

MICROSEMI CORP  
Form 10-Q  
August 02, 2016

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 20549

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FORM 10-Q

(Mark One)

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

For the Quarterly Period ended July 3, 2016

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission file number # 000-08866

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MICROSEMI CORPORATION

(Exact name of Registrant as specified in its charter)

Delaware 95-2110371

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

One Enterprise, Aliso Viejo, California 92656

(Address of principal executive offices) (Zip Code)

(949) 380-6100

Registrant's telephone number, including area code

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding twelve months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ 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 (section 232.405 of this chapter) during the preceding twelve months (or for such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐

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

Large Accelerated Filer ☒ Accelerated Filer ☐

Non-Accelerated Filer ☐ Smaller Reporting Company ☐

(Do not check if a smaller reporting company)

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

The number of outstanding shares of Common Stock on July 27, 2016 was 113,188,059.

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## IMPORTANT FACTORS RELATED TO FORWARD-LOOKING STATEMENTS AND ASSOCIATED RISKS

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

- expectations that we will be able to successfully integrate acquired companies and personnel with our existing operations;
- expectations regarding our liquidity and capital resources, including our loan covenants;
- demand, growth and sales expectations for our products;
- expectations that plant consolidations will result in anticipated cost savings without unanticipated costs or expenses;
- expectations regarding tax exposures and future tax rates, our ability to realize deferred tax assets and the outcome or effects of examinations by U.S., state or foreign jurisdictions;
- expectations regarding competitive conditions;
- new market opportunities and emerging applications for our products;
- expectations concerning the anticipated benefits of our acquisitions;
- expectations that we will be able to identify or complete prospective acquisitions in a market with increasing competition from other potential acquirers, the effects of a consolidating semiconductor industry and high valuations of acquisition candidates;
- the uncertainty of litigation, administrative and similar matters, the associated costs and expenses, and the potential material adverse effect that these matters could have on our business and results of operations;
- beliefs our customers will not cancel orders or terminate or renegotiate their purchasing relationships with us and will pay receivables when contractually due;
- expectations concerning the potential termination or renegotiation of U.S. government contracts, uncertainties of governmental appropriations and national defense policies and priorities and the effects of past or future government shutdowns and contract terminations or renegotiations on our business and results of operations;
- expectations that we will not suffer production delays as a result of a supplier's inability to supply parts;
- the effect of events such as natural disasters and related disruptions on our operations;
- beliefs that we stock adequate supplies of all materials;
- beliefs that we will be able to successfully resolve any disputes and other business matters as anticipated;
- beliefs that we will be able to meet our operating cash and capital commitment requirements in the foreseeable future;
- critical accounting estimates;
- expectations regarding our financial and operating results;

• expectations regarding our performance and competitive position in future periods; and  
• expectations regarding our outlook for our end markets.

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

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

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The unaudited condensed consolidated statements of operations and comprehensive income (loss) for the quarter and nine months ended July 3, 2016 of Microsemi Corporation and its subsidiaries (which we herein refer to collectively as "Microsemi," "the Company," "we," "our," "ours" or "us"), the unaudited condensed consolidated statement of cash flows for nine months ended July 3, 2016, and the comparative unaudited condensed consolidated financial statements for the corresponding period of the prior year, together with the unaudited condensed consolidated balance sheets as of July 3, 2016 and September 27, 2015, are included herein.

The unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q, and therefore do not include all information and note disclosures necessary for a fair statement of our consolidated financial position, results of operations and cash flows in conformity with United States generally accepted accounting principles. The unaudited condensed consolidated financial statements and notes thereto must be read in their entirety in conjunction with the consolidated financial statements and notes thereto in our Annual Report on Form 10-K for the fiscal year ended September 27, 2015.

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## MICROSEMI CORPORATION AND SUBSIDIARIES

## Condensed Consolidated Balance Sheets

(unaudited, amounts in millions, except par value)

	July 3, 2016	September 27, 2015
Assets		
Current assets:		
Cash and cash equivalents	\$ 131.8	\$ 256.4
Accounts receivable, net of allowances of \$36.0 at July 3, 2016 and \$26.0 at September 27, 2015	241.7	186.9
Inventories	231.2	227.2
Deferred income taxes, net	26.2	26.2
Other current assets	52.8	39.9
Total current assets	683.7	736.6
Property and equipment, net	179.8	152.7
Goodwill	2,447.7	1,139.3
Intangible assets, net	974.2	357.8
Deferred income taxes, net	19.8	26.8
Other assets	59.3	36.9
Total assets	\$4,364.5	\$ 2,450.1
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$ 116.7	\$ 82.3
Accrued liabilities	158.7	86.8
Current maturity of long term debt	40.7	32.5
Total current liabilities	316.1	201.6
Long term debt	2,186.7	953.9
Deferred income taxes	80.4	41.1
Other long-term liabilities	107.2	46.3
Commitments and contingencies (Note 10)		
Stockholders' equity:		
Preferred stock, \$1.00 par value; authorized 1 share; none issued	—	—
Common stock, \$0.20 par value; 250.0 authorized, 113.2 issued and outstanding at July 3, 2016 and 95.1 issued and outstanding at September 27, 2015	22.6	19.0
Capital in excess of par value of common stock	1,341.9	808.1
Retained earnings	310.1	383.2
Accumulated other comprehensive loss	(0.5)	(3.1)
Total stockholders' equity	1,674.1	1,207.2
Total liabilities and stockholders' equity	\$4,364.5	\$ 2,450.1

The accompanying notes are an integral part of these statements.

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## MICROSEMI CORPORATION AND SUBSIDIARIES

## Condensed Consolidated Statements of Operations and Comprehensive Income (Loss)

(unaudited, amounts in millions, except earnings per share)

	Quarter Ended		Nine Months Ended	
	July 3, 2016	June 28, 2015	July 3, 2016	June 28, 2015
Net sales	\$431.4	\$317.1	\$1,204.9	\$916.8
Cost of sales (excluding amortization of intangible assets below)	164.5	145.0	549.6	407.4
Gross profit	266.9	172.1	655.3	509.4
Operating expenses				
Selling, general and administrative	82.9	66.7	265.8	187.7
Research and development	83.0	52.3	225.7	146.3
Amortization of intangible assets	44.9	24.8	115.6	71.1
Restructuring and severance charges	4.9	3.1	58.3	14.0
Total operating expenses	215.7	146.9	665.4	419.1
Operating income (loss)	51.2	25.2	(10.1 )	90.3
Other income (expense)				
Interest expense, net	(46.8 )	(7.4 )	(93.0 )	(19.5 )
Other expense, net	(5.3 )	(0.6 )	(83.7 )	(1.4 )
Gain on divestiture	125.5	—	125.5	—
Total other income (expense)	73.4	(8.0 )	(51.2 )	(20.9 )
Income (loss) before income taxes	124.6	17.2	(61.3 )	69.4
Provision for income taxes	9.4	2.5	11.8	10.2
Net income (loss)	\$115.2	\$14.7	\$(73.1 )	\$59.2
Earnings (loss) per share:				
Basic	\$1.03	\$0.16	\$(0.69 )	\$0.63
Diluted	\$1.00	\$0.15	\$(0.69 )	\$0.62
Weighted-average common shares outstanding:				
Basic	112.1	94.5	105.3	94.1
Diluted	114.6	96.4	105.3	95.6
Net income (loss)	\$115.2	\$14.7	\$(73.1 )	\$59.2
Other comprehensive income (loss), net of tax:				
Translation adjustment	0.2	0.4	2.8	(1.4 )
Unrealized actuarial loss on pension benefits	(0.1 )	(0.1 )	(0.2 )	(0.2 )
Other comprehensive income (loss), net of tax	0.1	0.3	2.6	(1.6 )
Total comprehensive income (loss)	\$115.3	\$15.0	\$(70.5 )	\$57.6

The accompanying notes are an integral part of these statements.

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## MICROSEMI CORPORATION AND SUBSIDIARIES

## Condensed Consolidated Statements of Cash Flows

(unaudited, amounts in millions)

	Nine Months Ended	
	July 3, 2016	June 28, 2015
Cash flows from operating activities:		
Net income (loss)	\$(73.1 )	\$59.2
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	150.2	98.0
Change in allowance for doubtful accounts	0.8	(0.1 )
Amortization of deferred financing cost	30.4	0.9
Gain on divestiture	(125.5 )	—
Loss on disposition or impairment of assets	1.3	2.5
Deferred income taxes	7.1	5.3
Charge for stock-based compensation	80.3	35.9
Change in assets and liabilities (net of acquisitions and divestitures):		
Accounts receivable	(18.7 )	4.1
Inventories	64.4	3.3
Other current assets	0.3	(4.3 )
Other assets	0.8	(5.5 )
Accounts payable	(33.8 )	(4.6 )
Accrued liabilities	(33.7 )	(1.5 )
Other long-term liabilities	21.5	(1.6 )
Net cash provided by operating activities	72.3	191.6
Cash flows from investing activities:		
Purchases of property and equipment	(34.2 )	(34.9 )
Proceeds from the sale of short term investments	0.3	0.4
Proceeds from divestitures	321.0	—
Payments for acquisitions, net of cash acquired	(1,671.3 )	(363.6 )
Net cash used in investing activities	(1,384.2 )	(398.1 )
Cash flows from financing activities:		
Proceeds from debt	3,494.4	425.0
Repayments of debt	(1,082.2 )	(142.7 )
Payments of debt issuance costs	(53.8 )	(8.7 )
Extinguishment of debt	(1,136.8 )	—
Repurchase of common stock	—	(50.0 )
Payments for stock settled tax withholdings	(38.4 )	(17.7 )
Proceeds from exercise of stock options	4.1	42.4
Net cash provided by financing activities	1,187.3	248.3
Net increase (decrease) in cash and cash equivalents	(124.6 )	41.8
Cash and cash equivalents at beginning of period	256.4	162.2
Cash and cash equivalents at end of period	\$131.8	\$204.0

The accompanying notes are an integral part of these statements.





Microsemi Corporation and Subsidiaries  
Notes to Unaudited Condensed Consolidated Financial Statements

Note 1 Presentation of Financial Information

The unaudited condensed consolidated financial statements include the accounts of Microsemi Corporation and its subsidiaries. Intercompany transactions have been eliminated in consolidation.

The condensed consolidated financial statements are unaudited, but in the opinion of our management, include all adjustments (all of which are normal or recurring adjustments) necessary for a fair statement of the results of operations for the periods indicated. The results of operations for the most recently reported quarter and nine months ended July 3, 2016 are not necessarily indicative of the results to be expected for the full year.

The unaudited condensed consolidated financial statements have been prepared in accordance with the requirements of Form 10-Q and Article 10 of the Securities and Exchange Commission Regulation S-X, and therefore do not include all information and note disclosures necessary for a fair statement of our consolidated financial position, results of operations and cash flows in conformity with United States generally accepted accounting principles. The unaudited condensed consolidated financial statements and notes thereto must be read in their entirety in conjunction with the consolidated financial statements and notes thereto in our Annual Report on Form 10-K for the fiscal year ended September 27, 2015.

The unaudited condensed consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles, which require us to make estimates and assumptions that may materially affect the reported amounts of assets and liabilities at the date of the unaudited condensed consolidated financial statements and revenues and expenses during the periods reported. Actual results could differ materially from those estimates. Information with respect to our accounting policies that we believe could have the most significant effect on our reported results and require subjective or complex judgments is contained in the notes to the consolidated financial statements in our Annual Report on Form 10-K for the fiscal year ended September 27, 2015. In referencing a year, we are referring to the fiscal year ended on the Sunday closest to September 30. Except for per-share amounts, dollar amounts are presented in millions unless otherwise stated.

Earnings Per Share

Basic earnings per share have been computed based upon the weighted-average number of common shares outstanding during the respective periods. Diluted earnings per share have been computed, when the result is dilutive, using the treasury stock method for stock awards outstanding during the respective periods. Earnings per share were calculated as follows:

	Quarter Ended		Nine Months Ended	
	July 3, 2016	June 28, 2015	July 3, 2016	June 28, 2015
<b>Basic</b>				
Net income (loss)	\$ 115.2	\$ 14.7	\$(73.1)	\$ 59.2
Weighted-average common shares outstanding	112.1	94.5	105.3	94.1
Basic earnings (loss) per share	\$ 1.03	\$ 0.16	\$(0.69)	\$ 0.63
<b>Diluted</b>				
Net income (loss)	\$ 115.2	\$ 14.7	\$(73.1)	\$ 59.2
Weighted-average common shares outstanding for basic	112.1	94.5	105.3	94.1
Dilutive effect of stock awards	2.5	1.9	—	1.5
Weighted-average common shares outstanding on a diluted basis	114.6	96.4	105.3	95.6
Diluted earnings (loss) per share	\$ 1.00	\$ 0.15	\$(0.69)	\$ 0.62

For the quarter ended July 3, 2016, we excluded 0.2 million of stock awards in the computation of diluted earnings per share as these stock awards would have been anti-dilutive. For nine months ended July 3, 2016, all stock awards were

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Microsemi Corporation and Subsidiaries  
Notes to Unaudited Condensed Consolidated Financial Statements

excluded as we reported a net loss in this period. For the quarter and nine months ended June 28, 2015, we excluded 0.1 million and 0.3 million, respectively, of stock awards in the computation of diluted earnings per share as these stock awards would have been anti-dilutive.

Recently Issued Accounting Standards

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-09 which provides guidance on how an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the Entity expects to be entitled in exchange for those goods or services and on accounting for costs to obtain or fulfill a contract with a customer. The ASU also requires expanded disclosure regarding the nature, amount, timing and uncertainty of revenue that is recognized. In July 2015, the FASB decided to delay the effective date of this ASU by one year. ASU 2014-09 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2017, and can be adopted either retrospectively to each prior reporting period presented or as a cumulative-effect adjustment as of the date of adoption, with early application permitted as of the original effective date. In March 2016, the FASB issued ASU No. 2016-08, Revenue from Contracts with Customers (Topic 606) – Principal versus Agent Considerations, which clarifies the implementation guidance for principal versus agent considerations in ASU 2014-09. In April 2016, the FASB issued ASU No. 2016-10, Revenue from Contracts with Customers (Topic 606) – Identifying Performance Obligations and Licensing, which amends the guidance in ASU 2014-09 related to identifying performance obligations and accounting for licenses of intellectual property. We are currently assessing the adoption and impact of these ASUs on our consolidated financial position and results of operations.

In January 2016, the FASB issued ASU No. 2016-01, Financial Instruments – Overall (Subtopic 825-10), which updates certain aspects of recognition, measurement, presentation and disclosure of financial instruments. ASU 2016-01 is effective for annual periods beginning in our first quarter of 2019. We are currently assessing the impact of this ASU on our consolidated financial position and results of operations.

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842), which modified lease accounting for both lessees and lessors to increase transparency and comparability by recognizing lease assets and lease liabilities by lessees for those leases classified as operating leases under previous accounting standards and disclosing key information about leasing arrangements. ASU 2016-02 is effective for annual periods beginning after December 15, 2018. We are currently evaluating the timing of its adoption and the impact of adopting the new lease standard on our consolidated financial position and results of operations.

In March 2016, the FASB issued ASU No. 2016-09, Compensation-Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting. Several aspects of the accounting for share-based payment award transactions are simplified, including: (a) income tax consequences; (b) classification of awards as either equity or liabilities; (c) classification on the statement of cash flows; and (d) classification of related deferred tax balances as non-current. The amendments in this update are effective for annual periods beginning after December 16, 2016, and interim periods within those fiscal years. We are currently assessing the impact of this ASU on our consolidated financial position and results of operations.

Note 2 Acquisition and Divestitures

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Acquisition

On January 15, 2016 (the "Acquisition Date"), we acquired all outstanding shares of PMC-Sierra, Inc. ("PMC"), for \$2.0 billion in cash and the issuance of approximately 16.0 million shares of Microsemi common stock and the assumption of certain PMC restricted stock units. The acquisition has provided Microsemi with a leading position in high performance and scalable storage solutions, while also adding a complementary portfolio of high-value communications products.



