Spansion Inc.
Form 10-K
February 12, 2010
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.
For the fiscal year ended December 27, 2009

OR

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.
For the transition period from to

Commission File Number 000-51666

SPANSION INC.

(DEBTOR-IN-POSSESSION)

(Exact name of registrant as specified in its charter)

Delaware	**20-3898239**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

915 DeGuigne Drive

P.O. Box 3453

Sunnyvale, CA 94088

(408) 962-2500

(Address, including zip code, and telephone number, including area code, of registrant s principal executive offices)

Securities registered pursuant to Section 12(b) of the Act:

None

Securities registered pursuant to Section 12(g) of the Act:

Title of each class
Class A Common Stock, $0.001 Par Value Per Share

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ¨ No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ¨ No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ¨

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 (section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ¨ 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 definition of accelerated filer, large accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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

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

The aggregate market value of Class A Common Stock (Common Stock) held by non-affiliates of the registrant based upon the closing sale price as reported on The Pink Sheets on June 26, 2009 was approximately $10.3 million. Shares held by each executive officer, director and by each person who owns 10 percent or more of the outstanding Common Stock have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Section 12, 13, or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes ¨ No ¨

The number of shares outstanding of each of the registrant s classes of common stock as of the close of business on February 11, 2010:

Class	Number of Shares
Class A Common Stock, $0.001 par value	162,441,984

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the Annual Meeting of Stockholders, which we expect will be held on or about May 28, 2010, or 2010 Proxy Statement, are incorporated by reference into Part III hereof.

Table of Contents

Spansion Inc.

(Debtor-in-Possession)

FORM 10-K

For The Fiscal Year Ended December 27, 2009

INDEX

Table of Contents

PART I

Cautionary Statement Regarding Forward-Looking Statements

This Annual Report on Form 10-K contains forward-looking statements. These statements relate to future events or our future financial performance. Forward-looking statements may include words such as may, will, should, expect, plan, intend, anticipate, believe, estimate, predict, potential, continue or other wording indicating future results or expectations. Forward-looking statements are subject to risks and uncertainties, and actual events or results may differ materially. Factors that could cause our actual results to differ materially include, but are not limited to, those discussed under Risk Factors in this report as well as risks and uncertainties relating to our Creditor Protection Proceedings including our ability to: generate cash from operations and maintain adequate cash on hand; continue to maintain cash management arrangements; attract and retain customers or avoid reduction in, or delay or suspension of, customer orders as a result of the uncertainty caused by the Creditor Protection Proceedings; maintain market share, as competitors move to capitalize on customer concerns; retain or replace major suppliers on acceptable terms and avoid disruptions in our supply chain; maintain relationships with reseller partners, joint venture partners and strategic alliance partners; retain and motivate key employees and attract new employees; actively and adequately communicate on and respond to events, media and rumors associated with the Creditor Protection Proceedings that could adversely affect our relationships with customers, suppliers, partners and employees; obtain court orders or approvals with respect to motions filed from time to time; prevent third parties from obtaining court orders or approvals that are contrary to our interests; resolve ongoing issues with creditors and other third parties whose interests may differ from ours; develop, obtain required approvals for and successfully implement a plan of reorganization; obtain sufficient exit financing to support a plan of reorganization; and realize full or fair value for any assets or business that may be divested as part of a reorganization. We also face risks and uncertainties associated with: limitations or actions against any Debtor during the Chapter 11 Cases; the values, if any, that will be prescribed pursuant to any plan of reorganization to outstanding Spansion securities; the uncertainty of the existence of a trading market in our shares of common stock; claims not discharged in the Chapter 11 Cases and their effect on our results of operations and profitability; our substantial indebtedness and its impact on our financial health and operations; fluctuations in foreign currency exchange rates; the sufficiency of workforce and cost reduction initiatives and risks and uncertainties relating to our business including our ability to: successfully focus on and pursue the embedded portion of the Flash memory market; maintain our improved gross margins and continue to implement successfully our cost reduction efforts; control our operating expenses, particularly our sales, general and administrative costs; obtain additional financing in the future; obtain materials in support of our business at terms favorable to us; retain and expand our customer base in our focus markets and retain and grow our share of business within our customer base; successfully introduce our next generation products to market in a timely manner; effectively and timely achieve volume production of our next generation products; increase market acceptance of our products based on our MirrorBit technology; penetrate further the Flash memory market with our high density products and expand the number of customers in emerging markets; successfully develop and transition to the latest technologies; develop our MirrorBit NAND architecture, introduce new products based on these architectures, and achieve customer acceptance of these products; develop systems-level solutions that provide value to customers of our products; enter new markets not traditionally served by Flash memory; negotiate successfully patent and other intellectual property licenses and patent cross-licenses and acquire additional patents; and effectively manage, operate and compete in the current sustained economic downturn and extraordinarily volatile market conditions effected in part by cautious capital spending by our customers as they face their own economic challenges. We undertake no obligation to revise or update any forward-looking statements to reflect any event or circumstance that arises after the date of this Report, or to conform such statements to actual results or changes in our expectations.

Table of Contents

ITEM 1. BUSINESS
Overview

We are a semiconductor device company that is principally dedicated to designing, developing, manufacturing, marketing and selling NOR Flash memory products and solutions. We sell our NOR Flash memory products to approximately 4,500 customers worldwide. Our products are used in a wide range of applications, including automotive electronics such as navigation systems and engine control, PC and peripheral computing equipment such as printers, consumer equipment such as set top boxes and home networking, communication equipment such as enterprise networking and cellular infrastructure, arcade gaming equipment, industrial control equipment and mobile phones. For fiscal 2009, our net sales were approximately $1.4 billion and our net loss was approximately $514.1 million compared to net sales of approximately $2.3 billion and net loss of approximately $2.4 billion for fiscal 2008.

We are headquartered in Sunnyvale, California, with research and development, manufacturing and assembly operations in the United States, Middle East, Europe, and Asia. We operate one Flash memory fabrication facility located in Austin, Texas and two assembly and test facilities in Bangkok, Thailand and Kuala Lumpur, Malaysia. We also operate a facility in Penang, Malaysia which is used for sort services. For financial information about geographic areas and for information with respect to our sales, refer to the information set forth in Part II, Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations, beginning on page 45, below.

Our mailing address and executive offices are located at 915 DeGuigne Drive, Sunnyvale, California 94088, and our telephone number is (408) 962-2500. References in this report to Spansion, we, us, our, or the Company shall mean Spansion Inc. and our consolidated subsidiar unless the context indicates otherwise. We are subject to the information and periodic reporting requirements of the Securities Exchange Act of 1934, or Exchange Act, and, in accordance therewith, file periodic reports, proxy statements and other information with the Securities and Exchange Commission, or SEC. Such periodic reports, proxy statements and other information is available for inspection and copying at the SEC s Public Reference Room at 100 F Street, NE., Washington, DC 20549 or may be obtained by calling the SEC at 1-800-SEC-0330. In addition, the SEC maintains a Web site at *http://www.sec.gov* that contains reports, proxy statements and other information regarding issuers that file electronically with the SEC. We also post on the Investor Relations page of our Web site, *www.spansion.com*, a link to our filings with the SEC, our Code of Ethics for our Chief Executive Officer, Chief Financial Officer, Corporate Controller and other Senior Finance Executives, our Code of Business Conduct, which applies to all directors and all our employees, and the charters of our Audit, Compensation, Finance and Nominating and Corporate Governance committees. Our filings with the SEC are posted as soon as reasonably practical after they are filed electronically with the SEC. Please note that information contained on our Web site is not incorporated by reference in, or considered to be a part of, this document. You can also obtain copies of these documents free of charge by writing to us at: Corporate Secretary, Spansion Inc., 915 DeGuigne Drive, Sunnyvale, California 94088, or emailing us at: *Corporate.Secretary@spansion.com*.

Our Industry

During the last ten years, Flash memory has become a broadly familiar solution for common applications such as Flash memory cards for digital cameras, memory sticks for computer file storage and music storage in portable MP3 music players. Moreover, during the past twenty years, Flash memory has also become a critical embedded component in other applications, such as automotive, computing, consumer, gaming, telecommunication, networking, industrial and mobile phone electronic equipment. It is this type of embedded Flash memory that we primarily manufacture and sell to our customers, which include original equipment manufacturers, or OEMs, and original design manufacturers, or ODMs.

There are two primary types of Flash memory, NOR and NAND. The terms NOR and NAND refer to the architecture of the connections between the memory cells of the device which produce the different characteristics of the two memory types. According to iSuppli, as of December 2009, products classified as

Table of Contents

NAND Flash memory are the largest and fastest growing category of the Flash memory market, with estimated 2009 revenues of approximately $13.7 billion and a projected 12 percent compound annual growth rate (CAGR) from 2009 to 2012.

NAND Flash memory offers a number of desirable attributes: it is relatively inexpensive, a small device can hold a large amount of information, and its performance characteristics are particularly well suited for data storage such as music, pictures and video. The market for NAND Flash memory has grown rapidly in recent years as a result of the increasing popularity of devices that consumers can use to access their personal media in a portable, battery-powered format.

In contrast, NOR Flash memory supports the operation or execution of software code directly from the device as its read times are very fast and its architecture can better support software execution, enabling a more efficient and cost effective design in some applications. According to iSuppli, as of December 2009, products classified as NOR Flash memory had estimated 2009 revenues of approximately $4.4 billion and a negative one percent (-1%) projected CAGR from 2009 to 2012. Although NOR Flash memory is generally more expensive than NAND Flash memory at comparable densities, it is also available in much lower densities with lower prices than NAND Flash memory and primarily for this reason it is preferred in many applications that do not require the greater storage capacity that NAND Flash memory provides. At higher densities, we believe that the high reliability and ease of use of NOR Flash memory, in addition to its ability to support a more efficient and cost effective memory sub-system in certain applications such as consumer, arcade gaming, telecommunications, networking and industrial control electronics, drive NOR Flash memory use in embedded applications. For example, automobiles use NOR Flash memory for engine control, transmission control, anti-lock brake systems, anti-roll systems and other operations in the vehicle. NOR Flash memory is also used in many other applications, including mobile phone, computing, arcade gaming, telecommunications, networking, consumer and industrial electronic equipment.

The total market for memory systems and devices used in electronic systems is quite large, typically $50 billion or greater per year. Large, well-entrenched suppliers compete vigorously within a number of segments and across segments. Technology advances rapidly and suppliers have active development programs to enhance the features and capabilities of their respective product offerings. Thus, characteristics that traditionally divide market segments can change over time. In the case of Flash memory, system designers have devised systems where NAND Flash memory can replace traditional NOR Flash memory, which in certain applications yields acceptable reliability and performance at a lower overall cost. This example illustrates a general characteristic of technology-centric industries and the memory industry in particular: advancing technology creates market share dislocations. Thus, while NOR Flash has traditionally held well-established positions in certain applications, it may be possible in the future to expand its use into other applications, and, conversely, there is no guarantee that existing positions will not be reduced. The challenge participants face in competing in this industry is to leverage existing capabilities in creative ways to create value for customers.

