CREE INC
Form 10-Q
April 27, 2016
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q
(Mark One)
[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 27, 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 0-21154
CREE, INC.
(Exact name of registrant as specified in its charter)

North Carolina	56-1572719
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

4600 Silicon Drive Durham, North Carolina	27703
(Address of principal executive offices)	(Zip Code)

(919) 407-5300
(Registrant’s telephone number, including area code)
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
Yes [X] No [ ]

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate 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 [X] No [ ]
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer”, “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer [X]	Accelerated filer [ ]
Non-accelerated filer [ ] (Do not check	Smaller reporting company [ ]

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[X]
The number of shares outstanding of the registrant's common stock, par value $0.00125 per share, as of April 20, 2016, was 100,427,836.

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PART I - FINANCIAL INFORMATION
Item 1. Financial Statements
CREE, INC.
UNAUDITED CONSOLIDATED BALANCE SHEETS

	March 27, 2016	June 28, 2015
	(In thousands, except par value)	
ASSETS		
Current assets:		
Cash and cash equivalents	$115,562	$139,710
Short-term investments	504,888	573,481
Total cash, cash equivalents and short-term investments	620,450	713,191
Accounts receivable, net	178,606	186,157
Income tax receivable	12,261	—
Inventories	297,860	280,576
Deferred income taxes	—	39,190
Prepaid expenses	20,755	29,932
Other current assets	57,807	54,851
Assets held for sale	5,700	4,353
Total current assets	1,193,439	1,308,250
Property and equipment, net	612,072	635,072
Goodwill	618,828	616,345
Intangible assets, net	309,919	310,729
Other long-term investments	41,661	57,595
Deferred income taxes	28,578	8,951
Other assets	9,648	11,091
Total assets	$2,814,145	$2,948,033
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable, trade	$129,963	$163,128
Accrued salaries and wages	45,993	45,415
Income taxes payable	—	2,035
Other current liabilities	42,046	44,208
Total current liabilities	218,002	254,786
Long-term liabilities:		
Long-term debt	225,000	200,000
Deferred income taxes	1,270	10,211
Other long-term liabilities	16,416	21,084
Total long-term liabilities	242,686	231,295
Commitments and contingencies (Note 12)		
Shareholders' equity:		
Preferred stock, par value $0.01; 3,000 shares authorized at March 27, 2016 and June 28, 2015; none issued and outstanding	—	—
Common stock, par value $0.00125; 200,000 shares authorized at March 27, 2016 and June 28, 2015; 100,424 and 105,507 shares issued and outstanding at March 27, 2016 and June 28, 2015, respectively	124	131
Additional paid-in-capital	2,336,099	2,285,554

Accumulated other comprehensive income, net of taxes	7,206	5,798
Retained earnings	10,028	170,469
Total shareholders' equity	2,353,457	2,461,952
Total liabilities and shareholders' equity	$2,814,145	$2,948,033

The accompanying notes are an integral part of the consolidated financial statements.

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CREE, INC.
UNAUDITED CONSOLIDATED STATEMENTS OF INCOME (LOSS)

	Three Months Ended		Nine Months Ended	
	March 27, 2016	March 29, 2015	March 27, 2016	March 29, 2015
	(In thousands, except per share amounts)			
Revenue, net	$366,919	$409,519	$1,228,214	$1,250,348
Cost of revenue, net	257,886	284,371	854,163	853,119
Gross profit	109,033	125,148	374,051	397,229
Operating expenses:				
Research and development	41,871	43,823	127,363	137,537
Sales, general and administrative	64,489	71,860	214,443	213,927
Amortization or impairment of acquisition-related intangibles	7,318	6,749	21,442	19,743
(Gain) loss on disposal or impairment of long-lived assets	(104)	1,459	16,483	3,641
Total operating expenses	113,574	123,891	379,731	374,848
Operating (loss) income	(4,541)	1,257	(5,680)	22,381
Non-operating income (expense), net	717	(866)	(14,075)	3,766
(Loss) income before income taxes	(3,824)	391	(19,755)	26,147
Income tax (benefit) expense	(3,976)	(85)	(8,860)	2,739
Net income (loss)	$152	$476	($10,895)	$23,408
Earnings (loss) per share:				
Basic	$—	$—	($0.11)	$0.20
Diluted	$—	$—	($0.11)	$0.20
Weighted average shares used in per share calculation:				
Basic	100,606	110,662	102,157	115,177
Diluted	101,221	111,590	102,157	116,304

The accompanying notes are an integral part of the consolidated financial statements.

CREE, INC.
UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

	Three Months Ended		Nine Months Ended	
	March 27, 2016	March 29, 2015	March 27, 2016	March 29, 2015
	(In thousands)			
Net income (loss)	$152	$476	($10,895)	$23,408
Other comprehensive income (loss):				
Currency translation gain (loss)	432	(2,071)	(357)	(3,971)
Net unrealized gain (loss) on available-for-sale securities, net of tax (expense) benefit of ($716), ($741), ($1,092) and $86, respectively	1,152	1,186	1,765	(126)
Other comprehensive income (loss)	1,584	(885)	1,408	(4,097)
Comprehensive income (loss)	$1,736	($409)	($9,487)	$19,311

The accompanying notes are an integral part of the consolidated financial statements.

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CREE, INC.
UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Nine Months Ended	
	March 27, 2016	March 29, 2015
	(In thousands)	
Cash flows from operating activities:		
Net (loss) income	($10,895)	$23,408
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
Depreciation and amortization	119,920	131,171
Stock-based compensation	44,318	49,260
Excess tax benefit from stock-based payment arrangements	(12)	(1,656)
Impairment of acquisition-related intangibles	—	254
Loss on disposal or impairment of long-lived assets	16,483	3,641
Amortization of premium/discount on investments	4,100	4,809
Loss on equity method investment	13,712	2,991
Foreign exchange loss on equity method investment	2,220	710
Deferred income taxes	537	(1,729)
Changes in operating assets and liabilities:		
Accounts receivable, net	8,594	7,579
Inventories	(17,517)	(15,101)
Prepaid expenses and other assets	(14,792)	2,275
Accounts payable, trade	(18,279)	(69,330)
Accrued salaries and wages and other liabilities	(9,626)	(44,583)
Net cash provided by operating activities	138,763	93,699
Cash flows from investing activities:		
Purchases of property and equipment	(99,692)	(158,277)
Purchases of patent and licensing rights	(11,034)	(14,550)
Proceeds from sale of property and equipment	5,199	122
Purchases of short-term investments	(192,728)	(254,883)
Proceeds from maturities of short-term investments	228,774	337,331
Proceeds from sale of short-term investments	31,262	207,551
Purchase of other long-term investments	—	(80,566)
Purchase of acquired business, net of cash acquired	(12,513)	—
Net cash (used in) provided by investing activities	(50,732)	36,728
Cash flows from financing activities:		
Proceeds from long-term debt borrowings	538,000	440,000
Payments on long-term debt borrowings	(513,000)	(290,000)
Net proceeds from issuance of common stock	13,321	26,832
Excess tax benefit from stock-based payment arrangements	12	1,656
Repurchases of common stock	(149,555)	(390,088)
Net cash used in financing activities	(111,222)	(211,600)
Effects of foreign exchange changes on cash and cash equivalents	(957)	(923)
Net decrease in cash and cash equivalents	(24,148)	(82,096)
Cash and cash equivalents:		
Beginning of period	139,710	286,824
End of period	$115,562	$204,728
Supplemental disclosure of cash flow information:		
Significant non-cash transactions:		

Accrued property and equipment	$7,317	$11,182

The accompanying notes are an integral part of the consolidated financial statements.

