MICROSEMI CORP
Form 10-Q
February 08, 2008

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

ý **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the Quarterly Period Ended December 30, 2007

or

o **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the transition period from to
Commission File No. 0-08866

MICROSEMI CORPORATION

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**95-2110371** (I.R.S. Employer Identification No.)
2381 Morse Avenue, Irvine, California (Address of principal executive offices)	**92614** (Zip Code)

(949) 221-7100

(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 twelve 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 ý No o

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

Large accelerated filer ý Accelerated filer o Non-accelerated filer o

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

The number of shares of the issuer's Common Stock, $0.20 par value, outstanding on January 25, 2008 was 78,195,606.

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IMPORTANT FACTORS RELATED TO FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of the federal securities laws. Any statements that do not relate to historical or current facts or matters are forward-looking statements. You can identify some of the forward-looking statements by the use of forward-looking words, such as "may," "will," "could," "should," "project," "believe," "anticipate," "expect," "plan," "estimate," "forecast," "potential," "intend," "maintain," "continue" and variations of these words and comparable words. In addition, all of the information herein that does not state a historical fact is forward-looking, including any statement or implication about an estimate or a judgment, or an expectation as to a future time, future result or other future circumstance. Statements concerning current conditions may also be forward-looking if they imply a continuation of current conditions. Examples of forward-looking statements in this Form 10-Q include, but are not limited to, statements concerning:

- expectations that we will be able to successfully complete announced and to-be-announced plant consolidations on the anticipated schedules and without unanticipated costs or expenses, and that such consolidations will result in anticipated cost savings;
- demand, growth and sales expectations for our products, including in the commercial air / space, defense, implantable medical, mobile / connectivity, and notebook / LCD television / display end markets;
- expectations regarding competitive conditions within the analog, mixed-signal and discrete semi-conductor, integrated circuit or custom component assembly industries;
- new market opportunities and emerging applications for our products;
- expected impact of our price position program;
- expectations regarding the effects of seasonality;
- expectations regarding the supply of raw materials;
- beliefs that our customers will not cancel orders or terminate or renegotiate their purchasing relationships with us;
- beliefs that we will be able to successfully resolve any disputes and other business matters as anticipated;
- our belief that we will be able to meet our current operating cash and debt service requirements;
- our critical accounting estimates;
- our tax exposure and tax rates; and
- our expected financial and operating results.

Forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from the results that the forward-looking statements suggest. You are urged to carefully review the disclosures we make in this report concerning risks and other factors that may affect our business and operating results, including those made under the heading "ITEM 1A. RISK FACTORS" included below in this Quarterly Report on Form 10-Q, as well as in our other reports filed with the Securities and Exchange Commission ("SEC"). Forward-looking statements are not a guarantee of future performance and should not be regarded as a representation by us or any other person that all of our estimates shall necessarily prove correct or that all of our objectives or plans shall necessarily be achieved. You are, therefore, cautioned not to place undue reliance on these forward-looking statements, which are made only as of the date of this report. We do not intend, and undertake no obligation, to update or revise the forward-looking statements to reflect events or circumstances after the date of this report, whether as a result of new information, future events or otherwise.

PART I FINANCIAL INFORMATION

Item 1. FINANCIAL STATEMENTS

This Form 10-Q must be read in its entirety. The unaudited consolidated income statement for the quarter ended December 30, 2007 of Microsemi Corporation and Subsidiaries (which we herein sometimes refer to collectively as "Microsemi", "the Company", "we", "our", "ours" or "us"), the unaudited consolidated statement of cash flows for the quarter ended December 30, 2007, and the comparative unaudited consolidated financial information for the corresponding period of the prior year, together with the unaudited balance sheets as of September 30, 2007 and December 30, 2007 are included herein.

