

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

FORM 10-Q

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

For the quarterly period ended April 3, 2011

OR

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

Commission file number 1-10079

CYPRESS SEMICONDUCTOR CORPORATION

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

94-2885898
(I.R.S. Employer
Identification No.)

198 Champion Court, San Jose, California 95134
(Address of principal executive offices and zip code)

(408) 943-2600
(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 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

The total number of outstanding shares of the registrant's common stock as of May 2, 2011 was 168,032,433.

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PART I—FINANCIAL INFORMATION

Forward-Looking Statements

The discussion in this Quarterly Report on Form 10-Q contains statements that are not historical in nature, but are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, that involve risks and uncertainties, including, but not limited to, statements related to our manufacturing strategy; the number and impact of future personnel terminations and the expenses related thereto; our expectations, including the timing and savings, related to our restructuring activities which includes the sale of our restructured assets, including the Texas property; our expectations regarding our active litigation matters and our intent to defend ourselves in those matters; our foreign currency exposure, the adequacy of our cash and working capital positions; our expected return on our yield-enhancement program and the risks related to such an investment, our intended use of our line of credit; the value and liquidity of our investments, including auction rate securities and our other debt investments, our expectations regarding our outstanding warranty liability, our plans to repurchase stock under our stock repurchase program, the volatility of our stock price, and the likelihood that we will need to settle the outstanding Grace lease payments. We use words such as “plan,” “anticipate,” “believe,” “expect,” “future,” “intend” and similar expressions to identify forward-looking statements. Such forward-looking statements are made as of the date hereof and are based on our current expectations, beliefs and intentions regarding future events or our financial performance and the information available to management as of the date hereof. Except as required by law, we assume no responsibility to update any such forward-looking statements. Our actual results could differ materially from those expected, discussed or projected in the forward-looking statements contained in this Quarterly Report on Form 10-Q for any number of reasons, including, but not limited to, the state and future of the general economy and its impact on the markets we serve and our investments; the current credit conditions; our ability to expand our customer base, our ability to transform our business with a leading portfolio of programmable products; the number and nature of our competitors; the changing environment and/or cycles of the semiconductor industry; our ability to efficiently manage our manufacturing facilities and achieve our cost goals emanating from our flexible manufacturing strategy; our ability to achieve our goals related to our restructuring activities; our ability to maintain the tax-free nature of the SunPower spin-off; our success in our pending litigation matters, our ability to manage our investments and interest rate and exchange rate exposure; our ability to achieve liquidity in our investments and/or the materialization of one or more of the risks set forth above or in Item 1A (*Risk Factors*) in this Quarterly Report on Form 10-Q.

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ITEM 1. FINANCIAL STATEMENTS

CYPRESS SEMICONDUCTOR CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

	April 3, 2011	January 2, 2011
	(In thousands, except per-share amounts)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 119,598	\$ 263,183
Short-term investments	141,321	171,078
Accounts receivable, net	173,389	117,726
Inventories, net	104,122	101,763
Other current assets	70,969	41,908
Total current assets	609,399	695,658
Property, plant and equipment, net	267,033	260,122
Goodwill	31,836	31,836
Intangible assets, net	11,929	12,499
Other long-term assets	73,744	72,686
Total assets	<u>\$ 993,941</u>	<u>\$ 1,072,801</u>
LIABILITIES AND EQUITY		
Current liabilities:		
Accounts payable	\$ 64,528	\$ 59,817
Accrued compensation and employee benefits	44,812	43,292
Deferred revenues less cost of revenues	178,181	131,757
Income taxes payable	10,619	11,631
Other current liabilities	66,534	65,792
Total current liabilities	364,674	312,289
Deferred income taxes and other tax liabilities	55,818	53,830
Other long-term liabilities	4,643	3,789
Total liabilities	<u>425,135</u>	<u>369,908</u>
Commitments and contingencies (Note 9)		
Equity:		
Preferred stock, \$.01 par value, 5,000 shares authorized; none issued and outstanding	—	—
Common stock, \$.01 par value, 650,000 and 650,000 shares authorized; 268,231 and 259,394 shares issued; 171,232 and 170,753 shares outstanding at April 3, 2011 and January 2, 2011, respectively	2,682	2,594
Additional paid-in-capital	2,381,119	2,401,996
Accumulated other comprehensive loss	(2,090)	(3,203)
Accumulated deficit	(438,628)	(494,002)
	1,943,083	1,907,385
Less: shares of common stock held in treasury, at cost; 96,998 and 88,641 shares at April 3, 2011 and January 2, 2011, respectively	(1,372,550)	(1,202,949)
Total Cypress stockholders' equity	570,533	704,436
Noncontrolling interest	(1,727)	(1,543)
Total equity	<u>568,806</u>	<u>702,893</u>
Total liabilities and equity	<u>\$ 993,941</u>	<u>\$ 1,072,801</u>

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

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CYPRESS SEMICONDUCTOR CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended	
	April 3, 2011	April 4, 2010
	(In thousands, except Per-share amounts)	
Revenues	\$233,110	\$202,271
Costs and expenses:		
Cost of revenues	104,334	95,784
Research and development	47,865	40,049
Selling, general and administrative	58,652	51,281
Amortization of acquisition-related intangibles	698	776
Restructuring costs	734	327
Gain on divestiture	(34,291)	—
Total costs and expenses, net	177,992	188,217
Operating income	55,118	14,054
Interest and other income, net	1,606	730
Income before income taxes	56,724	14,784
Income tax provision	(1,350)	(2,110)
Income, net of taxes	55,374	12,674
Noncontrolling interest, net of taxes	(184)	(163)
Net income	55,190	12,511
Less: net loss attributable to noncontrolling interest	184	163
Net income attributable to Cypress	<u>\$ 55,374</u>	<u>\$ 12,674</u>
Net income per share attributable to Cypress:		
Basic	\$ 0.32	\$ 0.08
Diluted	\$ 0.28	\$ 0.07
Shares used in net income per share calculation:		
Basic	171,346	158,931
Diluted	199,943	190,892

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

CYPRESS SEMICONDUCTOR CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Three Months Ended	
	April 3, 2011	April 4, 2010
(In thousands)		
Cash flows from operating activities:		
Net income	\$ 55,190	\$ 12,511
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	13,543	12,673
Stock-based compensation expense	20,837	21,574
Charitable contribution of building	4,000	—
Gain on divestiture of business	(34,291)	—
Restructuring charges	412	327
Loss on sale or retirement of property and equipment	524	4
Deferred income taxes and other tax liabilities	696	1,070
Changes in operating assets and liabilities:		
Accounts receivable	(55,663)	(22,655)
Inventories	(7,564)	6,264
Other assets	(15,831)	(31)
Accounts payable and other accrued liabilities	7,066	(3,786)
Deferred revenues less cost of revenues	46,424	10,172
Net cash provided by operating activities	<u>35,343</u>	<u>38,123</u>
Cash flows from investing activities:		
Purchases of available-for-sale investments	(43,385)	(25,910)
Proceeds from sales or maturities of available-for-sale investments	78,326	2,411
Net contributions (distributions) of deferred compensation plan	382	(386)
Acquisition of property and equipment	(19,309)	(17,872)
Proceeds from sales of property and equipment	759	—
Proceeds from divestiture	14,951	—
Cash paid for other investments	(1,013)	(2,000)
Net cash provided by (used in) investing activities	<u>30,711</u>	<u>(43,757)</u>
Cash flows from financing activities:		
Repurchase of common shares	(76,404)	—
Withholding of common shares for tax obligations on vested restricted shares	(40,714)	(8,713)
Proceeds from issuance of common shares under employee stock plans	23,888	19,786
Yield enhancement structured agreements settled in cash, net	46,965	2,208
Yield enhancement structured agreements settled in stock	(52,483)	(34,164)
Yield enhancement structured agreements unsettled	(110,891)	—
Net cash used in financing activities	<u>(209,639)</u>	<u>(20,883)</u>
Net decrease in cash and cash equivalents	(143,585)	(26,517)
Cash and cash equivalents, beginning of period	263,183	243,558
Cash and cash equivalents, end of period	<u>\$ 119,598</u>	<u>\$217,041</u>

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

CYPRESS SEMICONDUCTOR CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Fiscal Years

Cypress Semiconductor Corporation (“Cypress” or the “Company”) reports on a fiscal-year basis. We end our quarters on the Sunday closest to the end of the applicable calendar quarter, except in a 53-week fiscal year, in which case the additional week falls into the fourth quarter of that fiscal year. Fiscal 2011 has 52 weeks and fiscal 2010 had 52 weeks. The first quarter of fiscal 2011 ended on April 3, 2011 and the first quarter of fiscal 2010 ended on April 4, 2010.

Basis of Presentation

In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments necessary to state fairly the financial information included therein. The financial data should be read in conjunction with the audited consolidated financial statements and related notes thereto included in our Annual Report on Form 10-K for the fiscal year ended January 2, 2011.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

The condensed consolidated results of operations for the three months ended April 3, 2011 are not necessarily indicative of the results to be expected for the full fiscal year.

Recently Adopted and Recently Issued Accounting Standards

In January 2010, the FASB issued updated guidance related to fair value measurements and disclosures, which requires a reporting entity to disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and to describe the reasons for the transfers. In addition, in the reconciliation for fair value measurements using significant unobservable inputs, or Level 3, a reporting entity should disclose separately information about purchases, sales, issuances and settlements (that is, on a gross basis rather than one net number). The updated guidance also requires that an entity should provide fair value measurement disclosures for each class of assets and liabilities and disclosures about the valuation techniques and inputs used to measure fair value for both recurring and non-recurring fair value measurements for Level 2 and Level 3 fair value measurements. The updated guidance is effective for interim or annual financial reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances and settlements in the roll forward activity in Level 3 fair value measurements, which are effective for fiscal years beginning after December 15, 2010 and for interim periods within those fiscal years. Except for the presentation and disclosure requirements required by this guidance, there was no impact on our condensed consolidated financial statements.

CYPRESS SEMICONDUCTOR CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

NOTE 2. DIVESTITURE

As part of Cypress's continued efforts to focus on programmable products including our flagship PSoC® programmable system-on-chip solution and our TrueTouch™ touch-sensing controllers, we divested our image sensors product family and sold it to ON Semiconductor Corporation (ON). Dan McCranie, a member of the board of directors of Cypress, is the chairman of the board of directors at ON.

Product Families / Businesses	Reportable Segment	Buyer	Total Consideration
The image sensors product family	Memory and Imaging Division	ON Semiconductor	\$ 34.0 million

In connection with the divestiture, we recorded a total gain of \$34.3 million. We received \$14.9 million in cash consideration in March of 2011 and received the remaining \$19.1 million on April 29, 2011. The following table summarizes the components of the gain:

	Image Sensors (In thousands)
Cash proceeds	\$ 34,025
Assets sold:	
Inventories	(3,617)
Prepaid and other assets	(2,003)
Property, plant and equipment	(1,178)
Liabilities disposed of:	
Accounts payable	1,508
Other liabilities	3,416
Taxes payable	1,129
Customer advances	1,239
Transaction and other costs	(228)
Gain on divestiture	<u>\$ 34,291</u>

In connection with the divestiture of the image sensors product family, we transferred approximately 80 employees to ON. In addition, we entered into a transition service agreement with ON where we act as an agent for them and provide certain services related to shipping, manufacturing, planning and general administrative functions. As a result of this agreement we may end up with a net payable or receivable to or from ON. As of April 3, 2011 the transition service agreement resulted in a \$0.4 million receivable from ON and is reflected in "Other current assets" in the Condensed Consolidated Balance Sheet.

