

CADENCE DESIGN SYSTEMS INC

Form 10-Q

July 26, 2012

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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 June 30, 2012

OR

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

For the transition period from            to

Commission file number 000-15867

**CADENCE DESIGN SYSTEMS, INC.**

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(Exact Name of Registrant as Specified in Its Charter)

**Delaware**  
(State or Other Jurisdiction of

**77-0148231**  
(I.R.S. Employer

Incorporation or Organization)

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 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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

Large accelerated filer

Accelerated filer

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

Smaller reporting company

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

On June 30, 2012, 274,894,103 shares of the registrant's common stock, \$0.01 par value, were outstanding.

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**Table of Contents****PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****CADENCE DESIGN SYSTEMS, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS****(In thousands)****(Unaudited)**

	June 30, 2012	December 31, 2011
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 661,658	\$ 601,602
Short-term investments	51,304	3,037
Receivables	123,243	136,772
Inventories	41,066	43,243
2015 Notes Hedges	219,199	215,113
Prepaid expenses and other	61,976	64,216
<b>Total current assets</b>	<b>1,158,446</b>	<b>1,063,983</b>
Property, plant and equipment, net of accumulated depreciation of \$668,328 and \$658,990, respectively	251,920	262,517
Goodwill	192,238	192,125
Acquired intangibles, net of accumulated amortization of \$89,572 and \$91,542, respectively	159,807	173,234
Long-term receivables	7,750	11,371
Other assets	59,096	58,039
<b>Total Assets</b>	<b>\$ 1,829,257</b>	<b>\$ 1,761,269</b>

**LIABILITIES AND STOCKHOLDERS EQUITY**

Current Liabilities:		
Convertible notes	\$ 301,292	\$ 294,061
2015 Notes Embedded Conversion Derivative	219,199	215,113
Accounts payable and accrued liabilities	153,957	165,791
Current portion of deferred revenue	328,405	340,401
<b>Total current liabilities</b>	<b>1,002,853</b>	<b>1,015,366</b>
Long-Term Liabilities:		
Long-term portion of deferred revenue	58,213	73,959
Convertible notes	135,006	131,920
Other long-term liabilities	131,172	128,894
<b>Total long-term liabilities</b>	<b>324,391</b>	<b>334,773</b>

Commitments and Contingencies (Note 12)

Stockholders Equity:

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Common stock and capital in excess of par value	1,741,869	1,733,884
Treasury stock, at cost	(266,820)	(290,462)
Accumulated deficit	(1,018,190)	(1,083,245)
Accumulated other comprehensive income	45,154	50,953
Total stockholders' equity	502,013	411,130
Total Liabilities and Stockholders' Equity	\$ 1,829,257	\$ 1,761,269

See notes to condensed consolidated financial statements.

**Table of Contents****CADENCE DESIGN SYSTEMS, INC.****CONDENSED CONSOLIDATED INCOME STATEMENTS****(In thousands, except per share amounts)****(Unaudited)**

	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
<b>Revenue:</b>				
Product	\$ 208,301	\$ 157,938	\$ 398,325	\$ 299,757
Services	28,966	29,477	58,508	57,282
Maintenance	89,209	95,855	185,473	192,333
<b>Total revenue</b>	<b>326,476</b>	<b>283,270</b>	<b>642,306</b>	<b>549,372</b>
<b>Costs and Expenses:</b>				
Cost of product	21,585	20,074	36,986	34,268
Cost of services	17,071	20,616	36,445	40,691
Cost of maintenance	10,821	10,716	22,632	21,614
Marketing and sales	80,418	77,006	164,213	155,378
Research and development	112,031	99,268	220,625	200,567
General and administrative	30,244	25,377	58,014	44,679
Amortization of acquired intangibles	3,643	4,505	7,429	8,964
Restructuring and other charges (credits)	43	751	(8)	710
<b>Total costs and expenses</b>	<b>275,856</b>	<b>258,313</b>	<b>546,336</b>	<b>506,871</b>
Income from operations	50,620	24,957	95,970	42,501
Interest expense	(8,566)	(10,768)	(17,103)	(21,754)
Other income, net	3,669	8,394	6,103	12,863
Income before provision (benefit) for income taxes	45,723	22,583	84,970	33,610
Provision (benefit) for income taxes	9,337	(4,325)	17,480	379
<b>Net income</b>	<b>\$ 36,386</b>	<b>\$ 26,908</b>	<b>\$ 67,490</b>	<b>\$ 33,231</b>
Basic net income per share	\$ 0.13	\$ 0.10	\$ 0.25	\$ 0.13
Diluted net income per share	\$ 0.13	\$ 0.10	\$ 0.24	\$ 0.12
Weighted average common shares outstanding basic	269,739	263,191	268,840	262,362
Weighted average common shares outstanding diluted	275,318	270,885	276,526	269,732

See notes to condensed consolidated financial statements.



**Table of Contents****CADENCE DESIGN SYSTEMS, INC.****CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME****(In thousands)****(Unaudited)**

	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
Net income	\$ 36,386	\$ 26,908	\$ 67,490	\$ 33,231
Other comprehensive loss, net of tax effects:				
Foreign currency translation loss	(2,366)	5,725	(4,832)	5,605
Changes in unrealized holding gains or losses on available-for-sale securities, net of reclassification adjustment for realized gains and losses	(1,017)	(7,709)	(1,021)	(8,078)
Changes in defined benefit plan liabilities	84	45	54	13
Total other comprehensive loss, net of tax effects	(3,299)	(1,939)	(5,799)	(2,460)
Comprehensive income	\$ 33,087	\$ 24,969	\$ 61,691	\$ 30,771

See notes to condensed consolidated financial statements.



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

	Six Months Ended	
	June 30, 2012	July 2, 2011
Cash and Cash Equivalents at Beginning of Period	\$ 601,602	\$ 557,409
<b>Cash Flows from Operating Activities:</b>		
Net income	67,490	33,231
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	43,736	46,283
Amortization of debt discount and fees	11,529	14,587
Stock-based compensation	21,886	19,698
Gain on investments, net	(4,169)	(13,676)
Non-cash restructuring and other charges	125	136
Deferred income taxes	459	(4,811)
Provisions (recoveries) for losses (gains) on trade and installment contract receivables, net		(5,885)
Other non-cash items	3,439	2,518
Changes in operating assets and liabilities, net of effect of acquired businesses:		
Current and long-term receivables	16,513	64,535
Inventories	499	(6,987)
Prepaid expenses and other	414	1,969
Other assets	(169)	1,479
Accounts payable and accrued liabilities	(4,694)	(48,650)
Deferred revenue	(27,446)	25,979
Other long-term liabilities	(1,424)	(4,628)
<b>Net cash provided by operating activities</b>	<b>128,188</b>	<b>125,778</b>
<b>Cash Flows from Investing Activities:</b>		
Proceeds from the sale and maturity of available-for-sale securities	136	9,588
Purchases of available-for-sale securities	(49,083)	
Proceeds from the sale of long-term investments	44	2,785
Purchases of property, plant and equipment	(18,269)	(11,312)
Investment in venture capital partnerships and equity investments	(250)	(608)
Cash paid in business combinations and asset acquisitions, net of cash acquired, and acquisitions of intangibles	(1,041)	(22,865)
<b>Net cash used for investing activities</b>	<b>(68,463)</b>	<b>(22,412)</b>
<b>Cash Flows from Financing Activities:</b>		
Principal payments on receivable sale financing	(2,907)	(2,829)
Tax effect related to employee stock transactions allocated to equity	4,075	967
Payment of acquisition-related contingent consideration	(39)	
Proceeds from issuance of common stock	13,063	10,302
Stock received for payment of employee taxes on vesting of restricted stock	(9,897)	(7,389)
<b>Net cash provided by financing activities</b>	<b>4,295</b>	<b>1,051</b>

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Effect of exchange rate changes on cash and cash equivalents	(3,964)	3,491
Increase in cash and cash equivalents	60,056	107,908
Cash and Cash Equivalents at End of Period	\$ 661,658	\$ 665,317

See notes to 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 United States 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 on Form 10-Q comply with the requirements of Section 13(a) of the Securities Exchange Act of 1934, as amended, or the Exchange Act, 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 31, 2011. Certain prior period balances have been reclassified to conform to current period presentation.

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 of operations, cash flows and financial position for the periods and dates 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 United States 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 revenue and expenses during the reporting period. Actual results could differ from those estimates.

**NOTE 2. CONVERTIBLE NOTES**

**2015 Notes**

In June 2010, Cadence issued \$350.0 million principal amount of 2.625% Cash Convertible Senior Notes Due 2015, or the 2015 Notes. At maturity, the holders of the 2015 Notes will be entitled to receive the principal amount of the 2015 Notes plus accrued interest. The 2015 Notes are convertible into cash prior to maturity upon the occurrence of certain conditions described in the table below. If a holder of the 2015 Notes elects to convert its notes prior to maturity, the holder of the notes will be entitled to receive cash equal to the principal amount of the notes plus any additional conversion value as described in the table below under the heading "Conversion feature."

Cadence entered into hedge transactions, or the 2015 Notes Hedges, in connection with the issuance of the 2015 Notes. The purpose of the 2015 Notes Hedges was to limit Cadence's exposure to the additional cash payments above the principal amount of the 2015 Notes that may be due to the holders. As a result of the 2015 Notes Hedges, Cadence's maximum expected cash exposure upon conversion of the 2015 Notes is the \$350.0 million principal balance of the notes. In June 2010, Cadence also sold warrants in separate transactions, or the 2015 Warrants. As a result of the 2015 Warrants, Cadence will experience dilution to its

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diluted earnings per share if its average closing stock price exceeds \$10.78 for any fiscal quarter. To the extent that Cadence's stock price exceeds \$10.78 at expiration of the 2015 Warrants, Cadence will issue shares to settle the 2015 Warrants.

A summary of key terms of the 2015 Notes is as follows:

	2015 Notes (In thousands, except percentages)
Outstanding principal maturity value at June 30, 2012	\$350,000
Contractual interest rate	2.625%
Contractual maturity date	June 1, 2015
Initial conversion rate	132.5205 shares of common stock per \$1,000 principal amount of notes, which is equivalent to a conversion price of approximately \$7.55 per share of Cadence common stock.
Conversion feature (in addition to principal amount payable in cash)	Cash to the extent Cadence's stock price exceeds approximately \$7.55 per share, calculated based on the applicable conversion rate multiplied by the volume weighted average price of Cadence common stock over a specified period.
Early conversion conditions (or the Early Conversion Conditions)	Closing stock price greater than \$9.81 for at least 20 of the last 30 trading days in a fiscal quarter (convertible only for subsequent quarter).
	Specified corporate transactions.
	Note trading price falls below a calculated minimum.
Conversion immediately preceding maturity	From March 1, 2015 until the second trading day immediately preceding the maturity date, holders may convert their 2015 Notes at any time into cash as described above under Conversion feature.
Redemption at Cadence's option prior to maturity	None.

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Fundamental change put right	Upon certain fundamental corporate changes prior to maturity, the 2015 Note holders could require Cadence to repurchase their notes for cash equal to the principal amount of the notes plus accrued interest.
Make-whole premium	Upon certain fundamental changes prior to maturity, if Cadence's stock price were between \$6.16 and \$40.00 per share at that time, the holders of the notes would be entitled to an increase to the conversion rate. This is referred to as a make-whole premium.
Financial covenants	None.
<i>Impact of Early Conversion Conditions on Financial Statements</i>	

The 2015 Notes are convertible into cash from July 1, 2012 through September 29, 2012 because Cadence's closing stock price exceeded \$9.81 for at least 20 days in the 30-day period prior to June 30, 2012. Accordingly, the net balance of the 2015 Notes of \$301.3 million is classified as a current liability on Cadence's Condensed Consolidated Balance Sheet as of June 30, 2012. The classification of the 2015 Notes as current or long-term on the Condensed Consolidated Balance Sheet is evaluated at each balance sheet date and may change from time to time depending on whether Cadence's closing stock price has exceeded \$9.81 during the periods specified in the table above under Early conversion conditions.

If one of the 2015 Notes Early Conversion Conditions is met in any future fiscal quarter, Cadence would classify its net liability under the 2015 Notes as a current liability on the Condensed Consolidated Balance Sheet as of the end of that fiscal quarter. If none of the 2015 Notes Early Conversion Conditions have been met in a future fiscal quarter prior to the one-year period immediately preceding the maturity date, Cadence would classify its net liability under the 2015 Notes as a long-term liability on the Condensed Consolidated Balance Sheet as of the end of that fiscal quarter. If the note holders elect to convert their 2015 Notes prior to maturity, any unamortized discount and transaction fees will be expensed at the time of conversion. If the entire outstanding principal amount had been converted on June 30, 2012, Cadence would have recorded an expense of \$55.4 million associated with the conversion, comprised of \$48.7 million of unamortized debt discount and \$6.7 million of unamortized transaction fees.

As of June 30, 2012, the if-converted value of the 2015 Notes to the note holders of approximately \$509.7 million exceeded the principal amount of \$350.0 million. The fair value of the 2015 Notes was \$544.5 million as of June 30, 2012 and was \$527.8 million as of December 31, 2011. The 2015 Notes currently trade at a premium to the if-converted value of the notes. As of June 30, 2012, none of the note holders had elected to convert their 2015 Notes.

*2015 Notes Embedded Conversion Derivative*

The conversion feature of the 2015 Notes, or the 2015 Notes Embedded Conversion Derivative, requires bifurcation from the 2015 Notes and is accounted for as a derivative liability. The fair value of the 2015 Notes Embedded Conversion Derivative at the time of issuance of the 2015 Notes was \$76.6 million and was recorded as original debt discount for purposes of accounting for the debt component of the 2015 Notes. This discount is amortized as interest expense using the effective interest method over the term of the 2015 Notes. The 2015 Notes Embedded Conversion Derivative is carried on the Condensed Consolidated Balance Sheet at its estimated fair value. The fair value was \$219.2 million as of June 30, 2012 and \$215.1 million as of December 31, 2011.

**Table of Contents***2015 Notes Hedges*

The 2015 Notes Hedges expire on June 1, 2015 and must be settled in cash. The aggregate cost of the 2015 Notes Hedges was \$76.6 million. The 2015 Notes Hedges are accounted for as derivative assets and are carried on the Condensed Consolidated Balance Sheet at their estimated fair value. The fair value was \$219.2 million as of June 30, 2012 and \$215.1 million as of December 31, 2011. The 2015 Notes Embedded Conversion Derivative liability and the 2015 Notes Hedges asset are adjusted to fair value each reporting period and unrealized gains and losses are reflected in the Condensed Consolidated Income Statements. The 2015 Notes Embedded Conversion Derivative and the 2015 Notes Hedges are designed to have similar fair values. Accordingly, the changes in the fair values of these instruments offset during the three and six months ended June 30, 2012 and July 2, 2011 and did not have a net impact on the Condensed Consolidated Income Statements for the respective periods.

The classification of the 2015 Notes Embedded Conversion Derivative liability and the 2015 Notes Hedges asset as current or long-term on the Condensed Consolidated Balance Sheet corresponds with the classification of the 2015 Notes, is evaluated at each balance sheet date and may change from time to time depending on whether the closing stock price early conversion condition is met.

*2015 Warrants*

In June 2010, Cadence sold the 2015 Warrants in separate transactions for the purchase of up to approximately 46.4 million shares of Cadence's common stock at a strike price of \$10.78 per share, for total proceeds of \$37.5 million, which was recorded as an increase in stockholders' equity. The 2015 Warrants expire on various dates from September 2015 through December 2015 and must be settled in net shares of Cadence's common stock. Therefore, upon expiration of the 2015 Warrants Cadence will issue shares of common stock to the purchasers of the 2015 Warrants that represent the value by which the price of the common stock exceeds the strike price stipulated within the particular warrant agreement. Changes in the fair value of the 2015 Warrants will not be recognized in the Condensed Consolidated Financial Statements as long as the instruments remain classified as equity.

*Components of 2015 Notes*

The components of the 2015 Notes as of June 30, 2012 and December 31, 2011 were as follows:

	As of	
	June 30, 2012	December 31, 2011
	(In thousands)	
Principal amount	\$ 350,000	\$ 350,000
Unamortized debt discount	(48,708)	(55,939)
Liability component	\$ 301,292	\$ 294,061

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The effective interest rate and components of interest expense of the 2015 Notes for the three and six months ended June 30, 2012 and July 2, 2011 were as follows:

	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
	(In thousands, except percentages)			
Effective interest rate	8.1%	8.1%	8.1%	8.1%
Contractual interest expense	\$ 2,289	\$ 2,289	\$ 4,578	\$ 4,578
Amortization of debt discount	\$ 3,638	\$ 3,376	\$ 7,231	\$ 6,713

**2013 Notes and 2011 Notes**

In December 2006, Cadence issued \$250.0 million principal amount of 1.500% Convertible Senior Notes Due December 15, 2013, or the 2013 Notes. At the same time, Cadence issued \$250.0 million principal amount of 1.375% Convertible Senior Notes Due December 15, 2011, or the 2011 Notes. The 2011 Notes matured on December 15, 2011, at which time Cadence paid the remaining balance on the 2011 Notes in full.

At maturity, the holders of the 2013 Notes will be entitled to receive the principal amount of the 2013 Notes plus accrued interest. The 2013 Notes are convertible into a combination of cash and shares of Cadence common stock upon the occurrence of certain conditions described in the table below. If a holder of the 2013 Notes elects to convert its notes prior to maturity, the holder of the notes will be entitled to receive cash for the principal amount of the notes plus shares for any additional conversion value as described in the table below under the heading Conversion feature. As of June 30, 2012, the 2013 Notes were not convertible.

Cadence entered into hedge transactions, or the 2013 Notes Hedges and the 2011 Notes Hedges, in connection with the issuance of the 2013 Notes and the 2011 Notes. The 2011 Notes Hedges expired unexercised on December 15, 2011. Pursuant to the 2013 Notes Hedges, Cadence has the option to receive the amount of shares that may be owed to the 2013 Notes holders. The purpose of the 2013 Notes Hedges was to limit Cadence's exposure to the dilution that may result from the issuance of shares upon conversion of the notes. In December 2006, Cadence also sold warrants in separate transactions, or the 2013 Warrants and the 2011 Warrants. As a result of the 2013 Warrants, Cadence will experience dilution to its diluted earnings per share to the extent its average closing stock price exceeds \$31.50 for any fiscal quarter. If Cadence's stock price is above \$31.50 at the expiration of the 2013 Warrants, Cadence will issue shares to settle the 2013 Warrants.

