MACOM Technology Solutions Holdings, Inc.
Form 10-Q
May 03, 2018

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

FORM 10-Q

(Mark One)
ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 30, 2018
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: 001-35451

MACOM Technology Solutions Holdings, Inc.
(Exact name of registrant as specified in its charter)

Delaware	27-0306875
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

100 Chelmsford Street
Lowell, MA 01851
(Address of principal executive offices and zip code)
(978) 656-2500
(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 x No ¨
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, 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 x 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," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

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

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.¨

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

As of April 27, 2018, there were 64,706,145 shares of the registrant’s common stock outstanding.

MACOM TECHNOLOGY SOLUTIONS HOLDINGS, INC.
FORM 10-Q
TABLE OF CONTENTS

		Page No.
PART I—FINANCIAL INFORMATION		
Item 1.	Financial Statements (Unaudited)	1
	Condensed Consolidated Balance Sheets	1
	Condensed Consolidated Statements of Operations	2
	Condensed Consolidated Statements of Comprehensive Income (Loss)	3
	Condensed Consolidated Statement of Stockholders' Equity	4
	Condensed Consolidated Statements of Cash Flows	5
	Notes to Condensed Consolidated Financial Statements	6
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations	24
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	31
Item 4.	Controls and Procedures	32
PART II—OTHER INFORMATION		
Item 1.	Legal Proceedings	33
Item1A.	Risk Factors	33
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	35
Item 6.	Exhibits	36
Signatures		37

PART I—FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS
MACOM TECHNOLOGY SOLUTIONS HOLDINGS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands)
(Unaudited)

	March 30, 2018	September 29, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$162,695	$ 130,104
Short term investments	27,396	84,121
Accounts receivable (less allowances of $8,003 and $9,410, respectively)	107,093	136,096
Inventories	143,897	136,074
Income tax receivable	18,970	18,493
Assets held for sale	—	35,571
Prepaid and other current assets	15,158	22,438
Total current assets	$475,209	$ 562,897
Property and equipment, net	138,542	131,019
Goodwill	317,094	313,765
Intangible assets, net	584,035	621,092
Deferred income taxes	1,713	948
Other investments	37,415	—
Other long-term assets	7,162	7,402
TOTAL ASSETS	$1,561,170	$ 1,637,123
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Current portion of lease payable	$804	$ 815
Current portion of long-term debt	6,885	6,885
Accounts payable	29,224	47,038
Accrued liabilities	51,674	60,237
Liabilities held for sale	—	2,144
Total current liabilities	$88,587	$ 117,119
Lease payable, less current portion	23,586	17,275
Long-term debt, less current portion	659,921	661,471
Warrant liability	9,151	40,775
Deferred income taxes	15,975	15,172
Other long-term liabilities	5,684	7,937
Total liabilities	$802,904	$ 859,749
Stockholders' equity:		
Common stock	65	64
Treasury stock, at cost	(330)	(330)
Accumulated other comprehensive income	7,173	2,977
Additional paid-in capital	1,057,410	1,041,644
Accumulated deficit	(306,052)	(266,981)
Total stockholders' equity	$758,266	$ 777,374
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$1,561,170	$ 1,637,123

See notes to condensed consolidated financial statements.

1

MACOM TECHNOLOGY SOLUTIONS HOLDINGS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)
(Unaudited)

	Three Months Ended		Six Months Ended	
	March 30, 2018	March 31, 2017	March 30, 2018	March 31, 2017
Revenue	$150,414	$186,084	$281,338	$337,836
Cost of revenue	84,813	117,220	154,784	190,477
Gross profit	65,601	68,864	126,554	147,359
Operating expenses:				
Research and development	41,596	39,685	83,246	69,859
Selling, general and administrative	39,287	62,327	76,922	98,822
Impairment charges	6,575	—	6,575	—
Restructuring charges	1,539	469	6,200	1,757
Total operating expenses	88,997	102,481	172,943	170,438
Loss from operations	(23,396)	(33,617)	(46,389)	(23,079)
Other (expense) income				
Warrant liability gain (expense)	17,015	(2,573)	31,624	(7,395)
Interest expense, net	(7,970)	(7,374)	(15,209)	(14,724)
Other expense	(4,139)	(898)	(4,133)	(903)
Total other income (expense), net	4,906	(10,845)	12,282	(23,022)
Loss before income taxes	(18,490)	(44,462)	(34,107)	(46,101)
Income tax (benefit) expense	(3,024)	89,805	(1,671)	90,337
Loss from continuing operations	(15,466)	(134,267)	(32,436)	(136,438)
(Loss) income from discontinued operations	(18)	4,136	(5,617)	5,342
Net loss	$(15,484)	$(130,131)	$(38,053)	$(131,096)
Net (loss) income per share:				
Basic (loss) income per share:				
Loss from continuing operations	$(0.24)	$(2.21)	$(0.50)	$(2.38)
(Loss) income from discontinued operations	0.00	0.07	(0.09)	0.09
Loss per share - basic	$(0.24)	$(2.14)	$(0.59)	$(2.29)
Diluted (loss) income per share:				
Loss from continuing operations	$(0.50)	$(2.21)	$(0.98)	$(2.38)
(Loss) income from discontinued operations	0.00	0.07	(0.09)	0.09
Loss per share - diluted	$(0.50)	$(2.14)	$(1.07)	$(2.29)
Shares used:				
Basic	64,549	60,813	64,437	57,276
Diluted	65,132	60,813	65,120	57,276

See notes to condensed consolidated financial statements.