Microsemi Corporation and Subsidiaries  
Notes to Unaudited Condensed Consolidated Financial Statements

A summary of the consideration for PMC is as follows:

Cash consideration	\$1,983.2
Share consideration	476.2
Assumption of equity awards	15.7
Accrued cash consideration	0.3
Total consideration	\$2,475.4

We recorded PMC's tangible and intangible assets and liabilities based on their estimated fair values as of the Acquisition Date and allocated the remaining purchase consideration to goodwill. The preliminary allocation is as follows:

Cash and cash equivalents	\$313.0
Accounts receivable	53.3
Inventories	98.2
Other current assets	15.8
Property and equipment	38.0
Other assets	19.7
Identifiable intangible assets	741.6
Goodwill	1,435.0
Deferred income taxes, net	(39.3 )
Current liabilities	(139.4 )
Other non-current liabilities	(60.5 )
Total consideration	\$2,475.4

As of the Acquisition Date, the gross contractual amount of acquired accounts receivable of \$53.3 million was expected to be fully collected.

The valuation of identifiable intangible assets and their estimated useful lives are as follows:

	Asset	Weighted Average Useful Life (Years)
Completed technology	\$ 447.0	6
In-process research and development	241.0	
Customer relationships	46.0	9
Other	7.6	1
	\$ 741.6	

#### Valuation methodology

The fair value of completed technology and in-process research and development ("IPR&D") was estimated by performing a discounted cash flow analysis using the multiperiod excess earnings approach. This method includes discounting the projected cash flows associated with each technology over its expected life. Projected cash flows attributable to the completed technology and IPR&D were discounted to their present value at a rate commensurate with the perceived risk. IPR&D consists of four main projects with expected completion dates of between six months and two years. Following a release date, expected useful lives are between five and eight years.

The valuation of customer relationships was based on the distributor method, taking into account the profit margin a market participant distributor would obtain in selling PMC products. The useful lives of customer relationships are estimated based upon customer turnover data and management estimates. Other identifiable intangible assets consisted of backlog, valued using the distributor method, and trade name, valued using a relief from royalty method.

Microsemi Corporation and Subsidiaries  
Notes to Unaudited Condensed Consolidated Financial Statements

Assumptions used in forecasting cash flows for each of the identified intangible assets included consideration of the following:

- Historical performance including sales and profitability.
- Business prospects and industry expectations.
- Estimated economic life of asset.
- Development of new technologies.
- Acquisition of new customers.
- Attrition of existing customers.
- Obsolescence of technology over time.

Depending on the structure of a particular acquisition, goodwill and identifiable intangible assets may not be deductible for tax purposes. We determined that goodwill and identifiable intangible assets related to the PMC acquisition are not deductible.

The factors that contributed to a purchase price resulting in the recognition of goodwill include:

- Our belief the merger will create a more diverse semiconductor company with expansive offerings which will enable us to expand our product offerings.
- Our belief we are committed to improving cost structures in accordance with our operational and restructuring plans which should result in a realization of cost savings and an improvement of overall efficiencies.

The purchase price allocation described above is preliminary, primarily with respect to tax contingency matters. A final determination of fair values of assets acquired and liabilities assumed relating to the transaction could differ from the preliminary purchase price allocation. We utilize the straight line method of amortization for completed technology, customer relationships and trade name.

Supplemental pro forma data (unaudited)

The supplemental pro forma data presented is for illustrative purposes only and is not necessarily indicative of the financial position or results of operations that would have been realized if the transaction had been completed on the date indicated, does not reflect synergies that might have been achieved, nor is it indicative of future operating results or financial position. The pro forma adjustments are based upon currently available information and certain assumptions we believe are reasonable under the circumstances.

The following supplemental pro forma data summarizes the results of operations for the periods presented, as if we completed the acquisition noted above as of the first day of 2015. The supplemental pro forma data reports actual operating results, adjusted to include the pro forma effect and timing of the impact in amortization expense of identified intangible assets, incremental interest expense and the related tax effects of the acquisition. In accordance with the pro forma acquisition date we recorded, in the 2015 supplemental pro forma data, cost of goods sold from manufacturing profit in acquired inventory of \$66.2 million, PMC-related restructuring costs of \$46.7 million and acquisition-related costs of \$38.1 million, with a corresponding reduction in the 2016 supplemental proforma data. Net sales related to products from the acquisition of PMC contributed approximately 20% to 25% of net sales for the nine months ended July 3, 2016. Post-acquisition net sales and earnings on a standalone basis are generally impracticable to determine as, on the acquisition date, we implemented a plan developed prior to the completion of the acquisition and began to immediately integrate the acquisition into existing operations, engineering groups, sales distribution networks and management structure.

## Microsemi Corporation and Subsidiaries

## Notes to Unaudited Condensed Consolidated Financial Statements

Supplemental pro forma data is as follows:

	Nine Months Ended	
	July 3, 2016	June 28, 2015
Net sales	\$1,354.4	\$1,311.5
Net income (loss)	46.9	(170.0 )
Earnings (loss) per share		
Basic	\$0.42	\$(1.52 )
Diluted	\$0.41	\$(1.52 )

## Divestitures

On April 28, 2016, we divested our Remote Radio Head business to MaxLinear, Inc. for \$21.0 million in cash. The Remote Radio Head business was operated as a non-strategic component of the enterprise storage and communications solution business. On May 2, 2016, we divested our membership interest in Microsemi LLC - RF Integrated Solutions ("RF LLC") to Mercury Systems, Inc. for \$300.0 million in cash. RF LLC operated a non-strategic component of a board level systems and packaging business. These transactions resulted in a gain on divestiture of \$125.5 million.

## Acquisition and Divestiture Costs

During the nine months ended July 3, 2016, we incurred \$31.2 million in acquisition and divestiture costs related to the acquisition of PMC and divestitures of our Remote Radio Head business and RF LLC. These costs were recorded in selling, general and administrative expense.

## Note 3 Inventories

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Inventories are summarized as follows:

	July 3, 2016	September 27, 2015
Raw materials	\$41.9	\$ 56.5
Work in process	112.4	111.7
Finished goods	76.9	59.0
	\$231.2	\$ 227.2

## Note 4 Goodwill and Intangible Assets, Net

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Goodwill and intangible assets, net consisted of the following components:

	July 3, 2016	September 27, 2015
Amortizable intangible assets		
Completed technology	\$604.4	\$ 238.0
Customer relationships	124.7	119.1
Backlog, trade name and other	4.1	0.7
	\$733.2	\$ 357.8

## Non-amortizable intangible assets

Goodwill	\$2,447.7	\$ 1,139.3
In-process research and development	\$241.0	\$ —





Microsemi Corporation and Subsidiaries  
Notes to Unaudited Condensed Consolidated Financial Statements

A reconciliation of goodwill for the nine months ended July 3, 2016 is as follows:

Balance as of September 27, 2015	\$1,139.3
Additions from acquisition	1,435.0
Reductions from divestitures	(125.0 )
Adjustments from prior acquisitions	(1.6 )
Balance as of July 3, 2016	\$2,447.7

Goodwill reductions from divestitures of RF LLC and our Remote Radio Head business. Goodwill allocated to these divestitures was calculated using the relative fair market value of each divestiture as of the respective divestiture date.

Amortization of intangible assets included in operating expenses is as follows:

	Quarter Ended		Nine Months Ended	
	July 3, 2016	June 28, 2015	July 3, 2016	June 28, 2015
Completed technology	\$32.4	\$ 13.3	\$76.9	\$ 36.2
Customer relationships	11.6	11.3	34.5	33.7
Backlog, trade name and other	0.9	0.2	4.2	1.2
	\$44.9	\$ 24.8	\$115.6	\$ 71.1

Estimated amortization expense for amortizable intangible assets in each of the five succeeding years and thereafter is as follows:

Less than 1 Year	1-2 Years	2-3 Years	3-4 Years	4-5 Years	Thereafter
\$176.5	\$140.5	\$115.3	\$106.0	\$105.2	\$ 89.7

Note 5 Income Taxes

For the quarter and nine months ended July 3, 2016, we recorded an income tax provision of \$9.4 million and \$11.8 million, respectively. For the quarter and nine months ended June 28, 2015, we recorded an income tax provision of \$2.5 million and \$10.2 million, respectively. The difference in our effective tax rate from the U.S. statutory rate of 35% primarily reflects the impact of the mix of domestic and international pre-tax income, valuation allowance and credits. Our tax provisions for the nine months ended July 3, 2016 and June 28, 2015 were the combined calculated tax expenses, benefits and credits for various jurisdictions.

We file U.S., state, and foreign income tax returns in jurisdictions with varying statutes of limitations. The 2007 through 2015 tax years generally remain subject to examination by federal tax authorities, most state tax authorities and in significant foreign jurisdictions. Each quarter, we reassess our uncertain tax positions for additional unrecognized tax benefits, interest and penalties, and deletions due to statute expirations. Based on federal, state and foreign statute expirations in various jurisdictions, we anticipate a potential decrease in unrecognized tax benefits of approximately \$44.9 million within the next twelve months.

In December 2015, the U.S. government permanently reinstated the federal research and development tax credit retroactively to January 1, 2015. We are currently in a loss position for U.S. income tax purposes with a full valuation allowance; therefore, no benefit has been recognized for the quarter and nine months ended July 3, 2016.

We establish liabilities for possible assessments by tax authorities resulting from known tax exposures including, but not limited to, international tax issues and certain tax credits. The Internal Revenue Service is currently examining our income tax returns for tax years 2007 through 2012 and the Canada Revenue Agency is currently examining income tax returns assumed from the PMC acquisition for tax years 2007 through 2014. Both examinations primarily relate to transfer pricing matters. Management believes that our position is appropriate and that an adequate provision has



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been made for any adjustments that may result from tax examinations. However, the outcome of tax audits cannot be predicted with certainty. If any issues addressed in our tax audits are resolved in a manner not consistent with management's expectations, we would be required to adjust our provision for income tax in the period such resolution occurs. While we believe our reported results are appropriate, any significant adjustments could have a material adverse effect on our results of operations, cash flows and financial position if not resolved within management expectations.

Note 6 Debt

Credit Agreement

On January 15, 2016, we entered into a Credit Agreement (as amended, the "Credit Agreement") with Morgan Stanley Senior Funding, Inc. ("MSSF"), as administrative agent and collateral agent, the other agents party thereto and the lenders referred to therein (collectively, the "Lenders"). The Lenders provided \$2.5 billion senior secured first lien credit facilities (collectively, as amended, the "Credit Facilities"), consisting of a term A loan facility (as amended, the "Term Loan A Facility") in an aggregate principal amount of \$450.0 million, a term B loan facility (as amended, the "Term Loan B Facility") in an aggregate principal amount of \$1.7 billion and a revolving credit facility (the "Revolving Facility") with commitments in an aggregate principal amount of \$325.0 million. The Credit Facilities financed a portion of the acquisition of PMC and fees and expenses related thereto. The Revolving Facility is also available for working capital requirements and other general corporate purposes.

Refinancing of Credit Agreement

On June 29, 2016, we entered into an Increase Term Joinder to the Credit Agreement with respect to an incremental Term Loan A Facility in an aggregate principal amount of \$364.3 million under our existing Credit Agreement. We used the total proceeds to pay down a portion of our Term Loan B Facility. In addition, on June 29, 2016, we entered into Amendment No. 1 to our existing Credit Agreement (together with the Increase Term Joinder, the "First Amendment"). The First Amendment provided for, among other things, (i) new pricing terms for the outstanding Term B Loan Facility in the aggregate principal amount of \$739.7 million, (ii) certain modifications to the repricing event prepayment provisions and (iii) certain other modifications to facilitate restructuring of our subsidiaries. The Credit Facilities bear interest, at our option, at Base Rate or LIBOR, plus a margin. Starting after the fiscal third quarter, the margin for borrowings under the Term Loan A Facility and Revolving Facility will vary depending upon our consolidated net leverage ratio. At July 3, 2016, the principal amounts outstanding were Eurodollar Rate loans and interest rate information were as follows:

	Principal Outstanding	Base Rate	Base Rate Margin	Eurodollar Rate Margin	Eurodollar Floor	Applicable Rate
Revolving Facility	\$ 275.0	3.50 %	1.50 %	2.50 %	—	2.93 %
Term Loan A Facility	\$ 808.7	3.50 %	1.50 %	2.50 %	—	2.93 %
Term Loan B Facility	\$ 739.7	3.50 %	2.00 %	3.00 %	0.75	3.75 %

As of July 3, 2016, the fair value of principal outstanding on the Credit Agreement was \$1.8 billion. We classify this valuation as a Level 2 fair value measurement.

The Credit Agreement also requires us to pay a commitment fee for the unused portion of the Revolving Facility, which will be a minimum of 0.25% and a maximum of 0.35%, depending on the Company's consolidated net leverage ratio. Interest for Base Rate loans is calculated on the basis of a 365/366-day year and interest for LIBOR-based loans is calculated on the basis of a 360-day year.

The obligations under the Credit Facilities are collateralized by a lien on substantially all of our personal property and material real property assets (collectively, the "Collateral").

The Term Loan A Facility matures January 15, 2021. The Term Loan A Facility requires quarterly principal payments of 1.25% of the amended principal amount for the first two years following the closing date and 2.5% of the amended principal amount for the remaining three years. The Term Loan B Facility matures on January 15, 2023. The Term Loan B Facility requires quarterly principal payments equal to 0.25% of the original principal amount of the Term

Loan B

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Facility. We have made optional principal payments on our Term Loan B Facility such that there are no scheduled principal payments until maturity.

The Credit Facilities include financial maintenance covenants including a maximum consolidated net leverage ratio and minimum fixed charge coverage ratio and also contain other customary affirmative and negative covenants and events of default. We were in compliance with our covenants as of July 3, 2016.

Senior Unsecured Notes

On January 15, 2016, we completed the sale of \$450.0 million of our 9.125% senior unsecured notes due April 2023 (the "Notes") to qualified institutional buyers and pursuant to Regulation S in a private offering exempt from the registration requirements of the Securities Act of 1933, as amended. The Notes were issued under an indenture, dated January 15, 2016, among Microsemi, the subsidiaries of Microsemi party thereto as note guarantors, and U.S. Bank National Association, as trustee (the "Indenture").

As of July 3, 2016, the fair value of principal outstanding on the Senior Unsecured Notes was \$496.1 million. We classify this valuation as a Level 1 fair value measurement.

The Notes accrue cash interest at a rate of 9.125% per year, payable semi-annually on April 15 and October 15 of each year, beginning on October 15, 2016. The Notes mature on April 15, 2023. We may redeem the Notes, and the holders of the Notes may require us to repurchase the Notes, prior to this date of maturity in certain circumstances pursuant to the terms and conditions of the Indenture. The Indenture contains customary affirmative and negative covenants and events of default.

Debt Extinguishment, Modification, and Issuance Costs

On January 15, 2016, concurrent with entering into the Credit Agreement, we terminated our senior secured credit agreement with Bank of America, N.A., which included a term loan A facility and a revolving facility maturing on August 19, 2019 and a term loan B facility maturing on February 19, 2020 (the "2011 Credit Agreement"). We accounted for this termination as debt extinguishment. In addition, we accounted for the refinancing of our Term Loan A Facility and Term Loan B Facility pursuant to the First Amendment as a debt modification with respect to amounts that remained in the syndicate and debt extinguishment with respect to the amounts that exited the syndicate.

During the quarter ended April 3, 2016, we paid financing fees related to the Credit Agreement of \$112.2 million, of which \$61.3 million was recorded in cash flows from operating activities and \$50.9 million was recorded in cash flows from financing activities. We recorded a debt extinguishment charge of \$72.3 million consisting of \$61.3 million in fees paid during the second quarter and \$11.0 million of deferred financing fees from the 2011 Credit Agreement. During the quarter ended July 3, 2016, we paid financing fees related to the First Amendment of \$19.1 million, of which \$16.1 million was recorded in cash flow from operating activities and \$3.0 million was recorded in cash flows from financing activities. We recorded a debt extinguishment charge of \$4.5 million as an allocation of credit facility fees to parties exiting the Credit Agreement. We reported debt extinguishment charges in other expense, net in our Condensed Consolidated Statement of Operations and Comprehensive Income. Debt issuance costs recorded as a reduction to principal outstanding in the condensed consolidated balance sheets were \$45.9 million as of July 3, 2016 and \$11.7 million as of September 27, 2015.