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CREE, INC.
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Note 1 – Basis of Presentation and New Accounting Standards
Overview
Cree, Inc. (the Company) is a leading innovator of lighting-class light emitting diode (LED) products, lighting products and wide bandgap semiconductor products for power and radio-frequency (RF) applications. The Company's products are targeted for applications such as indoor and outdoor lighting, video displays, transportation, electronic signs and signals, power supplies, inverters and wireless systems.
The Company's lighting products primarily consist of LED lighting systems and bulbs. The Company designs, manufactures and sells lighting fixtures and lamps for the commercial, industrial and consumer markets.
The Company's LED products consist of LED components, LED chips and silicon carbide (SiC) materials. The Company's success in selling LED products depends upon its ability to offer innovative products and to enable its customers to develop and market LED-based products that successfully compete against other LED-based products and drive LED adoption against traditional lighting products.
In addition, the Company develops, manufactures and sells power and RF devices based on wide bandgap semiconductor materials such as SiC and gallium nitride (GaN). As previously announced, the Company has filed a confidential registration statement for an initial public offering to take this business public under the name Wolfspeed, Inc. This initial public offering is dependent upon many factors, and may not occur on favorable terms or at all. The Company's power products are made from SiC and provide increased efficiency, faster switching speeds and reduced system size and weight over comparable silicon-based power devices. The Company's RF devices are made from GaN and provide improved efficiency, bandwidth and frequency of operation as compared to silicon or gallium arsenide (GaAs).
The majority of the Company's products are manufactured at its production facilities located in North Carolina, Wisconsin and China. The Company also uses contract manufacturers for certain products and aspects of product fabrication, assembly and packaging. The Company operates research and development facilities in North Carolina, California, Wisconsin, India and China (including Hong Kong).
Cree, Inc. is a North Carolina corporation established in 1987 and is headquartered in Durham, North Carolina.
The Company's three reportable segments are:

- Lighting Products
- LED Products
- Power and RF Products

For financial results by reportable segment, please refer to Note 13, "Reportable Segments."
Basis of Presentation
The consolidated balance sheet at March 27, 2016, the consolidated statements of income (loss) for the three and nine months ended March 27, 2016 and March 29, 2015, the consolidated statements of comprehensive income (loss) for the three and nine months ended March 27, 2016 and March 29, 2015, and the consolidated statements of cash flows for the nine months ended March 27, 2016 and March 29, 2015 (collectively, the consolidated financial statements) have been prepared by the Company and have not been audited. In the opinion of management, all normal and recurring adjustments necessary to fairly state the consolidated financial position, results of operations and cash flows at March 27, 2016, and for all periods presented, have been made. All intercompany accounts and transactions have been eliminated. The consolidated balance sheet at June 28, 2015 has been derived from the audited financial statements as of that date.
These financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) for interim information and with the instructions to Form 10-Q and Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for annual financial statements. These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the fiscal year ended June 28, 2015 (fiscal 2015). The results of operations for the three and

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nine months ended March 27, 2016 are not necessarily indicative of the operating results that may be attained for the entire fiscal year ending June 26, 2016 (fiscal 2016).

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses, and the disclosure of contingent assets and liabilities. Actual amounts could differ materially from those estimates.

Certain fiscal 2015 amounts in the accompanying consolidated financial statements have been reclassified to conform to the fiscal 2016 presentation. These reclassifications had no effect on previously reported consolidated net income or shareholders' equity.

Revision of Prior Period Financial Statements

During the third quarter of fiscal 2016, the Company identified errors in its previously reported financial statements in which amortization expense was understated as certain patents were being amortized over a life longer than the life of the underlying patent right.

The Company assessed the materiality of these errors on prior periods' financial statements in accordance with the United States Securities and Exchange Commission (SEC) Staff Accounting Bulletin (SAB) No. 99, Materiality, codified in the Accounting Standards Codification (ASC) 250, Presentation of Financial Statements, and concluded that they were not material individually or in the aggregate to any prior annual or interim periods. However, through the second quarter of fiscal 2016 the aggregate amount of the prior period errors of $6.8 million before income taxes would have been material to our current interim Consolidated Statements of Income (Loss). Consequently, in accordance with ASC 250, the Company corrected these errors, and other immaterial errors, for all prior periods presented by revising the consolidated financial statements and other financial information included herein. Periods not presented herein will be revised, as applicable in future filings.

The following table summarizes the effects of the revision on the Consolidated Balance Sheet as of June 28, 2015 (in thousands):

	As Previously Reported	Revision Adjustments	As Revised
Intangible assets, net	$317,154	($6,425)	$310,729
Deferred income taxes	8,893	58	8,951
Total assets	2,954,400	(6,367)	2,948,033
Deferred income taxes	12,174	(1,963)	10,211
Total long-term liabilities	233,258	(1,963)	231,295
Retained earnings	174,873	(4,404)	170,469
Total shareholders' equity	2,466,356	(4,404)	2,461,952
Total liabilities and shareholders' equity	2,954,400	(6,367)	2,948,033

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The following table summarizes the effects of the revision on the Consolidated Statements of Income (Loss) (in thousands):

	Three Months Ended March 29, 2015			Nine Months Ended March 29, 2015		
	As Previously Reported	Revision Adjustments	As Revised	As Previously Reported	Revision Adjustments	As Revised
Cost of revenue, net	284,111	260	284,371	852,341	778	853,119
Gross profit	125,408	(260)	125,148	398,007	(778)	397,229
Operating (loss) income	1,517	(260)	1,257	23,159	(778)	22,381
(Loss) income before income taxes	651	(260)	391	26,925	(778)	26,147
Income tax (benefit) expense	—	(85)	(85)	2,993	(254)	2,739
Net income (loss)	651	(175)	476	23,932	(524)	23,408
Earnings (loss) per share:						
Basic	0.01	(0.01)	—	0.21	(0.01)	0.20
Diluted	0.01	(0.01)	—	0.21	(0.01)	0.20

The revision had no net impact on the Company’s net cash provided by operating activities.

Recently Issued Accounting Pronouncements

Revenue from Contracts with Customers

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09: Revenue from Contracts with Customers (Topic 606). The FASB has subsequently issued multiple ASUs which amend and clarify the guidance in Topic 606. The ASU establishes a principles-based approach for accounting for revenue arising from contracts with customers and supersedes existing revenue recognition guidance. The ASU provides that an entity should apply a five-step approach for recognizing revenue, including (1) identify the contract with a customer; (2) identify the performance obligations in the contract; (3) determine the transaction price; (4) allocate the transaction price to the performance obligations in the contract; and (5) recognize revenue when, or as, the entity satisfies a performance obligation. Also, the entity must provide various disclosures concerning the nature, amount and timing of revenue and cash flows arising from contracts with customers. The effective date will be the first quarter of the Company's fiscal year ending June 30, 2019, using one of two retrospective application methods. The Company is currently analyzing the impact of this new accounting guidance.

Income Taxes

In November 2015, the FASB issued ASU No. 2015-17: Income Taxes (Topic 740). The ASU requires entities to present deferred tax assets and deferred tax liabilities as noncurrent in a classified balance sheet. The ASU simplifies the current guidance, which requires entities to separately present deferred tax assets and deferred tax liabilities as current or noncurrent in a classified balance sheet. The ASU is effective for financial statements issued for annual periods beginning after December 15, 2016, and interim periods within those annual periods. Early application of the ASU is permitted as of the beginning of an interim or annual reporting period and may be applied either prospectively or retrospectively to all periods presented. The Company has adopted the provisions of this ASU prospectively for the interim period ended December 27, 2015 and therefore, prior periods were not retrospectively adjusted. The Company’s adoption of the new accounting guidance did not have a significant impact on its consolidated financial statements.

Leases

In February 2016, the FASB issued ASU No. 2016-02: Leases (Topic 842). The ASU requires that a lessee recognize in its statement of financial position a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term. The asset will be based on the liability, subject to adjustment, such as for initial direct costs. For leases with a term of 12 months or less, a lessee is permitted to make an accounting policy election by class of underlying asset not to recognize lease assets and lease liabilities. For income statement purposes, leases are still required to be classified as either operating or finance. Operating leases will result in straight-line expense while finance leases will result in a front-loaded expense pattern. The effective date will be the first quarter of the Company's fiscal year ending June 28, 2020, using a modified retrospective approach. The Company is currently analyzing the impact of this new pronouncement.