A summary of key terms of the 2013 Notes is as follows:

	2013 Notes (In thousands, except percentages)
Principal maturity value at issuance	\$ 250,000
Outstanding principal maturity value at June 30, 2012	\$ 144,461
Contractual interest rate	1.500%
Contractual maturity date	December 15, 2013

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Initial conversion rate	47.2813 shares of common stock per \$1,000 principal amount of notes, which is equivalent to a conversion price of approximately \$21.15 per share of Cadence common stock.
Conversion feature (in addition to principal amount payable in cash)	Shares to the extent Cadence's stock price exceeds \$21.15 per share, calculated based on the applicable conversion rate multiplied by the volume weighted average price of Cadence common stock over a specified period.
Early conversion conditions (or the Early Conversion Conditions)	Closing stock price greater than \$27.50 for at least 20 of the last 30 trading days in a calendar quarter (convertible only for subsequent quarter).
	Specified corporate transactions.
	Note trading price falls below calculated minimum.
Conversion immediately preceding maturity	From November 1, 2013 and until the trading day immediately preceding the maturity date, holders may convert their 2013 Notes at any time into cash and Cadence shares as described above under Conversion feature.
Redemption at Cadence's option prior to maturity	None.
Fundamental change put right	Upon a fundamental change prior to maturity, the 2013 Note holders could require Cadence to repurchase their notes for cash equal to the principal amount of the notes plus accrued interest.
Make-whole premium	Upon certain fundamental changes, prior to maturity, if Cadence's stock price were between \$18.00 and \$60.00 per share at that time, the holders of the notes would be entitled to an increase to the conversion rate. This is referred to as a make-whole premium.
Financial covenants	None.
<i>Impact of Early Conversion Conditions on Financial Statements</i>	

As of June 30, 2012, none of the 2013 Notes Early Conversion Conditions had been met and the 2013 Notes are classified as a long-term liability on the Condensed Consolidated Balance Sheet. The classification of the 2013 Notes as a current or long-term liability on the Condensed Consolidated Balance Sheet is evaluated at each balance sheet date and may change from time to time, depending on whether the closing stock price early conversion condition is met for that particular quarter.



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As of June 30, 2012, the if-converted value of the 2013 Notes to the note holders did not exceed the principal amount of the 2013 Notes. The total fair value of the 2013 Notes, including the equity component, was \$141.2 million as of June 30, 2012 and was \$142.3 million as of December 31, 2011.

*2013 and 2011 Notes Hedges*

The 2011 Notes Hedges expired unexercised on December 15, 2011. The 2013 Notes Hedges expire on December 15, 2013 and must be settled in net shares of Cadence common stock. Therefore, upon expiration of the 2013 Notes Hedges the counterparties will deliver shares of common stock to Cadence that represent the value, if any, by which the price of the common stock exceeds the price stipulated within the particular hedge agreement. The aggregate cost of the hedges entered into in connection with the 2011 Notes Hedges (which had similar conversion features as the 2013 Notes) and 2013 Notes Hedges was \$119.8 million and was recorded as a reduction to stockholders' equity. In connection with the purchase of a portion of the 2013 Notes and 2011 Notes in June 2010, and the purchase of a portion of the 2013 Notes in November 2010, Cadence also sold a portion of the 2013 Notes Hedges and the 2011 Notes Hedges representing options to purchase approximately 9.7 million shares of Cadence's common stock for proceeds of \$0.4 million. The estimated fair value of the remaining 2013 Notes Hedges was \$0.7 million as of June 30, 2012 and \$1.4 million as of December 31, 2011. Subsequent changes in the fair value of the 2013 Notes Hedges will not be recognized in the Condensed Consolidated Financial Statements as long as the instruments remain classified as equity.

*2013 and 2011 Warrants*

In December 2006, Cadence sold warrants in separate transactions, which consisted of the 2013 Warrants and the 2011 Warrants, for the purchase of up to 23.6 million shares of Cadence's common stock at a strike price of \$31.50 per share for proceeds of \$39.4 million, which was recorded as an increase in stockholders' equity. In connection with the purchase of some of the 2013 Notes and the 2011 Notes in June 2010 and November 2010, Cadence also purchased some of the 2013 Warrants and the 2011 Warrants, reducing the number of shares of Cadence common stock available for purchase by 9.7 million shares at a cost of \$0.1 million. The 2011 Warrants expired on various dates from February 2012 through April 2012 and the 2013 Warrants will expire on various dates from February 2014 through April 2014. The 2013 Warrants must be settled in net shares of Cadence's common stock. Therefore, upon expiration of the 2013 Warrants Cadence will issue shares of common stock to the purchasers of the warrants that represent the value, if any, by which the price of the common stock exceeds the strike price stipulated within the particular warrant agreement. During the six months ended June 30, 2012, the 2011 Warrants expired, reducing the number of shares of Cadence common stock available for purchase by 7.1 million shares. Changes in the fair value of the 2013 Warrants and the 2011 Warrants will not be recognized in the Condensed Consolidated Financial Statements as long as the instruments remain classified as equity.

*Components of the 2013 Notes*

The components of the 2013 Notes as of June 30, 2012 and December 31, 2011 were as follows:

	As of	
	June 30, 2012	December 31, 2011
	(In thousands)	
Equity component included in common stock	\$ 63,027	\$ 63,027
Principal amount	\$ 144,461	\$ 144,461
Unamortized debt discount	(9,633)	(12,719)
Liability component	\$ 134,828	\$ 131,742

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The effective interest rate and components of interest expense of the 2013 Notes for the three and six months ended June 30, 2012 and of the 2013 Notes and 2011 Notes for the three and six months ended July 2, 2011 were as follows:

	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
	(In thousands, except percentages)			
Effective interest rate	6.4%	6.3%	6.4%	6.3%
Contractual interest expense	\$ 540	\$ 1,053	\$ 1,080	\$ 2,106
Amortization of debt discount	\$ 1,547	\$ 3,212	\$ 3,086	\$ 6,409

**Zero Coupon Zero Yield Senior Convertible Notes Due 2023**

In August 2003, Cadence issued \$420.0 million principal amount of its Zero Coupon Zero Yield Senior Convertible Notes Due 2023, or the 2023 Notes. As of June 30, 2012 and December 31, 2011, the remaining balance and the total fair value of the 2023 Notes was \$0.2 million.

**NOTE 3. ACQUISITION-RELATED CONTINGENT CONSIDERATION**

For business combinations completed after January 3, 2009, contingent consideration is recorded at fair value on the acquisition date and adjusted to fair value at the end of each reporting period.

One of the fiscal 2011 acquisitions includes contingent consideration payments based on certain future financial measures associated with the acquired technology. This contingent consideration arrangement requires payments of up to \$5.0 million if certain financial measures are met during the three-year period subsequent to October 1, 2011. The fair value of the contingent consideration arrangement recorded on the date of the acquisition was \$3.5 million. The fair value of the contingent consideration as of June 30, 2012 was \$3.9 million.

Cadence may be obligated to make cash payments in connection with business combinations and asset acquisitions, based on, or subject to the satisfaction of, certain performance metrics. If performance is such that these payments are fully achieved, Cadence may be obligated to pay up to an aggregate of \$21.2 million over the next 46 months. Of the \$21.2 million, up to \$12.6 million would be recorded as operating expenses in the Condensed Consolidated Income Statements and up to \$1.2 million would be recorded as additional goodwill.

**NOTE 4. GOODWILL AND ACQUIRED INTANGIBLES****Goodwill**

The changes in the carrying amount of goodwill during the six months ended June 30, 2012 were as follows:

	Gross Carrying Amount (In thousands)
Balance as of December 31, 2011	\$ 192,125
Effect of foreign currency translation	113
Balance as of June 30, 2012	\$ 192,238

**Table of Contents****Acquired Intangibles, Net**

Acquired intangibles with finite lives as of June 30, 2012 were as follows, excluding intangibles that were fully amortized as of December 31, 2011:

	Gross Carrying Amount	Accumulated Amortization (In thousands)	Acquired Intangibles, Net
Existing technology	\$ 90,516	\$ (22,917)	\$ 67,599
Agreements and relationships	117,580	(32,212)	85,368
Distribution rights	30,100	(27,090)	3,010
Tradenames, trademarks and patents	11,183	(7,353)	3,830
<b>Total acquired intangibles</b>	<b>\$ 249,379</b>	<b>\$ (89,572)</b>	<b>\$ 159,807</b>

Acquired intangibles with finite lives as of December 31, 2011 were as follows, excluding intangibles that were fully amortized as of January 1, 2011:

	Gross Carrying Amount	Accumulated Amortization (In thousands)	Acquired Intangibles, Net
Existing technology	\$ 90,433	\$ (17,119)	\$ 73,314
Agreements and relationships	118,060	(27,123)	90,937
Distribution rights	30,100	(25,585)	4,515
Tradenames, trademarks and patents	26,183	(21,715)	4,468
<b>Total acquired intangibles</b>	<b>\$ 264,776</b>	<b>\$ (91,542)</b>	<b>\$ 173,234</b>

Amortization of acquired intangibles for the three and six months ended June 30, 2012 and July 2, 2011 was as follows:

	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
	(In thousands)			
Cost of product	\$ 2,891	\$ 2,483	\$ 5,790	\$ 4,679
Amortization of acquired intangibles	3,643	4,505	7,429	8,964
<b>Total amortization of acquired intangibles</b>	<b>\$ 6,534</b>	<b>\$ 6,988</b>	<b>\$ 13,219</b>	<b>\$ 13,643</b>

Amortization of costs from existing technology is included in cost of product.

Estimated amortization expense for the following five fiscal years and thereafter is as follows:

	(In thousands)
2012 remaining period	\$ 13,186
2013	23,099
2014	20,315

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2015	20,001
2016	19,562
Thereafter	63,644
Total estimated amortization expense	\$ 159,807

**Table of Contents****NOTE 5. RESTRUCTURING AND OTHER CHARGES**

Cadence has initiated various restructuring plans in the past in an effort to operate more efficiently. These restructuring plans were primarily comprised of severance and termination costs related to headcount reductions and facility-related lease loss charges. As of June 30, 2012, all severance and termination benefits have been paid.

The following table presents activity for Cadence's restructuring plans for the three months ended June 30, 2012:

	Excess Facilities	Other (In thousands)	Total
Balance, March 31, 2012	\$ 4,792	\$ 5	\$ 4,797
Restructuring and other charges (credits), net	48	(5)	43
Cash payments	(155)		(155)
Effect of foreign currency translation	(173)		(173)
Balance, June 30, 2012	\$ 4,512	\$	\$ 4,512

The following table presents activity for Cadence's restructuring plans for the six months ended June 30, 2012:

	Severance and Benefits	Excess Facilities	Other	Total
	(In thousands)			
Balance, December 31, 2011	\$ 46	\$ 4,976	\$ 5	\$ 5,027
Restructuring and other charges (credits), net	(29)	26	(5)	(8)
Cash payments	(17)	(460)		(477)
Effect of foreign currency translation		(30)		(30)
Balance, June 30, 2012	\$	\$ 4,512	\$	\$ 4,512

**NOTE 6. ACCOUNTS RECEIVABLE AND ALLOWANCES FOR DOUBTFUL ACCOUNTS**

Cadence's current and long-term accounts receivable balances as of June 30, 2012 and December 31, 2011 were as follows:

	As of	
	June 30, 2012	December 31, 2011
	(In thousands)	
Accounts receivable	\$ 75,135	\$ 99,686
Installment contract receivables, short-term	48,108	37,086
Long-term receivables	7,750	11,371
Total receivables	\$ 130,933	\$ 148,143

Cadence's customers are primarily concentrated within the semiconductor and electronics systems industry. As of June 30, 2012 and December 31, 2011, no single customer accounted for more than 10% of Cadence's total receivables. As of June 30, 2012, approximately 49% of Cadence's total receivables were attributable to the ten customers with the largest balances of total receivables. As of December 31, 2011,

approximately 45% of Cadence's total receivables were attributable to the ten customers with the largest balances of total receivables.

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**NOTE 7. FAIR VALUE**

Inputs to valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect Cadence's market assumptions. These two types of inputs have created the following fair-value hierarchy:

Level 1 Quoted prices for identical instruments in active markets;

Level 2 Quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets; and

Level 3 Valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable.

This hierarchy requires Cadence to minimize the use of unobservable inputs and to use observable market data, if available, when determining fair value. Cadence recognizes transfers between levels of the hierarchy based on the fair values of the respective financial instruments at the end of the reporting period in which the transfer occurred. There were no transfers between levels of the fair value hierarchy during the three and six months ended June 30, 2012.

The carrying value of Cadence's cash and cash equivalents held in money market funds approximates fair value and is based on level 1 inputs. The carrying value of Cadence's receivables, interest receivable, accounts payable and accrued liabilities approximates their fair value due to the short-term nature of these instruments and is based on level 2 inputs. The carrying values of Cadence's long-term receivables approximate their fair values and are based on level 2 inputs, including current market rates of interest. The fair values of Cadence's 2013 Notes and 2015 Notes, which differ from their carrying values, are influenced by interest rates and Cadence's stock price and stock price volatility and are determined by prices for the 2013 Notes and 2015 Notes observed in market trading, which are level 2 inputs. The fair values of Cadence's 2015 Notes Hedges and 2015 Notes Embedded Conversion Derivative are determined by level 1 and level 2 inputs, including interest rates, Cadence's stock price and stock price volatility.

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On a quarterly basis, Cadence measures at fair value certain financial assets and liabilities. The fair value of financial assets and liabilities was determined using the following levels of inputs as of June 30, 2012 and December 31, 2011:

	Fair Value Measurements as of June 30, 2012:			
	Total	Level 1	Level 2	Level 3
	(In thousands)			
<b>Assets</b>				
Cash equivalents:				
Money market funds	\$ 520,546	\$ 520,546	\$	\$
Commercial paper	1,200		1,200	
Bank certificates of deposit	1,000		1,000	
Short-term investments:				
Corporate debt securities	26,084		26,084	
United States government agency securities	2,208	2,208		
United States Treasury securities	17,255	17,255		
Bank certificates of deposit	1,995		1,995	
Commercial paper	1,498		1,498	
Marketable equity securities	2,264	2,264		
Trading securities held in Non-Qualified Deferred Compensation Plan, or NQDC	24,009	24,009		
2015 Notes Hedges	219,199		219,199	
Foreign currency exchange contracts	942		942	
<b>Total Assets</b>	<b>\$ 818,200</b>	<b>\$ 566,282</b>	<b>\$ 251,918</b>	<b>\$</b>

	Fair Value Measurements as of June 30, 2012:			
	Total	Level 1	Level 2	Level 3
	(In thousands)			
<b>Liabilities</b>				
Acquisition-related contingent consideration	\$ 3,997	\$	\$	\$ 3,997
2015 Notes Embedded Conversion Derivative	219,199		219,199	
<b>Total Liabilities</b>	<b>\$ 223,196</b>	<b>\$</b>	<b>\$ 219,199</b>	<b>\$ 3,997</b>

	Fair Value Measurements as of December 31, 2011:			
	Total	Level 1	Level 2	Level 3
	(In thousands)			
<b>Assets</b>				
Cash equivalents money market funds	\$ 484,102	\$ 484,102	\$	\$
Short-term investments:				
Marketable equity securities	3,037	3,037		
Trading securities held in NQDC	24,058	24,058		
2015 Notes Hedges	215,113		215,113	
Foreign currency exchange contracts	200		200	
<b>Total Assets</b>	<b>\$ 726,510</b>	<b>\$ 511,197</b>	<b>\$ 215,313</b>	<b>\$</b>

	Fair Value Measurements as of December 31, 2011:			
	Total	Level 1	Level 2	Level 3
	(In thousands)			
<b>Liabilities</b>				
Acquisition-related contingent consideration	\$ 3,911	\$	\$	\$ 3,911
2015 Notes Embedded Conversion Derivative	215,113		215,113	



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Total Liabilities	\$ 219,024	\$	\$ 215,113	\$ 3,911
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**Table of Contents****Level 1 Measurements**

Cadence's cash equivalents held in money market funds, available-for-sale United States Treasury securities, United States government agency securities, equity securities and the trading securities held in Cadence's NQDC trust are measured at fair value using level 1 inputs.

**Level 2 Measurements**

The 2015 Notes Hedges and the 2015 Notes Embedded Conversion Derivative are measured at fair value using level 2 inputs. These instruments are not actively traded and are valued using an option pricing model that uses observable market data for all inputs, such as implied volatility of Cadence's common stock, risk-free interest rate and other factors. Cadence's available-for-sale corporate debt securities, bank certificates of deposit and commercial paper are measured at fair value using level 2 inputs. Cadence obtains the fair values of its level 2 available-for-sale securities from a professional pricing service and validates the fair values by assessing the pricing methods and inputs and by comparing the fair values to another independent source.

Cadence's foreign currency exchange contracts are measured at fair value using observable foreign currency exchange rates.

**Level 3 Measurements**

The liabilities included in level 3 represent the fair value of contingent consideration associated with certain of Cadence's 2011 and 2010 acquisitions. Cadence makes estimates regarding the fair value of contingent consideration liabilities on the acquisition date and at the end of each reporting period until the contingency is resolved. The fair value of these arrangements is determined by calculating the net present value of the expected payments using significant inputs that are not observable in the market, including revenue projections and discount rates consistent with the level of risk of achievement. The fair value of these contingent consideration arrangements is affected most significantly by the changes in the revenue projections, but is also impacted by the discount rate used to adjust the outcomes to their present values. If the revenue projections increase or decrease, the fair value of the contingent consideration will increase or decrease accordingly, in amounts that will vary based on the timing of the projected revenues, the timing of the expected payments and the discount rate used to calculate the present value of the expected payments. Cadence used discount rates ranging from 11% to 16% to value its contingent consideration liabilities as of June 30, 2012 and December 31, 2011. Cadence believes that its estimates and assumptions are reasonable, but significant judgment is involved.

Changes in the fair value of contingent consideration liabilities subsequent to the acquisition are recorded in general and administrative expense in the Condensed Consolidated Income Statements. For an additional description of the related business combinations, see Note 3.

The following table summarizes the level 3 activity for the six months ended June 30, 2012:

	(In thousands)
Balance as of December 31, 2011	\$ 3,911
Payments	(39)
Adjustments	125
Balance as of June 30, 2012	\$ 3,997

**Table of Contents****NOTE 8. CASH, CASH EQUIVALENTS AND INVESTMENTS****Cash and Cash Equivalents**

Cadence considers all highly liquid investments with original maturities of three months or less on the date of purchase to be cash equivalents. The following table summarizes Cadence's cash and cash equivalents at fair value as of June 30, 2012 and December 31, 2011:

	June 30, 2012	As of December 31, 2011
	(In thousands)	
Cash and interest bearing deposits	\$ 138,912	\$ 117,500
Money market funds	520,546	484,102
Commercial paper	1,200	
Bank certificates of deposit	1,000	
<b>Total cash and cash equivalents</b>	<b>\$ 661,658</b>	<b>\$ 601,602</b>

**Short-Term Investments**

Cadence's short-term investments include marketable debt securities with original maturities greater than three months on the date of purchase and marketable equity securities. Cadence considers its entire portfolio of marketable debt and equity securities to be available for sale and available to fund current operations. Available-for-sale debt securities are carried at fair value, with the unrealized gains and losses presented net of tax as a separate component of other comprehensive income. Unrealized and realized gains and losses are determined using the specific identification method.

