Item 7. ***Management's Discussion and Analysis of Financial Condition and Results of Operations***

The following discussion of our financial condition and results of operations should be read in conjunction with the financial statements and related notes included in this Annual Report on Form 10-K. This discussion may contain forward-looking statements based upon current expectations that involve risks and uncertainties including those discussed under Part I, Item 1A, "Risk Factors." These risks and uncertainties may cause actual results to differ materially from those discussed in the forward-looking statements.

Overview

We are a fabless semiconductor provider of high-performance application-specific standard products. Our core strength of expertise is the development of complex SoC devices, leveraging our extensive technology portfolio of intellectual property in the areas of analog, mixed-signal, digital signal processing, and embedded and standalone integrated circuits. The majority of our product portfolio leverages the ARM technology portfolio. We also develop platforms that we define as integrated hardware along with software that incorporates digital computing technologies designed and configured to provide an optimized computing solution. Our broad product portfolio includes devices for data storage, enterprise-class Ethernet data switching, Ethernet PHY, mobile handsets, connectivity and other consumer electronics. Our products serve diverse applications used in carrier, metropolitan, enterprise and PC-client data communications and storage systems. Additionally, we serve the consumer electronics market for the convergence of voice, video and data applications. As a fabless integrated circuit company, we rely on independent, third-party contractors to perform manufacturing, assembly and test functions. This approach allows us to focus on designing, developing and marketing our products and significantly reduces the amount of capital we need to invest in manufacturing products.

Historically, a relatively small number of customers have accounted for a significant portion of our net revenue. We had two end customers who each represented greater than 10% of our total net revenue in fiscal 2014. Combined revenue from these two customers was 36% of total net revenue in fiscal 2014. No distributors accounted for more than 10% of our net revenue for fiscal 2014. We had three end customers who represented greater than 10% of our total net revenue in fiscal 2013. Combined revenue from these three customers was 44% of total net revenue in fiscal 2013. We also had one distributor who accounted for more than 10% of our net revenue in fiscal 2013. We had one end customer who represented greater than 10% of our total net revenue in fiscal 2012. Revenue from this customer was 19% of total net revenue in fiscal 2012. We also had one distributor who accounted for more than 10% of our net revenue in fiscal 2012.

We expect to continue to experience significant customer concentration in future periods and most of our sales are made to customers located outside of the United States, primarily in Asia. Sales to customers in Asia represented approximately 95%, 90% and 88% of our net revenue for fiscal 2014, 2013 and 2012, respectively. Because many manufacturers and manufacturing subcontractors of our customers are located in Asia, we expect that most of our net revenue will continue to be represented by sales to our customers in that region. Substantially all of our sales are denominated in U.S. dollars.

A significant number of our products are being incorporated into consumer electronics products, including gaming devices and personal computers, which are subject to significant seasonality and fluctuations in demand. Holiday and back to school buying trends may at times negatively impact our results in the first and fourth quarter and positively impact our results in the second and third quarter of our fiscal years. In addition, consumer electronics sales are heavily dependent on new product launch timelines and product refreshes. For example, our sales of wireless connectivity products may increase significantly during a period when one of our consumers launches a new gaming console, and these sales may taper significantly after the initial launch period.

A relatively large portion of our sales have historically been made on the basis of purchase orders rather than long-term agreements. In addition, the sales cycle for our products is long, which may cause us to experience a delay between the time we incur expenses and the time revenue is generated from these expenditures. We anticipate that the rate of new orders may vary significantly from quarter to quarter. Consequently, if anticipated sales and shipments in any quarter do not occur when expected, expenses and inventory levels could be disproportionately high, and our operating results for that quarter and future quarters may be adversely affected.

Our fiscal year is the 52- or 53-week period ending on the Saturday closest to January 31. In a 52-week year, each fiscal quarter consists of 13 weeks. The additional week in a 53-week year is added to the fourth quarter, making such quarter consist of 14 weeks. Fiscal 2014 and fiscal 2012 had a 52-week period, and fiscal 2013 had a 53-week period.

Critical Accounting Policies and Estimates

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates, judgments and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, we evaluate our estimates, including those related to performance-based compensation, revenue recognition, provisions for sales returns and allowances, inventory excess and obsolescence, investment fair values, goodwill and other intangible assets, restructuring, income taxes, litigation and other contingencies. In addition, we use assumptions when employing the Monte Carlo simulation and Black-Scholes valuation models to calculate the fair value of share-based awards granted. We base our estimates of the carrying value of certain assets and liabilities on historical experience and on various other assumptions that are believed to be reasonable under the circumstances when these carrying values are not readily available from other sources. Actual results could differ from these estimates, and such differences could affect the results of operations reported in future periods. We believe the following critical accounting policies affect our more significant judgments and estimates used in the preparation of our consolidated financial statements.

Revenue Recognition. We recognize revenue when there is persuasive evidence of an arrangement, delivery has occurred, the fee is fixed or determinable, and collection is reasonably assured.

Product revenue is generally recognized upon shipment of product to customers, net of accruals for estimated sales returns and rebates. However, some of our sales are made through distributors under agreements allowing for price protection, shipped from stock pricing adjustment rights, and limited rights of stock rotation on product unsold by the distributors. Although title passes to the distributor upon shipment terms and payment by our distributors is not contingent on resale of the product, product revenue on sales made through distributors with price protection, shipped from stock pricing adjustment rights and stock rotation rights are deferred until the distributors sell the product to end customers. Deferred revenue less the related cost of the inventories is reported as deferred income. We do not believe that there is any significant exposure related to impairment of deferred cost of sales, as our historical returns have been minimal and inventory turnover for our distributors generally ranges from 60 to 90 days. Our sales to direct customers are made primarily pursuant to standard purchase orders for delivery of products.

A portion of our net revenue is derived from sales through third-party logistics providers, who maintain warehouses in close proximity to our customer's facilities. Revenue from sales through these third-party logistics providers is not recognized until the product is pulled from stock by the customer.

The provision for estimated sales returns and allowances on product sales is recorded in the same period the related revenues are recorded. These estimates are based on historical sales returns, analysis of credit memo data and other known factors. In addition, quality issues covered by warranties to our customers may be recorded as a reduction of revenue, in cases where the related products are not returned to us and/or the amount of the payment is not sufficiently supported by evidence of fair value. Actual returns could differ from these estimates. We account for rebates by recording reductions to revenue in the same period that the related revenue is recorded. The amount of these reductions is based upon the terms agreed to with the customers.