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Stock Compensation

In March 2016, the FASB issued ASU No. 2016-09: Compensation-Stock Compensation (Topic 718). The ASU simplifies the current stock compensation guidance for tax consequences. The ASU requires an entity to recognize all excess tax benefits and tax deficiencies as income tax expense or benefit in its income statement. The ASU also eliminates the requirement to defer recognition of an excess tax benefit until the benefit is realized through a reduction to taxes payable. For cash flows statement purposes, excess tax benefits should be classified as an operating activity and cash payments made to taxing authorities on the employee's behalf for withheld shares should be classified as financing activity. The ASU is effective for public companies for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. The Company is currently analyzing the impact of this new pronouncement.

Note 2 – Acquisition

On July 8, 2015, the Company closed on the acquisition of Arkansas Power Electronics International, Inc. (APEI), a global leader in power modules and power electronics applications, pursuant to a merger agreement with APEI and certain shareholders of APEI, whereby the Company acquired all of the outstanding share capital of APEI in exchange for a base purchase price of $13.8 million, subject to certain adjustments. In addition, if certain goals are achieved over the next two years, additional cash payments totaling up to $4.6 million may be made to the former APEI shareholders. In connection with this acquisition, APEI became a wholly owned subsidiary of the Company, renamed Cree Fayetteville, Inc. (Cree Fayetteville). Cree Fayetteville is not considered a significant subsidiary of the Company and its results from operations are reported as part of the Company's Power and RF Products segment.

The total purchase price for this acquisition is as follows (in thousands):

Cash consideration paid to shareholders	$13,797
Post-closing adjustments	181
Contingent consideration	4,625
Total purchase price	$18,603

The purchase price for this acquisition has been allocated to the assets acquired and liabilities assumed based on their estimated fair values as follows (in thousands):

Tangible assets:	
Cash and cash equivalents	$1,284
Accounts receivable	1,006
Inventories	143
Property and equipment	935
Other assets	270
Total tangible assets	3,638
Intangible assets:	
Patents	40
Customer relationships	4,500
Developed technology	11,403
In-process research and development	7,565
Non-compete agreements	231
Goodwill	2,483
Total intangible assets	26,222
Liabilities assumed:	
Accounts payable	55
Accrued expenses and liabilities	1,911
Other long-term liabilities	9,291
Total liabilities assumed	11,257
Net assets acquired	$18,603

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The identifiable intangible assets acquired as a result of the acquisition will be amortized over their respective estimated useful lives as follows (in thousands, except for years):

	Asset Amount	Estimated Life in Years
Patents	$40	20
Customer relationships	4,500	4
Developed technology	11,403	10
In-process research and development[1]	7,565	7
Non-compete agreements	231	3
Total identifiable intangible assets	$23,739	

(1) In-process research and development (IPR&D) is initially classified as indefinite-lived assets and tested for impairment at least annually or when indications of potential impairment exist. When an IPR&D project is complete, it is reclassified as an amortizable intangible asset and amortized over its estimated useful life.

Goodwill largely consists of expansion of product offerings of power modules and power electronics applications, manufacturing and other synergies of the combined companies, and the value of the assembled workforce.

The assets, liabilities, and operating results of APEI have been included in the Company's consolidated financial statements from the date of acquisition and are not significant to the Company as a whole.

Note 3 – Financial Statement Details

Accounts Receivable, net

The following table summarizes the components of accounts receivable, net (in thousands):

	March 27, 2016	June 28, 2015
Billed trade receivables	$230,302	$246,969
Unbilled contract receivables	2,781	2,223
	233,083	249,192
Allowance for sales returns, discounts and other incentives	(48,832)	(58,094)
Allowance for bad debts	(5,645)	(4,941)
Accounts receivable, net	$178,606	$186,157

Inventories

The following table summarizes the components of inventories (in thousands):

	March 27, 2016	June 28, 2015
Raw material	$88,074	$86,331
Work-in-progress	102,320	93,424
Finished goods	107,466	100,821
Inventories	$297,860	$280,576

Other Current Liabilities

The following table summarizes the components of other current liabilities (in thousands):

	March 27, 2016	June 28, 2015
Accrued taxes	$13,108	$13,935
Accrued professional fees	7,634	10,180
Accrued warranty	14,168	13,006
Accrued other	7,136	7,087
Other current liabilities	$42,046	$44,208

Accumulated Other Comprehensive Income, net of taxes

The following table summarizes the components of accumulated other comprehensive income, net of taxes (in thousands):

	March 27, 2016	June 28, 2015
Currency translation gain	$4,629	$4,986
Net unrealized gain on available-for-sale securities	2,577	812
Accumulated other comprehensive income, net of taxes	$7,206	$5,798

Non-Operating Income (Expense), net

The following table summarizes the components of non-operating income (expense), net (in thousands):

	Three Months Ended		Nine Months Ended	
	March 27, 2016	March 29, 2015	March 27, 2016	March 29, 2015
Foreign currency gain (loss), net	$348	$776	($4,331)	($1,820)
Gain on sale of investments, net	47	107	63	883
Loss on equity method investment	(790)	(3,670)	(13,712)	(2,991)
Interest income, net	1,024	1,823	3,541	7,441
Other, net	88	98	364	253
Non-operating income (expense), net	$717	($866)	($14,075)	$3,766

Reclassifications Out of Accumulated Other Comprehensive Income, net of taxes

The following table summarizes the amounts reclassified out of accumulated other comprehensive income, net of taxes (in thousands):

Accumulated Other Comprehensive Income Component	Amount Reclassified Out of Accumulated Other Comprehensive Income				Affected Line Item in the Consolidated Statements of Income (Loss)
	Three Months Ended		Nine Months Ended		
	March 27, 2016	March 29, 2015	March 27, 2016	March 29, 2015	
Net unrealized gain on available-for-sale securities, net of taxes	$47	$107	$63	$883	Non-operating income (expense), net
	47	107	63	883	(Loss) income before income taxes
	49	(23)	28	93	Income tax (benefit) expense
	($2)	$130	$35	$790	Net income (loss)

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Note 4 – Investments

Investments consist of municipal bonds, corporate bonds and certificates of deposit. All short-term investments are classified as available-for-sale. Other long-term investments consist of the Company's ownership interest in Lextar Electronics Corporation.

The following tables summarize short-term investments (in thousands):

	March 27, 2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Municipal bonds	$188,312	$2,563	($50)	$190,825
Corporate bonds	163,898	1,976	(311)	165,563
U.S. certificates of deposit	3,500	—	—	3,500
Non-U.S. certificates of deposit	145,000	—	—	145,000
Total short-term investments	$500,710	$4,539	($361)	$504,888

	June 28, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Municipal bonds	$194,123	$988	($341)	$194,770
Corporate bonds	152,831	832	(158)	153,505
U.S. certificates of deposit	—	—	—	—
Non-U.S. certificates of deposit	225,206	—	—	225,206
Total short-term investments	$572,160	$1,820	($499)	$573,481

The following tables present the gross unrealized losses and estimated fair value of the Company's short-term investments, aggregated by investment type and the length of time that individual securities have been in a continuous unrealized loss position (in thousands, except numbers of securities):

	March 27, 2016					
	Less than 12 Months		Greater than 12 Months		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Municipal bonds	$12,447	($35)	$5,286	($15)	$17,733	($50)
Corporate bonds	49,798	(311)	—	—	49,798	(311)
Total	$62,245	($346)	$5,286	($15)	$67,531	($361)
Number of securities with an unrealized loss		37		2		39

	June 28, 2015					
	Less than 12 Months		Greater than 12 Months		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Municipal bonds	$53,204	($341)	$—	$—	$53,204	($341)
Corporate bonds	46,636	(143)	1,812	(15)	48,448	(158)
Total	$99,840	($484)	$1,812	($15)	$101,652	($499)
Number of securities with an unrealized loss		54		1		55

The Company utilizes specific identification in computing realized gains and losses on the sale of investments. Realized gains and losses from the sale of investments are included in Non-operating income (expense), net in the Consolidated Statements of Income (Loss) and unrealized gains and losses are included as a separate component of equity, net of tax, unless the loss is