Note 7 Stock-Based Compensation

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Stock Based Compensation

In February 2016, our stockholders approved amendments to the Microsemi Corporation 2008 Performance Incentive Plan (the "2008 Plan"). The amendments a) increased the share limit by an additional approximately 4.8 million shares so that the amended aggregate share limit for the 2008 Plan is approximately 41.8 million shares; b) extended the term of the 2008 Plan to December 2, 2025; c) limited the grant date value of awards that may be granted to non-employee directors under the 2008 Plan during any one calendar year to \$0.4 million (or \$0.6 million as to any newly elected or appointed non-employee director or a non-employee director serving as chairman of the Board or lead independent director); and d) extended the Company's authority to grant awards under the 2008 Plan intended to qualify as "performance-based awards" within the meaning of Section 162(m) of the U.S. Internal Revenue Code



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through the first annual meeting of stockholders that occurs in 2021. For every one share issued in connection with a full value award (as defined in the 2008 Plan), 2.41 shares will be counted against the share limit.

Except as described in this paragraph, shares that are subject to or underlie awards which expire or for any reason, are canceled or terminated, are forfeited, fail to vest, or for any other reason are not paid or delivered under the 2008 Plan will again be available for subsequent awards under the 2008 Plan. Shares exchanged by a participant or withheld by the Company as full or partial payment in connection with any award granted under the 2008 Plan that is a full-value award, as well as any shares exchanged by a participant or withheld by the Company or one of its subsidiaries to satisfy the tax withholding obligations related to any full-value award granted under the 2008 Plan will be available for subsequent awards under the 2008 Plan. Shares exchanged by a participant or withheld by the Company to pay the exercise price of a stock option or stock appreciation right granted under the 2008 Plan, as well as any shares exchanged or withheld to satisfy the tax withholding obligations related to any such award, will not be available for subsequent awards under the 2008 Plan. Tax withholding obligations are established at the statutory minimum requirements for any shares exchanged or withheld.

Awards authorized by the 2008 Plan include options, stock appreciation rights, restricted stock, stock bonuses, stock units, performance share awards, and other cash or share-based awards. The shares issued under the 2008 Plan may be newly issued or shares held by Microsemi as treasury stock. The maximum term of a stock option grant or a stock appreciation right granted under the 2008 Plan is 6 years. For the quarter and nine months ended July 3, 2016, stock-based compensation expense was \$18.9 million and \$57.2 million, respectively. For the quarter and nine months ended June 28, 2015, stock-based compensation expense was \$13.7 million and \$36.2 million, respectively.

The quantity of restricted shares and performance stock units at target levels granted and their weighted-average fair value are as follows (quantity in millions):

Nine Months Ended	Quantity	Weighted-Average Fair Value per Award
June 28, 2015		
Restricted shares	1.3	\$ 29.18
Restricted shares assumed from acquisition	0.3	\$ 33.01
Performance stock units	0.4	\$ 27.54
Stock options assumed from acquisition	0.2	\$ 10.91
July 3, 2016		
Restricted shares	1.2	\$ 31.99
Restricted shares assumed from acquisition	1.9	\$ 29.77
Performance stock units	0.3	\$ 35.14

#### Restricted Shares

Compensation expense for restricted shares was calculated based on the closing price of our common stock on the date of grant and the restricted shares are subject to forfeiture if a participant does not meet length of service requirements. Restricted stock awards granted to employees typically vest over a three year period and awards granted to non-employee directors vest in accordance with our director compensation policy.

#### Performance Stock Units

Compensation expense for performance stock units was calculated based upon expected achievement of the performance metrics specified in the grant and the closing price of our common stock on the date of grant, or when a grant contains a market condition, the grant date fair value using a Monte Carlo simulation which incorporates estimates of the potential outcomes of the market condition on the fair value date of each award.

Performance units granted in 2014, 2015 and 2016 include performance and market conditions and are eligible to vest based on our rate of growth for net sales and earnings per share (subject to certain adjustments) relative to the growth rates for that metric over the relevant performance period for a peer group of companies. The performance period for





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each grant is over three fiscal years and portion of the performance units may vest based on performance after each fiscal year of the performance period.

For the 2014 grants, 40% of each performance-based award opportunity is subject to the net sales metric for the performance period and 60% is subject to the earnings per share metric for the performance period. The maximum percentage for a particular metric is 200% of the "target" number of units subject to the award related to that metric. For the 2015 and 2016 grants, 70% of each performance-based award opportunity is subject to the net sales metric for the performance period and 30% is subject to the earnings per share metric for the performance period. The maximum percentage for a particular metric is 225% of the "target" number of units subject to the award related to that metric. The maximum percentage is further adjusted by our total shareholder return relative to a peer group selected by the Compensation Committee. For the 2014 grants, the maximum adjustment is 125% and for the 2015 and 2016 grants, the maximum adjustment is 120%.

Note 8 Segment Information

We manage our business on the basis of one reportable segment, as a manufacturer of semiconductors in different geographic areas, including the United States, Europe and Asia. We derive revenue from sales of our high-performance analog/mixed-signal integrated circuits and power and high-reliability individual component semiconductors. These products include individual components as well as integrated circuit solutions that enhance customer designs by improving performance, reliability and battery optimization, reducing size or protecting circuits. As a percentage of consolidated net sales, customers with a ship-to location in Hong Kong totaled 19% and 18% for the quarter and nine months ended July 3, 2016, respectively and 14% and 12% for the quarter and nine months ended June 28, 2015, respectively.

Note 9 Restructuring and Severance Charges

The following table reflects restructuring activities and the accrued liabilities at the dates below:

	Employee Severance	Contract Termination Costs	Other Associated Costs	Total
Balance at September 27, 2015	\$ 2.9	\$ 3.2	\$ 0.1	\$6.2
Assumed from acquisition	3.0	—	—	3.0
Provisions	53.9	2.2	5.6	61.7
Reversal of prior provision	(3.1 )	—	(0.3 )	(3.4 )
Cash expenditures	(28.0 )	(2.0 )	(0.4 )	(30.4 )
Other non-cash settlement	(22.9 )	(0.4 )	(2.1 )	(25.4 )
Balance at July 3, 2016	\$ 5.8	\$ 3.0	\$ 2.9	\$11.7

We recorded net provisions for employee severance of \$50.8 million for the nine months ended July 3, 2016, of which \$46.7 million is related to actions following our acquisition and integration of PMC. The non-cash settlement of employee severance relates to the acceleration of restricted stock awards in connection of the acquisition of PMC. Employee severance covered individuals in engineering, manufacturing, administration and sales and is expected to be paid within the next twelve months.

We recorded provisions for contract termination costs of \$2.2 million for the nine months ended July 3, 2016, primarily for the fair value at the cease-use date of operating lease liabilities for space we have exited. Facilities consisted of manufacturing sites, as well as sales, engineering and administrative space.

We recorded net provisions for other associated costs for restructuring of \$5.3 million for the nine months ended July 3, 2016, of which \$2.4 million is related to facility consolidation.



Note 10 Commitments and Contingencies

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We are generally self-insured for losses and liabilities related to workers' compensation and employer's liability insurance. Accrued workers' compensation liability was \$2.1 million and \$2.3 million at July 3, 2016 and September 27, 2015, respectively. Our self-insurance accruals are based on estimates and, while we believe that the amounts accrued are adequate, the ultimate claims may be in excess of the amounts provided.

We are involved in pending litigation, administrative and similar matters arising out of the normal conduct of our business, including litigation relating to acquisitions, employment matters, commercial transactions, contracts, environmental matters and matters related to compliance with governmental regulations. The ultimate aggregate amount of monetary liability or financial impact with respect to these matters is subject to many uncertainties and is therefore not predictable with assurance. In the opinion of management, the final outcome of these matters, if they are adverse, will not have a material adverse effect on our financial position, results of operations or cash flows. However, there can be no assurance with respect to such result, and monetary liability, financial impact or other sanctions imposed on us from these matters could differ materially from those projected.

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

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This Quarterly Report on Form 10-Q includes current beliefs, expectations and other forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from the results contemplated by these forward-looking statements due to certain factors, including those discussed in Part II, Item 1A, "Risk Factors" and elsewhere in this Quarterly Report. This "Management's Discussion and Analysis of Financial Condition and Results of Operations" ("MD&A") and the accompanying condensed consolidated financial statements and notes thereto must be read in conjunction with the MD&A and the consolidated financial statements and notes thereto in our Annual Report on Form 10-K for the fiscal year ended September 27, 2015, in their entirety.

Unless the context otherwise requires, the "Company," "Microsemi," "we," "our," "ours" and "us" refer to Microsemi Corporation and its consolidated subsidiaries.

**OVERVIEW**

We are a leading designer, manufacturer and marketer of high-performance analog and mixed-signal semiconductor solutions differentiated by power, security, reliability and performance. We offer a comprehensive portfolio of semiconductor and system solutions for aerospace & defense, communications, data center and industrial markets. Products include high-performance and radiation-hardened analog mixed-signal integrated circuits ("ICs"), field programmable gate arrays ("FPGAs"), system on chip solutions ("SoCs") and application-specific integrated circuits ("ASICs"); power management products; timing and synchronization devices and precise time solutions, setting the world's standard for time; voice processing devices; radio frequency ("RF") solutions; discrete components; enterprise storage and communication solutions; security technologies and scalable anti-tamper products; Ethernet solutions; Power-over-Ethernet ICs and midspans; as well as custom design capabilities and services.

The principal end markets that we serve include Aerospace & Defense, Communications, Data Center, and Industrial. Today, Microsemi products are found in applications such as: communications infrastructure systems, both wireless and wired LAN systems, implantable pacemakers and defibrillators, radar systems, military and commercial satellites and aircrafts, and enterprise storage and hyperscale data centers.

**Mission and Vision Statements**

**Mission:** Strengthen and leverage the industry's most comprehensive product technology portfolio, differentiated by power, security, reliability and performance, to expand our leadership position in high-value, high-barrier-to-entry markets. Develop innovative leading-edge solutions that provide our customers with an unparalleled competitive edge, and deliver best-in-class technical service and support.

**Vision:** Leading-edge semiconductor solutions, solving the most difficult problems where performance matters, reliability is vital and security is non-negotiable.

Our growth strategy is dependent on our ability to successfully develop new technologies and products, and is complemented by our ability to implement our selective acquisitions strategy. New technologies or products that we may develop may not lead to an incremental increase in revenues, and there is a risk that these new technologies or products will decrease the demand for our existing products and result in an offsetting reduction in revenues. There can be no assurance that the benefits of any acquisition will outweigh the attendant costs, and if they do not, our results of operations and stock price may be adversely affected.

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## Summary of Financial Results

Net sales, gross profit and gross margin were as follows:

	Quarter Ended				Nine Months Ended			
	July 3, 2016	June 28, 2015	Variance \$	Variance %	July 3, 2016	June 28, 2015	Variance \$	Variance %
Net sales	\$431.4	\$317.1	\$114.3	36.0 %	\$1,204.9	\$916.8	\$288.1	31.4 %
Gross profit	\$266.9	\$172.1	\$94.8	55.1 %	\$655.3	\$509.4	\$145.9	28.6 %
Gross margin	61.9 %	54.3 %	7.6 %		54.4 %	55.6 %	(1.2 %)	

We recorded an increase in net sales between the quarters ended July 3, 2016 ("Q3 2016") and June 28, 2015 ("Q3 2015"), and an increase in net sales between the nine months ended July 3, 2016 ("2016 YTD") and June 28, 2015 ("2015 YTD"). Net sales related to products from the acquisition of PMC-Sierra, Inc. ("PMC"), which occurred in the second quarter of 2016, contributed approximately 20% to 25% of net sales for 2016. On July 28, 2016, we announced that we expect our consolidated net sales for the fourth quarter of fiscal year 2016 of approximately \$438 million and \$458 million.

Gross profit increased \$94.8 million to \$266.9 million (61.9% of net sales) for Q3 2016 from \$172.1 million (54.3% of net sales) for Q3 2015 and increased \$145.9 million to \$655.3 million (54.4% of net sales) for 2016 YTD from \$509.4 million (55.6% of net sales) for 2015 YTD. In 2016 YTD, we recorded costs related to manufacturing profit in acquired inventory of \$66.2 million related to the PMC acquisition. In the Q3 2015 and 2015 YTD, we recorded costs related to manufacturing profit in acquired inventory of \$8.6 million and \$11.0 million, respectively. Adjusting for these costs, gross margin improvements were primarily attributable to favorable product mix, including from products from the PMC acquisition, and improvements in manufacturing efficiencies. In 2016 YTD, we also recorded \$4.0 million in inventory reserves related to the shutdown of a wafer fabrication facility.

As discussed further in "Results of Operations", during 2016 YTD, we recorded net provisions for employee severance of \$50.8 million, contract termination costs of \$2.2 million and other associated costs for restructuring of \$5.3 million. Employee severance primarily related to actions following our acquisition of PMC. Contract termination costs and other associated costs resulted from facility consolidation and equipment charges related to actions following our acquisition of PMC and from the closure of a wafer fabrication facility.

For Q3 2016 and 2016 YTD, we recorded an income tax provision of \$9.4 million and \$11.8 million, respectively. For Q3 2015 and 2015 YTD, we recorded an income tax provision of \$2.5 million and \$10.2 million, respectively. The difference in our effective tax rate from the U.S. statutory rate of 35% primarily reflects the impact of the mix of domestic and international pre-tax income, valuation allowance and credits. Our tax provision for 2016 YTD and 2015 YTD was the combined calculated tax expenses, benefits and credits for various jurisdictions.

Uncertain macroeconomic conditions worldwide and international operations and sales subject us to certain risks (see Part II, Item 1A, Risk Factors, "Negative or uncertain worldwide economic conditions may adversely affect our business, financial condition, cash flow and results of operations," "The concentration of the facilities that service the semiconductor industry, including facilities of current or potential vendors or customers, makes us more susceptible to events or disasters affecting the areas in which they are most concentrated," "We may be unable to successfully implement our acquisitions strategy or integrate acquired companies and personnel with existing operations," and "International operations and sales expose us to material risks and may increase the volatility of our operating results").

## Markets

Our products include discretely and ICs, modules, and subsystem solutions that enhance customer designs by improving performance, security, reliability and power consumption. The principal end markets we serve include: Aerospace & Defense - Microsemi's high-performance solutions are used by the majority of commercial airliners manufactured today and all Tier 1 prime contractors in a variety of homeland and offshore security applications. Microsemi products are used in the latest advanced models such as the Boeing 787 Dreamliner, Airbus A350 and Airbus A380. Microsemi's high-reliability products are used in most satellites and in a wide range of commercial and military avionics systems. Microsemi's product offering for aerospace include radiation



hardened and radiation tolerant solutions for the satellite market to which it supplies all of the top manufacturers. Microsemi's defense and security solutions are also used in products such as unmanned aerial vehicles, radar applications and radio and guidance systems.

**Communications** - Microsemi is a key supplier to top-tier companies focused on wired and wireless communications products. These products are deployed in applications ranging from the central office to the enterprise and the home, and to a broad array of wired and wireless networked devices. Microsemi boasts the largest and most complete timing product offering, as well as the industry's only end to end timing product portfolio. Microsemi also pioneered the concept and development of Power-over-Ethernet ("PoE") technology and offers ICs and system solutions (midspans) based on this increasingly popular power transmission solution.

**Data Center** - Microsemi's data center products and solutions enable high-speed communications between the servers, switches and storage devices that comprise these systems thereby allowing large quantities of data to be stored, managed and moved securely. As storage demand continues to grow, managing the data becomes more critical for the operation of the entire company or service provider. Our focus in this area is in developing controllers and switches for high-performance storage systems in cloud and enterprise data center applications.

**Industrial** - Microsemi delivers secure and highly reliable solutions for applications including industrial controls, machine-to-machine (M2M) communications, energy exploration and drilling, semiconductor capital equipment and alternative energy platforms. Microsemi is also a leading supplier of ultra-low power wireless solutions used in medical devices including implantable defibrillators and pacemakers, MRI machines, and portable medical equipment.

