

CADENCE DESIGN SYSTEMS INC

Form 10-Q

April 25, 2008

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**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 March 29, 2008

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 0-15867

CADENCE DESIGN SYSTEMS, INC.
(Exact Name of Registrant as Specified in Its Charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

77-0148231
(I.R.S. Employer
Identification No.)

2655 Seely Avenue, Building 5, San Jose, California
(Address of Principal Executive Offices)

95134
(Zip Code)

(408) 943-1234
Registrant's Telephone Number, including Area Code

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes 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. (Check one):

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

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

On March 29, 2008, 257,854,529 shares of the registrant's common stock, \$0.01 par value, were outstanding.

**CADENCE DESIGN SYSTEMS, INC.
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**CADENCE DESIGN SYSTEMS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS**

(In thousands)

(Unaudited)

ASSETS

| | March 29, 2008 | December 29, 2007 |
|---------------------------------------------------------------------------------------------------------|-------------------|----------------------|
| Current Assets: | | |
| Cash and cash equivalents | \$ 825,545 | \$ 1,062,920 |
| Short-term investments | 11,157 | 15,193 |
| Receivables, net of allowances of \$2,752 and \$2,895, respectively | 346,321 | 326,211 |
| Inventories | 29,771 | 31,003 |
| Prepaid expenses and other | 97,940 | 94,236 |
| Total current assets | 1,310,734 | 1,529,563 |
| Property, plant and equipment, net of accumulated depreciation of \$633,059 and \$624,680, respectively | 345,918 | 339,463 |
| Goodwill | 1,315,561 | 1,310,211 |
| Acquired intangibles, net | 124,196 | 127,072 |
| Installment contract receivables | 214,991 | 238,010 |
| Other assets | 326,003 | 326,831 |
| Total Assets | \$ 3,637,403 | \$ 3,871,150 |

LIABILITIES AND STOCKHOLDERS EQUITY

| | | |
|------------------------------------------|------------|------------|
| Current Liabilities: | | |
| Convertible notes | \$ 230,385 | \$ 230,385 |
| Accounts payable and accrued liabilities | 220,906 | 289,934 |
| Current portion of deferred revenue | 298,956 | 265,168 |
| Total current liabilities | 750,247 | 785,487 |
| Long-Term Liabilities: | | |
| Long-term portion of deferred revenue | 135,465 | 136,655 |
| Convertible notes | 500,000 | 500,000 |
| Other long-term liabilities | 357,986 | 368,942 |
| Total long-term liabilities | 993,451 | 1,005,597 |

| | | |
|-------------------------------------------------|--------------|--------------|
| Stockholders' Equity: | | |
| Common stock and capital in excess of par value | 1,528,671 | 1,516,493 |
| Treasury stock, at cost | (780,999) | (619,125) |
| Retained earnings | 1,119,176 | 1,162,441 |
| Accumulated other comprehensive income | 26,857 | 20,257 |
| Total stockholders' equity | 1,893,705 | 2,080,066 |
| Total Liabilities and Stockholders' Equity | \$ 3,637,403 | \$ 3,871,150 |

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

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CADENCE DESIGN SYSTEMS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share amounts)
(Unaudited)

| | Three Months Ended | |
|-----------------------------------------------------------|--------------------|-------------------|
| | March 29, 2008 | March 31, 2007 |
| Revenue: | | |
| Product | \$ 156,193 | \$ 237,904 |
| Services | 32,196 | 31,922 |
| Maintenance | 98,800 | 95,359 |
| Total revenue | 287,189 | 365,185 |
| Costs and Expenses: | | |
| Cost of product | 12,001 | 15,652 |
| Cost of services | 25,193 | 23,615 |
| Cost of maintenance | 14,540 | 15,123 |
| Marketing and sales | 93,034 | 102,698 |
| Research and development | 125,356 | 117,065 |
| General and administrative | 37,708 | 40,611 |
| Amortization of acquired intangibles | 5,760 | 4,509 |
| Restructuring and other charges (credits) | ---- | (945) |
| Write-off of acquired in-process technology | 600 | ---- |
| Total costs and expenses | 314,192 | 318,328 |
| Income (loss) from operations | (27,003) | 46,857 |
| Interest expense | (2,995) | (3,460) |
| Other income, net | 5,763 | 19,530 |
| Income (loss) before provision (benefit) for income taxes | (24,235) | 62,927 |
| Provision (benefit) for income taxes | (5,488) | 18,506 |
| Net income (loss) | \$ (18,747) | \$ 44,421 |
| Basic net income (loss) per share | \$ (0.07) | \$ 0.16 |
| Diluted net income (loss) per share | \$ (0.07) | \$ 0.15 |
| Weighted average common shares outstanding basic | 262,825 | 269,660 |
| Weighted average common shares outstanding diluted | 262,825 | 293,603 |