Cadence recognizes gains on its available-for-sale securities when they are realized. Cadence recognizes losses on its available-for-sale securities when they are realized or when Cadence has determined that an other-than-temporary decline in fair value has occurred. Cadence reviews its available-for-sale securities each quarter to determine if an other-than-temporary decline in fair value has occurred. For an available-for-sale debt security, an other-than-temporary decline in fair value has occurred when the security's fair value is less than its amortized cost basis and Cadence intends to sell the security, or it is more likely than not that Cadence will be required to sell the security, before recovery of its amortized cost basis. Cadence records realized gains, realized losses and other-than-temporary impairments as part of other income, net in the Condensed Consolidated Income Statements.

The following tables summarize Cadence's short-term investments as of June 30, 2012 and December 31, 2011:

	Amortized Cost	As of June 30, 2012 Gross		Fair Value
		Unrealized Gains	Unrealized Losses	
	(In thousands)			
Corporate debt securities	\$ 26,101	\$ 7	\$ (24)	\$ 26,084
United States government agency securities	2,206	2		2,208
United States Treasury securities	17,258		(3)	17,255
Bank certificates of deposit	2,000		(5)	1,995
Commercial paper	1,497	1		1,498
Marketable equity securities	1,830	434		2,264
<b>Total short-term investments</b>	<b>\$ 50,892</b>	<b>\$ 444</b>	<b>\$ (32)</b>	<b>\$ 51,304</b>



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	Amortized Cost	As of December 31, 2011		Fair Value
		Unrealized Gains	Unrealized Losses	
		(In thousands)		
Marketable equity securities	\$ 1,830	\$ 1,207	\$	\$ 3,037
Total short-term investments	\$ 1,830	\$ 1,207	\$	\$ 3,037

Cadence purchased its investments in marketable debt securities during the three months ended June 30, 2012. As of June 30, 2012, any security Cadence held with an unrealized loss had been held for less than three months.

The amortized cost and estimated fair value of marketable debt securities included in short-term investments as of June 30, 2012, by contractual maturity, are shown in the table below. Actual maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations without call or prepayment penalties.

	Amortized Cost	Fair Value
	(In thousands)	
Due in less than one year	\$ 13,124	\$ 13,115
Due in one to three years	35,938	35,925
Total marketable debt securities included in short-term investments	\$ 49,062	\$ 49,040

Realized gains from the sale of marketable equity securities during three and six months ended June 30, 2012 and July 2, 2011 were as follows:

	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
	(In thousands)		(In thousands)	
Gains on sale of marketable equity securities	\$	\$ 7,987	\$ 117	\$ 8,052
Losses on sale of marketable equity securities	(2)	(8)	(2)	(8)
Total net gains (losses) on sale of marketable equity securities	\$ (2)	\$ 7,979	\$ 115	\$ 8,044

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Amortization of premium or discount related to Cadence's marketable debt securities for the three and six months ended June 30, 2012 and July 2, 2011 was as follows:

	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
	(In thousands)		(In thousands)	
Amortization of premium (discount)	\$ 20	\$	\$ 20	\$

**Non-Marketable Investments**

Cadence's non-marketable investments generally consist of voting preferred stock or convertible debt of privately-held companies and are included in other assets on Cadence's Condensed Consolidated Balance Sheets. If Cadence determines that it has the ability to exercise significant influence over the issuer, which may include considering whether the investments are in-substance common stock, the investment is accounted for using the equity method.

Cadence's non-marketable investments as of June 30, 2012 and December 31, 2011 were as follows:

	June 30,	As of
	2012	December 31, 2011
	(In thousands)	
Cost method	\$ 6,135	\$ 6,157
Equity method	4,320	4,303
<b>Total non-marketable investments</b>	<b>\$ 10,455</b>	<b>\$ 10,460</b>

Net realized gains on the sale of non-marketable investments during the three and six months ended June 30, 2012 and July 2, 2011 were as follows:

	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
	(In thousands)		(In thousands)	
Gains on sale of non-marketable investments	\$	\$ 108	\$	\$ 2,729

**NOTE 9. NET INCOME PER SHARE**

Basic net income per share is computed by dividing net income during the period by the weighted average number of shares of common stock outstanding during that period, less unvested restricted stock awards. None of Cadence's outstanding grants of restricted stock contain nonforfeitable dividend rights. Diluted net income per share is impacted by equity instruments considered to be potential common shares, if dilutive, computed using the treasury stock method of accounting.

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The calculations for basic and diluted net income per share for the three and six months ended June 30, 2012 and July 2, 2011 are as follows:

	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
	(In thousands, except per share amounts)			
Net income	\$ 36,386	\$ 26,908	\$ 67,490	\$ 33,231
Weighted average common shares used to calculate basic net income per share	269,739	263,191	268,840	262,362
2023 Notes	11	11	11	11
2015 Warrants	637		1,580	
Stock-based compensation	4,931	7,683	6,095	7,359
Weighted average common shares used to calculate diluted net income per share	275,318	270,885	276,526	269,732
Basic net income per share	\$ 0.13	\$ 0.10	\$ 0.25	\$ 0.13
Diluted net income per share	\$ 0.13	\$ 0.10	\$ 0.24	\$ 0.12

The following table presents shares of Cadence's common stock outstanding for the three and six months ended June 30, 2012 and July 2, 2011 that were excluded from the computation of diluted net income per share because the effect of including these shares in the computation of diluted net income per share would have been anti-dilutive:

	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
	(In thousands)			
2015 Warrants (various expiration dates through 2015)		46,382		46,382
2011 Warrants and 2013 Warrants (various expiration dates through 2014)	6,830	14,184	6,830	14,184
Options to purchase shares of common stock (various expiration dates through 2022)	14,228	18,812	14,149	18,564
Non-vested shares of restricted stock	203	9	118	25
Total potential common shares excluded	21,261	79,387	21,097	79,155

**Table of Contents****NOTE 10. ACCUMULATED DEFICIT**

The changes in accumulated deficit for the three and six months ended June 30, 2012 were as follows:

	Three Months Ended (In thousands)
Balance as of March 31, 2012	\$ (1,053,745)
Net income	36,386
Reissuance of treasury stock	(831)
Balance as of June 30, 2012	\$ (1,018,190)

	Six Months Ended (In thousands)
Balance as of December 31, 2011	\$ (1,083,245)
Net income	67,490
Reissuance of treasury stock	(2,435)
Balance as of June 30, 2012	\$ (1,018,190)

**NOTE 11. OTHER COMPREHENSIVE INCOME**

Cadence's other comprehensive income is comprised of foreign currency translation gains and losses, changes in unrealized holding gains and losses on available-for-sale securities net of reclassifications for realized gains and losses and changes in defined benefit plan liabilities as presented in Cadence's Condensed Consolidated Statements of Comprehensive Income.

Changes in unrealized holding gains or losses on available-for-sale securities include the following for the three and six months ended June 30, 2012 and July 2, 2011:

	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
	(In thousands)		(In thousands)	
Unrealized holding gains or losses	\$ (1,019)	\$ 270	\$ (906)	\$ (34)
Reclassification of unrealized holding gains or losses to other income, net	2	(7,979)	(115)	(8,044)
Changes in unrealized holding gains or losses	\$ (1,017)	\$ (7,709)	\$ (1,021)	\$ (8,078)

Accumulated other comprehensive income was comprised of the following as of June 30, 2012 and December 31, 2011:



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	June 30, 2012	December 31, 2011
	(In thousands)	
Foreign currency translation gain	\$ 49,158	\$ 53,990
Changes in defined benefit plan liabilities	(4,414)	(4,468)
Unrealized holding gains on available-for-sale securities	410	1,431
 Total accumulated other comprehensive income	 \$ 45,154	 \$ 50,953

**NOTE 12. CONTINGENCIES**

**Legal Proceedings**

From time to time, Cadence is involved in various disputes and litigation that arise in the ordinary course of business. These include disputes and lawsuits related to intellectual property, indemnification

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obligations, mergers and acquisitions, licensing, contracts, distribution arrangements and employee relations matters. At least quarterly, Cadence reviews the status of each significant matter and assesses its potential financial exposure. If the potential loss from any claim or legal proceeding is considered probable and the amount or the range of loss can be estimated, Cadence accrues a liability for the estimated loss. Legal proceedings are subject to uncertainties, and the outcomes are difficult to predict. Because of such uncertainties, accruals are based on Cadence's judgments using the best information available at the time. As additional information becomes available, Cadence reassesses the potential liability related to pending claims and litigation matters and may revise estimates.

During fiscal 2008, three complaints were filed in the United States District Court for the Northern District of California, or District Court, all alleging violations of Sections 10(b) and 20(a) of the Exchange Act, and Rule 10b-5 promulgated thereunder, on behalf of a purported class of purchasers of Cadence's common stock. On March 4, 2009, the District Court entered an order consolidating these three complaints and captioning the consolidated case *In re Cadence Design Systems, Inc. Securities Litigation*. The District Court also named a lead plaintiff and lead counsel for the consolidated litigation. The lead plaintiff filed its consolidated amended complaint on April 24, 2009 (subsequently amended on October 13, 2009), naming Cadence, Michael J. Fister, Kevin S. Palatnik, William Porter and Kevin Bushby as defendants, and alleging violations of Sections 10(b) and 20(a) of the Exchange Act, and Rule 10b-5 promulgated thereunder, on behalf of a purported class of purchasers of Cadence's common stock who traded Cadence's common stock between April 23, 2008 and December 10, 2008, or the Alleged Class Period. The amended complaint alleged that Cadence and the individual defendants made statements during the Alleged Class Period regarding Cadence's financial results that were false and misleading because Cadence had recognized revenue that should have been recognized in subsequent periods. The amended complaint requested certification of the action as a class action, unspecified damages, interest and costs, and unspecified equitable relief. On July 7, 2010, the parties agreed, and the District Court ordered, that the litigation be stayed in order to facilitate mediation.

On February 11, 2011, the parties to the securities litigation agreed to settle the securities litigation for consideration of \$38.0 million, of which approximately \$22.2 million was to be paid by Cadence's insurance carriers, with the balance to be paid by Cadence. Cadence agreed to this settlement without admitting any wrongdoing on the part of the company or any of its current or former directors or executive officers. On April 23, 2012, the District Court entered an order granting final approval of the securities litigation settlement, and entered its final judgment and order of dismissal with prejudice.

During fiscal 2008, two derivative complaints were filed in Santa Clara County Superior Court, or Superior Court. A motion to consolidate these complaints was granted on January 20, 2009, and the cases were captioned *In re Cadence Design Systems, Inc. Derivative Litigation*. The consolidated cases were then stayed by agreement of the parties. The plaintiffs filed a consolidated amended derivative complaint on June 1, 2010. The consolidated amended derivative complaint named as defendants Cadence (as a nominal defendant), James S. Miller, R.L. Smith McKeithen, John B. Shoven, Lip-Bu Tan, Alberto Sangiovanni-Vincentelli, Donald L. Lucas, Sr., Roger S. Siboni, George Scalise, Michael J. Fister, John A.C. Swainson, Kevin S. Palatnik, William Porter and Kevin Bushby. The consolidated amended derivative complaint alleged purported causes of action for breach of fiduciary duty, abuse of control, gross mismanagement, waste of corporate assets and unjust enrichment (which is asserted against certain defendants). Many of the factual allegations of the consolidated amended derivative complaint were similar to those alleged in the securities class action case described above. In addition, the claims included allegations that the director defendants made inappropriate personnel decisions with respect to the former officers and that the former officers were unjustly enriched. The consolidated derivative complaint sought unspecified monetary damages and equitable relief, disgorgement of profits and compensation, and costs and attorneys' fees.

On April 28, 2010, a derivative complaint was filed in the District Court, captioned *Walter Hamilton, derivatively on behalf of nominal defendant Cadence Design Systems, Inc. v. Michael J. Fister*,

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William Porter, James S. Miller, Jr., Kevin Bushby, R.L. Smith McKeithen, Lip-Bu Tan, Alberto Sangiovanni-Vincentelli, John B. Shoven, Donald L. Lucas, George M. Scalise, Roger S. Siboni, John A.C. Swainson and KPMG LLP. The allegations underlying these claims were similar or identical to the allegations in the consolidated securities class action lawsuits and consolidated derivative complaints described above. In addition, the claims included allegations that Cadence's independent auditors performed allegedly inadequate audits. The complaint sought unspecified monetary relief, injunctive relief relating to certain corporate governance matters, and attorneys' costs and fees. On June 28, 2010, the plaintiff dismissed Cadence's independent auditors from the case, without prejudice.

On August 17, 2010, two complaints were filed in the District Court: one captioned George Powers, derivatively on behalf of Cadence Design Systems, Inc. v. Michael J. Fister, Kevin Bushby, R.L. Smith McKeithen, James S. Miller, Jr., William Porter, James J. Cowie, Kevin S. Palatnik, John B. Shoven, PhD, Donald L. Lucas and Roger S. Siboni; the other captioned Arash Samani, derivatively on behalf of Cadence Design Systems, Inc. v. Michael J. Fister, Kevin Bushby, R.L. Smith McKeithen, James S. Miller, Jr., William Porter, James J. Cowie, Kevin S. Palatnik, John B. Shoven, PhD, Donald L. Lucas and Roger S. Siboni. These complaints were virtually identical to one another, and purported to bring suit derivatively, on behalf of Cadence, against certain of Cadence's current and former officers and directors for breach of fiduciary duty. Many of the allegations underlying this claim were similar or identical to the allegations in the consolidated securities class action lawsuits described above. The complaints sought unspecified monetary and equitable relief, as well as attorneys' fees and costs.

These cases were stayed while the parties participated in the mediation process. On February 8, 2011, the parties to these derivative cases agreed to settle all of them in exchange for certain corporate governance changes that Cadence agreed to put in place, along with an agreement that an application by plaintiffs' counsel to the Court for an attorneys' fee of approximately \$1.8 million is appropriate. The fee was paid by Cadence's insurance carriers during the three months ended June 30, 2012. Cadence agreed to this settlement without admitting any wrongdoing on the part of the company or any of its current or former directors or executive officers. On April 23, 2012, the District Court entered an order granting final approval of the derivative settlement, and entered its final judgment and order of dismissal with prejudice.

## **Other Contingencies**

Cadence provides its customers with a warranty on sales of hardware products, generally for a 90-day period. Cadence did not incur any significant costs related to warranty obligations during the three and six months ended June 30, 2012 or July 2, 2011.

Cadence's product license and services agreements typically include a limited indemnification provision for claims from third parties relating to Cadence's intellectual property. If the potential loss from any indemnification claim is considered probable and the amount or the range of loss can be estimated, Cadence accrues a liability for the estimated loss. The indemnification is generally limited to the amount paid by the customer. Cadence did not incur any significant losses from indemnification claims during the three and six months ended June 30, 2012 or July 2, 2011.

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The supplemental cash flow information for the six months ended June 30, 2012 and July 2, 2011 is as follows:

	Six Months Ended	
	June 30, 2012	July 2, 2011
	(In thousands)	
<b>Cash Paid During the Period for:</b>		
Interest	\$ 5,677	\$ 6,708
Income taxes, including foreign withholding tax	\$ 9,801	\$ 9,209
<b>Non-cash Investing and Financing Activities:</b>		
Stock options assumed for acquisition	\$	\$ 1,600
Available-for-sale securities received from customer	\$ 15	\$ 160

**NOTE 14. OTHER INCOME, NET**

Cadence's other income, net, for the three and six months ended June 30, 2012 and July 2, 2011 was as follows:

	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
	(In thousands)			
Interest income	\$ 308	\$ 324	\$ 645	\$ 697
Gains (losses) on sale of marketable equity securities	(2)	7,979	115	8,044
Gains on sale of non-marketable equity investments		108		2,729
Gains on securities in Cadence's non-qualified deferred compensation trust	2,278	1,177	4,076	2,912
Gains (losses) on foreign exchange	1,070	(1,246)	1,170	(1,725)
Equity losses from non-marketable investments	(34)	(35)		(65)
Write-down of non-marketable investments	(22)		(22)	
Other income, net	71	87	119	271
<b>Total other income, net</b>	<b>\$ 3,669</b>	<b>\$ 8,394</b>	<b>\$ 6,103</b>	<b>\$ 12,863</b>

**NOTE 15. SEGMENT REPORTING**

Segment reporting is based on the management approach, following the method that management organizes the company's reportable segments for which separate financial information is made available to, and evaluated regularly by, the chief operating decision maker in allocating resources and in assessing performance. Cadence's chief operating decision maker is its President and Chief Executive Officer, or CEO, who reviews Cadence's consolidated results as one reportable segment. In making operating decisions, the CEO primarily considers consolidated financial information, accompanied by disaggregated information about revenues by geographic region.

Outside the United States, Cadence markets and supports its products and services primarily through its subsidiaries. Revenue is attributed to geography based on the country in which the product is used or services are delivered. Long-lived assets are attributed to geography based on the country where the assets are located.

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The following table presents a summary of revenue by geography for the three and six months ended June 30, 2012 and July 2, 2011:

	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
	(In thousands)			
<b>Americas:</b>				
United States	\$ 142,925	\$ 124,191	\$ 273,380	\$ 236,210
Other Americas	5,802	8,200	13,926	13,341
<b>Total Americas</b>	<b>148,727</b>	<b>132,391</b>	<b>287,306</b>	<b>249,551</b>
Europe, Middle East and Africa	64,996	56,458	124,705	112,734
Japan	53,880	49,194	110,099	99,359
Asia	58,873	45,227	120,196	87,728
<b>Total</b>	<b>\$ 326,476</b>	<b>\$ 283,270</b>	<b>\$ 642,306</b>	<b>\$ 549,372</b>

The following table presents a summary of long-lived assets by geography as of June 30, 2012 and December 31, 2011:

	As of	
	June 30, 2012	December 31, 2011
	(In thousands)	
<b>Americas:</b>		
United States	\$ 222,232	\$ 230,884
Other Americas	23	35
<b>Total Americas</b>	<b>222,255</b>	<b>230,919</b>
Europe, Middle East and Africa	4,858	4,813
Japan	2,695	3,960
Asia	22,112	22,825
<b>Total</b>	<b>\$ 251,920</b>	<b>\$ 262,517</b>

**NOTE 16. SUBSEQUENT EVENT**

On July 2, 2012, Cadence acquired Sigrity, Inc., or Sigrity, a provider of signal and power integrity analysis tools for system, printed circuit board and integrated circuit package design, for cash consideration of approximately \$78.3 million, net of cash acquired of approximately \$7.8 million. The consideration includes approximately \$14.2 million of cash payments that were deferred on the acquisition date and are conditioned upon certain Sigrity shareholders remaining employees of Cadence over designated retention periods. Cadence will expense the \$14.2 million over the designated retention periods. The remaining consideration of approximately \$64.1 million will be allocated based on the fair value of the net assets acquired. Cadence is in the process of determining the fair value of the net assets acquired and will include Sigrity's results of operations in its financial statements with effect from the purchase date. Comparative pro forma financial information for this acquisition has not been presented because the results of operations were not material to Cadence's Condensed Consolidated Financial Statements.