#### Recent Product Introductions

Microsemi marketed a number of recently introduced products, including:

- the newest member of its high-reliability space product portfolio, the LX7710 radiation-tolerant diode array, the industry's first integrated solution of its kind offering eight diode pair channels designed specifically for satellites and other space applications;

- its RTG4™ PROTO FPGAs and RTG4 Development Kit, developed specifically to enable prototyping of space systems, enable lower cost prototyping and design validation activities for the latest radiation-tolerant high-speed FPGAs, and the only reprogrammable prototyping solution of their kind providing the same timing and power characteristics as space flight units;

- fifteen new products from its RF, millimeter wave ICs, monolithic microwave integrated circuits ("MMICs"), ultra-low power sub-GHz transceivers and high performance WLAN monolithic radio frequency integrated circuits portfolio, which build upon Microsemi's rich history in RF, microwave and millimeter wave solutions and are ideal for the defense, communications, instrumentation, industrial and aerospace industries;

- the latest member of its SparX-IV Ethernet switch product family, VSC7440 SparX-IV-34, designed to enable more cost effective, smaller form factor and lower power networking solutions with 2.5G and 10 gigabit Ethernet connectivity;

- its new Ocelot product family, a low power, feature-rich Ethernet switch family optimized for communications networking in the industrial Internet of Things ("IIoT") market, designed for applications including factory automation, process control, smart grid/smart energy and physical security;

- a phase-compliant embedded solution enabling IEEE 1588 across a wide variety of applications which adds support for the ITU-T G.8275.2 Precision Time Protocol ("PTP") profile for timing and phase with partial timing support;

- new enhancements to Microsemi's TimeProvider® series TP2700 and TP5000 PTP Grandmaster system product lines, enabling customers to implement phase synchronization in switches and routers in networks which are not completely phase-aware, without having to replace unaware nodes or any major infrastructure in the network;



enhancements to its SmartFusion™2 SoC FPGA-based deterministic multi-axis motor control solution, expanding its features to support applications using encoder, Hall sensor, controller area network ("CAN") bus and induction motors.

#### Results of Operations

Net sales increased \$114.3 million or 36.0% to \$431.4 million for Q3 2016 from \$317.1 million for Q3 2015 and increased \$288.1 million or 31.4% to \$1,204.9 million for 2016 YTD from \$916.8 million for 2015 YTD. Products from the acquisition of PMC contributed approximately 20% to 25% of net sales for 2016.

Estimated sales by end markets are based on our understanding of end market uses of our products. An estimated breakout of net sales by end market is as follows:

	Quarter Ended		Nine Months Ended	
	July 3, 2016	June 28, 2015	July 3, 2016	June 28, 2015
Aerospace & Defense	\$113.0	\$131.7	\$379.7	\$389.2
Communications	162.0	115.2	448.4	318.1
Data Center	92.2	3.1	181.8	7.3
Industrial	64.2	67.1	195.0	202.2
	\$431.4	\$317.1	\$1,204.9	\$916.8

Net sales in the Aerospace & Defense end market decreased \$18.7 million to \$113.0 million in Q3 2016 from \$131.7 million in Q3 2015 and decreased \$9.5 million to \$379.7 million in 2016 YTD from \$389.2 million in 2015 YTD. The decline in Q3 2016 compared to Q3 2015 was primarily attributable to the divestiture in May 2016 of RF LLC that operated a non-strategic component of a board level systems and packaging business. Absent the impact of this divestiture, aerospace sales have increased, and though aerospace growth has moderated but our outlook for commercial air remains healthy. We believe we are benefiting from significant content growth on newer aircrafts such as the Boeing 787, Airbus A350 and A380 and our differentiated highly-reliable and secure FPGA technology will contribute to growth in this end market. We see continued strength in commercial air as customers ramp production against strong multiyear backlogs and as our contact in each aircraft grows. We also expect satellite sales, which includes higher margin FPGA products, to improve over the upcoming year. We continue to note an improving defense market where we have increased dollar content in the form of our FPGAs and timing products, growing foreign military sales and normalization of channel inventories. We believe that procurement plans that emphasize command, control, communications, computers, intelligence, surveillance and reconnaissance equates to growing electronic content.

Net sales in the Communications end market increased \$46.8 million to \$162.0 million in Q3 2016 from \$115.2 million in Q3 2015 and increased \$130.3 million to \$448.4 million in 2016 YTD from \$318.1 million in 2015 YTD. This end market benefited in Q3 2016 and 2016 YTD from products from both the PMC acquisition which we consummated in January 2016 and the Vitesse Semiconductor Corporation ("Vitesse") acquisition which was consummated in April 2015, as well as increased contributions of Ethernet switching, broadband gateway applications, voice circuit, and higher sales of LTE applications. We believe the communications infrastructure market continued its recovery with continued sales growth. We expect long-term growth from our timing products, driven by ongoing strength of our optical transport network products. We believe we have the broadest portfolio of timing products which allows us to better anticipate and serve our customers' needs while improving our market share. While growth in China LTE and capital expenditures at carriers was slower than expected for the most recently completed fiscal year, we believe our design win activity will enable us to outpace industry growth in this end market for 2016. Net sales in the Data Center end market increased \$89.1 million to \$92.2 million in Q3 2016 from \$3.1 million in Q3 2015 and increased \$174.5 million to \$181.8 million in 2016 YTD from \$7.3 million in 2015 YTD. Initially, amounts reported in this end market will consist of the storage controllers, interconnect devices and board level products from the acquisition of PMC along with various power management and Ethernet switching products from Microsemi's existing portfolio which have been selling into Data Center applications. Over the longer term, we expect to drive our

Ethernet switching, FPGA, and other secure devices into high-growth hyperscale applications as we execute on Microsemi's solution-sell go to market strategy. We expect to leverage our strong product portfolio and customer relationships to increase net sales in a high-growth data center market.

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Net sales in the Industrial end market decreased \$2.9 million to \$64.2 million in Q3 2016 from \$67.1 million in Q3 2015 and decreased \$7.2 million to \$195.0 million in 2016 YTD from \$202.2 million in 2015 YTD. This end market was impacted in Q3 2016 by the divestiture of RF LLC in May 2016. Over the last year, this end market has been impacted by the decline in oil prices which has affected products used in energy exploration applications but has benefited from increased shipments of ultra-low power radios in medical applications, as well as from broad-based strength for our power products in the plasma and semiconductor capital equipment markets. We continue to forecast modest growth for 2016 based on the strength of our ultra-low power RF products and several emerging market opportunities such as automotive charging stations in China.

Gross profit increased \$94.8 million to \$266.9 million (61.9% of net sales) for Q3 2016 from \$172.1 million (54.3% of net sales) for Q3 2015 and increased \$145.9 million to \$655.3 million (54.4% of net sales) for 2016 YTD from \$509.4 million (55.6% of net sales) for 2015 YTD. In Q2 2016, we recorded costs related to manufacturing profit in acquired inventory of \$66.2 million related to the PMC acquisition. In the third quarter of 2015, we recorded costs related to manufacturing profit in acquired inventory of \$8.6 million and \$11.0 million, respectively. Adjusting for these costs, gross margin improvements were primarily attributable to favorable product mix, including from products from the PMC acquisition, and improvements in manufacturing efficiencies. In Q2 2016, we also recorded \$4.0 million in inventory reserves related to the shutdown of a wafer fabrication facility.

Selling, general and administrative ("SG&A") expenses increased \$16.2 million to \$82.9 million for Q3 2016 from \$66.7 million in Q3 2015 and increased \$78.1 million to \$265.8 million for 2016 YTD from \$187.7 million for 2015 YTD. The increases in SG&A expenses were due to incremental operating expenses attributed to our recent acquisitions and costs associated with our acquisition and divestiture activities. For Q3 2016 and 2016 YTD, we recorded costs of \$2.8 million and \$31.2 million, respectively, with Q3 2016 costs primarily related to the RF LLC divestiture and prior quarter costs primarily related to the PMC acquisition. For Q3 2015 and 2015 YTD, we recorded costs of \$3.3 million and \$5.5 million, respectively, primarily related to our acquisition of Vitesse.

Research and development expense increased \$30.7 million to \$83.0 million for Q3 2016 from \$52.3 million for Q3 2015 and increased \$79.4 million to \$225.7 million for 2016 YTD from \$146.3 million for 2015 YTD. While incremental costs from recent acquisitions contributed to increased research and development expenses, the increases were partially offset by selectively investing in strategic product roadmaps. The spending on research and development was principally to develop new higher-margin application-specific products, including, among others, our process and core architecture development for next generation programmable products, storage and optical products, higher power PoE solutions, the continued roadmap development of our industry-leading timing & synchronization products, our silicon germanium (SiGe) RF power amplifier solutions for wireless LAN applications, and the ongoing development of gallium nitride (GaN) and silicon carbide (SiC) power management and RF solutions. Amortization of intangible assets included in operating expenses is as follows:

	Quarter Ended		Nine Months Ended	
	July 3, 2016	June 28, 2015	July 3, 2016	June 28, 2015
Completed technology	\$32.4	\$ 13.3	\$76.9	\$ 36.2
Customer relationships	11.6	11.3	34.5	33.7
Backlog, trade name and other	0.9	0.2	4.2	1.2
	\$44.9	\$ 24.8	\$115.6	\$ 71.1

The following table reflects the related restructuring activities and the accrued liabilities at the dates below:

	Employee Severance	Contract Termination Costs	Other Associated Costs	Total
Balance at September 27, 2015	\$ 2.9	\$ 3.2	\$ 0.1	\$6.2
Assumed from acquisition	3.0	—	—	3.0
Provisions	53.9	2.2	5.6	61.7
Reversal of prior provision	(3.1 )	—	(0.3 )	(3.4 )
Cash expenditures	(28.0 )	(2.0 )	(0.4 )	(30.4 )
Other non-cash settlement	(22.9 )	(0.4 )	(2.1 )	(25.4 )
Balance at July 3, 2016	\$ 5.8	\$ 3.0	\$ 2.9	\$11.7

We recorded net provisions for employee severance of \$50.8 million for 2016 YTD, of which \$46.7 million is related to actions following our acquisition of PMC. Employee severance covered individuals in engineering, manufacturing, administration and sales and is expected to be paid within the next twelve months.

We recorded provisions for contract termination costs of \$2.2 million for 2016 YTD, primarily for the fair value at the cease-use date of operating lease liabilities for space we have exited. Facilities consisted of manufacturing sites, as well as sales, engineering and administrative space.

We recorded provisions for other associated costs for restructuring of \$5.3 million for 2016 YTD, of which \$2.4 million is related to facility consolidation.

On April 28, 2016, we divested our Remote Radio Head business to MaxLinear, Inc. for \$21.0 million in cash. The Remote Radio Head business was operated as a non-strategic component of the enterprise storage and communications solution business. On May 2, 2016, we divested our membership interest in RF LLC to Mercury Systems, Inc. for \$300.0 million in cash. RF LLC operated a non-strategic component of a board level systems and packaging business. These transactions resulted in a gain on divestiture of \$125.5 million.

During the nine months ended July 3, 2016, we recorded debt extinguishment charges of \$76.9 million consisting of \$61.3 million we paid during the quarter ended April 3, 2016 in connection with the Credit Agreement and \$3.0 million we paid during the quarter ended July 3, 2016 in connection with the refinancing of our Term Loan A Facility and Term Loan B facility reported in net cash provided by operating activities and \$12.6 million related to prior deferred financing fees we expensed in connection with the termination of our prior senior secured credit agreement and extinguishment of amounts that exited the Term Loan A Facility and Term Loan B Facility syndicate. These amounts were reported in other expense, net in our Condensed Consolidated Statement of Operations and Comprehensive Income.

For Q3 2016 and 2016 YTD, we recorded an income tax provision of \$9.4 million and \$11.8 million, respectively. For Q3 2015 and 2015 YTD, we recorded an income tax provision of \$2.5 million and \$10.2 million, respectively. The difference in our effective tax rate from the U.S. statutory rate of 35% primarily reflects the impact of the mix of domestic and international pre-tax income, valuation allowance and credits. Our tax provision for 2016 YTD and 2015 YTD was the combined calculated tax expenses, benefits and credits for various jurisdictions.

In December 2015, the U.S. government permanently reinstated the federal research and development tax credit retroactively to January 1, 2015. We are currently in a loss position for U.S. income tax purposes with a full valuation allowance; therefore, no benefit has been recognized for Q3 2016 and 2016 YTD.

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## CAPITAL RESOURCES AND LIQUIDITY

We had \$131.8 million and \$256.4 million in cash and cash equivalents at July 3, 2016 and September 27, 2015, respectively. During 2016 YTD, we financed our operations with cash generated from operations. We believe that we have the ability to raise cash in the United States through existing and new credit facilities or by settling loans receivable with our foreign subsidiaries. We believe that through our cash flows from operations, together with our existing cash and cash equivalents, we will be able to meet our operating and capital requirements for at least the next twelve months.

Our various foreign subsidiaries hold cash and cash equivalents, and as we intend to reinvest certain foreign earnings indefinitely, these balances held outside the United States may not be readily available to meet our domestic cash requirements. We require a substantial amount of cash in the United States for operating requirements, purchases of property and equipment, debt service, potential repurchases of our common stock and potential future acquisitions. If we are unable to meet our domestic cash requirements using domestic cash flows from operations, domestic cash and cash equivalents, or by settling loans with our foreign subsidiaries, it may be necessary for us to consider raising funds through debt or equity offerings or repatriate earnings that we have designated as permanently reinvested. Any repatriation of earnings may require us to record additional income tax expense and remit additional taxes, which could have a material effect on our results of operations, cash flows and financial condition.

Net cash provided by operating activities decreased \$119.3 million to \$72.3 million for 2016 YTD from \$191.6 million for 2015 YTD. A summary of net cash provided by operating activities for 2016 YTD and 2015 YTD is as follows:

	Nine Months Ended	
	July 3, 2016	June 28, 2015
Net income (loss)	\$(73.1)	\$59.2
Depreciation and amortization	150.2	98.0
Change in allowance for doubtful accounts	0.8	(0.1)
Amortization of deferred financing cost	30.4	0.9
Gain on divestiture	(125.5)	—
Loss on disposition or impairment of assets	1.3	2.5
Deferred income taxes	7.1	5.3
Charge for stock-based compensation	80.3	35.9
Net change in working capital accounts	(21.5)	(3.1)
Net change in other long-term assets and liabilities	22.3	(7.0)
Net cash provided by operating activities	\$72.3	\$191.6

Accounts receivable increased \$54.8 million to \$241.7 million at July 3, 2016 from \$186.9 million at September 27, 2015. Inventories increased \$4.0 million to \$231.2 million at July 3, 2016 from \$227.2 million at September 27, 2015. These changes were due primarily to the acquisition of PMC, partially offset by the divestitures of RF LLC and our Remote Radio Head business.

Current liabilities increased \$114.5 million to \$316.1 million at July 3, 2016 from \$201.6 million at September 27, 2015 due to the acquisition of PMC, an increase in accrued interest of \$19.9 million due to timing of interest due dates on our Senior Unsecured Bond and Amended Credit Agreement and an \$8.2 million increase in the current portion of long term debt. These amounts were partially offset by the divestitures of RF LLC and our Remote Radio Head business.

During the quarter ended April 3, 2016, we paid financing fees related to the Credit Agreement of \$112.2 million, of which \$61.3 million was recorded in cash flows from operating activities and \$50.9 million was recorded in cash flows from financing activities. During the quarter ended July 3, 2016, we paid financing fees related to the First Amendment of \$19.1 million, of which \$16.1 million was recorded in cash flow from operating activities and \$3.0 million was recorded in cash flows from financing activities.

Net cash used in investing activities was \$1.4 billion for 2016 YTD and consisted of \$1.7 billion in payments for acquisitions, net of cash acquired, and purchases of property and equipment of \$34.2 million and, partially offset by \$0.3 million for the proceeds from the sale of short term investments and \$321.0 million for the proceeds from the

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divestitures. Net cash used in investing activities was \$398.1 million for 2015 YTD and consisted of \$34.9 million in purchases of property and equipment, partially offset by \$0.4 million for the proceeds from the sale of short term investments.

Net cash provided by financing activities was \$1.2 billion for 2016 YTD compared to net cash used for financing activities of \$248.3 million for 2015 YTD. Net cash provided by financing activities in 2016 YTD consisted of \$3.5 billion in credit facility proceeds and \$4.1 million from the exercise of stock options, partially offset by \$1.1 billion in debt extinguishment, primarily representing the principal balance on our credit facility before the PMC acquisition, \$1.1 billion in principal payments, \$53.8 million for credit facility issuance costs, and \$38.4 million of stock settled tax withholdings. Net cash used in financing activities in 2015 YTD consisted of \$42.4 million in net proceeds from the exercise of stock options and \$425.0 million in credit facility proceeds, partially offset by \$17.7 million of stock settled tax withholdings, \$8.7 million for credit facility issuance costs, \$142.7 million in principal payments and \$50.0 million in the repurchase of common stock.