MICROSEMI CORPORATION AND SUBSIDIARIES

Unaudited Consolidated Balance Sheets

(amounts in thousands, except per share data)

	December 30, 2007	September 30, 2007
ASSETS		
Current assets:		
Cash and cash equivalents	$ 105,263	$ 107,685
Accounts receivable, net of allowance for doubtful accounts of $1,329 and $1,424 at December 30, 2007 and September 30, 2007, respectively	87,037	81,035
Inventories	118,171	115,038
Deferred income taxes	16,882	14,315
Other current assets	15,272	10,843
Total current assets	342,625	328,916
Property and equipment, net	71,272	68,846
Deferred income taxes	4,550	742
Goodwill	179,094	177,668
Other intangible assets, net	55,817	54,714
Other assets	7,640	6,394
TOTAL ASSETS	$ 660,998	$ 637,280
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Current maturity of long-term liabilities	$ 724	$ 724
Accounts payable	26,002	25,923
Accrued liabilities	26,902	34,598
Total current liabilities	53,628	61,245
Long-term liabilities	17,411	6,630
Stockholders' equity:		
Preferred stock, $1.00 par value; authorized 1,000 shares; none issued		
Common stock, $0.20 par value; authorized 100,000 shares; issued and outstanding 78,180 and 77,154 at December 30, 2007 and September 30, 2007, respectively	15,636	15,431
Capital in excess of par value of common stock	441,300	429,277
Retained earnings	132,458	124,257
Accumulated other comprehensive income	565	440
Total stockholders' equity	589,959	569,405
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 660,998	$ 637,280

The accompanying notes are an integral part of these statements.

MICROSEMI CORPORATION AND SUBSIDIARIES

Unaudited Consolidated Income Statements

(amounts in thousands, except per share data)

	Quarter Ended	
	December 30, 2007	**December 31, 2006**
Net sales	$ 123,474	$ 102,289
Cost of sales	70,940	58,131
Gross profit	52,534	44,158
Operating expenses:		
Selling, general and administrative	26,761	18,425
Research and development	11,154	8,824
Amortization of intangible assets	3,099	2,003
Impairment of assets, restructuring and severance charges	42	903
In process research and development	440	
Total operating expenses	41,496	30,155
Operating income	11,038	14,003
Other income (expense):		
Interest income	1,119	1,482
Interest expense	(42)	(44)
Other, net	41	25
Total other income	1,118	1,463
Income before income taxes	12,156	15,466
Provision for income taxes	3,543	4,872
NET INCOME	$ 8,613	$ 10,594
Earnings per share:		
Basic	$ 0.11	$ 0.15
Diluted	$ 0.11	$ 0.14
Common and common equivalent shares outstanding:		
Basic	77,328	71,632
Diluted	79,645	73,425

The accompanying notes are an integral part of these statements.

MICROSEMI CORPORATION AND SUBSIDIARIES

Unaudited Consolidated Statements of Cash Flows

(amounts in thousands)

	Quarter Ended	
	December 30, 2007	**December 31, 2006**
Cash flows from operating activities:		
Net income	$ 8,613	$ 10,594
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	6,927	5,646
Stock based compensation	6,141	1,585
In process research and development	440	
Changes in assets and liabilities:		
Accounts receivable, net	(5,138)	(2,219)
Inventories, net	(2,054)	(6,802)
Other current assets	933	(3,661)
Deferred income taxes	(3,062)	(898)
Accounts payable	(392)	717
Accrued liabilities	(6,243)	(5,485)
Income taxes payable	1,515	2,955
Other long term liabilities	73	
Net cash provided by operating activities	7,753	2,432
Cash flows from investing activities:		
Purchases of property and equipment	(5,158)	(4,359)
Changes in other assets	(1,197)	(171)
Payments for acquisitions, net of cash acquired	(8,871)	
Net cash used in investing activities	(15,226)	(4,530)
Cash flows from financing activities:		
Payments of long-term liabilities		(58)
Excess tax benefit stock options	736	538
Exercise of stock options	4,315	1,539
Net cash provided by financing activities	5,051	2,019
Net decrease in cash and cash equivalents	(2,422)	(79)
Cash and cash equivalents at beginning of period	107,685	165,415
Cash and cash equivalents at end of period	$ 105,263	$ 165,336

The accompanying notes are an integral part of these statements.