NOTE 3. GOODWILL AND INTANGIBLE ASSETS***Goodwill***

The carrying amount of goodwill at April 3, 2011 was \$31.8 million in the Consumer and Computation Division ("CCD") and was unchanged from the balance at January 2, 2011. CCD is the only reportable business segment with goodwill.

Intangible Assets

The following tables present details of our intangible assets:

CYPRESS SEMICONDUCTOR CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

<u>As of April 3, 2011</u>	<u>Gross</u>	<u>Accumulated Amortization (In thousands)</u>	<u>Net</u>
Total acquisition-related intangible assets	\$ 95,135	\$ (86,588)	\$ 8,547
Non-acquisition related intangible assets	10,548	(7,166)	3,382
Total intangible assets	<u>\$105,683</u>	<u>\$ (93,754)</u>	<u>\$11,929</u>

<u>As of January 2, 2011</u>	<u>Gross</u>	<u>Accumulated Amortization (In thousands)</u>	<u>Net</u>
Acquisition-related intangible assets	\$100,134	\$ (91,490)	\$ 8,644
Non-acquisition related intangible assets	10,548	(6,693)	3,855
Total intangible assets	<u>\$110,682</u>	<u>\$ (98,183)</u>	<u>\$12,499</u>

As of April 3, 2011, the estimated future amortization expense of intangible assets was as follows:

<u>(In thousands)</u>	
2011 (remaining nine months)	\$ 3,514
2012	4,246
2013	3,301
2014	868
Total future amortization expense	<u>\$11,929</u>

CYPRESS SEMICONDUCTOR CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

NOTE 4. RESTRUCTURING

For the three months ended April 3, 2011 and April 4, 2010, we recorded restructuring charges of \$0.7 million and \$0.3 million, respectively. The determination of when we accrue for severance and benefits costs, and which accounting standard applies, depends on whether the termination benefits are provided under a one-time benefit arrangement or under an on-going benefit arrangement.

Fiscal 2010 Restructuring Plan

During the third quarter of fiscal 2010, we implemented a restructuring plan to exit certain of our back-end manufacturing operations located in the Philippines (“Fiscal 2010 Restructuring Plan”). These actions are intended to reduce the cost of our back-end manufacturing by selling our labor intensive assembly and test operations to lower cost third-party subcontractors in other parts of Asia and by the continued shifting of these operations to our fully automated back-end processes.

Under the Fiscal 2010 Restructuring Plan, we recorded total restructuring charges of \$2.7 million. As of April 3, 2011, our restructuring provision of \$2.4 million was related to personnel costs associated with severance and benefits of our employees. We expect to eliminate approximately 300 manufacturing positions and 200 contractors or approximately 34% of our Philippines plant workforce by the end of fiscal 2011.

Fiscal 2008/9 Restructuring Plan

In fiscal 2008, we initiated a restructuring plan as part of a company-wide cost saving initiative which continued into 2011 aimed to reduce operating costs in response to the economic downturn (“Fiscal 2008/9 Restructuring Plan”).

Restructuring activities related to personnel costs are summarized as follows:

<u>(In thousands)</u>	
Balance as of January 2, 2011	\$1,106
Provision	322
Non-Cash	257
Cash payments	<u>(373)</u>
Balance as of April 3, 2011	<u>\$1,312</u>

As a result of the Fiscal 2008/9 plan, we have eliminated approximately 835 positions. In the fourth quarter of 2010, we substantially completed the remaining actions we had for this plan.

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Fiscal 2007 Restructuring Plan

During fiscal 2007, we implemented a restructuring plan to exit our manufacturing facility located in Round Rock, Texas (“Fiscal 2007 Restructuring Plan”). The Fiscal 2007 Restructuring Plan included the termination of employees and the disposal of assets, primarily consisting of land, building and manufacturing equipment, located in the Texas facility.

The actions related to the 2007 Restructuring Plan were substantially completed in fiscal 2009. In the second quarter of 2010, we recorded a \$2.4 million gain on the sale of certain equipment in our Texas facility. On a quarterly basis we continue to incur expenses related to ongoing maintenance and upkeep of the Texas facility until we complete the sale of the property.

Assets Held For Sale:

The Texas facility ceased operations in the fourth quarter of fiscal 2008. As our management has committed to a plan to sell the assets associated with the facility, we have classified the assets as held for sale and recorded the assets at the lower of their carrying amount or estimated fair value less cost to sell. Fair value was determined by an analysis of market prices for similar assets. In the second quarter of fiscal 2010, we recorded a \$1.5 million write-down to the estimated fair value related to these assets.

The net book value of the remaining restructured assets that were classified as held for sale and included in “Other current assets” in the Condensed Consolidated Balance Sheets was \$6.9 million as of April 3, 2011 and as of January 2, 2011.

We had expected to complete the disposal of the restructured assets by the fourth quarter of fiscal 2009; however, due to the downturn and uncertainty in the commercial real estate market, we were unable to secure a buyer for the Texas facility. In response, during fiscal 2010 we revised the asking price for the property and expect to sell the facility within the next twelve months; however, there can be no assurance of this and our ability to complete the sale of any restructured assets may be impacted by the current economic and credit conditions.

NOTE 5. BALANCE SHEET COMPONENTS

Accounts Receivable, Net

	As of	
	April 3, 2011	January 2, 2011
	(In thousands)	
Accounts receivable, gross	\$177,657	\$121,876
Allowance for doubtful accounts receivable and sales returns	(4,268)	(4,150)
Total accounts receivable, net	<u>\$173,389</u>	<u>\$117,726</u>

Inventories, Net

	As of	
	April 3, 2011	January 2, 2011
	(In thousands)	
Raw materials	\$ 8,010	\$ 7,350
Work-in-process	75,560	72,072
Finished goods	20,552	22,341
Total inventories, net	<u>\$104,122</u>	<u>\$101,763</u>

CYPRESS SEMICONDUCTOR CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Other Current Assets

	As of	
	April 3, 2011	January 2, 2011
	(In thousands)	
Prepaid expenses	\$24,568	\$ 24,004
Receivable from ON Semiconductor Corporation (see Note 2)	19,074	—
Prepaid to Grace (see Note 9)	7,700	—
Assets held for sale (see Note 4)	6,913	6,913
Other current assets	12,714	10,991
Total other current assets	<u>\$70,969</u>	<u>\$ 41,908</u>

Other Long-Term Assets

	As of	
	April 3, 2011	January 2, 2011
	(In thousands)	
Employee deferred compensation plan	\$32,314	\$ 30,458
Investments:		
Debt securities	19,094	23,708
Equity securities	4,236	2,804
Prepaid to Grace (see Note 9)	4,432	—
Other assets	13,668	15,716
Total other long-term assets	<u>\$73,744</u>	<u>\$ 72,686</u>

Other Current Liabilities

	As of	
	April 3, 2011	January 2, 2011
	(In thousands)	
Employee deferred compensation plan	\$31,992	\$ 29,974
Restructuring accrual (See Note 4)	3,957	3,559
Other current liabilities	30,585	32,259
Total other current liabilities	<u>\$66,534</u>	<u>\$ 65,792</u>

Deferred Income Taxes and Other Tax Liabilities

	As of	
	April 3, 2011	January 2, 2011
	(In thousands)	
Deferred income taxes	\$ 216	\$ (1,135)
Non-current tax liabilities	55,602	54,965
Total deferred income taxes and other tax liabilities	<u>\$55,818</u>	<u>\$ 53,830</u>

CYPRESS SEMICONDUCTOR CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

NOTE 6. FAIR VALUE MEASUREMENTS

Assets/Liabilities Measured at Fair Value on a Recurring Basis

The following tables present the fair value hierarchy for our financial assets and liabilities measured at fair value on a recurring basis:

	As of April 3, 2011			Total
	Level 1	Level 2	Level 3	
(In thousands)				
Financial Assets				
Investments:				
Commercial paper	\$ —	\$ 2,700	\$ —	\$ 2,700
Money market funds	15,334	—	—	15,334
Corporate notes/bonds	—	40,130	—	40,130
Auction rate securities	—	—	19,094	19,094
Federal Agency	—	33,857	—	33,857
US Treasury	48,073	—	—	48,073
Employee deferred compensation plan:				
Commercial Paper	2,161	—	—	2,161
Money market	384	—	—	384
Mutual funds	21,756	—	—	21,756
Fixed income	2,101	—	—	2,101
Equity securities	5,911	—	—	5,911
Total financial assets	\$ 95,720	\$76,687	\$19,094	\$191,501
Financial Liabilities				
Employee deferred compensation plan	\$ 31,992	\$ —	\$ —	\$ 31,992
Total financial liabilities	\$ 31,992	\$ —	\$ —	\$ 31,992

	As of January 2, 2011			Total
	Level 1	Level 2	Level 3	
(In thousands)				
Financial Assets				
Investments:				
Commercial paper	\$ —	\$ 2,399	\$ —	\$ 2,399
Money market funds	105,058	—	—	105,058
U.S. treasuries	50,054	—	—	50,054
Corporate notes/bonds	—	52,503	—	52,503
Federal agency	—	25,958	—	25,958
Auction rate securities	—	—	23,708	23,708
Marketable equity securities	804	—	—	804
Employee deferred compensation plan:				
Cash and cash equivalents	1,771	—	—	1,771
Money market	386	—	—	386
Mutual funds	20,579	—	—	20,579
Fixed income	3,045	—	—	3,045
Equity securities	4,677	—	—	4,677
Total financial assets	\$186,374	\$80,860	\$23,708	\$290,942
Financial Liabilities				
Employee deferred compensation plan	\$ 29,974	\$ —	\$ —	\$ 29,974
Total financial liabilities	\$ 29,974	\$ —	\$ —	\$ 29,974

CYPRESS SEMICONDUCTOR CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Valuation Techniques:

We use quoted prices for identical instruments in active markets to determine the fair value for our Level 1 financial instruments, which include U.S. treasuries, money market funds and marketable equity securities. In addition, our employee deferred compensation plan is classified as Level 1 as the plan invests in mutual funds, marketable equity securities and our common stock.

If quoted prices in active markets for identical assets or liabilities are not available to determine the fair value of our financial instruments, then we use observable inputs including benchmark yields, reported trades, broker/dealer quotes or alternative pricing sources with reasonable levels of price transparency. These investments are classified as Level 2 and primarily consist of federal agency, commercial paper and corporate notes/bonds. In addition, we have derivative instruments that are classified as Level 2 financial assets. We determine the fair value of these instruments based on modeling techniques that include inputs such as market volatilities, spot rates and interest differentials from published sources.

Our Level 3 financial assets primarily include investments in auction rate securities and a commercial paper investment. The valuation techniques are described as follows:

Auction Rate Securities:

As of April 3, 2011, all of our auction rate securities are classified as Level 3 financial instruments. Auction rate securities are investments with contractual maturities generally between 20 and 30 years and are usually found in the form of municipal bonds, preferred stock, a pool of student loans or collateralized debt obligations with interest rates resetting every seven to 49 days through an auction process. At the end of each reset period, investors can sell or continue to hold the securities at par. The auction rate securities held by us are backed by student loans originated under the Federal Family Education Loan Program (FFELP), which are guaranteed by the U.S. Federal Department of Education.