MACOM TECHNOLOGY SOLUTIONS HOLDINGS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(In thousands)
(Unaudited)

	Three Months Ended		Six Months Ended	
	March 30, 2018	March 31, 2017	March 30, 2018	March 31, 2017
Net loss	$(15,484)	$(130,131)	$(38,053)	$(131,096)
Unrealized (loss) gain on short term investments, net of tax	(247)	52	(514)	6
Foreign currency translation gain (loss), net of tax	4,421	3,567	4,710	(6,030)
Other comprehensive income (loss), net of tax	4,174	3,619	4,196	(6,024)
Total comprehensive (loss) income	$(11,310)	$(126,512)	$(33,857)	$(137,120)

See notes to condensed consolidated financial statements.

MACOM TECHNOLOGY SOLUTIONS HOLDINGS, INC.
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
(In thousands)
(Unaudited)

	Common Stock		Treasury Stock		Accumulated Other Comprehensive Income	Additional Paid-in Capital	Accumulated Deficit	Total Stockholders' Equity
	Shares	Amount	Shares	Amount				
Balance at September 29, 2017	64,279	$ 64	(23)	$ (330)	$ 2,977	$ 1,041,644	$ (266,981)	$ 777,374
Cumulative effect of ASU 2016-09	—	—	—	—	—	1,018	(1,018)	—
Stock options exercises	19	—	—	—	—	57	—	57
Vesting of restricted common stock and units	500	1	—	—	—	—	—	1
Issuance of common stock pursuant to employee stock purchase plan	114	—	—	—	—	3,195	—	3,195
Shares repurchased for stock withholdings on restricted stock awards	(184)	—	—	—	—	(3,846)	—	(3,846)
Share-based compensation	—	—	—	—	—	15,342	—	15,342
Other comprehensive income, net of tax	—	—	—	—	4,196	—	—	4,196
Net loss	—	—	—	—	—	—	(38,053)	(38,053)
Balance at March 30, 2018	64,728	$ 65	(23)	$ (330)	$ 7,173	$ 1,057,410	$ (306,052)	$ 758,266

See notes to condensed consolidated financial statements.

4

MACOM TECHNOLOGY SOLUTIONS HOLDINGS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Six Months Ended	
	March 30, 2018	March 31, 2017
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$(38,053)	$(131,096)
Adjustments to reconcile net loss to net cash provided by operating activities (net of acquisitions):		
Depreciation and intangibles amortization	54,439	40,097
Share-based compensation	15,342	17,731
Warrant liability (gain) expense	(31,624)	7,395
Acquired inventory step-up amortization	224	31,373
Deferred financing cost amortization	2,536	1,423
Acquisition prepaid compensation amortization	—	506
Loss on extinguishment of debt	—	871
Gain on disposition of business	—	(21,770)
Deferred income taxes	(573)	86,123
Impairment related charges	9,143	—
Loss on minority equity investment	4,085	—
Changes in assets held for sale from discontinued operations	(6,237)	—
Other adjustments, net	841	4,334
Change in operating assets and liabilities (net of acquisitions):		
Accounts receivable	28,992	(10,879)
Inventories	(9,240)	458
Prepaid expenses and other assets	749	1,358
Accounts payable	(11,438)	(2,219)
Accrued and other liabilities	(4,115)	(7,680)
Income taxes	(3,915)	2,814
Net cash provided by operating activities	11,156	20,839
CASH FLOWS FROM INVESTING ACTIVITIES:		
Acquisition of businesses, net	—	(229,423)
Purchases of property and equipment	(26,580)	(16,295)
Proceeds from sale of assets	—	215
Proceeds from sales and maturities of investments	77,853	19,037
Purchases of investments	(21,612)	(26,976)
Purchases of other investments	(5,000)	—
Payments associated with discontinued operations	(263)	21,770
Net cash provided by (used in) investing activities	24,398	(231,672)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from stock option exercises and employee stock purchases	3,252	2,688
Payments on notes payable	(3,442)	(3,026)
Payments of capital leases and assumed debt	(405)	(618)
Repurchase of common stock	(3,846)	(10,027)
Proceeds from corporate facility financing obligation	1,081	4,250
Payments of contingent consideration and other	—	(2,517)
Net cash used in financing activities	(3,360)	(9,250)

Foreign currency effect on cash	397	(279)
NET CHANGE IN CASH AND CASH EQUIVALENTS	32,591	(220,362)
CASH AND CASH EQUIVALENTS — Beginning of period	$130,104	$332,977
CASH AND CASH EQUIVALENTS — End of period	$162,695	$112,615
Supplemental disclosure of non-cash activities		
Issuance of common stock in connection with the AppliedMicro Acquisition (See Note 2 - Acquisitions)	$—	$465,082

See notes to condensed consolidated financial statements.