Our Business

Historically, we derived 50 percent or more of our net sales from cell phone manufacturers, or the wireless market. During the last decade, the dynamics of that market changed as a result of increasing feature sets that drove demand for data storage favoring implementation of NAND over NOR architecture, and a consolidation of cell phone manufacturers. At the same time, in order to meet the demands of the wireless market, we were required to increase investment in research and development and leading edge wafer manufacturing capability in the face of rapidly declining prices. These changes eroded our profitability to unsustainable levels. As a result of this and other factors, we filed for bankruptcy protection in March 2009 as described in more detail below under the heading, Creditor Protection Proceedings.

Shortly after commencing bankruptcy proceedings, we began exiting a large portion of the wireless market. While this significantly reduced our net sales, it allowed us to dramatically reduce our research and development expenses without impairing our ability to compete in other markets. Our exit from a large portion of the wireless

Table of Contents

market, related reductions in research and development expenses and capital expenditures, combined with other cost reductions including disposal of manufacturing facilities, enabled us to begin generating positive cash flow. We achieved modest profitability in the second half of fiscal 2009 even as our net sales contracted approximately 40 percent from historical run-rates.

We are now pursuing a business model that requires significantly less capital expenditures as we rely on a combination of internal and external manufacturing capacity (fab lite strategy). We believe this transition to utilization of outsourced manufacturing capacity will enable us to maintain a long-term, stable supply of new and existing products for customers. In addition, we have further streamlined our business by (i) reducing headcount globally, (ii) exiting certain less profitable markets, and (iii) focusing primarily on the embedded portion of the Flash memory market. We continue to have leading market share and remain dedicated to, and focused on, the embedded market, i.e., the market for NOR Flash memory used for code storage in industrial, consumer, communications, gaming, and automotive applications. We intend to continue to selectively engage in portions of the wireless market where we can do so advantageously. We believe that though the embedded market is mature and will grow more slowly than some other sectors of the semiconductor industry, we can compete successfully with our continued focus on providing best in class customer service, quality and reliability, and solutions engineering. We believe we can mitigate the historical and anticipated trend of rapid selling price reductions by serving applications with growing unit demand, migrating customers to higher density and more feature-rich devices, capturing market share, and expanding our product offerings.

Creditor Protection Proceedings

On February 10, 2009, Spansion Japan Limited, a wholly-owned subsidiary of Spansion LLC (Spansion Japan), filed a proceeding under the Corporate Reorganization Law (*Kaisha Kosei Ho*) of Japan to obtain protection from Spansion Japan s creditors (the Spansion Japan Proceeding), and the Tokyo District Court approved the filing of the Spansion Japan Proceeding on March 3, 2009 (the Commencement Date), and appointed the incumbent representative director of Spansion Japan as trustee.

On March 1, 2009 (the Petition Date), Spansion Inc., Spansion Technology LLC, Spansion LLC, Spansion International, Inc. and Cerium Laboratories LLC (the Debtors), each filed a voluntary petition for relief under Chapter 11 of the U. S. Bankruptcy Code in the U. S. Bankruptcy Court for the District of Delaware (the Chapter 11 Cases). The Chapter 11 Cases, together with the Spansion Japan Proceeding are referred to collectively as the Creditor Protection Proceedings.

We continue to operate our businesses as debtors-in-possession under jurisdiction of the U.S. Bankruptcy Court and in accordance with the applicable provisions of the U.S. Bankruptcy Code and orders of the U.S. Bankruptcy Court. Non-U.S subsidiaries that are not included in the Creditor Protection Proceedings continue to operate without the supervision of the U.S. Bankruptcy Court.

Plan of Reorganization

On October 26, 2009, we filed with the U.S. Bankruptcy Court a proposed Plan of Reorganization, together with an accompanying Disclosure Statement. On each of November 25, 2009 and December 9, 2009, we filed an amended proposed Plan of Reorganization together with an accompanying amended Disclosure Statement. On December 17, 2009, we filed a Second Amended Joint Plan of Reorganization Dated December 16, 2009 (as the same may be amended from time to time, the Plan of Reorganization) and accompanying amended Disclosure Statement. The Plan of Reorganization provides for an equitable distribution to holders of allowed claims in certain classes of creditors, preserves the value of the Debtors businesses as going concerns and preserves employment. The Plan of Reorganization, if accepted by the requisite majorities of one or more of the affected class of creditors and approved by the U.S. Bankruptcy Court (and any applicable appellate courts if the order of the U.S. Bankruptcy Court approving the Plan of Reorganization is appealed), would be binding on all creditors within each affected class, including those that did not vote to accept the proposal. The ultimate recovery to creditors will not be determined until the Plan of Reorganization has been effectuated and all claims have been fully adjudicated or resolved.

Table of Contents

Under the Plan of Reorganization, the Debtors will be reorganized (Reorganized Debtors) through the consummation of several transactions in which new securities of the Reorganized Debtors will be issued and distributed in accordance with the Plan of Reorganization. These transactions will include:

- the distribution of cash, new senior notes or cash raised through a rights offering and/or debt issuance, providing that such cash is raised no later than the confirmation date for the Plan of Reorganization, to holders of the Company s existing Floating Rate Notes;

- the distribution of new Spansion common stock to holders of general unsecured claims;

- the cancellation of Spansion Inc. s existing equity securities, including all shares of Common Stock and existing options to purchase shares of Common Stock; and

- the retention of the assets of the Debtors in the reorganized Debtors.

The Plan of Reorganization provides for the treatment of claims of creditors on a waterfall basis that allocates value to the Debtors creditors and stockholders in accordance with the priorities of the Bankruptcy Code. Pursuant to the Plan of Reorganization, allowed administrative claims and priority tax claims would be paid in full in cash or cash equivalents. Other allowed secured claims would be reinstated, paid in full in cash or have the collateral securing such claims returned to the secured creditor. Allowed unsecured convenience claims (in an amount equal to, less than or reduced to $2,000) would be paid in full in cash. Any remaining value would be distributed on a pro rata basis, subject to any applicable subordination agreements, to holders of allowed unsecured claims (other than certain claims, including claims based on non-compensatory damages and penalties and intercompany claims) in the form of new Spansion common stock. Under the Plan of Reorganization, our current stockholders will not be entitled to any recovery, making such shares of common stock valueless.

As set forth in the Second Amended Disclosure Statement, the Debtors have assumed that allowed claims will range from approximately $1.6 billion to approximately $2.1 billion after completion of the claims objection, reconciliation and resolution process. In addition to the range specified above, Spansion Japan has asserted that it has been damaged as a result of the foundry agreement rejection in the amount up to $761.2 million. As of December 27, 2009, we accrued expected allowed claims totaling $1.8 billion classified as liabilities subject to compromise in the accompanying balance sheet. If the expected amount of allowed claims increases over the amount currently accrued, we will record additional reorganization expense in the period of such determination. Because disputed claims have not yet been finally adjudicated, and the Debtors total enterprise value upon emergence has not yet been finally determined, no assurances can be given that actual recoveries to creditors and interest holders will not be materially higher or lower than proposed in the Plan of Reorganization.

On December 18, 2009, the U.S. Bankruptcy Court approved the adequacy of the Disclosure Statement, the solicitation and notice procedures with respect to confirmation of the Plan of Reorganization and the form of various ballots and notices in connection therewith. The U.S. Bankruptcy Court established December 14, 2009, as the record date for determining eligibility to vote on the Plan of Reorganization. Nothing contained in this Report is intended to be, nor should it be construed as, a solicitation for a vote on the Plan of Reorganization.

The Plan of Reorganization will become effective only if it is confirmed by the U.S. Bankruptcy Court. The objection deadline with respect to the Plan of Reorganization occurred January 26, 2010, subject to extensions agreed to by the Debtors for certain parties. The voting deadline with respect to the Plan of Reorganization was February 8, 2010. The confirmation hearing in the U.S. Bankruptcy Court is scheduled to begin on February 24, 2010. If the U.S. Bankruptcy Court confirms the Plan of Reorganization, the Debtors expect to emerge from Chapter 11 shortly thereafter. However, there can be no assurance that the Debtors will be successful in obtaining the necessary votes to approve the Plan of Reorganization, that the U.S. Bankruptcy Court will confirm the Plan of Reorganization or that it will be implemented successfully.

Table of Contents

Business Relationship with Spansion Japan and Foundry Agreement

Spansion Japan is now managed by a trustee appointed by the Tokyo District Court and is subject to the general supervision of the Tokyo District Court and a court appointed supervisory attorney. As a result, the financial results of Spansion Japan are no longer included in our consolidated financial results for periods beginning March 3, 2009. Because Spansion Japan s results are still consolidated for periods prior to March 3, 2009, we do not believe that a comparison of financial results spanning this date is meaningful. The effect of the deconsolidation at March 3, 2009 was a $30.1 million gain representing the difference between the carrying value of our investment in and net accounts receivable from Spansion Japan and the fair value of our retained non-controlling interest in Spansion Japan, which was valued at zero.

Spansion Japan facilitates distribution of our products in Japan and also manufactures and supplies sorted and unsorted silicon wafers to us. The wafers purchased from Spansion Japan are a material component of our cost of goods sold, and historically the wafer prices were governed by a foundry agreement. We believe that the prices under the foundry agreement greatly exceeded the amounts that the U.S. Bankruptcy Court would have required us to pay for wafers purchased during the period from February 9, 2009 (20 days prior to the Petition Date) through October 27, 2009 (the Disputed Period). We and Spansion Japan mutually agreed to pricing terms for purchases following October 27, 2009.

After our efforts to renegotiate the prices for the Disputed Period proved unsuccessful, we filed a motion with the U.S. Bankruptcy Court in October 2009 to reject the foundry agreement because the foundry agreement was no longer consistent with our business plan. An order rejecting the foundry agreement was issued by the U.S. Bankruptcy Court on November 19, 2009. As a result, there was no valid contract establishing pricing for the wafers we received from Spansion Japan from February 9, 2009 through October 27, 2009.

On January 8, 2010, we reached an agreement in principle (the Settlement) with Spansion Japan to (i) acquire Spansion Japan s distribution business; (ii) obtain foundry services, including wafer and sort services, from Spansion Japan; and (iii) resolve our dispute with Spansion Japan relating to pricing of wafers purchased during the Disputed Period. The Settlement remains subject to the completion of definitive agreements. On January 29, 2010, the U.S. Bankruptcy Court and on February 1, 2010, the Tokyo District Court approved the Settlement. We expect the definitive agreements implementing the Settlement to be executed in February 2010 and to provide for, among other things, the following material terms:

- Payment to Spansion Japan of approximately $45 million during the four quarters of fiscal 2010;
- Agreement to purchase from Spansion Japan (i) a minimum of 10 billion yen (equivalent to $109.5 million as of December 27, 2009) of wafers over the next six quarters, and (ii) sort services during the six-quarter period with both sort services and wafer production to be subject to normal and customary foundry performance conditions;
- The purchase of Spansion Japan s distribution and research and development business located in Kawasaki, Japan for approximately $12.5 million;
- The claims of the Debtors against Spansion Japan arising prior to February 9, 2009, will be deemed allowed unsecured non-priority claims in the Spansion Japan s corporate reorganization proceeding, but the Debtors will not be entitled to receive any distribution on account of such claims;
- Spansion Japan shall retain its rejection damage claims against the Debtors in respect of the rejection of the Foundry Agreement, subject to our various defenses described in further detail below; and
- All other claims of Spansion Japan and the Debtors against each other shall be expunged, released and satisfied.

