SEMTECH CORP
Form 10-Q
November 30, 2016

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

FORM 10-Q

(Mark One)

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended October 30, 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 1-6395

SEMTECH CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	95-2119684
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

200 Flynn Road, Camarillo, California, 93012-8790
(Address of principal executive offices, Zip Code)

Registrant's telephone number, including area code: (805) 498-2111

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company)	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

Number of shares of Common Stock, $0.01 par value per share, outstanding at November 25, 2016: 65,636,833

SEMTECH CORPORATION
INDEX TO FORM 10-Q
FOR THE QUARTER ENDED OCTOBER 30, 2016

Unless the context otherwise requires, the use of the terms "Semtech," "the Company," "we," "us" and "our" in this Quarterly Report on Form 10-Q refers to Semtech Corporation and its consolidated subsidiaries.

Special Note Regarding Forward-Looking and Cautionary Statements

This Quarterly Report on Form 10-Q contains "forward-looking statements" within the meaning of the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995, as amended, based on our current expectations, estimates and projections about our operations, industry, financial condition, performance, results of operations, and liquidity. Forward-looking statements are statements other than historical information or statements of current condition and relate to matters such as future financial performance, future operational performance, the anticipated impact of specific items on future earnings, and our plans, objectives and expectations. Statements containing words such as "may," "believe," "anticipate," "expect," "intend," "plan," "project," "estimate," "should," "will," "designed to," "proj "business outlook," or other similar expressions constitute forward-looking statements. Forward-looking statements involve known and unknown risks and uncertainties that could cause actual results and events to differ materially from those projected.

Potential factors that could cause actual results to differ materially from those in the forward-looking statements include, but are not limited to:

- fluctuation in the Company's future results;
- downturns in the business cycle;
- reduced demand for the Company's products, including due to global economic conditions;
- business interruptions;
- the Company's reliance on a limited number of suppliers and subcontractors for components and materials;
- potentially insufficient liability insurance if the Company's products are found to be defective;
- obsolete inventories as a result of changes in demand and change in life cycles for the Company's products;
- the Company's inability to successfully develop and sell new products;
- lengthy and expensive product qualification processes without any assurance of product sales;
- the Company's products failing to meet industry standards;
- the Company's inability to protect intellectual property rights;
- the Company suffering losses if its products infringe the intellectual property rights of others;
- the Company's need to commit resources to product production prior to receipt of purchase commitments;
- increased business risk from foreign customers;
- the Company's foreign currency exposures;
- potential increased tax liabilities and effective tax rate if the Company needs to repatriate funds held by foreign subsidiaries;
- export restrictions and laws affecting the Company's trade and investments;
- competition against larger, more established entities;
- increased competition due to industry consolidation;
- the loss of any one of the Company's significant customers;
- volatility of customer demand;
- termination of a contract by a distributor;
- government regulations and other standards, including those that impose operational and reporting requirements;
- the Company's failure to comply with applicable environmental regulations;
- compliance with conflict minerals regulations;
- increase in the Company's cost of doing business as a result of having to comply with the codes of conduct of certain of the Company's customers and suppliers;

- changes in tax laws and review by taxing authorities;
- taxation of the Company in other jurisdictions;
- the Company’s failure to maintain effective internal control over financial reporting and disclosure controls and procedures;
- the Company’s limited experience with government contracting;
- potential government investigations and inquiries;
- loss of the Company’s key personnel;
- risks associated with companies the Company has acquired in the past and may acquire in the future and the Company’s ability to successfully integrate acquired businesses and benefit from expected synergies;
- the Company may be required to recognize additional impairment charges;
- the Company may be adversely affected by new accounting pronouncements;
- the Company’s ability to generate cash to service its debt obligations;
- restrictive covenants in the Company’s credit agreement which may restrict its ability to pursue its business strategies;
- the Company’s reliance on certain critical information systems for the operation of its business;
- costs associated with the Company’s indemnification of certain customers, distributors and other parties;
- the Company’s share price could be subject to extreme price fluctuations;
- the impact on the Company’s common stock price if securities or industry analysts do not publish reports about the Company’s business or adversely change their recommendations regarding the Company’s common stock;
- anti-takeover provisions in the Company’s organizational documents could make an acquisition of the Company more difficult;
- the Company is subject to litigation risks which may be costly to defend;
- the Company’s ability to realize expected benefits from the implementation of a new enterprise resource planning (“ERP”) system, and disruption of the Company’s operations caused by the adjustment to the new ERP system and the transition from the Company’s legacy systems and databases.

Additionally, forward-looking statements should be considered in conjunction with the cautionary statements contained in this Quarterly Report on Form 10-Q, including, without limitation, information under the captions “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and “Risk Factors” and additional factors that accompany the related forward-looking statements in this Quarterly Report on Form 10-Q, in our Annual Report on Form 10-K for the fiscal year ended January 31, 2016 including, without limitation information under the caption “Risk Factors”, in other filings with the Securities and Exchange Commission (“SEC”), and in material incorporated herein and therein by reference. In light of the significant risks and uncertainties inherent in the forward-looking information included herein that may cause actual performance and results to differ materially from those predicted, any such forward-looking information should not be regarded as representations or guarantees by the Company of future performance or results, or that its objectives or plans will be achieved, or that any of its operating expectations or financial forecasts will be realized. Reported results should not be considered an indication of future performance. Investors are cautioned not to place undue reliance on any forward-looking information contained herein, which reflect management’s analysis only as of the date hereof. Except as required by law, the Company assumes no obligation to publicly release the results of any update or revision to any forward-looking statement that may be made to reflect new information, events or circumstances after the date hereof or to reflect the occurrence of unanticipated or future events, or otherwise.

In addition to regarding forward-looking statements with caution, you should consider that the preparation of the consolidated financial statements requires us to draw conclusions and make interpretations, judgments, assumptions and estimates with respect to certain factual, legal, and accounting matters. Our financial statements might have been materially impacted if we had reached different conclusions or made different interpretations, judgments, assumptions or estimates.

PART I - FINANCIAL INFORMATION

ITEM 1. Financial Statements

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

	Three Months Ended		Nine Months Ended	
	October 30, 2016	October 25, 2015	October 30, 2016	October 25, 2015
Net sales	$137,185	$115,810	$404,241	$371,610
Cost of sales	56,120	46,226	162,877	148,050
Gross profit	81,065	69,584	241,364	223,560
Operating costs and expenses:				
Selling, general and administrative	35,116	30,747	101,654	102,383
Product development and engineering	25,600	26,855	77,097	84,771
Intangible amortization	6,286	6,308	19,017	18,648
Gain on disposition of business operations	(25,036)	—	(25,036)	—
Changes in the fair value of contingent earn-out obligations	—	(14,186)	(162)	(13,618)
Restructuring charge	—	962	—	4,526
Total operating costs and expenses	41,966	50,686	172,570	196,710
Operating income	39,099	18,898	68,794	26,850
Interest expense, net	(1,890)	(1,964)	(5,857)	(5,698)
Non-operating expense, net	(690)	(777)	(871)	(1,152)
Income before taxes	36,519	16,157	62,066	20,000
Provision for taxes	5,743	5,453	15,424	9,750
Net income	$30,776	$10,704	$46,642	$10,250
Earnings per share:				
Basic	$0.47	$0.16	$0.71	$0.16
Diluted	$0.46	$0.16	$0.71	$0.15
Weighted average number of shares used in computing earnings per share:				
Basic	65,549	65,117	65,331	65,920
Diluted	66,206	65,217	65,899	66,251

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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SEMTECH CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF
COMPREHENSIVE INCOME
(in thousands)
(unaudited)

	Three Months Ended		Nine Months Ended	
	October 30, 2016	October 25, 2015	October 30, 2016	October 25, 2015
Net income	$30,776	$ 10,704	$46,642	$ 10,250
Other comprehensive (loss) income:				
Foreign currency hedge:				
Unrealized (loss) gain on foreign currency cash flow hedges, net of tax	(422)	—	321	—
Adjustment for net gains realized and included in net income, net of tax	(88)	—	(546)	—
Interest rate hedge:				
Change in unrealized loss on interest rate cap, net of tax	—	—	—	(33)
Adjustment for net (loss) income realized and included in interest expense, net of tax	(37)	129	48	299
Benefit plans:				
Change in employee benefit plans, net of tax of $967 for the three and nine months ended October 30, 2016	(3,429)	—	(3,429)	—
Other changes to comprehensive income	129	—	129	—
Other comprehensive (loss) income, net of tax	(3,847)	129	(3,477)	266
Total comprehensive income	$26,929	$ 10,833	$43,165	$ 10,516

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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SEMTECH CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands, except share data)