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determined to be other-than-temporary.
The Company evaluates its investments for possible impairment or a decline in fair value below cost basis that is deemed to be other-than-temporary on a periodic basis. It considers such factors as the length of time and extent to which the fair value has been below the cost basis, the financial condition of the investee, and its ability and intent to hold the investment for a period of time that may be sufficient for an anticipated full recovery in market value. Accordingly, the Company considered declines in its investments to be temporary in nature, and did not consider its securities to be impaired as of March 27, 2016 and June 28, 2015.
The contractual maturities of short-term investments as of March 27, 2016 were as follows (in thousands):

	Within One Year	After One, Within Five Years	After Five, Within Ten Years	After Ten Years	Total
Municipal bonds	$26,540	$130,981	$33,305	$—	$190,826
Corporate bonds	25,267	104,509	35,786	—	165,562
U.S. certificates of deposit	—	3,500	—	—	3,500
Non-U.S. certificates of deposit	145,000	—	—	—	145,000
Total short-term investments	$196,807	$238,990	$69,091	$—	$504,888

Note 5 – Fair Value of Financial Instruments
Under U.S. GAAP, fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (i.e., the exit price) in an orderly transaction between market participants at the measurement date. In determining fair value, the Company uses various valuation approaches, including quoted market prices and discounted cash flows. U.S. GAAP also establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are obtained from independent sources and can be validated by a third party, whereas unobservable inputs reflect assumptions regarding what a third party would use in pricing an asset or liability. The fair value hierarchy is categorized into three levels based on the reliability of inputs as follows:

- Level 1 - Valuations based on quoted prices in active markets for identical instruments that the Company is able to access. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these products does not entail a significant degree of judgment.
- Level 2 - Valuations based on quoted prices in active markets for instruments that are similar, or quoted prices in markets that are not active for identical or similar instruments, and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets.
- Level 3 - Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

The financial assets for which the Company performs recurring fair value remeasurements are cash equivalents, short-term investments and long-term investments. As of March 27, 2016, financial assets utilizing Level 1 inputs included money market funds, and financial assets utilizing Level 2 inputs included municipal bonds, corporate bonds, certificates of deposit, and common stock of non-U.S. corporations. Level 2 assets are valued based on quoted prices in active markets for instruments that are similar or using a third-party pricing service's consensus price, which is a weighted average price based on multiple sources. These sources determine prices utilizing market income models which factor in, where applicable, transactions of similar assets in active markets, transactions of identical assets in infrequent markets, interest rates, bond or credit default swap spreads and volatility. The Company did not have any financial assets requiring the use of Level 3 inputs as of March 27, 2016. There were no transfers between Level 1 and Level 2 during the nine months ended March 27, 2016.

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The following table sets forth financial instruments carried at fair value within the U.S. GAAP hierarchy (in thousands):

	March 27, 2016				June 28, 2015			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Assets:								
Cash equivalents:								
U.S. agency securities	$—	$—	$—	$—	$—	$—	$—	$—
Non-U.S. certificates of deposit	—	3,605	—	3,605	—	157	—	157
Money market funds	1,347	—	—	1,347	16,457	—	—	16,457
Total cash equivalents	1,347	3,605	—	4,952	16,457	157	—	16,614
Short-term investments:								
Municipal bonds	—	190,825	—	190,825	—	194,770	—	194,770
Corporate bonds	—	165,563	—	165,563	—	153,505	—	153,505
U.S. certificates of deposit	—	3,500	—	3,500	—	—	—	—
Non-U.S. certificates of deposit	—	145,000	—	145,000	—	225,206	—	225,206
Total short-term investments	—	504,888	—	504,888	—	573,481	—	573,481
Other long-term investments:								
Common stock of non-U.S. corporations	—	41,661	—	41,661	—	57,595	—	57,595
Total other long-term investments	—	41,661	—	41,661	—	57,595	—	57,595
Total assets	$1,347	$550,154	$—	$551,501	$16,457	$631,233	$—	$647,690

Note 6 – Intangible Assets

Intangible Assets, net

The following table presents the components of intangible assets, net (in thousands):

	March 27, 2016			June 28, 2015		
	Gross	Accumulated Amortization	Net	Gross	Accumulated Amortization	Net
Intangible assets with finite lives:						
Customer relationships	$141,420	($76,871)	$64,549	$136,920	($72,063)	$64,857
Developed technology	174,163	(106,399)	67,764	162,760	(91,562)	71,198
In-process research and development	7,565	(270)	7,295	—	—	—
Non-compete agreements	10,475	(9,485)	990	10,244	(7,958)	2,286
Trade names, finite-lived	520	(520)	—	520	(520)	—
Patent and licensing rights	153,462	(63,821)	89,641	150,038	(57,330)	92,708
Total intangible assets with finite lives	487,605	(257,366)	230,239	460,482	(229,433)	231,049
Trade names, indefinite-lived	79,680		79,680	79,680		79,680
Total intangible assets	$567,285	($257,366)	$309,919	$540,162	($229,433)	$310,729

For the three and nine months ended March 27, 2016, total amortization of finite-lived intangible assets was $10.2 million and $29.9 million, respectively. For the three and nine months ended March 29, 2015, total amortization of finite-lived intangible assets was $9.3 million and $27.7 million, respectively. During the quarter ended March 27, 2016, the Company started amortizing IPR&D assets acquired in the APEI acquisition that were completed during the quarter.

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Total future amortization expense of finite-lived intangible assets is estimated to be as follows (in thousands):

Fiscal Year Ending	
June 26, 2016 (remainder of fiscal 2016)	$9,929
June 25, 2017	37,836
June 24, 2018	36,605
June 30, 2019	23,878
June 28, 2020	18,732
Thereafter	103,259
Total future amortization expense	$230,239

Goodwill

Goodwill assigned to the Power and RF Products reporting unit increased by $2.5 million during the nine months ended March 27, 2016 due to the acquisition of APEI, as discussed in Note 2, "Acquisition."

Note 7 – Long-term Debt

As of March 27, 2016, the Company had a $500 million secured revolving line of credit under which the Company can borrow, repay and reborrow loans from time to time prior to its scheduled maturity date of January 9, 2020. The Company classifies balances outstanding under its line of credit as long-term debt in the consolidated balance sheets. At March 27, 2016, the Company had $225 million outstanding under the line of credit and $275 million available for borrowing. For the three and nine months ended March 27, 2016, the average interest rate was 1.21% and 1.07%, respectively. For the three and nine months ended March 27, 2016 the average commitment fee percentage was 0.09%. The Company was in compliance with all covenants in the line of credit at March 27, 2016.

Note 8 – Shareholders' Equity

As of March 27, 2016, pursuant to an approval by the Board of Directors, the Company is authorized to repurchase shares of its common stock having an aggregate purchase price not exceeding $500 million for all purchases from June 29, 2015 through the expiration of the program on June 26, 2016. During the nine months ended March 27, 2016, the Company repurchased 5.8 million shares of common stock for $149.6 million under the stock repurchase program.

Note 9 – Earnings (Loss) Per Share

The following table presents the computation of basic earnings (loss) per share (in thousands, except per share amounts):

	Three Months Ended		Nine Months Ended	
	March 27, 2016	March 29, 2015	March 27, 2016	March 29, 2015
Net income (loss)	$152	$476	($10,895)	$23,408
Weighted average common shares	100,606	110,662	102,157	115,177
Basic earnings (loss) per share	$—	$—	($0.11)	$0.20

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The following computation reconciles the differences between the basic and diluted earnings (loss) per share presentations (in thousands, except per share amounts):

	Three Months Ended		Nine Months Ended	
	March 27, 2016	March 29, 2015	March 27, 2016	March 29, 2015
Net income (loss)	$152	$476	($10,895)	$23,408
Weighted average common shares - basic	100,606	110,662	102,157	115,177
Dilutive effect of stock options, nonvested shares and Employee Stock Purchase Plan purchase rights	615	928	—	1,127
Weighted average common shares - diluted	101,221	111,590	102,157	116,304
Diluted earnings (loss) per share	$—	$—	($0.11)	$0.20

Potential common shares that would have the effect of increasing diluted earnings per share or decreasing diluted loss per share are considered to be anti-dilutive and as such, these shares are not included in calculating diluted earnings per share. For the three and nine months ended March 27, 2016, there were 10.2 million and 11.5 million, respectively, of potential common shares not included in the calculation of diluted earnings (loss) per share because their effect was anti-dilutive. For the three and nine months ended March 29, 2015, there were 7.7 million and 6.8 million, respectively, of potential common shares not included in the calculation of diluted earnings (loss) per share because their effect was anti-dilutive.

