SYNAPTICS INC
Form 10-Q
April 29, 2011

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

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

For the quarterly period ended March 31, 2011

For the quarterly period ended March 26, 2011
Commission file number 000-49602
SYNAPTICS INCORPORATED
(Exact name of registrant as specified in its charter)

Delaware	**77-0118518**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

3120 Scott Blvd.
Santa Clara, California 95054
(Address of principal executive offices) (Zip code)
(408) 454-5100
(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 þ No o

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 þ No o

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

Number of shares of Common Stock outstanding at April 21, 2011: 34,253,171

SYNAPTICS INCORPORATED
QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTER ENDED MARCH 31, 2011
TABLE OF CONTENTS

Table of Contents

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

SYNAPTICS INCORPORATED AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except share data)
(unaudited)

	March 31, 2011	June 30, 2010
ASSETS		
Current assets:		
Cash and cash equivalents	$ 246,285	$ 209,858
Accounts receivable, net of allowances of $709 and $500 at March 31, 2011 and June 30, 2010, respectively	97,661	101,509
Inventories	32,624	18,667
Prepaid expenses and other current assets	4,438	4,471
Total current assets	381,008	334,505
Property and equipment at cost, net of accumulated depreciation of $26,909 and $20,256 at March 31, 2011 and June 30, 2010, respectively	27,260	25,821
Goodwill	1,927	1,927
Non-current investments	29,078	28,012
Other assets	27,037	24,414
	$ 466,310	$ 414,679
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 60,107	$ 65,618
Accrued compensation	11,703	11,330
Income taxes payable	6,293	10,061
Other accrued liabilities	20,756	18,962
Total current liabilities	98,859	105,971
Notes payable	2,305	2,305
Other liabilities	20,443	19,892
Stockholders equity:		
Common stock:		
$0.001 par value; 120,000,000 and 60,000,000 shares authorized; 46,500,890 and 44,891,834 shares issued, and 34,178,397 and 34,020,521 shares outstanding, at March 31, 2011 and June 30, 2010, respectively	47	45
Additional paid-in capital	394,895	347,764
Treasury stock: 12,322,493 and 10,871,313 common treasury shares at March 31, 2011 and June 30, 2010, respectively, at cost	(322,142)	(281,932)
Accumulated other comprehensive income	2,911	1,515

Retained earnings	268,992	219,119
Total stockholders equity	344,703	286,511
	$ 466,310	$ 414,679

See notes to condensed consolidated financial statements (unaudited).

3

Table of Contents

SYNAPTICS INCORPORATED AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(in thousands, except per share data)
(unaudited)

	Three Months Ended March 31, 2011	Three Months Ended March 31, 2010	Nine Months Ended March 31, 2011	Nine Months Ended March 31, 2010
Net revenue	$ 142,406	$ 116,212	$ 455,172	$ 369,127
Cost of revenue	84,790	68,910	269,690	219,672
Gross margin	57,616	47,302	185,482	149,455
Operating expenses:				
Research and development	25,956	21,212	77,516	63,629
Selling, general, and administrative	17,244	14,635	51,750	44,974
Total operating expenses	43,200	35,847	129,266	108,603
Operating income	14,416	11,455	56,216	40,852
Interest income	242	200	679	772
Interest expense	(4)	(4)	(13)	(2,395)
Impairment (loss)/recovery on investments, net	10		20	(443)
Income before provision for income taxes	14,664	11,651	56,902	38,786
Provision for income taxes	1,168	45	7,029	5,149
Net income	$ 13,496	$ 11,606	$ 49,873	$ 33,637
Net income per share:				
Basic	$ 0.40	$ 0.35	$ 1.46	$ 0.99
Diluted	$ 0.38	$ 0.33	$ 1.40	$ 0.95
Shares used in computing net income per share:				
Basic	33,992	33,526	34,118	33,826
Diluted	35,346	35,095	35,565	35,371

See notes to condensed consolidated financial statements (unaudited).

SYNAPTICS INCORPORATED AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(unaudited)

	Nine Months Ended March 31, 2011	Nine Months Ended March 31, 2010
Cash flows from operating activities		
Net income	$ 49,873	$ 33,637
Adjustments to reconcile net income to net cash provided by operating activities:		
Share-based compensation costs	25,708	27,339
Deferred taxes	(2,300)	(3,137)
Tax benefit realized from share-based compensation	3,155	5,294
Excess tax benefit from share-based compensation	(3,155)	(5,294)
Depreciation of property and equipment	8,184	6,320
Amortization of debt issuance costs		118
Impairment/(recovery) of investments, net	(20)	443
Amortization of debt discount		2,069
Changes in operating assets and liabilities:		
Accounts receivable, net	3,848	(3,253)
Inventories	(13,957)	(3,258)
Prepaid expenses and other current assets	120	168
Other assets	(410)	(3,259)
Accounts payable	(5,511)	15,994
Accrued compensation	373	1,834
Income taxes	(3,259)	(1,176)
Other accrued liabilities	1,836	3,715
Net cash provided by operating activities	64,485	77,554
Cash flows from investing activities		
Purchases of short-term investments		(5,986)
Proceeds from sales and maturities of short-term investments		28,912
Proceeds from sales and maturities of non-current investments	350	1,125
Purchases of property and equipment	(9,623)	(6,267)
Net cash (used in) provided by investing activities	(9,273)	17,784
Cash flows from financing activities		
Purchases of treasury stock	(40,210)	(44,545)
Proceeds from issuance of common stock upon exercise of options and stock purchase plan	20,581	8,148
Retirement of debt, net of discount		(62,998)
Excess tax benefit from share-based compensation	3,155	5,294
Payroll taxes for deferred stock units	(2,311)	(1,608)

Net cash used in financing activities		(18,785)		(95,709)
Net increase (decrease) in cash and cash equivalents		36,427		(371)
Cash and cash equivalents at beginning of period		209,858		169,036
Cash and cash equivalents at end of period	$	246,285	$	168,665

Supplemental disclosures of cash flow information

Cash paid for income taxes	$	9,459	$	11,342

See notes to condensed consolidated financial statements (unaudited).

SYNAPTICS INCORPORATED AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission, or the SEC, and U.S. generally accepted accounting principles, or U.S. GAAP. However, certain information or footnote disclosures normally included in financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to such SEC rules and regulations. In our opinion, the financial statements include all adjustments, which are of a normal and recurring nature, necessary for the fair presentation of the results of the interim periods presented. The results of operations for the interim periods are not necessarily indicative of the operating results for the full fiscal year or any future period. These financial statements should be read in conjunction with the audited consolidated financial statements and related notes included in our annual report on Form 10-K for the fiscal year ended June 30, 2010.

The consolidated financial statements include our financial statements and those of our wholly owned subsidiaries. All significant intercompany balances and transactions have been eliminated upon consolidation.

Our fiscal year is the 52- or 53-week period ending on the last Saturday in June. Our fiscal 2011 will be a 52-week period ending on June 25, 2011. Our fiscal 2010 was a 52-week period ending on June 26, 2010. The fiscal periods presented in this report were 13-week periods for the three months ended March 26, 2011 and March 27, 2010. For ease of presentation, the accompanying consolidated financial statements have been shown as ending on March 31 and calendar quarter end dates for all annual, interim, and quarterly financial statement captions, unless otherwise indicated.

Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue, expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, we evaluate our estimates, including those related to revenue recognition, allowance for doubtful accounts, cost of revenue, inventories, product warranty, share-based compensation costs, provision for income taxes, income taxes payable, intangible assets, investments, and contingencies. We base our estimates on historical experience, applicable laws and regulations, and various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

2. Revenue Recognition

We recognize revenue from product sales when there is persuasive evidence that an arrangement exists, delivery has occurred and title has transferred, the price is fixed or determinable, and collection is reasonably assured. We accrue for estimated sales returns and other allowances, based on historical experience, at the time we recognize revenue.