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

*The following discussion should be read in conjunction with the Condensed Consolidated Financial Statements and notes thereto included in this Quarterly Report on Form 10-Q, or this Quarterly Report, and in conjunction with our Annual Report on Form 10-K for the fiscal year ended December 31, 2011. Certain of these statements, including, but not limited to, statements regarding the extent and timing of future revenues and expenses and customer demand, statements regarding the deployment of our products, statements regarding our reliance on third parties and other statements using words such as anticipates, believes, could, estimates, expects, forecasts, intends, may, plans, projects, should, will and would, and words of similar import and the negatives thereof, constitute forward-looking statements. These statements are predictions based upon our current expectations about future events. Actual results could vary materially as a result of certain factors, including, but not limited to, those expressed in these statements. We refer you to the Risk Factors, Results of Operations, Disclosures About Market Risk, and Liquidity and Capital Resources sections contained in this Quarterly Report, and the risks discussed in our other Securities Exchange Commission, or SEC, filings, which identify important risks and uncertainties that could cause actual results to differ materially from those contained in the forward-looking statements.*

*We urge you to consider these factors carefully in evaluating the forward-looking statements contained in this Quarterly Report. All subsequent written or oral forward-looking statements attributable to our company or persons acting on our behalf are expressly qualified in their entirety by these cautionary statements. The forward-looking statements included in this Quarterly Report are made only as of the date of this Quarterly Report. We do not intend, and undertake no obligation, to update these forward-looking statements.*

#### **Overview**

We develop software, hardware and intellectual property which are used by semiconductor and electronic system customers to develop and design integrated circuits and electronic devices. We license our software, and two categories of intellectual property, or IP, commonly referred to as verification IP, or VIP, and Design IP. In addition, we sell and lease hardware technology. We provide maintenance for our product offerings and provide engineering services related to methodology, education, and hosted design solutions which help customers manage and accelerate their electronics product development processes.

Substantially all of our revenue is generated from integrated circuit, or IC, and electronics systems manufacturers and designers and is dependent upon their commencement of new design projects. As a result, our revenue is significantly influenced by our customers' business outlook and investment in the introduction of new products and the improvement of existing products.

In order to be competitive and profitable in the price-sensitive markets they serve, our customers demand high levels of productivity from their design teams, better predictability in their development

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schedules and high quality products. Semiconductor and electronics systems companies are responding to demand for increased functionality and miniaturization by combining subsystems such as radio frequency, or RF, wireless communication, video signal processing and microprocessors either onto a single silicon chip, creating a system-on-chip, or SoC, or by combining multiple chips into a single chip package in a format referred to as system-in-package, or SiP. The trend toward subsystem integration has required these chip makers to find solutions to challenges previously addressed by system companies, such as verifying system-level functionality and hardware-software interoperability.

Our offerings address many of the challenges associated with developing unique silicon circuitry, integrating that circuitry with Design IP developed by us or third parties to create SoCs, and combining ICs and SoCs with software to create electronic systems. Our strategy is to provide our customers with the ability to address the broad range of issues that arise at the silicon, SoC and system levels.

The most significant issues that our customers face in creating their products include optimizing energy consumption, manufacturing microscopic circuitry, verifying device functionality and achieving technical performance targets, all while meeting aggressive cost requirements. Our semiconductor and systems customers deliver a wide range of products in segments such as smart phones, tablets, televisions, communications and internet infrastructure, and computing platforms. Providers of EDA solutions must deliver products that address the technical challenges while improving the productivity, predictability, reliability and profitability of the design processes and products of their customers.

Our products are engineered to improve our customers design productivity and design quality by providing a comprehensive set of EDA solutions and a differentiated portfolio of Design IP and VIP. Product revenues include all fees earned from granting licenses to use our software and IP, and from sales and leases of our hardware products.

We combine our products and technologies into categories related to major design activities:

Digital IC Design;

Functional Verification and Design IP;

Custom IC Design;

Design for Manufacturing, or DFM; and

System Interconnect Design.

The major Cadence® design platforms are branded as Incisive® functional verification, Encounter® digital IC design, Virtuoso® custom design and Allegro® system interconnect design. Our functional verification offerings include VIP products and are supplemented by our Design IP offerings. In addition, we augment these platform product offerings with a set of DFM products that service both the digital and custom IC design flows.

The products and technologies included in these categories are combined with services, ready-to-use packages of technologies assembled from our broad portfolio and other associated components that provide comprehensive solutions for low power, mixed signal and advanced-node designs, as well as popular designs based on intellectual property owned and licensed by ARM Holdings, Plc. These solutions and their constituent elements are marketed to users who specialize in areas such as system design and verification, functional verification, logic design, digital implementation, custom IC design and printed circuit board, or PCB, and IC package and SiP design.

We have identified certain items that management uses as performance indicators to manage our business, including revenue, certain elements of operating expenses and cash flow from operations, and we describe these items further below under the heading Results of Operations and Liquidity and Capital Resources.





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### **Subsequent Event**

On July 2, 2012, we acquired Sigrity, Inc., or Sigrity, a provider of signal and power integrity analysis tools for system, printed circuit board and IC package design. We expect to incorporate the Sigrity technology into our Allegro and OrCad product offerings and to sell the Sigrity technology on a stand-alone basis as well.

### **Critical Accounting Estimates**

In preparing our Condensed Consolidated Financial Statements, we make assumptions, judgments and estimates that can have a significant impact on our revenue, operating income and net income, as well as on the value of certain assets and liabilities on our Condensed Consolidated Balance Sheets. We base our assumptions, judgments and estimates on historical experience and various other factors that we believe to be reasonable under the circumstances. Actual results could differ materially from these estimates under different assumptions or conditions. At least quarterly, we evaluate our assumptions, judgments and estimates and make changes accordingly. Historically, our assumptions, judgments and estimates relative to our critical accounting estimates have not differed materially from actual results. For further information about our critical accounting estimates, see the discussion in Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations, under the heading "Critical Accounting Estimates" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2011.

### **Results of Operations**

Financial results for the three and six months ended June 30, 2012, as compared to the three and six months ended July 2, 2011, reflect the following:

An increase in product revenue primarily because of:

A general increase in the annualized values of software contracts with our customers;

Increases in the sale and lease of our hardware products; and

Our continuing transition to a ratable license mix, under which most orders made in any period generate revenue in future periods.

An increase in employee-related costs, consisting primarily of variable compensation.

An increase in the provision for income taxes, primarily resulting from non-recurring tax benefits recognized during three and six months ended July 2, 2011.

### **Revenue**

We primarily generate revenue from licensing our EDA software and IP, selling or leasing our hardware technology, providing maintenance for our software, IP and hardware and providing engineering services. We principally use three license types: subscription, term and perpetual. The different license types provide a customer with different conditions of use for our products, such as:

The right to access new technology;

The duration of the license; and

Payment timing.

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The timing of our product revenue is significantly affected by the mix of license types in the bookings executed in any given period and whether the revenue for such bookings is recognized over multiple periods or up-front, upon completion of delivery.

We seek to achieve a mix of bookings with approximately 90% of the aggregate value of our bookings of a type for which the revenue is recurring, or ratable, in nature, and the remainder of the resulting revenue recognized up-front, upon completion of delivery. Our ability to achieve this bookings mix may be impacted by an increase in hardware sales beyond our current expectations, because revenue for hardware sales is generally recognized up-front in the quarter in which delivery is completed.

Approximately 90% of the aggregate value of our bookings during the three and six months ended June 30, 2012 and July 2, 2011 was of a type for which the revenue is recurring, or ratable, in nature.

For an additional description of the impact of hardware sales on the anticipated mix of bookings, our other license types and the timing of revenue recognition for license transactions, see the discussion under the heading *Critical Accounting Estimates Revenue Recognition* in *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations* in our Form 10-K for the fiscal year ended December 31, 2011.

Although we believe that pricing volatility has not generally been a material component of the change in our revenue from period to period, we believe that the amount of revenue recognized in future periods will depend on, among other things, the:

Competitiveness of our new technology;

Length of our sales cycle; and

Size, duration, timing, terms and type of:

Contract renewals with existing customers;

Additional sales to existing customers; and

Sales to new customers.

The value and renewal of contracts, and consequently product revenue recognized, are affected by the competitiveness of our products. Product revenue recognized in any period is also affected by the extent to which customers purchase subscription, term or perpetual licenses, and by the extent to which contracts contain flexible payment terms.

*Revenue by Period*

The following table shows our revenue for the three months ended June 30, 2012 and July 2, 2011 and the change in revenue between periods:

	Three Months Ended		Change	
	June 30, 2012	July 2, 2011	Amount	Percentage
	(In millions, except percentages)			
Product	\$ 208.3	\$ 157.9	\$ 50.4	32%
Services	29.0	29.5	(0.5)	(2)%

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Maintenance	89.2	95.9	(6.7)	(7)%
Total revenue	\$ 326.5	\$ 283.3	\$ 43.2	15%

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The following table shows our revenue for the six months ended June 30, 2012 and July 2, 2011 and the change in revenue between periods:

	Six Months Ended		Change	
	June 30, 2012	July 2, 2011	Amount	Percentage
	(In millions, except percentages)			
Product	\$ 398.3	\$ 299.8	\$ 98.5	33%
Services	58.5	57.3	1.2	2%
Maintenance	185.5	192.3	(6.8)	(4)%
Total revenue	\$ 642.3	\$ 549.4	\$ 92.9	17%

For software arrangements, we generally recognize revenue ratably over the duration of the arrangement and such revenue is allocated between product and maintenance revenue. As the duration decreases, the allocation to maintenance revenue decreases and the allocation to product revenue increases. Combined, product and maintenance revenue increased during the three and six months ended June 30, 2012, as compared to the three and six months ended July 2, 2011, primarily because of increased business levels, an increase in revenue related to the sale and lease of our hardware products and increased revenue recognized from bookings in prior periods. Maintenance revenue decreased on a standalone basis during the three and six months ended June 30, 2012, as compared to the three and six months ended July 2, 2011, primarily because of the increased allocation to product revenue due to the decreased duration of our software license arrangements.

*Revenue by Product Group*

The following table shows the percentage of product and related maintenance revenue contributed by each of our five product groups, and Services and other for the past five consecutive quarters:

	Three Months Ended				
	June 30, 2012	March 31, 2012	December 31, 2011	October 1, 2011	July 2, 2011
Functional Verification and Design IP	33%	30%	32%	30%	33%
Digital IC Design	22%	23%	21%	22%	21%
Custom IC Design	22%	23%	23%	23%	22%
System Interconnect	8%	8%	8%	9%	8%
Design for Manufacturing	6%	7%	6%	6%	6%
Services and other	9%	9%	10%	10%	10%
Total	100%	100%	100%	100%	100%

As described in Note 2 in the Notes to Consolidated Financial Statements in our Annual Report on Form 10-K for the fiscal year ended December 31, 2011, certain of our licensing arrangements allow customers the ability to remix among software products. Additionally, we have arrangements with customers that include a combination of our products, with the actual product selection and number of licensed users to be determined at a later date. For these arrangements, we estimate the allocation of the revenue to product groups based upon the expected usage of our products. The actual usage of our products by these customers may differ and, if that proves to be the case, the revenue allocation in the table above would differ.

The changes in the percentage of revenue contributed by the Functional Verification and Design IP product group for the quarters presented are generally related to changes in revenue related to our hardware products.

*Revenue by Geography*

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	Three Months Ended		Change	
	June 30, 2012	July 2, 2011	Amount	Percentage
	(In millions, except percentages)			
United States	\$ 142.9	\$ 124.2	\$ 18.7	15%
Other Americas	5.8	8.2	(2.4)	(29%)
Europe, Middle East and Africa	65.0	56.5	8.5	15%
Japan	53.9	49.2	4.7	10%
Asia	58.9	45.2	13.7	30%
Total revenue	\$ 326.5	\$ 283.3	\$ 43.2	15%

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	Six Months Ended		Change	
	June 30, 2012	July 2, 2011	Amount	Percentage
	(In millions, except percentages)			
United States	\$ 273.4	\$ 236.2	\$ 37.2	16%
Other Americas	13.9	13.3	0.6	5%
Europe, Middle East and Africa	124.7	112.8	11.9	11%
Japan	110.1	99.4	10.7	11%
Asia	120.2	87.7	32.5	37%
Total revenue	\$ 642.3	\$ 549.4	\$ 92.9	17%

For the primary factors contributing to our increase in revenue across our geographies see the general description under Revenue by Period above.

*Revenue by Geography as a Percent of Total Revenue*

	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
United States	44%	44%	43%	43%
Other Americas	2%	3%	2%	2%
Europe, Middle East and Africa	20%	20%	19%	21%
Japan	16%	17%	17%	18%
Asia	18%	16%	19%	16%
Total	100%	100%	100%	100%

No one customer accounted for 10% or more of total revenue during the three and six months ended June 30, 2012 and July 2, 2011.

Most of our revenue is transacted in the United States dollar. However, certain transactions are denominated in foreign currencies, primarily the Japanese yen, and we recognize additional revenue from those contracts in periods when the United States dollar weakens in value against the Japanese yen and reduced revenue from those contracts in periods when the United States dollar strengthens against the Japanese yen. For an additional description of how changes in foreign exchange rates affect our Condensed Consolidated Financial Statements, see the discussion under the heading Item 3. Quantitative and Qualitative Disclosures About Market Risk Foreign Currency Risk.

**Cost of Revenue**

	Three Months Ended		Change	
	June 30, 2012	July 2, 2011	Amount	Percentage
	(In millions, except percentages)			
Product	\$ 21.6	\$ 20.1	\$ 1.5	7%
Services	17.1	\$ 20.6	(3.5)	(17%)
Maintenance	10.8	\$ 10.7	0.1	1%

	Six Months Ended		Change	
	June 30, 2012	July 2, 2011	Amount	Percentage
	(In millions, except percentages)			

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Product	\$ 37.0	\$ 34.3	\$ 2.7	8%
Services	36.4	\$ 40.7	(4.3)	(11%)
Maintenance	22.6	\$ 21.6	1.0	5%



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The following table shows cost of revenue as a percentage of related revenue for the three and six months ended June 30, 2012 and July 2, 2011:

	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
Product	10%	13%	9%	11%
Services	59%	70%	62%	71%
Maintenance	12%	11%	12%	11%

*Cost of Product*

Cost of product includes costs associated with the sale and lease of our hardware and licensing of our software and IP products. Cost of product associated with our hardware products includes materials, assembly and overhead. These additional hardware manufacturing costs make our cost of hardware product higher, as a percentage of revenue, than our cost of software and IP products. Cost of product also includes the cost of employee salary, benefits and other employee-related costs, including stock-based compensation expense, amortization of acquired intangibles directly related to our products, as well as the costs of technical documentation and royalties payable to third-party vendors.

A summary of cost of product is as follows:

	Three Months Ended		Change	
	June 30, 2012	July 2, 2011	Amount	Percentage
	(In millions, except percentages)			
Product-related costs	\$ 18.7	\$ 17.6	\$ 1.1	6%
Amortization of acquired intangibles	2.9	2.5	0.4	16%
<b>Total cost of product</b>	<b>\$ 21.6</b>	<b>\$ 20.1</b>	<b>\$ 1.5</b>	<b>7%</b>

	Six Months Ended		Change	
	June 30, 2012	July 2, 2011	Amount	Percentage
	(In millions, except percentages)			
Product-related costs	\$ 31.2	\$ 29.6	\$ 1.6	5%
Amortization of acquired intangibles	5.8	4.7	1.1	23%
<b>Total cost of product</b>	<b>\$ 37.0</b>	<b>\$ 34.3</b>	<b>\$ 2.7</b>	<b>8%</b>

The changes in cost of product during the three and six months ended June 30, 2012, as compared to the three and six months ended July 2, 2011, were primarily due to increases in hardware costs and amortization of acquired intangibles. Hardware costs increased primarily due to an increase in hardware sales. Amortization of acquired intangibles included in cost of product increased primarily due to amortization of intangible assets acquired with our fiscal 2011 acquisitions.

Cost of product depends primarily upon the mix of hardware and software product sales in any given period, and also depends upon the extent to which we acquire intangible assets, acquire or license third-parties intellectual property or technology and sell our products that include such acquired or licensed intellectual property or technology.

**Table of Contents***Cost of Services*

Cost of services primarily includes employee salary, benefits and other employee-related costs, costs to maintain the infrastructure necessary to manage a services organization, and provisions for contract losses, if any. Cost of services decreased by \$3.5 million during the three months ended June 30, 2012, as compared to the three months ended July 2, 2011, and decreased by \$4.3 million during the six months ended June 30, 2012, as compared to the six months ended July 2, 2011, primarily due to a decrease in employee salary, benefits and other employee-related costs. Certain of our design services engineers have been redeployed to internal research and development projects or to assist with pre-sales activities, resulting in lower cost of services expense. We expect to continue to utilize our services engineers on internal projects and expect our cost of services to continue to decrease during the remainder of fiscal 2012, as compared to fiscal 2011.

*Cost of Maintenance*

Cost of maintenance includes the cost of our customer support services, such as telephone, online and on-site support, employee salary, benefits and other employee-related costs, and documentation of maintenance updates. There were no significant changes in cost of maintenance during the three and six months ended June 30, 2012, as compared to the three and six months ended July 2, 2011.

**Operating Expenses**

Our operating expenses include marketing and sales, research and development and general and administrative expenses. Factors that may cause our operating expenses to fluctuate include changes in the number of employees due to hiring, acquisitions or restructuring activities, foreign exchange rates, cost reduction strategies and the impact of our variable compensation programs, which are driven by overall operating results. Our employee salary and other compensation-related costs increased during the three and six months ended June 30, 2012, when compared to the three and six months ended July 2, 2011, primarily due to improved business levels resulting in higher variable compensation and due to hiring additional research and development employees.

We expect our operating expenses to increase during the remainder of fiscal 2012, as compared to the same period in 2011, due to anticipated hiring during the remainder of fiscal 2012 and due to our acquisition of Sigrity on July 2, 2012.