Note 10 – Stock-Based Compensation

Overview of Employee Stock-Based Compensation Plans

The Company currently has one equity-based compensation plan, the 2013 Long-Term Incentive Compensation Plan (2013 LTIP), from which stock-based compensation awards can be granted to employees and directors. The 2013 LTIP provides for awards in the form of incentive stock options, non-qualified stock options, stock appreciation rights, restricted stock, restricted stock units, performance shares, performance units and other awards. The Company has other equity-based compensation plans that have been terminated so that no future grants can be made under those plans, but under which stock options, restricted stock and restricted stock units are currently outstanding.

The Company’s stock-based awards can be either service-based or performance-based. Performance-based conditions are generally tied to future financial and/or operating performance of the Company. The compensation expense with respect to performance-based grants is recognized if the Company believes it is probable that the performance condition will be achieved. The Company reassesses the probability of the achievement of the performance condition at each reporting period, and adjusts the compensation expense for subsequent changes in the estimate or actual outcome. As with non-performance based awards, compensation expense is recognized over the vesting period. The vesting period runs from the date of grant to the expected date that the performance objective is likely to be achieved.

The Company also has an Employee Stock Purchase Plan (ESPP) that provides employees with the opportunity to purchase common stock at a discount. The ESPP limits employee contributions to 15% of each employee’s compensation (as defined in the plan) and allows employees to purchase shares at a 15% discount to the fair market value of common stock on the purchase date two times per year. The ESPP provides for a twelve-month participation period, divided into two equal six-month purchase periods, and also provides for a look-back feature. At the end of each six-month period in April and October, participants purchase the Company’s common stock through the ESPP at a 15% discount to the fair market value of the common stock on the first day of the twelve-month participation period or the purchase date, whichever is lower. The plan also provides for an automatic reset feature to start participants on a new twelve-month participation period if the fair market value of common stock declines during the first six-month purchase period.

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Stock Option Awards

The following table summarizes stock option awards outstanding as of March 27, 2016 and changes during the nine months then ended (numbers of shares in thousands):

	Number of Shares	Weighted Average Exercise Price
Outstanding at June 28, 2015	10,714	$43.10
Granted	1,969	$26.13
Exercised	(250)	$25.30
Forfeited or expired	(976)	$43.62
Outstanding at March 27, 2016	11,457	$40.53

Restricted Stock Awards and Units

A summary of nonvested restricted stock awards (RSAs) and restricted stock unit awards (RSUs) outstanding as of March 27, 2016, and changes during the nine months then ended is as follows (numbers of awards and units in thousands):

	Number of RSAs/RSUs	Weighted Average Grant-Date Fair Value
Nonvested at June 28, 2015	926	$45.47
Granted	1,179	$26.10
Vested	(348)	$45.00
Forfeited	(142)	$41.83
Nonvested at March 27, 2016	1,615	$31.75

Stock-Based Compensation Valuation and Expense

The Company accounts for its employee stock-based compensation plans using the fair value method. The fair value method requires the Company to estimate the grant-date fair value of its stock-based awards and amortize this fair value to compensation expense over the requisite service period or vesting term.

The Company uses the Black-Scholes option-pricing model to estimate the fair value of the Company’s stock option and ESPP awards. The determination of the fair value of stock-based payment awards on the date of grant using an option-pricing model is affected by the Company’s stock price as well as assumptions regarding a number of complex and subjective variables. These variables include the expected stock price volatility over the term of the awards, actual and projected employee stock option exercise behaviors, the risk-free interest rate and expected dividends. Due to the inherent limitations of option-valuation models, future events that are unpredictable and the estimation process utilized in determining the valuation of the stock-based awards, the ultimate value realized by award holders may vary significantly from the amounts expensed in the Company’s financial statements.

For RSAs and RSUs, the grant-date fair value is based upon the market price of the Company’s common stock on the date of the grant. This fair value is then amortized to compensation expense over the requisite service period or vesting term.

Stock-based compensation expense is recognized net of estimated forfeitures such that expense is recognized only for those stock-based awards that are expected to vest. A forfeiture rate is estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from initial estimates.

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Total stock-based compensation expense was as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	March 27, 2016	March 29, 2015	March 27, 2016	March 29, 2015
Income Statement Classification:				
Cost of revenue, net	$3,078	$3,158	$9,226	$9,511
Research and development	3,694	4,212	10,554	12,795
Sales, general and administrative	8,084	8,694	24,538	26,954
Total stock-based compensation expense	$14,856	$16,064	$44,318	$49,260

Note 11 – Income Taxes

The variation between the Company's effective income tax rate and the U.S. statutory rate of 35% is due to the impact of the Company’s pre-tax income or loss relative to favorable tax rate impacts associated predominantly with the Company’s: (i) projected income for the full year derived from international locations with lower tax rates than the U.S. and (ii) projected tax credits generated. Tax credits and other deductions have the impact of increasing the tax rate above the statutory rate of 35% in periods in which the Company reports pre-tax losses as they provide a benefit that is recoverable in future periods.

U.S. GAAP requires a two-step approach to recognizing and measuring uncertain tax positions. 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 cumulatively more than 50% likely to be realized upon ultimate settlement.

As of June 28, 2015, the Company's liability for unrecognized tax benefits was $17.8 million. During the nine months ended March 27, 2016, the Company recognized a $0.6 million increase to the liability for unrecognized tax benefits due to uncertainty regarding intercompany transactions recently challenged by the Italian tax authority. In addition, there was a $0.1 million decrease to the amount of unrecognized tax benefits following statute expirations. As a result, the total liability for unrecognized tax benefits as of March 27, 2016 was $18.3 million. If any portion of this $18.3 million is recognized, the Company will then include that portion in the computation of its effective tax rate. Although the ultimate timing of the resolution and/or closure of audits is highly uncertain, the Company believes it is reasonably possible that $4.3 million of gross unrecognized tax benefits will change in the next 12 months as a result of audit closures and statute requirements.

The Company files U.S. federal, U.S. state and foreign tax returns. For U.S. federal purposes, the Company is generally no longer subject to tax examinations for fiscal years prior to 2013. For U.S. state tax returns, the Company is generally no longer subject to tax examinations for fiscal years prior to 2012. For foreign purposes, the Company is generally no longer subject to tax examinations for tax periods 2005 and prior. Certain carryforward tax attributes generated in prior years remain subject to examination, adjustment and recapture. The Company is currently under audit by the Italian Revenue Agency for the fiscal year ended June 30, 2013.

During the three months ended September 27, 2015, the Company concluded that it is likely that $2.3 million of North Carolina income tax credits will expire unused. As a result, during that period, the Company recorded a $1.5 million valuation allowance against the related deferred tax asset, representing the $2.3 million expiring credits net of federal benefit. During the three months ended March 27, 2016, the Company concluded that it is likely an additional $0.6 million of North Carolina income tax credits will expire unused. The Company increased the valuation allowance against the related deferred tax asset by $0.4 million, representing the $0.6 million expiring tax credits net of federal benefit, resulting in an additional $0.4 million of income tax expense during the three months ended March 27, 2016.