As of April 3, 2011, all of our auction rate securities held by us were rated as either AAA or Aaa by the major independent rating agencies and all of our auction rate securities have experienced failed auctions due to sell orders exceeding buy orders. These failures are not believed to be a credit issue with the underlying investments, but rather caused by a lack of liquidity. Under the contractual terms, the issuer is obligated to pay penalty rates should an auction fail. The funds associated with failed auctions are not expected to be accessible until one of the following occurs: a successful auction occurs, the issuer redeems the issue, a buyer is found outside of the auction process or the underlying securities have matured. Given these circumstances and the lack of liquidity, we have classified our auction rate securities totaling \$19.1 million as long-term investments as of April 3, 2011.

During fiscal 2011, we performed analyses to assess the fair value of our auction rate securities. In the absence of a liquid market to value these securities, we prepared a valuation model based on discounted cash flows. The assumptions used at April 3, 2011 were as follows:

- 7 years to liquidity;
- continued receipt of contractual interest which provides a premium spread for failed auctions; and
- discount rates of 1.86% – 5.52%, which incorporates a spread for both credit and liquidity risk.

Based on these assumptions, we estimated that the value of our auction rate securities is approximately 91% of their stated par value as of April 3, 2011, representing a decline in value of approximately \$2.0 million which was recorded in accumulated other comprehensive income as an unrealized loss.

CYPRESS SEMICONDUCTOR CORPORATION
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The following table presents a summary of changes in our Level 3 investments measured at fair value on a recurring basis:

	<u>Auction Rate Securities</u>
Balance as of January 2, 2011	\$ 23,708
Unrealized gain recorded in "Accumulated other comprehensive loss"	586
Realized loss	(75)
Amount settled at par	(5,125)
Balance as of April 3, 2011	<u>\$ 19,094</u>

Available-For-Sale Securities

The following table presents our fair value hierarchy for our investments measured at fair value on a non-recurring basis and the impairment loss related to these investments:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total as of April 3, 2011</u>	<u>Impairment Loss recorded in "Interest and Other Income (Expense), Net" Three Months Ended</u>	
					<u>April 3, 2011</u>	<u>April 4, 2010</u>
Non-marketable equity securities	\$ —	\$ —	\$2,000	\$ 2,000	\$ —	\$ —

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NOTE 7. INVESTMENTS

Available-For-Sale Securities

The following tables summarize our available-for-sale and other investments:

<u>As of April 3, 2011</u>	<u>Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
	(In thousands)			
Cash equivalents:				
Money market funds	\$ 15,334	\$ —	\$ —	\$ 15,334
Commercial paper	1,500	—	—	1,500
Total cash equivalents	16,834	—	—	16,834
Short-term investments:				
Certificate of deposit	18,061	—	—	18,061
Commercial paper	1,200	—	—	1,200
Corporate notes/bonds	40,022	112	(4)	40,130
Federal Agency	33,906	1	(50)	33,857
U.S. Treasuries	48,059	14	—	48,073
Total short-term investments	141,248	127	(54)	141,321
Long-term investments:				
Auction rate securities	21,100	—	(2,006)	19,094
Marketable equity securities	1,817	419	—	2,236
Total long-term investments	22,917	419	(2,006)	21,330
Total available-for-sale securities and other investments	\$180,999	\$ 546	\$ (2,060)	\$179,485
<u>As of January 2, 2011</u>	<u>Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
	(In thousands)			
Cash equivalents:				
Money market funds	\$105,058	\$ —	\$ —	\$105,058
Total cash equivalents	105,058	—	—	105,058
Short-term investments:				
Certificate of deposit	40,163	—	—	40,163
U.S. treasuries	50,053	2	(1)	50,054
Corporate notes/bonds	52,390	135	(22)	52,503
Federal agency	25,983	5	(30)	25,958
Commercial paper	2,400	—	—	2,400
Total short-term investments	170,989	142	(53)	171,078
Long-term investments:				
Auction rate securities	26,300	—	(2,592)	23,708
Marketable equity securities	1,187	—	(383)	804
Total long-term investments	27,487	—	(2,975)	24,512
Total available-for-sale securities and other investments	\$303,534	\$ 142	\$ (3,028)	\$300,648

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The available-for-sale debt investments that we hold are all high investment grade. The unrealized losses on our investments are due primarily to changes in interest rates and market conditions of the underlying securities. Because we do not intend to sell and it is likely we will not be required to sell before recovering our cost, which may be at maturity, except for the impairment recorded in the respective periods, we did not consider these investments to be other-than-temporarily impaired as of April 3, 2011 and January 2, 2011.

For individual marketable equity securities with unrealized losses, we evaluated the near-term prospects in relation to the severity and duration of the impairment. Based on that evaluation and our ability and intent to hold these investments for a reasonable period of time, we did not consider these investments to be other-than-temporarily impaired as of April 3, 2011 and January 2, 2011.

As of April 3, 2011, contractual maturities of our available-for-sale, non-equity investments were as follows:

	<u>Cost</u>	<u>Fair Value</u>
	<u>(In thousands)</u>	
Maturing within one year	\$105,880	\$105,949
Maturing in one to three years	52,202	52,206
Maturing in more than three years	21,100	19,094
Total	<u>\$179,182</u>	<u>\$177,249</u>

Realized gains and realized losses from sales of available-for-sale and non-equity investments were immaterial in both three months periods ended April 3, 2011 and April 4, 2010. Proceeds from sales or maturities of available-for-sale investments were \$78.3 million and \$2.4 million for the three months ended April 3, 2011 and April 4, 2010, respectively.

Investments in Equity Securities

The following table summarizes our equity investments:

	<u>As of</u>	
	<u>April 3,</u>	<u>January 2,</u>
	<u>2011</u>	<u>2011</u>
	<u>(In thousands)</u>	
Long-term investments:		
Marketable equity securities	\$2,236	\$ 804
Non-marketable equity securities	<u>2,000</u>	<u>2,000</u>
Total long-term investments	<u>4,236</u>	<u>2,804</u>
Total equity investments	<u>\$4,236</u>	<u>\$ 2,804</u>

We did not sell any equity investments during first quarter of fiscal 2011 or fiscal 2010.

Impairment of Investments

For the three month periods ended April 3, 2011 and April 4, 2010, no impairment charges were recorded for our investments.

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Employee Deferred Compensation Plan

We have a deferred compensation plan, which provides certain key employees, including our executive management, with the ability to defer the receipt of compensation in order to accumulate funds for retirement on a tax-deferred basis. We do not make contributions to the deferred compensation plan or guarantee returns on the investments. Participant deferrals and investment gains and losses remain as our liabilities and the underlying assets are subject to claims of general creditors.

Under the deferred compensation plan, the assets are recorded at fair value in each reporting period with the offset being recorded in “Other income (expense), net.” The liabilities are recorded at fair value in each reporting period with the offset being recorded as an operating expense or income. As of April 3, 2011 and January 2, 2011, the fair value of the assets was \$32.3 million and \$30.5 million, respectively, and the fair value of the liabilities was \$32.0 million and \$30.0 million, respectively.

All non-cash expense and income recorded under the deferred compensation plan were included in the following line items in the Condensed Consolidated Statements of Operations:

	Three Months Ended	
	April 3, 2011	April 4, 2010
	(In thousands)	
Changes in fair value of assets recorded in:		
Interest and other income, net	\$ 1,474	\$ 835
Changes in fair value of liabilities recorded in:		
Cost of revenues	(204)	(141)
Research and development expenses	(509)	(290)
Selling, general and administrative expenses	(923)	(596)
Total expense	<u>\$ (162)</u>	<u>\$ (192)</u>

NOTE 8. STOCK-BASED COMPENSATION

Outstanding Employee Equity Awards

In the third quarter of 2008, a committee of our Board of Directors (the “Board”) approved the distribution of the SunPower Class B common stock held by us to our stockholders. On September 29, 2008 we completed the distribution of 42.0 million shares of SunPower Class B common stock to our stockholders (the “Spin-Off”).

In conjunction with the Spin-Off, the Board approved certain adjustments to our 1994 and 1999 Stock Plans (together, the “Plans”). Specifically, the Board approved amendments to make proportionate adjustments to, among other things, outstanding employee equity awards, including stock options, restricted stock units and restricted stock awards under the Plans to preserve the intrinsic value of the awards before and after the Spin-Off. These changes included a proportionate adjustment in the number of shares issuable pursuant to the outstanding awards and the per-share exercise price of the options.

The Board also approved certain adjustments with respect to our Employee Stock Purchase Plan (the “ESPP”) to offset the decrease in our common stock price resulting from the Spin-Off. These changes included a proportionate adjustment in the offering date price per share of our common stock and the maximum number of shares participants may purchase under the ESPP.

The modification of the outstanding employee equity awards and the ESPP related to the Spin-Off resulted in additional non-cash stock-based compensation. The amount was measured based upon the difference between the fair value of the awards immediately before and after the modification. Of the total additional non-cash stock-based compensation, \$1.7 million and \$6.2 million, net of forfeitures was recognized in the first quarter of fiscal 2011 and 2010, respectively. The remaining \$5.9 million will be recognized over the remaining vesting periods on an accelerated basis, less forfeitures.

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The following table summarizes the stock-based compensation expense, by line item recorded in the Condensed Consolidated Statements of Operations:

	<u>Three Months Ended</u>	
	<u>April 3, 2011</u>	<u>April 4, 2010</u>
	(In thousands)	
Cost of revenues	\$ 6,510	\$ 5,970
Research and development	5,473	4,357
Selling, general and administrative	8,854	11,247
Total stock-based compensation expense	<u>\$20,837</u>	<u>\$21,574</u>

As stock-based compensation expense recognized in the Condensed Consolidated Statements of Operations is based on awards ultimately expected to vest, it has been reduced for estimated forfeitures. The accounting guidance requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates.

Consolidated cash proceeds from the issuance of shares under the employee stock plans were approximately \$23.9 million and \$19.8 million for the three months ended April 3, 2011 and April 4, 2010, respectively. We did not recognize a tax benefit from stock option exercises for the three months ended April 3, 2011 or April 4, 2010.

As of April 3, 2011 and January 2, 2011, stock-based compensation capitalized in inventories totaled \$4.6 million and \$6.2 million, respectively.

The following table summarizes the stock-based compensation expense by type of award:

	<u>Three Months Ended</u>	
	<u>April 3, 2011</u>	<u>April 4, 2010</u>
	(In thousands)	
Stock options	\$ 3,519	\$ 5,263
Restricted stock units and restricted stock awards	15,342	15,080
ESPP	1,976	1,231
Total stock-based compensation expense	<u>\$20,837</u>	<u>\$21,574</u>

The following table summarizes the unrecognized stock-based compensation balance by type of award:

	<u>As of April 3, 2011</u>	<u>Weighted- Average Amortization Period</u>
	(In thousands)	(In years)
Stock options	\$ 28,758	1.93
Restricted stock units and restricted stock awards	105,689	1.38
ESPP	2,781	0.45
Total unrecognized stock-based compensation balance	<u>\$ 137,228</u>	1.48

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Valuation Assumptions

We estimated the fair value of the stock options and ESPP using the Black-Scholes valuation model with the following assumptions:

	Three Months Ended	
	April 3, 2011	April 4, 2010
Expected life	0.5 – 7.0 years	0.5 – 7.0 years
Volatility	47.4% - 50.3%	42.2% - 54.2%
Risk-free interest rate	0.2% - 2.9%	0.1% - 3.1%
Dividend yield	0.0%	0.0%

The fair value of the restricted stock units and the restricted stock awards was based on our stock price on the date of grant.