On January 15, 2010, Spansion Japan filed a general unsecured proof of claim in the U.S. Bankruptcy Court asserting that it has been damaged in the amount of approximately $761 million as a result of the November 19, 2009 foundry agreement rejection order. We believe we have strong defenses to the amount of Spansion Japan s

proof of claim, and we intend to vigorously contest this matter. An award of damages resulting from the rejection of the foundry agreement could impact our future earnings. However, under the Plan of Reorganization, Spansion Japan would not be entitled to any recovery on such proof of claim. Nonetheless, if the U.S. Bankruptcy Court found that such claim were more appropriately classified as a general unsecured claim in Class 5B of the Plan of Reorganization, Spansion Japan would be entitled, at most, to its pro-rata distribution of new Spansion common stock.

Although we have agreed to the Settlement with Spansion Japan regarding certain issues outlined in this Report, there is risk in continuing to do business with Spansion Japan due to the uncertainty of whether Spansion Japan will successfully reorganize. The current deadline for Spansion Japan to submit a plan of reorganization to the Tokyo District Court is February 24, 2010. We can provide no assurance that Spansion Japan s plan of reorganization will be approved, or that Spansion Japan will not be liquidated. As a result, we have plans to either replace with in-house capabilities the services that Spansion Japan provides or to utilize another third party for such services in order to mitigate the impact that would result if for any reason Spansion Japan reduced its supply of, or ceased supplying, the goods and services to us. Nevertheless, a sudden and unanticipated reduction or cessation of the supply of goods and services from Spansion Japan would likely be disruptive and have an adverse impact on our results of operations and that impact could be material.

Our Products and Technology

Our current product portfolio offers densities ranging from 1-megabit to 2-gigabits and a broad array of interfaces and features. We have developed two Flash memory technologies, single-bit-per-cell floating gate technology and one-, two- or more-bit-per-cell MirrorBit technology, our proprietary charge trapping non-volatile memory technology. Our current MirrorBit products are based primarily on two-bits per cell and allow us to offer a broad range of product configurations and capabilities, including high read performance and high reliability. Compared to competing floating gate multilevel cell NOR technology, two-bit-per-cell MirrorBit technology has a simpler cell architecture requiring fewer manufacturing steps and supporting higher yields, resulting in lower costs. The majority of our new product designs and revenue are based on MirrorBit technology.

Our products that are designed primarily for code storage and execution are based on NOR Flash memory architecture and utilize either traditional floating gate technology or our MirrorBit technology. We have created and own fundamental intellectual property in both floating gate and MirrorBit technologies.

Floating Gate Technology

Floating gate is the conventional memory cell technology that is utilized by most Flash memory companies today for both NOR and NAND products. We have created innovations in floating gate technology that have become industry standards, such as negative gate erase, single power supply and embedded programming algorithms, and we continue to hold a strong position in the NOR Flash memory segment with our products based on floating gate technology. Our products using floating gate technology are typically used for code storage in applications requiring very high read speeds or the ability to operate at extreme temperatures in harsh environments such as those found in automotive applications.

MirrorBit Technology

To achieve storage density of two bits per cell, we developed MirrorBit NOR technology. MirrorBit NOR technology stores two distinct charges in a single memory cell, with each charge equivalent to one bit of data thereby at least doubling the density, or storage capacity, of each memory cell and enabling higher density, lower cost products. MirrorBit technology, which enables the storage of charge without it diffusing, moving or flowing, is generally referred to as charge trapping technology. MirrorBit technology is the foundation for our product roadmap.

Table of Contents

Sales and Marketing

We market and sell our products worldwide under the Spansion trademark. Since the beginning of the second quarter of fiscal 2006, we have sold our products to our customers directly or through distributors. We rely on Fujitsu to act as our largest distributor in Japan and our nonexclusive distributor throughout the rest of the world, other than Europe and the Americas, with limited exceptions.

We market our products through a variety of direct and indirect channels. We have direct relationships with many of our top customers worldwide. We supplement this effort with programs designed to support design-in of our products on reference designs, which are typically used by our Flash memory customers when choosing Flash memory solutions. In addition, we focus a portion of our marketing efforts on providers of complementary products to ensure our products interoperate effectively with the most widely used components in various embedded applications.

Our marketing activities targeting customers, reference design houses and our potential partners include a combination of direct marketing activities such as trade shows, events and marketing collateral and indirect activities such as public relations and other marketing communications activities.

Customers

We serve our customers worldwide directly or through our distributors, including Spansion Japan and Fujitsu, who buy products from us and resell them to their OEMs and ODMs, either directly or through their own distributors. Customers for our products consist of OEMs, ODMs and contract manufacturers. After the deconsolidation of Spansion Japan as discussed above, in fiscal 2009, sales to Spansion Japan accounted for approximately 21 percent of our total net sales. Spansion Japan resells substantially all its purchases to Fujitsu who in turn acts as a distributor of our products in Japan. No OEM, ODM or contract manufacturer accounted for more than ten percent of our net sales for fiscal 2009. We believe that our recent decision to focus on the embedded portion of the Flash memory market will reduce our customer concentration in the future. For fiscal 2008, Nokia Corporation accounted for approximately 18 percent of our net sales, and for fiscal 2008 and fiscal 2007, Fujitsu accounted for approximately 29 percent and 35 percent of our net sales. Net sales to Fujitsu (in its capacity as a distributor) for fiscal 2009, including sales made through Spansion Japan after its deconsolidation, accounted for approximately 24 percent of our total net sales. We did not have significant transactions directly with Fujitsu for the period from March 3, 2009 through December 27, 2009 as we transacted with Fujitsu through our intermediary Spansion Japan.

Original Equipment Manufacturers

OEMs consist primarily of foreign and domestic manufacturers of mobile phones, consumer electronics, automotive electronics and networking equipment companies, selected regional accounts and customers in other target applications.

Third-Party Distributors

Our third-party distributors typically resell to OEMs, ODMs and contract manufacturers. Sales through our direct distributors are typically made pursuant to agreements that provide return rights for discontinued products or for products that are not more than twelve months older than their manufacturing date code. In addition, some of our agreements with distributors may contain standard stock rotation provisions permitting limited levels of product returns.

We generally warrant that products sold to our customers and our distributors will, at the time of shipment, be free from defects in workmanship and materials and conform to our approved specifications. Subject to specific exceptions, we offer a one-year limited warranty.

Table of Contents

Research and Development

Research and development is critical to our success and is focused on process, product and system level development. We conduct our product and system engineering activities primarily in Sunnyvale, California and Netanya, Israel, with additional design and development engineering teams located in the United States, Europe and Asia. Our primary development focus is on MirrorBit products for embedded applications. We conduct our process development primarily in Sunnyvale, California, at our fabrication facility located in Austin, Texas (Fab 25) and at third party foundries that provide foundry services to us. We are developing non-volatile memory process technologies with continuing refinement of our 65-nanometer process technology and plans for deployment of 45-nanometer and more advanced technology. In April 2009, we stopped further production of development wafers at our research and development manufacturing facility known as the Sub-micron Development Center, or SDC, in Sunnyvale, California, as part of our strategy to reduce research and development costs by utilizing third party foundries for process development.

Our research and development expenses for fiscal 2009, fiscal 2008 and fiscal 2007 were approximately $136.4 million, $431.8 million and $436.8 million, respectively. For more information, see Part II, Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations.

Manufacturing

We own and operate one wafer fabrication facility in Austin, Texas (Fab 25), which has approximately 114,000 square feet of clean room space. This facility produces 200-millimeter wafers, manufactured using 110-nanometer, 90-nanometer and 65-nanometer process technology. We also own two assembly and test facilities in Bangkok, Thailand and in Kuala Lumpur, Malaysia, and we use a number of third party companies to provide supplemental final manufacturing services for us. We own a third facility in Penang, Malaysia which is currently utilized for sort services.

We plan to outsource production of more advanced technology nodes and a significant portion of our manufacturing function to external foundry partners. To augment our internal wafer fabrication capacity, we have foundry agreements with Semiconductor Manufacturing International Corporation, or SMIC, Fujitsu Limited and Spansion Japan . The arrangement with SMIC provides flexibility to support customer demand for advanced technology products at 65-nanometer if we are unable to support such demand from our own in house capacity. Also, the deployment of leading edge technology in support of foundry manufacturing provides a more cost efficient solution for future research and development wafer production as an alternative to an in house dedicated research and development manufacturing facility for wafer production. The arrangement with Fujitsu Limited, using our former JV1 and JV2 wafer fabrication facilities which we sold to them in April 2007, provides us with the ability to efficiently support the declining customer demand for legacy products on legacy production process nodes. The arrangement with Spansion Japan has evolved over time. Historically, Spansion Japan provided us foundry services. As discussed above, on January 8, 2010, we agreed to the Settlement with Spansion Japan. Under the terms of the Settlement, we will, among other things, obtain foundry services, including wafer and sort services, from Spansion Japan. In September 2009, we sold to Powertech Technology Inc. (PTI) our final manufacturing facility located in Suzhou, China, and certain related equipment. Following the sale, PTI began providing final manufacturing services to us at the Suzhou facility, further representing our shift to an outsourced manufacturing model. We may in the future change the location where our products are manufactured to reflect changes in customer demand. We have in the past, and may in the future, obtain foundry, subcontractor and other arrangements with third parties to meet demand.

Our manufacturing processes require many raw materials, such as silicon wafers, mold compound, substrates and various chemicals and gases, and the necessary equipment for manufacturing. We obtain these materials and equipment from a large number of suppliers located throughout the world.

Table of Contents

Environmental Matters

Many of our facilities are located on properties or in areas with a long history of industrial activity. Prior to our reorganization in 2003, environmental audits were conducted for each of our manufacturing facilities. The audits described various conditions customary of facilities in our industry and, in particular, noted historical soil and groundwater contamination at our Sunnyvale, California facility arising from the leakage of chlorinated solvent storage tanks that previously had been located on this property. This property is listed on the U.S. Environmental Protection Agency s Superfund National Priorities List. AMD, as the former owner of the property, is investigating and remediating this contamination.

In connection with our reorganization in 2003, each of AMD and Fujitsu agreed to indemnify us against losses arising out of the presence or release, prior to June 30, 2003, of hazardous substances at or from these and other sites they each contributed to us. Conversely, our subsidiary agreed to indemnify each of AMD and Fujitsu from and against liabilities arising out of events or circumstances occurring after June 30, 2003, in connection with the operation of our business. AMD and Fujitsu, on the one hand, and we, on the other, agreed to indemnify the other against liability arising from permit violations attributable to our respective activities. To the extent AMD and Fujitsu cannot meet their obligations under any of their indemnity agreements, or material environmental conditions arise, we may be required to incur costs to address these matters, which could have a material adverse effect on us.