	October 30, 2016 (unaudited)	January 31, 2016
Assets		
Current assets:		
Cash and cash equivalents	$297,939	$211,810
Accounts receivable, less allowances of $8,103 at October 30, 2016 and $7,793 at January 31, 2016	59,193	44,132
Inventories	62,679	63,875
Prepaid taxes	6,982	5,236
Other current assets	11,917	16,168
Total current assets	438,710	341,221
Non-current assets:		
Property, plant and equipment, net of accumulated depreciation of $156,549 at October 30, 2016 and $143,782 at January 31, 2016	95,547	101,006
Deferred tax assets	8,711	7,354
Goodwill	329,703	329,703
Other intangible assets, net	68,064	88,430
Other assets	60,314	43,803
TOTAL ASSETS	$1,001,049	$911,517
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$43,931	$35,486
Accrued liabilities	43,731	41,204
Deferred revenue	11,026	8,628
Current portion - long-term debt	19,094	18,569
Total current liabilities	117,782	103,887
Non-current liabilities:		
Deferred tax liabilities	22,462	6,802
Long term debt, less current portion	228,795	239,177
Other long-term liabilities	46,115	33,600
Stockholders' equity:		
Common stock, $0.01 par value, 250,000,000 shares authorized, 78,136,144 issued and 65,598,116 outstanding on October 30, 2016 and 78,136,144 issued and 64,998,368 outstanding on January 31, 2016	785	785
Treasury stock, at cost, 12,538,028 shares as of October 30, 2016 and 13,137,776 shares as of January 31, 2016	(256,138)	(266,175)
Additional paid-in capital	384,150	379,508
Retained earnings	459,922	413,280
Accumulated other comprehensive (loss) income	(2,824)	653
Total stockholders' equity	585,895	528,051
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$1,001,049	$911,517

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

SEMTECH CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(unaudited)

	Nine Months Ended					
	October 30, 2016			October 25, 2015		
Cash flows from operating activities:						
Net income	$	46,642		$	10,250	
Adjustments to reconcile net income to net cash provided by operating activities:						
Depreciation, amortization and impairments	35,506			36,534		
Accretion of deferred financing costs and debt discount	492			1,054		
Deferred income taxes	15,659			4,366		
Share-based compensation	21,198			13,398		
(Gain) loss on disposition of business operations and assets	(24,988		)	23		
Earn-out liabilities	(162		)	(13,618		)
Environmental reserve	(68		)	2,855		
Changes in assets and liabilities:						
Accounts receivable, net	(15,994		)	14,577		
Inventories	1,302			2,694		
Prepaid expenses and other assets	(11,785		)	5,975		
Accounts payable	6,775			677		
Accrued liabilities	8,885			(15,631		)
Deferred revenue	3,300			1,033		
Income taxes payable and prepaid taxes	(7,875		)	2,086		
Other liabilities	5,807			1,343		
Net cash provided by operating activities	84,694			67,616		
Cash flows from investing activities:						
Purchase of property, plant and equipment	(13,754		)	(10,705		)
Acquisitions, net of cash acquired	—			(44,432		)
	(3,248		)	(5,230		)

Purchases of other investments		
Proceeds from disposition of business operations	32,045	—
Proceeds from sale of equity investments	555	5,261
Net cash provided by (used in) investing activities	15,598	(55,106)
Cash flows from financing activities:		
Borrowings under line of credit	—	35,000
Payment for employee share-based compensation payroll taxes	(5,928)	(6,070)
Proceeds from exercises of stock options	1,678	3,965
Repurchase of outstanding common stock	(539)	(57,311)
Payment of long term debt	(9,374)	(26,063)
Net cash used in financing activities	(14,163)	(50,479)
Net increase (decrease) in cash and cash equivalents	86,129	(37,969)
Cash and cash equivalents at beginning of period	211,810	230,328
Cash and cash equivalents at end of period	$ 297,939	$ 192,359

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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SEMTECH CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
Note 1: Organization and Basis of Presentation
Nature of Business
Semtech Corporation (together with its subsidiaries, the “Company” or “Semtech”) is a global supplier of analog and mixed-signal semiconductor products. The end-customers for the Company’s products are primarily original equipment manufacturers (“OEM’s”) that produce and sell electronics.
The Company designs, develops and markets a wide range of products for commercial applications, the majority of which are sold into the enterprise computing, communications, high-end consumer and industrial end-markets.
Enterprise Computing: datacenters, passive optical networks, desktops, notebooks, servers, graphic boards, monitors, printers and other computer peripherals.
Communications: base stations, optical networks, carrier networks, switches and routers, cable modems, wireless LAN and other communication infrastructure equipment.
High-End Consumer: handheld products, smartphones, wireless charging, set-top boxes, digital televisions, tablets, digital video recorders and other consumer equipment.
Industrial: video broadcast equipment, automated meter reading, Internet of Things (“IoT”), smart grid, wireless charging, military and aerospace, medical, security systems, automotive, industrial and home automation, video security and surveillance and other industrial equipment.
Fiscal Year
The Company reports results on the basis of 52 and 53 week periods and ends its fiscal year on the last Sunday in January. The other quarters generally end on the last Sunday of April, July and October. All quarters consist of 13 weeks except for one 14-week period in the fourth quarter of 53-week years. The third quarter of fiscal years 2017 and 2016 each consisted of 13 weeks.
Principles of Consolidation
The accompanying interim unaudited condensed consolidated financial statements have been prepared by the Company, in accordance with accounting principles generally accepted in the United States (“GAAP”) for interim financial information and the instructions to quarterly report on Form 10-Q under the Securities Exchange Act of 1934, as amended, and Article 10 of Regulation S-X. In the opinion of the Company, these unaudited statements contain all adjustments (consisting of normal recurring adjustments) necessary to present fairly, in all material respects, the financial position of the Company for the interim periods presented. All significant intercompany balances have been eliminated. Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations, and the Company believes that the included disclosures are adequate to make the information presented not misleading. The Company evaluated all subsequent events through the date these interim unaudited condensed consolidated financial statements were issued.
On March 4, 2015, the Company completed the acquisition of Triune Systems, L.L.C. (“Triune”). On January 13, 2015, the Company completed the acquisition of selected assets from EnVerv, Inc. (“EnVerv”). The interim unaudited condensed consolidated financial statements include the results of income of Triune and EnVerv commencing as of the acquisition dates.
These interim unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the notes thereto included in the Company’s Annual Report on Form 10-K for the year ended January 31, 2016. The results reported in these interim unaudited condensed consolidated financial statements should not be regarded as indicative of results that may be expected for any subsequent period or for the entire year.
Segment Information
The Company’s Chief Executive Officer (“CEO”) has been identified as the Chief Operating Decision Maker (“CODM”) as defined by guidance regarding segment disclosures (see Note 14 for further discussion). In fiscal year 2016, the Company updated its assessment of its operations in light of its restructuring efforts (see Note 17 for further

discussion) and strategic business decisions. Based on this assessment, at that time the Company had identified five operating segments in total. Four of the operating segments aggregated into one reportable segment, the Semiconductor Products Group. The remaining operating segment, the Systems Innovation Group (shown as “All others”), could not be aggregated with the other operating segments and did not meet the criteria for a separate reportable segment as defined by the guidance regarding segment disclosure. As a result, the financial activity associated with the Systems Innovation Group was reported separately from the Company’s Semiconductor Products Group. This separate reporting was included in the “All others” category. On August 5, 2016, the Company completed its divestiture of its Snowbush Intellectual Property (“Snowbush IP”) business (previously part of the Company’s Systems Innovation Group) to Rambus Inc. (“Rambus”) for a purchase price of $32.0 million in cash along with the opportunity to receive additional payments from Rambus through 2022 based upon a percentage of sales by Rambus of new products expected to be developed by Rambus from the disposed assets. Beginning in the third quarter of fiscal year 2017, the Company no longer has a Systems Innovation Group or an “All others” category, and therefore has only four operating segments that aggregate into one reportable segment, the Semiconductor Products Group.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Derivatives and Hedging Activities

Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) 815, Derivatives and Hedging, provides the disclosure requirements for derivatives and hedging activities with the intent to provide users of financial statements with an enhanced understanding of: (a) how and why an entity uses derivative instruments, (b) how the entity accounts for derivative instruments and related hedged items, and (c) how derivative instruments and related hedged items affect an entity’s financial position, financial performance, and cash flows. Further, qualitative disclosures are required that explain the Company’s objectives and strategies for using derivatives, as well as quantitative disclosures about the fair value of and gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative instruments.

As required by ASC 815, the Company records all derivatives on the balance sheet at fair value. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative, whether the Company has elected to designate a derivative in a hedging relationship and apply hedge accounting and whether the hedging relationship has satisfied the criteria necessary to apply hedge accounting. Derivatives designated and qualifying as a hedge of the exposure to variability in expected future cash flows, or other types of forecasted transactions, are considered cash flow hedges. Hedge accounting generally provides for the matching of the timing of gain or loss recognition on the hedging instrument with the recognition of the changes in the fair value of the hedged asset or liability that are attributable to the hedged risk in a fair value hedge or the earnings effect of the hedged forecasted transactions in a cash flow hedge. The Company may enter into derivative contracts that are intended to economically hedge certain of its risk, even though hedge accounting does not apply or the Company elects not to apply hedge accounting.

In accordance with the FASB’s fair value measurement guidance, the Company made an accounting policy election to measure the credit risk of its derivative financial instruments that are subject to master netting agreements on a net basis by counterparty portfolio.

Recent Accounting Pronouncements

On August 26, 2016, the FASB issued Accounting Standards Update (“ASU”) 2016-15, “Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments.” The primary purpose of this ASU is to reduce the diversity in practice that has resulted from the lack of consistent principles on this topic. This ASU is effective for fiscal years beginning after December 15, 2017. This ASU will be effective for the Company as of the beginning of Fiscal 2019. Early adoption is permitted in any interim or annual period. The Company is in the process of determining the impact of the adoption of this guidance on its consolidated financial statements or notes thereto; however, it does not anticipate that the new guidance will have a significant impact on its consolidated financial statements.