3. Net Income Per Share

The computation of basic and diluted net income per share was as follows (in thousands, except per share data):

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2011	2010	2011	2010
Numerator:				
Net income	$ 13,496	$ 11,606	$ 49,873	$ 33,637
Denominator:				
Shares, basic	33,992	33,526	34,118	33,826
Effect of dilutive share-based awards	1,354	1,569	1,447	1,545
Shares, diluted	35,346	35,095	35,565	35,371
Net income per share:				
Basic	$ 0.40	$ 0.35	$ 1.46	$ 0.99
Diluted	$ 0.38	$ 0.33	$ 1.40	$ 0.95

Our basic net income per share amounts for each period presented have been computed using the weighted average number of shares of common stock outstanding. Our diluted net income per share amounts for each period presented include the weighted average effect of potentially dilutive shares. We use the treasury stock method to determine the dilutive effect of our share-based awards and convertible notes.

Dilutive net income per share amounts do not include the weighted average effect of 3,471,863 and 3,778,523 share-based awards that were outstanding during the three months ended March 31, 2011 and 2010, respectively, and 3,507,168 and 3,614,277 share-based awards that were outstanding during the nine months ended March 31, 2011 and 2010, respectively. These share-based awards were not included in the computation of diluted net income per share because the proceeds received, if any, from such share-based awards combined with the average unamortized compensation costs adjusted for the hypothetical tax benefit or deficiency creditable or chargeable, respectively, to additional paid-in capital were greater than the average market price of our common stock, and therefore, their effect would have been antidilutive.

4. Auction Rate Securities Investments

Our non-current investments include auction rate securities, or ARS, which are reported at fair value, with unrealized gains and losses excluded from earnings and are shown separately as a component of accumulated other comprehensive income within stockholders equity. We charge any other-than-temporary declines in the fair value of a debt security to earnings (within impairment (loss)/recovery on investments, net) if the decline results from a credit loss or to other comprehensive income if the decline results from a noncredit loss. We charge any other-than-temporary declines in the fair value of equity securities to earnings (within impairment (loss)/recovery on investments, net). Other-than-temporary declines result in the establishment of a new cost basis for the security. We include interest earned on investments in interest income.

Our ARS investments have failed to settle in auctions and are not liquid. In the event we need to access these funds prior to their maturity, we will not be able to do so without a loss of principal, unless redeemed by the issuers or a future auction on these investments is successful. During the three months ended March 31, 2011 and 2010, $100,000 and $125,000 of our ARS investments were redeemed at par, respectively, and during the nine months ended March 31, 2011 and 2010, $350,000 and $1.1 million of our ARS investments were redeemed at par, respectively.

As there are currently no active markets for our various failed ARS investments, we have estimated the fair value as of March 31, 2011 using a trinomial discounted cash flow analysis. The analysis considered, among other factors, the following:

- the collateral underlying the security investments;
- creditworthiness of the counterparty;
- timing of expected future cash flows;
- the probability of a successful auction in a future period;
- the underlying structure of each investment;

the present value of future principal and interest payments discounted at rates considered to reflect current market conditions;

consideration of the probabilities of default, passing a future auction, or redemption at par for each period; and

estimates of the recovery rates in the event of default for each investment.

When possible, our failed ARS investments were compared to other observable market data or securities with similar characteristics. Our estimate of the fair value of our ARS investments could change materially from period to period based on future market conditions.

Contractual maturities for our ARS investments are generally greater than five years, with fair value of $10.5 million maturing from 2015 to 2017, $8.7 million maturing from 2034 to 2045, and $9.9 million having no stated maturity. Of our ARS investments, $21.9 million par value are investment grade, and the remaining $18.5 million par value are below investment grade. For the nine-month period ended March 31, 2010, we recognized a $449,000 other-than-temporary impairment charge on our ARS investments in preferred stock.

The various types of ARS investments we held as of March 31, 2011, including the original cost basis, other-than-temporary impairment included in other comprehensive income, other-than-temporary impairment included in retained earnings, new cost basis, unrealized gain, and fair value consisted of the following (in thousands):

		Cumulative Other-than-temporary Impairment				
	Original Cost Basis	Included in Other Comprehensive Income	Included in Retained Earnings	New Cost Basis	Unrealized Gain	Fair Value
Student loans	$ 9,200	$ (596)	$ (242)	$ 8,362	$ 347	$ 8,709
Closed end municipal and corporate funds	10,650	(1,112)	(93)	9,445	476	9,921
Credit linked notes	13,500	(156)	(8,765)	4,579	3,999	8,578
Preferred stock	5,000		(5,000)			
Municipals	2,000	(203)	(83)	1,714	156	1,870
Total ARS	$ 40,350	$ (2,067)	$ (14,183)	$ 24,100	$ 4,978	$ 29,078

The various types of ARS investments we held as of June 30, 2010, including the original cost basis, other-than-temporary impairment included in other comprehensive income, other-than-temporary impairment included in retained earnings, new cost basis, unrealized gain, and fair value consisted of the following (in thousands):

		Cumulative Other-than-temporary Impairment				
	Original Cost Basis	Included in Other Comprehensive Income	Included in Retained Earnings	New Cost Basis	Unrealized Gain	Fair Value
Student loans	$ 9,550	$ (617)	$ (262)	$ 8,671	$ 251	$ 8,922
Closed end municipal and corporate funds	10,650	(1,112)	(93)	9,445	293	9,738
Credit linked notes	13,500	(156)	(8,765)	4,579	2,952	7,531
Preferred stock	5,000		(5,000)			
Municipals	2,000	(203)	(83)	1,714	107	1,821

Total ARS	$ 40,700	$ (2,088)	$ (14,203)	$ 24,409	$ 3,603	$ 28,012

Table of Contents

We have accounted for all of our ARS investments as non-current (included in non-current investments in the accompanying condensed consolidated balance sheets) as we are not able to reasonably determine when the ARS markets will recover or be restructured. Based on our ability to access our cash, our expected operating cash flows, and our other sources of cash, we have the intent and ability to hold these investments until the value recovers or the investments mature. We will continue to monitor our ARS investments and evaluate our accounting for these investments quarterly. Subsequent to recording other-than-temporary impairment charges, certain of our ARS investments have increased in value above their new cost bases, and this increase is included as unrealized gain above and in accumulated other comprehensive income in the accompanying condensed consolidated balance sheets.

5. Fair Value of Cash Equivalents and Investments

Certain financial assets and liabilities have been recognized or disclosed at fair value on a recurring basis. For other financial assets and liabilities, we elected not to apply the fair value option.

Current accounting standards establish a consistent framework for measuring fair value on either a recurring or nonrecurring basis in which inputs, used in valuation techniques, are assigned a hierarchical level.

The following are the hierarchical levels of inputs to measure fair value:

Level 1 inputs are observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 inputs reflect quoted prices for identical assets or liabilities in markets that are not active; quoted prices for similar assets or liabilities in active markets; inputs other than quoted prices that are observable for the assets or liabilities; or inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3 inputs are unobservable inputs reflecting our assumptions, which are incorporated into valuation techniques and models used to determine fair value. The assumptions are consistent with market participant assumptions that are reasonably available. Our Level 3 assets consist of non-current ARS investments. We estimated the fair value of our ARS investments based on, among other factors, the following: (i) the collateral underlying the security investments, (ii) creditworthiness of the counterparty, (iii) timing of expected future cash flows, (iv) the probability of a successful auction in a future period, (v) the underlying structure of each investment; (vi) the present value of future principal and interest payments discounted at rates considered to reflect current market conditions; (vii) consideration of the probabilities of default, passing a future auction, or repurchase at par for each period; and (viii) estimates of the recovery rates in the event of default for each investment.

Financial assets and liabilities measured at fair value on a recurring basis, by level within the fair value hierarchy consisted of the following (in thousands):

	March 31, 2011		June 30, 2010	
	Level 1	Level 3	Level 1	Level 3
Money market	$ 241,326	$	$ 208,040	$
Auction rate securities		29,078		28,012
Total available-for-sale securities	$ 241,326	$ 29,078	$ 208,040	$ 28,012

Table of Contents

Money market balances are included in cash and cash equivalents as of March 31, 2011 and June 30, 2010. ARS are included in non-current investments as of March 31, 2011 and June 30, 2010.