Our operating expenses for the three and six months ended June 30, 2012 and July 2, 2011 were as follows:

	Three Months Ended		Change	
	June 30, 2012	July 2, 2011	Amount	Percentage
	(In millions, except percentages)			
Operating expenses	\$ 222.6	\$ 201.7	\$ 20.9	10%
Percentage of total revenue	68%	71%		

	Six Months Ended		Change	
	June 30, 2012	July 2, 2011	Amount	Percentage
	(In millions, except percentages)			
Operating expenses	\$ 442.8	\$ 400.7	\$ 42.1	11%
Percentage of total revenue	69%	73%		

**Table of Contents***Marketing and Sales*

	Three Months Ended		Change	
	June 30, 2012	July 2, 2011	Amount	Percentage
	(In millions, except percentages)			
Marketing and sales	\$ 80.4	\$ 77.0	\$ 3.4	4%
Percentage of total revenue	25%	27%		

	Six Months Ended		Change	
	June 30, 2012	July 2, 2011	Amount	Percentage
	(In millions, except percentages)			
Marketing and sales	\$ 164.2	\$ 155.4	\$ 8.8	6%
Percentage of total revenue	26%	28%		

The changes in marketing and sales expense for the three and six months ended June 30, 2012, as compared to the three and six months ended July 2, 2011, were due to the following:

	Change	
	Three Months Ended	Six Months Ended
	(In millions)	
Salary, benefits and other employee-related costs	\$ 3.3	\$ 7.8
Other individually insignificant items	0.1	1.0
	\$ 3.4	\$ 8.8

*Research and Development*

	Three Months Ended		Change	
	June 30, 2012	July 2, 2011	Amount	Percentage
	(In millions, except percentages)			
Research and development	\$ 112.0	\$ 99.3	\$ 12.7	13%
Percentage of total revenue	34%	35%		

	Six Months Ended		Change	
	June 30, 2012	July 2, 2011	Amount	Percentage
	(In millions, except percentages)			
Research and development	\$ 220.6	\$ 200.6	\$ 20.0	10%
Percentage of total revenue	34%	37%		

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The changes in research and development expense for the three and six months ended June 30, 2012, as compared to the three and six months ended July 2, 2011, were due to the following:

	Change	
	Three Months Ended	Six Months Ended
	(In millions)	
Salary, variable compensation, benefits and other employee-related costs	\$ 9.7	\$ 16.2
Other individually insignificant items	3.0	3.8
	\$ 12.7	\$ 20.0

*General and Administrative*

	Three Months Ended		Change	
	June 30, 2012	July 2, 2011	Amount	Percentage
	(In millions, except percentages)			
General and administrative	\$ 30.2	\$ 25.4	\$ 4.8	19%
Percentage of total revenue	9%	9%		

	Six Months Ended		Change	
	June 30, 2012	July 2, 2011	Amount	Percentage
	(In millions, except percentages)			
General and administrative	\$ 58.0	\$ 44.7	\$ 13.3	30%
Percentage of total revenue	9%	8%		

The changes in general and administrative expense for the three and six months ended June 30, 2012, as compared to the three and six months ended July 2, 2011, were due to the following:

	Change	
	Three Months Ended	Six Months Ended
	(In millions)	
Professional services	\$ 2.4	\$ 4.3
Salary, benefits and other employee-related costs	0.7	1.1
Net recoveries of allowance for doubtful accounts	0.7	5.9
Other individually insignificant items	1.0	2.0
	\$ 4.8	\$ 13.3

We recorded net recoveries of our allowance for doubtful accounts of \$5.9 million during the six months ended July 2, 2011 because we collected certain receivables that previously had been included in our allowance for doubtful accounts. We had previously recorded reserves for certain customers based on changes in our assessment of collectability for those customers. The principal factor for the assessment at that time was a general deterioration of economic conditions having a significant impact on certain customers. These customers' business prospects eventually improved, and we were able to collect the majority of those receivables that had previously been reserved, resulting in recoveries of previously reserved bad debts.

**Amortization of Acquired Intangibles**

	Three Months Ended		Change	
	June 30, 2012	July 2, 2011	Amount	Percentage
	(In millions, except percentages)			
Amortization of acquired intangibles	\$ 3.6	\$ 4.5	\$ (0.9)	(20)%

	Six Months Ended		Change	
	June 30, 2012	July 2, 2011	Amount	Percentage
	(In millions, except percentages)			
Amortization of acquired intangibles	\$ 7.4	\$ 9.0	\$ (1.6)	(18)%

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The change in amortization of acquired intangibles resulted from certain acquired intangibles becoming fully amortized.

**Interest Expense**

	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
	(In millions)			
<b>Contractual cash interest expense:</b>				
2011 Notes	\$	\$ 0.5	\$	\$ 1.0
2013 Notes	0.5	0.5	1.0	1.1
2015 Notes	2.3	2.3	4.6	4.6
<b>Amortization of debt discount:</b>				
2011 Notes		1.7		3.5
2013 Notes	1.5	1.5	3.0	2.9
2015 Notes	3.6	3.4	7.2	6.7
<b>Amortization of deferred financing costs:</b>				
2011 Notes		0.2		0.3
2013 Notes	0.1	0.1	0.2	0.2
2015 Notes	0.5	0.5	1.0	0.9
Other	0.1	0.1	0.1	0.6
<b>Total interest expense</b>	<b>\$ 8.6</b>	<b>\$ 10.8</b>	<b>\$ 17.1</b>	<b>\$ 21.8</b>

**Other Income, Net**

Other income, net, for the three and six months ended June 30, 2012 and July 2, 2011 was as follows:

	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
	(In millions)			
Interest income	\$ 0.3	\$ 0.3	\$ 0.7	\$ 0.7
Gains on sale of marketable equity securities		8.0	0.1	8.0
Gains on sale of non-marketable equity investments		0.1		2.7
Gains on trading securities in the non-qualified deferred compensation trust	2.3	1.2	4.1	2.9
Gains (losses) on foreign exchange	1.1	(1.3)	1.2	(1.7)
Other income, net		0.1		0.3
<b>Total other income, net</b>	<b>\$ 3.7</b>	<b>\$ 8.4</b>	<b>\$ 6.1</b>	<b>\$ 12.9</b>

**Table of Contents****Income Taxes**

The following table presents the provision for income taxes and the effective tax rate for the three and six months ended June 30, 2012 and July 2, 2011:

	Three Months Ended		Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
	(In millions, except percentages)			
Provision (benefit) for income taxes	\$ 9.3	\$ (4.3)	\$ 17.5	\$ 0.4
Effective tax rate	20.4%	(19.2%)	20.6%	1.1%

Our provision for income taxes for the three and six months ended June 30, 2012 primarily consisted of tax expense related to certain of our foreign subsidiaries, interest expense on unrecognized tax benefits, and excess tax benefits from stock-based compensation that were allocated to equity. Our provision (benefit) for income taxes for the three and six months ended July 2, 2011 primarily consisted of a tax benefit related to the effective settlement of the Internal Revenue Service, or IRS, examination of our federal income tax returns for the tax years 2003 through 2005 and a tax benefit from the release of valuation allowance against our deferred tax assets, due to the acquisition of intangible assets held by a company acquired during the periods.

We estimate our annual effective tax rate for fiscal 2012 to be approximately 10.0%, consisting of tax expense related to certain of our foreign subsidiaries, interest expense on unrecognized tax benefits, excess tax benefits from stock-based compensation allocated to equity and the expected release of valuation allowance against our deferred tax assets due to the acquisition of intangible assets held by Sigrity which was acquired on July 2, 2012. Our estimate excludes additional excess tax benefits from stock-based compensation that may be allocated to equity in future periods since the excess tax benefits cannot be reasonably estimated. Excess tax benefits from stock-based compensation that are allocated to equity will increase the annual effective tax rate. Our estimate also does not include any tax expense or tax benefit related to effective settlements of tax examinations that may occur in the future.

We regularly review our deferred tax assets for recoverability and establish a valuation allowance if it is more than 50% likely that some portion or all of the deferred tax assets will not be realized. Our cumulative loss in the United States incurred over the three year period ended June 30, 2012 was considered significant negative evidence with a high level of objectivity that outweighed our ability to rely on projections of future income in determining whether a valuation allowance was needed. It is reasonably possible that we could have cumulative income over a three year period within the next twelve months. If, in the future, we determine that these deferred tax assets are more likely than not to be realized, a release of all or part of the related valuation allowance could result in a material income tax benefit in the period such determination is made.

For further discussion regarding our income taxes, including the status of examinations by tax authorities and considerations related to the establishment or release of valuation allowance, see Note 6 in the Notes to Consolidated Financial Statements in our Annual Report on Form 10-K for the fiscal year ended December 31, 2011.

**Liquidity and Capital Resources**

	As of		Change
	June 30, 2012	December 31, 2011	
	(In millions)		
Cash, cash equivalents and short-term investments	\$ 713.0	\$ 604.6	\$ 108.4
Net working capital	\$ 155.6	\$ 48.6	\$ 107.0

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	Six Months Ended		
	June 30, 2012	July 2, 2011	Change
		(In millions)	
Cash provided by operating activities	\$ 128.2	\$ 125.8	\$ 2.4
Cash used for investing activities	\$ (68.5)	\$ (22.4)	\$ (46.1)
Cash provided by financing activities	\$ 4.3	\$ 1.1	\$ 3.2

**Cash and Cash Equivalents and Short-term Investments**

As of June 30, 2012, our principal sources of liquidity consisted of \$713.0 million of cash, cash equivalents and short-term investments, as compared to \$604.6 million as of December 31, 2011.

During the three months ended June 30, 2012, we invested \$49.1 million of our cash equivalents in marketable debt securities, including corporate debt securities, United States Treasury securities, United States government agency securities, bank certificates of deposit and commercial paper. Our investments in marketable debt securities are classified as available for sale and are included in short-term investments as of June 30, 2012. Our investments are made in accordance with our cash investment policy, which governs the amounts and types of investments we hold in our portfolio. Our investment portfolio could be affected by various risks and uncertainties including credit risk, interest rate risk and general market risk, as outlined in Part II, Item 1A, Risk Factors.

Our primary source of cash, cash equivalents and short-term investments during the six months ended June 30, 2012 was customer payments for products, maintenance and services. We also received cash from stock purchases under our ESPP and from the exercise of stock options.

Our primary use of cash, cash equivalents and short-term investments during the six months ended June 30, 2012 was payments relating to salaries, benefits, other employee-related costs and other operating expenses. We also used cash to purchase property, plant and equipment.

Approximately 50% of our cash, cash equivalents and short-term investments were held by our foreign subsidiaries as of June 30, 2012. Our intent is to permanently reinvest our earnings from certain foreign operations. We do not anticipate we will need to repatriate dividends from foreign operations that are permanently reinvested in order to fund our domestic operations. In the event that dividends from foreign operations that are currently permanently reinvested are needed to fund United States liquidity, we could be required to accrue and pay additional taxes in order to repatriate these funds.

We expect that current cash, cash equivalents and short-term investment balances and cash flows that are generated from operations will be sufficient to meet our working capital, other capital and liquidity requirements for at least the next 12 months.



**Table of Contents****Net Working Capital**

Net working capital increased by \$107.0 million as of June 30, 2012, as compared to December 31, 2011, due to the following:

	Change (In millions)
Increase in cash and cash equivalents	\$ 60.1
Increase in short-term investments	48.3
Decrease in current portion of deferred revenue	12.0
Decrease in accounts payable and accrued liabilities	11.8
Decrease in prepaid expenses and other	(2.2)
Decrease in inventories	(2.2)
Increase in convertible notes	(7.2)
Decrease in receivables, net	(13.5)
Other individually insignificant items	(0.1)
	\$ 107.0

The 2015 Notes are convertible into cash from July 1, 2012 through September 29, 2012 because our closing stock price exceeded \$9.81 for at least 20 of the last 30 trading days prior to June 30, 2012. Accordingly, the net balance of the 2015 Notes of \$301.3 million is classified as a current liability on our Condensed Consolidated Balance Sheet as of June 30, 2012. The classification of the 2015 Notes as a current or long-term liability on the Condensed Consolidated Balance Sheet is evaluated at each balance sheet date and may change from time to time, depending on whether the stock price conversion condition, as described above, has been met in a particular fiscal quarter. If the note holders elect to convert their 2015 Notes prior to maturity, any unamortized discount and transaction fees will be expensed at the time of conversion. If the entire outstanding principal amount had been converted on June 30, 2012, we would have recorded an expense of \$55.4 million associated with the conversion, comprised of \$48.7 million of unamortized debt discount and \$6.7 million of unamortized transaction fees.

The classification of the liability associated with the 2015 Notes Embedded Conversion Derivative and the 2015 Notes Hedges asset as current or long-term on our Condensed Consolidated Balance Sheet corresponds with the classification of the 2015 Notes. As such, we classified the fair value of the 2015 Notes Embedded Conversion Derivative as a current liability on our Condensed Consolidated Balance Sheets as of June 30, 2012 and December 31, 2011. We also classified the fair value of the 2015 Notes Hedges as current assets on our Condensed Consolidated Balance Sheets as of June 30, 2012 and December 31, 2011. The value of the 2015 Notes Embedded Conversion Derivative liability and the value of the 2015 Notes Hedges asset offset one another and the changes in the fair value of these instruments resulted in no net change to our net working capital as of June 30, 2012.

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If the holders of our 2015 Notes elect to convert their notes into cash, we would be required to make cash payments of up to \$350.0 million prior to the maturity of the 2015 Notes. In connection with the 2015 Notes, we entered into the 2015 Notes Hedges and sold warrants to limit our exposure to the additional cash payments above the \$350.0 million principal balance in the event of a cash conversion of the 2015 Notes. The 2015 Notes currently trade at a premium to their if-converted value, and we do not anticipate a conversion of the 2015 Notes by the note holders between July 1, 2012 and September 29, 2012. However, if the holders of the 2015 Notes elect to convert their notes between July 1, 2012 and September 29, 2012, we expect to have sufficient cash, cash equivalents and short-term investments to fund any payment resulting from a conversion.

For an additional description of our 2015 Notes, and the conversion terms thereof, see Note 2 in the Notes to Condensed Consolidated Financial Statements.

**Cash Flows from Operating Activities**

Cash flows from operating activities increased \$2.4 million during the six months ended June 30, 2012, as compared to the six months ended July 2, 2011, due to the following:

	Change (In millions)
Net income, net of non-cash related gains and losses	\$ 52.4
Changes in operating assets and liabilities, net of effect of acquired businesses	(50.0)
	\$ 2.4

Cash flows from operating activities include net income, adjusted for certain non-cash charges, as well as changes in the balances of certain assets and liabilities. Our cash flows from operating activities are significantly influenced by business levels and the payment terms set forth in our license agreements.

If our customers experience adverse changes in the future, are not successful in generating sufficient cash or are precluded from securing financing, they may delay purchasing our products and services, or they may not be able to pay, or may delay payment of, accounts receivable that are owed to us, although these obligations are generally not cancelable. Our customers' inability to fulfill payment obligations would adversely affect our cash flow. Additionally, our customers may seek to renegotiate pre-existing contractual commitments. Though we have not experienced a material level of defaults, any material payment default by our customers or significant reductions in existing contractual commitments would have a material adverse effect on our financial condition and cash flows from operations.

We expect to pay an additional \$4.5 million related to our previous restructuring activities, primarily for payments related to vacated facilities, net of expected sublease income.

We expect that cash flows from operating activities will fluctuate in future periods due to a number of factors, including our operating results and the timing of our billings, collections and tax payments.

**Cash Flows from Investing Activities**

The changes in net cash used for investing activities for the six months ended June 30, 2012, as compared to the six months ended July 2, 2011, were due to the following:

	Change (In millions)
Purchases of available-for-sale securities	\$ (49.1)
Proceeds from the sale and maturity of available-for-sale securities	(9.5)
Purchases of property, plant and equipment	(7.0)

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Proceeds from the sale of long-term investments	(2.8)
Cash paid in business combinations and asset acquisitions, net of cash acquired	21.8
Other individually insignificant items	0.5
	\$ (46.1)

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During the three months ended June 30, 2012, we invested \$49.1 million of our cash equivalents in marketable debt securities. For an additional description of these investments, see [Cash and Cash Equivalents and Short-term Investments](#) above.

In connection with our business combinations and asset acquisitions completed before June 30, 2012, we may be obligated to make payments based on, or subject to the satisfaction of, certain performance metrics. If performance is such that these payments are fully achieved, we would be obligated to pay up to an aggregate of \$21.2 million in cash during the next 46 months.

On July 2, 2012, we acquired Sigrity for cash consideration of approximately \$78.3 million, net of cash acquired of approximately \$7.8 million. The consideration includes approximately \$14.2 million of cash payments that were deferred on the acquisition date and are conditioned upon certain Sigrity shareholders remaining employees of Cadence over designated retention periods. We will expense the \$14.2 million over the designated retention periods and will include these payments as a use of cash for operating activities in the period we make the payments. During July 2012, we paid approximately \$64.1 million, net of the cash acquired, related to the Sigrity acquisition that we will include as a use of cash for investing activities during the three months ending September 29, 2012.

We expect to continue our investing activities, including purchasing property, plant and equipment, purchasing intangible assets, purchasing software licenses, business combinations, and making long-term equity investments.

**Cash Flows from Financing Activities**

The changes in net cash provided by financing activities for the six months ended June 30, 2012, as compared to the six months ended July 2, 2011, were due to the following:

	Change (In millions)
Tax effect related to employee stock transactions allocated to equity	\$ 3.1
Proceeds from the issuance of common stock	2.8
Stock received for payment of employee taxes on vesting of restricted stock	(2.5)
Other individually insignificant items	(0.2)
	\$ 3.2

For an additional description of our 2013 Notes and 2015 Notes, and the conversion terms thereof, see Note 2 in our Notes to Condensed Consolidated Financial Statements and [Net Working Capital](#), above.

**Other Factors Affecting Liquidity and Capital Resources**

As of June 30, 2012, we had convertible notes outstanding with a net liability value of \$436.1 million and that mature between December 15, 2013 and June 1, 2015. The principal maturity value of these convertible notes is \$494.5 million. The total cash or stock payable upon the early conversion of these notes, as determined by the indenture of each security, will be their principal amount plus any additional conversion value that would be due upon conversion.

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In the case of our 2015 Notes, we will owe additional cash to the note holders upon early conversion if our stock price exceeds \$7.55 per share. We entered into hedges with counterparties to limit our exposure to the additional cash payments above the principal amount of the 2015 Notes that may be due to the holders upon conversion. In separate transactions, we sold warrants, or the 2015 Warrants, with a strike price of \$10.78 per share. Although our incremental cash payout exposure above the conversion price is limited by the hedges to the \$350.0 million outstanding principal value of the 2015 Notes, we will experience dilution to our stock and to our diluted earnings per share from the outstanding 2015 Warrants to the extent our average closing stock price exceeds \$10.78 in any fiscal quarter until the 2015 Notes are converted and the 2015 Warrants are settled.

Additionally, holders may convert their 2015 Notes into cash during any quarter following a quarter in which our stock price closes above \$9.81 for at least 20 of the last 30 trading days. While holders of the 2015 Notes would have the right to convert their notes if early conversion conditions are met, we do not expect holders of the 2015 Notes to convert their notes under such circumstances because the economic value to the holders of the notes has exceeded and likely will continue to exceed the cash received upon conversion. If the holders of the 2015 Notes elect to convert their notes between July 1, 2012 and September 29, 2012, we expect to have sufficient cash, cash equivalents and short-term investments to fund any payment resulting from a conversion. However, if holders of a significant portion of the 2015 Notes were to choose to convert at a time in which the notes are convertible, it could have a significant negative impact on our cash, cash equivalents and short-term investments and liquidity.

In the case of our 2013 Notes, we may owe shares of our common stock to the note holders upon conversion if our stock price exceeds \$21.15 per share. We entered into hedges with counterparties to limit our exposure to the dilution that may result from the issuance of shares upon conversion of the 2013 Notes. In separate transactions, we sold warrants with a strike price of \$31.50 per share. We will experience dilution to our stock and to diluted earnings per share from the outstanding warrants to the extent our stock price exceeds \$31.50.