We have made and will continue to make capital and other expenditures to comply with environmental laws, but we do not expect compliance with environmental requirements to result in material expenditures in the foreseeable future. Environmental laws and regulations are complex, change frequently and have tended to become more stringent over time factors that could alter the current outlook. See Item 1A Risk Factors We are subject to a variety of environmental laws that could result in liabilities.

Competition

Our principal NOR Flash memory competitors are Numonyx B.V., Macronix International Co., Ltd. and Samsung Electronics Co., Ltd. We increasingly compete with NAND Flash memory manufacturers where NAND Flash memory has the ability to replace NOR Flash memory in customer applications. Our principal NAND Flash memory competitors include Samsung Electronics Co., Ltd., Numonyx B.V. and Micron Technology, Inc. In the future, our principal NAND Flash memory competitors may include Hynix Semiconductor Inc., Toshiba Semiconductor Company and SanDisk Corporation.

We believe Flash memory providers must also possess the following attributes to remain competitive:

- strong relationships with OEMs, ODMs and contract manufacturers that are acknowledged leaders within their respective industries;
- discipline to continually reduce costs ahead of historically declining semiconductor market prices;
- strong market focus to identify emerging Flash memory applications;
- leadership in research and development;
- flexibility in manufacturing capacity and utilization so as to take advantage of industry conditions through market cycles;
- access to the financial resources needed to maintain a highly competitive technological position;
- focus on sustainable and profitable segments;

the ability to establish and sustain strategic relationships and alliances with key industry participants;

the ability to manufacture products with a high degree of market acceptance and a low cost structure; and

rapid time to market for new products, measured by the time elapsed from first conception of a new product to its commercialization.

Table of Contents

Employees

After deconsolidation of Spansion Japan in March 2009 and combined workforce reductions of 3,200 employees in February, May and October 2009, we had approximately 3,400 employees at December 27, 2009.

Backlog

We generally manufacture and market standard lines of products. Consequently, a significant portion of our sales are made from inventory on a current basis. Sales are made primarily pursuant to purchase orders for current delivery or agreements covering purchases over a period of time. These orders or agreements may be revised or canceled without penalty. Generally, in light of current industry practice and experience, we do not believe that backlog information is necessarily indicative of actual sales for any succeeding period.

Intellectual Property

Our success depends in part on our proprietary technology. While we attempt to protect our proprietary technology through patents, copyrights and trade secrets, we believe that our success will depend more upon technological expertise, continued development of new products, and successful cost reductions achievable by improving process technologies. In addition, we have access to intellectual property through certain cross-license arrangements with AMD and Fujitsu. There can be no assurance that we will be able to protect our technology or that competitors will not be able to develop similar technology independently. We currently have a number of United States and foreign patents and patent applications. There can be no assurance that the claims allowed on any patents we hold will be sufficiently broad to protect our technology, or that any patents will issue from any application pending or filed by us. In addition, there can be no assurance that any patents issued to us will not be challenged, invalidated or circumvented or that the rights granted thereunder will provide competitive advantages to us.

Rights to Intellectual Property

We rely on a combination of protections provided by contracts, including confidentiality and non-disclosure agreements, copyrights, patents, trademarks and common law rights, such as trade secrets, to protect our intellectual property. Our U.S. patents are potentially valid and enforceable for either 17 years from the date they were issued or 20 years from the date they were filed. Accordingly, some of our existing patents will only survive for a few more years while others will survive for approximately another 15 years. We do not believe that the expiration of any specific patent will have a material adverse effect on us. In addition, the duration of our valid and enforceable trademarks is indefinite.

AMD and Fujitsu have each contributed to us various intellectual property rights pursuant to an Amended and Restated Intellectual Property Contribution and Ancillary Matters Agreement. Under this agreement, we became owners, or joint owners with each of Fujitsu and AMD, of certain patents, patent applications, trademarks, and other intellectual property rights and technology. AMD and Fujitsu reserved rights, on a royalty-free basis, to practice the contributed patents and to license these patents to their affiliates and successors-in-interest to their semiconductor groups. AMD and Fujitsu each have the right to use the jointly-owned intellectual property for their own internal purposes and to license such intellectual property to others to the extent consistent with their non-competition obligations to us. Subject to our confidentiality obligations to third parties, and only for so long as AMD s and Fujitsu s ownership interests in us remain above specific minimum levels, which ownership interests we expect will be reduced below such levels upon emergence from the Chapter 11 Cases in accordance with the Plan of Reorganization, we are obligated to identify any of our technology to each of AMD and Fujitsu, and to provide copies of and training with respect to that technology to them. In addition, we have granted a non-exclusive, perpetual, irrevocable, fully paid and royalty-free license of our rights in that technology to each of AMD and Fujitsu.

In connection with our reorganization in June 2003, we entered into separate patent cross-license agreements with each of AMD and Fujitsu in which we granted to AMD or Fujitsu, as applicable, and AMD or

Fujitsu, as applicable, each granted to us, non-exclusive licenses under certain patents and patent applications of their semiconductor groups to make, have made, use, sell, offer to sell, lease, import and otherwise dispose of specific semiconductor-related products anywhere in the world. The patents and patent applications that are licensed are those with an effective filing date prior to the termination of our patent cross-license agreements. Each agreement will automatically terminate on the later of June 30, 2013 or the date AMD s or Fujitsu s, whichever is the other party to the agreement, ownership interest in us is transferred or disposed of in its entirety. Each agreement may be terminated by a party on a change in control of the other party or its semiconductor group. The licenses to patents under license at the time of the termination will survive until the last such patent expires.

Under each agreement, in cases where there is a change of control of us or the other party (AMD or Fujitsu, or each of their semiconductor groups, as applicable), the other party shall have the right to terminate the agreement (or to invoke the provisions described in this paragraph if the agreement had been previously terminated) by giving 30 days written notice within 90 days after receiving notice of the change of control. If so terminated, the rights, licenses and immunities granted under the agreement will continue solely with respect to those licensed patents that are entitled to an effective filing date that is on or before, and are licensed as of, the date of such change of control, and will continue until the expiration of the last to expire of such licensed patents. Moreover, with respect to circuit patents, which are patents (other than process patents) covering elements relating to electrical signals to achieve a particular function, the rights, licenses and immunities granted to the party undergoing the change of control are limited solely to:

i. each existing and pending product of such party as of the date of change of control;

ii. each existing and pending product of the acquiring third party of such party as of the date of change of control that would have been in direct competition with products described in (i) above; and

iii. successor products of products described in (i) and (ii) above provided such successor product is based substantially on the same technology.

Beginning in November 2008, we no longer incurred royalties associated with licenses that survive the termination of the cross-license agreement. In both fiscal 2008 and fiscal 2007, we incurred royalty expenses of approximately $3 million to each of AMD and Fujitsu under their respective patent cross-license agreements.

We may be subject to claims that we are infringing intellectual property rights of third parties through the manufacture and sale of our products and the operation of our business. Therefore, absent negotiating our own license agreements with the third parties who own such intellectual property, we will be vulnerable to claims by such parties that our products or operations infringe such parties patents or other intellectual property rights.

We will continue to attempt to negotiate our own agreements and arrangements with third parties for intellectual property and technology that is important to our business. We will also attempt to acquire new patents as our success in negotiating patent cross-license agreements with other industry participants will depend in large part upon the strength of our patent portfolio relative to that of the third party with which we are negotiating.

Patents and Patent Applications

As of December 27, 2009, we had 1,442 U.S. patents and 740 foreign patents as well as 552 patent applications pending in the United States. We expect to file future patent applications in both the United States and abroad on significant inventions, as we deem appropriate. In addition, under our cross-license agreement with AMD, AMD granted us the right to use a substantial number of patents that AMD owns. Similarly, under our cross-license agreement with Fujitsu, Fujitsu also granted us the right to use a substantial number of patents that Fujitsu owns. There can be no assurance that the claims allowed on any patents we hold will be sufficiently broad to protect our technology, or that any patents will issue from any application pending or filed by us.

ITEM 1A. RISK FACTORS

You should carefully consider the risks described below and the other information in this Annual Report on Form 10-K. If any of the following risks materialize, our business could be materially harmed, and our financial condition and results of operations could be materially and adversely affected.

Certain statements in this report contain words such as could, expect, may, anticipate, will, believe, intend, estimate, plan, envision, seek and other similar language and are considered forward-looking statements. These statements are based on our current expectations, estimates, forecasts and projections about the operating environment, economies and markets in which we operate. In addition, other written or oral statements that are considered forward-looking may be made by us or others on our behalf. These statements are subject to important risks, uncertainties and assumptions, that are difficult to predict and actual outcomes may be materially different. The Creditor Protection Proceedings will have a direct impact on our business and exacerbate these risks and uncertainties. In particular, the risks described below could cause actual events to differ materially from those contemplated in forward-looking statements. Unless otherwise required by applicable securities laws, we do not have any intention or obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

The risks described below are not the only ones facing us. Additional risks not currently known to us or that we currently believe are immaterial may also impair our business, results of operations, financial condition and liquidity.

Risks Related to the Creditor Protection Proceedings

On February 10, 2009, Spansion Japan Limited, a wholly-owned subsidiary of Spansion LLC (Spansion Japan), filed a proceeding under the Corporate Reorganization Law (*Kaisha Kosei Ho*) of Japan to obtain protection from Spansion Japan s creditors (the Spansion Japan Proceeding); and the Tokyo District Court approved the filing of the Spansion Japan Proceeding on March 3, 2009 (the Commencement Date), and appointed the incumbent representative director of Spansion Japan as trustee. On March 1, 2009 (the Petition Date), Spansion Inc., Spansion LLC, Spansion Technology LLC, Spansion International, Inc. and Cerium Laboratories LLC each filed a voluntary petition for relief under Chapter 11 of the U. S. Bankruptcy Code in the U.S. Bankruptcy Court for the District of Delaware (the Chapter 11 Cases, together with the Spansion Japan Proceeding, the Creditor Protection Proceedings). The following risks relate to the Creditor Protection Proceedings.

Our business, operations and financial position are subject to the risks and uncertainties associated with the Chapter 11 Cases.

For the duration of the Chapter 11 Cases, our business, operations and financial position will be subject to the risks and uncertainties associated with such proceedings. These risks, without limitation and in addition to the risks otherwise noted in this Report, include:

Strategic risks, including risks associated with our ability to:

- stabilize the business to maximize the chances of preserving all or a portion of the enterprise;
- successfully focus on and pursue the embedded portion of the Flash memory market;
- resolve ongoing issues with creditors and other third parties whose interests may differ from ours;
- obtain creditor, court and any other requisite third party approvals for the Plan of Reorganization; and
- successfully implement the Plan of Reorganization.