MACOM TECHNOLOGY SOLUTIONS HOLDINGS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Unaudited Interim Financial Information—The accompanying unaudited, condensed consolidated financial statements have been prepared according to the rules and regulations of the United States (the “U.S.”) Securities and Exchange Commission (“SEC”) and, in the opinion of management, reflect all adjustments, which include normal recurring adjustments, necessary for a fair statement of the condensed consolidated balance sheets, condensed consolidated statements of operations, condensed consolidated statement of comprehensive income (loss), condensed consolidated statements of stockholders' equity and condensed consolidated statements of cash flows of MACOM Technology Solutions Holdings, Inc. (“MACOM”, the “Company”, “us”, “we” or “our”) for the periods presented. We prepare our interim financial information using the same accounting principles we use for our annual audited consolidated financial statements. Certain information and note disclosures normally included in the annual audited consolidated financial statements have been condensed or omitted in accordance with prescribed SEC rules. We believe that the disclosures made in our condensed consolidated financial statements and the accompanying notes are adequate to make the information presented not misleading.

The consolidated balance sheet at September 29, 2017 is as reported in our audited consolidated financial statements as of that date. Our accounting policies are described in the notes to our September 29, 2017 consolidated financial statements, which were included in our Annual Report on Form 10-K for our fiscal year ended September 29, 2017 filed with the SEC on November 15, 2017 and our Quarterly Report on Form 10-Q for the fiscal quarter ended December 29, 2017 filed with the SEC on February 7, 2018. We recommend that the financial statements included in this Quarterly Report on Form 10-Q be read in conjunction with the consolidated financial statements and notes included in our Annual Report on Form 10-K for our fiscal year ended September 29, 2017.

Principles of Consolidation—We have one reportable segment, semiconductors and modules. The accompanying consolidated financial statements include our accounts and the accounts of our majority-owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

We have a 52 or 53-week fiscal year ending on the Friday closest to the last day of September. The fiscal years 2018 and 2017 include 52 weeks. To offset the effect of holidays, for fiscal years in which there are 53 weeks, we typically include the extra week arising in our fiscal years in the first quarter.

Use of Estimates—The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the U.S. requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities during the reporting periods, the reported amounts of revenue and expenses during the reporting periods, and the disclosure of contingent assets and liabilities at the date of the financial statements. On an ongoing basis, we base estimates and assumptions on historical experience, currently available information and various other factors that management believes to be reasonable under the circumstances. Actual results may differ materially from these estimates and assumptions.

Recent Accounting Pronouncements—Our Recent Accounting Pronouncements are described in the notes to our September 29, 2017 consolidated financial statements, which were included in our Annual Report on Form 10-K for our fiscal year ended September 29, 2017.

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update ("ASU") 2014-09, Revenue from Contracts with Customers ("Topic 606"). In March, April, May and December 2016, the FASB issued additional guidance related to Topic 606. The new standard will supersede nearly all existing revenue recognition guidance. Under Topic 606, an entity is required to recognize revenue upon transfer of promised goods or services to customers in an amount that reflects the expected consideration to be received in exchange for those goods or services. Topic 606 defines a five-step process in order to achieve this core principle, which may require the use of judgment and estimates, and also requires expanded qualitative and quantitative disclosures relating to the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers, including significant judgments and estimates used. The new standard also defines accounting for certain costs related to origination and fulfillment of contracts with customers, including whether such costs should be capitalized. The new standard permits adoption either by using (i) a full retrospective approach for all periods presented in the period of adoption or (ii) a modified retrospective approach where the new standard is applied in the financial statements starting with the year of adoption. Under both approaches, cumulative impact of the adoption is reflected as an adjustment to retained earnings (accumulated equity (deficit)) as of the earliest date presented in accordance with the new standard. In August 2015, the FASB issued ASU 2015-14, Revenue from Contracts with Customers: Deferral of the Effective Date, which delayed the effective date of the new standard from January 1, 2017 to January 1, 2018. We plan to implement the new guidance on September 29, 2018, the beginning of our next fiscal year, using the modified retrospective approach, applied to those contracts that were not completed as of that date. We are currently analyzing the impact of this new accounting standards update. We do not expect the adoption