We expect to fund the maturity of the 2013 Notes in December 2013 with our cash on hand and future cash flows from operations. The 2013 Notes could become convertible prior to their maturity if certain conversion conditions are met. However, we do not currently expect any of the conversion conditions to be met prior to the maturity of the 2013 Notes. We also believe that we will have sufficient cash in future periods to service the maturities of our 2015 Notes, but future changes in our cash position, cash flows from operating activities, cash flows from investing activities, cash flows from financing activities, as well as general business levels and changes in our access to financing may impact our ability to settle the principal amount payable to the holders of the 2013 Notes and 2015 Notes when they mature or convert.

For an additional description of the 2015 Notes and 2013 Notes, the conversion terms thereof and the hedge and warrants transactions, see Note 2 in our Notes to Condensed Consolidated Financial Statements and Net Working Capital, above.

## **Item 3. Quantitative and Qualitative Disclosures About Market Risk**

### **Foreign Currency Risk**

A material portion of our revenue, expenses and business activity are transacted in the United States dollar. However, certain of our operations include transactions in foreign currencies that can affect our results

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of operations. In certain countries where we invoice customers in the local currency, Japan in particular, our revenues benefit from a weaker dollar and are adversely affected by a stronger dollar. The opposite impact occurs in countries where we record expenses in local currencies. In those cases, our operating expenses benefit from a stronger dollar and are adversely affected by a weaker dollar. Most of our revenue is transacted in United States dollars. The fluctuations in our operating expenses outside the United States resulting from volatility in the United States dollar against certain foreign currencies are not generally moderated by corresponding fluctuations in our revenues, except for our operations in Japan.

We enter into foreign currency forward exchange contracts with financial institutions to protect against currency exchange risks associated with existing assets and liabilities. A foreign currency forward exchange contract acts as a hedge by increasing in value when underlying assets decrease in value or underlying liabilities increase in value due to changes in foreign exchange rates. Conversely, a foreign currency forward exchange contract decreases in value when underlying assets increase in value or underlying liabilities decrease in value due to changes in foreign exchange rates. These forward contracts are not designated as accounting hedges, so the unrealized gains and losses are recognized in other income, net, in advance of the actual foreign currency cash flows with the fair value of these forward contracts being recorded as accrued liabilities or other current assets.

We do not use forward contracts for trading purposes. Our forward contracts generally have maturities of 90 days or less. We enter into currency forward exchange contracts based on estimated future asset and liability exposures, and the effectiveness of our hedging program depends on our ability to estimate these future asset and liability exposures. Recognized gains and losses with respect to our current hedging activities will ultimately depend on how accurately we are able to match the amount of currency forward exchange contracts with actual underlying asset and liability exposures.

The following table provides information about our forward foreign currency contracts as of June 30, 2012. The information is provided in United States dollar equivalent amounts. The table presents the notional amounts, at contract exchange rates, and the weighted average contractual foreign currency exchange rates expressed as units of the foreign currency per United States dollar, which in some cases may not be the market convention for quoting a particular currency. All of these forward contracts mature before or during August 2012.

	Notional Principal (In millions)	Weighted Average Contract Rate
<b>Forward Contracts:</b>		
British pound	\$ 34.4	0.65
European Union euro	30.4	0.80
India rupee	22.3	56.04
Japanese yen	17.1	78.36
Chinese renminbi	17.0	6.35
Canadian dollar	13.5	1.03
Other	23.1	N/A
<b>Total</b>	<b>\$ 157.8</b>	
 Estimated fair value	 \$ 0.9	

While we actively monitor our foreign currency risks, there can be no assurance that our foreign currency hedging activities will substantially offset the impact of fluctuations in currency exchange rates on our results of operations, cash flows and financial position.

**Table of Contents****Interest Rate Risk**

Our exposure to market risk for changes in interest rates relates primarily to our portfolio of marketable debt securities and to our portfolio of cash and cash equivalents. We are exposed to interest rate fluctuations in many of the world's leading industrialized countries, but the fair value of our marketable debt securities and our interest income and expense is most sensitive to fluctuations in the general level of United States interest rates. In this regard, changes in United States interest rates affect the interest earned on our marketable debt securities and cash and cash equivalents, any unrealized and realized gains or losses on our marketable debt securities and the costs associated with foreign currency hedges. As part of our investment policy, we limit the amount of our credit exposure to any one issuer, other than in securities issued by the United States Treasury and United States government agencies.

Our short-term investments as of June 30, 2012 include \$49.0 million of marketable debt securities that may have their market value adversely impacted if market interest rates rise. Such variability in market interest rates may result in a negative impact on the results of our investment activities. As of June 30, 2012, an increase in the market rates of interest of 1% would result in a decrease in the fair values of our marketable debt securities by approximately \$0.6 million.

All highly liquid securities with a maturity of three months or less at the date of purchase are considered to be cash equivalents. Securities with maturities greater than three months are classified as available for sale and are considered to be short-term investments. The carrying value of our interest-bearing instruments approximated fair value as of June 30, 2012.

**Equity Price Risk****Convertible Notes**

Our 2015 Notes and 2013 Notes include conversion and settlement provisions that are based on the price of our common stock at conversion or at maturity of the notes. In addition, the hedges and warrants associated with these convertible notes also include settlement provisions that are based on the price of our common stock. The amount of cash we may be required to pay, or the number of shares we may be required to provide to note holders at conversion or maturity of these notes, is determined by the price of our common stock. The amount of cash or number of shares that we may receive from hedge counterparties in connection with the related hedges and the number of shares that we may be required to provide warrant counterparties in connection with the related warrants are also determined by the price of our common stock.

Upon the expiration of our 2015 Warrants, Cadence will issue shares of common stock to the purchasers of the warrants to the extent our stock price exceeds the warrant strike price of \$10.78 at that time. The following table shows the number of shares that Cadence would issue to 2015 Warrant counterparties at expiration of the warrants assuming various Cadence closing stock prices on the date of warrant expiration:

	Shares (In millions)
\$11.00	0.9
\$12.00	4.7
\$13.00	7.9
\$14.00	10.7
\$15.00	13.0
\$16.00	15.1

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Prior to the expiration of the 2015 Warrants, our diluted weighted-average shares outstanding for purposes of calculating diluted earnings per share will increase when our average closing stock price for a quarter exceeds \$10.78.

For an additional description of our 2015 Notes and 2013 Notes, see Note 2 in our Notes to Condensed Consolidated Financial Statements and Liquidity and Capital Resources – Other Factors Affecting Liquidity and Capital Resources, under Item 2, Management’s Discussion and Analysis of Financial Condition and Results of Operations.

## **Equity Investments**

We have a portfolio of equity investments that includes marketable equity securities and non-marketable investments. Our equity investments are made primarily in connection with our strategic investment program. Under our strategic investment program, from time to time we make cash investments in companies with technologies that are potentially strategically important to us. See Note 8 in Notes to Condensed Consolidated Financial Statements, and Note 10 in the Notes to Consolidated Financial Statements in our Annual Report on Form 10-K for the fiscal year ended December 31, 2011, for an additional description of these investments. Our non-marketable investments had a carrying value of \$10.5 million as of June 30, 2012 and as of December 31, 2011.

## **Item 4. Controls and Procedures**

### **Evaluation of Disclosure Controls and Procedures**

As required by Rule 13a-15 of the Securities Exchange Act of 1934, as amended, or the Exchange Act, under the supervision and with the participation of our management, including our Chief Executive Officer, or CEO, and our Chief Financial Officer, or CFO, we evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of June 30, 2012.

The evaluation of our disclosure controls and procedures included a review of our processes and the effect on the information generated for use in this Quarterly Report on Form 10-Q. In the course of this evaluation, we sought to identify any material weaknesses in our disclosure controls and procedures, to determine whether we had identified any acts of fraud involving personnel who have a significant role in our disclosure controls and procedures, and to confirm that any necessary corrective action, including process improvements, was taken. This type of evaluation is done every fiscal quarter so that our conclusions concerning the effectiveness of these controls can be reported in our periodic reports filed with the SEC. The overall goals of these evaluation activities are to monitor our disclosure controls and procedures and to make modifications as necessary. We intend to maintain these disclosure controls and procedures, modifying them as circumstances warrant.

Based on their evaluation as of June 30, 2012, our CEO and CFO have concluded that our disclosure controls and procedures were effective to provide reasonable assurance that the information required to be disclosed by us in our reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms and is accumulated and communicated to our management, including the CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.



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### **Changes in Internal Control Over Financial Reporting**

There were no changes in our internal control over financial reporting during the fiscal quarter ended June 30, 2012 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

### **Inherent Limitations on Effectiveness of Controls**

Our management, including our CEO and CFO, does not expect that our disclosure controls and procedures or our internal control over financial reporting will prevent or detect all errors and all fraud. Internal control over financial reporting, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of internal control are met. Further, the design of internal control must reflect the fact that there are resource constraints, and the benefits of the control must be considered relative to their costs. While our disclosure controls and procedures and internal control over financial reporting are designed to provide reasonable assurance of their effectiveness, because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within Cadence, have been detected.

## **PART II. OTHER INFORMATION**

### **Item 1. Legal Proceedings**

From time to time, we are involved in various disputes and litigation that arise in the ordinary course of business. These include disputes and lawsuits related to intellectual property, indemnification obligations, mergers and acquisitions, licensing, contracts, distribution arrangements and employee relations matters. At least quarterly, we review the status of each significant matter and assess our potential financial exposure. If the potential loss from any claim or legal proceeding is considered probable and the amount or the range of loss can be estimated, we accrue a liability for the estimated loss. Legal proceedings are subject to uncertainties, and the outcomes are difficult to predict. Because of such uncertainties, accruals are based on our judgments using the best information available at the time. As additional information becomes available, we reassess the potential liability related to pending claims and litigation matters and may revise our estimates.

On April 23, 2012, the United States District Court entered final approval of the settlements of the pending derivative and securities litigation, and dismissed those lawsuits. See Note 12 in our Notes to Condensed Consolidated Financial Statements for an additional description of our legal proceedings and these settlements.

### **Item 1A. Risk Factors**

*Our operations and financial results are subject to various risks and uncertainties, including those described below, that could adversely affect our business, financial condition, results of operations, cash flows, and the trading price of our common stock.*

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### **Risks Related to Our Business**

#### **Uncertainty in the global economy in general, and any potential downturn in the semiconductor and electronics industries in particular, may negatively impact our business and reduce our bookings levels and revenue.**

Purchases of our products and services are dependent upon the commencement of new design projects by IC manufacturers and electronics systems companies. The IC and electronics systems industries are cyclical and are characterized by constant and rapid technological change, rapid product obsolescence and price erosion, evolving standards, short product life cycles and wide fluctuations in product supply and demand.

For example, the IC and electronics systems industries experienced a significant downturn in 2009. The IC and electronic systems industries have also experienced significant downturns in connection with, or in anticipation of, maturing product cycles of both these industries and their customers' products. This economic downturn in the industries we serve contributed to the reduction in our revenue in 2009, as compared to prior years. Although the semiconductor industry experienced growth in 2010, semiconductor industry revenues for 2011 remained at levels similar to 2010. Spending on EDA products and services grew moderately during the first half of 2012.

While we cannot predict global economic conditions, uncertainty about future economic conditions and future decline in consumer spending could negatively impact our customers' businesses, reducing the number of new chip designs, their overall research and development spending, including their spending on EDA products and services, and as a result decrease demand for our products. Decreased bookings for our products and services, customer bankruptcies, or consolidation among our customers could also adversely affect our ability to grow our business. Our future business and financial results are subject to considerable uncertainty that could impact our stock price. If economic conditions deteriorate in the future, or, in particular, if semiconductor industry revenues do not grow, our future revenues and financial results could be adversely affected. However, if economic conditions improve for our customers, the positive impact on our revenues and financial results may be deferred due to cautious customer research and development spending and our ratable license mix.

#### **We have experienced varied operating results, and our operating results for any particular fiscal period are affected by the timing of significant bookings for our products, fluctuations in customer preferences for license types and the timing of revenue recognition under those license types.**

We have recorded net losses in the past and may record net losses in the future. Various factors affect our operating results and some of them are not within our control. Our operating results for any period are affected by the timing of certain bookings for our software and hardware products and by bookings levels.

Our operating results are also affected by the mix of software license types and bookings for sales or leases of hardware products executed in any given period. Revenue is affected by the timing of software license renewals, changes in existing contractual arrangements with customers and the mix of license types (i.e., perpetual, term or subscription) for existing customers. Our software license mix is such that a substantial proportion of licenses require ratable revenue recognition, and we expect the license mix, combined with the modest growth in spending by our customers in the semiconductor sector, may make it difficult for us to rapidly increase our revenue in future fiscal periods. The timing of our revenue recognition may be deferred until payments become due and payable from customers with nonlinear payment terms or as cash is collected from customers with low credit ratings.

Revenue related to our hardware business is generally recognized upon delivery. We expect revenue related to our hardware business to be cyclical, with our hardware related revenue generally increasing after the release of a new generation of hardware products and then declining gradually as that generation of hardware products gets older, until eventually, a new generation of hardware products is released and the cycle restarts. Any variation from these expectations could have a material impact on our business. In

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addition, sales of our hardware products depend on the commencement of new projects for the design and development of complex integrated circuits and systems by our customers. These projects often require significant commitments of time and capital, so our hardware sales may be delayed or may decrease if our customers delay commencement of projects or cancel projects because their capital spending is constrained due to end market uncertainty or uncertainty in the global economy generally. The verification hardware market is highly competitive and our customers may choose to purchase a competitor's verification hardware product based on cost, performance or other factors. These factors may result in lower hardware revenue, which would have an adverse effect on our business, results of operations or cash flows.

We plan our operating expenses based on forecasted revenue, expected business needs and other factors. These expenses and the effect of long-term commitments are relatively fixed in the short term. Bookings and the related revenue are harder to forecast in a difficult economic environment. If the macroeconomic environment weakens, and we experience a shortfall in bookings, our operating results could differ from our expectations because we may not be able to quickly reduce our expenses in response to short-term business changes.

The methods, estimates and judgments that we use in applying our accounting policies have a significant impact on our results of operations (see Critical Accounting Estimates under Part I, Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations). Such methods, estimates and judgments are, by their nature, subject to substantial risks, uncertainties and assumptions, and factors may arise over time that may lead us to change our methods, estimates and judgments. Changes in those methods, estimates and judgments could significantly affect our results of operations.

You should not view our historical results of operations as reliable indicators of our future performance. If our revenue, operating results or business outlook for future periods fall short of the levels expected by securities analysts or investors, the trading price of our common stock could decline.

### **Our failure to respond quickly to technological developments or customers' increasing technological requirements could make our products uncompetitive and obsolete.**

The industries in which we compete experience rapid technology developments, changes in industry standards and customer requirements and frequent new product introductions and improvements. Currently, the industries we serve are experiencing the following trends:

Migration to nanometer design—the continuous shrinkage of the size of process features and other features, such as wires, transistors and contacts on ICs, due to the ongoing advances in the semiconductor manufacturing processes—represents a major challenge for participants in the semiconductor industry, from IC design and design automation to design of manufacturing equipment and the manufacturing process itself. Shrinking transistor sizes are challenging the industry in the application of more complex physics and chemistry in order to produce advanced silicon devices. For EDA tools, models of each component's electrical properties and behavior become more complex as do requisite analysis, design and verification capabilities. Novel design tools and methodologies must be invented quickly to remain competitive in the design of electronics in the smallest nanometer ranges.

The challenges of nanometer design are leading some customers to work with older, less risky manufacturing processes that may reduce their need to upgrade or enhance their EDA products and design flows.

The ability to design SoCs increases the complexity of managing a design that, at the lowest level, is represented by billions of shapes on fabrication masks. In addition, SoCs typically incorporate microprocessors and digital signal processors that are programmed with software, requiring simultaneous design of the IC and the related software embedded on the IC.

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With the availability of seemingly endless gate capacity, there is an increase in design reuse, or the combining of off-the-shelf Design IP with custom logic to create ICs or SoCs. The unavailability of a broad range of high-quality Design IP (including our own) that can be reliably incorporated into a customer's design with our software products and services could lead to reduced demand for our products and services.

Increased technological capability of the Field-Programmable Gate Array, or FPGA, which is a programmable logic chip, creates an alternative to IC implementation for some electronics companies. This could reduce demand for our IC implementation products and services.

A growing number of low-cost engineering services businesses could reduce the need for some IC companies to invest in EDA products.

Adoption of cloud computing technologies with accompanying new business models for an increasing number of software categories, including EDA.

If we are unable to respond quickly and successfully to these trends, we may lose our competitive position, and our products or technologies may become uncompetitive or obsolete. To compete successfully, we must develop, acquire or license new products and improve our existing products and processes on a schedule that keeps pace with technological developments and the requirements for products addressing a broad spectrum of designers and designer expertise in our industries. Our hardware platforms must be enhanced periodically to reduce the likelihood that a competitor surpasses the capabilities we offer. We must also be able to support a range of changing computer software, hardware platforms and customer preferences. A rapid transition to different business models associated with cloud computing technologies could result in reduced revenue. We cannot guarantee that we will be successful in keeping pace with all, or any, of the customer trends.

### **Our operating results and revenue could be adversely affected by customer payment delays, customer bankruptcies and defaults or modifications of licenses.**

Occasionally, our customers file for bankruptcy or request to modify license terms, but these events generally have not had a material impact on our business or operating results. If our customers experience adverse changes in their business, they may delay or default on their payment obligations to us, file for bankruptcy or modify or cancel plans to license our products. If our customers are not successful in generating sufficient cash or are precluded from securing financing, they may not be able to pay, or may delay payment of, accounts receivable that are owed to us, although these obligations are generally not cancelable. Our customers' inability to fulfill payment obligations may adversely affect our revenue and cash flow. Additionally, our customers may seek to renegotiate pre-existing contractual commitments. Payment defaults by our customers or significant reductions in existing contractual commitments could have a material adverse effect on our financial condition and operating results. Because of the relatively high levels of volatility that continue to drive significant fluctuations in asset prices, as well as concern regarding high levels of leverage in sovereign and corporate debt, the capital and credit markets are volatile and unpredictable. If we were to seek funding from the capital or credit markets in response to any material level of customer defaults, we may not be able to secure funding on terms acceptable to us or at all, which may have a material negative effect on our business.

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### **Our stock price has been subject to significant fluctuations and may continue to be subject to fluctuations.**

The market price of our common stock has experienced significant fluctuations and may fluctuate or decline in the future, and as a result you could lose the value of your investment. The market price of our common stock may be affected by a number of factors, including, but not limited to:

Announcements of our quarterly operating results and revenue and earnings forecasts that fail to meet or are inconsistent with earlier projections or the expectations of our securities analysts or investors;

Changes in our bookings, revenue or earnings estimates;

Announcements of a restructuring plan;

Changes in management;

A gain or loss of a significant customer or market segment share;

Material litigation;

Announcements of new products or acquisitions of new technologies by us, our competitors or our customers; and

Market conditions in the IC, electronics systems and semiconductor industries.