Table of Contents

Financial risks, including risks associated with our ability to:

- generate cash from operations and maintain adequate available cash;
- continue to maintain currently approved intercompany lending and transfer pricing arrangements and ongoing deployment of cash resources throughout our company and subsidiaries in connection with ordinary course intercompany trade obligations and requirements;
- continue to maintain our cash management arrangements; and obtain any further approvals from the court, creditors or other third parties, as necessary to continue such arrangements;
- maintain research and development investments; and
- realize full or fair value for any assets or business we may divest as part of the Plan of Reorganization.

Operational risks, including risks associated with our ability to:

- continue to depend on Spansion Japan for wafer production and distribution of products in Japan due to actions taken by either (i) Spansion Japan (at the direction of the Spansion Japan trustee or pursuant to orders of the Tokyo District Court or otherwise) or (ii) Spansion Inc. or Spansion LLC (pursuant to the order of the U.S. Bankruptcy Court or otherwise);
- transfer wafer production capacity in-house or to a third-party foundry, or to find alternative methods of distributing and selling our products, in the event that Spansion Japan is not successful in, or has difficulties in reorganizing, and we are unable to negotiate a new foundry agreement with Spansion Japan;
- retain and attract customers despite the uncertainty caused by the Creditor Protection Proceedings;
- maintain market share generally and at specific customer accounts despite the uncertainty caused by the Creditor Protection Proceedings, including uncertainty surrounding future research and development expenditures, plans relating to the introduction of new products, price reductions and manufacturing;
- respond to competitors efforts to capitalize on customer concerns;
- operate our business effectively in consultation with the U.S. Bankruptcy Court and our creditors;
- actively and adequately communicate on and respond to events, media and rumors associated with the Creditor Protection Proceedings that could adversely affect our relationships with customers, suppliers, partners and employees;

- retain and incentivize key employees and attract new employees;
- retain, or if necessary, replace major suppliers on acceptable terms; and
- avoid disruptions in our supply chain as a result of uncertainties related to the Creditor Protection Proceedings.

Procedural risks, including risks associated with our ability to:

- obtain court orders or approvals with respect to motions we file from time to time, including motions seeking extensions of the applicable stays of actions and proceedings against us, or obtain timely approval of transactions outside the ordinary course of business, or other events that may require a timely reaction by us;
- resolve the claims made against us in such proceedings for amounts not exceeding our recorded liabilities subject to compromise;
- prevent third parties from obtaining court orders or approvals that are contrary to our interests, such as the appointment of a Chapter 11 trustee to replace our current management or the termination or shortening of the exclusivity period in the United States during which we can propose and seek confirmation of the Plan of Reorganization or the conversion of the Chapter 11 Cases to Chapter 7

Table of Contents

liquidation cases, in which case the U.S. Bankruptcy Court would sell the Debtors non-exempt property and distribute the proceeds to our creditors in accordance with the U.S. Bankruptcy Code; and

reject, repudiate or terminate contracts.

Because of these risks and uncertainties, we cannot predict the ultimate outcome of the restructuring process, or predict or quantify the potential impact on our business, financial condition or results of operations. The Chapter 11 Cases provide us with a period of time to attempt to stabilize our operations and financial condition and develop a plan of reorganization. It is not possible to predict the outcome of the Chapter 11 Cases and, as such, the realization of assets and discharge of liabilities are each subject to significant uncertainty. Accordingly, substantial doubt exists as to whether we will be able to continue as a going concern. Our independent registered public accounting firm has included a going-concern explanatory paragraph in its report on our consolidated financial statements for the year ended December 27, 2009.

Our continuation as a going concern is dependent upon, among other things, our ability to obtain confirmation or approval of, and implement, the Plan of Reorganization; generate cash from operations, maintain adequate cash on hand and obtain sufficient other financing during the Creditor Protection Proceedings and thereafter; resolve ongoing issues with creditors and other third parties; and achieve profitability. Even assuming a successful emergence from the Chapter 11 Cases, we cannot assure you as to the overall long-term viability of our reorganized operations, including our ability to generate sufficient cash to support our operating needs, fulfill our transformation objectives and fund continued investment in technology and product development without incurring substantial indebtedness that will hinder our ability to compete, adapt to market changes and grow our business in the future. In addition, we may not be able to secure financing necessary or desirable to facilitate our emergence from bankruptcy. The application of fresh start accounting principles in accordance with U.S. GAAP upon eventual emergence from bankruptcy may result in valuations of long-lived and intangible assets that are less than the carrying value of those assets as currently reflected in the financial statements, which may further hinder our ability to raise financing at or subsequent to emergence from the Chapter 11 Cases.

In addition, a long period of operating under the Chapter 11 Cases may exacerbate the potential harm to our business and further restrict our ability to pursue certain business strategies or require us to take actions that we otherwise would not. These challenges are in addition to business, operational and competitive challenges that we would normally face absent the Creditor Protection Proceedings.

If our settlement with Spansion Japan is not consummated or if our relationship with Spansion Japan is impaired or terminated as a result of the Creditor Protection Proceedings or other reasons , our business and financial condition could be materially and adversely affected.

Spansion Japan facilitates distribution of our products in Japan and also manufactures and supplies sorted and unsorted silicon wafers to us. The wafers purchased from Spansion Japan are a material component of our cost of goods sold, and historically the wafer prices were governed by a pre-petition foundry agreement, which was rejected in the Chapter 11 Cases. Thus, there was a dispute between us and Spansion Japan over pricing for the wafers we received from Spansion Japan for the period beginning February 9, 2009 through October 27, 2009 (the Disputed Period). On January 8, 2010, we reached an agreement in principle (the Settlement) with Spansion Japan to (i) acquire Spansion Japan s distribution business; (ii) obtain foundry services, including wafer and sort services, from Spansion Japan; and (iii) resolve our dispute with Spansion Japan relating to pricing of wafers purchased during the Disputed Period. The Settlement remains subject to completion of definitive agreements. On January 29, 2010, the U.S. Bankruptcy Court and on February 1, 2010, the Tokyo District Court approved the Settlement. We expect the definitive agreements to be executed in February 2010. If we are unable to consummate the Settlement with definitive agreements, we will be forced to pursue alternate arrangements for the distribution and sale of our products in Japan and to procure wafers and sort services from an alternate source.

On January 15, 2010, Spansion Japan filed a general unsecured proof of claim in the U.S. Bankruptcy Court asserting that it has been damaged in the amount of approximately $761 million as a result of the November 19, 2009

Table of Contents

foundry agreement rejection order. We believe we have strong defenses to the amount of Spansion Japan s proof of claim, and we intend to vigorously contest this matter. An award of damages resulting from the rejection of the foundry agreement could result in an impact to future earnings. However, under the Plan of Reorganization, Spansion Japan would not be entitled to any recovery on such proof of claim. Nonetheless, if the U.S. Bankruptcy Court found that such claim were more appropriately classified as a general unsecured claim in Class 5B of our proposed Plan of Reorganization, Spansion Japan would be entitled, at most, to its pro-rata distribution of new Spansion common stock.

Although we have agreed to the Settlement with Spansion Japan, there is risk in continuing to do business with Spansion Japan due to the uncertainty of whether Spansion Japan will successfully reorganize. The current deadline for Spansion Japan to submit a plan of reorganization to the Tokyo District Court is February 24, 2010. We can provide no assurance that Spansion Japan s plan of reorganization will be approved, or that Spansion Japan will not be liquidated. As a result, we have plans to either replace with in-house capabilities the services that Spansion Japan provides or to utilize another third party for such services in order to mitigate the impact that would result if for any reason Spansion Japan reduced its supply of, or ceased supplying, the goods and services to us. Nevertheless, a sudden and unanticipated reduction or cessation of the supply of goods and services from Spansion Japan would likely be disruptive and have an adverse impact on our results of operations and that impact could be material.

Continuing or increasing pressure on our business, cash and liquidity could materially and adversely affect our ability to fund and reorganize our business operations, react to and withstand the current economic downturn, as well as volatile and uncertain market and industry conditions, and implement the Plan of Reorganization. Additional sources of funds may not be available.

Historically, we have deployed our cash throughout the enterprise, through a variety of intercompany borrowing and transfer pricing arrangements. As a result of the Creditor Protection Proceedings, cash in the various jurisdictions is generally available to fund operations in the particular jurisdictions, but generally is not freely transferable between jurisdictions or regions, other than as highlighted in Liquidity and Capital Resources in the Management s Discussion and Analysis of Financial Condition and Results of Operations section of this Report. Thus, there is greater pressure and reliance on cash balances and generation capacity in specific regions and jurisdictions.

We cannot assure you that any further required court approvals for any future financing transactions will be obtained. Furthermore, we cannot assure you that we will be able to continue to maintain ongoing deployment of cash resources throughout our organization worldwide in connection with ordinary course intercompany trade obligations. If our subsidiaries are unable to pay dividends or provide us with loans or other forms of financing in sufficient amounts, or if we continue to have restrictions on the transfer of cash between us and our subsidiaries, including those imposed by courts, foreign governments and commercial limitations on transfers of cash, our cash position would likely be under considerable pressure and our liquidity and our ability to meet our obligations would be adversely affected.

Access to additional funds from liquidity-generating transactions or other sources of external financing may not be available to us and, if available, would be subject to market conditions and certain limitations including court approvals and other requisite approvals by other third parties. We cannot provide any assurance that our net cash requirements will be as we currently expect and will be sufficient for the successful confirmation and implementation of the Plan of Reorganization.

We may not be able to successfully obtain the U.S. Bankruptcy Court s confirmation of, or implement, the Plan of Reorganization. Failure to obtain the confirmation of, or failure to successfully implement, the Plan of Reorganization could lead to the liquidation of all of our assets. We must continue to restructure and transform our business and the assumptions underlying these efforts may prove to be inaccurate.

On October 26, 2009, we filed with the U.S. Bankruptcy Court a proposed Plan of Reorganization and an accompanying disclosure statement, and on each of November 25, 2009 and December 9, 2009, we filed with the

Table of Contents

U.S. Bankruptcy Court amended plans of reorganization and amended disclosure statements. On December 17, 2009, we filed a Second Amended Joint Plan of Reorganization dated December 16, 2009 (as amended from time to time, the Plan of Reorganization).

The Plan of Reorganization will become effective only if it is confirmed by the U.S. Bankruptcy Court. The objection deadline with respect to the Plan of Reorganization occurred January 26, 2010, subject to extensions agreed to by us for certain parties. The voting deadline with respect to the Plan of Reorganization was February 8, 2010. The confirmation hearing in the U.S. Bankruptcy Court is scheduled to begin on February 24, 2010. If the U.S. Bankruptcy Court confirms the Plan of Reorganization, we expect to emerge from Chapter 11 shortly thereafter. However, there can be no assurance that the U.S. Bankruptcy Court will confirm the plan of reorganization or that it will be implemented successfully.