#### Credit Agreement

On January 15, 2016, we entered into a Credit Agreement (as amended, the "Credit Agreement") with Morgan Stanley Senior Funding, Inc. ("MSSF"), as administrative agent and collateral agent, the other agents party thereto and the lenders referred to therein (collectively, the "Lenders"). The Lenders provided \$2.5 billion senior secured first lien credit facilities (collectively, as amended, the "Credit Facilities"), consisting of a term A loan facility (as amended, the "Term Loan A Facility") in an aggregate principal amount of \$450.0 million, a term B loan facility (as amended, the "Term Loan B Facility") in an aggregate principal amount of \$1.7 billion and a revolving credit facility (the "Revolving Facility") with commitments in an aggregate principal amount of \$325.0 million. The Credit Facilities financed a portion of the acquisition of PMC and fees and expenses related thereto. The Revolving Facility is also available for working capital requirements and other general corporate purposes.

#### Refinancing of Credit Agreement

On June 29, 2016, we entered into an Increase Term Joinder to the Credit Agreement with respect to an incremental Term Loan A Facility in an aggregate principal amount of \$364.3 million under our existing Credit Agreement. We used the total proceeds to pay down a portion of our Term Loan B Facility. In addition, on June 29, 2016, we entered into Amendment No. 1 to our existing Credit Agreement (together with the Increase Term Joinder, the "First Amendment"). The First Amendment provided for, among other things, (i) new pricing terms for the outstanding Term B Loan Facility in the aggregate principal amount of \$739.7 million, (ii) certain modifications to the repricing event prepayment provisions and (iii) certain other modifications to facilitate restructuring of our subsidiaries. The Credit Facilities bear interest, at our option, at Base Rate or LIBOR, plus a margin. Starting after the fiscal third quarter, the margin for borrowings under the Term Loan A Facility and Revolving Facility will vary depending upon our consolidated net leverage ratio. At July 3, 2016, the principal amounts outstanding were Eurodollar Rate loans and interest rate information were as follows:

	Principal Outstanding	Base Rate	Base Rate Margin	Eurodollar Rate Margin	Eurodollar Floor	Applicable Rate
Revolving Facility	\$ 275.0	3.50 %	1.50 %	2.50 %	—	2.93 %
Term Loan A Facility	\$ 808.7	3.50 %	1.50 %	2.50 %	—	2.93 %
Term Loan B Facility	\$ 739.7	3.50 %	2.00 %	3.00 %	0.75	3.75 %

As of July 3, 2016, the fair value of principal outstanding on the Credit Agreement was \$1.8 billion. We classify this valuation as a Level 2 fair value measurement.

The Credit Agreement also requires us to pay a commitment fee for the unused portion of the Revolving Facility, which will be a minimum of 0.25% and a maximum of 0.35%, depending on the Company's consolidated net leverage ratio. Interest for Base Rate loans is calculated on the basis of a 365/366-day year and interest for LIBOR-based loans is calculated on the basis of a 360-day year.

The obligations under the Credit Facilities are collateralized by a lien on substantially all of our personal property and material real property assets (collectively, the "Collateral").





The Term Loan A Facility matures January 15, 2021. The Term Loan A Facility requires quarterly principal payments of 1.25% of the amended principal amount for the first two years following the closing date and 2.5% of the amended principal amount for the remaining three years. The Term Loan B Facility matures on January 15, 2023. The Term Loan B Facility requires quarterly principal payments equal to 0.25% of the original principal amount of the Term Loan B Facility. We have made optional principal payments on our Term Loan B Facility such that there are no scheduled principal payments until maturity.

The Credit Facilities include financial maintenance covenants including a maximum consolidated net leverage ratio and minimum fixed charge coverage ratio and also contain other customary affirmative and negative covenants and events of default. We were in compliance with our covenants as of July 3, 2016.

#### Senior Unsecured Notes

On January 15, 2016, we completed the sale of \$450.0 million of our 9.125% senior unsecured notes due April 2023 (the "Notes") to qualified institutional buyers and pursuant to Regulation S in a private offering exempt from the registration requirements of the Securities Act of 1933, as amended. The Notes were issued under an indenture, dated January 15, 2016, among Microsemi, the subsidiaries of Microsemi party thereto as note guarantors, and U.S. Bank National Association, as trustee (the "Indenture").

As of July 3, 2016, the fair value of principal outstanding on the Senior Unsecured Notes was \$496.1 million. We classify this valuation as a Level 1 fair value measurement.

The Notes accrue cash interest at a rate of 9.125% per year, payable semi-annually on April 15 and October 15 of each year, beginning on October 15, 2016. The Notes mature on April 15, 2023. We may redeem the Notes, and the holders of the Notes may require us to repurchase the Notes, prior to this date of maturity in certain circumstances pursuant to the terms and conditions of the Indenture. The Indenture contains customary affirmative and negative covenants and events of default.

#### Debt Extinguishment, Modification, and Issuance Costs

On January 15, 2016, concurrent with entering into the Credit Agreement, we terminated our senior secured credit agreement with Bank of America, N.A., which included a term loan A facility and a revolving facility maturing on August 19, 2019 and a term loan B facility maturing on February 19, 2020 (the "2011 Credit Agreement"). We accounted for this termination as debt extinguishment. In addition, we accounted for the refinancing of our Term Loan A Facility and Term Loan B Facility pursuant to the First Amendment as a debt modification with respect to amounts that remained in the syndicate and debt extinguishment with respect to the amounts that exited the syndicate. During the quarter ended April 3, 2016, we paid financing fees related to the Credit Agreement of \$112.2 million, of which \$61.3 million was recorded in cash flows from operating activities and \$50.9 million was recorded in cash flows from financing activities. We recorded a debt extinguishment charge of \$72.3 million consisting of \$61.3 million in fees paid during the second quarter and \$11.0 million of deferred financing fees from the 2011 Credit Agreement. During the quarter ended July 3, 2016, we paid financing fees related to the First Amendment of \$19.1 million, of which \$16.1 million was recorded in cash flow from operating activities and \$3.0 million was recorded in cash flows from financing activities. We recorded a debt extinguishment charge of \$4.5 million as an allocation of credit facility fees to parties exiting the Credit Agreement. We reported debt extinguishment charges in other expense, net in our Condensed Consolidated Statement of Operations and Comprehensive Income. Debt issuance costs recorded as a reduction to principal outstanding in the condensed consolidated balance sheets were \$45.9 million as of July 3, 2016 and \$11.7 million as of September 27, 2015.

**CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

The unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States that require us to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the unaudited condensed consolidated financial statements and revenues and expenses during the periods reported. Actual results could differ from those estimates. Information, with respect to our critical accounting policies, that we believe could have the most significant effect on our reported results and require subjective or complex judgments is contained in Note 1 of the notes to the consolidated financial statements included in our Annual Report on Form 10-K for the fiscal year ended September 27, 2015. We have made no significant changes to our critical accounting policies from those described in our Annual Report on Form 10-K for the year ended September 27, 2015.

**RECENTLY ISSUED ACCOUNTING STANDARDS**

Please refer to Note 1, "Presentation of Financial Information" of our notes to unaudited condensed consolidated financial statements for a discussion of recently issued accounting standards.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We are exposed to various forms of market risk, which is the potential loss arising from adverse changes in interest rates, foreign currency exchange rates, credit risk, or the stock market.

**Interest Rates**

Under our Credit Agreement, we had the ability to borrow under a "Base Rate" which approximated the prime rate plus an applicable margin or "Eurodollar Rate" which approximated LIBOR plus an applicable margin. Eurodollar Rate loans were also subject to a Eurodollar Floor. At July 3, 2016, the principal amounts outstanding were Eurodollar Rate loans and interest rate information as of July 3, 2016 were as follows:

	Principal Outstanding	Base Rate	Base Rate Margin	Eurodollar Rate Margin	Eurodollar Rate	Eurodollar Floor	Applicable Rate
Revolving Facility	\$ 275.0	3.50%	1.50 %	2.50 %	—	%	2.93 %
Term Loan A Facility	\$ 808.7	3.50%	1.50 %	2.50 %	—	%	2.93 %
Term Loan B Facility	\$ 739.7	3.50%	2.00 %	3.00 %	0.75	%	3.75 %

Our 2011 Credit Agreement was terminated and repaid in full on January 15, 2016 and replaced with the Credit Agreement governing the Credit Facilities. See Note 6, "Debt" of our notes to unaudited condensed consolidated financial statements for information regarding interest rates under our Credit Facilities and the Notes.

We have historically conducted a limited interest rate hedging program and currently have no outstanding interest rate hedging instruments. We have considered and may continue to consider increasing expanding our interest rate hedging program.

**Foreign Currency Exchange Rates**

We conduct a relatively small portion of our business in a number of foreign currencies, principally the European Union Euro, Canadian Dollar, British Pound, Israeli Shekel and Chinese RMB. We may receive some revenues in foreign currencies and purchase some inventory and services in foreign currencies. Accordingly, we are exposed to transaction gains and losses that could result from changes in exchange rates of foreign currencies relative to the U.S. dollar. Because transactions in foreign currencies have represented a relatively small portion of our business, foreign currency fluctuations have not had a material impact historically on our revenues or results of operations. However, there can be no assurance future fluctuations in the value of foreign currencies will not have material adverse effects on our results of operations, cash flows or financial condition. We have conducted a limited foreign currency hedging program thus far. We have considered and may continue to consider the adoption of a more broad based foreign currency hedging program.



### Credit Risk

A significant portion of our sales are or may be derived from U.S. government agencies or customers whose principal sales are to U.S. government agencies which creates concentrations of credit risk. Future sales are subject to the uncertainties of governmental appropriations and national defense policies and priorities, including lingering impacts of sequestration under the Budget Control Act of 2011, constraints of the budgetary process and timing and potential changes in these policies and priorities. Additionally, the long-term outlook for the fiscal position of the U.S. federal government is also uncertain, as illustrated by the 2013 budget negotiations and the shutdown of non-essential U.S. federal government services in October 2013.

We have experienced delays and reduction in appropriations on programs that include our products. Further delays, reductions in or terminations of government contracts or subcontracts, including those caused by any past or future shutdown of the U.S. federal government, could materially and adversely affect our operating results. While we generally function as a subcontractor, further changes in U.S. government procurement regulations and practices, particularly surrounding initiatives to reduce costs, may adversely impact the contracting environment and our operating results.

Generally, the U.S. government and its contractors and subcontractors may terminate their contracts with us at any time, with or without cause. We have in the past experienced the termination of a contract due to the termination of the underlying government contract. All government contracts are also subject to price renegotiation in accordance with the U.S. Government Renegotiation Act. By reference to such contracts, all of the purchase orders we receive that are related to government contracts are subject to these possible events. In addition, the recent shutdown of non-essential U.S. government services and any future government shutdowns may significantly increase the risk of further contract terminations or renegotiations, and any such termination or renegotiation could have a material adverse impact upon our revenues and results of operations.

### ITEM 4. CONTROLS AND PROCEDURES

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#### (a) Evaluation of disclosure controls and procedures.

Our Chief Executive Officer and Chief Financial Officer, with the assistance of other members of management, conducted an evaluation of our disclosure controls and procedures (as such term is defined in Rule 13a-15(e) and Rule 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of July 3, 2016.

#### (b) Changes in internal control over financial reporting.

On January 15, 2016, Microsemi completed the acquisition of PMC and has commenced the integration of PMC into our disclosure controls and procedures. There have been no other changes in the Company's internal control over financial reporting during the fiscal quarter ended July 3, 2016 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## PART II. OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

We are involved in pending litigation, administrative and similar matters arising out of the normal conduct of our business, including litigation relating to acquisitions, employment matters, commercial transactions, contracts, environmental matters and matters related to compliance with governmental regulations. The ultimate aggregate amount of monetary liability or financial impact with respect to these matters is subject to many uncertainties and is therefore not predictable with assurance. In the opinion of management, the final outcome of these matters, if they are adverse, will not have a material adverse effect on our financial position, results of operations or cash flows. However, there can be no assurance with respect to such result, and monetary liability, financial impact or other sanctions imposed on us from these matters could differ materially from those projected.

### ITEM 1A. RISK FACTORS

We routinely update our risk factors previously disclosed in Part I, Item 1A of our Annual Report on Form 10-K for the fiscal year ended September 27, 2015, as filed with the Securities and Exchange Commission (the "SEC") on November 12, 2015. For the convenience of our readers, our updated risk factors are included below in this Item 1A, and we recommend that they be read in their entirety. There have been no material changes from the risk factors previously disclosed in our Annual Report on Form 10-K for the fiscal year ended September 27, 2015.

We may be unable to successfully implement our acquisitions strategy or integrate acquired companies and personnel with existing operations.

We have in the past acquired a number of businesses or companies, additional product lines and assets, and we may continue to expand and diversify our operations with additional acquisitions. We may be unable to identify or complete prospective acquisitions for many reasons, including increasing competition from other potential acquirers, the effects of a consolidating semiconductor industry and high valuations of acquisition candidates. In addition, applicable antitrust laws and other regulations may limit our ability to acquire targets or force us to divest an acquired business. If we are unable to identify suitable targets or complete acquisitions, our growth prospects may suffer, and we may not be able to realize sufficient scale advantages to compete effectively in all markets. To the extent we are successful in making acquisitions, if we are unsuccessful in integrating acquired companies or product lines with existing operations, or if integration is more difficult or more costly than anticipated, we may experience disruptions that could have a material adverse effect on our business, financial condition and results of operations. In addition, the market price of our common stock could be adversely affected if the effect of any acquisitions on the Microsemi consolidated group's financial results is dilutive or is below the market's or financial analysts' expectations. Some of the risks that may affect our ability to integrate or realize any anticipated synergies, benefits, or improved financial performance from acquired companies, businesses or assets include those associated with:

- unexpected losses of key employees or customers of the acquired company;
- conforming the acquired company's standards, processes, procedures and controls with our operations;
- coordinating new product and process development;
- increasing complexity from combining recent acquisitions;
- hiring additional management and other critical personnel;
- increasing the scope, geographic diversity and complexity of our operations;
- difficulties in consolidating facilities and transferring processes and know-how;
- other difficulties in the assimilation of acquired operations, technologies or products;
- diversion of management's attention from other business concerns; and

adverse effects on existing business relationships with customers.

In connection with acquisitions, we may:

- use a significant portion of our available cash;

- issue equity securities, which would dilute current stockholders' percentage ownership;

- incur substantial debt;

- incur or assume contingent liabilities, known or unknown, including potential lawsuits, infringement actions and similar liabilities;

- incur impairment charges related to goodwill or other intangibles;

- incur large, immediate accounting write-offs; and

- face antitrust or other regulatory inquiries or actions.

There can be no assurance the benefits of any acquisitions will outweigh the attendant costs, and if they do not, our results of operations and stock price may be adversely affected.

Our leverage and provisions in our credit facility and indenture for our senior unsecured notes could adversely affect our consolidated financial position and our ability to operate our business.

Our credit facilities requires that we comply with financial and restrictive covenants. Although we are currently in compliance with these covenants, unexpected downturns in our business may trigger certain covenants that increase our cost of borrowing, decrease the amounts available under our credit facilities, or both. The current amount outstanding on our credit facilities, and the outstanding principal amount of our 9.125% senior unsecured notes, each exceeds our current cash and cash equivalents balance, and we may incur additional debt in the future. Some of the risks associated with our leverage include the following:

- our ability to obtain additional financing in the future for acquisitions, capital expenditures, general corporate purposes or other purposes may be impaired;

- our current credit facilities only permit borrowing on variable rates of interest and increases in certain benchmark interest rates will increase the cost of borrowing;

- leverage will increase our vulnerability to declining economic conditions, particularly if the decline is prolonged;

- failure to comply with any of our debt covenants may result in an event of default which, if not cured or waived, could have a material adverse effect on us;

financial and restrictive covenants in our credit facilities and indenture governing the senior unsecured notes may adversely affect or limit our ability to implement business plans, react to changes in economic conditions, benefit from changes in tax regulations, pay a cash dividend or execute repurchases of our common stock;

- debt service payments will continue to have a negative impact on our cash flows; and prepayment terms may discourage us from refinancing our current credit agreement or reduce the benefit of lower interest rates.