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

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CADENCE DESIGN SYSTEMS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

| | Three Months Ended | |
|-----------------------------------------------------------------------------------------------------|--------------------|-------------------|
| | March 29, 2008 | March 31, 2007 |
| Cash and Cash Equivalents at Beginning of Period | \$ 1,062,920 | \$ 934,342 |
| Cash Flows from Operating Activities: | | |
| Net income (loss) | (18,747) | 44,421 |
| Adjustments to reconcile net income (loss) to net cash provided by (used for) operating activities: | | |
| Depreciation and amortization | 32,982 | 31,920 |
| Stock-based compensation | 21,590 | 27,682 |
| Equity in loss from investments, net | 333 | 637 |
| Gain on investments, net | (224) | (7,498) |
| Gain on sale and leaseback of land and buildings | (535) | (11,127) |
| Write-down of investment securities | 5,401 | ---- |
| Write-off of acquired in-process technology | 600 | ---- |
| Tax benefit of call options | ---- | 1,906 |
| Deferred income taxes | ---- | 191 |
| Proceeds from the sale of receivables, net | 15,660 | 41,434 |
| Provisions (recoveries) for losses (gains) on trade accounts receivable and sales returns | (142) | 1,283 |
| Other non-cash items | 1,075 | 3,216 |
| Changes in operating assets and liabilities, net of effect of acquired businesses: | | |
| Receivables | (20,431) | 18,156 |
| Installment contract receivables | 23,253 | (87,504) |
| Inventories | 1,281 | (651) |
| Prepaid expenses and other | (3,546) | (9,832) |
| Other assets | (4,344) | (4,346) |
| Accounts payable and accrued liabilities | (80,931) | (37,729) |
| Deferred revenue | 22,530 | 6,661 |
| Other long-term liabilities | (14,886) | 143 |
| Net cash provided by (used for) operating activities | (19,081) | 18,963 |
| Cash Flows from Investing Activities: | | |
| Proceeds from sale of short-term investments | ---- | 197 |
| Proceeds from the sale of long-term investments | 3,250 | 4,787 |
| Proceeds from the sale of property, plant and equipment | ---- | 46,500 |
| Purchases of property, plant and equipment | (24,595) | (20,394) |
| Purchases of software licenses | (375) | ---- |

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| | | |
|-----------------------------------------------------------------------------------------------------------------|------------|------------|
| Investment in venture capital partnerships and equity investments | ---- | (1,499) |
| Cash paid in business combinations and asset acquisitions, net of cash acquired, and acquisition of intangibles | (5,560) | (1,547) |
| Net cash provided by (used for) investing activities | (27,280) | 28,044 |
| Cash Flows from Financing Activities: | | |
| Principal payments on term loan | ---- | (28,000) |
| Tax benefit from employee stock transactions | 95 | 8,642 |
| Proceeds from issuance of common stock | 25,485 | 111,616 |
| Stock received for payment of employee taxes on vesting of restricted stock | (2,207) | (6,223) |
| Purchases of treasury stock | (216,236) | (121,455) |
| Net cash used for financing activities | (192,863) | (35,420) |
| Effect of exchange rate changes on cash and cash equivalents | 1,849 | 825 |
| Increase (decrease) in cash and cash equivalents | (237,375) | 12,412 |
| Cash and Cash Equivalents at End of Period | \$ 825,545 | \$ 946,754 |

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

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CADENCE DESIGN SYSTEMS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTE 1. BASIS OF PRESENTATION

The Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q have been prepared by Cadence Design Systems, Inc., or Cadence, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission, or the SEC. Certain information and footnote disclosures normally included in consolidated financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. However, Cadence believes that the disclosures contained in this Quarterly Report comply with the requirements of Section 13(a) of the Securities Exchange Act of 1934, as amended, for a Quarterly Report on Form 10-Q and are adequate to make the information presented not misleading. These Condensed Consolidated Financial Statements are meant to be, and should be, read in conjunction with the Consolidated Financial Statements and the notes thereto included in Cadence's Annual Report on Form 10-K for the fiscal year ended December 29, 2007.

The unaudited Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q reflect all adjustments (which include only normal, recurring adjustments and those items discussed in these Notes) that are, in the opinion of management, necessary to state fairly the results for the periods presented. The results for such periods are not necessarily indicative of the results to be expected for the full fiscal year.