Share-based Compensation. We measure our share-based compensation at the grant date, based on the fair value of the award, and is recognized as expense over the requisite service period. We amortize share-based compensation expense for time-based and market-based awards under the straight-line attribution method over the vesting period, which is generally four years for annual grants to employees and five years for new hire grants. Performance-based awards are amortized using the accelerated method.

We estimate the fair value of time-based stock option awards on the date of grant using the Black Scholes option-pricing model. The fair value of market-based option awards is estimated on the date of grant using a Monte Carlo simulation model. The value of the portion of the awards that is ultimately expected to vest is recognized as expense over the requisite service periods. The Black-Scholes and Monte Carlo models incorporate various highly subjective assumptions including expected term of awards, expected future stock price volatility and expected forfeiture rates.

In developing estimates used to calculate assumptions, we establish the expected term for employee options, as well as expected forfeiture rates, based on the historical settlement experience and after giving consideration to vesting schedules. Assumptions for stock option exercises and pre-vesting terminations of stock options were stratified by employee groups with sufficiently distinct behavior patterns. Expected volatility was developed based on an equally weighted combination of historical stock price volatility and implied volatility derived from traded options on our stock in the marketplace. The expected dividend yield is calculated by dividing annualized dividend payments by the closing stock price on the grant date of the option.

Forfeitures are estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from initial estimates. Share-based compensation expense is recorded net of estimated forfeitures such that expense is recorded only for those share-based awards that are expected to vest. Previously recognized expense is reversed for the portion of awards forfeited prior to vesting as and when forfeitures occurred.

The fair value of each restricted stock unit is estimated based on the market price of the Company’s common shares on the date of grant less the expected dividend yield.

In addition, for both stock options and restricted stock units, we are required to estimate forfeiture rates, and true up these forfeiture rates when actual results are different from our estimates. Assumptions for forfeitures are stratified by employee groups with sufficiently distinct behavior patterns. Changes in the estimated forfeiture rate can have a significant effect on reported share-based compensation expense, as the effect of adjusting the rate for all expense amortization is recognized in the period the forfeiture estimate is changed. If the actual forfeiture rate is higher than the estimated forfeiture rate, then an adjustment will be made to increase the estimated forfeiture rate, which will result in a decrease to the expense recognized in the financial statements. If the actual forfeiture rate is lower than the estimated forfeiture rate, then an adjustment will be made to lower the estimated forfeiture rate, which will result in an increase to the expense recognized in the financial statements. The expense we recognize in future periods could be affected by changes in the estimated forfeiture rate and may differ significantly from amounts recognized in the current period and/or our forecasts.

Additionally, for certain of our performance-based awards, we must make subjective assumptions regarding the likelihood that the related performance metrics will be met. These assumptions are based on various revenue and operating performance criteria. Changes in our actual performance could cause a significant adjustment in future periods for these performance-based awards.

Accounting for Income Taxes. We estimate our income taxes in each of the jurisdictions in which we operate. This process involves estimating our actual tax exposure together with assessing temporary differences resulting from the differing treatment of certain items for tax return and financial statement purposes. These differences result in deferred tax assets and liabilities, which are included within our consolidated balance sheets.

We recognize income taxes using an asset and liability approach. This approach requires the recognition of taxes payable or refundable for the current year and deferred tax liabilities and assets for the future tax consequences of events that have been recognized in our consolidated financial statements or tax returns. The measurement of current and deferred taxes is based on provisions of the enacted tax law and the effects of future changes in tax laws or rates are not anticipated.

Evaluating the need for an amount of a valuation allowance for deferred tax assets often requires judgment and analysis of all the positive and negative evidence available to determine whether all or some portion of the deferred tax assets will not be realized. A valuation allowance must be established for deferred tax assets when it is more likely than not that they will not be realized. Based on the available evidence and judgment, we have determined that it is more likely than not that our U.S. research credits, which we earn in excess of our current year tax liabilities, and certain acquired net operating losses will not be realized. Therefore, we have provided a full valuation allowance against these credits and a portion against the net operating losses. If there is a change in our ability to realize our deferred tax assets, then our tax provision may decrease in the period in which we determine that realization is more likely than not.

As a multinational corporation, we conduct our business in many countries and are subject to taxation in many jurisdictions. The taxation of our business is subject to the application of various and sometimes conflicting tax laws and regulations as well as multinational tax conventions. Our effective tax rate is highly dependent upon the geographic distribution of our worldwide earnings or losses, the tax regulations and tax holidays in each geographic region, the availability of tax credits and carryforwards, and the effectiveness of our tax planning strategies. The application of tax laws and regulations is subject to legal and factual interpretation, judgment and uncertainty. Tax laws themselves are subject to change as a result of changes in fiscal policy, changes in legislation, and the evolution of regulations and court rulings. Consequently, taxing authorities may impose tax assessments or judgments against us that could materially impact our tax liability and/or our effective income tax rate.

We are subject to income tax audits by the respective tax authorities in all of the jurisdictions in which we operate. We recognize the effect of income tax positions only if these positions are more likely than not of being sustained. Recognized income tax positions are measured at the largest amount that is more than 50% likely of being realized. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs. We record interest and penalties related to unrecognized tax benefits in income tax expense. The calculation of our tax liabilities involves the inherent uncertainty associated with the application of GAAP and complex tax laws. We believe we have adequately provided for in our financial statements additional taxes that we estimate may be required to be paid as a result of such examinations. While we believe that we have adequately provided for all tax positions, amounts asserted by tax authorities could be greater or less than our accrued position. These tax liabilities, including the interest and penalties, are released pursuant to a settlement with tax authorities, completion of audit or expiration of various statutes of limitation. The material jurisdictions in which we may be subject to potential examination by tax authorities throughout the world include China, Israel, Singapore, Switzerland and the United States.

The recognition and measurement of current taxes payable or refundable and deferred tax assets and liabilities require that we make certain estimates and judgments. Changes to these estimates or a change in judgment may have a material impact on our tax provision in a future period.