In February 2016, FASB issued ASU No. 2016-02, Leases (Topic 842), which will require that substantially all leases be recognized by lessees on their balance sheet as a right-of-use asset and corresponding lease liability, including leases currently accounted for as operating leases. The new standard also will result in enhanced quantitative and qualitative disclosures, including significant judgments made by management, to provide greater insight into the extent of revenue and expense recognized and expected to be recognized from existing leases. The standard requires modified retrospective adoption and will be effective December 15, 2018, with early adoption permitted. The Company does not expect the adoption of this update to have a material impact on its consolidated financial statements.

In July 2015, the FASB issued ASU 2015-11, Inventory (Topic 330) Related to Simplifying the Measurement of Inventory which will apply to all inventory except inventory that is measured using last-in, first-out (“LIFO”) or the retail inventory method. Inventory measured using first-in, first-out or average cost is covered by the new amendments. Inventory within the scope of the new guidance should be measured at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. Subsequent measurement is unchanged for inventory measured using LIFO or the retail inventory method. The amendments will take effect for public business entities for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. The new guidance should be applied prospectively, and earlier application is permitted as of the beginning of an interim or annual reporting period. The Company is currently assessing the impact this update will have on its consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606), which will require an entity to recognize revenue from the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The guidance addresses, in particular, contracts with more than one performance obligation, as well as the accounting for some costs to obtain or fulfill a contract with a customer, and provides for additional disclosures with respect to revenues and cash flows arising from contracts with customers. Public entities are required to apply the amendments on either a full- or modified-retrospective basis for annual periods beginning after December 15, 2017 and for interim periods within those annual periods. This update will be effective for the Company beginning in the first quarter of fiscal year 2019. Early adoption is not permitted. The Company is currently assessing the basis of adoption and evaluating the impact of the adoption of the update on its consolidated financial statements.

Note 2: Acquisitions

Triune Systems, L.L.C

On March 4, 2015, the Company acquired Triune Systems, L.L.C., a privately-held supplier of isolated switching, wireless charging and power management platforms targeted at, among other things, high and low power, high efficiency applications. Under the terms of the purchase agreement, the Company acquired all of the outstanding equity interest in Triune for a guaranteed minimum purchase price of $45.0 million consisting of $35.0 million in cash paid at closing, with an additional cash consideration of $10.0 million of which $9.5 million was paid in September 2015 and $0.5 million was paid in the second quarter of fiscal year 2017. In March 2015, the Company borrowed $35.0 million under its prior revolving line of credit in connection with this acquisition (see Note 10 for discussion regarding Credit Facilities).

Subject to achieving certain future financial goals ("Triune Earn-out"), up to $70.0 million of contingent consideration will be paid over the next two years if certain net revenue targets are achieved in each of fiscal years 2017 and 2018. An additional payment of up to $16.0 million will be paid after fiscal year 2018 if certain cumulative net revenue and contribution margin targets are achieved.

The Triune Earn-out targets for fiscal year 2016 were not met and the Company does not expect the fiscal year 2017 or 2018 targets to be achieved. The fair value of the Triune Earn-out liability was zero as of October 30, 2016. See Notes 7 and 12.

The Triune business meets the definition of a business and is accounted for under the acquisition method of accounting in accordance with the FASB's ASC Topic 805, Business Combinations. The purchase price allocation for the Triune acquisition was finalized in the second quarter of fiscal year 2016. Total acquisition consideration has been allocated to the acquired tangible and intangible assets and assumed liabilities of Triune based on their respective estimated fair values as of the acquisition date. Acquisition-related transaction costs are not included as a component of consideration transferred, but are accounted for as an expense in the period in which the costs are incurred. Any excess of the acquisition consideration over the fair value of the assets acquired and liabilities assumed has been allocated to goodwill. The goodwill resulted from expected synergies from the transaction, including complementary products that will enhance the Company's overall product portfolio, and opportunities within new markets. The Company expects that all such goodwill will be deductible for tax purposes.

The Company's allocation of the total purchase price for Triune is summarized below:

(in thousands)	At March 4, 2015
Current assets	$877
Property, plant, and equipment, net	226
Core technologies	10,000
Customer relationships	2,000
Goodwill	49,384
Current liabilities	(1,287)
Earn-out liability	(16,200)
Total acquisition consideration	$45,000

Triune's technology complemented the portfolio of products offered in the Company's legacy Power and High-Reliability reporting unit. The Company concluded that the Triune and legacy Power and High-Reliability components should be aggregated and deemed a single reporting unit after considering similarities among different economic characteristics such as concentration of key customers, unit selling price decreases, increased competitors due to market expansion and chain of command of the newly acquired business.

Net revenues and earnings attributable to Triune since the acquisition date have not been material. Pro forma results of operations have not been presented as Triune’s annual operating results are not material to the Company’s unaudited condensed consolidated financial statements.

EnVerv, Inc.

On January 13, 2015, the Company paid $4.9 million to acquire selected assets from EnVerv, Inc., a privately-held supplier of power line communications and Smart Grid solutions targeted at advanced metering infrastructure, home energy management systems and IoT applications. The Company has concluded that the acquired assets constituted a business and accordingly accounted for this transaction as a business combination.

The purchase price allocation for the EnVerv acquisition was finalized in the first quarter of fiscal year 2016. Total acquisition consideration has been allocated to the acquired tangible and intangible assets and assumed liabilities based on their respective estimated fair values as of the acquisition date. The excess of the acquisition consideration over the fair value of assets acquired and liabilities assumed has been allocated to goodwill. As of January 25, 2015, $1.4 million of the total acquisition consideration has been allocated to core technologies and $3.4 million has been allocated to goodwill. The remaining balance has been allocated to acquired tangible assets and assumed liabilities. The Company expects that all such goodwill will be deductible for tax purposes.

Net revenues and earnings attributable to EnVerv since the acquisition date have not been material. Pro forma results of operations have not been presented as EnVerv's annual operating results are not material to the Company's unaudited condensed consolidated financial statements.

Note 3: Earnings per Share

The computation of basic and diluted earnings per common share is as follows:

(in thousands, except per share amounts)	Three Months Ended		Nine Months Ended	
	October 30, 2016	October 25, 2015	October 30, 2016	October 25, 2015
Net income	$30,776	$ 10,704	$46,642	$ 10,250
Weighted average common shares outstanding - basic	65,549	65,117	65,331	65,920
Dilutive effect of options and restricted stock units	657	100	568	331
Weighted average common shares outstanding - diluted	66,206	65,217	65,899	66,251
Basic earnings per common share	$0.47	$ 0.16	$0.71	$ 0.16
Diluted earnings per common share	$0.46	$ 0.16	$0.71	$ 0.15
Anti-dilutive shares not included in the above calculations	989	3,728	1,498	2,392

Basic earnings per common share is computed by dividing net income available to common stockholders by the weighted-average number of shares of common stock outstanding during the reporting period. Diluted earnings per common share incorporate the incremental shares issuable, calculated using the treasury stock method, upon the assumed exercise of stock options and the vesting of restricted stock.

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Note 4: Revenue Recognition

The Company recognizes product revenue when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable and collectability is probable. Recovery of costs associated with product design and engineering services are recognized during the period in which services are performed. The product design and engineering recovery, when recognized, will be reported as a reduction to product development and engineering expense. Historically, these recoveries have not exceeded the cost of the related development efforts.

The Company includes revenue related to technology licenses as part of "Net sales." Historically, revenue from these arrangements has not been significant though it is part of the Company's recurring ordinary business.

The Company defers revenue recognition on shipment of products to certain customers, principally distributors, under agreements which provide for limited pricing credits or return privileges, until these products are sold through to end users or the return privileges lapse. For sales subject to certain pricing credits or return privileges, the amount of future pricing credits or inventory returns cannot be reasonably estimated given the relatively long period in which a particular product may be held by the customer. Therefore, the Company has concluded that sales to customers under these agreements are not fixed and determinable at the date of the sale and revenue recognition has been deferred. The Company estimates the deferred gross margin on these sales by applying an average gross profit margin to the actual gross sales. The average gross profit margin is calculated for each category of material using standard costs which is expected to approximate actual costs at the date of sale. The estimated deferred gross margins on these sales, where there are no outstanding receivables, are recorded on the condensed consolidated balance sheets under the heading of "Deferred revenue."

The Company records a provision for estimated sales returns in the same period as the related revenues are recorded. The Company bases these estimates on historical sales returns and other known factors. Actual returns could be different from Company estimates and current provisions for sales returns and allowances, resulting in future charges to earnings. There were no significant impairments of deferred cost of sales in the third quarters of fiscal years 2017 or 2016.

The Company records a provision for sales rebates in the same period as the related revenues are recorded. These estimates are based on sales activity during the period. Actual rebates given could be different from our estimates and current provisions for sales rebates, resulting in future charges to earnings. The estimated sales rebates for sales activity during the period where there are no outstanding receivables are recorded on the condensed consolidated balance sheets under the heading of "Accrued liabilities." The portion of the estimated sales rebate where there are outstanding receivables is recorded on the balance sheet as a reduction to accounts receivable.