of Topic 606 to have a material impact on our financial position and results of operations. As we continue our evaluation, we are also assessing any disclosure requirements and preparing to implement changes to accounting policies, business processes and internal controls to support the new standard.
In March 2016, the FASB issued ASU 2016-09, Compensation - Stock Compensation ("Topic 718"), which simplifies several aspects of the accounting for employee share-based payment transactions for both public and nonpublic entities. We adopted this ASU as of September 30, 2017. Prior to ASU 2016-09, the accounting for share-based compensation required forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. ASU 2016-09 allows an entity to make an entity-wide accounting policy election to either estimate the number of awards that are expected to vest or account for forfeitures when they occur. ASU 2016-09 requires an entity that elects to account for forfeitures when they occur to apply the accounting change on a modified retrospective basis as a cumulative-effect adjustment to retained earnings as of the date of adoption. We elected to account for forfeitures when they occur, and recorded a $1.0 million cumulative-effect adjustment to beginning retained earnings as of September 30, 2017. We did not record any adjustments to retained earnings for the tax effect of the adoption of ASU 2016-09 as we are in a full valuation allowance position against our U.S deferred tax asset. ASU 2016-09 requires all excess tax benefits and tax deficiencies to be recorded in the consolidated income statement on a prospective basis when the awards vest or are settled. Due to our full U.S. valuation allowance, ASU 2016-09 had no impact to our tax expense for the three and six months ended March 30, 2018.
2. ACQUISITIONS
Acquisition of Applied Micro Circuits Corporation— On January 26, 2017, we completed the acquisition of Applied Micro Circuits Corporation (“AppliedMicro”), a global provider of silicon solutions for next-generation cloud infrastructure and Cloud Data Centers, as well as connectivity products for edge, metro and long-haul communications equipment (the “AppliedMicro Acquisition”). We acquired AppliedMicro in order to expand our business in enterprise and Cloud Data Center applications. In connection with the AppliedMicro Acquisition, we acquired all of the outstanding common stock of AppliedMicro for total consideration of $695.4 million, which included cash paid of $287.1 million, less $56.8 million of cash acquired, and equity issued at a fair value of $465.1 million. In conjunction with the equity issued, we granted vested out-of-money stock options and unvested restricted stock units to replace outstanding vested out-of-money stock options and unvested restricted stock units of AppliedMicro. The total fair value of granted vested out-of-money stock options and unvested restricted stock units was $14.5 million, of which $9.3 million was attributable to pre-combination service and was included in the total consideration transferred. We funded the AppliedMicro Acquisition with cash on hand and short term investments. We recorded transaction costs related to the acquisition in selling, general and administrative expense. For the three and six months ended March 30, 2018, we recorded no transaction costs. For the three and six months ended March 31, 2017, we recorded transaction costs of $8.3 million and $11.8 million. The AppliedMicro Acquisition was accounted for as a stock purchase and the operations of AppliedMicro have been included in our consolidated financial statements since the date of acquisition. We recognized the AppliedMicro assets acquired and liabilities assumed based upon the fair value of such assets and liabilities measured as of the date of acquisition. The aggregate purchase price for AppliedMicro has been allocated to the tangible and identifiable intangible assets acquired and liabilities assumed based on their estimated fair value at the date of acquisition. The excess of the purchase price over the fair value of the acquired net assets represents cost and revenue synergies specific to the Company, as well as non-capitalizable intangible assets, such as the employee workforce acquired, and has been allocated to goodwill, none of which will be tax deductible.
In connection with the acquisition of AppliedMicro, we entered into a plan to divest a portion of AppliedMicro's business specifically related to its compute business (the "Compute business"). The divestiture of the Compute business was completed on October 27, 2017. See Note 3 - Discontinued Operations for further details of the divestiture.
The following table summarizes the total estimated acquisition consideration (in thousands):

Cash consideration paid to AppliedMicro common stockholders	$287,060
Common stock issued (9,544,125 shares of our common stock at $47.53 per share)	453,632
Equity consideration for vested "in the money" stock options and unvested restricted stock units	2,143

Fair value of the replacement equity awards attributable to pre-acquisition service	9,307
Total consideration paid, excluding cash acquired	$752,142

We finalized the purchase accounting during the fiscal quarter ended December 29, 2017. The final purchase price allocation is as follows (in thousands):

	Preliminary Allocation as of September 29, 2017	Allocation Adjustments	Adjusted Allocation December 29, 2017
Current assets	$ 70,434	$ (553)	$ 69,881
Intangible assets	412,848	—	412,848
Assets held for sale	40,944	—	40,944
Other assets	9,800	—	9,800
Total assets acquired	534,026	(553)	533,473
Liabilities assumed:			
Liabilities held for sale	4,444	—	4,444
Other liabilities	17,627	651	18,278
Total liabilities assumed	22,071	651	22,722
Net assets acquired	511,955	(1,204)	510,751
Consideration:			
Cash paid upon closing	230,298	—	230,298
Common stock issued	455,775	—	455,775
Equity instruments issued	9,307	—	9,307
Total consideration	$ 695,380	$ —	$ 695,380
Goodwill	$ 183,425	$ 1,204	$ 184,629

The components of the acquired intangible assets were as follows (in thousands):

	Included In Assets Held For Sale	Included in Retained Business	Useful Lives (Years)
Developed technology	$ 9,600	$78,448	7 years
Customer relationships	—	334,400	14 years
Total acquired intangible assets	$ 9,600	$412,848	

The overall weighted-average life of the identified intangible assets acquired in the AppliedMicro Acquisition is estimated to be 12.7 years and the assets are being amortized over their estimated useful lives based upon the pattern over which we expect to receive the economic benefit from these assets.

The following is a summary of AppliedMicro revenue and earnings included in our accompanying condensed consolidated statements of operations for the three months ended March 31, 2017 (in thousands):

	Three Months Ended March 31, 2017
Revenue	$36,445
Loss from continuing operations	(30,304)
Loss from discontinued operations	(16,430)

The pro forma statements of operations data for the six months ended March 31, 2017, below, give effect to the AppliedMicro Acquisition, described above, as if it had occurred at October 2, 2015. These amounts have been calculated after applying our accounting policies and adjusting the results of AppliedMicro to reflect transaction costs, retention compensation expense, the impact of the step-up to the value of acquired inventory, as well as the additional intangible amortization that would have been charged assuming the fair value adjustments had been applied and incurred since October 2, 2015. This pro forma data is presented for informational purposes only and does not purport to be indicative of our future results of operations.