Inventories. We value our inventory at the lower of cost or market, cost being determined under the first-in, first-out method. We regularly review inventory quantities on hand and record a reduction to the total carrying value of our inventory for any difference between cost and estimated market value of inventory that is determined to be excess, obsolete or unsellable inventory based primarily on our estimated forecast of product demand and production requirements. The estimate of future demand is compared to our inventory levels, including open purchase commitments, to determine the amount, if any, of obsolete or excess inventory. Demand for our products can fluctuate significantly from period to period. A significant decrease in demand could result in an increase in the amount of excess inventory on hand. In addition, our industry is characterized by rapid technological change, frequent new product development and rapid product obsolescence that could result in an increase in the amount of obsolete inventory quantities on hand. Additionally, our estimates of future product demand may prove to be inaccurate, in which case we may have understated or overstated the reduction to the total carrying value of our inventory for excess and obsolete inventory. In the future, if our inventory is determined to be overvalued, we would be required to recognize such costs in our cost of goods sold at the time of such determination. Likewise, if our inventory is determined to be undervalued, we may have over-reported our cost of goods sold in previous periods and would be required to recognize additional gross margin at the time the related inventory is sold. Therefore, although we make every effort to ensure the accuracy of our forecasts of future product demand, any significant unanticipated changes in demand or technological developments could have a significant impact on the value of our inventory and our results of operations.

Long-lived Assets and Intangible Assets. We assess the impairment of long-lived assets and intangible assets whenever events or changes in circumstances indicate that the carrying value of such assets may not be recoverable. Circumstances which could trigger a review include, but are not limited to the following:

- significant decreases in the market price of the asset;
- significant adverse changes in the business climate or legal factors;
- accumulation of costs significantly in excess of the amount originally expected for the acquisition or construction of the asset;
- current period cash flow or operating losses combined with a history of losses or a forecast of continuing losses associated with the use of the asset; and
- current expectation that the asset will more likely than not be sold or disposed of significantly before the end of its estimated useful life.

Whenever events or changes in circumstances suggest that the carrying amount of long-lived assets and intangible assets may not be recoverable, we estimate the future cash flows expected to be generated by the asset from its use or eventual disposition. If the sum of the expected future cash flows is less than the carrying amount of those assets, we recognize an impairment loss based on the excess of the carrying amount over the fair value of the assets. Significant management judgment is required in the forecasts of future operating results that are used in the discounted cash flow method of valuation.

As of February 1, 2014, we had a total of $49.0 million in acquired intangible assets, of which $3.4 million represented remaining in-process research and development (“IPR&D”). In connection with our IPR&D, we performed a qualitative assessment in 2014 to determine whether it was more likely than not that our IPR&D was impaired. Based on our assessment we determined that there was no impairment in fiscal 2014. However, we recorded a charge of $0.8 million in fiscal 2013 to write off IPR&D related to an abandoned project.

Goodwill. We evaluate goodwill for impairment whenever events or changes in circumstances indicate that the carrying value of such assets may not be recoverable. Factors we consider important which could trigger a goodwill impairment review include;

- significant underperformance relative to historical or projected future operating results;
- significant changes in the manner of our use of the acquired assets or the strategy for our overall business;
- significant negative industry or economic trends;
- a significant decline in our stock price for a sustained period; and
- a significant change in our market capitalization relative to our net book value.

When performing our assessment, we include a control premium, in addition to our fair value to reflect the full value and amount that a buyer would be willing to pay for the company. Since our inception, we have not recognized any impairment of goodwill.

Litigation Costs. From time to time, we are involved in legal actions arising in the ordinary course of business. There can be no assurance these actions or other third-party assertions will be resolved without costly litigation, in a manner that does not adversely impact our financial position, results of operations or cash flows or without requiring royalty payments in the future, which may adversely impact gross margins. We are aggressively defending these litigation matters and believe no material adverse outcome will result. We record a liability when it is probable that a loss has been incurred and the amount can be reasonably estimated. In determining the probability of a loss and consequently, determining a reasonable estimate, management is required to use significant judgment. Given the uncertainties associated with any litigation, the actual outcome can be different than our estimates and could adversely affect our results of operations, financial position and cash flows.

Results of Operations

Fiscal 2014 was the start of a turnaround for Marvell. Revenue in fiscal 2014 was $3.4 billion, which was 7% higher compared to net revenue of $3.2 billion in fiscal 2013. Revenue for products in the storage market was strong and grew approximately 13% over fiscal 2013 due to strong growth in our solid state drives (“SSD”) business and continued share gains in our hard disk drive (“HDD”) business. Revenue from our mobile and wireless end market delivered modest growth in fiscal 2014 after undergoing two years of customer and product transitions, and we are now well positioned to deliver strong growth in fiscal 2015. Although revenue for products in our networking market declined in fiscal 2014, the decline was consistent with the overall enterprise networking market. We believe our sustained investments in advanced technologies leading to new innovations will help drive increased business opportunities. We are seeing many of our customers introducing new devices using our innovative solutions, which we believe will drive success across all of our end markets. Our future growth is expected to be driven by areas such as mobile handsets, tablets, connectivity, smart home devices and SSDs.

- In the mobile market, our 3G unified platform is in mass production at multiple top tier OEMs. For example, Samsung has successfully launched their 7-inch Galaxy Tab 3 globally based on our dual-core platform and China Mobile has selected our dual-core platform to launch its first branded smartphone. In addition to our dual-core devices, our quad-core platform is now in production with leading OEM customers who have introduced multiple quad-core smartphone models targeting the mass-market segments for both WCDMA and TD-SCDMA. In the deployment of LTE technology, we continued to make steady progress with our LTE solution, which passed qualifications in China. In North America, our LTE solution is now fully certified for voice and data at one major carrier and we are expecting to achieve full certification with another large carrier in early fiscal 2015. We also recently introduced the ARMADA Mobile PXA1928, a 64-bit single-chip quad-core, 5-mode LTE solution supporting all global mobile broadband standards, including LTE TDD/FDD, HSPA+,TD-HSPA+ and EDGE.
- In the wireless connectivity market, one of the new design wins is in the Google Chromecast, an innovative new product that allows consumers to seamlessly connect and stream video content from a small screen mobile device to any large screen. Several service providers have started to ship our platform video solutions for the IPTV and hybrid set-top box products. We are also seeing leading OEMs launch Smart TV and set-top box products using our platform video solutions. In the gaming market, our wireless connectivity solutions are being used in the new game consoles that were launched for the holiday season. We expect wireless connectivity and other advanced features in these new game consoles to help drive growth for us in the industry in the upcoming year. In addition, in the smartphone market, we have ongoing 100% attach rates on our new mobile platforms for our connectivity solutions with our 3G and 4G mobile platforms. We are seeing new opportunities for our connectivity solutions across multiple market segments.