In connection with the transformation of our business, we have made, and will continue to make, judgments as to whether we should further reduce, relocate or otherwise change our workforce. Costs incurred in connection with workforce reduction efforts may be higher than estimated. In addition, our workforce reduction efforts may impair our ability to achieve our current or future business objectives. Any further workforce efforts including reductions may not occur on the expected timetable and may result in the recording of additional charges.

Further, we have made, and will continue to make, judgments as to whether we should limit investment in, exit, or dispose of certain parts of our business. The Chapter 11 Cases may result in the sale or divestiture of assets, but we cannot assure you that we will be able to complete any sale or divestiture on acceptable terms or at all. Any decision by management to further limit investment in, or exit or dispose of parts of our business may result in the recording of additional charges. As part of our review of our restructured business, we look at the recoverability of tangible and intangible assets. Future market conditions may indicate these assets are not recoverable based on changes in forecasts of future business performance and the estimated useful life of these assets, and this may trigger further write-downs of these assets which may have a material adverse effect on our business, results of operations and financial condition.

While the Chapter 11 Cases are pending, our financial results may be volatile and may not reflect historical trends.

While the Chapter 11 Cases are pending, we expect our financial results to continue to be volatile as asset impairments, asset dispositions, restructuring activities, contract terminations and rejections and claims assessments may significantly impact our consolidated financial statements. As a result, our historical financial performance is likely not indicative of our financial performance following the filing of the Chapter 11 Cases. Further, we may sell or otherwise dispose of assets and liquidate or settle liabilities, with court approval, for amounts other than those reflected in our historical financial statements. Any such sale or disposition and the Plan of Reorganization could materially change the amounts and classifications reported in our historical consolidated financial statements, which do not give effect to any adjustments to the carrying value of assets or amounts of liabilities that might be necessary as a consequence of the Plan of Reorganization.

Our ability to independently manage our business is restricted during the Creditor Protection Proceedings, and steps or actions in connection therewith may require the approval of the U.S. Bankruptcy Court, the U.S. Trustee and our creditors.

Pursuant to the various U.S. Bankruptcy Court orders and the U.S Bankruptcy Code, during the Chapter 11 Cases, some or all of the decisions with respect to our business may require consultation with, review by or ultimate approval of the U.S. Bankruptcy Court and the U.S. Trustee, our general unsecured creditors committee and the Floating Rate Noteholders. For example, on January 22, 2010, a motion was filed in U.S. Bankruptcy Court to appoint a Chapter 11 trustee to replace or directly supervise current management. The lack of independence and the related consulting and reporting requirements have significantly increased the amount of time required for us to take necessary actions and conclude and execute on decisions, and may make it impossible for us to take actions that we believe are appropriate and necessary. We cannot assure you that the

Table of Contents

U.S. Bankruptcy Court, the U.S. Trustee, the Creditors Committee, other creditors or the Floating Rate Noteholders will support our positions on matters presented to the U.S. Bankruptcy Court in the future, or on the Plan of Reorganization. Disagreements between us and these various third parties could protract the Chapter 11 Cases, negatively impact our ability to operate and delay our emergence from the Chapter 11 Cases.

The Creditor Protection Proceedings have had a material adverse effect on our ability to continue operating as a globally integrated unit. Upon commencement of the Spansion Japan Proceeding, Spansion LLC, in its capacity as the sole stockholder of Spansion Japan, and Spansion Japan s board of directors lost operational control of, and management authority over, Spansion Japan. At that time, all such control and management was vested in the trustee appointed in the Spansion Japan Proceeding, under the supervision of the Tokyo District Court and a supervising attorney appointed by the Tokyo District Court.

In addition, although we have historically deployed our cash throughout the enterprise, through a variety of intercompany borrowing and transfer pricing arrangements, cash in the various jurisdictions is generally available to fund operations in the particular jurisdictions, but generally is not freely transferable between jurisdictions or regions and we have to renegotiate some of our transfer pricing arrangements. The resulting contracts and financial arrangements may adversely affect our financial results and business. Furthermore, our inability to repatriate cash throughout the enterprise as needed could have a material adverse effect on our financial condition and results of operations.

Transfers or issuances of our equity, or a debt restructuring, may impair or reduce our ability to utilize our net operating loss carry-forwards and certain other tax attributes in the future.

Pursuant to U.S. tax rules, a corporation is generally permitted to deduct from taxable income in any year net operating losses (NOLs) carried forward from prior years. We have NOL carryforwards in the United States of approximately $1.1 billion as of December 27, 2009. Our ability to utilize these NOL carryforwards could be subject to a significant limitation if we were to undergo an ownership change for purposes of Section 382 of the Internal Revenue Code of 1986, as amended, during or as a result of the Chapter 11 Cases. During the Chapter 11 Cases, the U.S. Bankruptcy Court has entered an order that places certain restrictions on trading in our common stock. However, we can provide no assurances that these limitations will prevent an ownership change or that our ability to utilize our NOL carryforwards may not be significantly limited as a result of our restructuring.

A restructuring of our debt pursuant to the Chapter 11 Cases may give rise to cancellation of indebtedness or debt forgiveness (COD), which if it occurs would generally be non-taxable. If the COD is non-taxable, we will be required to reduce our NOL carryforwards and other attributes such as capital loss carryforwards and tax basis in assets, by an amount equal to the non-recognized COD. Therefore, it is possible that, as a result of the successful completion of a plan of reorganization, we will have a reduction of NOL carryforwards and/or other tax attributes in an amount that cannot be determined at this time and that could have a material adverse effect on our future financial results.

Trading in our securities on the Pink Sheets during the pendency of the Chapter 11 Cases is highly speculative and poses substantial risks.

Our common stock has been delisted from The NASDAQ Stock Market and is traded on the Pink Sheets, which makes our common stock significantly less liquid. Trading prices of our securities are very volatile and may bear little or no relationship to the actual recovery, if any, by the holders under the Plan of Reorganization. In the Plan of Reorganization, our existing securities, in particular our common stock will be cancelled and holders will receive no payment or other consideration in return.

Table of Contents

If we are unable to attract and retain qualified personnel at reasonable costs, we may not be able to achieve our business objectives, and our ability to successfully emerge from the Chapter 11 Cases may be harmed.

We are dependent on the experience and industry knowledge of our senior management and other key employees to execute our current business plans and lead us, particularly during the Chapter 11 Cases and throughout the implementation of the Plan of Reorganization. Competition for certain key positions and specialized technical and sales personnel in the high-technology industry remains strong. Our deteriorating financial performance, along with the Chapter 11 Cases and workforce reductions create uncertainty that has led to an increase in unwanted attrition, and additional challenges in attracting and retaining new qualified personnel. We have lost many key employees with long tenures and broad knowledge about our historical operations and we are at risk of losing or being unable to hire talent critical to a successful reorganization and ongoing operation of our business. Our ability to retain and attract critical talent is restricted in part by the Chapter 11 Cases that, among other things, limit our ability to implement a retention program or take other measures to attract new hires to the Company or motivate employees to remain with us. Our future success depends in part on our continued ability to hire, assimilate in a timely manner and retain qualified personnel, particularly in key senior management positions. If we are not able to attract, recruit or retain qualified employees (including as a result of headcount and salary reductions), we may not have the personnel necessary to implement the Plan of Reorganization, and our business, results of operations and financial condition could be materially adversely impacted.

Risks Related to our Financial Condition

If we cannot generate sufficient operating cash flows and obtain external financing, we may be materially adversely affected.

Our capital expenditures, together with ongoing operating expenses, have been a substantial drain on our cash flows and have decreased our cash balances. Since fiscal 2008, we have increased cost cutting activities, including: salary reductions; cutting capital spending; reducing and freezing headcount; cutting research and development projects; and reducing administrative expenses. Some cost cutting activities may require initial cost outlays before the cost reductions are realized. We cannot assure you that we will be able to achieve anticipated expense reductions. If our expense reduction efforts are unsuccessful, our operating results and business may be materially adversely affected.

Additional funds from liquidity-generating transactions or other sources of external financing may not be available to us. Such financing would be subject to certain limitations, including court approvals and other requisite approvals by other third parties. Our inability to obtain needed financing or to generate sufficient cash from operations may require us to abandon projects or curtail capital expenditures, or may have an adverse effect on our restructuring process. If we cannot generate sufficient operating cash flows or obtain external financing, we would be materially adversely affected.

Financial market conditions may impede access to or increase the cost of financing operations and investments.

The changes in U.S. and global financial and equity markets, including market disruptions and tightening of the credit markets, compounded by us being subject to the Chapter 11 Cases, may make it more difficult for us to obtain financing for our operations or investments or increase the cost of obtaining financing, which would materially adversely affect us.

We are party to several debt instruments for which, as a result of the Chapter 11 Cases, an event of default has occurred. In connection with our reorganization, we may enter into debt arrangements in the future, each of which may subject us to restrictive covenants which could limit our ability to operate our business.

As of December 27, 2009, we had an aggregate principal amount of approximately $1.1 billion in outstanding debt, almost all of which became due and immediately payable upon events of default triggered by the occurrence of events related to the Creditor Protection Proceedings. During the Chapter 11 Cases and upon

Table of Contents

emergence from them, we will need to incur additional indebtedness through arrangements such as credit agreements or term loans that may include restrictions and covenants that are similar or more restrictive than the covenants in our existing debt instruments. These restrictions and covenants limit, and any future covenants and restrictions likely will limit our ability to respond to market conditions, to make capital investments or to take advantage of business opportunities. Any debt arrangements we enter into would likely require us to make regular interest payments, which could adversely affect our results of operations.

We cannot assure you that in the future we will be able to satisfy or comply with the provisions, covenants, financial tests and ratios of our debt instruments, which can be affected by events beyond our control. If we fail to satisfy or comply with such provisions, covenants, financial tests and ratios, or if we disagree with our lenders about whether or not we are in compliance, we cannot assure you that we will be able to obtain waivers for any future failures to comply with our financial covenants or any other terms of the debt instruments. We also may not be able to obtain amendments which will prevent a failure to comply in the future. A breach of any of the provisions, covenants, financial tests or ratios under our debt instruments could result in a default under the applicable agreement, which in turn could trigger cross-defaults under other debt instruments, any of which would materially adversely affect us.

Our investments in auction rate securities are subject to risks which may cause losses and affect the liquidity of these investments.

As of December 27, 2009, our auction rate securities (ARS) totaled approximately $100.3 million and consisted solely of AAA/Aaa securities with auction reset features whose underlying assets are student loans and are substantially backed by the U.S. government Federal Family Education Loan Program. During 2008, we experienced failed auctions of our ARS and we cannot assure you that any future auctions would be successful. In November 2008, we accepted an offer to participate in an auction rate securities settlement from UBS Bank USA (UBS), providing us the right, but not the obligation, to sell to UBS up to all of our ARS at par, commencing June 30, 2010 through July 2, 2012. This right represents a put option for a payment equal to the par value of the ARS.