In addition, equity markets in general, and the equities of technology companies in particular, have experienced extreme price and volume fluctuations. Such price and volume fluctuations may adversely affect the market price of our common stock for reasons unrelated to our business or operating results.

### **Litigation could adversely affect our financial condition or operations.**

We currently are, and in the future may be, involved in various disputes and litigation that arise in the ordinary course of business. These include disputes and lawsuits related to intellectual property, including customer indemnification, mergers and acquisitions, licensing, contracts, distribution arrangements and employee relations matters. For information regarding the litigation matters in which we are currently engaged, please refer to the discussion under Item 1, Legal Proceedings and Note 12 in our Notes to Condensed Consolidated Financial Statements. We cannot provide any assurances that the final outcome of these lawsuits or any other proceedings that may arise in the future will not have a material adverse effect on our business, operating results, financial condition or cash flows. Litigation can be time consuming and expensive and could divert management's time and attention from our business, which could have a material adverse effect on our revenues and operating results.

### **Our future revenue is dependent in part upon our installed customer base continuing to license or buy additional products, renew maintenance agreements and purchase additional services.**

Our installed customer base has traditionally generated additional new license, service and maintenance revenues. In future periods, customers may not necessarily license or buy additional products or contract for additional services or maintenance. In some cases, maintenance is renewable annually at a customer's option, and there are no mandatory payment obligations or obligations to license additional software. If our customers decide not to renew their maintenance agreements or license additional products or contract for additional services, or if they reduce the scope of the maintenance agreements, our revenue could decrease, which could have an adverse effect on our operating results. Our

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customers, many of which are large semiconductor and systems companies, often have significant bargaining power in negotiations with us. Mergers or acquisitions of our customers can reduce the total level of purchases of our software and services, and in some cases, increase customers' bargaining power in negotiations with their suppliers, including us.

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### **The competition in our industries is substantial and we may not be able to continue to successfully compete in our industries.**

The EDA industry and the commercial electronics engineering services industry are highly competitive. If we fail to compete successfully in these industries, it could seriously harm our business, operating results or financial condition. To compete in these industries, we must identify and develop or acquire innovative and cost-competitive EDA products, integrate them into platforms and market them in a timely manner. We must also gain industry acceptance for our engineering services and offer better strategic concepts, technical solutions, prices and response time, or a combination of these factors, than those of our competitors and the internal design departments of electronics manufacturers. We may not be able to compete successfully in these industries. Factors that could affect our ability to succeed include:

The development by others of competitive EDA products or platforms and engineering services, possibly resulting in a shift of customer preferences away from our products and services and significantly decreased revenue;

Decisions by electronics manufacturers to perform engineering services internally, rather than purchase these services from outside vendors due to budget constraints or excess engineering capacity;

The challenges of developing (or acquiring externally developed) technology solutions, including hardware offerings, that are adequate and competitive in meeting the rapidly evolving requirements of next-generation design challenges;

The significant number of current and potential competitors in the EDA industry and the low cost of entry;

Intense competition to attract acquisition targets, possibly making it more difficult for us to acquire companies or technologies at an acceptable price or at all;

The combination of two or more of our EDA competitors or collaboration among many EDA companies to deliver more comprehensive offerings than they could individually; and

Aggressive pricing competition by some of our competitors may cause us to lose our competitive position, which could result in lower revenues or profitability and could adversely impact our ability to realize the revenue and profitability forecasts for our software or hardware systems products.

We compete in EDA products and maintenance most frequently with Synopsys, Inc. and Mentor Graphics Corporation, but also with numerous other EDA providers (such as Ansys, Inc., Atrenta, Inc., ATopTech, Inc., Berkeley Design Automation, Inc., EVE SA, SpringSoft, Inc. and Zuken Ltd., and many others offering point solutions), with manufacturers of electronic devices that have developed, acquired or have the capability to develop their own EDA products, and with numerous electronics design and consulting companies. In the area of Design IP, we compete with Synopsys and numerous smaller IP companies. Synopsys recently acquired Magma Design Automation, Inc., which will impact the competitive landscape of the industry. We expect that Synopsys's integration of Magma technology into its product offerings will result in increased competition, which could harm our business, results of operations or cash flows.

### **We may need to change our pricing models to compete successfully. Competitive pressures could constrain the prices we can charge for our products, which could have an adverse effect on our results of operations.**

The highly competitive markets in which we do business can put pressure on us to reduce the prices of our products. If our competitors offer deep discounts on certain products in an effort to recapture or gain market share or to sell other software or hardware products, we may then need to lower our prices or offer other favorable terms to compete successfully. Any such changes would be likely to reduce our profit margins and could adversely affect our operating results. Any substantial changes to our prices and pricing policies could cause sales and software license revenues to decline or be delayed as our sales force implements and our customers adjust to the new pricing policies. Some of our competitors may bundle





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products for promotional purposes or as a long-term pricing strategy or provide guarantees of prices and product implementations. These practices could, over time, significantly constrain the prices that we can charge for our products. If we cannot offset price reductions with a corresponding increase in the number of sales or with lower spending, then the reduced license revenues resulting from lower prices could have an adverse effect on our results of operations.

### **Risks associated with our international operations could seriously harm our financial condition.**

A significant amount of our revenue is derived from our international operations and we have offices throughout the world, including key research and development facilities outside of the United States. Our international operations may also be subject to other risks, including:

The adoption or expansion of government trade restrictions, including tariffs and other trade barriers;

Limitations on repatriation of earnings;

Limitations on the conversion of foreign currencies;

Reduced protection of intellectual property rights in some countries;

International economic downturn;

Longer collection periods for receivables and greater difficulty in collecting accounts receivable;

Difficulties in managing foreign operations;

Political and economic instability;

Unexpected changes in regulatory requirements;

Inability to continue to offer competitive compensation in certain growing regions; and

United States and other governments licensing requirements for exports, which may lengthen the sales cycle or restrict or prohibit the sale or licensing of certain products.

Some of our international research and development and other facilities are in parts of the world that are not as politically stable as the United States. Consequently, we may face a greater risk of business interruption as a result of terrorist acts or military conflicts than businesses located domestically. Furthermore, this potential harm is exacerbated because damage to or disruptions at our international research and development facilities could have a more significant adverse effect on our ability to develop new or improve existing products than other businesses that may only have sales offices or other less critical operations abroad. We are not insured for losses or interruptions caused by acts of war. Furthermore, our operations are dependent upon the connectivity of our operations throughout the world. Activities that interfere with our international connectivity, such as cyber hacking, the introduction of a virus into our computer systems or natural disasters near any of our international locations, could significantly interfere with our business operations.

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In addition, internal controls, policies and procedures and employee training and compliance programs that we have implemented to deter prohibited practices may not prevent our employees, contractors or agents from violating or circumventing our policies and the laws and regulations applicable to our worldwide operations.

**We depend upon our management team and key employees, and our failure to attract, train, motivate and retain management and key employees may make us less competitive in our industries and therefore harm our results of operations.**

Our business depends upon the continued services, efforts and abilities of our senior management, including our Chief Executive Officer, and other key employees, including key development personnel. Competition for highly skilled executive officers and employees can be intense, particularly in geographic

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areas recognized as high technology centers such as the Silicon Valley area, where our principal offices are located, and in other locations where we maintain facilities. We may also experience increased compensation costs that are not offset by either improved productivity or higher sales. We may not be successful in recruiting new personnel and in retaining and motivating existing personnel. From time to time, there may be changes in our management team resulting from the hiring and departure of executive officers, and as a result, we may experience disruption to our business that may harm our operating results and our relationships with our employees, customers and suppliers may be adversely affected. To attract, retain and motivate individuals with the requisite expertise, we may be required to grant large numbers of stock options or other stock-based incentive awards, which may be dilutive to existing stockholders and increase compensation expense, and pay significant base salaries and cash bonuses, which could harm our operating results. The high cost of training new employees, not fully utilizing these employees, or losing trained employees to competing employers could also reduce our operating margins and harm our business or operating results.

In addition, applicable rules and regulations require stockholder approval for new equity compensation plans and significant amendments to existing equity compensation plans, including increases in shares available for issuance under such plans, and prohibit publicly-traded companies from giving a proxy to vote on equity compensation plans unless the beneficial owner of the shares has given voting instructions. These rules and regulations could make it more difficult for us to grant equity compensation to employees in the future. To the extent that these regulations make it more difficult or expensive to grant equity compensation to employees, we may incur increased compensation costs or find it difficult to attract, retain and motivate employees, which could materially and adversely affect our business.

**We may not receive significant revenue from our current research and development efforts for several years, if at all.**

Developing EDA technology and integrating acquired technology into existing platforms is expensive, and these investments often require a long time to generate returns. Our strategy involves significant investments in research and development and related product opportunities. We believe that we must continue to dedicate a significant amount of resources to our research and development efforts to maintain and improve our competitive position. However, we cannot ensure that we will receive significant, if any, revenue from these investments.

**We have acquired and expect to acquire other companies and businesses and may not realize the expected benefits of these acquisitions.**

We have acquired and expect to acquire other companies and businesses in the future. While we expect to carefully analyze each potential acquisition before committing to the transaction, we may not consummate any particular transaction, but may nonetheless incur significant costs, or if a transaction is consummated, we may not be able to integrate and manage acquired products and businesses effectively or to integrate and retain key personnel from the acquired companies or businesses. In addition, acquisitions involve a number of risks. If any of the following acquisition-related risks occur, our business, operating results or financial condition could be seriously harmed:

Difficulties in combining previously separate businesses into a single unit;

The substantial diversion of management's attention from day-to-day business when evaluating and negotiating these transactions and integrating an acquired business;

The discovery, after completion of the acquisition, of unanticipated liabilities assumed from the acquired business or of assets acquired, such that we cannot realize the anticipated value of the acquisition;

The failure to realize anticipated benefits such as cost savings and revenue enhancements;

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The failure to retain key employees of the acquired business;

Difficulties related to integrating the products of an acquired business in, for example, distribution, engineering, licensing models and customer support areas;

Unanticipated costs;

Customer dissatisfaction with existing license agreements with us, possibly dissuading them from licensing or buying products acquired by us after the effective date of the license; and

The failure to understand and compete effectively in markets where we have limited experience.

In a number of our completed acquisitions, we have agreed to make future payments, either in the form of employee bonuses or contingent purchase price payments based on the performance of the acquired businesses or the employees who joined us with the acquired businesses. We may continue to use contingent purchase price payments in connection with acquisitions in the future. The performance goals pursuant to which these future payments may be made generally relate to achievement by the acquired business, or by the employees who joined us with the acquired business of certain specified bookings, revenue, run rate, product proliferation, product development or employee retention goals during a specified period following completion of the applicable acquisition. Future acquisitions may involve issuances of stock as full or partial payment of the purchase price for the acquired business, grants of incentive stock or options to employees of the acquired businesses (which may be dilutive to existing stockholders), expenditure of substantial cash resources or the incurrence of material amounts of debt.

The specific performance goal levels and amounts and timing of employee bonuses or contingent purchase price payments vary with each acquisition. While we expect to derive value from an acquisition in excess of such contingent payment obligations, our strategy may change and we may be required to make certain contingent payments without deriving the anticipated value.

**We rely on our proprietary technology, as well as software and other intellectual property rights licensed to us by third parties, and we cannot assure you that the precautions taken to protect our rights will be adequate or that we will continue to be able to adequately secure such intellectual property rights from third parties.**

Our success depends, in part, upon our proprietary technology. We generally rely on patents, copyrights, trademarks, trade secret laws, licenses and restrictive agreements to establish and protect our proprietary rights in technology and products. Despite the precautions we may take to protect our intellectual property, third parties have tried in the past, and may try in the future, to challenge, invalidate or circumvent these safeguards. Our patents or other intellectual property rights may not provide us with sufficient competitive advantages. Patents may not be issued on any of our pending applications and our issued patents may not be sufficiently broad to protect our technology. Furthermore, the laws of foreign countries may not protect our proprietary rights in those countries to the same extent as applicable law protects these rights in the United States. The protection of our intellectual property may require the expenditure of significant financial and managerial resources. Moreover, the steps we take to protect our intellectual property may not adequately protect our rights, or deter or prevent third parties from infringing or misappropriating our proprietary rights.

Many of our products include software or other intellectual property licensed from third parties. We may have to seek new or renew existing licenses for such software and other intellectual property in the future. Our engineering services business holds licenses to certain software and other intellectual property owned by third parties, including that of our competitors. Our failure to obtain software, other intellectual property licenses or other intellectual property rights that are necessary or helpful for our business on favorable terms, or our need to engage in litigation over these licenses or rights, could seriously harm our business, operating results or financial condition.

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### **We could suffer serious harm to our business because of the infringement of our intellectual property rights by third parties or because of our infringement of the intellectual property rights of third parties.**

There are numerous EDA, VIP and Design IP product-related patents. New patents are being issued at a rapid rate and are owned by EDA companies as well as entities and individuals outside the EDA industry, including parties whose income is primarily derived from infringement-related litigation. It is not always practicable to determine in advance whether a product or any of its components infringes the patent rights of others. As a result, from time to time, we may be compelled to respond to or prosecute intellectual property infringement claims to protect our rights or defend a customer's rights.

Intellectual property infringement claims, including contractual defense reimbursement obligations related to third-party claims against our customers, regardless of merit, could consume valuable management time, result in costly litigation or cause product shipment delays, all of which could seriously harm our business, operating results or financial condition. The risk of infringement and related indemnification claims associated with Design IP products that are incorporated into a customer product broadly used by consumers, may be higher than the risk associated with our software products. In settling these claims, we may be required to enter into royalty or licensing agreements with the third parties claiming infringement. These royalty or licensing agreements, if available, may not have terms favorable to us. Being compelled to enter into a license agreement with unfavorable terms could seriously harm our business, operating results or financial condition. Any potential intellectual property litigation could compel us to do one or more of the following:

Pay damages (including the potential for treble damages), license fees or royalties (including royalties for past periods) to the party claiming infringement;

Stop licensing products or providing services that use the challenged intellectual property;

Obtain a license from the owner of the infringed intellectual property to sell or use the relevant technology, which license may not be available on reasonable terms, or at all; or

Redesign the challenged technology, which could be time consuming and costly, or not be accomplished.

If we were compelled to take any of these actions, our business or operating results may suffer.

### **If our security measures are breached and an unauthorized party obtains access to customer data or our proprietary business information, our information systems may be perceived as being insecure, which could harm our business and reputation.**

Our products and services involve the storage and transmission of our proprietary information and that of our customers. We have offices throughout the world, including key research and development facilities outside of the United States. Our operations are dependent upon the connectivity of our operations throughout the world. Despite our security measures, our information technology and infrastructure may be vulnerable to cyber attacks or breached due to an employee error or other disruption that could result in unauthorized disclosure of sensitive information and could significantly interfere with our business operations. Breaches of our security measures could expose us to a risk of loss or misuse of this information, litigation and potential liability. Because techniques used to obtain unauthorized access or to sabotage information systems change frequently and generally are not recognized until launched against a target, we may be unable to anticipate these techniques or to implement adequate preventive measures. In addition, if we select a vendor that uses cyber storage of information as part of their service or product offerings, despite our attempts to validate the security of such services, our proprietary information may be misappropriated by third parties. In the event of an actual or perceived breach of our security, or the security

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of one of our vendors, the market perception of the effectiveness of our security measures could be harmed and we could suffer damage to our reputation or our business, or lose existing customers and lose our ability to obtain new customers.

### **The long sales cycle of our products and services makes the timing of our revenue difficult to predict and may cause our operating results to fluctuate unexpectedly.**

Generally, we have a long sales cycle that can extend up to six months or longer. The complexity and expense associated with our products and services generally require a lengthy customer education, evaluation and approval process. Consequently, we may incur substantial expenses and devote significant management effort and expense to develop potential relationships that do not result in agreements or revenue and may prevent us from pursuing other opportunities.

In addition, sales of our products and services have been and may in the future be delayed if customers delay approval or commencement of projects because of:

The timing of customers' competitive evaluation processes; or

Customers' budgetary constraints and budget cycles.

Long sales cycles for acceleration and emulation hardware products subject us to a number of significant risks over which we have limited control, including insufficient, excess or obsolete inventory, variations in inventory valuation and fluctuations in quarterly operating results.

### **The effect of foreign exchange rate fluctuations may adversely impact our financial condition.**

We have significant operations outside the United States. Our revenue from international operations as a percentage of total revenue was approximately 56% during the three months ended June 30, 2012 and 56% during the three months ended July 2, 2011, a substantial portion of which is denominated in United States dollars. We expect that revenue from our international operations will continue to account for a significant portion of our total revenue. We also transact business in various foreign currencies, primarily the Japanese yen. The volatility of foreign currencies in certain regions, most notably the Japanese yen, European Union euro, British pound and Indian rupee have had and may in the future have an effect on our revenue or operating results.

Fluctuations in the rate of exchange between the United States dollar and the currencies of other countries where we conduct business could seriously affect our business, operating results or financial condition. For example, when a foreign currency declines in value relative to the United States dollar, it takes more of the foreign currency to purchase the same amount of United States dollars than before the change. If we price our products and services in the foreign currency, we receive fewer United States dollars than we did before the change. If we price our products and services in United States dollars, the decrease in value of the local currency results in an increase in the price for our products and services compared to those products of our competitors that are priced in local currency. This could result in our prices being uncompetitive in markets where business is transacted in the local currency. On the other hand, when a foreign currency increases in value relative to the United States dollar, it takes more United States dollars to purchase the same amount of the foreign currency. As we use the foreign currency to pay for payroll costs and other operating expenses in our international operations, this results in an increase in operating expenses.

Exposure to foreign currency transaction risk can arise when transactions are conducted in a currency different from the functional currency of one of our subsidiaries. A subsidiary's functional currency is generally the currency in which it primarily conducts its operations, including product pricing,

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expenses and borrowings. Although we attempt to reduce the effect of foreign currency fluctuations, significant exchange rate movements may hurt our results of operations as expressed in United States dollars.

### **Our reported financial results may be adversely affected by changes in United States generally accepted accounting principles.**

United States generally accepted accounting principles are subject to interpretation by the Financial Accounting Standards Board, or FASB, the American Institute of Certified Public Accountants, the SEC and various bodies formed to promulgate and interpret appropriate accounting principles. During fiscal 2010, the FASB issued exposure drafts of proposed accounting principles related to revenue recognition and leases which could change the way we account for certain of our transactions. The FASB issued a revised exposure draft of proposed accounting principles related to revenue recognition during fiscal 2011 and has continued to discuss these and other proposed accounting principles during the first half of fiscal 2012. A change in these or other principles or interpretations could have a significant effect on our reported financial results and could affect the reporting of transactions completed before the announcement of a change. In addition, the SEC announced a multi-year plan that could ultimately lead to the use of International Financial Reporting Standards by United States issuers in their SEC filings. Any such change could have a significant effect on our reported financial results.