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Note 12 – Commitments and Contingencies

Warranties

The following table summarizes the changes in the Company's product warranty liabilities (in thousands):

Balance at June 28, 2015	$13,968
Warranties accrued in current period	13,105
Recall costs accrued in current period	423
Expenditures	(12,069)
Balance at March 27, 2016	$15,427

Product warranties are estimated and recognized at the time the Company recognizes revenue. The warranty periods range from 90 days to 10 years. The Company accrues warranty liabilities at the time of sale, based on historical and projected incident rates and expected future warranty costs. The Company accrues estimated costs related to product recalls based on a formal campaign soliciting repair or return of that product when they are deemed probable and reasonably estimable. The warranty reserves, which are primarily related to Lighting Products, are evaluated quarterly based on various factors including historical warranty claims, assumptions about the frequency of warranty claims, and assumptions about the frequency of product failures derived from quality testing, field monitoring and the Company's reliability estimates. As of March 27, 2016, $1.3 million of the Company's product warranty liabilities were classified as long-term.

In June 2015, the Company issued a voluntary recall of its linear LED T8 replacement lamps due to the hazard of overheating and melting. The Company expects the majority of the costs of the recall to be recoverable from insurance proceeds resulting in an immaterial impact to the Company’s financial results.

Litigation

The Company is currently a party to various legal proceedings. While management presently believes that the ultimate outcome of such proceedings, individually and in the aggregate, will not materially harm the Company’s financial position, cash flows, or overall trends in results of operations, legal proceedings are subject to inherent uncertainties, and unfavorable rulings could occur. An unfavorable ruling could include money damages or, in matters for which injunctive relief or other conduct remedies may be sought, an injunction prohibiting the Company from selling one or more products at all or in particular ways. Were unfavorable final outcomes to occur, there exists the possibility of a material adverse impact on the Company’s business, results of operation, financial position and overall trends. The outcomes in these matters are not reasonably estimable.

Note 13 – Reportable Segments

The Company's operating and reportable segments are:

- Lighting Products
- LED Products
- Power and RF Products

Reportable Segments Description

The Company's Lighting Products segment primarily consists of LED lighting systems and bulbs. The Company's LED Products segment includes LED chips, LED components and SiC materials. The Company's Power and RF Products segment includes power devices and RF devices.

Financial Results by Reportable Segment

The table below reflects the results of the Company's reportable segments as reviewed by the Chief Operating Decision Maker (CODM) for the three and nine months ended March 27, 2016 and March 29, 2015. The Company's CODM is the Chief Executive Officer. The Company used the same accounting policies to derive the segment results reported below as those used in the Company's consolidated financial statements.

The Company's CODM does not review inter-segment transactions when evaluating segment performance and allocating resources to each segment, and inter-segment transactions are not included in the segment revenue presented in the table below. As such, total segment revenue in the table below is equal to the Company's consolidated revenue.

The Company's CODM reviews gross profit as the lowest and only level of segment profit. As such, all items below gross profit

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in the Consolidated Statements of Income (Loss) must be included to reconcile the consolidated gross profit presented in the table below to the Company's consolidated (loss) income before income taxes.

In order to determine gross profit for each reportable segment, the Company allocates direct costs and indirect costs to each segment's cost of revenue. The Company allocates indirect costs, such as employee benefits for manufacturing employees, shared facilities services, information technology, purchasing, and customer service, when the costs are identifiable and beneficial to the reportable segment. The Company allocates these indirect costs based on a reasonable measure of utilization that considers the specific facts and circumstances of the costs being allocated.

Unallocated costs in the table below consisted primarily of manufacturing employees' stock-based compensation, expenses for profit sharing and quarterly or annual incentive plans and matching contributions under the Company's 401(k) plan. These costs were not allocated to the reportable segments' gross profit because the Company's CODM does not review them regularly when evaluating segment performance and allocating resources.

Revenue, gross profit and gross margin for each of the Company's segments were as follows (in thousands, except percentages):

	Three Months Ended		Nine Months Ended	
	March 27, 2016	March 29, 2015	March 27, 2016	March 29, 2015
Revenue:				
Lighting Products revenue	$187,714	$224,109	$690,715	$677,363
LED Products revenue	150,189	154,384	451,759	479,851
Power and RF Products revenue	29,016	31,026	85,740	93,134
Total revenue	$366,919	$409,519	$1,228,214	$1,250,348
Gross Profit and Gross Margin:				
Lighting Products gross profit	$48,808	$58,315	$190,531	$178,608
Lighting Products gross margin	26.0 %	26.0 %	27.6 %	26.4 %
LED Products gross profit	52,102	55,358	156,489	182,406
LED Products gross margin	34.7 %	35.9 %	34.6 %	38.0 %
Power and RF Products gross profit	13,477	16,484	42,146	51,601
Power and RF Products gross margin	46.4 %	53.1 %	49.2 %	55.4 %
Total segment gross profit	114,387	130,157	389,166	412,615
Unallocated costs	(5,354)	(5,009)	(15,115)	(15,386)
Consolidated gross profit	$109,033	$125,148	$374,051	$397,229
Consolidated gross margin	29.7 %	30.6 %	30.5 %	31.8 %

Assets by Reportable Segment

Inventories are the only assets reviewed by the Company's CODM when evaluating segment performance and allocating resources to the segments. The CODM reviews all of the Company's assets other than inventories on a consolidated basis.

Unallocated inventories in the table below were not allocated to the reportable segments because the Company's CODM does not review them when evaluating performance and allocating resources to each segment. Unallocated inventories consisted primarily of manufacturing employees' stock-based compensation, profit sharing and quarterly or annual incentive compensation and matching contributions under the Company's 401(k) plan.

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Inventories for each of the Company's segments were as follows (in thousands):

	March 27, 2016	June 28, 2015
Lighting Products	$168,347	$150,755
LED Products	107,480	114,203
Power and RF Products	18,102	11,536
Total segment inventories	293,929	276,494
Unallocated inventories	3,931	4,082
Consolidated inventories	$297,860	$280,576

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Note 14 - Costs Associated with LED Business Restructuring

In June 2015, the Company's Board of Directors approved a plan to restructure the LED Products business. The restructuring reduced excess capacity and overhead in order to improve the cost structure moving forward. The primary components of the restructuring include the planned sale or abandonment of certain manufacturing equipment, facility consolidation and the elimination of certain positions. The restructuring activity ended in the second quarter of fiscal 2016. While no charges were incurred for the three months ended March 27, 2016, the Company did realize a $1.1 million gain of the sale of long-lived assets related to the restructuring which were sold for a value in excess of their estimated net realizable value.

The following table summarizes the actual and planned charges incurred through March 27, 2016 (in thousands):

Capacity and Overhead Cost Reductions	Estimated charges	Amounts incurred during the nine months ended March 27, 2016	Cumulative amounts incurred through March 27, 2016	Affected Line Item in the Consolidated Statements of Income (Loss)
Loss on disposal or impairment of long-lived assets	$57,651	$15,519	$57,651	Loss on disposal or impairment of long-lived assets
Severance expense	2,283	264	2,283	Sales, general and administrative expenses
Lease termination and facility consolidation costs	4,762	2,933	4,762	Sales, general and administrative expenses
Increase in channel inventory reserves	26,479	—	26,479	Revenue, net
Increase in inventory reserves	11,091	—	11,091	Cost of revenue, net
Total restructuring charges	$102,266	$18,716	$102,266	

The following table presents the changes in the severance liability under the LED Products restructuring plan (in thousands):

Severance liability at June 28, 2015	$2,019
Severance expense	264
Severance payments	(2,283)
Severance liability at March 27, 2016	$—

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Information set forth in this Quarterly Report on Form 10-Q contains various "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended (the Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). All information contained in this report relative to future markets for our products and trends in and anticipated levels of revenue, gross margins and expenses, as well as other statements containing words such as "believe," "project," "may," "will," "anticipate," "target," "plan," "estimate," "expe "intend" and other similar expressions constitute forward-looking statements. These forward-looking statements are subject to business, economic and other risks and uncertainties, both known and unknown, and actual results may differ materially from those contained in the forward-looking statements. Any forward-looking statements we make are as of the date made, and except as required under the U.S. federal securities laws and the rules and regulations of the Securities and Exchange Commission (the SEC), we have no duty to update them if our views later change. These forward-looking statements should not be relied upon as representing our views as of any date subsequent to the date of this Quarterly Report. Examples of risks and uncertainties that could cause actual results to differ materially from historical performance and any forward-looking statements include, but are not limited to, those described in "Risk Factors" in Part II, Item 1A of this Quarterly Report.