	Six Months Ended March 31, 2017
Revenue	$394,792
Income from continuing operations	(84,543)
Loss from discontinued operations	(19,316)

Acquisition of Picometrix LLC— On August 9, 2017, we completed the acquisition of Picometrix LLC ("Picometrix"), a supplier of optical-to-electrical converters for Cloud Data Center infrastructure (the "Picometrix Acquisition"). We acquired Picometrix in order to expand our business in enterprise and Cloud Data Center applications. The purchase consideration was $33.5 million, comprised of an upfront cash payment of $29.5 million, and $4.0 million placed in escrow for potential satisfaction of certain indemnification obligations that may arise from the closing date through December 15, 2018. For the three and six months ended March 30, 2018, we recorded no transaction costs. The Picometrix Acquisition was accounted for as a business acquisition, and the operations of Picometrix have been included in our consolidated financial statements since the date of acquisition.

We recognized the Picometrix assets acquired and liabilities assumed based upon the fair value of such assets measured as of the date of acquisition. The aggregate purchase price for the Picometrix assets and liabilities has been allocated to the tangible and identifiable intangible assets acquired based on their estimated fair value at the date of acquisition. The excess of the purchase price over the fair value of the acquired assets represents cost and revenue synergies specific to the Company, as well as non-capitalizable intangible assets, such as the employee workforce acquired, and has been allocated to goodwill, all of which will be tax deductible.

The purchase accounting is preliminary and subject to completion including certain fair value measurements, particularly the finalization of the valuation assessment of the acquired tangible and intangible assets. The adjustments arising from the completion of the outstanding matters may materially affect the preliminary purchase accounting.

The preliminary allocation of purchase price as of March 30, 2018 is as follows (in thousands):

	Preliminary Allocation as of September 29, 2017	Allocation Adjustments	Adjusted Allocation March 30, 2018
Current assets	$ 7,375	$ (1,088)	$ 6,287
Intangible assets	19,000	—	19,000
Other assets	3,301	(81)	3,220
Total assets acquired	29,676	(1,169)	28,507
Current liabilities	2,169	142	2,311
Other liabilities	190	(77)	113
Total liabilities assumed	2,359	65	2,424
Net assets acquired	27,317	(1,234)	26,083
Consideration:			

Cash paid upon closing, net of cash acquired	33,500	—	33,500
Goodwill	$ 6,183	$ 1,234	$ 7,417

The pro forma financial information for fiscal year 2017, including revenue and net income, is immaterial, and has not been separately presented.

3. DISCONTINUED OPERATIONS

On October 27, 2017, we entered into a Purchase Agreement to sell the Compute business. In consideration for the transfer and sale of the Compute business, we received an equity interest in the buyer valued at approximately $36.5 million, and representing less than 20.0% of the buyer's total outstanding equity. The operations of the Compute business were accounted for as discontinued operations through the date of divestiture.

In August 2015, we sold our automotive business (the "Automotive business") to Autoliv ASP Inc. ("Autoliv"), as the Automotive business was not consistent with our long-term strategic vision from both a growth and profitability perspective. Additionally, we entered into a consulting agreement pursuant to which we were to provide Autoliv with certain non-design advisory services for a period of two years following the closing of the transaction for up to $15.0 million (the "Consulting Agreement"). During the three and six months ended March 31, 2017, we recognized $1.9 million and $3.8 million of income, respectively, from the consulting agreement with Autoliv. During the three months ended March 31, 2017, we also received $18.0 million, the full amount of the indemnification escrow. No income was recognized during the three and six months ended March 30, 2018.

The accompanying consolidated statements of operations includes the following operating results related to these discontinued operations (in thousands):

	Three Months Ended		Six Months Ended	
	March 30, 2018	March 31, 2017	March 30, 2018	March 31, 2017
Revenue (1)	$2	$ 259	$—	$ 259
Cost of revenue (1)	(56)	1,620	(596)	1,620
Gross profit	58	(1,361)	596	(1,361)
Operating expenses:				
Research and development (1)	(12)	8,325	4,698	8,325
Selling, general and administrative (1)	88	6,744	1,515	6,744
Total operating expenses	76	15,069	6,213	15,069
Loss from operations	(18)	(16,430)	(5,617)	(16,430)
Other income (2)	—	1,875	—	3,750
Gain on sale (2)	—	18,022	—	18,022
(Loss) income before income taxes	(18)	3,467	(5,617)	5,342
Income tax provision	—	(669)	—	—
(Loss) income from discontinued operations	$(18)	$ 4,136	$(5,617)	$ 5,342
Cash flow from operating activities	(18)	(29,072)	(10,327)	(29,072)
Cash flow from investing activities	—	21,770	—	21,770

(1) Amounts are associated with the Compute business.

(2) Amounts are associated with the Automotive business.

10

As it relates to our Quarterly Report on Form 10-Q for the three and six months ended March 31, 2017, we identified an immaterial misstatement in our discontinued operations footnote table with regards to the cash flow amounts of our discontinued operations. The disclosure amounts incorrectly included cash flows from the continuing AppliedMicro business and incorrectly classified the $18.0 million indemnification escrow from the previously discontinued Automotive business, which was received during the three months ended March 31, 2017. Our footnote disclosure in the table above related to the discontinued operations for the three and six months ended March 31, 2017 has been restated to correct this error. The effect of this restatement is outlined below:

	Three and Six Months Ended March 31, 2017	
	As reported	As adjusted
Depreciation and amortization	2,535	—
Net cash provided by (used in) operating activities	12,487	(29,072)
Net cash (used in) provided by investment activities	(663)	21,770
Net cash used in financing activities	(32,201)	—

4. INVESTMENTS

Our short-term investments are invested in corporate bonds and commercial paper, and are classified as available-for-sale. The amortized cost, gross unrealized holding gains or losses, and fair value of our investments by major investment type as of March 30, 2018 and September 29, 2017 are summarized in the tables below (in thousands):

	March 30, 2018			
	Amortized Cost	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses	Aggregate Fair Value
Corporate bonds	$26,476	$ —	$ (677)	$ 25,799
Commercial paper	1,598	—	(1)	1,597
Total short term investments	$28,074	$ —	$ (678)	$ 27,396

	September 29, 2017			
	Amortized Cost	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses	Aggregate Fair Value
Corporate bonds	$26,366	$ 10	$ (166)	$ 26,210
Commercial paper	57,943	4	(36)	57,911
Total short term investments	$84,309	$ 14	$ (202)	$ 84,121

The contractual maturities of investments were as follows (in thousands):

	March 30, 2018	September 29, 2017
Less than 1 year	$ 2,612	$ 60,433
Over 1 year	24,784	23,688
Total short term investments	$ 27,396	$ 84,121

Available-for-sale investments are reported at fair value and as such, their associated unrealized gains and losses are reported as a separate component of stockholders' equity within accumulated other comprehensive income.

Other Investments— As of March 30, 2018 we held two non-marketable equity investments classified as other long-term investments.

One of these is an investment in a Series B preferred stock ownership of a privately held manufacturing corporation with preferred liquidation rights over other equity shares. This investment had a fair value of $5.0 million at the date of purchase and is held at cost, which approximates fair value. Since we do not have the ability to exercise significant influence or control over the investment we hold this investment at cost, which we evaluate for impairment at each balance sheet date and through March 30, 2018 no impairment has been recorded for this investment.

In addition, we had a minority investment of less than 20.0% of the outstanding equity of a privately held limited liability corporation ("Compute"). This investment was acquired in conjunction with the divestiture of the Compute business during the fiscal quarter ended December 29, 2017 and had an initial value of $36.5 million. This investment value is updated quarterly based on our proportionate share of the losses or earnings of Compute utilizing the equity method. During the three months ended March 30, 2018 we recorded a $4.1 million loss associated with this investment as other expense in our consolidated statement of operations.

5. FAIR VALUE

We group our financial assets and liabilities measured at fair value on a recurring basis in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

Level 1 - Quoted prices in active markets for identical assets or liabilities.

Level 2 - Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets with insufficient volume or infrequent transactions (less active markets), or model-driven valuations in which all significant inputs are observable or can be derived principally from, or corroborated with, observable market data.

Level 3 - Fair value is derived from valuation techniques in which one or more significant inputs are unobservable, including assumptions and judgments made by us.

Assets and Liabilities Measured and Recorded at Fair Value on a Recurring Basis

We measure certain assets and liabilities at fair value on a recurring basis such as our financial instruments and derivatives. There have been no transfers between Level 1, 2 or 3 assets or liabilities during the three and six months ended March 30, 2018.

Assets and liabilities measured at fair value on a recurring basis consist of the following (in thousands):

	March 30, 2018			
	Fair Value	Active Markets for Identical Assets (Level 1)	Observable Inputs (Level 2)	Unobservable Inputs (Level 3)
Assets				
Money market funds	$179	$ 179	$ —	$ —
Commercial paper	65,322	—	65,322	—
Corporate bonds	25,799	—	25,799	—
Total assets measured at fair value	$91,300	$ 179	$ 91,121	$ —
Liabilities				
Contingent consideration	$1,130	$ —	$ —	$ 1,130
Common stock warrant liability	9,151	—	—	9,151
Total liabilities measured at fair value	$10,281	$ —	$ —	$ 10,281

	September 29, 2017			
	Fair Value	Active Markets for Identical Assets (Level 1)	Observable Inputs (Level 2)	Unobservable Inputs (Level 3)
Assets				
Money market funds	$36	$ 36	$ —	$ —
Commercial paper	57,911	—	57,911	—
Corporate bonds	26,210	—	26,210	—

Total assets measured at fair value	$84,157	$ 36	$ 84,121	$ —
Liabilities				
Contingent consideration	$1,679	$ —	$ —	$ 1,679
Common stock warrant liability	40,775	—	—	40,775
Total liabilities measured at fair value	$42,454	$ —	$ —	$ 42,454

As of March 30, 2018 and September 29, 2017, the fair value of the common stock warrants has been estimated using a Black-Scholes option pricing model.