The put option is subject to a number of risks. Given the substantial dislocation in the financial markets and among financial services companies, we cannot assure you that UBS will ultimately have the ability to repurchase our ARS at par, or at any other price during the put period described above. We will be required to periodically assess the economic ability of UBS to meet that obligation in assessing the fair value of the rights. Moreover, if we choose to not exercise or UBS is unable to honor the put option, our ability to liquidate our investments in the near term may be limited, and our ability to fully recover the carrying value of our investments may be limited or non-existent. If issuers of these securities are unable to successfully close future auctions or their credit ratings deteriorate, we may in the future be required to record further impairment charges on these investments. It could take until the final maturity of the underlying notes (up to 39 years) to realize our investments recorded value. We can provide no assurance as to when these investments will again become liquid or as to whether we may ultimately have to recognize additional impairment charges in our results of operations with respect to these investments. Delays in liquidating these securities in the future could have a material adverse effect on us.

Risks Related to Our Business

The demand for our products depends in large part on continued growth in the industries into which they are sold. A decline in the markets served by any of these industries, or a decline in demand for Flash memory products in these industries, would have a material adverse effect on our results of operations.

If demand for mobile phones, other consumer products or industrial products utilizing Flash memory declines, our business could be materially adversely affected. Also, if the functionality of successive generations of such products does not require increasing Flash memory density or if such products no longer require Flash memory due to alternative technologies or otherwise, our operating results would be materially adversely affected.

Table of Contents

Our business has been characterized by an average selling price that declines over time, which can negatively affect our results of operations.

Generally, we endeavor to maintain or increase our average selling price while lowering our average costs, by improving our product mix, and selling more units. Historically, the selling prices of our products have decreased during the products lives, and we expect this trend to continue. When our selling prices decline, our net sales and gross margins also decline unless we are able to compensate by selling more units thereby reducing our manufacturing costs per product or introducing and selling new, higher margin products with higher densities and/or advanced features. If the average selling price for our products continues to decline, our operating results could be materially adversely affected.

During downturns, periods of extremely intense competition, or the presence of oversupply in the industry, the selling prices for our products has declined at a high rate over relatively short time periods as compared to historical rates of decline. We are unable to predict selling prices for any future periods and may experience unanticipated, sharp declines in selling prices for our products. When such pricing declines occur, we may not be able to mitigate the effects by selling more or higher margin units, or by reducing our manufacturing costs. In such circumstances, our operating results could be materially adversely affected.

The Flash memory market is highly cyclical and has experienced severe downturns that have materially adversely affected, and may in the future materially adversely affect, our business.

The Flash memory market is highly cyclical and in the past has experienced severe downturns, generally as a result of wide fluctuations in supply and demand, constant and rapid technological change, continuous new product introductions and price erosion. Our financial performance has been, and may in the future be, adversely affected by these downturns. We have incurred substantial losses in past downturns, and as a result of the most recent downturn, due principally to:

- substantial declines in selling prices, particularly due to competitive pressures and an imbalance in product supply and demand; and
- a decline in demand for end-user products that incorporate our products.

Our historical financial information does not necessarily indicate what our results of operations, financial condition or cash flows will be in the future. If our net sales decline in the future, or if these or other similar conditions continue or occur again in the future, we would likely be materially adversely affected.

Our forecasts of customer demand for our products may be inaccurate, which could result in excess or shortages in inventory, which could cause us to record write-downs or fail to meet customer demand. Inaccurate forecasting could materially and adversely affect our business and financial results.

Although our manufacturing cycle times are relatively lengthy, in excess of ten weeks, we nevertheless compete in a market where suppliers ability to respond quickly to new incoming orders is a competitive differentiator. Thus, we must forecast customer demand and produce requisite amounts of our products in order to fill current and future orders even though demand is volatile and difficult to predict. To forecast demand and value inventory, management considers, among other factors, the inventory on hand, historical customer demand data, backlog data, competitiveness of product offerings, market conditions and product life cycles. If we are unable to accurately assess these factors and anticipate future demand or market conditions, inventory write-downs may be required and would be reflected in cost of sales in the period the write-down is made. This would have a negative impact on our gross margin in that period. Inaccurate forecasting could also result in excess or obsolete inventory that would reduce our profit margins or shortages in inventory that would cause us to fail to meet customer demand. If, as a result of inaccurate forecasting, we are unable to produce the types and quantities of products required by our customers in the timeframes and on the delivery schedules required by our customers, we may lose customers or, in certain circumstances, be liable for losses incurred by our customers, which would materially adversely affect our business and financial results.

Table of Contents

Any future business combinations, divestitures, acquisitions or mergers expose us to risks, including the risk that we may not be able to successfully integrate these businesses or achieve expected operating synergies.

During the Chapter 11 Cases we will, and upon emergence from them we may periodically, consider strategic transactions. We may evaluate acquisitions, divestitures, joint ventures, alliances or co-production programs as opportunities arise and we may be engaged in varying levels of negotiations with third parties at any time. We may not be able to effect transactions and if we enter into transactions, we also may not realize the benefits we anticipate. Moreover, the integration of companies that have previously been operated separately involves a number of risks. Consummating any acquisitions, divestitures, joint ventures, alliances or co-production programs could result in the incurrence of additional transaction-related expenses, as well as unforeseen contingent liabilities, which could materially adversely affect us.

A significant market shift to NAND architecture would materially adversely affect us.

Flash memory products are generally based on either NOR or NAND architecture. To date, our Flash memory products have been based on NOR architecture which are typically produced at a higher cost-per-bit than NAND-based products. We are developing our MirrorBit NAND architectures primarily to address embedded applications currently served by NAND- based products or potentially served by NAND-based products in the future, but we cannot be certain that our MirrorBit NAND-based products will satisfactorily address those market needs.

From 2004 to 2008, industry sales of NAND-based Flash memory products increased as a percentage of total Flash memory sales compared to sales of NOR-based Flash memory products, resulting in NAND vendors in aggregate gaining a greater share of the overall Flash memory market and NOR vendors in aggregate losing overall market share. We expect the Flash memory market trend of decreasing market share for NOR-based Flash memory products relative to NAND-based Flash memory products to continue in the foreseeable future.

Customers manufacturing products for embedded applications may increasingly choose floating gate NAND-based Flash memory products over MirrorBit NOR- or NAND-based Flash memory products for their applications. If this occurs and customers continue to prefer floating gate NAND-based products over those of MirrorBit NOR- or NAND-based products for their applications, we may be materially and adversely affected. Moreover, some of our competitors are able to manufacture floating gate NAND-based Flash memory products on 300-millimeter wafers produced in much larger capacity fabrication facilities (fabs) than we currently have access to. In addition, some of our competitors may choose to utilize more advanced manufacturing process technologies than we may have available to offer products competitive to ours at a lower cost or with higher densities.

In addition, even if products based on NAND architecture are unsuccessful in displacing products based on NOR architecture, the average selling price for our products may be adversely affected by a significant decline in the price for NAND-based products. Such a decline may result in downward price pressure in the overall Flash memory market affecting the price we can obtain for our NOR-based products, which would adversely affect us. We believe such downward pricing pressure was a factor in the significant declines in the selling prices of our products in 2007 and 2008. If the prices for NAND products similarly decline in the future, we may be materially adversely affected.

We cannot be certain that our substantial investments in research and development will lead to timely improvements in technology or that we will have sufficient resources to invest in the level of research and development that is required to remain competitive.

In order to compete, we are required to make substantial investments in research and development for design, process technologies and production techniques in an effort to design and manufacture advanced Flash memory products. For example, in fiscal 2009, 2008 and 2007, our research and development expenses were approximately $136.4 million, $431.8 million and $436.8 million, respectively, or approximately 10, 19 and 17 percent, respectively, of our net sales.

Table of Contents

Currently, we are developing new non-volatile memory process technologies. We cannot assure you that we will have sufficient resources to maintain the level of investment in research and development that is required for us to remain competitive, which could materially adversely affect us. Further, we cannot assure you that our investments in research and development will result in increased sales or competitive advantage, which could materially adversely affect our operating results.

If we fail to successfully develop, introduce and commercialize new products and technologies, we may be materially adversely affected.

Our success depends to a significant extent on the development, qualification, production, introduction and acceptance of new product designs and improvements that provide value to Flash memory customers. Our ability to develop and qualify new products and related technologies to meet evolving industry requirements at prices acceptable to our customers and on a timely basis affects our competitiveness in our target markets. If we are delayed in developing or qualifying new products or technologies, we could be materially adversely affected.

Competitors may introduce new memory or other technologies that may make our Flash memory products uncompetitive or obsolete.

Our competitors are working on a number of new technologies, including FRAM, MRAM, polymer, charge trapping and phase-change based memory technologies. One of our competitors began shipping products based on phase-change based memory technology in 2008. If such products are successfully developed and commercialized as a viable alternative to MirrorBit or floating gate Flash memory, these other products could pose a competitive threat to existing Flash memory companies, including us. In addition, some of Saifun s licensees and customers are our competitors or work with our competitors and have licensed Flash memory intellectual property associated with charge trapping technology from Saifun. Use of this charge trapping intellectual property or use of independently developed charge trapping Flash memory technology by our competitors, if successfully developed and commercialized, may allow these competitors to develop Flash memory technology that may compete with our proprietary MirrorBit technology.

If we fail to successfully develop new applications and markets for our products our future operating results would be materially adversely affected.

We are developing new applications and opportunities for our products beyond our traditional customer base and in some cases plan to deploy our Flash memory solutions beyond current Flash memory markets. We expect these new applications to grow future net sales, future margin or a combination of both. However, some of these opportunities require that we are successful in creating, marketing, gaining customer acceptance of and deploying these new system architectures into a customer base where we do not have a historic business relationship and where our solution is required to replace established and proven solutions. In some cases our solutions rely on third parties to contribute a significant and necessary component of the solution without which the solution is nonviable. If we are unsuccessful in our attempts to bring new products to market, experience significant delays in generating sales, fail to establish the value of this solution or face competition from third parties or incumbent suppliers that result in lower margins than expected, then our future operating results would be materially adversely affected.

Our reliance on third-party manufacturers entails risks that could materially adversely affect us.

We have in the past and plan in the future to obtain foundry, subcontractor and other arrangements with third parties to meet demand. Foundry services suppliers from which we have obtained, and in the future may obtain, foundry services, include Spansion Japan, Fujitsu Microelectronics Limited (as a result of the sale of our JV1/JV2 manufacturing facilities in April 2007) and Semiconductor Manufacturing International Corporation. We also use independent contractors to perform some of the assembly, testing and packaging of our products. Some third-party manufacturers are often under no obligation to provide us with any specified minimum quantity of product. We depend on these manufacturers to allocate to us a portion of their manufacturing capacity sufficient to meet our needs, and, in the case of Spansion Japan, all of their manufacturing capacity has historically been allocated to us. We also depend on these manufacturers to produce products of acceptable quality and at acceptable manufacturing yields and to deliver those products to us on a timely basis at acceptable prices. In addition, we rely on these manufacturers to invest capital into their facilities and process technologies to meet our needs for new products using advanced process technologies. Given the Creditor Protection Proceedings and the current volatility and disruption in the capital and credit markets worldwide, we cannot assure you that they will make the investments in their facilities previously contemplated. We cannot assure you that these manufacturers will be able to meet our near-term or long-term manufacturing requirements and may not be able to attain qualification from our customers. In addition, any significant change in the payment terms we have with our key suppliers could adversely affect us.