Executive Summary

The following discussion is designed to provide a better understanding of our unaudited consolidated financial statements, including a brief discussion of our business and products, key factors that impacted our performance and a summary of our operating results. The following discussion should be read in conjunction with the unaudited condensed consolidated financial statements and the notes thereto included in Part I, Item 1 of this Quarterly Report on Form 10-Q, and the consolidated financial statements and notes thereto and Management’s Discussion and Analysis of Financial Condition and Results of Operations contained in our Annual Report on Form 10-K for the fiscal year ended June 28, 2015. Historical results and percentage relationships among any amounts in the financial statements are not necessarily indicative of trends in operating results for any future periods.

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Overview

Cree, Inc. (Cree, we, our, or us) is a leading innovator of lighting-class light emitting diode (LED) products, lighting products and wide bandgap semiconductor products for power and radio-frequency (RF) applications. Our products are targeted for applications such as indoor and outdoor lighting, video displays, transportation, electronic signs and signals, power supplies, inverters and wireless systems.

Our lighting products primarily consist of LED lighting systems and bulbs. We design, manufacture and sell lighting fixtures and lamps for the commercial, industrial and consumer markets.

Our LED products consist of LED components, LED chips, and silicon carbide (SiC) materials. Our success in selling LED products depends upon our ability to offer innovative products and to enable our customers to develop and market LED-based products that successfully compete against other LED-based products and traditional lighting products.

In addition, we develop, manufacture and sell power and RF devices based on wide bandgap semiconductor materials such as SiC and gallium nitride (GaN). As previously announced, we have filed a confidential registration statement for an initial public offering to take this business public under the name Wolfspeed, Inc. (Wolfspeed). This initial public offering is dependent upon many factors, and may not occur on favorable terms or at all. Our power products are made from SiC and provide increased efficiency, faster switching speeds and reduced system size and weight over comparable silicon-based power devices. Our RF devices are made from GaN and provide improved efficiency, bandwidth and frequency of operation as compared to silicon or gallium arsenide (GaAs).

The majority of our products are manufactured at our production facilities located in North Carolina, Wisconsin, and China. We also use contract manufacturers for certain products and aspects of product fabrication, assembly and packaging. We operate research and development facilities in North Carolina, California, Wisconsin, India, and China (including Hong Kong).

Cree, Inc. is a North Carolina corporation established in 1987, and our headquarters are in Durham, North Carolina.

For further information about our consolidated revenue and earnings, please see our consolidated financial statements included in Item 1 of this Quarterly Report.

Reportable Segments

Our three reportable segments are:

- Lighting Products
- LED Products
- Power and RF Products

For further information about our reportable segments, please refer to Note 13, "Reportable Segments," in our consolidated financial statements included in Item 1 of this Quarterly Report.

Industry Dynamics and Trends

There are a number of industry factors that affect our business which include, among others:

- Overall Demand for Products and Applications using LEDs. Our potential for growth depends significantly on the adoption of LEDs within the general lighting market and our ability to affect this rate of adoption. Although the market for LED lighting has grown in recent years, adoption of LEDs for general lighting is still in the relatively early stages. Demand also fluctuates based on various market cycles, a continuously evolving LED industry supply chain, and evolving competitive dynamics in the market. These uncertainties make demand difficult to forecast for us and our customers.
- Intense and Constantly Evolving Competitive Environment. Competition in the LED and lighting industries is intense. Many companies have made significant investments in LED development and production equipment. Traditional lighting companies and new entrants are investing in LED-based lighting products as LED adoption has gained momentum. Traditional lighting companies have taken steps to limit access to their sales channels, including lighting agents and distributors. Product pricing pressures exist as market participants often undertake pricing strategies to gain or protect market share, increase the utilization of their production capacity and open new applications to LED-based solutions. To remain competitive, market participants must continuously increase product performance and reduce costs. To address these competitive pressures, we have invested in research and development activities to support new product development and to deliver higher levels of performance and lower costs to

differentiate our products in the market.

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- Technological Innovation and Advancement. Innovations and advancements in lighting, LED, power and RF technologies continue to expand the potential commercial application for our products, particularly in the general illumination, power electronics and wireless markets. However, new technologies or standards could emerge or improvements could be made in existing technologies that could reduce or limit the demand for our products in certain markets.
- Regulatory Standards Concerning Energy Efficiency. Government agencies are involved in setting standards for energy efficient lighting, which can affect market acceptance and the availability of rebates from government agencies or third parties such as utilities. While this trend is generally positive, these regulations are affected by changing political priorities and evolving technical standards which can modify or limit the effectiveness of these new regulations.
- Intellectual Property Issues. Market participants rely on patented and non-patented proprietary information relating to product development, manufacturing capabilities and other core competencies of their business. Protection of intellectual property is critical. Therefore, steps such as additional patent applications, confidentiality and non-disclosure agreements, as well as other security measures are generally taken. To enforce or protect intellectual property rights, litigation or threatened litigation is common.

Overview of the Nine Months Ended March 27, 2016

The following is a summary of our financial results for the nine months ended March 27, 2016:

- Revenue decreased to $1.23 billion for the nine months ended March 27, 2016 from $1.25 billion for the nine months ended March 29, 2015.
- Gross profit decreased to $374 million for the nine months ended March 27, 2016 from $397 million for the nine months ended March 29, 2015. Gross margin declined to 30.5% for the nine months ended March 27, 2016 from 32% for the nine months ended March 29, 2015.
- Operating loss was $6 million for the nine months ended March 27, 2016 compared to operating income of $22 million for the nine months ended March 29, 2015. Net loss per diluted share was $0.11 for the nine months ended March 27, 2016 compared to net income per diluted share of $0.20 for the nine months ended March 29, 2015.
- Cash, cash equivalents and short-term investments decreased to $0.6 billion at March 27, 2016 compared to $0.7 billion at June 28, 2015. Cash provided by operating activities was $139 million for the nine months ended March 27, 2016 compared to $94 million for the nine months ended March 29, 2015.
- Inventories increased to $298 million at March 27, 2016 compared to $281 million at June 28, 2015.
- Purchases of property and equipment were $100 million for the nine months ended March 27, 2016 compared to $158 million for the nine months ended March 29, 2015.

Business Outlook

We continue to project that the markets for our products will expand, but remain highly competitive through the remainder of calendar 2016. We anticipate focusing on the following key areas, among others, to position the Company to take advantage of the growing market opportunities while responding to this competitive environment:

- Build financial momentum. We are focused on driving improved financial results in our fourth quarter and beyond. The key components are:
- grow our commercial Lighting business and improve product margins by improving execution and new product momentum;
- deliver LED results in a similar range to the third quarter of fiscal 2016;
- expand our Power and RF business; and
- manage our operating expenses to improve operating leverage.
- Innovate to continue to lead in each of our business segments. We have established ourselves as the innovation leader in Lighting, LEDs and wide bandgap Power and RF. We are focused on continuing to develop new products that deliver fundamentally more value to drive new customer demand and build our brand.

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- Promote future growth in Power and RF. Our Wolfspeed business filed a confidential registration statement for an initial public offering to raise capital to support the business's targeted future growth. We believe that such a transaction would allow Cree shareholders to better realize the full value of both businesses. This initial public offering is dependent upon many factors, and may not occur on favorable terms or at all.