The quantitative information utilized in the fair value calculation of our Level 3 liabilities is as follows:

			Inputs	
Liabilities	Valuation Technique	Unobservable Input	March 30, 2018	September 29, 2017
Contingent consideration	Discounted cash flow	Discount rate	9.2%	9.2%
		Probability of achievement	80% - 90%	70% - 100%
		Timing of cash flows	2 months	2 - 8 months
Warrant liability	Black-Scholes model	Volatility	55.6%	44.9%
		Discount rate	2.39%	1.62%
		Expected life	2.7 years	3.2 years
		Exercise price	$14.05	$14.05
		Stock price	$16.60	$44.61
		Dividend rate	—%	—%

The fair values of the contingent consideration liabilities were estimated based upon a risk-adjusted present value of the probability-weighted expected payments by us. Specifically, we considered base, upside and downside scenarios for the operating metrics upon which the contingent payments are to be based. Probabilities were assigned to each scenario and the probability weighted payments were discounted to present value using risk-adjusted discount rates.

The changes in liabilities with inputs classified within Level 3 of the fair value hierarchy consist of the following (in thousands):

	September 29, 2017	Net Realized/Unrealized Gains Included in Earnings	Purchases and Issuances	Sales and Settlements	March 30, 2018
Contingent consideration	$ 1,679	$ (549)	$ —	$ —	$ 1,130
Common stock warrant liability	$ 40,775	$ (31,624)	$ —	$ —	$ 9,151

	September 30, 2016	Net Realized/Unrealized Losses Included in Earnings	Purchases and Issuances	Sales and Settlements	March 31, 2017
Contingent consideration	$ 848	$ 33	$ —	$ (400)	$ 481
Common stock warrant liability	$ 38,253	$ 7,395	$ —	$ —	$ 45,648

6. INVENTORIES

Inventories, net of reserves, consist of the following (in thousands):

	March 30, 2018	September 29, 2017
Raw materials	$ 90,652	$ 78,999
Work-in-process	13,022	13,962
Finished goods	40,223	43,113
Total inventory, net	$ 143,897	$ 136,074

7. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consists of the following (in thousands):

	March 30, 2018	September 29, 2017
Construction in process	$27,207	$ 22,195
Machinery and equipment	174,817	160,955
Leasehold improvements	13,232	13,809
Furniture and fixtures	2,411	2,078
Computer equipment and software	17,086	16,539
Capital lease assets	20,764	20,410
Total property and equipment	$255,517	$ 235,986
Less accumulated depreciation and amortization	(116,975)	(104,967)
Property and equipment, net	$138,542	$ 131,019

Depreciation and amortization expense related to property, plant and equipment for the three and six months ended March 30, 2018 was $7.6 million and $15.4 million, respectively. Depreciation and amortization expense related to property, plant and equipment for the three and six months ended March 31, 2017 was $7.2 million and $13.1 million, respectively.

8. DEBT

As of March 30, 2018, we are party to a credit agreement dated as of May 8, 2014 with a syndicate of lenders and Goldman Sachs Bank USA, as administrative agent (as amended on February 13, 2015, August 31, 2016, March 10, 2017 and May 19, 2017, the “Credit Agreement”). As of March 30, 2018, the Credit Agreement consisted of term loans with an aggregate principal amount of $700.0 million (“Term Loans”) and a revolving credit facility with an aggregate borrowing capacity of $160.0 million (“Revolving Facility”). The Revolving Facility will mature in May 2019 and the Term Loans will mature in May 2024 and bear interest at: (i) for LIBOR loans for any interest period, a rate per annum equal to the LIBOR rate as determined by the administrative agent, plus an applicable margin of 2.25%; and (ii) for base rate loans, a rate per annum equal to the greater of (a) the prime rate quoted in the print edition of the Wall Street Journal, Money Rates Section, (b) the federal funds rate plus one-half of 1.00% and (c) the LIBOR rate applicable to a one-month interest period plus 1.00% (but, in each case, not less than 1.00%), plus an applicable margin of 1.25%.

All principal amounts outstanding and interest rate information as of March 30, 2018, for the Credit Agreement were as follows (in millions, except rate data):

	Principal Outstanding	LIBOR Rate	Margin	Effective Interest Rate
Term loans	$683.3	1.89%	2.25%	4.14%

As of March 30, 2018, approximately $11.8 million of deferred financing costs remain unamortized, of which $11.3 million is related to the Term Loans and is recorded as a direct reduction of the recognized debt liabilities in our accompanying consolidated balance sheet, and $0.5 million is related to the Revolving Facility and is recorded in other long-term assets in our accompanying consolidated balance sheet.

The Term Loans are secured by a first priority lien on substantially all of our assets and provide that we must comply with certain financial and non-financial covenants.

As of March 30, 2018, we had $160.0 million of borrowing capacity under our Revolving Facility.