Negative or uncertain worldwide economic conditions could prevent us from accurately forecasting demand for our products, which could adversely affect our operating results or market share.

Negative worldwide economic conditions and market instability in recent years have made it increasingly difficult for us, our customers and our suppliers to accurately forecast future product demand trends. If signs of improvement in the global economy do not progress as expected and global economic conditions worsen, our forecasts of product demand trends could prove to be incorrect and could cause us to produce excess products that can depress product prices, increase our inventory carrying costs and result in obsolete inventory. Alternatively, this forecasting difficulty

could cause a shortage of products, or materials used in our products, that could result in an inability to satisfy demand for our products and a loss of market share.

Negative or uncertain worldwide economic conditions may adversely affect our business, financial condition, cash flow and results of operations.

Recent domestic and global economic conditions have presented unprecedented and challenging conditions reflecting continued concerns about the availability and cost of credit, downgrades and continued negative pressure on sovereign credit ratings, the mortgage market, declining real estate values, volatility in energy costs, decreased consumer confidence and spending and added concerns fueled by the federal government's interventions in the financial and credit markets. These conditions have contributed to instability in both the domestic and international capital and credit markets, potentially increased the cost of credit and diminished expectations for the global economy. In addition, these conditions make it extremely difficult for our customers to accurately forecast and plan future business activities and could cause businesses to slow spending on our products, which could cause our sales to decrease or result in an extension of our sales cycles. Due to these conditions, our customers may have difficulties obtaining capital at adequate or historical levels to finance their ongoing businesses and operations, which could impair their ability to make timely payments to us. If that were to occur, we may be required to increase our allowance for doubtful accounts and our cash flows would be negatively impacted. We cannot predict the timing, strength or duration of any economic slowdown or subsequent economic recovery, worldwide or within our industry. If signs of improvement in the global economy do not progress as expected and economic conditions worsen, our business, financial condition, cash flows and results of operations will be adversely affected.

International operations and sales expose us to material risks and may increase the volatility of our operating results. Net sales from international markets represent a significant portion of total net sales and totaled 51% in 2015. These sales were principally to customers in Europe and Asia. Foreign sales are classified as shipments to foreign destinations. We maintain several international facilities or contracts with entities outside the United States, including Canada, China, France, India, Ireland, Israel, Japan, Korea, Malaysia, Macau, the Philippines, Taiwan, Thailand and the United Kingdom. There are risks inherent in doing business internationally, including:

- uncertainty and potentially divergent laws and regulations, highlighted by the recent vote by the United Kingdom to leave the European Union.

- legislative or regulatory requirements and potential changes in or interpretations of requirements in the United States and in the countries in which we manufacture or sell our products;
- trade restrictions, including sanctions and the suspension of export licenses;
- compliance with and changes in import/export regulations;
- restrictions in the transfer or repatriation of funds;
- tax regulations and treaties and potential changes in regulations and treaties in the United States and in and between countries in which we manufacture or sell our products;
- fluctuations in income tax expense and net income due to differing statutory tax rates in various domestic and international jurisdictions;
- uncertain interpretations of and difficulties enforcing intellectual property laws;
- local business and cultural factors that may differ from our domestic standards and practices, including business practices from which we are prohibited from engaging by the Foreign Corrupt Practices Act (the "FCPA") and other anti-corruption laws and regulations;
- availability of transportation services, including disruptions related to work stoppages, security incidents or natural events at manufacturing, shipping or receiving points or along transportation routes;
- work stoppages or disruption of local labor supply;

- communication interruptions;
- economic and political instability, including the recent uncertainty in the global financial markets;
- acts of war or terrorism, or health issues (such as for example Sudden Acute Respiratory Syndrome, Avian Influenza, or the H7N9, Ebola or Zika viruses), which could disrupt our manufacturing and logistical activities;
- changes in tariffs and freight rates;
- potentially longer payment cycles and difficulties in collecting receivables;
- difficulties and enforcing contracts generally; and
- currency exchange rate fluctuations, devaluation of foreign currencies, hard currencies shortages and exchange rate fluctuations.

International sales of our products that service the aerospace, defense and security markets are subject to U.S. and local government regulations and procurement policies and practices including regulations relating to import-export control. Violations of export control regulations could result in suspension of our ability to export our products. Depending on the scope of the suspension, this could have a material effect on our ability to perform certain international contracts. In addition, our failure or failures of our customers to maintain compliance with U.S. and foreign government regulations, including the FCPA and foreign anti-corruption measures, may result in export restrictions, fines and penalties that may materially and adversely affect our operating results.

If political, military, transportation, health or other issues in foreign countries result in cancellations of customer orders or contribute to a general decrease in economic activity or corporate spending, or directly impact Microsemi's marketing, manufacturing, financial and logistics functions, our consolidated results of operations and financial condition could be materially adversely affected. In addition, the laws of certain foreign countries may not protect our products, assets or intellectual property rights to the same extent as do U.S. laws. Therefore, the risk of piracy of our technology and products, which could result in a material adverse effect on our financial condition, operating results and cash flows, may be greater in those foreign countries.

Reliance on government contracts for a significant portion of our sales could have a material adverse effect on results of operations.

A significant portion of our sales are or may be derived from U.S. government agencies or customers whose principal sales are to U.S. government agencies which creates concentrations of credit risk. Future sales are subject to the uncertainties of governmental appropriations and national defense policies and priorities, including lingering impacts of sequestration under the Budget Control Act of 2011, constraints of the budgetary process and timing and potential changes in these policies and priorities. Additionally, the long-term outlook for the fiscal position of the U.S. federal government is also uncertain, as illustrated by the 2013 budget negotiations and the shutdown of non-essential U.S. federal government services in October 2013.

We have experienced delays and reduction in appropriations on programs that include our products. Further delays, reductions in or terminations of government contracts or subcontracts, including those caused by any past or future shutdown of the U.S. federal government, could materially and adversely affect our operating results. While we generally function as a subcontractor, further changes in U.S. government procurement regulations and practices, particularly surrounding initiatives to reduce costs, may adversely impact the contracting environment and our operating results.

Generally, the U.S. government and its contractors and subcontractors may terminate their contracts with us at any time, with or without cause. In the first quarter of 2014, the U.S. government terminated for convenience a \$75 million contract. We have in the past experienced the termination of at least one other contract due to the termination of the underlying government contract. All government contracts are also subject to price renegotiation in accordance with the U.S. Government Renegotiation Act. By reference to such contracts, all of the purchase orders we receive that are related to government contracts are subject to these possible events. In addition, the recent shutdown of non-essential U.S. government services and any future government shutdowns may significantly increase the risk of further contract terminations or renegotiations, and any such termination or renegotiation could have a material adverse impact upon our revenues and results of operations.





In addition, we are required to maintain compliance with government regulations, particularly for our facilities and products that service the defense markets. Maintaining compliance with these regulations, including audit requirements of the U.S. government and our customers that are subject to these requirements, requires we devote resources to matters including training, personnel, information technology and facilities. Failure to maintain compliance may result in the loss of certifications and fines and penalties that may materially and adversely affect our operating results.

From time to time, we have experienced declining defense-related sales, primarily as a result of contract award delays and reduced security and defense program funding. We may be unable to adequately forecast or respond to the timing of and changes to demand for security and defense-related products. In the past, defense-related spending on programs we participate in has increased at a rate that has been slower than expected, been delayed or declined. Our prospects for additional security and defense related sales may be adversely affected in a material manner by numerous events or actions outside our control.

We may not make the sales that are suggested by our order rates, backlog or book-to-bill ratio, and our book-to-bill ratio may be affected by product mix.

Undue reliance should not be placed on our backlog or book-to-bill ratios or changes to these amounts. We determine bookings substantially based on orders that are scheduled for delivery within 12 months. However, lead times for the release of purchase orders depend, in part, upon the scheduling practices of individual customers, and delivery times of new or non-standard products can be affected by scheduling factors and other manufacturing considerations. The rate of booking new orders can vary significantly from month to month. Customers frequently change their delivery schedules or cancel orders. We have in the past experienced long lead times for some of our products, which may have therefore resulted in orders in backlog being duplicative of other orders in backlog, which would increase backlog without resulting in additional revenues. Because of long lead times in certain products, our book-to-bill ratio may not be an indication of sales in subsequent periods. Uncertain worldwide economic conditions and market instability have also resulted in hesitance of our customers to place orders with long delivery schedules, which contributes to limited visibility into our markets.

The concentration of the facilities that service the semiconductor industry, including facilities of current or potential vendors or customers, makes us more susceptible to events or disasters affecting the areas in which they are most concentrated.

Relevant portions of the semiconductor industry, and the facilities that serve or supply this industry, tend to be concentrated in certain areas of the world. Events such as natural disasters and related disruptions, epidemics and health advisories like those related to Sudden Acute Respiratory Syndrome, Avian Influenza, H7N9 Virus, Ebola or Zika viruses, flooding, drought, earthquakes, tsunamis, power outages and infrastructure disruptions, and terrorism, civil unrest and political instability in those areas, have from time to time in the past, and may again in the future, adversely affect the semiconductor industry. In particular, events such as these could adversely impact our ability to manufacture or deliver our products and result in increased costs and a loss of revenue. Similarly, a localized risk affecting our employees or the staff of our suppliers could impair the total volume of products that we are able to manufacture, which could adversely affect our results of operations and financial condition.

In the first quarter of 2012, severe flooding in certain regions of Thailand forced a shutdown of our operations in two subcontracted facilities in Thailand. The two Thailand facilities together accounted for as much as 5% of our total quarterly revenues. In response to the impact of flooding at subcontractor facilities in Thailand, we implemented plans to move production to other facilities outside the affected area. Production capabilities at these other facilities compensated for the loss of production in the flooded facilities in Thailand and we believe we recovered from this event as of the end of the second quarter of 2012. However, unforeseen impacts on our customers, suppliers or subcontractors as a result of the flooding in Thailand, or other future natural disasters, could affect our revenue, consolidated financial position, results of operations and cash flows.

We are dependent on third parties for key functions including foundries for wafer supplies, subcontractors for assembly, test and packaging services and vendors for logistics, and problems at these third parties could adversely affect our business and operating results.

We depend on third party subcontractors, primarily in Asia, for wafer fabrication, assembly, testing and packaging of an increasing portion of our products. At the end of 2015, over 90% of our wafer, assembly and test requirements were sourced from third party foundries and subcontractors. We expect these percentages may increase due, in part, to the

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manufacturing of our next-generation products by third party subcontractors in Asia and from activity at recently acquired operations.

Our wafer designs requirements are increasing in technological complexity and in order to meet our designs specifications, our foundry partners must expend resources for capital equipment and develop or improve manufacturing processes. Our foundry partners' inability or unwillingness to expend these resources could adversely affect our business and operating results. The assembly, testing and packaging of our products is performed by a limited group of subcontractors. Disruption or termination of any of these subcontractors could occur and such disruptions or terminations could harm our business and operating results.

We utilize third party logistics services, including transportation, warehouse and shipping services. These service providers are subject to interruptions that affect their ability to service us, including the availability of transportation services, disruptions related to work stoppages, volatility in fuel prices and security incidents or natural events at manufacturing, shipping or receiving points or along transportation routes.

We generally do not have any long-term agreements with our subcontractors. As a result, we may be unable to directly control our quality assurance and product delivery schedules. The cost of product replacements or returns and other warranty matters in connection with quality assurance problems caused by third party subcontractors could materially adversely affect us. Third party manufacturers generally will have longer lead times for delivery of products as compared with our internal manufacturing, and therefore, when ordering from these suppliers, we will be required to make longer-term estimates of our customers' current demand for products, and these estimates are difficult to make accurately. Also, due to the amount of time typically required to qualify assemblers and testers, we could experience delays in the shipment of our products if we are forced to find alternate third parties to assemble or test our products. Any product delivery delays in the future could have a material adverse effect on our operating results, financial condition and cash flows. Our operations and ability to satisfy customer obligations could be adversely affected if our relationships with these subcontractors were disrupted or terminated. In addition, these subcontractors must be qualified by the U.S. government or customers for high-reliability processes. Historically the Defense Logistics Agency has rarely qualified any foreign manufacturing or assembly lines for reasons of national security; therefore, our ability to move certain manufacturing offshore may be limited or delayed.

In the event any of our subcontractors were to experience financial, operational, production or quality assurance difficulties resulting in a reduction or interruption in supply to us, our operating results could suffer until alternate qualified subcontractors, if any, were to become available and active.

Both our customers and we are subject to laws, regulations and similar requirements, changes to which may adversely affect our business and operations.

Both our customers and we are subject to laws, regulations and similar requirements that affect our business and operations, including, but not limited to, the areas of commerce, import and export control (especially related to products in our Aerospace & Defense end market), financial disclosures, intellectual property, income and other taxes, anti-trust, anti-corruption, labor, environmental, health and safety. Our compliance in these areas may be costly, especially in areas where there are inconsistencies between the various jurisdictions in which we operate. While we have implemented policies and procedures to comply with laws and regulations, there can be no assurance our employees, contractors, suppliers or agents will not violate such laws and regulations or our policies. Any such violation or alleged violation could materially and adversely affect our business. Any changes or potential changes to laws, regulations or similar requirements, or our ability to respond to these changes, may significantly increase our costs to maintain compliance or result in our decision to limit our business, products or jurisdictions in which we operate, any of which could materially and adversely affect our business and operations.

Federal and state regulatory agencies, including the United States Federal Communications Commission and the various state public utility commissions and public service commissions, regulate most of our domestic telecommunications customers. Similar government oversight also exists in the international market. While we may not be directly affected by this legislation, such regulation of our customers may negatively impact our business. For instance, the sale of our products may be affected by the imposition upon certain of our customers of common carrier tariffs and the taxation of telecommunications services. These regulations are continuously reviewed and changed by the various governmental agencies. Changes in current or future laws or regulations, in the United States or elsewhere,

could negatively impact our business and operating results.

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The Dodd-Frank Wall Street Reform and Consumer Protection Act includes provisions regarding certain minerals and metals, known as conflict minerals, mined from the Democratic Republic of Congo and adjoining countries. These provisions require companies to undertake due diligence procedures and report on the use of conflict minerals in its products, including products manufactured by third parties. Compliance with these provisions has caused and will continue to cause us to incur costs to determine whether our supply chain is conflict free and we may face difficulties if our suppliers are unwilling or unable to verify the source of their materials. Our ability to source these minerals and metals may also be adversely impacted. In addition, our customers may require that we provide them with a certification and our inability to do so may disqualify us as a supplier.

Changes in our tax provisions, or exposure to additional income tax or unfavorable results of tax examinations could affect our financial results.

We are subject to federal and state income taxes in the United States and numerous foreign jurisdictions. Our tax liabilities are affected by the amounts we record in intercompany transactions for inventory, services, licenses, funding and other items. We are subject to ongoing tax examinations in various jurisdictions. Tax authorities may disagree with our intercompany charges or other tax positions and assess additional taxes. Our application of transfer pricing has been the primary subject of the current examination of our U.S. federal and Canadian income tax returns. We regularly assess the likely outcomes of examinations in order to determine the appropriateness of our tax provision. However, the actual outcomes of examinations could result in large and unexpected tax liabilities for past tax periods and may have a material impact on our consolidated financial position, results of operations or cash flows. In addition, our effective tax rate in the future could be adversely affected by changes in the mix of earnings in countries with differing statutory tax rates and benefits, changes in available credits and incentives, changes in the valuation of deferred tax assets and liabilities, changes in tax laws, especially tax laws related to foreign operations, and the discovery of new information in the course of our tax return preparation process. Any of these changes could materially affect our operating results, cash flows and financial condition.

We hold cash and cash equivalents at various foreign subsidiaries that may not be readily available to meet domestic cash requirements.

Our various foreign subsidiaries hold cash and cash equivalents and as we intend to reinvest certain foreign earnings indefinitely these balances held outside the United States may not be readily available to meet our domestic cash requirements. We require a substantial amount of cash in the United States for operating requirements, purchases of property and equipment, debt service, repurchases of our common stock and potentially for future acquisitions. If we are unable to meet our domestic cash requirements using domestic cash flows from operations, domestic cash and cash equivalents, or by settling loans receivable with our foreign subsidiaries, it may be necessary for us to consider repatriation of earnings we have designated as permanently reinvested. This may require us to record additional income tax expense and remit additional taxes, which could have a material effect on our results of operations, cash flows and financial condition.