Note 5: Share-Based Compensation

Financial Statement Effects and Presentation. The following table summarizes pre-tax, share-based compensation included in the unaudited condensed consolidated statements of income for the three and nine months ended October 30, 2016 and October 25, 2015.

(in thousands)	Three Months Ended		Nine Months Ended	
	October 30, 2016	October 25, 2015	October 30, 2016	October 25, 2015
Revenue offset	$3,669	$ —	$3,669	$ —
Cost of sales	360	197	1,108	1,071
Selling, general and administrative	3,965	2,933	12,001	6,006
Product development and engineering	1,401	1,987	4,420	6,320
Share-based compensation	$9,395	$ 5,117	$21,198	$ 13,397
Net change in share-based compensation capitalized into inventory	$124	$ (233)	$106	$ 45

Grant Date Fair Values and Underlying Assumptions: Contractual Terms

The Company uses the Black-Scholes pricing model to value stock options. The estimated fair value of restricted stock units, for which vesting is not linked to a market condition, is calculated based on the market price of the Company’s common stock on the date of grant. For restricted stock units that vest according to a market condition, the Company uses a Monte Carlo simulation model to value the award.

Some of the restricted stock units granted in the first nine months of fiscal year 2017 and prior years are classified as liabilities rather than equity. For grants classified as equity, share-based compensation is measured at the grant date, based on the fair value of the award, and is recognized as an expense over the grantee’s requisite service period. For grants classified as liabilities, share-based compensation is measured at fair value at the end of each reporting period until the date of settlement, and is recognized as an expense over the grantee’s requisite service period. Expected volatilities are based on historical volatility using daily and monthly stock price observations.

The following table summarizes the assumptions used in the Black-Scholes model to determine the fair value of stock options granted in the three and nine months ended October 30, 2016 and October 25, 2015, respectively:

	Three Months Ended		Nine Months Ended	
	October 30, 2016	October 25, 2015	October 30, 2016	October 25, 2015
Expected lives, in years	4.2	4.2	4.1 - 4.5	4.2 - 4.3
Estimated volatility	32%	32%	32%	29% - 32%
Dividend yield	—	—	—	—
Risk-free interest rate	1.0%	1.3%	1.1% - 1.3%	1.24% - 1.29%
Weighted average fair value on grant date	$7.10	$4.80	$5.67	$6.09

Stock Options. The Company has historically granted stock options to both employees and non-employee directors. The fair values of these grants were measured on the grant date. The grant dates for these awards are equal to the measurement date. These awards are valued as of the measurement date and recognized as an expense over the requisite vesting period (typically 3-4 years).

The following table summarizes the activity for stock options for the nine months ended October 30, 2016:

(in thousands, except for per share amounts)	Number of Shares	Weighted Average Exercise Price (per share)	Aggregate Intrinsic Value	Aggregate Unrecognized Compensation	Number of Shares Exercisable	Weighted Average Contractual Term (in years)
Balance at January 31, 2016	1,507	$ 25.18	$ 962	$ 3,748	775	
Options granted	356	20.58				
Options exercised	(86)	19.17	482			
Options cancelled/forfeited	(95)	22.10				
Balance at October 30, 2016	1,682	$ 24.69	$ 3,419	$ 3,796	902	
Exercisable at October 30, 2016	902	$ 26.30	$ 873			2.3

Performance-Based Restricted Stock Units. The Company grants performance-based restricted stock units to select employees. These awards have a performance condition in addition to a service condition. The performance metrics are determined based on a pre-defined cumulative three-year performance of the Company’s net revenue and non-GAAP operating income measured against internal goals. The performance award which is granted in any fiscal year will be tied to the Company’s performance of that fiscal year and the succeeding two fiscal years. The performance award recipients must be employed for the entire three-year period, which is the explicit service and requisite service period, and be an active employee at the time of vesting of the awards (cliff vesting at the end of the third year). Under the terms of these awards, assuming the highest performance level of 200% with no cancellations due to forfeitures, the maximum number of shares that can be earned would be 582,032 shares and an additional 582,032 shares would be settled in cash. The Company would have a liability accrued under “Other liabilities” within the condensed consolidated balance sheets equal to the value of 582,032 shares on the settlement date, which would be settled in cash. Only cash performance-based restricted stock unit awards are classified as liabilities and the value of these awards is re-measured at each reporting date. At October 30, 2016, the performance metrics associated with the outstanding awards issued in fiscal years 2017 and 2016 are expected to be met at a level which would result in a grant at 190% and 0% of target, respectively.

In the first quarter of fiscal year 2016, the Company granted performance-based vesting restricted stock units to select employees as part of the EnVerv acquisition. These awards have a performance condition in addition to a service condition. The performance metrics are determined based on a pre-defined net revenue target. In addition to the performance vesting condition, these awards have a requisite four year vesting term (which is also the requisite vesting period) whereby 25% will vest, subject to attainment of the performance condition, on each anniversary of the grant date. Under the terms of these awards, assuming the highest performance level of 100% with no cancellations due to forfeitures, the maximum number of shares that can be earned would be 24,000. At October 30, 2016, the performance metrics associated with the outstanding awards issued in fiscal year 2016 are not expected to be met which would result in none of the shares being issued.

The performance-based restricted stock units are valued as of the measurement date and expense is recognized on a straight line basis for the awards expected to vest based on the probability of attainment of the performance condition for each separately vesting portion of the award.

The following table summarizes the activity for performance-based restricted stock units for the nine months ended October 30, 2016:

(in thousands, except for per unit amounts)	Total Units	Subject to Share Settlement Units	Subject to Cash Settlement Units	Recorded Liability	Weighted Average Grant Date Fair Value (per unit)	Aggregate Unrecognized Compensation	Weighted Average Period Over Which Expected to be Recognized (in years)
Balance at January 31, 2016	384	203	181	$ 237	$ 26.57	$ 1,925	1.5
Performance-based units granted	231	116	115		17.51		
Performance-based units vested	—	—	—		—		
Performance-based units cancelled/forfeited	(12)	(6)	(6)		17.51		
Change in liability				621			
Balance at October 30, 2016	603	313	290	$ 858	$ 23.29	$ 7,989	1.3

Changes in the liability associated with performance-based restricted stock units, which is recorded in "Other long-term liabilities" within the condensed consolidated balance sheets, is due to changes in proportionate vesting and estimated forfeitures, re-measurement adjustments related to changes in market value and changes in the expected performance results.

Market Performance Restricted Stock Units. On February 26, 2014, the Company granted its CEO restricted stock units with a market performance condition. The award is eligible to vest during the period commencing February 26, 2014 and ending February 26, 2019 (the "Performance Period") as follows: 30% of the restricted stock units covered by the award will vest if, during any consecutive 120 calendar day period that commences and ends during the Performance Period, the average per-share closing price of the Company's common stock equals or exceeds $35.00 ("Tranche 1") and the award will vest in full if, during any consecutive 120 calendar day period that commences and ends during the Performance Period, the average per-share closing price of the Company's common stock equals or exceeds $40.00 ("Tranche 2"). The award will also vest if a majority change in control of the Company occurs during the Performance Period and, in connection with such event, the Company's stockholders become entitled to receive per-share consideration having a value equal to or greater than $40.00. The fair value of the awards was determined to be $17.26 and $14.88 for Tranche 1 and Tranche 2, respectively, on the grant date by application of the Monte Carlo simulation model.
The following table summarizes the activity for market performance restricted stock units for the nine months ended October 30, 2016:

(in thousands, except for per unit amounts)	Total Units	Weighted Average Grant Date Fair Value (per unit)	Aggregate Unrecognized Compensation	Period Over Which Expected to be Recognized (in years)
Balance at January 31, 2016	220	$ 15.59	$ 143	0.1
Market performance units granted	—	—		
Market performance units vested	—	—		
Market performance units cancelled/forfeited	—	—		
Balance at October 30, 2016	220	$ 15.59	$ —	0.0

Restricted Stock Units, Employees. The Company grants restricted stock units to employees which are expected to be settled with stock. The grant date for these awards is equal to the measurement date. These awards are valued as of the measurement date and recognized as an expense over the requisite vesting period (typically 4 years).

The following table summarizes the employees' restricted stock unit activity for the nine months ended October 30, 2016:

(in thousands, except for per unit amounts)	Number of Units	Weighted Average Grant Date Fair Value (per unit)	Aggregate Intrinsic Value (1)	Aggregate Unrecognized Compensation	Weighted Average Period Over Which Expected to be Recognized (in years)
Balance at January 31, 2016	2,032	$ 23.70		$ 35,692	2.4
Restricted stock units granted	1,147	21.76			
Restricted stock units vested	(714)	25.28	$ 16,134		
Restricted stock units forfeited	(270)	20.77			
Balance at October 30, 2016	2,195	$ 22.53		$ 41,348	2.6

(1) Reflects the value of Semtech Corporation stock on the date that the restricted stock unit vested.