- In the storage market, we continue to execute well as the overall drive industry seems to have stabilized. We continue to grow within the HDD market as we have seen strong demand for our 500 gigabyte per platter products. In addition, we are seeing increased demand on enterprise drives at a top North America based HDD customer. Within the SSD market, our revenue has continued to grow and our strategy of partnering with top tier OEMs has resulted in excellent traction for our advanced SSD solutions. Our PCIe SSD solutions are now in mass production and we believe we have a lead in the market. We are also leveraging our technology leadership in HDD and SSD to help our customer migrate to hybrid storage devices. Here we are developing a single-chip solution that we believe will drive lower price points and allow the market to grow. We believe this will allow us to further increase our share and solidify our leadership position in the market.
- In the networking market, we experienced softer than expected demand from some of our enterprise networking customers in fiscal 2014 due to a weaker market overall. We continue to make strong progress with development design activity for our product portfolio addressing the infrastructure portion of the market. We announced our first 28nm network processor and traffic management solutions with our Xelerated AX and HX family of products targeting the infrastructure market, where we have engaged with Tier-1 customers on these new high-performance products for their next generation networking equipment. We continue to increase our footprint in the service provider market and are benefiting from modest improvements in the enterprise end market. We expect these new initiatives to drive better results starting in the second half of fiscal 2015.

Our cost of goods sold as a percentage of net revenue in fiscal 2014 was higher compared to fiscal 2013. As we expand our presence and grow revenue in the consumer space, we expect our gross margin to face downward pressure, as these end markets generally have lower average gross margins than the rest of our business. However, we expect growth in the consumer space will result in improvement to total gross margin dollars and operating profit. In addition, we are focused on efforts to improve both aspects of our gross profit, including through cost improvement and pricing.

Our financial position is strong and we remain committed to deliver shareholder value through our share repurchase and dividend programs.

- Our cash, cash equivalents and short-term investments were $2.0 billion at February 1, 2014 and we generated cash flows from operations of $448.0 million in fiscal 2014.
- We paid a cumulative cash dividend of $0.24 per share for a total of $119.4 million during fiscal 2014 and we recently announced a dividend of $0.06 per share to be paid in the first quarter of fiscal 2015.
- We repurchased a total of 33.1 million of our common shares for $354.1 million in cash during fiscal 2014.

We are currently involved in a patent litigation action with Carnegie Mellon University ("CMU") (See "Risk Factors" under Part I, Item 1A of this Annual Report on Form 10-K and "Note 10 — Commitments and Contingencies" in the Notes to Consolidated Financial Statements for a further discussion of the risks associated with this matter and other patent litigation matters). A jury has awarded past damages of $1.17 billion, and CMU has sought pre-judgment damages of up to $322 million, post-judgment interest, attorneys' fees, and an injunction and/or ongoing royalties. Due to the finding of willfulness during post-trial proceedings, the judge could enhance the damages by an amount up to triple the damages awarded by the jury at trial. We intend to appeal the final judgment and we would seek to stay any award of damages pending the appeal. We strongly believe that we do not infringe on the methods described in the CMU patents and that our products use our own internally developed patented read channel technology.

The following table sets forth information derived from our consolidated statements of operations expressed as a percentage of net revenue.

	Year Ended		
	February 1, 2014	February 2, 2013	January 28, 2012
Net revenue	100.0%	100.0%	100.0%
Operating costs and expenses:			
Cost of goods sold	48.9	47.1	43.2
Research and development	34.0	33.4	29.9
Selling and marketing	4.5	5.1	4.7
General and administrative	3.1	3.4	3.0
Amortization and write-off of acquired intangible assets	1.3	1.7	1.4
Total operating costs and expenses	91.8	90.7	82.2
Operating income	8.2	9.3	17.8
Interest and other income, net	0.7	0.5	0.4
Income before income taxes	8.9	9.8	18.2
Provision (benefit) for income taxes	(0.3)	0.1	0.1
Net income	9.2%	9.7%	18.1%

Years Ended February 1, 2014 and February 2, 2013

Net Revenue

	Year Ended		
	February 1, 2014	February 2, 2013	% Change in 2014
	(in thousands, except percentage)		
Net revenue	$3,404,400	$3,168,630	7.4%

Net revenue is gross revenue, net of accruals for estimated sales returns and rebates. The increase in net revenue during fiscal 2014 was driven by an increase in sales of our storage products, as we continued to see growth for our 500-gigabyte-per-platter products and increased demand for enterprise drives at a top North America based HDD customer. In addition, revenue for solid-state drive controllers increased significantly compared to the prior year, as these products continue to gain traction and popularity. We experienced growth in revenue for our mobile and wireless products in the second half of fiscal 2014 due to successful launches of our new multi-core 3G mobile devices with key OEM's into mobile handsets and tablets. In addition, we saw increased demand for our wireless products driven by the holiday ramp up of new gaming platforms at two of our customers and the launch of new programs such as the Google Chromecast. However, mobile and wireless revenue was flat year over year as fiscal 2013 included significantly higher revenue from a North American handset customer. The increase in net revenue for fiscal 2014 was partially offset by slightly lower revenue for our networking products, primarily due to a weaker overall market and its effect on our networking customers.

In the first quarter of fiscal 2015, we expect net revenue to be in the range of $870 million to $910 million, a decline of 4% at the midpoint, driven mainly by normal seasonality.

Cost of Goods Sold

	Year Ended		
	February 1, 2014	February 2, 2013	% Change in 2014
	(in thousands, except percentages)		
Cost of goods sold	$1,663,730	$1,493,497	11.4%
% of net revenue	48.9%	47.1%	

Cost of goods sold as a percentage of net revenue was higher in fiscal 2014. Although we continue to benefit from lower commodity costs driven by our replacement of gold in our products with copper, manufacturing costs were higher in fiscal 2014 due to increased royalty expense and the ramp up of new product designs in consumer-oriented products. Our cost of goods sold as a percentage of net revenue may fluctuate in future periods due to, among other things, changes in the mix of products sold; the timing of production ramps of new products; increased pricing pressures from our customers and competitors, particularly in the consumer product markets that we are targeting; charges for obsolete or potentially excess inventory; changes in the costs charged by our foundry; assembly and test subcontractors; product warranty costs; changes in commodity prices such as gold; and the margin profiles of our new product introductions.

We currently expect that cost of goods sold as a percentage of net revenue in the first quarter of fiscal 2015 will be approximately flat compared to the amount in the fourth quarter of fiscal 2014 based on the midpoint of our expected range.