Equity Incentive Program

As of April 3, 2011, approximately 11.1 million stock options or 5.9 million restricted stock units and restricted stock awards were available for grant under the Amended 1994 Stock Plan.

Stock Options:

The following table summarizes our stock option activities:

	Shares	Weighted-Average Exercise Price Per Share
	(In thousands, except per-share amount)	
Options outstanding as of January 2, 2011	36,070	\$ 5.51
Granted	278	\$ 21.50
Exercised	(5,128)	\$ 4.66
Forfeited or expired	(540)	\$ 7.72
Options outstanding as of April 3, 2011	<u>30,680</u>	\$ 5.76
Options exercisable as of April 3, 2011	<u>29,151</u>	\$ 5.60

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Restricted Stock Units and Restricted Stock Awards:

The following table summarizes our restricted stock unit and restricted stock award activities:

	<u>Shares</u>	<u>Weighted-Average Fair Value per Share</u>
	(In thousands, except per-share amounts)	
Balance as of January 2, 2011	14,970	\$ 4.90
Granted	94	\$ 21.25
Vested	(4,635)	\$ 21.27
Forfeited	(679)	\$ 8.16
Balance as of April 3, 2011	<u>9,750</u>	<u>\$ 2.95</u>

The balance as of April 3, 2011 included approximately 4.1 million performance-based restricted stock units and restricted stock awards granted under the 1994 Amended Plan. These performance-based awards (“PARS”) were issued to certain senior-level employees and can be earned ratably over a remaining period of one year, subject to the achievement of certain performance milestones set by the Compensation Committee of the Board. These performance milestones include:

- stock appreciation target against the Philadelphia Semiconductor Sector Index (“SOX”);
- certain levels of non-GAAP profit-before-taxes percentage; and
- annual revenue growth in total and for certain products.

If the milestones are not achieved, the shares are forfeited and cannot be earned in future periods.

We estimated the fair value of the shares with the market-condition milestone using a Monte Carlo valuation model with the following weighted-average assumptions:

	<u>Three Months Ended</u>	
	<u>April 3 2011</u>	<u>April 4 2010</u>
Volatility of common stock	35.7%	39.8%
Volatility of the SOX	25.2%	30.3%
Correlation coefficient	0.77	0.77
Risk-free interest rate	0.2%	0.3%

The fair value of the shares with the performance-related milestones was equivalent to the grant-date fair value of our common stock. In addition, we granted other performance-based and service-based restricted stock units whose fair value is typically equivalent to the grant-date fair value of our common stock.

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NOTE 9. COMMITMENTS AND CONTINGENCIES

During the fourth quarter of fiscal 2010, we advanced \$2.5 million in pre-payments to Grace Semiconductor Manufacturing Corporation (“Grace”), a strategic foundry partner, to secure access to a certain supply level of wafers. In the first quarter of fiscal 2011, we advanced an additional \$10.6 million in pre-payments. These payments will be applied against future purchases of inventory from Grace over an estimated period of 10 to 18 months but no longer than 2 years.

Product Warranties

We generally warrant our products against defects in materials and workmanship for a period of one year and that product warranty is generally limited to a refund of the original purchase price of the product or a replacement part. We estimate our warranty costs based on historical warranty claim experience. Warranty returns are included in the allowance for sales returns. The allowance for sales returns is reviewed quarterly to verify that it properly reflects the remaining obligations based on the anticipated returns over the balance of the obligation period.

The following table presents our warranty activities, including amounts recorded in the allowance for sales returns:

	Three Months Ended	
	April 3, 2011	April 4, 2010
	(In thousands)	
Beginning balance	\$ 3,347	\$ 3,151
Settlements made	(220)	(995)
Provisions	<u>339</u>	<u>2,545</u>
Ending balance	<u>\$ 3,466</u>	<u>\$ 4,701</u>

Charitable donation of building

On April 1, 2011 we sold a building to a charitable organization for \$4.0 million in exchange for a promissory note. The promissory note will be paid over the next four years in \$1.0 million annual payments and is reflected in our Condensed Consolidated Balance Sheet as “Other current assets” and “Other long-term assets”. In addition, we made a \$4.0 million unconditional pledge to the same charitable organization to be paid in four \$1.0 million installments over the next four years. This amount is reflected in “Other current liabilities” and “Other non-current liabilities”.

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Litigation and Asserted Claims

On August 21, 2009, X-Point Technologies filed a single patent infringement case against us and 29 other defendants in the U.S. District Court in Delaware. The patent at issue covers X-Point's technology for data transfer between storage devices and network devices without the use of a CPU or memory. The discovery phase of this case has now ended and trial has been set for February 2012. We believe we have meritorious defenses to the allegations set forth in the complaint and will vigorously defend ourselves in this matter.

On January 21, 2011, Avago Technologies filed a patent infringement case against us in the U.S. District Court in Delaware. The three patents at issue cover Avago's touch technology, including finger navigation. Avago has made no specific demand for relief in this matter. We believe we have meritorious defenses to the allegations set forth in the complaint and will vigorously defend ourselves in this matter.

On March 30, 2011, we filed a five patent infringement case against GSI Technology in the U.S. District Court in Minnesota. The five patents at issue cover GSI's static random access memory (SRAM) technology, including GSI's Sigma DDR and SigmaQuad II and III families of memory products. We are seeking damages as well as injunctive relief from the court.

We are currently a party to various other legal proceedings, claims, disputes and litigation arising in the ordinary course of business. Based on the our own investigations, we believe the ultimate outcome of our current legal proceedings, individually and in the aggregate, will not have a material adverse effect on our financial position, results of operation or cash flows. However, because of the nature and inherent uncertainties of the litigation, should the outcome of these actions be unfavorable, our business, financial condition, results of operations or cash flows could be materially and adversely affected.

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NOTE 10. DEBT AND EQUITY TRANSACTIONS

Line of Credit

In March 2011, we amended our revolving line of credit with Silicon Valley Bank to extend the maturity of the credit facility to February 28, 2012 and to reduce the commitment amount from \$25.0 million to \$15.0 million. Loans made under the line of credit bear interest based upon the Wall Street Journal Prime Rate (3.25% as of April 3, 2011) or LIBOR plus 2.5% (2.80% as of April 3, 2011). The line of credit agreement includes a variety of covenants including restrictions on the incurrence of indebtedness, incurrence of loans, the payment of dividends or distribution on our capital stock, and transfers of assets and financial covenants with respect to an adjusted quick ratio and tangible net worth. As of April 3, 2011, we were in compliance with all of the financial covenants under the line of credit. Our obligations under the line of credit are guaranteed and collateralized by the common stock of certain of our business entities. We intend to use the line of credit on an as-needed basis to fund working capital and capital expenditures. To date, there have been no borrowings under the line of credit.

Stock Repurchase Program

On October 21, 2010, our Board authorized a \$600 million stock buyback program. The program allows us to purchase our common stock or enter into equity derivative transactions related to our common stock. The timing and actual amount expended with the new authorized funds will depend on a variety of factors including the market price of our common stock, regulatory, legal, and contractual requirements, and other market factors. The program does not obligate us to repurchase any particular amount of common stock and may be modified or suspended at any time at our discretion. As of April 3, 2011, we used \$198.6 million to repurchase 10.1 million shares with \$401.4 million remaining under the program available for additional repurchases.

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Yield Enhancement Program

On October 28, 2009 the Audit Committee approved a yield enhancement strategy intended to improve the yield on our available cash. As part of this program, the Audit Committee authorized us to enter into short-term yield enhanced structured agreements, typically with maturities of 90 days or less, correlated to our stock price. Under the agreements we entered into to date, we pay a fixed sum of cash upon execution of an agreement in exchange for the financial institution's obligations to pay either a pre-determined amount of cash or shares of our common stock depending on the closing market price of our common stock on the expiration date of the agreement. Upon expiration of each agreement, if the closing market price of our common stock is above the pre-determined price, we will have our cash investment returned plus a yield substantially above the yield currently available for short-term cash investments. If the closing market price is at or below the pre-determined price, we will receive a number of shares specified at the agreement's inception. As the outcome of these arrangements is based entirely on our stock price and does not require us to deliver either shares or cash, other than the original investment, the entire transaction is recorded in equity.

We entered into a yield enhanced structured agreement based upon a comparison of the yields available in the financial markets for similar maturities against the expected yield to be realized per the structured agreement and the related risks associated with this type of arrangement. We believe the risk associated with these types of agreements is no different than alternative investments available to us with equivalent counterparty credit ratings. All counterparties to a yield enhancement program have a credit rating of at least Aa2 or A as rated by major independent rating agencies. For all such agreements that matured to date, the yields of the structured agreements were far superior to the yields available in the financial markets primarily due to the volatility of our stock price and the pre-payment aspect of the agreements. The counterparty is willing to pay a premium over the yields available in the financial markets due to the structure of the agreement.

The following table summarizes the activity and settlements of our yield enhancement program in the first quarter of fiscal 2011:

<u>Aggregate Price Paid</u>	<u>Total Proceeds Received Upon Maturity</u>	<u>Total Number of Shares Received Upon Maturity</u>	<u>Average Price Paid per Share</u>
(In thousands, except per-share amounts)			
\$ 43,926	\$ 46,965	—	\$ —
52,483	—	2,500	20.99
57,579	—	3,000	19.19
53,313	36,412	1,000	17.77
<u>\$207,301</u>	<u>\$ 83,377</u>	<u>6,500</u>	<u>\$ 19.67</u>

On March 1, 2011 we entered into a short-term yield enhanced structured agreement with a maturity of less than 45 days at an aggregate price of approximately \$57.6 million. On April 18, 2011, we settled this agreement and received 3 million shares of our common stock.

On March 9, 2011 we entered into a short-term yield enhanced structured agreement with a maturity of less than 45 days at an aggregate price of approximately \$53.3 million. On April 20, 2011, we settled this agreement and received 1 million shares of our common stock at an aggregate price of \$17.8 million and received upon maturity net proceeds of \$0.9 million.

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NOTE 11. ACCUMULATED OTHER COMPREHENSIVE INCOME AND COMPREHENSIVE LOSS

The components of accumulated other comprehensive income (loss) were as follows:

	As of	
	April 3, 2011	January 2, 2011
	(In thousands)	
Accumulated net unrealized gains on available-for-sale investments	\$(1,735)	\$ (2,698)
Other	(355)	(505)
Total accumulated other comprehensive income (loss)	<u>\$(2,090)</u>	<u>\$ (3,203)</u>

The components of comprehensive income (loss), net of tax, were as follows:

	Three Months Ended	
	April 3, 2011	April 4, 2010
	(In thousands)	
Net income attributable to Cypress	\$55,374	\$12,674
Net unrealized gains (losses) on available-for-sale investments	963	(432)
Other	150	—
Total comprehensive income (loss)	<u>\$56,487</u>	<u>\$12,242</u>

NOTE 12. FOREIGN CURRENCY DERIVATIVES

We operate and sell products in various global markets and purchase capital equipment using foreign currencies. As a result, we are exposed to risks associated with changes in foreign currency exchange rates. We may use various hedge instruments from time to time to manage the exposures associated with purchases of foreign sourced equipment, net asset or liability positions of our subsidiaries and forecasted revenues and expenses. We do not enter into foreign currency derivative financial instruments for speculative or trading purposes. The counterparties to these hedging transactions are creditworthy multinational banks and the risk of counterparty nonperformance associated with these contracts is not considered to be material as of April 3, 2011.