Restricted Stock Units, Cash Settled, Non-Employee Directors. The Company maintains a compensation program pursuant to which restricted stock units are granted to the Company's directors that are not employed by the Company or any of its subsidiaries. In June 2015, the Company changed its director compensation program so that a portion of the restricted stock units granted under the program would be settled in cash and a portion would be settled in stock. Restricted stock units awarded under the program are scheduled to vest on the earlier of (i) one year after the grant date or (ii) the day immediately preceding the annual meeting of shareholders in the year following the grant. The portion of a restricted stock unit award under the program that is to be settled in cash will, subject to vesting, be settled when the director who received the award separates from the board of directors. The portion of a restricted stock unit award under the program that is to be settled in stock will, subject to vesting, be settled promptly following vesting. There were no changes to the terms and conditions of the existing awards.

The restricted stock units that are to be settled in cash are accounted for as liabilities. Because these awards are not typically settled until a non-employee director's separation from service, the value of these awards is re-measured at the end of each reporting period until settlement. The following table summarizes the non-employee directors' activity for restricted stock units settled in cash for the nine months ended October 30, 2016:

(in thousands, except for per unit amounts)	Number of Units	Recorded Liability	Weighted Average Grant Date Fair Value (per unit)	Aggregate Unrecognized Compensation	Period Over Which Expected to be Recognized (in years)
Balance at January 31, 2016	28	$ 3,870	$ 19.70	$ 221	0.4
Restricted stock units granted	25		23.40		
Restricted stock units vested	(30)		19.65		
Restricted stock units forfeited	—		—		
Change in liability		502			
Balance at October 30, 2016	23	$ 4,372	$ 23.67	$ 403	0.6

As of October 30, 2016, the total number of vested but unsettled restricted stock units for non-employee directors is 173,657 units. As of October 30, 2016, $4.4 million of the liability associated with these awards is included in "Other long-term liabilities" within the condensed consolidated balance sheets.

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Restricted Stock Units, Stock Settled, Non-Employee Directors. As a result of the June 2015 changes to the Company’s director compensation program, beginning in July 2015, the Company began granting new restricted stock units to non-employee directors which are expected to be settled with stock at the time of vesting. The grant date for these awards is equal to the measurement date. These awards are valued as of the measurement date and recognized as an expense over the requisite vesting period (typically one year).
The following table summarizes the non-employee directors’ activity for restricted stock units settled with stock for the nine months ended October 30, 2016:

(in thousands, except for per unit amounts)	Number of Units	Weighted Average Grant Date Fair Value (per unit)	Aggregate Intrinsic Value (1)	Aggregate Unrecognized Compensation	Period Over Which Expected to be Recognized (in years)
Balance at January 31, 2016	24	$ 19.70		$ 186	0.4
Restricted stock units granted	21	23.40			
Restricted stock units vested	(25)	24.16	$ 616		
Restricted stock units forfeited	—	—			
Balance at October 30, 2016	20	$ 23.67		$ 312	0.6

(1) Reflects the value of Semtech Corporation stock on the date that the restricted stock unit vested.

Modification of Awards
On December 19, 2014 and August 17, 2015, the Company modified the equity awards of certain executive officers by providing for the acceleration of vesting upon termination of their employment in certain circumstances in connection with a change in control of the Company. These modifications impacted the stock awards of 12 executive employees and resulted in no incremental compensation cost for the fiscal year ended January 31, 2016 or the three or nine month periods ended October 30, 2016 and October 25, 2015.

Warrant. On October 5, 2016 the Company issued a warrant (the “Warrant”) to Comcast Cable Communications Management LLC (“Comcast”) to purchase up to 1,086,957 shares (the “Warrant Shares”) of the Company’s common stock, par value $0.01 per share, representing a total of $30.0 million worth of common stock based on the average closing price over the 10-trading day period ending October 4, 2016, at an exercise price of $0.01 per Warrant Share. The Warrant provides for net share settlement that, if elected by Comcast, will reduce the number of Warrant Shares issued upon exercise to reflect net settlement of the exercise price. Comcast may also request cash settlement of the Warrant upon exercise in lieu of the issuance of Warrant Shares; however, such cash settlement is at the sole and absolute discretion of the Company. The Warrant vested 10% on its issuance, and the remainder vests based on the achievement during the subsequent 30-month period (“Milestone Period”) by Comcast (or its designee) of certain milestones related to the deployment of a LoRaWAN™-based network in cities around the country. The number of Warrant Shares are subject to customary adjustment provisions for stock split, reclassification, reorganization, consolidation, merger, and similar transactions. The Warrant has a term of seven years from October 5, 2016.

The Warrant was issued by the Company to Comcast in connection with an agreement between the parties regarding the intended trial deployment by Comcast of a low-power wide-area Network (LPWAN) in the United States, based on the Company’s LoRa® Wireless Radio Frequency Technology.

The Warrant is accounted for as equity. The cost of the Warrant is recognized as an offset to net sales over the respective performance period. The Warrant consists of five performance tranches. The cost associated with each tranche is recognized based on the fair value at each reporting date until vesting which is the measurement date.

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The following table summarizes the underlying Warrant Shares issued to Comcast for the nine months ended October 30, 2016:

(in thousands, except for per Warrant Share amounts)	Number of Warrant Shares	Weighted Average Grant Date Fair Value (per Warrant Share)	Aggregate Intrinsic Value (1)	Aggregate Unrecognized Expense
Balance at January 31, 2016	—	$ —	—	$ —
Warrant shares granted	1,087	27.74		
Warrant shares vested	(109)	27.74	$ 3,015	
Change in value	—	—		23,674
Balance at October 30, 2016	978	$ 27.74		$ 23,674

(1) Reflects the value of Semtech Corporation Warrant Shares on the date the Warrant Shares vested.

Given the nominal exercise price of the Warrant Shares, the Company valued the awards using the closing price of the Company’s stock on the measurement date for shares that have vested and the fair value on the condensed consolidated balance sheets date for the other shares. As of October 30, 2016, no part of the Warrant has been exercised, and the Warrant has an estimated life of seven years.

Note 6: Investments

Investments that have original maturities of three months or less are accounted for as cash equivalents. This includes money market funds, time deposits and United States ("U.S.") government obligations. Temporary and long-term investments consist of government, bank and corporate obligations, with original maturity dates in excess of three months. Temporary investments have original maturities in excess of three months, but mature within twelve months of the balance sheet date. Long-term investments have original maturities in excess of twelve months. The Company determines the cost of securities sold based on the specific identification method. Realized gains or losses are reported in "Non-operating expense, net" within the unaudited condensed consolidated statements of income.

The Company classifies its investments as "available-for-sale" because it may sell some securities prior to maturity. The Company's investments are subject to market risk, primarily interest rate and credit risks. The Company's investments are managed by a limited number of outside professional managers that operate within investment guidelines set by the Company. These guidelines include specified permissible investments, minimum credit quality ratings and maximum average duration restrictions and are intended to limit market risk by restricting the Company's investments to high quality debt instruments with relatively short-term maturities.

As of October 30, 2016, the Company did not have any long-term investments.

The following table summarizes the Company's available-for-sale investments:

	October 30, 2016			January 31, 2016		
(in thousands)	Market Value	Adjusted Cost	Gross Unrealized Gain	Market Value	Adjusted Cost	Gross Unrealized Gain
Cash equivalents	$16,908	$16,908	$ —	$16,866	$16,866	$ —
Total investments	$16,908	$16,908	$ —	$16,866	$16,866	$ —

The following table summarizes the maturities of the Company's available-for-sale investments:

	October 30, 2016		January 31, 2016	
(in thousands)	Market Value	Adjusted Cost	Market Value	Adjusted Cost
Within 1 year	$16,908	$ 16,908	$16,866	$ 16,866
After 1 year through 5 years	—	—	—	—
Total investments	$16,908	$ 16,908	$16,866	$ 16,866

Unrealized gains and losses are the result of fluctuations in the market value of the Company's available-for-sale investments and are included in "Accumulated other comprehensive income" within the condensed consolidated balance sheets. The following table summarizes net unrealized losses arising in the periods presented in addition to the tax associated with these comprehensive income items:

	Three Months Ended		Nine Months Ended	
(in thousands)	October 30, 2016	October 25, 2015	October 30, 2016	October 25, 2015
Unrealized gain (loss), net of tax	$ —	$ 129	$(85)	$ 266
Increase to deferred tax liability	—	74	—	172

The Company did not generate any significant interest income in the three or nine month periods ended October 30, 2016 and October 25, 2015.

Equity and Cost Method Investments

The Company accounts for its equity investments under the cost method of accounting when it does not have the ability to exercise significant influence over the investees. For investments where the Company has the ability to exercise significant influence, it uses the equity method of accounting. The Company's total equity and cost method investments were $22.2 million and $20.2 million as of October 30, 2016 and January 31, 2016. All of these investments are in private companies and are included in "Other assets" within the condensed consolidated balance sheets.

The Company has the following investments which are accounted for as cost method investments:

Entity Name	Investment Value

(in thousands)	October 30, 2016	January 31, 2016
MultiPhy Ltd.	$14,000	$ 12,000
Skorpios Technologies Inc.	3,000	3,000
Guangdong Dapu Telecom Technology Co., Ltd.	3,300	3,300
Senet, Inc.	1,900	1,900
Jariet Technologies Inc.	—	—
Total	$22,200	$ 20,200

The Company evaluated its cost method investments for indicators of impairment at October 30, 2016. The Company did not identify any events or changes in circumstances that may have a significant adverse effect on the fair value of the investments and as a result did not estimate the fair value of its investments.