MICROSEMI CORPORATION AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

December 30, 2007

1. PRESENTATION OF FINANCIAL INFORMATION

The unaudited consolidated financial statements include the accounts of Microsemi Corporation and its subsidiaries (which we herein sometimes refer to collectively as "Microsemi", the "Company", "we", "our", "ours" or "us"). Intercompany transactions have been eliminated in consolidation.

The financial information furnished herein is unaudited, but in the opinion of our management, includes all adjustments (all of which are normal, recurring adjustments) necessary for a fair statement of the results of operations for the periods indicated. The results of operations for the first quarter of the current fiscal year are not necessarily indicative of the results to be expected for the full year.

The accompanying unaudited consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q, and therefore do not include all information and note disclosures necessary for a fair presentation of financial position, results of operations and cash flows in conformity with generally accepted accounting principles. The unaudited consolidated financial statements and notes must be read in conjunction with the consolidated financial statements and notes thereto in the Annual Report on Form 10-K for the fiscal year ended September 30, 2007.

Critical Accounting Policies and Estimates

The unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States that require us to make estimates and assumptions that may materially affect the reported amounts of assets and liabilities at the date of the unaudited consolidated financial statements and revenues and expenses during the periods reported. Actual results could differ materially from those estimates. Information with respect to our critical accounting policies which we believe could have the most significant effect on our reported results and require subjective or complex judgments is contained in the notes to the consolidated financial statements in the Annual Report on Form 10-K for the fiscal year ended September 30, 2007.

Income Taxes

In July 2006 the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes An Interpretation of FASB Statement No. 109* ("FIN 48"). FIN 48 provides detailed guidance for the financial statement recognition, measurement and disclosure of uncertain tax positions recognized in an enterprise's financial statements in accordance with SFAS 109. Income tax positions must meet a more-likely-than-not recognition threshold at the effective date to be recognized upon the adoption of FIN 48 and in subsequent periods. We adopted FIN 48 effective October 1, 2007, and the provisions of FIN 48 will be applied to all income tax positions commencing from that date. We recognize potential accrued interest and penalties related to unrecognized tax benefits within operations as income tax expense.

As a result of applying the provisions of FIN 48, we recognized a $413,000 decrease to retained earnings, as of October 1, 2007. Our unrecognized tax benefits totaled $14,063,000 at October 1, 2007 and relate to various US and foreign jurisdictions. This amount included $358,000 of penalties and $1,112,000 of interest. Included in the balance at October 1, 2007 are $7,998,000 of tax benefits that if recognized would reduce our annual effective income tax rate. FIN 48 did not have a material effect on our financial condition, results of operations or cash flows during the quarter ended December 30,

MICROSEMI CORPORATION AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

December 30, 2007

1. PRESENTATION OF FINANCIAL INFORMATION (Continued)

2007. We currently expect our unrecognized tax benefits to decrease approximately $500,000 over the next 12 months.

We file U.S., state and foreign income tax returns in jurisdictions with varying statutes of limitation. The 2004 through 2006 tax years generally remain subject to examination by federal and most state tax authorities. In significant foreign jurisdictions, the 2003 through 2006 tax years generally remain subject to examination by tax authorities.

2. INVENTORIES

Inventories were as follows (amounts in thousands):

	December 30, 2007	September 30, 2007
Raw Materials	$ 44,596	$ 42,524
Work in Progress	46,706	44,467
Finished Goods	26,869	28,047
	$ 118,171	$ 115,038

3. GOODWILL AND OTHER INTANGIBLE ASSETS, NET

Goodwill and other intangible assets, net, were as follows (amounts in thousands):

	December 30, 2007	September 30, 2007
Goodwill	$ 179,094	$ 177,668
Other intangible assets, net		
Completed technology	$ 50,065	$ 47,869
Customer relationships	4,261	5,011
Backlog	99	355
Trade names	1,392	1,479
	$ 55,817	$ 54,714