Changes in fair value of our Level 3 financial assets were as follows (in thousands):

Balance as of June 30, 2010	$	28,012
Net unrealized gain		1,396
Realized gain on redeemed securities		20
Redemptions		(350)
Balance as of March 31, 2011	$	29,078

There were no transfers in or out of our Level 1 or 3 assets during the nine months ended March 31, 2011.

The fair values of our cash equivalents, accounts receivable, accounts payable, and accrued liabilities approximate their carrying values because of the short-term nature of those instruments.

6. Inventories

Inventories are stated at the lower of cost (first-in, first-out method) or market (estimated net realizable value) and consisted of the following (in thousands):

		March 31, 2011		June 30, 2010
Raw materials	$	20,529	$	12,251
Finished goods		12,095		6,416
	$	32,624	$	18,667

Periodically, we purchase inventory from our contract manufacturers when a customer delays its delivery schedule or cancels its order. In those circumstances in which our customer has cancelled its order and we purchase inventory from our contract manufacturers, we consider a write-down to reduce the carrying value of the inventory purchased to its net realizable value. We charge write-downs to reduce the carrying value of obsolete, slow moving, and non-usable inventory to net realizable value to cost of revenue. The effect of these write-downs is to establish a new cost basis in the related inventory, which we do not subsequently write up.

7. Product Warranties, Indemnifications, and Contingencies

Product Warranties

We generally warrant our products for a period of 12 months or more from the date of sale and estimate probable product warranty costs at the time we recognize revenue. Factors that affect our warranty liability include historical and anticipated rates of warranty claims, materials usage, and service delivery costs. We assess the adequacy of our warranty obligations periodically and adjust the accrued warranty liability on the basis of our estimates.

Indemnifications

In connection with certain third-party agreements, we are obligated to indemnify the third party in connection with any technology infringement by us. We have also entered into indemnification agreements with our officers and directors. Maximum potential future payments cannot be estimated because these agreements do not have a maximum stated liability. However, historical costs related to these indemnification provisions have not been significant. We have not recorded any liability in our consolidated financial statements for such indemnification obligations.

Contingencies

We may receive notices from third parties that claim our products infringe their rights. From time to time, we receive notice from third parties alleging infringement of their intellectual property rights. We cannot be certain that our technologies and products do not or will not infringe issued patents or other proprietary rights of third parties.

Any infringement claims, with or without merit, could result in significant litigation costs and diversion of management and financial resources, including the payment of damages, which could have a material adverse effect on our business, financial condition, and results of operations.

8. Convertible Senior Subordinated Notes

In December 2004, we issued an aggregate of $125.0 million of convertible notes and incurred debt issuance costs of $4.3 million, consisting primarily of the initial purchasers discount and costs related to legal, accounting, and printing, which were amortized over five years. The notes were issued in a private offering pursuant to Rule 144A under the Securities Act of 1933, as amended, or the Securities Act, and mature December 1, 2024. We used the net proceeds for working capital and general corporate purposes.

In fiscal 2009, we repurchased and retired $59.7 million of our outstanding notes at a discount from par of approximately 7%, which resulted in a $1.1 million net loss on retirement of debt after deducting the associated unamortized discount and issuance costs. In December 2009, we repurchased and retired $63.0 million par value of our notes when investors exercised their rights to require us to repurchase their notes. The remaining $2.3 million par value of our notes outstanding are classified as long-term as the next date noteholders can require us to repurchase all or a portion of their notes is in December 2014.

We recorded interest expense on the notes of $4,000 during each of the three-month periods ended March 31, 2011 and 2010, and $13,000 and $2.4 million during the nine-month periods ended March 31, 2011 and 2010, respectively. Through December 31, 2009, interest expense included the amortization of discount and issuance costs. As of March 31, 2011, the if-converted value of the notes did not exceed the principal amount of the notes.

9. Share-Based Compensation

The purpose of our various share-based compensation plans is to attract, motivate, retain, and reward high-quality employees, directors, and consultants by enabling such persons to acquire or increase their proprietary interest in our common stock in order to strengthen the mutuality of interests between such persons and our stockholders and to provide such persons with long-term performance incentives to focus their best efforts in the creation of stockholder value. Consequently, share-based compensatory awards issued subsequent to the initial award to our employees and consultants are determined primarily on individual performance. Our share-based compensation plans with outstanding awards consist of our 1996 Stock Option Plan, or our 1996 Plan, our 2001 Incentive Compensation Plan, as amended, or our 2001 Plan, our 2010 Incentive Compensation Plan, or our 2010 Plan, and our 2010 Employee Stock Purchase Plan, or our 2010 ESPP.

Share-based compensation and the related tax benefit recognized in our consolidated statements of income were as follows (in thousands):

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2011	2010	2011	2010
Cost of revenue	$ 355	$ 553	$ 1,032	$ 1,816
Research and development	3,377	3,328	10,129	10,772
Selling, general, and administrative	4,619	4,314	14,547	14,751
Total	$ 8,351	$ 8,195	$ 25,708	$ 27,339
Tax benefit recorded on share-based compensation	$ 2,347	$ 1,735	$ 7,426	$ 7,042

We utilize the Black-Scholes option pricing model to estimate the grant date fair value of certain employee share-based compensatory awards, which requires the input of highly subjective assumptions, including expected volatility and expected life. Historical and implied volatilities were used in estimating the fair value of our share-based awards, while the expected life of our options and estimated forfeitures for share-based awards that are not expected to vest were estimated based on historical trends since our initial public offering. Changes in these inputs and assumptions can materially affect the measure of estimated fair value of our share-based compensation. We charge the estimated fair value less estimated forfeitures to earnings on a straight-line basis over the vesting period of the underlying awards, which is generally four years for our stock options and deferred stock units, or DSUs, and up to two years for our 2010 ESPP. The Black-Scholes option pricing model was developed for use in estimating the fair value of traded options having no vesting restrictions and being fully transferable. As our stock option and 2010 ESPP awards have characteristics that differ significantly from traded options, and as changes in the subjective assumptions can materially affect the estimated value, our estimate of fair value may not accurately represent the value assigned by a third party in an arms -length transaction. While our estimate of fair value and the associated charge to earnings materially affects our results of operations, it has no impact on our cash position.

Table of Contents

We recognize tax benefit upon expensing certain share-based awards associated with our share-based compensation plans, including nonqualified stock options and DSUs, but we cannot recognize tax benefit concurrent with the recognition of share-based compensation expenses associated with qualified stock options (incentive stock options and employee stock purchase plan shares). For qualified stock options that vested after we began to expense share-based compensation, we recognize tax benefit only in the period when disqualifying dispositions of the underlying stock occur, which historically has been up to several years after vesting and in a period when our stock price substantially increases. For qualified stock options that vested prior to when we began to expense share-based compensation, we record the tax benefit directly to additional paid-in capital.

We determine excess tax benefit using the long-haul method in which we compare the actual tax benefit associated with the tax deduction from share-based award activity to the hypothetical tax benefit on the grant date fair values of the corresponding share-based awards. Tax benefit associated with excess tax deduction creditable to additional paid-in capital is not recognized until the deduction reduces taxes payable.

Historically, we have issued new shares in connection with our share-based compensation plans; however, treasury shares were also available for issuance as of March 31, 2011. Any additional shares repurchased under our stock repurchase program would be available for issuance under our share-based compensation plans.

Stock Options

Our share-based compensation plans with outstanding stock option awards include our 1996 Plan, our 2001 Plan, and our 2010 Plan. We currently grant stock-based awards only under our 2010 Plan. Under the 2010 Plan, we may grant employees, consultants, and directors incentive stock options or nonqualified stock options to purchase shares of our common stock at not less than 100% of the fair market value, or FMV, on the date of grant. Stock options granted to our employees generally are incentive stock options, or qualified options, under the Internal Revenue Code, subject to calendar year vesting limitations with any balance being nonqualified stock options.

Stock option activity and weighted average exercise prices for options outstanding and exercisable, the weighted average exercise prices and the aggregate intrinsic value were as follows:

	Stock Option Awards Outstanding	Weighted Average Exercise Price	Aggregate Intrinsic Value (thousands)
Balance at June 30, 2010	7,748,570	$ 22.43	
Granted	1,141,323	28.98	
Exercised	(1,078,524)	14.35	
Forfeited	(410,058)	28.97	
Balance at March 31, 2011	7,401,311	24.25	$ 28,421
Exercisable at March 31, 2011	4,416,551	22.11	$ 26,843

The aggregate intrinsic value is based on the closing price of our common stock on March 25, 2011 and excludes stock options with exercise prices above the closing price of $26.98. Options granted under our 2010 Plan generally vest over four years from the vesting commencement date and expire seven years after the grant date if not exercised.