On January 11, 2016, the Company announced that it had entered into a strategic agreement to accelerate the introduction of a 100Gbps single wavelength optical module solution. As part of this agreement, the Company made an investment under which the Company acquired preferred stock and a call option that is exercisable through June 30, 2018, that would allow the Company to purchase all of the outstanding equity of MultiPhy Ltd. (“MultiPhy”) at a fixed price. The Company does not expect to exercise this option within the next twelve months.

Note 7: Fair Value Measurements

Instruments Measured at Fair Value on a Recurring Basis

Financial assets and liabilities measured and recorded at fair value on a recurring basis were presented within the Company’s condensed consolidated balance sheets as follows:

	Fair Value as of October 30, 2016				Fair Value as of January 31, 2016			
(in thousands)	Total	(Level 1)	(Level 2)	(Level 3)	Total	(Level 1)	(Level 2)	(Level 3)
Financial assets:								
Cash equivalents	$16,908	$16,908	$—	$—	$16,866	$16,866	$ —	$—
Derivative financial instruments	215	—	215	—	—	—	—	—
Total financial assets	$17,123	$16,908	$215	$—	$16,866	$16,866	$ —	$—
Financial liabilities:								
Triune Earn-out	$—	$—	$—	$—	$—	$—	$ —	$—
Cycleo Earn-out	1,295	—	—	1,295	1,457	—	—	1,457
Derivative financial instruments	445	—	445	—	—	—	—	—
Total financial liabilities	$1,740	$—	$445	$1,295	$1,457	$—	$ —	$1,457

During the nine months ended October 30, 2016, the Company had no transfers of financial assets or liabilities between Level 1, Level 2 or Level 3. As of October 30, 2016 and January 31, 2016, the Company had not elected the fair value option for any financial assets and liabilities for which such an election would have been permitted.

The Company’s available-for-sale securities consist primarily of money market accounts that do not have a stated maturity date.

The fair values of the foreign exchange forward contracts are valued using Level 2 inputs. Foreign currency forward contracts are valued using readily available foreign currency forward and interest rate curves. The fair value of each contract is determined by comparing the contract rate to the forward rate and discounting to the present value. Contracts in a gain position are recorded in the condensed consolidated balance sheets under the caption “Other current assets” and the value of contracts in a loss position are recorded under the caption “Accrued liabilities” within the condensed consolidated balance sheets. Please see Note 19 for further discussion of the Company’s derivative instruments.

The Triune Earn-out liability is valued utilizing estimates of annual revenue and operating income (Level 3 inputs) during a period of approximately two-years ending January 2018. These estimates represent inputs for which market data are not available and are developed using the best information available about the assumptions that market participants would use when pricing the liability.

The Cycleo Earn-out liability (see “Earn-out Liability” in Note 12) is valued utilizing estimates of annual revenue and operating income (Level 3 inputs) during a four-year period ending April 2020. These estimates represent inputs for which market data are not available and are developed using the best information available about the assumptions that market participants would use when pricing the liability.

The Company measures contingent earn-out liabilities at fair value on a recurring basis using significant unobservable inputs classified within Level 3 of the fair value hierarchy. The Company uses a Monte Carlo valuation method as a valuation technique to determine the value of the earn-out liability. The significant unobservable inputs used in the fair value measurements are revenue projections over the earn-out period, and the probability outcome percentages assigned to each scenario. Significant increases or decreases to either of these inputs in isolation would result in a significantly higher or lower liability, with a higher liability capped by the contractual maximum of the contingent earn-out obligation. Ultimately, the liability will be equivalent to the amount paid, and the difference between the fair value estimate and amount paid will be recorded in earnings. For both the Triune Earn-out and Cycleo Earn-out, these companies have business profiles comparable to a start-up company. Accordingly, their respective revenue projections are subject to significant revisions. This characteristic has resulted in volatile changes to the measurement of fair value of the Triune Earn-out since the time of the Triune acquisition.

The Company reviews and re-assesses the estimated fair value of contingent consideration on a quarterly basis, and the updated fair value could differ materially from the previous estimates. Changes in the estimated fair value of the Company's contingent earn-out liabilities related to the time component of the present value calculation are reported in "Interest expense" within the unaudited condensed consolidated statements of income. Adjustments to the estimated fair value related to changes in all other unobservable inputs are reported in operating income.

A reconciliation of the change in the earn-out liability during the nine months ended October 30, 2016 is as follows:

(in thousands)	Cycleo	Triune	Total
Balance at January 31, 2016	$1,457	$ —	$1,457
Changes in the fair value of contingent earn-out obligations	(162)	—	(162)
Balance as of October 30, 2016	$1,295	$ —	$1,295

Instruments Not Recorded at Fair Value on a Recurring Basis

Some of the Company’s financial instruments are not measured at fair value on a recurring basis but are recorded at amounts that approximate fair value due to their liquid or short-term nature. Such financial assets and financial liabilities include: cash and cash equivalents, net receivables, certain other assets, accounts payable, accrued expenses, accrued personnel costs, and other current liabilities.

The Company’s long-term debt is not recorded at fair value on a recurring basis, but is measured at fair value for disclosure purposes. The fair value of the Company’s Term Loans (as defined in Note 10) is $67.8 million and $77.1 million and Revolving Commitments (as defined in Note 10) is $181.0 million as of both October 30, 2016 and January 31, 2016, respectively. These are based on Level 2 inputs which are derived from transactions with similar amounts, maturities, credit ratings and payment terms.

Assets and Liabilities Recorded at Fair Value on a Non-Recurring Basis

The Company reduces the carrying amounts of its goodwill, intangible assets, long-lived assets and non-marketable equity securities to fair value when held for sale or determined to be impaired.

For its investment in equity interests, the Company has not identified events or changes in circumstances that may have a significant adverse effect on the fair value of its equity investments during the first nine months of fiscal year 2017.

Note 8: Inventories

Inventories, consisting of material, material overhead, labor, and manufacturing overhead, are stated at the lower of cost (first-in, first-out) or market and consist of the following:

(in thousands)	October 30, 2016	January 31, 2016
Raw materials	$ 3,342	$ 2,094
Work in progress	40,731	40,940
Finished goods	18,606	20,841
Inventories	$ 62,679	$ 63,875

Note 9: Goodwill and Intangible Assets

Goodwill – Changes in the carrying amount of goodwill were as follows:

(in thousands)	Signal Integrity	Power and High Reliability	Wireless and Sensing	Total
Balance at January 31, 2016	$261,891	$ 49,384	$18,428	$329,703
Additions	—	—	—	—
Balance at October 30, 2016	$261,891	$ 49,384	$18,428	$329,703

Goodwill is not amortized, but is tested for impairment using a two-step method on an annual basis and whenever events or changes in circumstances indicate that the carrying value may not be recoverable. The recoverability of goodwill is measured at the reporting unit level by comparing the reporting unit's carrying amount, including goodwill, to the fair market value of the reporting unit.

Goodwill is allocated to three reporting units (Signal Integrity, Power and High Reliability and Wireless and Sensing) (see Note 14). The difference between the fair value and the carrying amount of these reporting units is one of several factors the Company will consider before reaching its conclusion about whether to perform the first step of the goodwill impairment test.

Goodwill was tested for impairment as of November 30, 2015, the date of the Company's annual impairment review, at the reporting unit level for Signal Integrity, Power and High Reliability and Wireless and Sensing. The Company estimated the fair values using an income approach, as well as other generally accepted valuation methodologies. The cash flows for each reporting unit were based on discrete financial forecasts developed by management for planning purposes. Cash flows beyond the discrete forecasts were estimated using a terminal value calculation, which incorporated historical and forecasted financial trends for each identified reporting unit and considered perpetual earnings growth rates for publicly traded peer companies.

Goodwill is measured at fair value on a non-recurring basis. That is, goodwill is not measured at fair value on an ongoing basis, but is subject to fair value adjustments using Level 3 inputs in certain circumstances (e.g., when there is evidence of impairment). At October 30, 2016, the Company concluded that there were no indicators of such impairment.

Purchased Intangibles – The following table sets forth the Company's finite-lived intangible assets resulting from business acquisitions and technology licenses purchased, which continue to be amortized:

		October 30, 2016			January 31, 2016		
(in thousands)	Estimated Useful Life	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Core technologies	5-8 years	$144,930	$(87,753)	$ 57,177	$148,210	$ (74,006)	$ 74,204
Customer relationships	5-10 years	30,030	(19,147)	10,883	30,030	(15,847)	14,183
Technology licenses (1)	2 years	100	(96)	4	100	(57)	43
Other intangibles assets	1-5 years	6,600	(6,600)	—	6,600	(6,600)	—
Total finite-lived intangible assets		$181,660	$(113,596)	$ 68,064	$184,940	$ (96,510)	$ 88,430

(1) Technology licenses relate to end-license agreements for intellectual property that is used by the Company in research and development activities and also has alternative future uses. Amortization expense related to technology licenses is reported as "Product development and engineering" within the unaudited condensed consolidated statements of income.