Share-Based Compensation Expense

	Year Ended	
	February 1, 2014	February 2, 2013
	(in thousands)	
Cost of goods sold	$ 8,863	$ 8,142
Research and development	109,432	87,149
Selling and marketing	13,940	13,278
General and administrative	23,638	18,711
	$ 155,873	$ 127,280

Share-based compensation expense increased by $28.6 million in fiscal 2014 compared to fiscal 2013. These increases were primarily due to increased headcount in fiscal 2014, combined with higher expense related to the employee stock purchase plan. The offering price of the employee stock purchase plan was reset in June 2012 and also in December 2012 due to the decline in our stock price. In addition, equity awards granted in fiscal 2014 contained shorter vesting periods, which accelerated the amount of share-based compensation expense.

Research and Development

	Year Ended		
	February 1, 2014	February 2, 2013	% Change 2014
	(in thousands, except percentages)		
Research and development	$1,156,885	$1,057,445	9.4%
% of net revenue	34.0%	33.4%	

Research and development expense increased by $99.4 million in fiscal 2014 compared to fiscal 2013, primarily attributable to higher personnel-related costs as a result of increased headcount in fiscal 2014 to support new designs, higher share-based compensation and higher average employee compensation. The increase in expense also reflects higher computer-aided design tool costs, and higher depreciation and amortization costs as we continue to invest in the development of innovative solutions.

Selling and Marketing

	Year Ended		
	February 1, 2014	February 2, 2013	% Change in 2014
	(in thousands, except percentages)		
Selling and marketing	$ 152,698	$ 161,817	(5.6)%
% of net revenue	4.5%	5.1%	

Selling and marketing expense decreased by $9.1 million in fiscal 2014 compared to fiscal 2013. The decrease was primarily attributable to lower costs for marketing communication activities as a result of efforts to control discretionary spending and lower personnel-related costs caused by a decrease in headcount in fiscal 2014.

General and Administrative

	Year Ended		
	February 1, 2014	February 2, 2013	% Change in 2014
	(in thousands, except percentages)		
General and administrative	$ 106,471	$ 108,514	(1.9)%
% of net revenue	3.1%	3.4%	

General and administrative expense decreased by $2.0 million in fiscal 2014 compared to fiscal 2013. The decrease was primarily attributable to lower legal costs for ongoing litigation matters, partially offset by higher share-based compensation.

Amortization and Write-Off of Acquired Intangible Assets

	Year Ended		
	February 1, 2014	February 2, 2013	% Change in 2014
	(in thousands, except percentages)		
Amortization and write-off of acquired intangible assets	$ 43,925	$ 52,700	(16.7)%
% of net revenue	1.3%	1.7%	

Amortization and write-off of acquired intangible assets decreased by $8.8 million in fiscal 2014 compared to fiscal 2013. The decrease was primarily due to certain intangible assets that became fully amortized. In addition, fiscal 2014 included a write-off of $8.1 million for the impairment of an acquired intangible asset compared to fiscal 2013, which included a $0.8 million write-off of IPR&D related to an abandoned project.

Restructuring

	Year Ended	
	February 1, 2014	February 2, 2013
	(in thousands)	
Research and development	$ 2,886	$ 47
Selling and marketing	795	(3)
General and administrative	1,051	1,213
	$ 4,732	$ 1,257

We recorded a $4.2 million charge primarily related to the closure of two sites in fiscal 2014. This amount included $2.8 million of severance costs, $1.3 million for other exit-related costs in connection with vacating three facilities and $0.1 million for the write off of equipment. All activities related to the closure of the two sites were substantially completed by the end of the fiscal year.

During fiscal 2014, we also continued to make payments and incur ongoing operating expenses related to vacated facilities under previous restructure actions.

Interest and Other Income, net

	Year Ended		
	February 1, 2014	February 2, 2013	% Change in 2014
	(in thousands, except percentages)		
Interest and other income, net	$ 25,566	$ 15,533	64.6%
% of net revenue	0.7%	0.5%	

Interest and other income, net, increased by $10.0 million in fiscal 2014 as compared to fiscal 2013, primarily due to a $7.0 million gain on the sale of a business (See "Note 2 — Acquisitions and Divestitures" in our Notes to the Consolidated Financial Statements set forth in Part II, Item 8 of the Annual Report on Form 10-K for further information) and the impact of the strengthening of the U.S. dollar on our foreign currency denominated tax liabilities. This was partially offset by lower interest income from lower average cash and investment balances, lower realized investment gains, and higher imputed interest expense related to technology license obligations during fiscal 2014. We also had $1.5 million in write downs of equity investments in fiscal 2014.

Provision (benefit) for Income Taxes

	Year Ended		
	February 1, 2014	February 2, 2013	% Change in 2014
	(in thousands, except percentages)		
Provision (benefit) for income taxes	$ (9,063)	$ 3,605	(351.4)%
% of net revenue	(0.3)%	0.1%	

The income tax benefit for fiscal 2014 included the current income tax liability of $13.2 million plus a $3.9 million reduction in net deferred tax assets that includes $1.2 million charge for the settlement of an audit in a non-U.S. jurisdiction. These tax charges were offset by a net reduction in unrecognized tax benefits of $22.6 million combined with a $3.9 million tax benefit due to return-to-provision adjustments upon filing of tax returns in fiscal 2014 that includes a $0.5 million benefit from the settlement of an audit in a non-U.S. jurisdiction. The reduction in net deferred tax assets was mostly due to an increase in the Singapore deferred tax liability since the Singapore government has not yet granted an extension of the tax incentive arrangement in Singapore which expires in June 2014 (See "Note 9 — Income Taxes" in our Notes to the Consolidated Financial Statements set forth in Part II, Item 8 of the Annual Report on Form 10-K for further information). The net reduction in unrecognized tax benefits primarily arose from the expiration of statute of limitations in non-U.S. jurisdictions and from the settlement of two audits in non-U.S. jurisdictions less an increase in current unrecognized tax estimates.