Preparation of the Condensed Consolidated Financial Statements in conformity with generally accepted accounting principles 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 Condensed Consolidated Financial Statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

In September 2006, the Financial Accounting Standards Board, or FASB, issued Statement of Financial Accounting Standard, or SFAS, No. 157, Fair Value Measurements, which defines fair value, establishes guidelines for measuring fair value and expands disclosures regarding fair value measurements. SFAS No. 157 does not require any new fair value measurements but rather eliminates inconsistencies in guidance found in various prior accounting pronouncements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007. In February 2008, the FASB issued FASB Staff Position, or FSP, FAS No. 157-2, Effective Date of FASB Statement No. 157, which delayed the effective date of SFAS No. 157 to fiscal years beginning after November 15, 2008 and interim periods within those fiscal years for all non-financial assets and non-financial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). Cadence adopted SFAS No. 157 for fiscal 2008, except as it applies to those non-financial assets and non-financial liabilities as described in FSP FAS No. 157-2, and it did not have a material impact on its consolidated financial position, results of operations or cash flows. See Note 3 for information and related disclosures regarding Cadence's fair value measurements.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities. Under SFAS No. 159, companies may elect to measure certain financial instruments and certain other items at fair value. The standard requires that unrealized gains and losses on items for which the fair value option has been elected be reported in earnings. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. Cadence adopted SFAS No. 159 for fiscal 2008. However Cadence did not elect to apply the fair value option to any

financial instruments or other items upon adoption of SFAS No. 159 or during the three months ended March 29, 2008. Therefore, the adoption of SFAS No. 159 did not impact Cadence's consolidated financial position, results of operations or cash flows.

NOTE 2. STOCK-BASED COMPENSATION

Cadence has equity incentive plans that provide for the grant to employees of stock-based awards, including stock options, restricted stock awards and restricted stock units. Restricted stock awards and restricted stock units are referred to in this Form 10-Q as restricted stock. In addition, the 1995 Directors Stock Option Plan, or

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1995 Directors Plan, provides for the automatic grant of stock options to non-employee members of Cadence's Board of Directors. Cadence also has an employee stock purchase plan, or ESPP, which enables employees to purchase shares of Cadence common stock.

Stock-based compensation expense and the related income tax benefit recognized under SFAS No. 123R, "Share-Based Payment" in the Condensed Consolidated Statements of Operations in connection with stock options, restricted stock and the ESPP for the three months ended March 29, 2008 and March 31, 2007 were as follows:

| | Three Months Ended | |
|----------------------------------------|--------------------|-------------------|
| | March 29, 2008 | March 31, 2007 |
| | (In thousands) | |
| Stock options | \$ 7,519 | \$ 10,430 |
| Restricted stock and stock bonuses | 11,164 | 15,184 |
| ESPP | 2,907 | 2,068 |
| Total stock-based compensation expense | \$ 21,590 | \$ 27,682 |
| Income tax benefit | \$ 6,060 | \$ 10,011 |

Stock Options

The exercise price of each stock option granted under Cadence's employee equity incentive plans is equal to or greater than the market price of Cadence's common stock on the date of grant. Generally, option grants vest over four years, expire no later than ten years from the grant date and are subject to the employee's continuing service to Cadence. The options granted under the 1995 Directors Plan vest one year from the date of grant. Options assumed in connection with acquisitions generally have exercise prices that differ from the fair value of Cadence's common stock on the date of acquisition and such options generally continue to vest under their original vesting schedules and expire on the original dates stated in the acquired company's option agreements. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model. The weighted average grant date fair value of options granted and the weighted average assumptions used in the model for the three months ended March 29, 2008 and March 31, 2007 were as follows:

| | Three Months Ended | |
|------------------------------------------------|--------------------|-------------------|
| | March 29, 2008 | March 31, 2007 |
| Dividend yield | None | None |
| Expected volatility | 45.0% | 23.0% |
| Risk-free interest rate | 2.51% | 4.54% |
| Expected life (in years) | 4.5 | 4.4 |
| Weighted average fair value of options granted | \$ 4.29 | \$ 4.75 |

The computation of the expected volatility assumption used in the Black-Scholes pricing model for new grants is based on implied volatility. When establishing the expected life assumption, Cadence reviews annual historical

employee exercise behavior with respect to option grants having similar vesting periods. The risk-free interest rate for the period within the expected term of the option is based on the yield of United States Treasury notes in effect at the time of grant. Cadence has not historically paid dividends; thus the expected dividend yield used in the calculation is zero.

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Restricted Stock and Stock Bonuses

The cost of restricted stock is determined using the fair value of Cadence's common stock on the date of the grant, and compensation expense is recognized over the vesting period. The weighted average grant date fair values of restricted stock granted during the three months ended March 29, 2008 and March 31, 2007 were as follows: