	\$ 23,928
Other comprehensive income (loss), before tax				
Net changes to available-for-sale securities				
Unrealized gains (losses) arising during the period	(84)	154	(137)	(179)
Reclassification for losses included in net income				10
Net changes to cash flow hedges				
Unrealized gains (losses) arising during the period	202	(459)	(211)	(1,035)
Reclassification for losses included in net income	64	165	191	376
Other comprehensive income (loss), before tax	182	(140)	(157)	(828)
Provision (benefit) for income taxes	63	(50)	(55)	(291)
Other comprehensive income (loss)	119	(90)	(102)	(537)
Comprehensive income	\$ 20,137	\$ 9,885	\$ 41,283	\$ 23,391

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

Table of Contents**Silicon Laboratories Inc.****Condensed Consolidated Statements of Cash Flows****(In thousands)****(Unaudited)**

	Nine Months Ended	
	October 1, 2016	October 3, 2015
Operating Activities		
Net income	\$ 41,385	\$ 23,928
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation of property and equipment	9,912	9,293
Amortization of other intangible assets and other assets	21,461	21,686
Stock-based compensation expense	30,057	30,798
Income tax benefit (shortfall) from stock-based awards	(1,238)	1,727
Excess income tax benefit from stock-based awards	(373)	(2,118)
Deferred income taxes	(1,460)	1,571
Changes in operating assets and liabilities:		
Accounts receivable	(11,322)	12,097
Inventories	(1,558)	2,259
Prepaid expenses and other assets	7,404	8,409
Accounts payable	1,280	(5,686)
Accrued expenses	8,930	(280)
Deferred income on shipments to distributors	11,573	(2,825)
Income taxes	1,459	(3,413)
Other non-current liabilities	(10,891)	(10,031)
Net cash provided by operating activities	106,619	87,415
Investing Activities		
Purchases of available-for-sale investments	(131,741)	(55,433)
Sales and maturities of available-for-sale investments	129,511	136,262
Purchases of property and equipment	(8,545)	(7,281)
Purchases of other assets	(4,994)	(5,291)
Acquisition of business, net of cash acquired		(76,899)
Net cash used in investing activities	(15,769)	(8,642)
Financing Activities		
Proceeds from issuance of long-term debt, net		81,238
Payments on debt	(5,000)	(92,206)
Repurchases of common stock	(40,543)	(71,448)
Payment of taxes withheld for vested stock awards	(10,521)	(12,652)
Proceeds from the issuance of common stock	8,451	12,575
Excess income tax benefit from stock-based awards	373	2,118
Payment of acquisition-related contingent consideration	(9,500)	(4,464)
Net cash used in financing activities	(56,740)	(84,839)
Increase (decrease) in cash and cash equivalents	34,110	(6,066)
Cash and cash equivalents at beginning of period	114,085	141,706
Cash and cash equivalents at end of period	\$ 148,195	\$ 135,640

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

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Silicon Laboratories Inc.

Notes to Condensed Consolidated Financial Statements

(Unaudited)

1. Significant Accounting Policies

Basis of Presentation and Principles of Consolidation

The Condensed Consolidated Financial Statements included herein are unaudited; however, they contain all normal recurring accruals and adjustments which, in the opinion of management, are necessary to present fairly the condensed consolidated financial position of Silicon Laboratories Inc. and its subsidiaries (collectively, the Company) at October 1, 2016 and January 2, 2016, the condensed consolidated results of its operations for the three and nine months ended October 1, 2016 and October 3, 2015, the Condensed Consolidated Statements of Comprehensive Income for the three and nine months ended October 1, 2016 and October 3, 2015, and the Condensed Consolidated Statements of Cash Flows for the nine months ended October 1, 2016 and October 3, 2015. All intercompany balances and transactions have been eliminated in consolidation. The condensed consolidated results of operations for the three and nine months ended October 1, 2016 are not necessarily indicative of the results to be expected for the full year.

The accompanying unaudited Condensed Consolidated Financial Statements do not include certain footnotes and financial presentations normally required under U.S. generally accepted accounting principles (GAAP). Therefore, these Condensed Consolidated Financial Statements should be read in conjunction with the audited Consolidated Financial Statements and notes thereto for the year ended January 2, 2016, included in the Company's Form 10-K filed with the Securities and Exchange Commission (SEC) on February 5, 2016.