As of April 3, 2011 and January 2, 2011, our hedge instruments consisted primarily of foreign currency forward contracts. We estimate the fair value of our forward contracts based on spot and forward rates from published sources.

We record hedges of certain foreign currency denominated monetary assets and liabilities at fair value at the end of each reporting period with the related gains or losses recorded in "Interest and other income, net" in the Condensed Consolidated Statements of Operations. The gains or losses on these contracts are substantially offset by transaction gains or losses on the underlying balances being hedged. As of April 3, 2011 and January 2, 2011, we had outstanding forward contracts with an aggregate notional value of \$0.4 million at each period end, to hedge the risks associated with foreign currency denominated assets and liabilities.

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NOTE 13. INCOME TAXES

Our income tax expense was \$1.4 million for the three months ended April 3, 2011 and \$2.1 million for the three months ended April 4, 2010. The tax provision for the first quarter of fiscal 2011 and fiscal 2010 was primarily attributable to non-U.S. taxes on income earned in foreign jurisdictions.

Unrecognized Tax Benefits

As of April 3, 2011 and January 2, 2011, the amount of unrecognized tax benefits that, if recognized, would affect our effective tax rate totaled \$43.5 million and \$43.6 million, respectively.

Management believes events that could occur in the next twelve months and cause a material change in our unrecognized tax benefits include, but are not limited to, the following:

- completion of examinations by the U.S. or foreign taxing authorities; and
- expiration of statutes of limitations on our tax returns.

The calculation of unrecognized tax benefits involves dealing with uncertainties in the application of complex global tax regulations. Management regularly assess our tax positions in light of legislative, bilateral tax treaty, regulatory and judicial developments in the countries in which we do business. We believe it is possible that we may recognize approximately \$21 million to \$23 million of our existing unrecognized tax benefits within the next twelve months as a result of the lapse of statutes of limitations, and the resolution of examinations with U.S. and various foreign tax authorities.

Classification of Interest and Penalties

Our policy is to classify interest and penalties, if any, as components of the income tax provision in the Condensed Consolidated Statements of Operations. As of April 3, 2011 and January 2, 2011, the amount of accrued interest and penalties totaled \$10.4 million and \$10.1 million, respectively.

Tax Years and Examination

The Internal Revenue Service (“IRS”) is currently conducting an examination of our federal income tax returns for fiscal years 2006-2008. As of April 3, 2011, no material adjustments to our tax liabilities have been proposed by the IRS. However, the IRS has not completed their examination and there can be no assurance that there will be no material adjustments upon completion of their review. In addition, non-U.S. tax authorities have completed their examination of our subsidiary in India for fiscal years 2005-2007. As of April 3, 2011, the proposed adjustments have been appealed. We believe the ultimate outcome of these appeals will not result in a material adjustment to our tax liability.

While our U.S. federal income tax returns for years prior to 2006 are not open for assessment, the IRS can adjust net operating loss and research and development credit carryovers that were generated in prior years and carried forward to 2006 and subsequent years.

Spin-Off of SunPower

We have a tax sharing agreement with SunPower providing for each of the parties’ obligations concerning various tax liabilities. The tax sharing agreement is structured such that we will pay all federal, state, local and foreign taxes that are calculated on a consolidated or combined basis (as defined under applicable federal, state or foreign law) reduced by SunPower’s portion of such tax liability or benefit determined based upon its separate return tax liability as defined under the tax sharing agreement. Such liability or benefit will be based on a pro forma calculation as if SunPower were filing a separate income tax return in each jurisdiction, rather than on a combined or consolidated basis with us subject to adjustments as set forth in the tax sharing agreement.

In connection with the Spin-Off, Cypress and SunPower entered into an amendment to the existing tax sharing agreement between the parties to address certain transactions that may affect the tax treatment of the Spin-Off and certain other matters. Under the amended tax sharing agreement, SunPower agreed that it will not: (a) effect a Recapitalization during the 36 month period following the Spin-Off without first obtaining a tax opinion to the effect that such Recapitalization (either alone or when taken together with any other transaction or transactions) will not cause the Spin-Off to become taxable under Section 355(e), or (b) seek

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any private ruling, including any supplemental private ruling, from the IRS with regard to the Spin-Off, or any transaction having any bearing on the tax treatment of the Spin-Off, without our prior written consent.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

NOTE 14. NET INCOME PER SHARE

The following table sets forth the computation of basic and diluted net income per share:

	Three Months Ended	
	April 3, 2011	April 4, 2010
	(In thousands, except per-share amounts)	
Net income attributable to Cypress	\$ 55,374	\$ 12,674
Weighted-average common shares	171,346	158,931
Weighted-average diluted shares	199,943	190,892
Net income per share—basic	\$ 0.32	\$ 0.08
Net income per share—diluted	\$ 0.28	\$ 0.07

Anti-dilutive securities excluded from the diluted computation for the three months ended April 3, 2011 and April 4, 2010 were approximately 1.4 million and 1.1 million, respectively, from stock options, restricted stock units and restricted stock awards.

NOTE 15. SEGMENT, GEOGRAPHICAL AND CUSTOMER INFORMATION***Segment Information***

The following tables set forth certain information relating to our reportable business segments:

Revenues:

	Three Months Ended	
	April 3, 2011	April 4, 2010
	(In thousands)	
Consumer and Computation Division	\$107,768	\$ 74,163
Data Communications Division	27,446	26,959
Memory Products Division	91,837	98,556
Emerging Technologies and Other	6,059	2,593
Total revenues	<u>\$233,110</u>	<u>\$202,271</u>

Income from Continuing Operations before Income Taxes:

	Three Months Ended	
	April 3, 2011	April 4, 2010
	(In thousands)	
Consumer and Computation Division	\$ 16,424	\$ 4,181
Data Communications Division	8,473	8,654
Memory Products Division	31,400	30,879
Emerging Technologies and Other	(6,902)	(6,031)
Unallocated items:		
Amortization of acquisition-related intangibles	(698)	(776)
Restructuring charges	(734)	(327)
Stock-based compensation	(20,837)	(21,574)
Gain on divestiture	34,291	—
Charitable donation of building	(4,125)	—
Other	(568)	(222)
Income before income taxes	<u>\$ 56,724</u>	<u>\$ 14,784</u>

CYPRESS SEMICONDUCTOR CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Geographical Information

The following table presents our revenues by geographical locations:

	Three Months Ended	
	April 3, 2011	April 4, 2010
	(In thousands)	
United States	\$ 31,121	\$ 33,404
Europe	35,420	29,225
Asia:		
China	55,410	42,610
Hong Kong	23,976	16,724
Rest of World	87,183	80,308
Total revenues	<u>\$233,110</u>	<u>\$202,271</u>

Customer Information

For the three months ended April 3, 2011, two global distributors accounted for 23% of our total revenues and no one end customer accounted for more than 10% of our total revenues. For the three months ended April 4, 2010, one global distributor accounted for 15% of our total revenues and no end customer accounted for more than 10% of our total revenues.

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

The Management's Discussion and Analysis of Financial Condition and Results of Operations in this Quarterly Report of Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, that involve risks and uncertainties, which are discussed in the "Forward-Looking Statements" section under Part I of this Quarterly Report on Form 10-Q.

EXECUTIVE SUMMARY

General

Cypress Semiconductor Corporation ("Cypress") delivers high-performance, mixed-signal, programmable solutions that provide customers with rapid time-to-market and exceptional system value. Our offerings include the flagship Programmable System-on-Chip ("PSoC®") families and derivatives such as PowerPSoC® solutions for high-voltage and LED lighting applications, CapSense® touch sensing and TrueTouch™ solutions for touchscreens. We are the world leader in universal serial bus ("USB") controllers, including the high-performance West Bridge® solution that enhances connectivity and performance in multimedia handsets. We are also a leader in high-performance memories and programmable timing devices. We serve numerous markets including consumer, mobile handsets, computation, data communications, automotive, industrial and military.

As of the end of the first quarter of fiscal 2011, our organization included the following business segments:

Business Segments	Description
Consumer and Computation Division	A product division focusing on PSoC, touch-sensing and touchscreen solutions, USB and timing solutions.
Data Communications Division	A product division focusing on data communication devices for wireless handset and professional video systems.
Memory Products Division	A product division focusing on static random access memories and nonvolatile memories.
Emerging Technologies and Other	Includes Cypress EnviroSystems and AgigA Tech, Inc., both majority-owned subsidiaries of Cypress, the Optical Navigation Systems ("ONS") business unit, China business unit, foundry-related services, other development stage companies and certain corporate expenses.

Sale of Image Sensors Product Family

As part of Cypress's continued efforts to focus on programmable products including our flagship PSoC® programmable system-on-chip solution and our TrueTouch™ touch-sensing controllers, we divested our image sensors product family by selling it to ON Semiconductor Corporation on February 27, 2011. The name of our Memory and Image Sensor Division was changed to Memory Products Division, ("MPD") to reflect the change in our business.

Manufacturing Strategy

Our core manufacturing strategy—"flexible manufacturing"—combines capacity from foundries with output from our internal manufacturing facilities. This initiative is intended to allow us to meet rapid swings in customer demand while lessening the burden of high fixed costs, a capability that is particularly important in high-volume consumer markets that we serve with our leading programmable product portfolio.

We currently manufacture approximately 50 %to 60% of our semiconductor products at our wafer manufacturing facility in Bloomington, Minnesota. External wafer foundries, mainly in Asia, manufactured the balance of our products.

We conduct assembly and test operations at our highly automated assembly and test facility in the Philippines. This facility accounts for approximately 55% to 60% of the total assembly output and 65% - 75% of the total test output. Various subcontractors in Asia performed the balance of the assembly and test operations.

Our facility in the Philippines performs assembly and test operations manufacturing volume products and packages where our ability to leverage manufacturing costs is high. This facility has nine fully integrated, automated manufacturing lines enabling complete assembly and test operations with minimal human intervention. These autolines have shorter manufacturing cycle times than conventional assembly/test operations, which enable us to respond more rapidly to changes in demand.

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Results of Operations

Revenues

The following table summarizes our consolidated revenues by segments:

	Three Months Ended	
	April 3, 2011	April 4, 2010
	(In thousands)	
Consumer and Computation Division	\$107,768	\$ 74,163
Data Communications Division	27,446	26,959
Memory Products Division	91,837	98,556
Emerging Technologies and Other	6,059	2,593
Total revenues	<u>\$233,110</u>	<u>\$202,271</u>

Consumer and Computation Division:

Revenues from the Consumer and Computation Division increased by \$33.6 million in the first quarter of fiscal 2011, or approximately 45.3%, compared to the same prior-year period. The increase was primarily attributable to an increase in sales of our PSOC family of products mainly due to higher demand in our capacitive and touchscreen applications in mobile devices. Our PSOC product families, including our touchscreen family, continued to gain new design wins, expanded our customer base and increase market penetration in a variety of end-market applications.

Data Communications Division:

Revenues from the Data Communications Division increased by \$0.5 million in the first quarter of fiscal 2011 or approximately 1.8%, compared to the same prior-year period. The revenue increase was primarily attributable to increases in sales of our West Bridge controllers and other products offset by a decrease in sales of our communications products.