Our operating results may fluctuate in future periods, which could cause our stock price to decline.

We have experienced, and expect to experience in future periods, fluctuations in net sales and operating results from period to period. Our projections and results may be subject to significant fluctuations as a result of a number of factors including:

- the timing of orders from and shipment of products to major customers;
- an unexpected reduction in sales to, or loss of, key customers;
- customer payments that are unexpectedly delayed;
- our product mix;
- changes in the prices of our products;
- manufacturing delays or interruptions;
- delays or failures in testing and processing products for aerospace and defense applications;

- inventory obsolescence or write-downs;
- restructuring charges;
- variations in the cost of components for our products;
- limited availability of components we obtain from a single or a limited number of suppliers; and
- seasonal and other fluctuations in demand for our products.

We have in the past closed, combined, sold or disposed of certain of our operations, have current plans to combine certain of our operations and may determine to do so in the future, which could reduce our sales volume, profitability and result in significant restructuring costs.

We face major technical challenges in regards to transferring component manufacturing between locations. Before a transfer of manufacturing, we must be finished qualifying the new facility appropriately with the U.S. government or certain customers. In addition, to mitigate the potential for manufacturing disruptions following a closure, we typically build inventory to support the transition process. While we generally plan to retain revenues and income of those operations by transferring the manufacturing elsewhere within Microsemi's subsidiaries, our plans may change at any time based on reassessment of the alternatives and consequences. While we hope to benefit overall from increased gross margins and increased capacity utilization rates at remaining operations, the remaining operations will need to bear the corporate administrative and overhead costs, which are charges to income that had been allocated to the discontinued business units. Moreover, delays in effecting our consolidations could result in changes in the timing of realized costs savings and in greater than anticipated costs incurred to achieve our projected longer-range savings.

We may make further specific determinations to consolidate, close, sell or divest of additional facilities, operations or product lines, which could be announced at any time. Possible adverse consequences from current and future consolidation or disposition activities may include a loss of revenues and various accounting charges such as for workforce reduction, including severance and other termination benefits and for excess facilities, including lease termination fees, future contractual commitments to pay lease charges, facility and environmental remediation costs and moving costs to remove property and equipment from facilities. We may also be adversely impacted from inventory buildup in preparation for the transition of manufacturing, disposition costs, impairments of goodwill, a possible immediate loss of revenues, and other items in addition to normal or attendant risks and uncertainties. We may be unsuccessful in any of our current or future efforts to consolidate our business into a smaller number of facilities. Our plans to minimize or eliminate any loss of revenues during consolidation may not be achieved.

We may not be able to develop new technologies and products to satisfy changes in customer demand or industry standards, and our competitors could develop products that decrease the demand for our products.

Rapidly changing technologies and industry standards, along with frequent new product introductions, characterize the semiconductor industry. Our financial performance depends, in part, on our ability to design, develop, manufacture, assemble, test, market and support new products and enhancements on a timely and cost-effective basis. If we are unable to continue to reduce package sizes, improve manufacturing yields and expand sales, we may not remain competitive. The principal focus of our research and development activities has been to improve processes and to develop new products that support the growth of our businesses. The spending on research and development was principally to develop new higher-margin application-specific products, including, among others, our process and core architecture development for next generation programmable products, storage and optical products, higher power PoE solutions, the continued roadmap development of our industry-leading timing & synchronization products, our silicon germanium (SiGe) RF power amplifier solutions for wireless LAN applications, and the ongoing development of gallium nitride (GaN) and silicon carbide (SiC) power management and RF solutions. These projects are subject to various risks and uncertainties we are not able to control, including changes in customer demand and the introduction of new or superior technologies by others. Moreover, any failure by us in the future to develop new technologies or timely react to changes in existing technologies could materially delay our development of new products, which could result in product obsolescence, decreased revenues and a loss of our market share to our competitors. New technologies or products we may develop may not lead to an incremental increase in revenues, and there is a risk these new technologies or products will decrease the demand for our existing products and result in an offsetting reduction in revenues. In addition, products or technologies developed by others may render our products or technologies obsolete

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or non-competitive. A fundamental shift in technologies in our product markets could have a material adverse effect on our competitive position within the industry.

Additionally, our ability to compete within our industry will depend on our ability to identify and ensure compliance with constantly evolving industry standards. The emergence of new industry standards could render our products incompatible with products developed by major manufacturers. As a result, we could be required to invest significant time and effort and incur significant expense to redesign our products to ensure compliance with relevant standards. If our products are not in compliance with prevailing industry standards, it could have a material adverse effect on our business operations and financial results.

We must commit resources to research and development, design, and production prior to receipt of purchase commitments and could lose some or all of the associated investment.

We sell products primarily pursuant to purchase orders for current delivery, rather than pursuant to long-term supply contracts. Many of these purchase orders may be revised or canceled without penalty. As a result, we must commit resources to the research, design and production of products without any advance purchase commitments from customers. Any inability to sell a product after we devote significant resources to it could have a material adverse effect on our business, financial condition, results of operations and cash flows.

There may be unanticipated costs associated with appropriately scaling our manufacturing capacity to meet expected changes in customer demand.

We may incur unanticipated costs as we scale our manufacturing capacity to meet expected changes in customer demand. During periods of anticipated increases in customer demand, we may determine our business will require increased manufacturing capacity on our part and on the part of certain outside foundries, assembly shops, or testing facilities for some of our integrated circuit products or other products. Expansion activities are subject to a number of risks, including:

- unavailability or late delivery of the advanced, and often customized, equipment used in the production of our specialized products;
- availability of qualified manufacturing personnel;
- delays in bringing new production equipment on-line;
- delays in supplying satisfactory designs or products to our existing customers;
- unforeseen environmental, engineering or manufacturing qualification problems relating to existing or new facilities; and
- overexpansion may result in unfavorable manufacturing variances, restructuring costs and impairments.

These and other risks may affect the ultimate cost and timing of any expansion of our capacity.

Downturns in the highly cyclical semiconductor industry have in the past adversely affected our operating results, cash flows and the value of our business, and may continue to do so in the future.

The semiconductor industry is highly cyclical and is characterized by constant technological change, rapid product obsolescence and price erosion, short product life-cycles, consolidations of customers, and fluctuations in product supply and demand. During recent years we, as well as many others in our industry, have experienced significant declines in the pricing of, as well as demand for, products during the "down" portions of these cycles, which have sometimes been severe and prolonged. We have also noted consolidations of customers, particularly our distributors, which may adversely affect our pricing leverage or ability to maintain sufficient distributor channel inventory to meet end customer demand. In the future, these downturns may prove to be as, or possibly even more, severe than past ones. Our ability to sell our products depends, in part, on continued demand in each of our diverse end markets. Each of these end markets has, in the past, experienced reductions in demand, and current and future downturns in any of these markets may continue to adversely affect our revenues, operating results, cash flows and financial condition.

The semiconductor business is subject to downward price pressure.

The market for our products has been characterized by declining selling prices, and we anticipate that our average selling prices will decrease in future periods, although the timing and amount of these decreases cannot be predicted with any certainty. The pricing pressure in the semiconductor industry in past years has been due to a large number of factors, many of which were not easily foreseeable, such as the Asian currency crisis, industry-wide excess manufacturing capacity, weak economic growth, the slowdown in capital spending that followed the "dot-com" collapse, the reduction in capital spending by telecom companies and satellite companies, and the effects of the tragic events of terrorism on September 11, 2001. Similar to past years, recent unfavorable economic conditions have resulted in a tightening of the credit markets. If signs of improvement in the global economy do not progress as expected and global economic conditions worsen, we may experience a decline in our average selling prices. In addition, our competitors have in the past, and may again in the future, lower prices in order to increase their market share. Continued downward price pressure in the industry may reduce our operating results and harm our financial and competitive position.

The semiconductor industry is highly competitive.

The semiconductor industry, including the areas in which we do business, is highly competitive. We expect intensified competition from existing competitors and new entrants. Competition is based on price, product performance, product availability, quality, reliability and customer service. In addition, companies not currently in direct competition with us may introduce competing products in the future. Some of our current major competitors are Altera Corporation; Texas Instruments, Inc.; Integrated Device Technology, Inc.; Linear Technology Corp.; M/A COM Technology Solutions Inc.; Maxim Integrated Products, Inc.; Semtech Corp.; Silicon Laboratories, Inc.; Skyworks Solutions, Inc.; and Xilinx, Inc. Several of these companies are larger than we are and have greater resources than we have and may therefore be better able than we are to penetrate new markets, pursue acquisition candidates, and withstand adverse economic or market conditions. We expect intensified competition from both of these existing competitors and new entrants into our markets. To the extent we are not able to compete successfully in the future, our financial condition, operating results or cash flows could be harmed.

Compound semiconductor products may not successfully compete with silicon-based products.

Our choice of technologies for development and future implementation may not reflect future market demand. The production of gallium arsenide (GaAs), indium gallium phosphide (InGaP), indium gallium arsenide phosphide (InGaAsP) SiGe or SiC ICs is more costly than the production of silicon circuits, and we believe it will continue to be more costly in the future. The costs differ because of higher costs of raw materials, lower production yields and higher unit costs associated with lower production volumes. Silicon semiconductor technologies are widely used in process technologies for integrated circuits, and these technologies continue to improve in performance. As a result, we must offer compound semiconductor products that provide vastly superior performance to that of silicon for specific applications in order for our products to be competitive with silicon products. If we do not offer compound semiconductor products that provide sufficiently superior performance to offset the cost differential and otherwise successfully compete with silicon-based products, our revenues and operating results may be materially and adversely affected.

Production delays related to new compound semiconductors could adversely affect our future results.

We utilize process technology to manufacture compound semiconductors such as GaAs, InGaP, InGaAsP, SiGe and SiC primarily to manufacture semiconductor components. We are pursuing this development effort internally as well as with third party foundries. Our efforts sometimes may not result in commercially successful products. Certain competitors offer this capability and our customers may purchase our competitors' products instead of ours for this reason. In addition, the third party foundries we use may delay delivery of, or even completely fail to deliver, technology and products to us. Our business and financial prospects could be materially and adversely affected by any failure by us to timely produce these products.

We may be unable to retain our customers due in part to our inability to fulfill our customer demand and other factors.

Our ability to fulfill our customers' demand for our products is and will continue to be dependent in part on our order volumes and long lead times with regards to our manufacturing and testing of certain high-reliability products. The

lead time for manufacturing and testing of high-reliability products can be many months. In response to current demand, we have recently increased our capital expenditures for production equipment as well as increased expenses for

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personnel at certain manufacturing locations. We may have delays or other difficulties in regards to increasing our production and in hiring and retaining qualified personnel. In addition, we have raised prices on certain products, primarily in our Aerospace & Defense and Industrial end markets. Manufacturing delays and price increases may result in our customers reducing their purchase levels with us and/or seeking alternative solutions to meet their demand. In addition, the current demand may not continue in the future. Decreased sales as a result of a loss of one or more significant customers could materially and adversely impact our business and results of operations.

Unfavorable or uncertain conditions in certain markets our original equipment manufacturer customers address may cause fluctuations in our rate of revenue growth or financial results.

Demand for our products is dependent on demand for our customers' products. Markets for our customers' product may not develop in the manner or in the time periods our customers anticipate. If domestic and global economic conditions worsen, overall spending may be reduced or shifted to products other than those made by our customers, which would adversely impact demand for products in these markets. Reduced sales by our customers will adversely impact demand by our customers for our products and could also slow new product introductions by our customers and by us. Lower net sales of our products would have an adverse effect on our revenue, cash flow and results of operations.

Fluctuations in sales of high-reliability products for use in medical devices may adversely affect our financial results. Although the market for medical devices is growing, customers in this market could reduce their reliance on outside suppliers. The medical device market also fluctuates based on several other factors, such as product recalls and the need to secure regulatory approvals. Product recalls can, from time to time, accelerate sales to levels that cannot be sustained for long periods of time. The timing and qualification of new generations of products brought to market by OEMs can also result in fluctuations in order rates.

Variability of our manufacturing yields may affect our gross margins and profits.

Our manufacturing yields vary significantly among products, depending on the complexity of a particular product's design and our experience in manufacturing that type of product. We have in the past experienced difficulties in achieving planned yields, which have adversely affected our gross margins and profits.

The fabrication of semiconductor products is a highly complex and precise process. Problems in the fabrication process can cause a substantial percentage of wafers to be rejected or numerous circuits on each wafer to be non-functional, thereby reducing yields. These difficulties primarily include:

- defects in masks, which are used to transfer circuit patterns onto our wafers;
- impurities in the materials used;
- contamination of the manufacturing environment; and
- equipment failure.

Because a large portion of our costs of manufacturing is relatively fixed and average selling prices for our products tend to decline over time, it is critical for us to improve the number of shippable circuits per wafer and increase the production volume of wafers in order to maintain and improve our results of operations. Yield decreases can result in substantially higher unit costs, which could materially and adversely affect our operating results and have done so in the past. Moreover, our process technologies have primarily utilized standard silicon semiconductor manufacturing equipment, and production yields of compound integrated circuits have been relatively low compared with silicon circuit devices. We may be unable to continue to improve yields in the future, and we may suffer periodic yield problems, particularly during the early production of new products or introduction of new process technologies. In either case, our results of operations could be materially and adversely affected.

Some of our facilities and the facilities of our suppliers and customers are located near major earthquake fault lines. Our headquarters, our major operating facilities, and certain other critical business operations and customers are located near known major earthquake fault lines. We presently do not have earthquake insurance. We could be materially and adversely affected in the event of a major earthquake.

Delays in beginning production, implementing production techniques, resolving problems associated with technical equipment malfunctions, or issues related to government or customer qualification of facilities could adversely affect our manufacturing efficiencies, our ability to realize cost savings and the timing and amount of revenue we realize. Microsemi's consolidated manufacturing efficiency will be an important factor in our future profitability, and we may be unsuccessful in our efforts to maintain or increase our manufacturing efficiency. Our manufacturing processes, and those utilized by our third-party subcontractors, are highly complex, require advanced and costly equipment and are sometimes modified in an effort to improve yields and product performance. We have from time to time, experienced difficulty in transitioning manufacturing processes to different facilities or adopting new manufacturing processes. As a consequence, we have at times experienced delays in product deliveries and reduced yields. Every silicon wafer fabrication facility utilizes very precise processing, and processing difficulties and reduced yields commonly occur, often as a result of contamination of the material. Reduced manufacturing yields can often result in manufacturing and shipping delays due to capacity constraints. Therefore, manufacturing problems can result in additional operating expenses and delayed or lost revenues. Microsemi may experience manufacturing problems in achieving acceptable yields or experience product delivery delays in the future as a result of, among other things, upgrading existing facilities, relocating processes to different facilities, or changing its process technologies, any of which could result in a loss of future revenues or an increase in manufacturing costs.

Interruptions, delays or cost increases affecting our materials, parts, equipment or subcontractors may impair our competitive position.

Our manufacturing operations, and the outside manufacturing operations that we use increasingly, in some instances, depend upon obtaining a governmental qualification of the manufacturing process, and in all instances, adequate supplies of materials including wafers, parts and equipment (including silicon, mold compounds and lead frames) on a timely basis from third parties. Some of the outside manufacturing operations we use are based in foreign countries. Our results of operations could be adversely affected if we are unable to obtain adequate supplies of materials, parts and equipment in a timely manner or if the costs of materials, parts or equipment increase significantly. From time to time, suppliers may extend lead times, limit supplies or increase prices due to capacity constraints or other factors. Although we generally use materials, parts and equipment available from multiple suppliers, we have a limited number of suppliers for some materials, parts and equipment. In addition, if signs of improvement in the global economy do not progress as expected and global economic conditions worsen, our suppliers may cease operations or be unable to obtain capital at adequate or historical levels to finance their ongoing businesses and operations, which could impair their ability to continue to supply us. If alternate suppliers for these materials, parts and equipment are not available, our operations could be interrupted, which would have a material adverse effect on our operating results, financial condition and cash flows.

Fixed costs may reduce operating results if our sales fall below expectations.

Our expense levels are based, in part, on our expectations for future sales. Many of our expenses, particularly those relating to capital equipment and manufacturing overhead, are relatively fixed. We might be unable to reduce spending quickly enough to compensate for reductions in sales. Accordingly, shortfalls in sales could materially and adversely affect our operating results. This challenge could be made even more difficult if lead times between orders and shipments are shortening.