Years Ended February 2, 2013 and January 28, 2012

Net Revenue

	Year Ended		
	February 2, 2013	January 28, 2012	% Change in 2013
	(in thousands, except percentage)		
Net revenue	$3,168,630	$3,393,040	(6.6)%

The revenue decline during fiscal 2013 was primarily due to declines in the mobile and wireless end market, and to a lesser extent, a decline in the storage end market. Within our mobile and wireless end market, revenue from our leading North American handset customer declined year-over-year due to the continued competitive challenges that they faced. Within the storage end market, revenue declined in fiscal 2013 compared to the prior year primarily as a result of the slowdown in the global market for PCs. The flooding in Thailand during the second half of fiscal 2012 impacted our overall HDD revenue in both fiscal 2012 and fiscal 2013. One of our customers, for which we entered fiscal 2013 with a relatively low market segment share of their products, was least impacted by the flooding in Thailand in the second half of fiscal 2012, which negatively impacted our revenue towards the beginning of fiscal 2013. However, during fiscal 2013, we continued to grow our share of revenue with this customer, offsetting most of the negative impacts from the floods. In addition, sales of our SSD products increased significantly in fiscal 2013 compared to fiscal 2012 as our products began to gain acceptance in the market. SSD sales still made up a small percentage of our total storage revenue, however, they grew and made up an increasingly larger percentage of overall revenue. Net revenue from our networking end market increased slightly in fiscal 2013 compared to the prior fiscal year, due to growth in our PON and networking processing unit products as well as growth in switching products.

Cost of Goods Sold

	Year Ended		
	February 2, 2013	January 28, 2012	% Change in 2013
	(in thousands, except percentages)		
Cost of goods sold	$1,493,497	$1,465,805	1.9%
% of net revenue	47.1%	43.2%	

Cost of goods sold as a percentage of net revenue in fiscal 2013 increased by 390 basis points, from 43.2% in fiscal 2012 to 47.1% in fiscal 2013. This increase was primarily due to product pricing declines outpacing the cost reductions received from our manufacturing partners. Unfavorable changes to the gross margin mix of our products sold compared to fiscal 2012, driven by growth in businesses with lower gross margins further contributed to the increase.

Share-Based Compensation Expense

	Year Ended	
	February 2, 2013	January 28, 2012
	(in thousands)	
Cost of goods sold	$ 8,142	$ 6,995
Research and development	87,149	85,924
Selling and marketing	13,278	12,920
General and administrative	18,711	14,024
	$ 127,280	$ 119,863

We recognized higher share-based compensation expense as a result of higher headcount in fiscal 2013, combined with the effect of an increase in expense related to the employee stock purchase plan. The offering price of the employee stock purchase plan was reset in June 2012 and also in December 2012 due to the decline in our stock price. Although share-based compensation expense increased by $7.4 million in fiscal 2013 compared to fiscal 2012, it included the recovery of previously recognized expense associated with unvested share-based awards that were cancelled as a result of the resignation in October 2012 of our then chief financial officer.

Research and Development

	Year Ended		
	February 2, 2013	January 28, 2012	% Change in 2013
	(in thousands, except percentages)		
Research and development	$1,057,445	$1,013,678	4.3%
% of net revenue	33.4%	29.9%	

Research and development expense increased by $43.8 million in fiscal 2013 compared to fiscal 2012, primarily due to higher personnel-related costs as a result of increased headcount in fiscal 2013 compared to fiscal 2012. In addition, since fiscal 2013 was a 53-week year, overall research and development expense was higher due to the additional week. The increase in the fiscal 2013 research and development expense was partially offset by a higher amount of product development funding from our customers.

Selling and Marketing

	Year Ended		
	February 2, 2013	January 28, 2012	% Change in 2013
	(in thousands, except percentages)		
Selling and marketing	$ 161,817	$ 159,434	1.5%
% of net revenue	5.1%	4.7%	

Selling and marketing expense increased by $2.4 million in fiscal 2013 compared to fiscal 2012. The increase was primarily due to increased trade show and marketing communication activities combined with higher expenses for other professional services. Although fiscal 2013 was a 53-week year, the increase in overall expense for the additional week was essentially offset by lower expenses for contractor services.

General and Administrative

	Year Ended		
	February 2, 2013	January 28, 2012	% Change in 2013
	(in thousands, except percentages)		
General and administrative	$ 108,514	$ 100,620	7.8%
% of net revenue	3.4%	3.0%	

General and administrative expense increased by $7.9 million in fiscal 2013 compared to fiscal 2012. The increase was primarily attributed to an increase in legal expenses, a significant portion of which related to the CMU trial towards the end of the fiscal year (See “Note 10 — Commitments and Contingencies” in the Notes to the Consolidated Financial Statements). In addition, since fiscal 2013 was a 53-week year, overall general and administrative expense was higher due to the additional week.

Amortization and Write-Off of Acquired Intangible Assets

	Year Ended		
	February 2, 2013	January 28, 2012	% Change in 2013
	(in thousands, except percentages)		
Amortization and write-off of acquired intangible assets	$ 52,700	$ 49,357	6.8%
% of net revenue	1.7%	1.4%	

Amortization and write-off of acquired intangible assets increased by $3.3 million in fiscal 2013 compared to fiscal 2012. This increase was primarily due to additional amortization expense related to the intangible assets acquired in the fourth quarter of fiscal 2012 and the additional week of expense since fiscal 2013 was a 53-week year.

Interest and Other Income, net

	Year Ended		
	February 2, 2013	January 28, 2012	% Change in 2013
	(in thousands, except percentages)		
Interest and other income, net	$ 15,533	$ 14,913	4.2%
% of net revenue	0.5%	0.4%	

Interest and other income, net, consists primarily of interest earned on cash, cash equivalents and short-term investment balances, gains and losses on the sale of marketable and equity securities and foreign currency impacts, net of interest. The increase in interest and other income, net in fiscal 2013 compared to fiscal 2012 was primarily due to higher gains on sales of marketable securities. This was partially offset by lower interest income in fiscal 2013 from lower average cash and investment balances, as well as a lower rate of return.

Provision for Income Taxes

	Year Ended		
	February 2, 2013	January 28, 2012	% Change in 2013
	(in thousands, except percentages)		
Provision for income taxes	$ 3,605	$ 3,968	(9.1)%
% of net revenue	0.1%	0.1%	

During fiscal 2013, the provision for income taxes consisted of the current income tax liability of $20.1 million, which was primarily offset by net reductions in unrecognized tax benefits of $18.8 million due to the expiration of the statutes of limitations in multiple jurisdictions less increases in unrecognized tax benefits including interest and penalties. The fiscal 2013 provision for income taxes also included $2.3 million in tax expense that mainly resulted from tax provision-to-tax return adjustments in various countries. This compares to the provision for income taxes in fiscal 2012 consisting of the current income tax liability of $12.4 million, which was primarily offset by net reductions in unrecognized tax benefits of $6.1 million due to the expiration of the statutes of limitations in multiple jurisdictions less increases in unrecognized tax benefits including interest and penalties. The fiscal 2012 provision for income taxes also included a benefit of $2.3 million from a decrease in tax expense that mainly resulted from tax provision-to-tax return adjustments in various countries and from the settlements of audits in non-U.S. jurisdictions.