Deferred Stock Units

Our 2010 Plan enables us to grant DSUs to our employees, consultants, and directors. A DSU is a promise to deliver shares of our common stock at a future date in accordance with the terms of the DSU grant agreement.

Table of Contents

DSU activity, including DSUs granted, delivered, and forfeited, and the balance and aggregate intrinsic value of DSUs were as follows:

	DSU Awards Outstanding	Aggregate Intrinsic Value (thousands)
Balance at June 30, 2010	821,146	
Granted	330,231	
Delivered	(287,978)	
Forfeited	(72,539)	
Balance at March 31, 2011	790,860	$ 21,337

The aggregate intrinsic value is based on the closing price of our common stock on March 25, 2011 of $26.98.

DSUs granted under our 2010 Plan generally vest over four years from the vesting commencement date. Delivery of shares under our 2010 Plan takes place on quarterly vesting dates. At the delivery date, we withhold shares to cover statutory minimum tax withholding by delivering a net number of shares. Until delivery of shares, the grantee has no rights as a stockholder.

Of the shares delivered, 79,307 shares valued at $2.3 million were withheld to meet statutory minimum tax withholding requirements.

Employee Stock Purchase Plan

Our 2010 ESPP became effective in October 2010. Our 2010 ESPP allows employees to designate up to 15% of their base compensation, subject to legal restrictions and limitations, to purchase shares of common stock at 85% of the lesser of the FMV at the beginning of the offering period or the exercise date. The offering period extends for up to two years and includes four exercise dates occurring at six-month intervals. Under the terms of our 2010 ESPP, if the FMV at an exercise date is less than the FMV at the beginning of the offering period, the current offering period will terminate and a new two-year offering period will commence.

Shares purchased, weighted average purchase price, cash received, and the aggregate intrinsic value for employee stock purchase plan purchases during the nine-month period ended March 31, 2011 were as follows (in thousands, except for shares purchased and weighted average purchase price):

Shares purchased	320,745
Weighted average purchase price	$ 15.90
Cash received	$ 5,099
Aggregate intrinsic value	$ 3,995

The early termination of an offering period followed by the commencement of a new offering period represents a modification to the terms of the underlying awards. Under the terms of our 2001 ESPP, the offering period that commenced on July 1, 2007 was terminated on December 31, 2008 and a new offering period commenced on January 1, 2009. The December 31, 2008 modification affected approximately 257 employees. The modification resulted in incremental compensation costs, which were not material and which were recognized on a straight-line basis over the two-year period ending December 31, 2010.

10. Income Taxes

We account for income taxes under the asset and liability method. We consider the operating earnings of our foreign subsidiaries to be indefinitely invested outside the United States. Accordingly, no provision has been made for the federal, state, or foreign taxes that may result from future remittances of undistributed earnings of our foreign subsidiaries.

13

Table of Contents

The provision for income taxes of $1.2 million and $45,000 for the three months ended March 31, 2011 and 2010, respectively, represented estimated federal, foreign, and state taxes. The effective tax rate for the three months ended March 31, 2011 was 8.0% and diverged from the combined federal and state statutory rate primarily because of increased foreign income taxed at lower tax rates, the federal and state research credit, and the release of unrecognized tax benefits, partially offset by foreign withholding taxes and net unrecognized tax benefit associated with qualified stock options. The effective tax rate for the three months ended March 31, 2010 was 0.4% and diverged from the combined federal and state statutory rate primarily because of increased foreign income taxed at lower tax rates, the recognition of tax benefit on the carryback of a prior year net operating loss, the release of unrecognized tax benefits, and the benefit of research tax credits, partially offset by foreign withholding taxes and net unrecognized tax benefit associated with qualified stock options. We recorded a tax benefit of $1.8 million from the carryback of a prior year net operating loss, which represents a revision of tax benefits generated in fiscal 2008 and 2009.

The provision for income taxes of $7.0 million and $5.1 million for the nine months ended March 31, 2011 and 2010, respectively, represented estimated federal, foreign, and state taxes. The effective tax rate for the nine months ended March 31, 2011 was 12.4% and diverged from the combined federal and state statutory rate primarily because of increased foreign income taxed at lower tax rates, the release of unrecognized tax benefits, the retroactive reinstatement of the federal research credit, and the state research credit, partially offset by foreign withholding taxes and net unrecognized tax benefit associated with qualified stock options. The effective tax rate for the nine months ended March 31, 2010 was 13.3% and diverged from the combined federal and state statutory rate primarily because of increased foreign income taxed at lower tax rates, the recognition of tax benefit on the carryback of a prior year net operating loss, the release of unrecognized tax benefits, and the benefit of research tax credits, partially offset by foreign withholding taxes, net unrecognized tax benefit associated with qualified stock options, the impairment of an investment for which a full valuation allowance was established, and the establishment of a valuation allowance on certain deferred tax assets.

Unrecognized Tax Benefits

The total liability for gross unrecognized tax benefits decreased $1.0 million during the quarter ended March 31, 2011 to $19.6 million from $20.6 million at December 31, 2010. The liability for gross unrecognized tax benefit, if recognized, would reduce the effective tax rate on income from continuing operations. The net decrease consisted of a release of unrecognized tax benefit of $1.6 million because of statute expiration and an increase of $586,000 from current year tax positions. The balance of interest and penalties accrued related to unrecognized tax benefits as of March 31, 2011 was $1.5 million and was unchanged from December 31, 2010. We classify interest and penalties, if any, as components of income tax expense.

No material unrecognized tax benefit is expected to be paid within one year, and we cannot make a reliable estimate when cash settlement with a taxing authority may occur. Any prospective adjustments to our unrecognized tax benefits will be recorded as an increase or decrease to income tax expense and cause a corresponding change to our effective tax rate. Accordingly, our effective tax rate could fluctuate materially from period to period.

Our major tax jurisdictions are the United States, California, and Hong Kong SAR, and fiscal 2003 onward remain subject to examination by one or more of these jurisdictions.

On December 17, 2010, President Obama signed into law the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, or the Act. The Act in part retroactively reinstated the research credit to January 1, 2010. Accordingly, our year-to-date effective tax rate for fiscal 2011 includes the benefit of the retroactive reinstatement.

11. Segment, Customers, and Geographic Information

We operate in one segment: the development, marketing, and sale of custom-designed capacitive interface solutions that enable people to interact more easily and intuitively with a wide variety of electronic devices and products. We generate our revenue from two broad product categories: the personal computing, or PC, market and digital lifestyle product market. The PC market accounted for 43% and 63% of net revenue for the three months ended March 31, 2011 and 2010, respectively, and 47% and 60% of net revenue for the nine months ended March 31, 2011 and 2010, respectively.

Table of Contents

Net revenue within geographic areas based on our customers locations for the periods presented was as follows (in thousands):

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2011	2010	2011	2010
China	$ 91,212	$ 81,760	$ 302,849	$ 285,744
Japan	17,623	6,741	51,970	24,325
Taiwan	13,489	18,895	62,903	32,712
Korea	6,612	8,459	16,352	25,814
Other	13,470	357	21,098	532
	$ 142,406	$ 116,212	$ 455,172	$ 369,127

In March 2011, Japan experienced a significant earthquake, triggering a tsunami that resulted in widespread damage and business interruption. While we have not identified any material impact on our business and operations at this time and believe we have taken actions necessary to ensure our ability to deliver products to meet our customers demands, we cannot predict what impact, if any, the current interruptions in Japan may have on our business and operations in the future.
Major customers as a percentage of net revenue for the periods presented were as follows:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2011	2010	2011	2010
Customer A	*	12%	*	*
Customer B	*	10%	*	11%

* Less than 10%

We sell our products primarily to contract manufacturers that provide manufacturing services to original equipment manufacturers, or OEMs. We extend credit based on an evaluation of a customer s financial condition, and we generally do not require collateral. Major customer accounts receivable as a percentage of accounts receivable for the periods presented were as follows:

	As of March 31, 2011	As of June 30, 2010
Customer A	12%	15%
Customer B	10%	*
Customer C	*	15%

* Less than 10%

Table of Contents

12. Comprehensive Income

Our comprehensive income generally consists of net income plus the effect of unrealized gains and losses on our investments primarily due to changes in market value of certain of our ARS investments and interest rate fluctuations on our fixed interest rate investments. In addition, we recognize the noncredit portion of other-than-temporary impairment in comprehensive income. We recognize remeasurement adjustments in our consolidated statement of income as the U.S. dollar is the functional currency of our foreign entities.