As of March 30, 2018, the following remained outstanding on the Term Loans (in thousands):

Principal balance	$683,298
Unamortized discount	(5,230)
Unamortized deferred financing costs	(11,262)
Total term loans	$666,806
Current portion	6,885
Long-term, less current portion	$659,921

As of March 30, 2018, the minimum principal payments under the Term Loans in future fiscal years were as follows (in thousands):

2018 (rest of fiscal year)	$3,442
2019	6,885
2020	6,885
2021	6,885
2022	6,885
Thereafter	652,316
Total	$683,298

The fair value of the Term Loans was estimated to be approximately $692.7 million as of March 30, 2018 and was determined using Level 2 inputs, including a quoted rate from a bank.

9. CAPITAL LEASE AND FINANCING OBLIGATIONS

Corporate Facility Financing Obligation

On May 26, 2016, we entered into a Purchase and Sale Agreement (the "Purchase and Sale Agreement") with Calare Properties, Inc. (together with its affiliates, "Calare"), for the sale and subsequent leaseback of our corporate headquarters, located at 100 Chelmsford Street, Lowell, Massachusetts. The transactions contemplated by the Purchase and Sale Agreement closed on December 28, 2016, at which time we also entered into three lease agreements with Calare including: (1) a 20 year leaseback of the facility located at 100 Chelmsford Street (the "100 Chelmsford Lease"), (2) a 20 year build-to-suit lease arrangement for the construction and subsequent lease back of a new facility to be located at 144 Chelmsford Street (the "144 Chelmsford Lease"), and (3) a 14 year building lease renewal of an adjacent facility at 121 Hale Street (the "121 Hale Lease", and together with the 100 Chelmsford Lease and the 144 Chelmsford Lease, the "Leases").

Because the transactions contemplated by the Purchase and Sale Agreement and the related Leases were negotiated and consummated at the same time and in contemplation of one another to achieve the same commercial objective, the transactions are accounted for by us as a single unit of accounting. In addition, the Leases were determined to represent a failed sale-leaseback due to our continuing involvement in the properties in the form of non-recourse financing. As a result, the Leases are accounted for under the financing method and we will be deemed the accounting owner under the arrangement, including the assets to be constructed under the 144 Chelmsford Lease. We will continue to recognize the existing building and improvements sold under the Purchase and Sale Agreement, capitalize the 121 Hale Street building as well as the assets constructed under the Leases, and depreciate the assets over the shorter of their estimated useful lives or the lease terms. The sale proceeds from the Purchase and Sale Agreement of $8.2 million (which includes $4.2 million in cash and $4.0 million in construction allowances) and the fair value of the 121 Hale Street building of $4.0 million were recognized as a financing obligation on our consolidated balance sheet and are being amortized over the 20 year lease term based on the minimum lease payments required under the Leases and our incremental borrowing rate. Future construction costs funded by Calare under the 144 Chelmsford Lease will be recognized as additional financing obligations on our consolidated balance sheet as incurred, and will be amortized over the 20 year lease term based on the minimum lease payments required under the Leases and our incremental borrowing rate.

As a result of the failed sale-leaseback accounting, we calculated a financing obligation based on the future minimum lease payments discounted at 8.6% as of March 30, 2018. The discount rate represents the estimated incremental borrowing rate over the lease term of 20 years. The minimum lease payments are recorded as interest expense and in part as a payment of principal reducing the financing obligation. The real property assets in the transaction remain on the consolidated balance sheets and continue to be depreciated over the remaining useful lives. As of March 30, 2018, approximately $22.4 million of the financing obligation was outstanding associated with the Leases, of which $10.2 million was associated with the 144 Chelmsford Lease that has not yet been placed in service.

Additionally, we have certain capital equipment lease obligations, of which approximately $1.9 million was outstanding as of March 30, 2018.

As of March 30, 2018, future minimum payments under capital lease obligations and financing obligations related to the Leases were as follows (in thousands):

Fiscal year ending:	Amount
2018 (rest of fiscal year)	$950
2019	1,809
2020	1,626
2021	1,483
2022	1,260
Thereafter	20,462
Total minimum capital lease payments	27,590
Less amount representing interest	(15,267)
Present value of net minimum capital lease payments (1)	$12,323

(1) Excludes $10.2 million associated with the 144 Chelmsford Lease that has not yet been placed in service.

10. INTANGIBLE ASSETS

Amortization expense related to intangible assets is as follows (in thousands):

	Three Months Ended		Six Months Ended	
	March 30, 2018	March 31, 2017	March 30, 2018	March 31, 2017
Cost of revenue	$ 8,172	$ 7,276	$16,319	$ 13,278
Selling, general and administrative	11,753	7,163	22,746	13,630
Total	$ 19,925	$ 14,439	$39,065	$ 26,908

Intangible assets consist of the following (in thousands):

	March 30, 2018	September 29, 2017
Acquired technology	$252,025	$ 251,655
Customer relationships	558,287	556,648
Trade name	3,400	3,400
Total	$813,712	$ 811,703
Less accumulated amortization	(229,677)	(190,611)
Intangible assets — net	$584,035	$ 621,092

Our trade name is an indefinite-lived intangible asset. A summary of the activity in intangible assets and goodwill follows (in thousands):

	Intangible Assets				
	Total Intangible Assets	Acquired Technology	Customer Relationships	Trade Name	Goodwill
Balance at September 29, 2017	$811,703				