4. COMMITMENTS AND CONTINGENCIES

We entered into a $75 million unsecured Revolving Credit Agreement dated as of December 29, 2006 with Comerica Bank (the "Revolving Credit Agreement" or the "New Credit Facility"). The New Credit Facility's Stated Maturity date is January 1, 2010. The New Credit Facility replaces the Company's existing $30 million Credit Agreement dated July 2, 1999, as amended, which had a Stated Maturity Date of March 31, 2008 ("Terminated Credit Agreement"). Proceeds of borrowing under the New Credit Facility can be used for working capital and other lawful corporate purposes, and initial borrowings were used to finance a portion of the Company's acquisition of PowerDsine Ltd. Interest accruing on the amount of each revolving borrowing under the New Credit Facility is determined based upon the Company's choice of either a Prime based Advance or Eurodollar based Advance. Prime

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MICROSEMI CORPORATION AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

December 30, 2007

4. COMMITMENTS AND CONTINGENCIES (Continued)

based Advances incur interest at a rate equal to the Prime Rate, as defined in the Revolving Credit Agreement, less 100 basis points. If the Company elects a Eurodollar based Advance, the borrowing bears interest at the Eurodollar based Rate, also defined in the Revolving Credit Agreement, which is determined, in part, by an Applicable Margin that fluctuates with the Company's Funded Debt to EBITDA ratio. Financial covenants, which include for example maintaining (i) a minimum EBITDA and (ii) a Maximum Funded Debt to EBITDA ratio, establish both conditions and current limitations on available amounts of borrowings. As of December 30, 2007, $75 million is the maximum that may be borrowed, but per the terms of the New Credit Facility, the maximum amount decreased to $60 million on January 2, 2008 and will decrease to $50 million on December 30, 2009. However, due to certain restrictions, the amount actually available to us for borrowing at any given time could be less than the amount stated. As of December 30, 2007, there were no amounts outstanding on the New Credit Facility and $0.4 million was outstanding in the form of a letter of credit and $74.6 million was available under the New Credit Facility. As of December 30, 2007, we were in compliance with the financial covenants required by our credit facility.

In Broomfield, Colorado, the owner of a property located adjacent to a manufacturing facility owned by Microsemi Corp. Colorado (the "Subsidiary") had notified the subsidiary and other parties, of a claim that contaminants migrated to his property, thereby diminishing its value. In August 1995, the subsidiary, together with Coors Porcelain Company, FMC Corporation and Siemens Microelectronics, Inc. (former owners of the manufacturing facility), agreed to settle the claim and to indemnify the owner of the adjacent property for remediation costs. Although TCE and other contaminants previously used by former owners at the facility are present in soil and groundwater on the subsidiary's property, we vigorously contest any assertion that the subsidiary caused the contamination. In November 1998, we signed an agreement with the three former owners of this facility whereby they have 1) reimbursed us for $530,000 of past costs, 2) assumed responsibility for 90% of all future clean-up costs, and 3) promised to indemnify and protect us against any and all third-party claims relating to the contamination of the facility. An Integrated Corrective Action Plan was submitted to the State of Colorado. Sampling and management plans were prepared for the Colorado Department of Public Health & Environment. State and local agencies in Colorado are reviewing current data and considering study and cleanup options. The most recent forecast estimated that the total project cost, up to the year 2020, would be approximately $5,300,000; accordingly, by assuming that this amount is accurate and that the indemnifying parties will pay 90% of this amount as agreed without need for us to incur material costs to enforce that agreement, we reserved for this contingency by recording a one-time charge of $530,000 for the life of this project in fiscal year 2003. There has not been any significant development since September 28, 2003.

We are involved in other normal litigation matters, arising out of the ordinary routine conduct of our business, including from time to time litigation relating to commercial transactions, contracts, and environmental matters. In the opinion of management, the final outcome of these matters will not have a material adverse effect on our financial position, results of operations or cash flows.