For the three months ended October 30, 2016 and October 25, 2015, amortization expense related to acquired finite-lived intangible assets was $6.3 million and $6.3 million, respectively. For the nine months ended October 30, 2016 and October 25, 2015, amortization expense related to acquired finite-lived intangible assets was $19.0 million and $18.6 million, respectively. Amortization expense related to acquired finite-lived intangible assets is reported as "Intangible amortization" within the unaudited condensed consolidated statements of income.

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The estimated annual amount of future amortization expense for all finite-lived intangible assets will be as follows:
(in thousands)

To be recognized in:	Core Technologies	Customer Relationships	Technology Licenses	Total
Remaining three months of fiscal year 2017	$ 5,188	$ 1,100	$ 4	$6,292
Fiscal year 2018	20,744	4,400	—	25,144
Fiscal year 2019	17,332	4,400	—	21,732
Fiscal year 2020	9,905	950	—	10,855
Fiscal year 2021	3,056	33	—	3,089
Thereafter	952	—	—	952
Total expected amortization expense	$ 57,177	$ 10,883	$ 4	$68,064

As of October 30, 2016, the Company had no intangible assets classified as having an indefinite life.

Note 10: Credit Facilities

On May 2, 2013, Semtech Corporation, with each of its domestic subsidiaries as guarantors (the “Prior Guarantors”), entered into a credit agreement (the “Prior Credit Agreement”) with the lenders referred to therein (the “Prior Lenders”) and HSBC Bank USA, National Association, as administrative agent and as swing line lender and letter of credit issuer. In accordance with the Prior Credit Agreement, the Prior Lenders provided Semtech Corporation with senior secured first lien credit facilities in an aggregate principal amount of $400.0 million for a five year term, consisting of term loans in an aggregate initial principal amount of $150.0 million (the “Prior Term Loans”) and revolving credit commitments in an aggregate principal amount of $250.0 million (the “Prior Revolving Commitments”). The Prior Revolving Commitments contained sub-facilities that could be used as follows: up to $40.0 million for letters of credit, up to $25.0 million for Swing Line Loans (as defined below), and up to $40.0 million for revolving loans and letters of credit in certain currencies other than U.S. Dollars (“Alternative Currencies”). “Swing Line Loans” refer to Base Rate (as defined below) loans made in immediately available funds denominated in dollars by the swing line lender in its sole and absolute discretion. As of October 30, 2016, there were no amounts outstanding under the letters of credit, Swing Line Loans, and Alternative Currencies.

Interest on loans made under the Prior Credit Agreement in U.S. Dollars accrued, at Semtech’s option, at a rate per annum equal to (1) the Base Rate plus a margin ranging from 0.25% to 1.25% depending upon Semtech’s consolidated leverage ratio or (2) London Interbank Offered Rate (“LIBOR”) (determined with respect to deposits in U.S. Dollars) for an interest period to be selected by Semtech plus a margin ranging from 1.25% to 2.25% depending upon Semtech’s consolidated leverage ratio. The “Base Rate” is equal to a fluctuating rate equal to the highest of (a) the prime rate (as published by The Wall Street Journal), (b) ½ of 1% above the federal funds effective rate or (c) one-month LIBOR (determined with respect to deposits in U.S. Dollars) plus 1%. Interest on loans in Alternative Currencies, other than Canadian Dollars, accrued at a rate per annum equal to LIBOR (determined with respect to deposits in the applicable Alternative Currency) for an interest period to be selected by Semtech plus a margin ranging from 1.25% to 2.25% depending upon Semtech’s consolidated leverage ratio. Interest on loans in Canadian Dollars accrued at a rate per annum equal to the CDOR Rate (as defined below) for an interest period to be selected by Semtech plus a margin ranging from 1.25% to 2.25% depending upon Semtech’s consolidated leverage ratio. The “CDOR Rate” for any interest period is the rate equal to the sum of: (a) the rate determined by the administrative agent with reference to the arithmetic average of the discount rate quotations of all institutions listed for CAD Dollar-denominated bankers’ acceptances displayed and identified on the “Reuters Screen CDOR Page” and (b) 0.10% per annum. CDOR Commitment fees on the unused portion of the Prior Revolving Commitments accrued at a rate per annum ranging from 0.20% to 0.45% depending upon Semtech’s consolidated leverage ratio. Interest was payable monthly for a Base Rate loan and swing line loan and quarterly for a Euro dollar rate loan. As of October 30, 2016, the interest rates payable on both the Prior Term Loans and the Prior Revolving Commitments was 2.28%.

As of October 30, 2016, there was $67.8 million outstanding under the Prior Term Loans and $181.0 million in revolving loans outstanding pursuant to the Prior Revolving Commitments. The Prior Term Loans and the Prior Revolving Commitments (and related revolving loans) were scheduled to mature on May 1, 2018.

All obligations of Semtech Corporation under the Prior Credit Agreement were unconditionally guaranteed by each of the Prior Guarantors and were secured by a first priority security interest in substantially all of the assets of Semtech Corporation and the Prior Guarantors, subject to certain customary exceptions.

Semtech Corporation and the Prior Guarantors were subject to customary covenants under the Prior Credit Agreement, including the maintenance of a minimum interest ratio of 3.50 to 1.00 and a maximum total consolidated leverage ratio of 3.00 to 1.00. Semtech Corporation and the Prior Guarantors were in compliance with such financial covenants as of October 30, 2016.

The Prior Credit Agreement also contained customary provisions pertaining to events of default. If any event of default had occurred, the principal, interest, and any other monetary obligations on all the then outstanding amounts could have become due and payable immediately.

On November 15, 2016, the Company, with each of its domestic subsidiaries as guarantors, entered into an amended and restated credit agreement (the "Amended and Restated Credit Agreement") with the lenders referred to therein (the "Lenders") and HSBC Bank USA, National Association, as administrative agent and as swing line lender and letter of credit issuer. The Amended and Restated Credit Agreement consists of a senior secured term A loan facility in the principal amount of $150.0 million and a senior secured revolving credit facility in the principal amount of $250.0 million, each of which is scheduled to mature in November 2021. The Amended and Restated Credit Agreement amended and restated the Prior Credit Agreement that was scheduled to mature in May of 2018 (see Note 20 for discussion regarding Subsequent Events).

Note 11: Income Taxes

The Company's effective tax rate differs from the statutory federal income tax rate of 35% due primarily to regional mix of income, valuation allowances in the U.S., and certain undistributed foreign earnings for which no U.S. taxes are provided because such earnings are intended to be indefinitely reinvested outside of the U.S.

The Company uses a two-step approach to recognize and measure uncertain tax positions ("UTP"). The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates that it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step is to measure the tax benefit as the largest amount that is more than 50% likely of being realized upon ultimate settlement.

A reconciliation of the beginning and ending amount of net unrecognized tax benefits is as follows:

(in thousands)	
Balance at January 31, 2016	$8,432
Additions based on tax positions related to the current year	80
Reductions for tax positions of prior years, net	(121)
Reductions for settlements with tax authorities	—
Balance as of October 30, 2016	$8,391

The gross unrecognized tax benefit (before federal impact of state items) was $10.6 million at both October 30, 2016 and January 31, 2016. Included in the balance of unrecognized tax benefits at October 30, 2016 and January 31, 2016, is $8.4 million and $8.4 million of net tax benefit (after federal impact of state items), respectively, that, if recognized, would impact the effective tax rate, subject to the valuation allowance.

The liability for UTP is reflected within the condensed consolidated balance sheets as follows:

(in thousands)	October 30, 2016	January 31, 2016
Deferred tax assets - non-current	$ 7,121	$ 7,162
Other long-term liabilities	1,270	1,270
Total accrued taxes	$ 8,391	$ 8,432

The Company's policy is to include net interest and penalties related to unrecognized tax benefits within the provision for taxes within the unaudited condensed consolidated statements of income. The Company had approximately $293,000 of net interest and penalties accrued at October 30, 2016 and January 31, 2016.

Tax years prior to 2012 (the Company's fiscal year 2013) are generally not subject to examination by the U.S. Internal Revenue Service ("IRS") except for items involving tax attributes that have been carried forward to tax years whose statute of limitations remains open. The Company is currently under IRS audit for fiscal years 2012 and 2013 and expects to close those audits within the next twelve months. The Company's reserves for UTP's are expected to be sufficient to address matters that may arise under examination. For state returns, the Company is generally not subject to income tax examinations for years prior to 2011 (the Company's fiscal year 2012). The Company has a significant tax presence in Switzerland for which Swiss tax filings have been examined through fiscal year 2015. The Company is also subject to routine examinations by various foreign tax jurisdictions in which it operates.

Note 12: Commitments and Contingencies

In accordance with accounting standards regarding loss contingencies, the Company accrues an undiscounted liability for those contingencies where the incurrence of a loss is probable and the amount can be reasonably estimated. The Company also discloses the amount accrued and the amount of a reasonably possible loss in excess of the amount accrued, if such disclosure is necessary for its financial statements not to be misleading. The Company does not record liabilities when the likelihood that the liability has been incurred is probable but the amount cannot be reasonably estimated, or when the liability is believed to be only reasonably possible or remote. The Company evaluates at least quarterly, developments in its legal matters that could affect the amount of liability that has been previously accrued, and makes adjustments as appropriate. Significant judgment is required to determine both probability and the estimated amount. The Company may be unable to estimate a possible loss or range of possible loss due to various reasons, including, among others: (i) if the damages sought are indeterminate; (ii) if the proceedings are in early stages, (iii) if there is uncertainty as to the outcome of pending appeals, motions or settlements, (iv) if there are significant factual issues to be determined or resolved, and (v) if there are novel or unsettled legal theories presented. In such instances, there is considerable uncertainty regarding the ultimate resolution of such matters, including a possible eventual loss, if any.