Our comprehensive income was as follows (in thousands):

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2011	2010	2011	2010
Net income	$ 13,496	$ 11,606	$ 49,873	$ 33,637
Net unrealized gain/(loss) on available-for-sale investments, net of tax	716	(11)	1,396	1,575
Total comprehensive income	$ 14,212	$ 11,595	$ 51,269	$ 35,212

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

Forward-Looking Statements and Factors That May Affect Results

You should read the following discussion and analysis in conjunction with our unaudited condensed consolidated financial statements and notes in Item 1 and with our audited consolidated financial statements and notes included in our Annual Report on Form 10-K for the year ended June 30, 2010.

In addition to the historical information contained in this report, this report contains forward-looking statements, including those related to our operating model and strategies; our market penetration and market share in the PC and digital lifestyle product markets; competitive factors in the PC and digital lifestyle product markets; revenue from the PC and digital lifestyle product markets; industry estimates of growth rates of these markets; average selling prices; product design mix; manufacturing costs; cost-improvement programs; gross margins; customer relationships; research and development expenses; selling, general, and administrative expenses; liquidity and anticipated cash requirements; our ability to provide local sales, operational, and engineering support to customers, and our assessment of the combination of the added value we bring to our OEM customers products in meeting their custom design requirements and the impact of our ongoing cost improvement programs. These forward-looking statements involve risks and uncertainties that could cause actual results to differ materially.

We caution that these statements are qualified by various factors that may affect future results, including the following: economic conditions; changes in the market for our products and the success of our customers products; our success in moving products from the design phase into the manufacturing phase; changes in the competitive environment; infringement claims; warranty obligations related to product failures; the failure of key technologies to deliver commercially acceptable performance; our dependence on certain key markets; penetration into new markets; the absence of both long-term purchase and supply commitments; and our lengthy development and product acceptance cycles. This report should be read in conjunction with our Annual Report on Form 10-K for the year ended June 30, 2010, including particularly Item 1A Risk Factors.

Overview

We are a leading worldwide developer and supplier of custom-designed human interface solutions that enable people to interact more easily and intuitively with a wide variety of mobile computing, communications, entertainment, and other electronic devices. We believe our results to date reflect the combination of our customer focus, the strength of our intellectual property, and our engineering know-how, which allow us to develop or engineer products that meet the demanding design specifications of OEMs.

Many of our customers have migrated their manufacturing operations from Taiwan to China, and many of our OEM customers have established design centers in that region. With our expanded global presence, including offices in Canada, China, Finland, Hong Kong, Japan, Korea, Switzerland, Taiwan, and the United States, we are well positioned to provide local sales, operational, and engineering support services to our existing customers, as well as potential new customers, on a global basis.

Our manufacturing operations are based on a variable cost model in which we outsource all of our production requirements and generally drop ship our products directly to our customers from our contract manufacturers facilities, eliminating the need for significant capital expenditures and allowing us to minimize our investment in inventories. This approach requires us to work closely with our contract manufacturers to ensure adequate production capacity to meet our forecasted volume requirements. We provide our contract manufacturers with six-month rolling forecasts and issue purchase orders based on our anticipated requirements for the next 90 days. However, we do not have any long-term supply contracts with any of our contract manufacturers. We use two third-party wafer manufacturers to supply wafers and two third-party packaging manufacturers to package our proprietary ASICs. In certain cases, we rely on a single source or a limited number of suppliers to provide other key components of our products. Our cost of revenue includes all costs associated with the production of our products, including materials, logistics, manufacturing, assembly, and test costs paid to third-party manufacturers and related overhead costs associated with our indirect manufacturing operations personnel. Additionally, we charge all warranty costs, yield losses, and any inventory provisions or write-downs to cost of revenue.

Our gross margin generally reflects the combination of the added value we bring to our OEM customers products in meeting their custom design requirements and the impact of our ongoing cost-improvement programs. These cost-improvement programs include reducing materials and component costs and implementing design and process improvements. Our newly introduced products may have lower margins than our more mature products, which have realized greater benefits associated with our ongoing cost-improvement programs. As a result, new product introductions may initially negatively impact our gross margin.

Our research and development expenses include personnel costs and supplies and materials costs related to product development, as well as the engineering costs incurred to design capacitive interface solutions for OEM customers prior to and after their commitment to incorporate those solutions into their products. These expenses have generally increased, reflecting our continuing commitment to the technological and design innovation required to maintain our position in our existing markets and to adapt our existing technologies or develop new technologies for new markets.

Selling, general, and administrative expenses include expenses related to sales, marketing, and administrative personnel; internal sales and outside sales representatives commissions; market and usability research; outside legal, accounting, and consulting costs; and other marketing and sales activities. These expenses have generally increased, primarily reflecting incremental staffing and related support costs associated with our increased business levels, growth in our existing markets, and penetration into new markets.

Critical Accounting Policies and Estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue, expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, we evaluate our estimates, including those related to revenue recognition, allowance for doubtful accounts, inventories, product warranty, provision for income taxes, income taxes payable, intangible assets, and contingencies. We base our estimates on historical experience, applicable laws, and various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

The methods, estimates, interpretations, and judgments we use in applying our most critical accounting policies can have a significant impact on the results that we report in our consolidated financial statements. The SEC considers an entity s most critical accounting policies to be those policies that are both most important to the portrayal of the entity s financial condition and results of operations and those that require the entity s most difficult, subjective, or complex judgments, often as a result of the need to make estimates about matters that are inherently uncertain. We believe the following critical accounting policies affect our more significant judgments and estimates used in the preparation of our consolidated financial statements.

Revenue Recognition

We recognize revenue from product sales when there is persuasive evidence that an arrangement exists, delivery has occurred or title has transferred, the price is fixed or determinable, and collection is reasonably assured. We accrue for estimated sales returns and other allowances, based on historical experience, at the time we recognize revenue.

Investments

We record available-for-sale securities at fair value, with unrealized gains and losses being reported as a component of other comprehensive income and we assess whether our investments with loss positions are other-than-temporarily impaired. We follow the hierarchal approach to determine fair value of our investments.

The accounting standards define fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Our fair value estimates consider, among other factors, the collateral underlying the security investments, creditworthiness of the counterparty, timing of expected future cash flows, and, in the case of ARS investments, the probability of a successful auction in a future period. We follow the guidance provided to estimate fair value when the volume and level of activity for an asset or liability have significantly decreased in relation to normal market activity for the asset or liability and to determine circumstances that may indicate that a transaction is not orderly.

18

Table of Contents

Further, we use judgment in evaluating whether a decline in fair value is temporary or other-than-temporary and consider the following indicators: changes in credit ratings or asset quality; changes in the economic environment; length of time and extent to which fair value has been below cost basis; changes in market conditions; and changes in expected cash flows. We do not intend to sell the investments, and it is more likely than not that we will not be required to sell the investments before recovery of their amortized cost basis. We record temporary declines in fair value as charges to accumulated other comprehensive income in the equity section of our balance sheet, while other-than-temporary declines in fair value are bifurcated between credit losses, which are charged to earnings, and noncredit losses, which depending on the type of investment, may be charged to other comprehensive income or earnings.