Memory Products Division:

Revenues from the Memory Products Division decreased by \$6.7 million in the first quarter of fiscal 2011 or approximately 6.8%, compared to the same prior-year period. The revenue decrease was primarily attributable to a decrease in sales of our SRAM products driven by decreased demand from wireless and wireline end customers. This amount was partially offset by an increase in sales by our Image sensors product family.

Emerging Technologies and Other:

Revenues from Emerging Technologies and Other increased by \$3.5 million in the first quarter of fiscal 2011 or approximately 133.7%, compared to the same prior-year period. The revenue increase was primarily attributable to an overall increase in demand as certain of the Emerging Technologies divisions are beginning initial production ramps.

[Table of Contents](#)**Cost of Revenues/Gross Margins**

	Three Months Ended	
	April 3, 2011	April 4, 2010
	(In thousands)	
Cost of revenues	\$104,334	\$95,784
Gross margin	55.2%	52.6%

Gross margin percentage increased to 55.2% in the first quarter of fiscal 2011 from 52.6% in the first quarter of fiscal 2010. The significant gross margin increase was primarily due to favorable product mix and increased factory utilization resulting from increased production when compared to the same prior-year periods.

Research and Development (“R&D”) Expenses

	Three Months Ended	
	April 3, 2011	April 4, 2010
	(In thousands, except percentages)	
R&D expenses	\$ 47,865	\$ 40,049
As a percentage of revenues	20.5%	19.8%

R&D expenditures increased by \$7.8 million in the first quarter of fiscal 2011 compared to the same prior-year period. The increase was primarily attributable to an increase of \$1.8 million in employee-related costs due to an increase in personnel in our Emerging Technologies divisions, and a \$1.7 million increase in certain bonus programs which paid out at higher levels when compared to the prior-year period. In addition, stock-based compensation increased \$1.1 million in the first quarter of fiscal 2011 which was driven by the higher fair value of stock option and restricted stock units granted subsequent to the first quarter of fiscal 2010.

Selling, General and Administrative (“SG&A”) Expenses

	Three Months Ended	
	April 3, 2011	April 4, 2010
	(In thousands, except percentages)	
SG&A expenses	\$ 58,652	\$ 51,281
As a percentage of revenues	25.2%	25.4%

SG&A expenses increased by \$7.4 million in the first quarter of fiscal 2011 compared to the same prior-year period. The increase was primarily attributable to a \$4.1 million donation of a building to a charitable organization, and higher payroll taxes of \$0.7 million related to an increase in stock option exercises and higher stock price for the performance based awards delivered in the first quarter of fiscal 2011. In addition, we had an increase in legal expense of \$1.4 million due to litigation matters, and an increase of \$1.2 million related to our annual sales conference in 2011 which did not take place in 2010. These amounts were partially offset by a reduction of \$2.4 million in stock-based compensation expense and the sale of patents totaling \$1.4 million.

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Amortization of Acquisition-Related Intangible Assets

For the three months ended April 3, 2011, amortization decreased by approximately \$0.1 million as compared to the same prior year period. The decrease in amortization was primarily due to certain intangible assets that had been fully amortized during fiscal 2010.

Restructuring

For the three months ended April 3, 2011 and April 4, 2010, we recorded restructuring charges of \$0.7 million and \$0.3 million, respectively. The determination of when we accrue for severance and benefits costs, and which accounting standard applies, depends on whether the termination benefits are provided under a one-time benefit arrangement or under an on-going benefit arrangement.

Fiscal 2010 Restructuring Plan

During the third quarter of fiscal 2010, we implemented a restructuring plan to exit certain of our back-end manufacturing operations located in the Philippines ("Fiscal 2010 Restructuring Plan"). These actions are intended to reduce the cost of our back-end manufacturing by selling our labor intensive assembly and test operations to lower cost third-party subcontractors in Asia and by the continued shifting of these operations to our fully automated back-end processes.

As of April 3, 2011, we recorded total restructuring charges of \$2.7 million under the Fiscal 2010 Restructuring Plan, which was all related to personnel costs. As of April 3, 2011, our restructuring provision of \$2.4 million was related to severance and benefits of our employees. We expect to eliminate approximately 300 manufacturing employees and 200 contractors or approximately 34% of our Philippines plant workforce by the end of fiscal 2011. Upon completion of all of our actions, we anticipate our annual savings impacting cost of goods sold after fiscal 2011 to be approximately \$1.0 million, although there can be no assurance of this.

Fiscal 2008/9 Restructuring Plan

In fiscal 2008, we initiated a restructuring plan as part of a company-wide cost saving initiative which continued into 2010 aimed to reduce operating costs in response to the economic downturn ("Fiscal 2008/9 Restructuring Plan").

Restructuring activities related to personnel costs are summarized as follows:

<u>(In thousands)</u>	
Balance as of January 2, 2011	\$1,106
Provision	322
Non cash	257
Cash payments	(373)
Balance as of April 3, 2011	<u>\$1,312</u>

As a result of the 2008/9 Restructuring Plan, we eliminated approximately 835 positions. In the fourth quarter of 2010, we completed the majority of the remaining actions we had for this plan.

During fiscal 2010, our annual savings from our actions taken was approximately \$70.0 million and proportionately impacted cost of goods sold by 50%, research and development expense by 25% and sales, general and administrative expense by 25%.

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Fiscal 2007 Restructuring Plan

During fiscal 2007, we implemented a restructuring plan to exit our manufacturing facility located in Round Rock, Texas (“Fiscal 2007 Restructuring Plan”). The Fiscal 2007 Restructuring Plan included the termination of employees and the planned disposal of assets, primarily consisting of land, building and manufacturing equipment, located in the Texas facility.

The actions related to the 2007 Restructuring Plan were substantially completed in fiscal 2009. In the second quarter of 2010, we recorded a \$2.4 million gain on the sale of certain equipment in our Texas facility. On a quarterly basis we continue to incur expenses related to ongoing maintenance and upkeep of the Texas facility until we complete the sale of the property.

Assets Held For Sale:

The Texas facility ceased operations in the fourth quarter of fiscal 2008. As our management has committed to a plan to sell the assets associated with the facility, we have classified the assets as held for sale and recorded the assets at the lower of their carrying amount or estimated fair value less cost to sell. Fair value was determined by an analysis of market prices for similar assets. In the second quarter of fiscal 2010, we recorded a \$1.5 million write-down to the estimated fair value related to these assets.

The net book value of the remaining restructured assets that were classified as held for sale and included in “Other current assets” in the Condensed Consolidated Balance Sheets was \$6.9 million as of April 3, 2011 and January 2, 2011.

We had expected to complete the disposal of the restructured assets by the fourth quarter of fiscal 2009; however, due to the downturn and uncertainty in the commercial real estate market we were unable to secure a buyer for the Texas facility. In response, during fiscal 2010 we revised the asking price for the property and expect to sell the facility within the next twelve months; however, there can be no assurance of this and our ability to complete the sale of any restructured assets may be impacted by the current economic and credit conditions.

Interest and Other Income, Net

The following table summarizes the components of interest and other income, net:

	<u>Three Months Ended</u>	
	<u>April 3, 2011</u>	<u>April 4, 2010</u>
	<u>(In thousands)</u>	
Interest income	\$ 487	\$ 589
Foreign currency exchange gain (loss), net	(462)	(471)
Changes in fair value of investment under the employee deferred compensation plan	1,474	835
Gain on sale of marketable equity investments	(71)	—
Other	178	(223)
Total interest and other income, net	<u>\$ 1,606</u>	<u>\$ 730</u>

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Employee Deferred Compensation Plan

We have a deferred compensation plan, which provides certain key employees, including our executive management, with the ability to defer the receipt of compensation in order to accumulate funds for retirements on a tax-free basis. We do not make contributions to the deferred compensation plan and we do not guarantee returns on the investments. Participant deferrals and investment gains and losses remain as our liabilities and the underlying assets are subject to claims of general creditors.

The increase in the fair value of the investments relates to the increased performance of the portfolio on a year over year basis.

Income Taxes

Our income tax expense was \$1.4 million for the three months ended April 3, 2011 and income tax expense was \$2.1 million for the three months ended April 4, 2010. The tax provision for the first quarter of fiscal 2011 and fiscal 2010 was primarily attributable to income taxes associated with our non-U.S. operations

LIQUIDITY AND CAPITAL RESOURCES

The following table summarizes information regarding our cash and investments and working capital:

(In thousands)	As of	
	April 3, 2011	January 2, 2011
Cash, cash equivalents and short-term investments	\$260,919	\$434,261
Working capital	\$244,725	\$383,369

Key Components of Cash Flows

(In thousands)	Three Months Ended	
	April 3, 2011	April 4, 2010
Net cash provided by operating activities	\$ 35,343	\$ 38,123
Net cash provided by (used in) investing activities	\$ 30,711	\$(43,757)
Net cash used in financing activities	\$(209,639)	\$(20,883)

During the three months ended April 3, 2011, net cash provided by operating activities was \$35.3 million compared to net cash provided by operating activities of \$38.1 million for the prior period. Operating cash flows for the three months ended April 3, 2011 were primarily driven by net income adjusted for certain non-cash items including depreciation and amortization, stock-based compensation and partially offset by the gain on the divestiture of Image Sensors product family. The changes in our working capital as of April 3, 2011 compared to January 2, 2011 were as follows:

- Accounts receivable increased by \$55.7 million due to higher distributor shipments.
- Deferred revenues less cost of revenues increased by \$46.4 million due to higher distributor shipments.
- Accounts payable increased by \$4.7 million due to timing of purchases and payments.

During the three months ended April 3, 2011, net cash provided by investing activities was \$30.7 million compared to net cash used in investing activities of \$43.8 million for the three months ended April 4, 2010. For the three months ended April 3, 2011, our investing activities primarily included the net proceeds of \$34.9 million from the sales and maturities of investments offset by purchases of investments and the receipt of \$14.9 million from our divestiture of image sensor business unit offset by expenditures of \$19.3 million for property and equipment,

During the three months ended April 3, 2011, net cash used in financing activities was \$209.6 million compared to net cash used in financing activities of \$20.9 million for the three months ended April 4, 2010. For the three months ended April 3, 2011, we used a net \$116.4 million on our yield enhancement program and used \$117.1 million to repurchase our common shares and for the withholding of common shares for the tax obligations as our employees restricted shares vested. This was offset by the proceeds of \$23.9 million from the issuance of common shares under our employee stock plans.

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Liquidity and Contractual Obligations

Auction Rate Securities:

As of April 3, 2011, all of our auction rate securities have experienced failed auctions due to sell orders exceeding buy orders. Currently, these failures are not believed to be a credit issue with the underlying investments, but rather caused by a lack of liquidity. We have classified our auction rate securities totaling \$19.1 million as long-term investments as of April 3, 2011.

During the first quarter of fiscal 2011, we performed analyses to assess the fair value of the auction rate securities. In the absence of a liquid market to value these securities, we prepared a valuation model based on discounted cash flows. Based on the discounted cash flows, we estimated that the value of our auction rate securities is approximately 91% of their stated par value as of April 3, 2011.

Yield Enhancement Program:

On March 1, 2011 we entered into a short-term yield enhanced structured agreement with a maturity of less than 45 days at an aggregate price of approximately \$57.6 million. On April 18, 2011, we settled this agreement and received 3 million shares of our common stock at an average price of \$19.19 per share.