From time to time, the Company is involved in various claims, litigation, and other legal actions that are normal to the nature of its business, including with respect to intellectual property, contract, product liability, employment, and environmental matters. The Company's evaluation of legal matters and proceedings often involves a series of complex assessments by management about future events and can rely heavily on estimates and assumptions. While the consequences of certain unresolved matters and proceedings are not presently determinable, and an estimate of the probable and reasonably possible loss or range of loss in excess of amounts accrued for such proceedings cannot be reasonably made, an adverse outcome from such proceedings could have a material adverse effect on the Company's earnings in any given reporting period. However, in the opinion of management, after consulting with legal counsel, and taking into account insurance coverage, any ultimate liability related to current outstanding claims and lawsuits, individually or in the aggregate, is not expected to have a material adverse effect on the Company's financial statements, as a whole. However, legal matters are inherently unpredictable and subject to significant uncertainties, some of which are beyond the Company's control. As such, even though the Company intends to vigorously defend itself with respect to its legal matters, there can be no assurance that the final outcome of these matters will not materially and adversely affect the Company's business, financial condition, results of operations, or cash flows.

The Company's currently pending legal matters of note are discussed below:

Environmental Matters

In 2001, the Company was notified by the California Department of Toxic Substances Control ("State") that it may have liability associated with the clean-up of the one-third acre Davis Chemical Company site in Los Angeles, California. The Company has been included in the clean-up program because it was one of the companies that used the Davis Chemical Company site for waste recycling and/or disposal between 1949 and 1990. The Company joined with other potentially responsible parties that sent acetone to the site and entered into a Consent Order with the State that required the group to perform a soils investigation at the site and submit a remediation plan. The State has approved the remediation plan, which addressed the group's initial obligations under the Consent Order. The Consent Order does not require the group to remediate the site and the State has indicated it intends to look to other parties for remediation. To date, the Company's share of the group's expenses has not been material and has been expensed as incurred. There is a pending settlement offer that would potentially resolve most, if not all, of the acetone group's potential liability. More recently, the State has indicated that it will pursue a smaller group of parties for additional remediation and/or costs, in particular parties the State alleges provided chlorinated solvents for recycling, including the Company. Due to the fact that there are fewer parties that are alleged to have provided chlorinated solvent wastes, the potential share of this alleged liability is much larger than the Company's share of acetone group potential liability. Settlement discussions regarding the potential liability for chlorinated solvents at the site have recently been initiated, but it is too soon to tell if those discussions will lead to a negotiated resolution of the issues.

The Company has used an environmental firm, specializing in hydrogeology, to perform monitoring of the groundwater at the Company's former facility in Newbury Park, California that was leased for approximately 40 years. The Company vacated the building in May 2002. Certain contaminants have been found in the local groundwater and site soils. The location of key soil contamination (and some related site groundwater impact associated with the soil contamination) is concentrated in and found to emanate from an area of an underground storage tank that the Company believes to have been installed and primarily used in the early 1960s by a former tenant at the site who preceded the Company's tenancy. There are no litigation claims pending with respect to environmental matters at the Newbury Park site.

The Los Angeles Regional Water Quality Control Board ("RWQCB") having authority over the site issued joint instructions in November 2008, ordering the Company and the current owner of the site to perform additional assessments and surveys, and to create ongoing groundwater monitoring plans before any final regulatory action for "no further action" may be approved. In September 2009, the regulatory agency issued supplemental instructions to the Company and the current site owner regarding previously ordered site assessments, surveys and groundwater monitoring. In October 2013, an order was issued including a scope of proposed additional site work, monitoring, and proposed remediation activities. The Company filed appeals of the October 2013 order seeking reconsideration by the RWQCB and review by the State Water Resources Control Board ("SWRCB") of the removal of two other potentially responsible parties, and seeking clarification of certain other factual findings. In April 2015, the RWQCB denied the Company's request to name the two other potentially responsible parties to the order, but did correct certain findings of fact identified by the Company in its petition for reconsideration. The SWRCB has not yet ruled on the Company's petition for review of the RWQCB's action as the petition was filed with a request it be held in abeyance.

The Company has been engaged with the regulatory agency, including technical discussion between the Company's environmental firm and RWQCB staff, and has initiated the technical efforts to comply with the order. The Company submitted technical reports prepared by the environmental firm to the RWQCB and has received confirmation regarding the satisfaction of portions of the order. The Company also submitted a remedial action plan prepared by the environmental firm outlining the cleanup of soil, groundwater, and soil vapor at the site. The Company's contractors have installed new monitoring wells and have submitted plans and applications in order to initiate pilot testing of a soil vapor extraction system. The parties are continuing to work toward compliance with the October 2013 order and anticipate working cooperatively on any ultimate proposed cleanup and abatement work.

The Company has accrued liabilities where it is probable that a loss will be incurred and the cost or amount of loss can be reasonably estimated. Based on the latest determinations by the RWQCB and the draft remedial action plan, the Company determined a revised range of probable loss between $5.2 million and $7.5 million. Given the uncertainties associated with environmental assessment and the remediation activities, the Company is unable to determine a best estimate within the range of loss. Therefore, the Company has recorded the minimum amount of probable loss as follows within the Company's condensed consolidated balance sheets.

(in thousands)	Accrued Liability	Other-Long Term Liability	Total
Balance at January 31, 2016	$ 1,150	$ 4,180	$ 5,330
Change in estimate	(499)	499	—
Utilization	(116)	—	(116)
Balance at October 30, 2016	$ 535	$ 4,679	$ 5,214

These estimates could change as a result of changes in planned remedial actions, further actions from the regulatory agency, remediation technology, and other factors.
Indemnification

The Company has entered into agreements with its current and former executives and directors indemnifying them against certain liabilities incurred in connection with the performance of their duties. The Company's Certificate of Incorporation and Bylaws contain comparable indemnification obligations with respect to the Company's current directors and employees.

Product Warranties

The Company's general warranty policy provides for repair or replacement of defective parts. In some cases, a refund of the purchase price is offered. In certain instances the Company has agreed to other or additional warranty terms, including indemnification provisions.

The product warranty accrual reflects the Company's best estimate of probable liability under its product warranties. The Company accrues for known warranty issues if a loss is probable and can be reasonably estimated, and accrues for estimated incurred but unidentified issues based on historical experience. Historically, warranty expense has been immaterial to the Company's consolidated financial statements.

Earn-out Liability

Pursuant to the terms of the amended earn-out arrangement ("Cycleo Amended Earn-out") with the former stockholders of Cycleo SAS ("Cycleo Earn-out Beneficiaries"), which the Company acquired on March 7, 2012, the Company potentially may make payments totaling up to approximately $16.0 million based on the achievement of a combination of certain revenue and operating income milestones over a defined period ("Cycleo Defined Earn-out Period"). The Cycleo Defined Earn-out Period covers the period April 27, 2015 to April 26, 2020. For certain of the Cycleo Earn-out Beneficiaries, payment of the earn-out liability is contingent upon continued employment and is accounted for as post-acquisition compensation expense over the service period. The portion of the earn-out liability that is not dependent on continued employment is not considered as compensation expense. The Company recorded a liability for the Cycleo Amended Earn-out of $8.3 million and $6.3 million as of October 30, 2016 and January 31, 2016, respectively, of which $1.8 million is expected to be paid within twelve months.

Pursuant to the terms of the Triune Earn-out with the former members of Triune ("Triune Earn-out Beneficiaries"), which the Company acquired on March 4, 2015, the Company potentially may make payments totaling up to approximately $70.0 million based on achievement of certain net revenue targets measured at each fiscal year end, starting with fiscal year 2016 and ending in fiscal year 2018. An additional payment of up to $16.0 million may be made based upon a combination of cumulative revenue and contribution margin targets measured from the acquisition date through the end of the Company's fiscal year 2018. For certain of the Triune Earn-out Beneficiaries, payment of the earn-out liability is contingent upon continued employment and is accounted for as post-acquisition compensation expense over the service period. The portion of the earn-out liability that is not dependent on continued employment is not considered as compensation expense. The Triune Earn-out targets for fiscal year 2016 were not met and the Company does not expect the fiscal year 2017 or 2018 targets to be achieved. Refer to Note 7 for additional discussion regarding fair value measurements.

A summary of earn-out liabilities by classification follows:

	Balance at October 30, 2016			Balance at January 31, 2016		
(in thousands)	Cycleo	Triune	Total	Cycleo	Triune	Total
Compensation expense	$6,379	$ —	$6,379	$4,397	$ —	$4,397
Not conditional upon continued employment	1,295	—	1,295	1,457	—	1,457
Interest expense	590	—	590	405	—	405
Total liability	$8,264	$ —	$8,264	$6,259	$ —	$6,259
Amount expected to be settled within twelve months	$1,829	$ —				