Liquidity and Capital Resources

Our principal source of liquidity as of February 1, 2014 consisted of approximately $2.0 billion of cash, cash equivalents and short-term investments.

Net Cash Provided by Operating Activities

Net cash provided by operating activities was $448.0 million for fiscal 2014 compared to $729.0 million for fiscal 2013 and $771.2 million for fiscal 2012. The cash inflows from operations for fiscal 2014 were primarily due to $623.0 million of net income adjusted for non-cash items and negative working capital changes of $175.0 million. The negative impact on working capital was primarily driven by an increase in accounts receivable from higher revenue levels and higher inventories due to the ramp up of new products.

The cash inflows from operations for fiscal 2013 were primarily due to $592.0 million of net income adjusted for non-cash items and positive working capital changes of $137.0 million. The positive change in working capital for fiscal 2013 was primarily driven by a decrease in inventories due to increased shipment towards the end of the current year and a decrease in accounts receivable due to improved collections in the fourth quarter of fiscal 2013 compared to the fourth quarter of fiscal 2012.

The cash inflows from operations for fiscal 2012 were primarily due to $884.5 million of net income adjusted for non-cash items. Within working capital during fiscal 2012, accounts receivable decreased due to lower levels of revenue in the fourth quarter of fiscal 2012. Inventories increased due primarily to two factors: (1) the floods in Thailand which increased our inventories of hard drive products at the end of fiscal 2012, and (2) the increased use of “hubs” managed by third-party logistics providers. When products are shipped to these third-party managed locations, the inventory remains on our books until pulled by the customer. Accounts payable decreased due to lower levels of purchasing activities near the end of fiscal 2012.

Net Cash Provided by and (Used in) Investing Activities

Net cash provided by investing activities was $74.8 million for fiscal 2014 compared to net cash provided by investing activities of $178.8 million for fiscal 2013 and net cash used in investing activities of $590.1 million for fiscal 2012. For fiscal 2014, net cash provided by investing activities was primarily generated from the sales and maturities of available-for-sale securities of $995.0 million less purchases of available-for-sale securities of $837.9 million. In addition, we paid $66.6 million for the purchase of property and equipment and $17.6 million for the purchase of technology licenses.

For fiscal 2013, net cash provided by investing activities was primarily generated from net sale and maturities of available-for-sale securities of $291.8 million. The net cash inflow from available-for-sale securities in fiscal 2013 was partially offset by the purchases of $68.2 million of property and equipment, and $35.0 million of IP licenses.

For fiscal 2012, net cash used in investing activities was primarily due to net purchases of available-for-sale securities of $393.5 million. In addition, we paid $93.9 million for acquisitions, purchased $88.8 million of property and equipment mainly to support additional capacity, and purchased $13.8 million of technology licenses in fiscal 2012.

Net Cash Used in Financing Activities

Net cash used in financing activities was $309.0 million for fiscal 2014 compared to $940.8 million for fiscal 2013 and $1.2 billion for fiscal 2012. For fiscal 2014, net cash used in financing activities was primarily attributable to repurchases under our share repurchase program. We also made payments of our quarterly dividends of $119.4 million. The cash outflow was partially offset by net proceeds of $194.1 million from the issuance of our common shares under our share-based plans less the minimum tax withholding on behalf of employees for net share settlements.

For fiscal 2013, net cash used in financing activities was primarily attributable to repurchases under our share repurchase program of 91.0 million of our common shares in the open market for $959.1 million. Of this amount, $22.2 million was unpaid and included in accrued liabilities as of February 2, 2013. We also paid cash dividends of $98.8 million in fiscal 2013. The cash outflow was partially offset by net proceeds of $94.8 million from the issuance of our common shares under our share-based plans less the minimum tax withholding paid on behalf of employees for net share settlements.

For fiscal 2012, net cash used in financing activities was primarily attributable to repurchases under our share repurchase program of 87.8 million of its common shares in the open market for $1.3 billion. The cash outflow was partially offset net by proceeds of $97.9 million from the issuance of common shares under our share-based plans less the minimum tax withholding paid on behalf of employees for net share settlements.

Off-Balance Sheet Arrangements

We plan to appeal the final judgment issued by the District Court in the CMU litigation, regardless of the dollar amount of the final judgment. The parties are currently engaged in discussions before a Special Master concerning the bonding of the judgment pending appeal. During October 2013, we entered into indemnity agreements with a consortium of insurers that would potentially provide financial assurance that each of the insurers will be indemnified by us should a loss occur under a surety bond. As of February 1, 2014 and as of the date of this filing, no final judgment has been issued and no surety bond has been issued. Therefore, these indemnity agreements have had no impact to our Consolidated Balance Sheets as of February 1, 2014. We expect that under a surety bond, the surety companies would agree to guarantee to the District Court our payment of a specific amount, to be determined. However, the terms of any surety bond arrangements have not been finalized and we cannot be certain that a surety bond will be available to us in sufficient amount to cover the full amount of a final judgment or on commercially reasonable terms. If we cannot obtain a surety bond in sufficient amount or on commercially reasonable terms, or if the District Court in the CMU litigation does not approve alternative arrangements to stay execution of the judgment pending our appeal, our business could be harmed. For example, if, under a surety bond, we must post our cash, cash equivalents and short term investments as collateral, we may be restricted from using such assets in the operation of our business and such assets would be classified as restricted cash in future filings.

As part of our ongoing business, we do not participate in transactions that generate relationships with unconsolidated entities of financial partnerships, such as entities often referred to as structured finance or special purpose entities (“SPEs”), which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. As of February 1, 2014, we were not involved in any unconsolidated SPE transactions.

Contractual Obligations and Commitments

Under our manufacturing relationships with our foundry partners, cancellation of outstanding purchase orders is allowed but requires repayment of all expenses incurred through the date of cancellation. As of February 1, 2014, these foundries had incurred approximately $270.9 million of manufacturing costs and expenses relating to our outstanding purchase orders.