On March 9, 2011 we entered into a short-term yield enhanced structured agreement with a maturity of less than 45 days at an aggregate price of approximately \$53.3 million. On April 20, 2011, we settled this agreement and received 1 million shares of our common stock at an aggregate price of \$17.8 million with an average price of \$17.77 per share. In addition, we received net cash proceeds of \$0.9 million upon maturity.

Purchase Obligations:

We have outstanding purchase obligations, which primarily include non-cancelable purchase orders for materials, services, manufacturing equipment, building improvements and supplies in the ordinary course of business. Purchase obligations are defined as enforceable agreements that are legally binding on us and that specify all significant terms, including quantity, price and timing. As of April 3, 2011, non-cancelable purchase obligations totaled approximately \$51.0 million.

Capital Resources and Financial Condition

Our long-term strategy is to maintain a minimum amount of cash and cash equivalents for operational purposes and to invest the remaining amount of our cash in interest-bearing and highly liquid cash equivalents, debt securities and the purchase of our stock through our stock buyback program. As of April 3, 2011, in addition to \$119.6 million in cash and cash equivalents, we had \$141.3 million invested in short-term investments for a total cash and short-term investment position of \$260.9 million that is available for use in our current operations. In addition, we had \$19.1 million of long-term investments primarily consisting of auction rate securities.

As of April 3, 2011, approximately 13% our cash and cash equivalents are offshore funds. While these amounts are primarily invested in U.S. dollars, a portion is held in foreign currencies. All offshore balances are exposed to local political, banking, currency control and other risks. In addition, these amounts, if repatriated may be subject to tax and other transfer restrictions. We believe that liquidity provided by existing cash, cash equivalents and investments and our borrowing arrangements will provide sufficient capital to meet our requirements for at least the next twelve months. However, should prevailing economic conditions and/or financial, business and other factors beyond our control adversely affect the estimates of our future cash requirements, we could be required to fund our cash requirements by alternative financing. There can be no assurance that additional financing, if needed, would be available on terms acceptable to us or at all. We may choose at any time to raise additional capital or debt to strengthen our financial position, facilitate growth, enter into strategic initiatives including the acquisition of other companies and provide us with additional flexibility to take advantage of other business opportunities that arise.

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Non-GAAP Financial Measures

Regulation G, conditions for use of Non-Generally Accepted Accounting Principles (“Non-GAAP”) financial measures, and other SEC regulations define and prescribe the conditions for use of certain Non-GAAP financial information. To supplement our condensed consolidated financial results presented in accordance with GAAP, we use Non-GAAP financial measures which are adjusted from the most directly comparable GAAP financial measures to exclude certain items, as described below. Management believes that these Non-GAAP financial measures reflect an additional and useful way of viewing aspects of our operations that, when viewed in conjunction with our GAAP results, provide a more comprehensive understanding of the various factors and trends affecting our business and operations. Non-GAAP financial measures used by us include gross margin, research and development expenses, selling, general and administrative expenses, operating income or loss, net income or loss and basic and diluted net income or loss per share.

Our Non-GAAP measures primarily exclude stock-based compensation, acquisition-related charges, impairments to goodwill, gain or losses on divestiture, investment-related gains and losses, discontinued operations, restructuring costs and other special charges and credits. Management believes these Non-GAAP financial measures provide meaningful supplemental information regarding our strategic and business decision making, internal budgeting, forecasting and resource allocation processes. In addition, these Non-GAAP financial measures facilitate management’s internal comparisons to our historical operating results and comparisons to competitors’ operating results.

We use each of these Non-GAAP financial measures for internal managerial purposes, when providing our financial results and business outlook to the public, to facilitate period-to-period comparisons and are used to formulate our formula driven cash bonus plan and any milestone based stock awards. Management believes that these Non-GAAP measures provide meaningful supplemental information regarding our operational and financial performance of current and historical results. Management uses these Non-GAAP measures for strategic and business decision making, internal budgeting, forecasting and resource allocation processes. In addition, these Non-GAAP financial measures facilitate management’s internal comparisons to our historical operating results and comparisons to competitors’ operating results.

The following table shows our Non-GAAP financial measures:

	Three Months Ended	
	April 3, 2011	April 4, 2010
	(In thousands, except per share amounts)	
Non-GAAP gross margin	\$135,427	\$112,599
Non-GAAP research and development expenses	\$ 41,883	\$ 35,400
Non-GAAP selling, general and administrative expenses	\$ 44,750	\$ 39,432
Non-GAAP operating income	\$ 48,795	\$ 37,766
Non-GAAP net income attributable to Cypress	\$ 48,483	\$ 34,256
Non-GAAP net income per share attributable to Cypress—diluted	\$ 0.24	\$ 0.17

We believe that providing these Non-GAAP financial measures, in addition to the GAAP financial results, are useful to investors because they allow investors to see our results “through the eyes” of management as these Non-GAAP financial measures reflect our internal measurement processes. Management believes that these Non-GAAP financial measures enable investors to better assess changes in each key element of our operating results across different reporting periods on a consistent basis and provides investors with another method for assessing our operating results in a manner that is focused on the performance of our ongoing operations.

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The following is a reconciliation of Non-GAAP measures to GAAP measures:

CYPRESS SEMICONDUCTOR CORPORATION
RECONCILIATION OF GAAP FINANCIAL MEASURES TO NON-GAAP FINANCIAL MEASURES
(In thousands, except per-share data)
(Unaudited)

	Three Months Ended	
	April 3, 2011	April 4, 2010
GAAP gross margin	\$128,776	\$106,487
Stock-based compensation expense	6,510	5,970
Changes in value of deferred compensation plan	204	142
Impairment of assets	(63)	—
Non-GAAP gross margin	<u>\$135,427</u>	<u>\$112,599</u>
GAAP research and development expenses	\$ 47,865	\$ 40,049
Stock-based compensation expense	(5,473)	(4,357)
Other acquisition-related expense	—	(2)
Changes in value of deferred compensation plan	(509)	(290)
Non-GAAP research and development expenses	<u>\$ 41,883</u>	<u>\$ 35,400</u>
GAAP selling, general and administrative expenses	\$ 58,652	\$ 51,281
Stock-based compensation expense	(8,854)	(11,247)
Other acquisition-related expense	—	(6)
Changes in value of deferred compensation plan	(923)	(596)
Building donation	(4,125)	—
Non-GAAP selling, general and administrative expenses	<u>\$ 44,750</u>	<u>\$ 39,432</u>
GAAP operating income	\$ 55,118	\$ 14,054
Stock-based compensation expense	20,837	21,574
Gain on divestiture	(34,291)	—
Other acquisition-related expense	698	784
Changes in value of deferred compensation plan	1,636	1,027
Restructuring charges	734	327
Building donation	4,125	—
Impairment of assets and other	(62)	—
Non-GAAP operating income	<u>\$ 48,795</u>	<u>\$ 37,766</u>
GAAP net income attributable to Cypress	\$ 55,374	\$ 12,674
Stock-based compensation expense	20,837	21,574
Gain on divestiture	(34,291)	—
Other acquisition-related expense	698	784
Changes in value of deferred compensation plan	162	192
Restructuring charges	734	327
Investment-related gains/losses	71	—
Building donation	4,125	—
Impairment of assets and other	(62)	—
Tax effects	835	(1,295)
Non-GAAP net income attributable to Cypress	<u>\$ 48,483</u>	<u>\$ 34,256</u>
GAAP net income per share attributable to Cypress - diluted	\$ 0.28	\$ 0.07
Stock-based compensation expense and other	0.10	0.11
Gain on divestiture	(0.17)	—
Building donation	0.02	—
Other acquisition-related expense	0.01	—
Tax effects	—	(0.01)
Non-GAAP net income per share attributable to Cypress - diluted	<u>\$ 0.24</u>	<u>\$ 0.17</u>

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate Risks

Our investment portfolio consists of a variety of financial instruments that exposes us to interest rate risk, including, but not limited to, money market funds, commercial paper and corporate securities. These investments are generally classified as available-for-sale and, consequently, are recorded on our balance sheets at fair market value with their related unrealized gain or loss reflected as a component of accumulated other comprehensive income in stockholders' equity. Due to the relatively short-term nature of our investment portfolio, we do not believe that an immediate 10% increase in interest rates would have a material effect on the fair market value of our portfolio. Since we believe we have the ability to liquidate this portfolio, we do not expect our operating results or cash flows to be materially affected to any significant degree by a sudden change in market interest rates on our investment portfolio.

Auction Rate Securities

As of April 3, 2011, all our auction rate securities are classified as Level 3 financial instruments. Auction rate securities are investments with contractual maturities generally between 20 and 30 years. The auction rate securities held by us are backed by student loans originated under the Federal Family Education Loan Program (FFELP), which are guaranteed by the U.S. Federal Department of Education.

As of April 3, 2011, all of our auction rate securities held by us were rated as either AAA or Aaa by the major independent rating agencies and all of our auction rate securities have experienced failed auctions due to sell orders exceeding buy orders. These failures are not believed to be a credit issue with the underlying investments, but rather caused by a lack of liquidity. Under the contractual terms, the issuer is obligated to pay penalty rates should an auction fail. The funds associated with failed auctions are not expected to be accessible until one of the following occurs: a successful auction occurs, the issuer redeems the issue, a buyer is found outside of the auction process or the underlying securities have matured. Given these circumstances and the lack of liquidity, we have classified our auction rate securities totaling \$19.1 million as long-term investments as of April 3, 2011. If the financial market continues to deteriorate, future downgrades could potentially impact the rating of our auction rate securities.

During fiscal 2011, we performed analyses to assess the fair value of the auction rate securities. In the absence of a liquid market to value these securities, we prepared a valuation model based on discounted cash flows. The assumptions used at April 3, 2011 were as follows:

- 7 years to liquidity;
- continued receipt of contractual interest which provides a premium spread for failed auctions; and
- discount rates of 1.86%—5.52%, which incorporates a spread for both credit and liquidity risk.

Based on these assumptions, we estimated that the auction rate securities would be valued at approximately 91% of their stated par value as of April 3, 2011, representing a decline in value of approximately \$2.0 million.

As a result of our adoption of the amended other-than-temporary impairment guidance on debt securities in the second quarter of fiscal 2009, we reclassified the non-credit portion of the previously recognized other-than-temporary impairment losses related to our auction rate securities of \$5.3 million from accumulated deficit to accumulated other comprehensive loss.

The following table summarizes certain information related to our auction rate securities as of April 3, 2011:

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	<u>Fair Value</u>	<u>Fair Value Given a 100 Basis Point Increase in Interest Rates</u> (In thousands)	<u>Fair Value Given a 100 Basis Point Decrease in Interest Rates</u>
Auction rate securities	\$ 19,094	\$ 21,003	\$ 17,185

Investments in Publicly Traded and Privately Held Companies

We have equity investments in certain publicly traded companies. The marketable equity securities are classified as available-for-sale investments and are recorded at fair value with unrealized gain (loss) reported as a component in "Accumulated other comprehensive loss" in the Condensed Consolidated Balance Sheets. The fair value of the common stock is subject to market price volatility. The following table summarizes certain information related to these investments as of April 3, 2011:

<u>Investments</u>	<u>Fair Value</u>	<u>Fair Value Given a 10% Increase in Stock Prices</u> (In thousands)	<u>Fair Value Given a 10% Decrease in Stock Prices</u>
Marketable equity securities	\$ 2,236	\$ 2,460	\$ 2,012

We also have equity investments in several privately held companies, many of which are start-ups or in development stages. These investments are inherently risky as the market for the technologies or products they have under development are typically in the early stages and may never materialize. As our equity investments generally do not permit us to exert significant influence or control, these amounts generally represent our cost of the investments, less any adjustments we make when we determine that an investment's net realizable value is less than its carrying cost. As of April 3, 2011, the carrying value of our investments in privately held companies was \$2.0 million.