Inventory

We state our inventories at the lower of cost or market. We base our assessment of the ultimate realization of inventories on our projections of future demand and market conditions. Sudden declines in demand, rapid product improvements, or technological changes, or any combination of these factors, can cause us to have excess or obsolete inventories. On an ongoing basis, we review for estimated obsolete or unmarketable inventories and write down our inventories to their net realizable value based upon our forecasts of future demand and market conditions. If actual market conditions are less favorable than our forecasts, additional inventory write-downs may be required. The following factors influence our estimates: changes to or cancellations of customer orders, unexpected decline in demand, rapid product improvements and technological advances, and termination or changes by our OEM customers of any product offerings incorporating our product solutions.

Periodically, we purchase inventory from our contract manufacturers when a customer delays its delivery schedule or cancels its order. In those circumstances in which our customer has cancelled its order and we purchase inventory from our contract manufacturers, we consider a write-down to reduce the carrying value of the inventory purchased to its net realizable value. We charge write-downs to reduce the carrying value of obsolete, slow moving, and non-usable inventory to net realizable value to cost of revenue. The effect of these write-downs is to establish a new cost basis in the related inventory, which we do not subsequently write up.

Share-Based Compensation Costs

We utilize the Black-Scholes option pricing model to estimate the grant date fair value of employee share-based compensatory awards, which requires the input of highly subjective assumptions, including expected volatility and expected life. Historical and implied volatilities were used in estimating the fair value of our share-based awards, while the expected life for our options was estimated based on historical trends since our initial public offering. Changes in these inputs and assumptions can materially affect the measure of estimated fair value of our share-based compensation. Further, we estimate forfeitures for share-based awards that are not expected to vest. We charge the estimated fair value less estimated forfeitures to earnings on a straight-line basis over the vesting period of the underlying awards, which is generally four years for our stock options and DSUs and up to two years for our ESPP.

The Black-Scholes option pricing model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. As our stock option and ESPP awards have characteristics that differ significantly from traded options, and as changes in the subjective assumptions can materially affect the estimated value, our estimate of fair value may not accurately represent the value assigned by a third party in an arms-length transaction. There currently is no market-based mechanism to verify the reliability and accuracy of the estimates derived from the Black-Scholes option pricing model or other allowable valuation models, nor is there a means to compare and adjust the estimates to actual values. While our estimate of fair value and the associated charge to earnings materially affects our results of operations, it has no impact on our cash position.

There are significant variations among allowable valuation models, and there is a possibility that we may adopt a different valuation model or refine the inputs and assumptions under our current valuation model in the future, resulting in a lack of consistency in future periods. Our current or future valuation model and the inputs and assumptions we make may also lack comparability to other companies that use different models, inputs, or assumptions, and the resulting differences in comparability could be material.

Income Taxes

We recognize federal, foreign, and state current tax liabilities or assets based on our estimate of taxes payable or refundable in the then current fiscal year for each tax jurisdiction. We also recognize federal, foreign, and state deferred tax liabilities or assets for our estimate of future tax effects attributable to temporary differences and carryforwards and record a valuation allowance to reduce any deferred tax assets by the amount of any tax benefits that, based on available evidence and our judgment, are not expected to be realized. If our assumptions, and consequently our estimates, change in the future, the valuation allowance we have established for our deferred tax assets may be changed, which could impact income tax expense.

Table of Contents

We use a two-step approach to recognizing and measuring uncertain tax positions. The first step is to determine whether it is more-likely-than-not that a tax position will be sustained upon examination, including resolution of any related appeals or litigation processes. The second step is to measure the tax benefit as the largest amount that is more than 50% likely of being realized upon ultimate settlement with a taxing authority. The calculation of tax liabilities involves significant judgment in estimating the impact of uncertainties in the application of highly complex tax laws. Resolution of these uncertainties in a manner inconsistent with our expectations could have a material impact on our consolidated financial position, result of operations, or cash flows. We believe we have adequately provided for reasonably foreseeable outcomes in connection with the resolution of income tax uncertainties. However, our results have in the past, and could in the future, include favorable and unfavorable adjustments to our estimated tax liabilities in the period a determination of such estimated tax liability is made or resolved, upon the filing of an amended return, upon a change in facts, circumstances, or interpretation, or upon the expiration of a statute of limitation. Accordingly, our effective tax rate could fluctuate materially from period to period.

We recognize tax benefit upon expensing nonqualified stock options and DSUs issued under our share-based compensation plans. However, under current accounting standards, we cannot recognize tax benefit concurrent with expensing qualified stock options (incentive stock options and employee stock purchase plan shares) issued under our share-based compensation plans. For qualified stock options that vested after our adoption of new accounting standards, we recognize tax benefit only in the period when disqualifying dispositions of the underlying stock occur, which historically has been up to several years after vesting and in periods when our stock price substantially increases. For qualified stock options that vested prior to our adoption of new accounting standards, we record the tax benefit directly to additional paid-in capital. Accordingly, because we cannot recognize the tax benefit for share-based compensation expense associated with qualified stock options until the occurrence of future disqualifying dispositions of the underlying stock and such disqualified dispositions may happen in periods when our stock price substantially increases, and because a portion of that tax benefit may be directly recorded to additional paid-in capital, our future quarterly and annual effective tax rates will be subject to greater volatility and, consequently, our ability to estimate reasonably our future quarterly and annual effective tax rates is greatly diminished.

Table of Contents

Results of Operations

Certain of our condensed consolidated statements of income data for the periods indicated, together with comparative absolute and percentage changes in these amounts, were as follows (in thousands, except percentages):

	Three Months Ended March 31,				Nine Months Ended March 31,			
	2011	2010	$ Change	% Change	2011	2010	$ Change	% Change
PC applications	$ 61,680	$ 72,936	$ (11,256)	(15.4%)	$ 211,559	$ 221,154	$ (9,595)	(4.3%)
Digital lifestyle product applications	80,726	43,276	37,450	86.5%	243,613	147,973	95,640	64.6%
Net revenue	142,406	116,212	26,194	22.5%	455,172	369,127	86,045	23.3%
Gross margin	57,616	47,302	10,314	21.8%	185,482	149,455	36,027	24.1%
Operating expenses:								
Research and development	25,956	21,212	4,744	22.4%	77,516	63,629	13,887	21.8%
Selling, general, and administrative	17,244	14,635	2,609	17.8%	51,750	44,974	6,776	15.1%
Income from operations	14,416	11,455	2,961	25.8%	56,216	40,852	15,364	37.6%
Interest income	242	200	42	21.0%	679	772	(93)	(12.0%)
Interest expense	(4)	(4)		0.0%	(13)	(2,395)	2,382	(99.5%)
Impairment (loss)/recovery of investment, net	10		10	n/m(1)	20	(443)	463	(104.5%)
Income before provision for income taxes	14,664	11,651	3,013	25.9%	56,902	38,786	18,116	46.7%
Provision for income taxes	1,168	45	1,123	2495.6%	7,029	5,149	1,880	36.5%
Net income	$ 13,496	$ 11,606	$ 1,890	16.3%	$ 49,873	$ 33,637	$ 16,236	48.3%

(1) not meaningful

Certain of our condensed consolidated statements of income data as a percentage of net revenue for the periods indicated were as follows:

	Three Months Ended March 31, 2011	Three Months Ended March 31, 2010	Percentage Point Increase (Decrease)	Nine Months Ended March 31, 2011	Nine Months Ended March 31, 2010	Percentage Point Increase (Decrease)
PC applications	43.3%	62.8%	(19.5%)	46.5%	59.9%	(13.4%)
Digital lifestyle product applications	56.7%	37.2%	19.5%	53.5%	40.1%	13.4%
Net revenue	100.0%	100.0%		100.0%	100.0%	
Gross margin	40.5%	40.7%	(0.2%)	40.7%	40.5%	0.2%
Operating expenses:						
Research and development	18.2%	18.3%	(0.1%)	17.0%	17.2%	(0.2%)
Selling, general, and administrative	12.1%	12.6%	(0.5%)	11.4%	12.2%	(0.8%)
Income from operations	10.1%	9.9%	0.2%	12.4%	11.1%	1.3%
Income before provision for income taxes	10.3%	10.0%	0.3%	12.5%	10.5%	2.0%
Provision for income taxes	0.8%	0.0%	0.8%	1.5%	1.4%	0.1%
Net income	9.5%	10.0%	(0.5%)	11.0%	9.1%	1.9%

Net Revenue.