The following table summarizes our contractual obligations as of February 1, 2014 and the effect that such obligations are expected to have on our liquidity and cash flow in future periods (in thousands):

	Payment Obligations by Fiscal Year						
	2015	2016	2017	2018	2019	Thereafter	Total
Contractual obligations:							
Facilities operating leases, net	$ 23,341	$ 17,705	$ 5,659	$ 376	$ 72	$ 527	$ 47,680
CAD and other operating leases	52,265	43,994	27,046	6,079	1,078	1,258	131,720
Purchase commitments to foundries	270,898	—	—	—	—	—	270,898
Capital purchase obligations	36,341	—	—	—	—	—	36,341
Technology license obligations	14,913	13,145	7,869	9,180	—	—	45,107
Other non-current obligations (1)	—	9,424	419	—	2,430	—	12,273
Total contractual cash obligations	$ 397,758	$ 84,268	$ 40,993	$ 15,635	$ 3,580	$ 1,785	$ 544,019

(1) Amounts represent anticipated future cash payments, including anticipated interest payments not recorded in the consolidated balance sheet.

In addition to the above commitments and contingencies, as of February 1, 2014, we have $43.2 million of unrecognized tax benefits as liabilities. We also have a liability for potential interest and penalties of $29.6 million as of February 1, 2014. During the next 12 months, it is reasonably possible that the amount of unrecognized tax benefits could increase or decrease significantly due to changes in tax law jurisdictions, new tax audits and changes in the U.S. dollar as compared to foreign currencies within the next 12 months. Excluding these factors, uncertain tax positions may decrease by as much as $20 million from the lapse of the statutes of limitation in various jurisdictions during the next 12 months.

Prospective Capital Needs

We believe that our existing cash, cash equivalents and short-term investments, together with cash generated from operations, exercise of employee stock options and purchases under our employee stock purchase plan will be sufficient to cover our working capital needs, capital expenditures, investment requirements, any declared dividends and commitments for at least the next 12 months. Our capital requirements will depend on many factors, including our rate of sales growth, market acceptance of our products, costs of securing access to adequate manufacturing capacity, the timing and extent of research and development projects and increases in operating expenses, which are all subject to uncertainty. In addition, we are named as defendants to several litigation actions and an unfavorable outcome in any current litigation could have a material adverse effect on our liquidity, cash flows and results of operations. Specifically, with respect to the CMU litigation, a jury has awarded past damages of $1.17 billion, and CMU has sought pre-judgment damages of up to $322 million, post-judgment interest, attorneys' fees, and an injunction and/or ongoing royalties. Due to the finding of willfulness during post trial proceedings, the judge could enhance the damages by an amount up to triple the damages awarded by the jury at trial. We intend to appeal the final judgment and we would seek to stay any award of damages pending the appeal. We strongly believe that we do not infringe on the methods described in the CMU patents and that our products use our own internally developed patented read channel technology. See the section entitled "Off-Balance Sheet Arrangements" above for a discussion of the effects on liquidity from the CMU litigation.

To the extent that our existing cash, cash equivalents and short-term investments and cash generated by operations are insufficient to fund our future activities, we may need to raise additional funds through public or private debt or equity financing. We may also enter into additional acquisitions of businesses, purchase assets or enter into other strategic arrangements in the future, which could also require us to seek debt or equity financing. Additional equity financing or convertible debt financing may be dilutive to our current shareholders. If we elect to raise additional funds, we may not be able to obtain such funds on a timely basis or on acceptable terms, if at all. If we raise additional funds by issuing additional equity or convertible debt securities, the ownership percentages of existing shareholders would be reduced. In addition, the equity or debt securities that we issue may have rights, preferences or privileges senior to our common shares.

Recent Accounting Pronouncements

Please see “Note 1 — The Company and its Significant Accounting Policies — Recent Accounting Pronouncements” for further details in our Notes to the Consolidated Financial Statements set forth in Part II, Item 8 of this Form 10-K.

Related Party Transactions

Please see “Note 14 — Related Party Transactions” for further details in our Notes to the Consolidated Financial Statements set forth in Part II, Item 8 of this Form 10-K.

Item 7A. *Quantitative and Qualitative Disclosures About Market Risk*

Interest Rate Risk. Our interest rate risk relates primarily to our fixed income short-term investment portfolio as we did not have any outstanding debt as of February 1, 2014. We maintain an investment policy that requires minimum credit ratings, diversification of credit risk and limits the long-term interest rate risk by requiring maturities of generally less than five years. We invest our excess cash primarily in highly liquid debt instruments of the U.S. government and its agencies, time deposits, money market mutual funds and corporate debt securities. These investments are 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 shareholders’ equity. Investments in both fixed rate and floating rate interest earning securities carry a degree of interest rate risk. Fixed rate securities may have their fair market value adversely impacted due to a rise in interest rates, while floating rate securities may produce less income than predicted if interest rates fall.

To provide an assessment of the interest rate risk associated with our investment portfolio, we performed a sensitivity analysis to determine the impact that an adverse change in interest rates would have on the value of the investment portfolio. Based on investment positions as of February 1, 2014, a hypothetical 100 basis point increase in interest rates across all maturities would result in a $13.8 million decline in the fair market value of the portfolio. Due to our positive cash flow from operations, the relatively short-term nature of our investment portfolio and our ability to hold investments to maturity, such change in fair market value would likely not have resulted in any cash flow impact.

As of February 1, 2014, our investment portfolio included $19.2 million in par value of auction rate securities. Beginning in February 2008, liquidity issues in the global credit markets resulted in a failure of auction rate securities, as the amount of securities submitted for sale in those auctions exceeded the amount of bids. Since this time, many of the issuers have refinanced their debt and paid down the auction rate securities which have resulted in a smaller pool of outstanding securities. Although these securities have continued to pay interest and show an improvement in the underlying collateralization, there is currently limited trading volume. To estimate the fair value of the auction rate securities, we use a discounted cash flow model based on estimated timing and amount of future interest and principal payments. In developing the cash flow model, we consider the credit quality and liquidity of the underlying securities and related issuer, the collateralization of underlying security investments and other considerations. As of February 1, 2014 the fair value of auction rate securities in our investment portfolio was $2.9 million less than par value and the fair value was recorded in long-term investments.

Based on our balance of approximately $2.0 billion in cash, cash equivalents and short-term investments, and the fact that we continue to generate positive cash flow on a quarterly basis, we do not anticipate having to sell these securities below par value and do not have the intent to sell these auction rate securities until recovery. Since we consider the impairment to be temporary, we recorded the unrealized loss to accumulated other comprehensive income, a component of shareholders’ equity.