The Company prepares financial statements on a 52- or 53-week fiscal year that ends on the Saturday closest to December 31. Fiscal 2016 will have 52 weeks and fiscal 2015 had 52 weeks. In a 52-week year, each fiscal quarter consists of 13 weeks.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Among the significant estimates affecting the financial statements are those related to inventories, stock-based compensation, investments in auction-rate securities, acquired intangible assets, goodwill, long-lived assets and income taxes. Actual results could differ from those estimates, and such differences could be material to the financial statements.

Reclassifications

Certain reclassifications have been made to prior year financial statements to conform to current year presentation.

Revenue Recognition

Revenues are generated predominately by sales of the Company's products. The Company recognizes revenue when all of the following criteria are met: 1) there is persuasive evidence that an arrangement exists, 2) delivery of goods has occurred, 3) the sales price is fixed or determinable, and 4) collectibility is reasonably assured. Generally, revenue from product sales to direct customers and contract manufacturers is recognized upon shipment.

A portion of the Company's sales are made to distributors under agreements allowing certain rights of return and price protection related to the final selling price to the end customers. Accordingly, the Company defers revenue and cost of revenue on such sales until the distributors sell the product to the end customers. The net balance of deferred revenue less deferred cost of revenue associated with inventory shipped to a distributor but not yet sold to an end customer is recorded in the deferred income on shipments to distributors liability on the Consolidated Balance Sheet. Such net deferred income balance reflects the Company's estimate of the impact of rights of return and price protection.

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Silicon Laboratories Inc.

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

A small portion of the Company's revenues is derived from the sale of patents. The above revenue recognition criteria for patent sales are generally met upon the execution of the patent sale agreement.

Recent Accounting Pronouncements

In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*. This ASU provides guidance on statement of cash flows presentation for eight specific cash flow issues where diversity in practice exists. This ASU is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. The Company is currently evaluating the effect that the adoption of this ASU will have on its financial statements.

In June 2016, the FASB issued ASU No. 2016-13, *Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. This ASU requires instruments measured at amortized cost to be presented at the net amount expected to be collected. Entities are also required to record allowances for available-for-sale debt securities rather than reduce the carrying amount. This ASU is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The Company is currently evaluating the effect that the adoption of this ASU will have on its financial statements.

In March 2016, the FASB issued ASU No. 2016-09, *Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting*. This ASU simplifies several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities and classification on the statement of cash flows. This ASU is effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. The Company is currently evaluating the effect that the adoption of this ASU will have on its financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*. The core principle of Topic 842 is that a lessee should recognize the assets and liabilities that arise from leases. For operating leases, a lessee is required to recognize a right-of-use asset and a lease liability, initially measured at the present value of the lease payments, in the statement of financial position. This ASU is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The Company is currently evaluating the effect that the adoption of this ASU will have on its financial statements.

In January 2016, the FASB issued ASU No. 2016-01, *Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. This ASU addresses certain aspects of recognition, measurement, presentation and disclosure of financial instruments. This ASU is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The Company is currently evaluating the effect that the adoption of this ASU will have on its financial statements.

In July 2015, the FASB issued ASU No. 2015-11, *Inventory (Topic 330): Simplifying the Measurement of Inventory*. This ASU requires inventory to be measured at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. This ASU is effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. The Company does not expect that the adoption of this ASU will have a material impact on its financial statements.

Table of Contents**Silicon Laboratories Inc.****Notes to Condensed Consolidated Financial Statements (Continued)****(Unaudited)**

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which supersedes the revenue recognition requirements in ASC 605, *Revenue Recognition*. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The guidance provides a five-step process to achieve that core principle. In August 2015, the FASB issued ASU No. 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, which deferred the effective date of ASU 2014-09 to annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. In 2016, the FASB issued the following amendments to ASC 606: ASU No. 2016-08, *Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)*, which clarifies the implementation guidance on principal versus agent considerations; ASU No. 2016-10, *Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing*, which clarifies guidance on identification of performance obligations and licensing implementation; and ASU No. 2016-12, *Compensation Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients*, which provides clarifying guidance on assessing collectibility, presentation of sales taxes, noncash consideration, contract modifications and completed contracts. The Company is currently evaluating the effect that the adoption of these ASUs will have on its financial statements.

2. Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per share (in thousands, except per share data):

	Three Months Ended		Nine Months Ended	
	October 1, 2016	October 3, 2015	October 1, 2016	October 3, 2015
Net income	\$ 20,018	\$ 9,975	\$ 41,385	\$ 23,928
Shares used in computing basic earnings per share	41,614	42,331	41,673	42,522
Effect of dilutive securities:				
Stock options and other stock-based awards	693	464	590	613
Shares used in computing diluted earnings per share	42,307	42,795	42,263	43,135
Earnings per share:				
Basic	\$ 0.48	\$ 0.24	\$ 0.99	\$ 0.56
Diluted	\$ 0.47	\$ 0.23	\$ 0.98	\$ 0.55

For the three months ended October 1, 2016 and October 3, 2015 and the nine months ended October 1, 2016 and October 3, 2015, approximately 0.1 million, 0.1 million, 0.2 million and 0.1 million shares, respectively, consisting of restricted stock awards (RSUs), market stock awards (MSUs) and stock options, were not included in the diluted earnings per share calculation since the shares were anti-dilutive.

Table of Contents**Silicon Laboratories Inc.****Notes to Condensed Consolidated Financial Statements (Continued)****(Unaudited)****3. Fair Value of Financial Instruments**

The fair values of the Company's financial instruments are recorded using a hierarchical disclosure framework based upon the level of subjectivity of the inputs used in measuring assets and liabilities. The three levels are described below:

Level 1 - Inputs are unadjusted, quoted prices in active markets for identical assets or liabilities at the measurement date.

Level 2 - Inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 - Inputs are unobservable for the asset or liability and are developed based on the best information available in the circumstances, which might include the Company's own data.

The following summarizes the valuation of the Company's financial instruments (in thousands). The tables do not include either cash on hand or assets and liabilities that are measured at historical cost or any basis other than fair value.

Description	Fair Value Measurements at October 1, 2016 Using			Total
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Assets:				
Cash equivalents:				
Money market funds	\$ 36,200	\$	\$	\$ 36,200
Certificates of deposit		2,956		2,956
Municipal bonds		301		301
Total cash equivalents	\$ 36,200	\$ 3,257	\$	\$ 39,457
Short-term investments:				
Municipal bonds	\$	\$ 60,682	\$	\$ 60,682
Corporate bonds		22,306		22,306
Variable-rate demand notes		15,324		15,324

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U.S. government bonds		14,392				14,392
Asset-backed securities				10,961		10,961
Commercial paper				6,466		6,466
International government bonds				1,008		1,008
Total short-term investments	\$	14,392	\$	116,747	\$	\$ 131,139
Long-term investments:						
Auction rate securities	\$		\$		\$ 6,980	\$ 6,980
Total long-term investments	\$		\$		\$ 6,980	\$ 6,980
Other assets, net:						
Derivative instruments	\$		\$	72	\$	\$ 72
Total	\$		\$	72	\$	\$ 72
Total	\$	50,592	\$	120,076	\$	6,980 \$ 177,648

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Silicon Laboratories Inc.

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Description	Fair Value Measurements at January 2, 2016 Using			Total
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Assets:				
Cash equivalents:				
Money market funds	\$ 37,721	\$	\$	\$ 37,721
Commercial paper		11,272		11,272
Certificates of deposit		2,845		2,845
U.S. government agency		1,599		1,599
Municipal bonds		1,577		1,577
Total cash equivalents	\$ 37,721	\$ 17,293	\$	\$ 55,014
Short-term investments:				
Municipal bonds	\$	\$ 93,516	\$	\$ 93,516
Commercial paper		11,176		11,176
Variable-rate demand notes		8,995		8,995
Certificates of deposit		8,000		8,000
U.S. government agency		3,998		3,998
International government bonds		2,220		2,220
Corporate bonds		996		996
Total short-term investments	\$	\$ 128,901	\$	\$ 128,901
Long-term investments:				
Auction rate securities	\$	\$	\$ 7,126	\$ 7,126
Total long-term investments	\$	\$	\$ 7,126	\$ 7,126
Other assets, net:				
Derivative instruments	\$	\$ 92	\$	\$ 92
Total	\$	\$ 92	\$	\$ 92
Total	\$ 37,721	\$ 146,286	\$ 7,126	\$ 191,133
Liabilities:				