Net revenue was $142.4 million for the quarter ended March 31, 2011 compared with $116.2 million for the quarter ended March 31, 2010, an increase of $26.2 million, or 22.5%. Of our third quarter fiscal 2011 net revenue, $61.7 million, or 43.3%, was from PC products and $80.7 million, or 56.7%, was from digital lifestyle products, including $80.0 million from mobile products. The increase in net revenue for the quarter ended March 31, 2011 was attributable to a $37.5 million, or a 86.5%, increase in net revenue from digital lifestyle product applications, partially offset by a $11.3 million, or 15.4%, decrease in net revenue from PC applications. The overall increase in net revenue was primarily attributable to a 16% increase in total unit shipments reflecting higher demand for our products in the digital lifestyle market, as well as a slightly higher priced product mix, partially offset by a decline in unit shipments in the PC market, primarily reflecting general softness in consumer notebook demand.

Table of Contents

Net revenue was $455.2 million for the nine months ended March 31, 2011 compared with $369.1 million for the nine months ended March 31, 2010, an increase of $86.0 million, or 23.3%. Of our nine months fiscal 2011 net revenue, $211.6 million, or 46.5%, was from PC applications and $243.6 million, or 53.5%, was from digital lifestyle products applications, including $240.0 million from mobile products. The increase in net revenue for the nine months ended March 31, 2011 was attributable to a $95.6 million, or 64.6%, increase in net revenue from digital lifestyle product applications, and a $9.6 million, or 4.3%, decrease in net revenue from PC applications. The overall increase in net revenue was primarily attributable to a 15% increase in total unit shipments, reflecting higher demand for our products in the digital lifestyle markets, as well as a slightly higher priced product mix, partially offset by a decline in unit shipments in the PC market, primarily reflecting general softness in consumer notebook demand.

In March 2011, Japan experienced a significant earthquake, triggering a tsunami that resulted in widespread damage and business interruption. While we have not identified any material impact on our business and operations at this time and believe we have taken actions necessary to ensure our ability to deliver products to meet our customers demands, we cannot predict what impact, if any, the current interruptions in Japan may have on our business and operations in the future.

Based on calendar year 2011 industry estimates, the notebook market is anticipated to increase approximately 10% and the mobile smartphone market is anticipated to increase approximately 49% over 2010 levels.

Gross Margin.

Gross margin as a percentage of net revenue was 40.5%, or $57.6 million, for the quarter ended March 31, 2011 compared with 40.7%, or $47.3 million, for the quarter ended March 31, 2010. Gross margin as a percentage of net revenue was 40.7%, or $185.5 million, for the nine months ended March 31, 2011 compared with 40.5%, or $149.5 million, for the nine months ended March 31, 2010.

As each custom-designed module we sell utilizes our capacitive sensing technology in a design that is generally unique or specific to a customer s application, gross margin varies on a product-by-product basis, making our cumulative gross margin a blend of our product specific designs and independent of the vertical markets that our products serve.

Operating Expenses.

Research and Development Expenses. Research and development expenses decreased slightly as a percentage of net revenue to 18.2% from 18.3%, while the cost of research and development activities increased $4.7 million, or 22.4%, to $26.0 million for the quarter ended March 31, 2011 compared with $21.2 million for the quarter ended March 31, 2010. The increase in research and development expenses primarily reflected a $2.0 million increase in employee related costs, a $1.3 million increase in temporary services, and an $894,000 increase in infrastructure and support costs for the additional staffing.

Research and development expenses decreased as a percentage of net revenue to 17.0% from 17.2%, while the cost of research and development activities increased $13.9 million, or 21.8%, to $77.5 million for the nine-month period ended March 31, 2011 compared with $63.6 million for the nine-month period ended March 31, 2010. The increase in research and development expenses primarily reflected a $6.1 million increase in employee related costs, a $3.7 million increase in temporary services, and a $2.9 million increase in infrastructure and support costs for the additional staffing.

Selling, General, and Administrative Expenses. Selling, general, and administrative expenses decreased as a percentage of net revenue to 12.1% from 12.6%, while the cost of selling, general, and administrative activities increased to $17.2 million for the three-month period ended March 31, 2011 compared with $14.6 million for the three-month period ended March 31, 2010. The increase in selling, general, and administrative expenses primarily reflected a $1.4 million increase in employee related costs, and a $1.1 million increase in infrastructure and support costs for the additional staffing.

Selling, general, and administrative expenses decreased as a percentage of net revenue to 11.4% from 12.2%, while the cost of selling, general, and administrative activities increased to $51.8 million for the nine-month period ended March 31, 2011 compared with $45.0 million for the nine-month period ended March 31, 2010. The increase in selling, general, and administrative expenses included $2.7 million of non-recurring executive officer resignation costs, a $2.0 million increase in employee related costs, and a $3.2 million increase in infrastructure and support costs.

Interest Expense. All of our interest expense related to our convertible notes issued in December 2004. Interest expense was $4,000 for each of the three months ended March 31, 2011 and 2010.

Table of Contents

Interest expense was $13,000 for the nine months ended March 31, 2011 compared with interest expense of $2.4 million, of which $2.1 million represents debt issuance cost amortization, for the nine months ended March 31, 2010. During fiscal 2010, $63.0 million of convertible notes were retired, leaving $2.3 million outstanding as of June 30, 2010 and March 31, 2011.

Provision for Income Taxes.

We account for income taxes under the asset and liability method. We consider the operating earnings of our foreign subsidiaries to be indefinitely invested outside the United States. Accordingly, no provision has been made for the U.S. federal, state, or foreign taxes that may result from future remittances of undistributed earnings of our foreign subsidiaries.

The provision for income taxes of $1.2 million and $45,000 for the three months ended March 31, 2011 and 2010, respectively, represented estimated federal, foreign, and state taxes. The effective tax rate for the three months ended March 31, 2011 was 8.0% and diverged from the combined federal and state statutory rate primarily because of increased foreign income taxed at lower tax rates, the federal and state research credit, and the release of unrecognized tax benefit, partially offset by foreign withholding taxes and net unrecognized tax benefits associated with qualified stock options. The effective tax rate for the three months ended March 31, 2010 was 0.4% and diverged from the combined federal and state statutory rate primarily because of increased foreign income taxed at lower tax rates, the recognition of tax benefit on the carryback of a prior year net operating loss, the release of unrecognized tax benefits, and the benefit of research tax credits, partially offset by foreign withholding taxes and net unrecognized tax benefit associated with qualified stock options. We recorded a tax benefit of $1.8 million from the carryback of a prior year net operating loss, which represents a revision of tax benefits generated in fiscal 2008 and 2009.

Tax benefit associated with share-based compensation was approximately $2.3 million and $1.7 million for the three months ended March 31, 2011 and 2010, respectively. Excluding the impact of share-based compensation and the related tax benefit, the effective tax rate for the three months ended March 31, 2011 and 2010 would have been 15.3% and 9.0%, respectively.

The provision for income taxes of $7.0 million and $5.1 million for the nine months ended March 31, 2011 and 2010, respectively, represented estimated federal, foreign, and state taxes. The effective tax rate for the nine months ended March 31, 2011 was 12.4% and diverged from the combined federal and state statutory rate primarily because of increased foreign income taxed at lower tax rates, the release of unrecognized tax benefits, the retroactive reinstatement of the federal research credit, and the state research credit, partially offset by foreign withholding taxes and net unrecognized tax benefits associated with qualified stock options. The effective tax rate for the nine months ended March 31, 2010 was 13.3% and diverged from the combined federal and state statutory rate primarily because of increased foreign income taxed at lower tax rates, the recognition of tax benefit on the carryback of a prior year net operating loss, the release of unrecognized tax benefits, and the benefit of research tax credits, partially offset by foreign withholding taxes, net unrecognized tax benefits associated with qualified stock options, the impairment of an investment for which a full valuation allowance was established, and the establishment of a valuation allowance on certain deferred tax assets.

Tax benefit associated with share-based compensation was approximately $7.4 million and $7.0 million for the nine months ended March 31, 2011 and 2010, respectively. Excluding the impact of share-based compensation and the related tax benefit, the effective tax rate for the nine months ended March 31, 2011 and 2010 would have been 17.5% and 18.4%, respectively.