Results of Operations

The following table sets forth certain consolidated statement of income (loss) data for the periods indicated (in thousands, except per share amounts and percentages):

	Three Months Ended				Nine Months Ended			
	March 27, 2016		March 29, 2015		March 27, 2016		March 29, 2015	
	Dollars	% of Revenue	Dollars	% of Revenue	Dollars	% of Revenue	Dollars	% of Revenue
Revenue, net	$366,919	100 %	$409,519	100 %	$1,228,214	100 %	$1,250,348	100 %
Cost of revenue, net	257,886	70 %	284,371	69 %	854,163	70 %	853,119	68 %
Gross profit	109,033	30 %	125,148	31 %	374,051	30 %	397,229	32 %
Research and development	41,871	11 %	43,823	11 %	127,363	10 %	137,537	11 %
Sales, general and administrative	64,489	18 %	71,860	18 %	214,443	17 %	213,927	17 %
Amortization or impairment of acquisition-related intangibles	7,318	2 %	6,749	2 %	21,442	2 %	19,743	2 %
(Gain) loss on disposal or impairment of long-lived assets	(104)	— %	1,459	— %	16,483	1 %	3,641	— %
Operating (loss) income	(4,541)	(1)%	1,257	— %	(5,680)	— %	22,381	2 %
Non-operating income (expense), net	717	— %	(866)	— %	(14,075)	(1)%	3,766	— %
(Loss) income before income taxes	(3,824)	(1)%	391	— %	(19,755)	(2)%	26,147	2 %
Income tax (benefit) expense	(3,976)	(1)%	(85)	— %	(8,860)	(1)%	2,739	— %
Net income (loss)	$152	— %	$476	— %	($10,895)	(1)%	$23,408	2 %
Basic earnings (loss) per share	$—		$—		($0.11)		$0.20	
Diluted earnings (loss) per share	$—		$—		($0.11)		$0.20	

LED Business Restructuring

In June 2015, our Board of Directors approved a plan to restructure the LED Products business. The restructuring reduced excess capacity and overhead in order to improve the cost structure moving forward. The primary components of the restructuring include the planned sale or abandonment of certain manufacturing equipment, facility consolidation and the elimination of certain positions. The restructuring activity ended in the second quarter of fiscal 2016. While no charges were incurred for the three months ended March 27, 2016, the Company did realize a $1.1 million gain of the sale of long-lived assets related to the restructuring which were sold for a value in excess of their estimated net realizable value.

The following table summarizes the actual and planned charges incurred through March 27, 2016 (in thousands):

Capacity and Overhead Cost Reductions	Estimated charges	Amounts incurred during the nine months ended March 27, 2016	Cumulative amounts incurred through March 27, 2016	Affected Line Item in the Consolidated Statements of Income (Loss)

Loss on disposal or impairment of long-lived assets	$57,651	$15,519	$57,651	Loss on disposal or impairment of long-lived assets
Severance expense	2,283	264	2,283	Sales, general and administrative expenses
Lease termination and facility consolidation costs	4,762	2,933	4,762	Sales, general and administrative expenses
Increase in channel inventory reserves	26,479	—	26,479	Revenue, net
Increase in inventory reserves	11,091	—	11,091	Cost of revenue, net
Total restructuring charges	$102,266	$18,716	$102,266	

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Revenue

Revenue was comprised of the following (in thousands, except percentages):

	Three Months Ended				Nine Months Ended			
	March 27, 2016	March 29, 2015	Change		March 27, 2016	March 29, 2015	Change	
Lighting Products revenue	$187,714	$224,109	($36,395)	(16)%	$690,715	$677,363	$13,352	2 %
Percent of revenue	51 %	55 %			56 %	54 %		
LED Products revenue	150,189	154,384	(4,195)	(3)%	451,759	479,851	(28,092)	(6)%
Percent of revenue	41 %	38 %			37 %	38 %		
Power and RF Products revenue	29,016	31,026	(2,010)	(6)%	85,740	93,134	(7,394)	(8)%
Percent of revenue	8 %	7 %			7 %	8 %		
Total revenue	$366,919	$409,519	($42,600)	(10)%	$1,228,214	$1,250,348	($22,134)	(2)%

Our consolidated revenue decreased 10% to $366.9 million for the three months ended March 27, 2016 from $409.5 million for the three months ended March 29, 2015. This decrease was driven by the 16% decrease in Lighting Products revenue, the 3% decrease in LED Products revenue and the 6% decrease in Power and RF Products revenue. For the nine months ended March 27, 2016, our consolidated revenue decreased 2% to $1.2 billion from $1.3 billion for the nine months ended March 29, 2015. This decrease was driven by the 6% decrease in LED Products revenue and the 8% decrease in Power and RF Products revenue partially offset by the 2% increase in Lighting Products revenue.

Lighting Products Segment Revenue

Lighting Products revenue represented approximately 51% and 55% of our total revenue for the three months ended March 27, 2016 and March 29, 2015, respectively.

Lighting Products revenue decreased 16% to $187.7 million for the three months ended March 27, 2016 from $224.1 million for the three months ended March 29, 2015 and increased 2% to $690.7 million for the nine months ended March 27, 2016 from $677.4 million for the nine months ended March 29, 2015. The decrease in revenue for the three months ended March 27, 2016 compared to the three months ended March 29, 2015 was due to a 32% decrease in the number of units sold, partially offset by a 22% increase in Average Selling Price (ASP). The increase in revenue for the nine months ended March 27, 2016 compared to the nine months ended March 29, 2015 was due to a 22% increase in ASP, partially offset by a 16% decrease in units sold. The decreases in units sold were primarily the result of lower commercial lighting fixture sales in our fiscal third quarter resulting from customer service disruptions related to our information technology systems conversion, new product delays and a slowdown in the North American retrofit market, as well as a decrease in consumer bulb sales. The increases in ASP were due to the higher mix of commercial lighting fixture sales, which have a higher ASP than our other lighting products.

LED Products Segment Revenue

LED Products revenue represented 41% and 38% of our total revenue for the three months ended March 27, 2016 and March 29, 2015, respectively.

LED Products revenue decreased 3% to $150.2 million for the three months ended March 27, 2016 from $154.4 million for the three months ended March 29, 2015 and decreased 6% to $451.8 million for the nine months ended March 27, 2016 from $479.9 million for the nine months ended March 29, 2015. The decrease in revenue for the three months ended March 27, 2016 compared to the three months ended March 29, 2015 was due to an 18% decrease in ASP, partially offset by an 18% increase in the number of units sold. The decrease in revenue for the nine months ended March 27, 2016 compared to the nine months ended March 29, 2015 was due to a 17% reduction in ASP, partially offset by a 12% increase in the number of units sold. The decreases in ASP were due primarily to increased global competition for LED products which impacted our LED product lines.

Power and RF Products Segment Revenue

Power and RF Products revenue represented approximately 8% and 7% of our total revenue for the three months ended March 27, 2016 and March 29, 2015, respectively.

Power and RF Products revenue decreased 6% to $29.0 million for the three months ended March 27, 2016 from $31.0 million for the three months ended March 29, 2015 and decreased 8% to $85.7 million for the nine months ended March 27, 2016 from $93.1 million for the nine months ended March 29, 2015. The decrease in revenue for the three months ended March 27, 2016 as compared to the three months ended March 29, 2015 was due to a 26% decrease in the number of units sold, partially offset by

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a 16% increase in ASP. The decrease in revenue for the nine months ended March 27, 2016 compared to the nine months ended March 29, 2015 was primarily the result of a 27% decrease in the number of units sold, partially offset by a 15% increase in ASP. The decreases in units sold were primarily the result of a lower number of RF units sold. The increases in ASP were due to an increase in both power and RF product ASP resulting from a greater mix of higher priced power and RF products.

Gross Profit and Gross Margin

Gross profit and gross margin were as follows (in thousands, except percentages):

	Three Months Ended				Nine Months Ended			
	March 27, 2016	March 29, 2015	Change		March 27, 2016	March 29, 2015	Change	
Lighting Products gross profit	$48,808	$58,315	($9,507)	(16)%	$190,531	$178,608	$11,923	7 %
Lighting Products gross margin	26.0 %	26.0 %			27.6 %	26.4 %		
LED Products gross profit	52,102	55,358	(3,256)	(6)%	156,489	182,406	(25,917)	(14)%
LED Products gross margin	34.7 %	35.9 %			34.6 %	38.0 %		