Foreign Currency Exchange Risk

We operate and sell products in various global markets and purchase capital equipment using foreign currencies but predominantly the U.S. dollar. As a result, we are exposed to risks associated with changes in foreign currency exchange rates. Changes in exchange rates between foreign currencies and the U.S. dollar may adversely affect our operating margins. For example, when foreign currencies appreciate against the U.S. dollar, inventory and expenses denominated in foreign currencies become more expensive. An increase in the value of the U.S. dollar relative to foreign currencies could make our products more expensive for international customers, thus potentially leading to a reduction in demand, and therefore in our sales and profitability. Furthermore, many of our competitors are foreign companies that could benefit from such a currency fluctuation, making it more difficult for us to compete with those companies. We cannot predict the impact of future exchange rate fluctuations on our business and results of operations.

We analyzed our foreign currency exposure, including our hedging strategies, to identify assets and liabilities denominated in other currencies. For those assets and liabilities, we evaluated the effects of a 10% shift in exchange rates between those currencies and the U.S. dollar. We have determined that there would be an immaterial effect on our results of operations from such a shift.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain “disclosure controls and procedures,” as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), that are designed to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating our disclosure controls and procedures, management recognized that disclosure controls and procedures, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the disclosure controls and procedures are met. Additionally, in designing disclosure controls and procedures, our management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible disclosure controls and procedures. The design of any disclosure controls and procedures also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

Based on their evaluation as of the end of the period covered by this Quarterly Report on Form 10-Q and subject to the foregoing, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were effective at the reasonable assurance level.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting that occurred during the three month period ended April 3, 2011 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II—OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The information required by this item is included in Note 10 of Notes to Condensed Consolidated Financial Statements under Item 1, Part 1 of this Quarterly Report on Form 10-Q and is incorporated herein by reference.

ITEM 1A. RISK FACTORS

With the exception of the update to the risk factors set forth in this Quarterly Report on Form 10-Q, there have been no material changes to the risk factors set forth in our Annual Report on Form 10-K for the year ended January 2, 2011.

We are increasingly dependent upon third-parties to manufacture, distribute, generate a significant portion of our sales, fulfill our customer orders and transport our product. Problems in the performance or availability of these companies could seriously harm our financial performance.

Although a majority of our products were fabricated in our manufacturing facilities located in Minnesota and the Philippines, we rely to a significant extent on independent contractors to manufacture our products. We expect to increase this reliance on third-party manufacturing in the future. For example, in December 2008, we substantially completed the exit of our manufacturing facility in Texas and transferred certain production to our more cost-competitive facility in Minnesota and outside foundries. In addition, if market demand for our products exceeds our internal manufacturing capacity and available capacity from our foundry partners, we may seek additional foundry manufacturing arrangements.

A shortage in foundry manufacturing capacity, which is more likely to occur at times of increasing demand, could hinder our ability to meet demand for our products and therefore adversely affect our operating results. In addition, greater demand for wafers produced by any such foundries without an offsetting increase in foundry capacity raises the likelihood of potential wafer price increases. Our operations would be disrupted if any of our foundry partners terminates its relationship with us or has financial issues and we are unable to arrange a satisfactory alternative to fulfill customer orders on a timely basis and in a cost-effective manner. However, there are only a few foundry vendors that have the capabilities to manufacture our most advanced products. If we engage alternative sources of supply, we may encounter start-up difficulties and incur additional costs. Also, shipments could be delayed significantly while these sources are qualified for volume production. The recent earthquake and tsunami in Japan and the aftermath have created significant economic uncertainty in that country. While we do not have significant operations in Japan, certain of our raw materials are sourced there. Based on a review of our extended semiconductor supply chain, we do not foresee any significant impact in the near term on our ability to supply product to our customers due to the events in Japan. We will continue to monitor the rapidly developing situation in Japan and its potential impact on our business.

While a high percentage of our products are assembled, packaged and tested at our manufacturing facility located in the Philippines, we rely on independent subcontractors to assemble, package and test the balance of our products. We cannot be certain that these subcontractors will continue to assemble, package and test products for us on acceptable economic and quality terms or at all and it might be difficult for us to find alternatives if they do not do so.

Our channel partners include distributors and resellers. We continue to expand and change our relationships with our distributors and see an increase in the proportion of our revenues generated from our distributor channel in the future. Worldwide sales through our distributors accounted for approximately 70% of our net sales in Q1, 2011. We rely on many distributors to assist us in creating customer demand, providing technical support and other value-added services to our customers, filling customer orders and stocking our products. We face ongoing business risks due to our reliance on our channel partners to create and maintain customer relationships where we have a limited or no direct relationship. Should our relationships with our channel partners or their effectiveness decline, we face the risk of declining demand which could affect our results of operations. Our contracts with our distributor may be terminated by either party upon notice. In addition, our distributors are located all over the world and are of various sizes and financial conditions. Any disruptions to our distributors' operations such as lower sales, lower earnings, debt downgrades, the inability to access capital markets and higher interest rates could have an adverse impact on our business.

We also rely on independent carriers and freight haulers to move our products between manufacturing plants and our customers' facilities. Transport or delivery problems due to their error or because of unforeseen interruptions in their business due to factors such as strikes, political instability, terrorism, natural disasters or accidents could seriously harm our business, financial condition and results of operations and ultimately impact our relationship with our customers.

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Claims by other companies that we infringe their intellectual property or that patents on which we rely are invalid could adversely affect our business.

We are also from time to time involved in litigation relating to alleged infringement by us of others' patents or other intellectual property rights. Moreover, a key element of our strategy is to enter new markets with our products. If we are successful in entering these new markets, we will likely be subject to additional risks of potential infringement claims against us as our technologies are deployed in new applications and face new competitors. We may be unable to detect the unauthorized use of, or take appropriate steps to enforce, our intellectual property rights, particularly in certain international markets, making misappropriation of our intellectual property more likely. Companies have asserted, and may again assert, patent, copyright and other intellectual property rights against our products or products using our technologies or other technologies used in our industry. We expect that we may continue to be involved in litigation and may have to appear in front of administrative bodies (such as the U.S. International Trade Commission) to defend against patent assertions against our products by companies, some of whom are attempting to gain competitive advantage or leverage in licensing negotiations. For example, we are a defendant in an alleged patent infringement case filed Avago Technologies, a competitor of the Company, and we are a plaintiff in a patent infringement case filed against GSI Technology.

We may not prevail in such litigation given the complex technical issues and inherent uncertainties in intellectual property litigation. If any of our products were found to infringe on another company's intellectual property rights, we could be subject to an injunction or required to redesign our products, which could be costly, or to license such rights and/or pay damages or other compensation to such other company. If we were unable to redesign our products, license such intellectual property rights used in our products or otherwise distribute our products through a licensed supplier, we could be prohibited from making and selling such products. In any potential dispute involving other companies' patents or other intellectual property, our customers could also become the targets of litigation. We may also be contingently liable under certain product sales, services, license and other agreements to indemnify certain customers against certain types of liability and/or damages arising from qualifying claims of patent infringement by products or services sold or provided by us. Reimbursements under indemnification arrangements we may agree to could have a material adverse effect on our results of operations. Any claims, regardless of their merit, could be time consuming to address, result in costly litigation, divert the efforts of our technical and management personnel or cause product release or shipment delays, any of which could have a material adverse effect upon our market share, revenue and/or operating results.

Other companies or entities also have commenced, and may again commence, actions seeking to establish the invalidity of our patents. In the event that one or more of our patents are challenged, a court may invalidate the patent(s) or determine that the patent(s) is not enforceable, which could harm our competitive position. If our key patents are invalidated, or if the scope of the claims in any of these patents is limited by court decision, we could be prevented from licensing the invalidated or limited portion of such patents. Such adverse decisions could negatively impact our revenues. Even if such a patent challenge is not successful, it could be expensive and time consuming to address, divert management attention from our business and harm our reputation.

We believe we have meritorious defenses to each of these matters and we intend to vigorously defend ourselves. Unfortunately, such litigation and other claims are subject to inherent uncertainties.

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We compete with others to attract and retain key personnel, and any loss of, or inability to attract, such personnel would harm us.

To a greater degree than most non-technology companies, we depend on the efforts and abilities of certain key members of management and other technical personnel. Our future success depends, in part, upon our ability to retain such personnel and to attract and retain other highly qualified personnel, particularly product and process engineers. We compete for these individuals with other companies, academic institutions, government entities and other organizations. Competition for such personnel is intense and we may not be successful in hiring or retaining new or existing qualified personnel. Equity awards are critical to our ability to hire and retain such key personnel. We are currently asking our stockholders to vote to approve an additional 15 million shares for the Company's 1994 Stock Plan. The vote will take place at our annual stockholders' meeting on May 13, 2011. If do not receive approval for the additional 15 million shares from our stockholders, our ability to compete for, hire and retain quality personnel may be negatively impacted. In addition we may also need to significantly increase our cash based compensation significantly.

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

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. [RESERVED]

ITEM 5. OTHER INFORMATION

On May 6, 2011, Cypress's Compensation Committee of the Board of Directors (the "Compensation Committee") approved the incentive payments to our executive officers for the first quarter of fiscal 2011 performance incentive plans. These payments were earned in accordance with the terms of our Key Employee Bonus Plan (the "KEBP") and the Performance Bonus Plan (the "PBP").

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The payments were determined based upon the financial performance of Cypress and each executive's performance. The performance measures under the KEBP include our non-GAAP profit-before-taxes percentage as well as individual strategic, operational and financial goals established for each executive. The following table sets forth the cash payments to our Named Executive Officers (as determined in our Proxy Statement filed with the Securities and Exchange Commission on March 29, 2011) under the KEBP and the PBP in the first quarter of fiscal 2011:

<u>Named Executive Officers</u>	<u>KEBP</u>	<u>PBP</u>
T.J. Rodgers, President and Chief Executive Officer	—	\$128,989
Christopher Seams, Executive Vice President, Sales, Marketing and Operations	\$34,403	—
Brad W. Buss, Executive Vice President, Finance & Administration and Chief Financial Officer	\$31,746	—
Paul Keswick, Executive Vice President, New Product Development	\$31,536	—
Norman Taffe, Executive Vice President, Consumer and Computation Division	\$27,187	—

Additionally, the Compensation Committee authorized quarterly and annual incentive payments under the KEBP, totaling \$128,675, to six other senior executive officers who are not Named Executive Officers.

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ITEM 6. EXHIBITS

<u>Exhibit Number</u>	<u>Description</u>
31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS*	XBRL Instance Document.
101.SCH*	XBRL Taxonomy Extension Schema Document.
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document.
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document.

* XBRL (Extensible Business Reporting Language) information is furnished and not filed or a part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, is deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, and otherwise is not subject to liability under these sections.

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.

CYPRESS SEMICONDUCTOR CORPORATION

Date: May 6, 2011

By: _____ /s/ BRAD W. BUSS
Brad W. Buss
Executive Vice President, Finance and Administration
and Chief Financial Officer

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