Table of Contents

Liquidity and Capital Resources

Our cash and cash equivalents were $246.3 million as of March 31, 2011 compared with $209.9 million as of June 30, 2010, an increase of $36.4 million. The increase reflects the combination of $64.5 million provided from operating cash flows and $20.6 million from the issuance of common stock under our share-based compensation plans, partially offset by $40.2 million used to repurchase 1,451,180 shares of our common stock and $9.6 million used for the purchase of capital equipment.

Cash Flows from Operating Activities. Operating activities during the nine months ended March 31, 2011 generated cash of $64.5 million compared with $77.6 million of cash generated during the nine months ended March 31, 2010. For the nine months ended March 31, 2011, net cash provided by operating activities was primarily attributable to net income of $49.9 million plus adjustments for non-cash charges of $31.6 million, partially offset by a $17.0 million net increase in operating assets and liabilities. The net increase in operating assets and liabilities was primarily attributable to a $14.0 million increase in inventory. Our days sales outstanding decreased from 63 to 62 days from June 30, 2010 to March 31, 2011 and our inventory turns decreased from 19 to 10 for the same period, reflecting an increase in our ASIC die bank and other components.

Cash Flows from Investing Activities. Our investing activities typically relate to purchases of government-backed securities and investment-grade fixed income instruments and purchases of property and equipment. Investing activities during the nine months ended March 31, 2011 used net cash of $9.3 million compared with $17.8 million of net cash generated during the nine months ended March 31, 2010. During the nine months ended March 31, 2011, net cash used in investing activities consisted of $9.6 million used for the purchase of property and equipment, partially offset by proceeds of $350,000 from non-current investments.

Cash Flows from Financing Activities. Net cash used in financing activities for the nine months ended March 31, 2011 was approximately $18.8 million compared with $95.7 million net cash used in financing activities for the nine months ended March 31, 2010. Cash used in financing activities for the nine months ended March 31, 2011 included $40.2 million used to repurchase 1,451,180 shares of our common stock and $2.3 million used for the payment of payroll taxes for DSUs, partially offset by $20.6 million of proceeds from common stock issued under our share-based compensation plans.

Common Stock Repurchase Program. Our Board of Directors has cumulatively authorized $420.0 million for our common stock repurchase program. The program authorizes us to purchase our common stock in the open market or in privately negotiated transactions depending upon market conditions and other factors. The number of shares repurchased and the timing of repurchases is based on the level of our cash balances, general business and market conditions, and other factors, including alternative investment opportunities. We hold common stock repurchased under this program as treasury stock. From April 2005 through March 31, 2011, we repurchased 12,322,493 shares of our common stock in the open market for an aggregate cost of $322.1 million. Treasury shares purchased prior to August 28, 2008 were not subject to the stock split on that date, if adjusted for the stock split the average cost would be $19.10. As of March 31, 2011, we had $97.9 million available under our common stock repurchase program, which expires in April 2012.

Bank Credit Facility. We currently maintain a $40.0 million unsecured working capital line of credit with Wells Fargo Bank. The Wells Fargo Bank revolving line of credit, which expires on September 1, 2011, provides for an interest rate equal to the prime lending rate or 250 basis points above LIBOR, depending on whether we choose a variable or fixed rate, respectively. We had not borrowed any amounts under the line of credit as of March 31, 2011.

$250 Million Shelf Registration. We have registered an aggregate of $250.0 million of common stock (including the associated rights), preferred stock, debt securities, depositary shares, warrants, purchase contracts, and units (collectively securities) for issuance to raise funds for general corporate purposes, which may include the repayment of indebtedness outstanding from time to time, working capital, capital expenditures, acquisitions, and repurchases of our common stock or other securities. Securities issued under the shelf registration generally will be freely tradeable after their issuance unless held by an affiliate of our company, in which case such shares will be subject to the volume and manner of sale restrictions of Rule 144.

$100 Million Shelf Registration. We have registered an aggregate of $100.0 million of common stock and preferred stock for issuance in connection with acquisitions, which shares generally will be freely tradeable after their issuance

under Rule 145 of the Securities Act unless held by an affiliate of the acquired company, in which case such shares will be subject to the volume and manner of sale restrictions of Rule 144.

Table of Contents

Liquidity and Capital Resources. We believe our existing cash and cash equivalents and anticipated cash flows from operating activities will be sufficient to meet our working capital and other cash requirements for at least the next 12 months. Our future capital requirements will depend on many factors, including our revenue, the timing and extent of spending to support product development efforts, costs related to protecting our intellectual property, the expansion of sales and marketing activities, the timing of introductions of new products and enhancements to existing products, the costs to ensure access to adequate manufacturing capacity, the continuing market acceptance of our product solutions, our common stock repurchase program, and the amount and timing of our investments in, or acquisitions of, other technologies or companies. Further equity or debt financing may not be available to us on acceptable terms or at all. If sufficient funds are not available or are not available on acceptable terms, our ability to take advantage of unexpected business opportunities or to respond to competitive pressures could be limited or severely constrained.

Our non-current investments consist of ARS investments, which have failed to settle in auctions. These failures generally resulted in the interest rates resetting on the regularly scheduled auction dates. These investments are not liquid, and in the event we need to access these funds, we will not be able to do so without a loss of principal, unless redeemed by the issuers or a future auction on these investments is successful. Based on our ability to access our cash and other short-term investments, our expected operating cash flows, and our other sources of cash, we do not anticipate the lack of liquidity on these investments will affect our ability to operate our business as usual.

Contractual Obligations and Commercial Commitments

Our material contractual obligations and commercial commitments as of March 31, 2011 were as follows (in millions):

	Payments due by period				
Contractual Obligations	Total	Less than 1 year	1-3 Years	3-5 Years	More than 5 Years
Convertible senior subordinated notes (1)	$ 3	$	$	$	$ 3
Leases	6	3	3		
Purchase obligations and other commitments	17	7	6	4	
Total	$ 26	$ 10	$ 9	$ 4	$ 3

(1) Represents both principal and interest payable through the maturity date of the underlying contractual obligations.

As of March 31, 2011, we were unable to make a reasonably reliable estimate of when cash settlement with a taxing authority may occur in connection with our unrecognized tax benefits of $19.6 million.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our market risk has not changed significantly from the interest rate and foreign currency risks disclosed in Item 7A of our Annual Report on Form 10-K for the fiscal year ended June 30, 2010.

ITEM 4. CONTROLS AND PROCEDURES

As of the end of the period covered by this report, our Interim Chief Executive Officer and Chief Financial Officer have reviewed and evaluated the effectiveness of our disclosure controls and procedures, which included inquiries made to certain other of our employees. Based on their evaluation, our Interim Chief Executive Officer and Chief Financial Officer have each concluded that our disclosure controls and procedures are designed and are effective to ensure that information required to be disclosed is accumulated and communicated to our management, including our Interim Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure and are effective and sufficient to ensure that we record, process, summarize, and report information required to be disclosed by us in our periodic reports filed under the Securities Exchange Act of 1934, as amended, within the time periods specified by the SEC s rules and forms.

During the fiscal quarter covered by this report, there have not been any changes in our internal control over financial reporting that have materially affected, or a reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

None.

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

Issuer Purchases of Equity Securities

Our Board of Directors has cumulatively authorized $420.0 million for our common stock repurchase program. The remaining amount authorized for the repurchase of our common stock is $97.9 million. There were no repurchases under the stock repurchase program during the three-month period ended March 31, 2011.

ITEM 6. EXHIBITS

31.1	Certification of Chief Executive Officer
31.2	Certification of Chief Financial Officer
32.1	Section 1350 Certification of Chief Executive Officer
32.2	Section 1350 Certification of Chief Financial Officer
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema Document
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document

* Pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.

Table of Contents

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.

SYNAPTICS INCORPORATED

Date: April 29, 2011

By: /s/ Russell J. Knittel

Name: Russell J. Knittel
Title: Interim President and Chief Executive Officer

By: /s/ Kathleen A. Bayless

Name: Kathleen A. Bayless
Title: Chief Financial Officer, Secretary, and Treasurer

28