### **We have substantial cash requirements in the United States, but a significant portion of our cash is held and generated outside of the United States, and if our cash available in the United States is insufficient to meet our operating expenses and debt repayment obligations in the United States, then we may be required to raise cash in ways that could negatively affect our financial condition, results of operations and the market price of our common stock.**

We have significant operations outside the United States. As of June 30, 2012, approximately 50% of our cash and cash equivalents balance was held by subsidiaries outside the United States, with the remainder of the balance held by us or our subsidiaries in the United States. We believe that the combination of our existing United States cash balances and future United States operating cash flows are sufficient to meet our ongoing United States operating expenses and debt repayment obligations. However, if these sources of cash were insufficient to meet our future funding obligations in the United States, we could be required to seek other available funding sources which could negatively impact our results of operations, financial position and the market price of our common stock.

### **The investment of our cash, cash equivalents and investments in money market funds and marketable debt securities are subject to risks which may cause losses and affect the liquidity of these investments.**

Our investments include various money market funds and marketable debt securities such as corporate debt securities, United States Treasury securities, United States government agency securities, bank certificates of deposit and commercial paper. The weakened financial markets have at times adversely impacted the general credit, liquidity, market and interest rates for these and other types of debt securities. Additionally, changes in monetary policy by the Federal Open Market Committee and concerns about the rising United States government debt level may cause a decrease in the purchasing power of the United States dollar and adversely affect our investment portfolio. The financial market and monetary risks associated with our investment portfolio may have a material adverse effect on our financial condition, liquidity, results of operations or cash flows.

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**Our operating results could be adversely affected as a result of changes in our effective tax rates or by material differences between our forecasted annual effective tax rates and actual tax rates.**

Our future effective tax rates could be adversely affected by the following:

Changes in tax laws or the interpretation of such tax laws, including potential United States and international tax reforms;

Earnings being lower than anticipated in countries where we are taxed at lower rates as compared to the United States federal and state statutory tax rates;

An increase in expenses not deductible for tax purposes, including certain stock-based compensation and impairment of goodwill;

Changes in the valuation allowance against our deferred tax assets;

Changes in judgment from the evaluation of new information that results in a recognition, derecognition or change in measurement of a tax position taken in a prior period;

Increases to interest or penalty expenses classified in the financial statements as income taxes;

New accounting standards or interpretations of such standards;

A change in our decision to indefinitely reinvest foreign earnings outside the United States; or

Results of tax examinations by the IRS, and state and foreign tax authorities.

Any significant change in our future effective tax rates could adversely impact our results of operations for future periods.

Forecasts of our annual effective tax rate are complex and subject to uncertainty because our income tax position for each year combines the effects of estimating our annual income or loss, the mix of profits and losses earned by us and our subsidiaries in tax jurisdictions with a broad range of income tax rates, as well as benefits from available deferred tax assets, the impact of various accounting rules and results of tax audits. Forecasts of our annual effective tax rate do not include the anticipation of future tax law changes. If there were a material difference between forecasted and actual tax rates then it could have a material impact on our results of operations.

**The IRS and other tax authorities regularly examine our tax returns, and the outcome of current and future tax examinations may have a material adverse effect on our results of operations and cash flows.**

The IRS and other tax authorities regularly examine our income tax returns. The calculation of our provision (benefit) for income taxes requires us to use significant judgment and involves dealing with uncertainties in the application of complex tax laws and regulations. In determining the adequacy of our provision (benefit) for income taxes, we regularly assess the potential settlement outcomes resulting from income tax examinations. However, the final outcome of tax examinations, including the total amount payable or the timing of any such payments upon resolution of these issues, cannot be estimated with certainty. In addition, we cannot be certain that such amount will not be materially different from the amount that is reflected in our historical income tax provisions and accruals. Should the IRS or other tax authorities assess additional taxes as a result of a current or a future examination, we may be required to record charges to operations in future periods that could have a material impact on our results of operations, financial position or cash flows in the applicable period or periods.



**We depend on a sole supplier for certain hardware components, making us vulnerable to supply shortages and price fluctuation.**

We are dependent on a sole supplier for certain hardware components. Our reliance on a sole supplier could result in product delivery problems and reduced control over product pricing and quality, as

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well as limit our ability to identify and qualify another supplier in a timely manner. While it is our goal to have multiple sources to procure certain key components, in some cases it is not practical or feasible to do so. We may suffer a disruption in the supply of certain hardware components if we are unable to purchase sufficient components on a timely basis or at all for any reason.

### **Our restructuring plans may not result in the benefits we have anticipated, possibly having a negative effect on our future operating results.**

In recent fiscal years, we have initiated restructuring plans in an effort to decrease costs by reducing our workforce and by consolidating facilities. While those restructuring plans are almost complete, we may not be able to realize the expected long-term benefits of our restructuring plans, such as improvements in operating margins and cash flows. Our inability to realize these benefits may result in an inefficient business structure that could negatively affect our results of operations. Our restructuring plans may also subject us to litigation risks and expenses. In addition, our restructuring plans may have other consequences, such as attrition beyond our planned reduction in workforce, a negative effect on employee morale or our ability to attract highly skilled employees. Our competitors may also seek to gain a competitive advantage over us. The restructuring plans could also cause our remaining employees to leave or result in reduced productivity by our employees, and, in turn, this may affect our revenue and other operating results in the future.

### **Failure to obtain export licenses could harm our business by rendering us unable to ship products and transfer our technology outside of the United States.**

We must comply with regulations of the United States and of certain other countries in shipping our software products and transferring our technology outside the United States and to foreign nationals. Any significant future difficulty in complying could harm our business, operating results or financial condition.

### **Errors or defects in our products and services could expose us to liability and harm our reputation.**

Our customers use our products and services in designing and developing products that involve a high degree of technological complexity, each of which has its own specifications. Because of the complexity of the systems and products with which we work, some of our products and designs can be adequately tested only when put to full use in the marketplace. As a result, our customers or their end users may discover errors or defects in our software or the systems we design, or the products or systems incorporating our design and intellectual property may not operate as expected. Errors or defects could result in:

Loss of customers;

Loss of market share;

Failure to attract new customers or achieve market acceptance;

Diversion of development resources to resolve the problem;

Loss of or delay in revenue;

Increased service costs; and

Liability for damages.

**If we become subject to unfair hiring claims, we could be prevented from hiring needed employees, incur liability for damages and incur substantial costs in defending ourselves.**

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Companies in our industry that lose employees to competitors frequently claim that these competitors have engaged in unfair hiring practices or that the employment of these persons would involve the disclosure or use of trade secrets. These claims could prevent us from hiring employees or cause us to

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incur liability for damages. We could also incur substantial costs in defending ourselves or our employees against these claims, regardless of their merits. Defending ourselves from these claims could also divert the attention of our management away from our operations.

### **Anti-takeover defenses in our certificate of incorporation and bylaws and certain provisions under Delaware law could prevent an acquisition of our company or limit the price that investors might be willing to pay for our common stock.**

Our certificate of incorporation and bylaws and certain provisions of the Delaware General Corporation Law that apply to us could make it difficult for another company to acquire control of our company. For example:

Our certificate of incorporation allows our Board of Directors to issue, at any time and without stockholder approval, preferred stock with such terms as it may determine. No shares of preferred stock are currently outstanding. However, the rights of holders of any of our preferred stock that may be issued in the future may be superior to the rights of holders of our common stock.

Section 203 of the Delaware General Corporation Law generally prohibits a Delaware corporation from engaging in any business combination with a person owning 15% or more of its voting stock, or who is affiliated with the corporation and owned 15% or more of its voting stock at any time within three years prior to the proposed business combination, for a period of three years from the date the person became a 15% owner, unless specified conditions are met.

All or any one of these factors could limit the price that certain investors would be willing to pay for shares of our common stock and could allow our Board of Directors to resist, delay or prevent an acquisition of our company, even if a proposed transaction were favored by a majority of our independent stockholders.

### **Our business is subject to the risk of earthquakes and other natural disasters.**

Our corporate headquarters, including certain of our research and development operations and certain of our distribution facilities, is located in the Silicon Valley area of Northern California, a region known to experience seismic activity. If significant seismic activity were to occur, our operations may be interrupted, which could adversely impact our business and results of operations.

Our other offices in the United States and in other countries around the world may be adversely impacted by natural disasters. If a natural disaster occurs at or near any of our offices, our operations may be interrupted, which could adversely impact our business and results of operations. If a natural disaster impacts a significant number of our customers, our business and results of operations could be adversely impacted.

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### **Risks Related to Our Securities and Indebtedness**

**Our debt obligations expose us to risks that could adversely affect our business, operating results or financial condition, and could prevent us from fulfilling our obligations under such indebtedness.**

We have a substantial level of debt. As of June 30, 2012, we had outstanding indebtedness with a principal balance of \$494.7 million as follows:

\$350.0 million related to our 2.625% Cash Convertible Senior Notes Due 2015, or our 2015 Notes;

\$144.5 million related to our 1.500% Convertible Senior Notes Due December 15, 2013, or our 2013 Notes; and

\$0.2 million related to our Zero Coupon Zero Yield Senior Convertible Notes Due 2023, or our 2023 Notes.

The level of our current or future indebtedness, among other things, could:

Make it difficult for us to satisfy our payment obligations on our debt as described above;

Make us more vulnerable in the event of a downturn in our business;

Reduce funds available for use in our operations or for developments or acquisitions of new technologies;

Make it difficult for us to incur additional debt or obtain any necessary financing in the future for working capital, capital expenditures, debt service, acquisitions or general corporate purposes;

Impose operating or financial covenants on us;

Limit our flexibility in planning for or reacting to changes in our business; or

Place us at a possible competitive disadvantage relative to less leveraged competitors and competitors that have greater access to capital resources.

If we are unable to generate sufficient cash flow or otherwise obtain funds necessary to make required payments, or if we fail to comply with the various requirements of our indebtedness, we would be in default, which would permit the holders of our indebtedness to accelerate the maturity of the indebtedness and could cause defaults under any other indebtedness as well.

Any default under our indebtedness could have a material adverse effect on our business, operating results and financial condition. In addition, a material default on our indebtedness could suspend our eligibility to register securities using certain registration statement forms under SEC guidelines that permit incorporation by reference of substantial information regarding us, potentially hindering our ability to raise capital through the issuance of our securities and increasing our costs of registration.

**Warrant transactions associated with our 2013 Notes and 2015 Notes will, in certain circumstances, dilute the ownership interests of existing stockholders.**

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We entered into separate warrant transactions concurrent with the issuance of the 2013 Notes. As of June 30, 2012, warrants for the purchase of approximately 6.8 million shares of Cadence's common stock were outstanding at a strike price of \$31.50 per share. We also entered into separate warrant transactions at the time of the issuance of the 2015 Notes for the purchase of up to approximately 46.4 million shares of Cadence's common stock at a strike price of \$10.78 per share. These warrants will be settled in net shares. Therefore, upon expiration of the warrants we will issue shares of our common stock to the purchasers of the warrants that represent the value by which the price of our common stock exceeds the strike price stipulated within the particular warrant agreement. If Cadence's stock price is above the warrants' strike price upon expiration of the warrants, the warrants will dilute the ownership interest to our existing stockholders. The warrants will also dilute our diluted earnings per share in periods when our average closing stock price exceeds the strike price of the particular warrant. Any sales in the public market of common stock issuable upon net settlement at expiration of the warrants could adversely affect then current market prices of our common stock.

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### **Conversion of our 2013 Notes and 2015 Notes prior to the scheduled maturities of the notes may adversely affect our liquidity and financial condition.**

Holders of our 2013 Notes and 2015 Notes may convert their notes into cash prior to the scheduled maturities if any of the conversion conditions for those notes are met. The 2015 Notes are convertible into cash only and the 2013 Notes are convertible into a combination of cash and shares of our common stock.

In order for the 2015 Notes to be convertible into cash in a particular fiscal quarter, a conversion condition must be met during the preceding fiscal quarter. During the three months ended June 30, 2012, our closing stock price exceeded \$9.81 for at least 20 of the last 30 trading days prior to June 30, 2012. As a result, the 2015 Notes are convertible into cash from July 1, 2012 through September 29, 2012 and we have classified our 2015 Notes as a current liability on our Condensed Consolidated Balance Sheet as of June 30, 2012. The 2013 Notes are not currently convertible.

So long as the 2015 Notes are outstanding, we will assess whether this conversion condition has been met at the end of each fiscal quarter. If a conversion condition is met in any future fiscal quarter, we would classify our 2015 Notes as a current liability on our Condensed Consolidated Balance Sheet as of the end of that fiscal quarter.

If one or more of the 2013 or 2015 Note holders elect to convert their notes at a time when the conversion conditions have been met, we would be required to settle the converted principal and, in the case of the 2015 Notes, the conversion value, through payment of cash, which could adversely affect our liquidity and financial condition.

### **At the option of the holders of the 2013 Notes and the 2015 Notes, under certain circumstances we may be required to repurchase the 2013 Notes or the 2015 Notes in cash.**

Under the terms of the 2013 Notes and the 2015 Notes, we may be required to repurchase the 2013 Notes and the 2015 Notes following a fundamental change in our corporate ownership or structure, such as a change of control in which substantially all of the consideration does not consist of publicly traded securities, prior to maturity of the 2013 Notes and the 2015 Notes. The repurchase price for the 2013 Notes and the 2015 Notes in the event of a fundamental change must be paid solely in cash. This repayment obligation may have the effect of discouraging, delaying or preventing a takeover of our company. Payment of the notes prior to their scheduled maturities could have a significant negative impact on our cash and liquidity and could impact our ability to invest financial resources in other strategic initiatives.

### **Hedge and warrant transactions entered into in connection with the issuance of the 2013 Notes and the 2015 Notes may affect the value of our common stock.**

We entered into hedge transactions with various financial institutions, at the time of issuance of the 2013 Notes and the 2015 Notes, with the objective of limiting the potential dilutive effect of issuing our common stock upon conversion of the 2013 Notes and our exposure to the additional cash payments above the principal amount upon conversion of the 2015 Notes. We also entered into separate warrant transactions with the same financial institutions. In connection with our hedge and warrant transactions associated with the 2013 Notes and the 2015 Notes, these financial institutions purchased our common stock in secondary market transactions and entered into various over-the-counter derivative transactions with respect to our common stock. These entities or their affiliates are likely to modify their hedge positions from time to time prior to conversion or maturity of the 2013 Notes and the 2015 Notes by purchasing and selling shares of our common stock, other of our securities or other instruments they may wish to use in connection with such hedging. Any of these transactions and activities could adversely affect the value of our common stock and, as a result, the number of shares and the value of the common stock that the 2013 Note holders will receive upon conversion of the 2013 Notes and the amount of cash that 2015 Notes holders will receive upon conversion of the 2015 Notes.

**Table of Contents****We are subject to the risk that the hedge participants fail to fulfill their obligations under the 2013 Notes hedge transactions and the 2015 Notes hedge transactions.**

If any of the participants in the hedge transactions is unwilling or unable to perform its obligations for any reason, we would not be able to receive the benefit of such transaction. We cannot provide any assurances as to the financial stability or viability of any of the participants in the hedge transactions. Our 2015 Notes became convertible into cash at the end of the second quarter of fiscal 2011, were not convertible as of the end of the third quarter of fiscal 2011, but were again convertible as of December 31, 2011 and as of June 30, 2012. The convertible note hedge transactions in connection with the 2015 Notes, or the 2015 Notes Hedges, are intended to reduce our exposure above the \$350.0 million principal balance in the event of a cash conversion of the 2015 Notes. If the hedge participants fail to meet their obligations for any reason, it could have a material adverse effect on our liquidity and financial condition.

**Rating agencies may provide unsolicited ratings on the 2013 Notes and the 2015 Notes that could reduce the market value or liquidity of our 2013 Notes, 2015 Notes or our common stock.**

We have not requested a rating of the 2013 Notes or the 2015 Notes from any rating agency and we do not anticipate that the 2013 Notes or the 2015 Notes will be rated. However, if one or more rating agencies independently elects to rate the 2013 Notes or the 2015 Notes and assigns the 2013 Notes or the 2015 Notes a rating lower than the rating expected by investors, or reduces such rating in the future, the market price or liquidity of the 2013 Notes or the 2015 Notes, as the case may be, and our common stock could be harmed. Should a decline occur in the market price of the 2013 Notes or the 2015 Notes, as compared to the price of our common stock, this may trigger the right of the holders of the 2013 Notes or the 2015 Notes to convert such notes into cash and shares of our common stock, as applicable.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

In February 2008, our Board of Directors authorized a program to repurchase shares of our common stock in the open market with a value of up to \$500.0 million in the aggregate. In August 2008, our Board of Directors authorized another program to repurchase shares of our common stock in the open market with a value of up to an additional \$500.0 million in the aggregate. The following table sets forth the repurchases we made during the three months ended June 30, 2012:

Period	Total Number of Shares Purchased <sup>(1)</sup>	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plan or Program	Maximum Dollar Value of Shares that May Yet Be Purchased Under Publicly Announced Plan or Program <sup>(1)</sup> (In millions)
April 1, 2012 – May 5, 2012	2,332	\$ 11.58		\$ 814.4
May 6, 2012 – June 2, 2012	290,419	\$ 10.96		\$ 814.4
June 3, 2012 – June 30, 2012	3,169	\$ 10.87		\$ 814.4
Total	295,920	\$ 10.96		

<sup>(1)</sup> Shares purchased that were not part of our publicly announced repurchase programs represent the surrender of shares of restricted stock to pay income taxes due upon vesting, and do not reduce the dollar value that may yet be purchased under our publicly announced repurchase programs.



**Table of Contents****Item 3. Defaults Upon Senior Securities**

None.

**Item 4. Mine Safety Disclosures**

Not applicable.

**Item 5. Other Information**

None.

**Item 6. Exhibits**

(a) The following exhibits are filed herewith:

Exhibit Number	Exhibit Title	Incorporated by Reference			Provided Herewith
		Form	File No.	Exhibit No. Filing Date	
10.01	The Registrant's 1995 Directors Stock Incentive Plan.				X
31.01	Certification of the Registrant's Chief Executive Officer, Lip-Bu Tan, pursuant to Rule 13a-14 of the Securities Exchange Act of 1934.				X
31.02	Certification of the Registrant's Chief Financial Officer, Geoffrey G. Ribar, pursuant to Rule 13a-14 of the Securities Exchange Act of 1934.				X
32.01	Certification of the Registrant's Chief Executive Officer, Lip-Bu Tan, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.				X
32.02	Certification of the Registrant's Chief Financial Officer, Geoffrey G. Ribar, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.				X
101.INS	XBRL Instance Document.				X
101.SCH	XBRL Taxonomy Extension Schema Document.				X
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.				X
101.DEF	XBRL Definition Linkbase Document.				X
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.				X
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.				X

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**SIGNATURES**

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

**CADENCE DESIGN SYSTEMS, INC.**

**(Registrant)**

DATE: July 26, 2012

By: /s/ Lip-Bu Tan  
Lip-Bu Tan  
President, Chief Executive Officer and Director

DATE: July 26, 2012

By: /s/ Geoffrey G. Ribar  
Geoffrey G. Ribar  
Senior Vice President and Chief Financial Officer

**Table of Contents****EXHIBIT INDEX**

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