Failure to manage consolidation of operations effectively could adversely affect our margins and earnings.

Our ability to successfully offer and sell our products requires effective planning and management processes. Our consolidations and realignments of operations, and expected future growth, may place a significant strain on our management systems and resources, including our financial and managerial controls, reporting systems, procedures



and information technology. In addition, we will need to continue to train and manage our workforce worldwide. Any unmet challenges in that regard could negatively affect our results of operations.

Any failure by us to protect our proprietary technologies or maintain the right to use certain technologies may negatively affect our ability to compete.

We rely heavily on our proprietary technologies. Our future success and competitive position depend in part upon our ability to obtain or maintain protection of certain proprietary technologies used in our principal products. We do not have significant patent protection on many aspects of our technology. The protection of some of our technology as "trade secrets" will not necessarily protect us from all uses by other persons of our technology, or their use of technology that is similar or superior to that which is embodied in our trade secrets. In addition, others may be able to independently duplicate or exceed our technology in whole or in part. In the instances in which we hold patents or patent licenses, such as with respect to some circuit components for notebook computers and LCD TVs, any patents held by us may be challenged, invalidated or circumvented, or the rights granted under any patents may not provide us with competitive advantages. Patents often provide only narrow protection and require public disclosure of information that may otherwise be subject to trade secret protection. In addition, patents eventually expire and are not renewable.

Obtaining or protecting our proprietary rights may require us to defend claims of intellectual property infringement by our competitors. We could also become subject to lawsuits in which it is alleged we or companies we have acquired have infringed or are infringing upon the intellectual property rights of others with or without our prior awareness of the existence of those third-party rights, if any. Litigation in connection with our intellectual property, whether instituted by us or others, could be very costly and distract management and other resources from our business. We are currently involved in certain patent litigation to protect our patents and patent rights, which could cause legal costs to increase above normal levels over the next several years. It is not possible to estimate the exact amounts of these costs, but it is possible these costs could have a negative effect on our future results.

Moreover, if any infringement, real or imagined, happens to exist, arise or is claimed in the future, we may be exposed to substantial liability for damages and may need to obtain licenses from the patent owners, discontinue or change our processes or products or expend significant resources to develop or acquire non-infringing technologies. We may not be successful in such efforts, or such licenses may not be available under reasonable terms. Any failure by us to develop or acquire non-infringing technologies or to obtain licenses on acceptable terms could have a material adverse effect on our operating results, financial condition and cash flows.

Our products may be found to be defective or hazardous and we may not have sufficient liability insurance.

There is at any time a risk that our products may be found to be defective or to contain, without the customer's knowledge, certain prohibited hazardous chemicals after we have already shipped the products in volume, perhaps requiring a product replacement or recall. We may be subject to product returns that could impose substantial costs and have a material and adverse effect on our business, financial condition and results of operations. Our aerospace, defense, and industrial businesses in particular expose us to potential liability risks that are inherent in the manufacturing and marketing of high-reliability electronic components for critical applications. Production of many of these products is sensitive to minute impurities, which can be introduced inadvertently in manufacturing. Any production mistake can result in large and unanticipated product returns, product liability and warranty liability. Environmental regulations have imposed on every major participant in the electronics industry a new burden of determining and tracking the presence and quantity of certain chemicals in the content of supplies we buy and add to our products for sale and to inform our customers about each of our finished goods' relevant chemical contents. The management and execution of this process is very challenging, and mistakes in this information gathering process could have a material adverse effect on our business.

We may be subject to product liability claims with respect to our products. Our product liability insurance coverage may be insufficient to pay all such claims. In addition, product liability insurance may become too costly for us to maintain or may become completely unavailable to us in the future. We may not have sufficient resources to satisfy any product liability claims not covered by insurance, which would materially and adversely affect our financial position.

Environmental liabilities could adversely impact our consolidated financial position.

Federal, state and local laws and regulations impose various restrictions and controls on the discharge of materials, chemicals and gases used in our semiconductor manufacturing processes or in our finished goods. Under recent

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environmental regulations, we are responsible for determining whether certain toxic metals or certain other toxic chemicals are present in any given component we purchase and in each given product we sell. These environmental regulations have required us to expend a portion of our resources and capital on relevant compliance programs. In addition, under other laws and regulations, we could be held financially responsible for remedial measures if our current or former properties are contaminated or if we send waste to a landfill or recycling facility that becomes contaminated, even if we did not cause the contamination. Also, we may be subject to additional common law claims if we release substances that damage or harm third parties. Further, future changes in environmental laws or regulations may require additional investments in capital equipment or the implementation of additional compliance programs in the future. Any failure to comply with existing or future environmental laws or regulations could subject us to significant liabilities and could have a material adverse effect on our operating results, cash flows and financial condition.

In the conduct of our manufacturing operations, we have handled and do handle materials that are considered hazardous, toxic or volatile under federal, state and local laws. The risk of accidental release of such materials cannot be completely eliminated. In addition, we operate or own facilities located on or near real property that was formerly owned and operated by others. These properties were used in ways that involved hazardous materials. Contaminants may migrate from, within or through any such property, which may give rise to claims against us. Third parties who are responsible for contamination may not have funds, or may not make funds available when needed, to pay remediation costs imposed upon us jointly with them under environmental laws and regulations.

Litigation could adversely impact our consolidated financial position.

We are and have been involved in various litigation matters, including from time to time, litigation relating to employment matters, commercial transactions, intellectual property matters, contracts, environmental matters and matters related to compliance with governmental regulations. Litigation is inherently uncertain and unpredictable. The potential risks and uncertainties include, but are not limited to, such factors as the costs and expenses of litigation and the time and attention required of management to attend to litigation. An unfavorable resolution of any particular legal claim or proceeding, and/or the costs and expenses incurred in connection with a legal claim or proceeding, could have a material adverse effect on our consolidated financial position or results of operations.

Our future success depends, in part, upon our ability to continue to attract and retain the services of our executive officers or other key management or technical personnel.

We could potentially lose the services of any of our senior management personnel at any time due to a variety of factors that could include, without limitation, death, incapacity, military service, personal issues, retirement, resignation or competing employers. Our ability to execute current plans could be adversely affected by such a loss.

We may fail to attract and retain qualified technical, sales, marketing and managerial personnel required to continue to operate our business successfully. Personnel with the expertise necessary for our business are scarce and competition for personnel with proper skills is intense. Also, attrition in personnel can result from, among other things, changes related to acquisitions, retirement and disability. We may not be able to retain existing key technical, sales, marketing and managerial employees or be successful in attracting, developing or retaining other highly-qualified technical, sales, marketing and managerial personnel, particularly at such times in the future as we may need to fill a key position. If we are unable to continue to develop and retain existing executive officers or other key employees or are unsuccessful in attracting new highly-qualified employees, our business, financial condition and results of operations could be materially and adversely affected.

The volatility of our stock price could affect the value of an investment in our stock and our future financial position. The market price of our stock has fluctuated widely. Between June 28, 2015 and July 3, 2016, the market sale price of our common stock ranged between a low of \$28.24 and a high of \$39.56. The historical market prices of our common stock may not be indicative of future market prices. We may not be able to sustain or increase the value of our common stock. The trading price of our common stock may be influenced by factors beyond our control, such as the recent unprecedented volatility of the financial markets and the current uncertainty surrounding domestic and foreign economies. Declines in the market price of our stock could adversely affect our ability to retain personnel with stock incentives, to acquire businesses or assets in exchange for stock and/or to conduct future financing activities with or involving our common stock.

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At times, our working capital levels have risen, which adversely affects cash flow.

At times, our working capital levels have risen and the increase has adversely affected cash flow. A factor contributing to the increase in our working capital has related to acquisitions with increases in accounts receivable and inventory generally exceeding increases in accounts payable and accrued liabilities. Other factors resulting in an increase in working capital have been delays in receiving customer payments and a buildup of inventory prior to the consolidation of our manufacturing operations. We built inventory cushions during the transition of manufacturing between facilities in order to maintain an uninterrupted supply of product. Obsolescence of any inventory has recently and could in the future result in adverse effects on our future results of operations and future revenue. We periodically evaluate the profitability of our various offerings and in 2014, our evaluation led us to selectively exit product offerings we believe will continue to lag our overall profitability goals. This resulted in inventory charges of \$7.9 million. We believe for many of these products, market dynamics dictate that price is the primary differentiator rather than our value-added core competencies of power, reliability, security and performance.

There may be some potential effects of system outages or data security breaches, which could adversely affect our operations, financial results or reputation.

We face risks from electrical or telecommunications outages, computer hacking or other general system failure. We rely heavily on our internal information and communications systems and on systems or support services from third parties to manage our operations efficiently and effectively. Any of these are subject to failure. System-wide or local failures that affect our information processing could have a material adverse effect on our business, financial condition, results of operations and cash flows. In addition, a system failure or data security breach could also result in the unintentional disclosure of confidential information about us, our customers or our employees, which could result in our incurring costs for remedial or preventative actions, damage our reputation with customers and reduce demand for our products and services. Further, insurance coverage does not generally protect from normal wear and tear, which can affect system performance. Any applicable insurance coverage for an occurrence could prove to be inadequate. Coverage may be or become unavailable or inapplicable to any risks then prevalent. We are upgrading and integrating, and have plans to upgrade and integrate further, our enterprise information systems, and these efforts may cause additional strains on personnel and system resources or may result in potential system outages.

Our accounting policies and estimates have a material effect on the financial results we report.

Critical accounting policies and estimates have a material effect on our calculations and estimations of amounts in our financial statements. Our operating results and balance sheets may be adversely affected either to the extent that actual results prove to be materially lower than previous accounting estimates or to the extent that accounting estimates are revised adversely. We base our critical accounting policies, including our policies regarding revenue recognition, reserves for returns, rebates, price protections, and bad debt and inventory valuation, on various estimates and subjective judgments we may make from time to time. The judgments made can significantly affect net income and our balance sheets. We are required to make significant judgments concerning inventory, and whether it becomes obsolete or excess, and concerning impairments of long-lived assets and of goodwill. Our judgments, estimates and assumptions are subject to change at any time. In addition, our accounting policies may change at any time as a result of changes in generally accepted accounting principles as they apply to us or changes in other circumstances affecting us. Changes in accounting policy have affected and could further affect, in each case materially and adversely, our results of operations or financial position.

If, in the future, we conclude our internal control over financial reporting is not effective, investors could lose confidence in the reliability of our financial statements, which could result in a decrease in the value of our common stock.

As directed by Section 404 of the Sarbanes-Oxley Act of 2002, the SEC adopted rules requiring public companies to include a report of management on the companies' internal control over financial reporting in their annual reports on Form 10-K, including an assessment by management of the effectiveness of the filing company's internal control over financial reporting. In addition, the independent registered public accounting firm auditing a public company's financial statements must attest to the effectiveness of the company's internal control over financial reporting. There is a risk that in the future we may identify internal control deficiencies that suggest that our controls are no longer effective. This could result in an adverse reaction in the financial markets due to a loss of confidence in the reliability

of our financial statements, which could cause the market price of our common stock to decline and make it more difficult for us to finance our operations.

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Our investments in securities subject us to principal, liquidity and counterparty risks that could adversely affect our financial results.

We invest cash balances primarily in money market funds. At times, we have also entered into interest rate swap and foreign currency forward contracts. While all of our investments to date are highly rated and we believe our counterparties to be highly rated, current credit market disruptions may adversely affect the value and liquidity of these investments and may affect the ability of our counterparties to fulfill their contractual obligations.

We may have increasing difficulty attracting and retaining qualified outside Board members.

The directors and management of publicly traded corporations are increasingly concerned with the extent of their personal exposure to lawsuits and shareholder claims, as well as governmental and creditor claims that may be made against them in connection with their positions with publicly-held companies. Outside directors are becoming increasingly concerned with the availability of directors' and officers' liability insurance to pay on a timely basis the costs incurred in defending shareholder claims. Directors' and officers' liability insurance is expensive and difficult to obtain. The SEC and the NASDAQ Stock Market have also imposed higher independence standards and certain special requirements on directors of public companies. Accordingly, it may become increasingly difficult to attract and retain qualified outside directors to serve on our Board.

Delaware law and our charter documents contain provisions that could discourage or prevent a potential takeover of Microsemi that might otherwise result in our stockholders receiving a premium over the market price for their shares. Provisions of Delaware law and our certificate of incorporation and bylaws could make more difficult an acquisition of Microsemi by means of a tender offer, a proxy contest, or otherwise, and the removal of incumbent officers and directors.

These provisions include:

Section 203 of the Delaware General Corporation Law, which prohibits a merger with a 15%-or-greater stockholder, such as a party that has completed a successful tender offer, without board approval until three years after that party became a 15%-or-greater stockholder; and

The authorization in the certificate of incorporation of undesignated preferred stock, which could be issued without stockholder approval in a manner designed to prevent or discourage a takeover or in a way that may dilute an investment in our common stock.

Certain provisions of our charter documents, including provisions eliminating the ability of stockholders to call special meetings and limiting the ability of stockholders to raise matters at a meeting of stockholders without giving advance notice, may have the effect of delaying or preventing changes in control or management of Microsemi. In addition, our charter documents do not permit cumulative voting, which may make it more difficult for a third party to gain control of our Board of Directors.

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

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On September 9, 2014, Microsemi Corporation's Board of Directors authorized the repurchase of up to \$100.0 million of the Company's common stock before September 30, 2016. On July 21, 2015, Microsemi Corporation's Board of Directors authorized a new stock repurchase program for the repurchase of up to an additional \$100.0 million of the Company's common stock before July 31, 2017. Repurchases under either authorization may be made in the open market or through privately negotiated transactions and may also be made under a Rule 10b5-1 plan. The number of shares to repurchase and the timing of such repurchases will be based on several factors, including the price of the Company's common stock, potential alternate and general market and business conditions. During the quarter ended July 3, 2016, the Company did not repurchase any shares under either program.

## ITEM 3. DEFAULTS UPON SENIOR SECURITIES

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Inapplicable.



ITEM 4. MINE SAFETY DISCLOSURES

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Inapplicable.

ITEM 5. OTHER INFORMATION

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Inapplicable.

ITEM 6. EXHIBITS

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Exhibit Number	Description
3.1	Amended and Restated Certificate of Incorporation of Microsemi Corporation (Incorporated by reference to Exhibit 3.1 to the Quarterly Report on Form 10-Q (filed by Microsemi Corporation on February 10, 2011))
3.2	Fourth Amended & Restated Bylaws of Microsemi Corporation (incorporated by reference to Exhibit 3.1 to the Current Report on Form 8-K filed by Microsemi Corporation on December 3, 2015)
10.1	Increase Term Joinder, dated as of June 29, 2016, among Microsemi Corporation, the incremental lenders party thereto and Morgan Stanley Senior Funding, Inc., as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed by Microsemi Corporation on June 30, 2016)
10.2	Amendment No. 1 to Credit Agreement, dated as of June 29, 2016, among Microsemi Corporation, the subsidiary guarantors party thereto, the lenders party thereto and Morgan Stanley Senior Funding, Inc., as administrative agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed by Microsemi Corporation on June 30, 2016)
31.1	Certification of Chief Executive Officer Pursuant to Securities Exchange Act Rules 13a-14(a) and 15d-14(a) as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, dated August 2, 2016†
31.2	Certification of Chief Financial Officer Pursuant to Securities Exchange Act Rules 13a-14(a) and 15d-14(a) as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, dated August 2, 2016†
32	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, dated August 2, 2016††
101	The following financial statements are from Microsemi Corporation's Quarterly Report on Form 10-Q for the quarter ended July 3, 2016, formatted in XBRL (eXtensible Business Reporting Language): (i) Unaudited Condensed Consolidated Balance Sheets; (ii) Unaudited Condensed Consolidated Statements of Operations and Comprehensive Income (Loss); (iii) Unaudited Condensed Consolidated Statements of Cash Flows; and (iv) Notes to Unaudited Condensed Consolidated Financial Statements†

† Filed with this Report.

†† Furnished with this Report.

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Signatures

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Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Microsemi Corporation

By /s/ John W. Hohener

John W. Hohener

Executive Vice President, Chief Financial Officer, Secretary and Treasurer

(Principal Financial and Accounting Officer and duly authorized to sign on behalf of the Registrant)

Dated: August 2, 2016

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Exhibit Index

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