These manufacturers, excluding Spansion Japan, also make products for other companies, including certain of our competitors, and/or for themselves and could choose to prioritize capacity for themselves or other customers beyond any minimum guaranteed amounts, reduce deliveries to us or, in the absence of price guarantees, increase the prices they charge us on short notice, such that we may not be able to pass cost increases on to our customers. The likelihood of this occurring may be greater as a result of the Creditor Protection Proceedings. We may be unable to secure an alternative supply for specific products in a short timeframe or at all at an acceptable cost to satisfy our production requirements. In addition, we may be required to incur additional development, manufacturing and other costs to establish alternative sources of supply. Other risks associated with our increased dependence on third-party manufacturers include: their ability to adapt to our proprietary technology, reduced control over delivery schedules, quality assurance, manufacturing yields and cost, lack of capacity in periods of excess demand, misappropriation of our intellectual property, reduced ability to manage inventory and parts and risks associated with operating in foreign countries. If we are unable to secure sufficient or reliable suppliers of wafers or obtain the necessary assembling, testing and packaging services, our ability to meet customer demand for our products may be adversely affected, which could have a material adverse effect on us.

We rely on Fujitsu Microelectronics Limited to distribute our products in Japan.

We currently rely on Fujitsu Microelectronics Limited (FML) through its subsidiary Fujitsu Electronics Inc. (FEI) to distribute our products to customers in Japan, which is an important geographic market for us. Under our distribution agreement with FML, FML has agreed to use its best efforts to promote the sale of our products in Japan and to other customers served by FML. In the event that we reasonably determine that FML s sales performance in Japan and to those customers served by FML is not satisfactory based on specified criteria, then we have the right to require FML to propose and implement an agreed-upon corrective action plan. If we reasonably believe that the corrective action plan is inadequate, we can take steps to remedy deficiencies ourselves through means that include appointing another distributor as a supplementary distributor to sell products in Japan and to customers served by FML. Pursuing these actions would be costly and disruptive to the sales of our products in Japan. If FML s sales performance in Japan is unsatisfactory or if we are unable to successfully maintain our distribution agreement and relationship with FML and we cannot timely find a suitable supplementary distributor, we could be materially adversely affected.

Under the terms of our distribution agreement with FML, either party may terminate the distribution agreement, either in whole or in part, for convenience upon 60 days written notice to the other party. If FML unexpectedly terminates its distribution agreement with us, or otherwise ceases its support of our customers in Japan, we would be required to rely on a relationship with another distributor or establish our own local sales organization and support functions. We cannot be certain that we will be successful in selling our products to customers currently served by FML or new customers. If customers currently served by FML, or potential new customers, refuse to purchase our products directly from us or from another distributor, our sales in Japan may decline, and we could be materially adversely affected.

Table of Contents

Industry overcapacity could require us to take actions which could have a material adverse effect on us.

Semiconductor companies with their own manufacturing facilities and specialist semiconductor foundries, which are subcontractors that manufacture semiconductors designed by others, have added significant capacity in recent years. In 2008, the significant excess capacity led to oversupply and a downturn in the memory industry. The contraction of the worldwide economy, especially in the fourth quarter of 2008, further compounded industry over capacity. Continuing manufacturing overcapacity in the industry is having a material adverse effect on us. Furthermore, fluctuations in the growth rate of industry capacity relative to the growth rate in demand for Flash memory products can contribute to cyclicality in the Flash memory market, which may in the future negatively impact our selling prices and materially adversely affect us.

It is difficult to predict future growth or decline in the markets we serve, making it very difficult to estimate requirements for production capacity. If our target markets do not grow as we anticipate, we may under-utilize our manufacturing capacity or we may be contractually obligated to purchase minimum quantities of certain products from our subcontractors. This may result in write-downs or write-offs of inventories and losses on products the demand for which is lower than we anticipate. In addition, during periods of industry overcapacity, customers do not generally order products as far in advance of the scheduled shipment date as they do during periods when our industry is operating closer to capacity, which can exacerbate the difficulty in forecasting capacity requirements.

Many of our costs are fixed. Additionally, pursuant to some of our subcontractor and foundry arrangements with third parties we may incur and pay penalties, according to which we have agreed to pay for a certain amount of product even if we do not accept delivery of all of such amount. Accordingly, during periods in which we under-utilize our manufacturing capacity as a result of reduced demand for some of our products, our costs cannot be reduced in proportion to the reduced net sales for such periods. When this occurs, our operating results are materially adversely affected.

Our customers ability to change booked orders may lead to excess inventory.

Because our manufacturing processes require long lead times, we use indicators such as booking rates in conjunction with other business metrics, to schedule production in our fabrication facilities. Consequently, when customers change orders booked with us, our planned manufacturing capacity may be greater or less than actual demand, resulting in less than optimal inventory levels. When this occurs, we adjust our production levels but such adjustments may not prevent our production of excess inventory in environments when bookings are strong. As a result, our business may be materially adversely affected.

Intense competition in the Flash memory market could materially adversely affect us.

Our principal NOR Flash memory competitors are Numonyx B.V., Macronix International Co., Ltd. and Samsung Electronics Co., Ltd. Additional significant NOR Flash memory competitors include Silicon Storage Technology, Inc. and Toshiba Corporation.

We increasingly compete with NAND Flash memory manufacturers where NAND Flash memory has the ability to replace NOR Flash memory in customer applications. Our principal NAND Flash memory competitors include Samsung Electronics Co., Ltd., Numonyx B.V. and Micron Technology, Inc. In the future our principal NAND Flash memory competitors may include Hynix Semiconductor Inc., Toshiba Corporation, Intel Corporation, IM Flash Technology LLC, the joint venture between Intel and Micron Technology, Inc. and SanDisk Corporation.

The Flash memory market is characterized by intense competition. The basis of competition is cost, selling price, performance, quality, customer relationships and ability to provide value-added solutions. In particular, in the past, our competitors have aggressively priced their products, which resulted in decreased selling prices for

Table of Contents

our products in the first half of fiscal 2007 and adversely impacted our results of operations. Some of our competitors, including Samsung and Toshiba, are more diversified than we are and may be able to sustain lower operating margins in their Flash memory business based on the profitability of their other, non-Flash memory businesses. In addition, capital investments by competitors have resulted in substantial industry manufacturing capacity, which may further contribute to a competitive pricing environment. Some of our competitors are able to manufacture floating gate NAND-based Flash memory products on 300-millimeter wafers produced in much larger capacity fabs than we may have access to or may choose to utilize more advanced manufacturing process technologies than we will have to offer products competitive to ours at a lower cost or higher density. Moreover, products based on our MirrorBit ORNAND-, MirrorBit Quad- and MirrorBit NAND-based architectures may not have the price, performance, quality and other features necessary to compete successfully for these applications.

We expect competition in the market for Flash memory devices to intensify as existing manufacturers introduce new products, new manufacturers enter the market, industry-wide production capacity increases and competitors aggressively price their Flash memory products to increase market share. The competition we face may also intensify, particularly in light of the Creditor Protection Proceedings, if our competitors, who may have greater financial resources than us, increase their focus on the Flash memory products, or segments of the Flash memory markets, that generate a significant portion of our net sales.

Competitive pressures may also increase if NOR memory vendors merge, if NAND memory vendors acquire NOR businesses or other NAND businesses, or if our competitors otherwise consolidate their operations. Furthermore, we face increasing competition from NAND Flash memory vendors targeting the embedded portion of the Flash memory market.

To compete successfully, we must decrease our manufacturing costs and develop, introduce and sell products at competitive prices that meet the increasing demand for greater Flash memory content in mobile phones, consumer electronics, automotive and other applications. If we are unable to compete effectively, we could be materially adversely affected.

Unless we maintain manufacturing efficiency, we may not become profitable and our future profitability could be materially adversely affected.

The Flash memory industry is characterized by rapid technological changes. For example, new manufacturing process technologies using smaller feature sizes and offering better performance characteristics are generally introduced every one to two years. The introduction of new manufacturing process technologies allows us to increase the functionality of our products while at the same time optimizing performance parameters, decreasing power consumption and/or increasing storage capacity. In addition, the reduction of feature sizes enables us to produce smaller chips offering the same functionality and thereby considerably reduces the cost per bit. In order to remain competitive, it is essential that we secure the capabilities to develop and qualify new manufacturing process technologies. For example, our leading Flash memory products must be manufactured at 65-nanometer and more advanced process technologies. If we are delayed in transitioning to these technologies and other future technologies, we could be materially adversely affected. As a result of the Creditor Protection Proceedings, we may be forced to shut down or abandon current plans for our manufacturing facilities which could materially adversely affect us.

Manufacturing our products involves highly complex processes that require advanced equipment. Our manufacturing efficiency is an important factor in our profitability, and we cannot be sure that we will be able to maintain or increase our manufacturing efficiency to the same extent as our competitors. For example, we continuously modify our manufacturing processes in an effort to improve yields and product performance and decrease costs. We are continuing to transition to 65-nanometer process technology for the manufacture of some of our products. During periods when we are implementing new process technologies, manufacturing facilities may not be fully productive. We may fail to achieve acceptable yields or may experience product delivery delays as a result of, among other things, capacity constraints, delays in the development of new process technologies,

Table of Contents

changes in our process technologies, upgrades or expansion of existing facilities, impurities or other difficulties in the manufacturing process. Any of these occurrences could adversely impact our relationships with customers, cause harm to our reputation in the marketplace, cause customers to move future business to our competitors or cause us to make financial concessions to our customers.

Improving our manufacturing efficiency in future periods is dependent on our ability to:

- develop advanced process technologies and advanced products that utilize those technologies;
- successfully transition to advanced process technologies;
- continue to reduce test times;
- ramp product and process technology improvements rapidly and effectively to commercial volumes;
- achieve acceptable levels of manufacturing wafer output and yields, which may decrease as we implement more advanced technologies; and
- maintain our quality controls and rely upon the quality and process controls of our suppliers.

If we cannot adequately protect our technology or other intellectual property in the United States and abroad, through patents, copyrights, trade secrets, trademarks and other measures, we may lose a competitive advantage and incur significant expenses.

We rely on a combination of protections provided by contracts, including confidentiality and non-disclosure agreements, copyrights, patents, trademarks and common law rights, such as trade secrets, to protect our intellectual property. However, we cannot assure you that we will be able to adequately protect our technology or other intellectual property from third-party infringement or from misappropriation in the United States and abroad. Any patent owned or licensed by us or issued to us could be challenged, invalidated or circumvented or rights granted under these patents or licenses may not provide a competitive advantage to us. Furthermore, patent applications that we file may not result in issuance of a patent or, if a patent is issued, the patent may not be issued in a form that is advantageous to us. Despite our efforts to protect our intellectual property rights, others may independently develop similar products, duplicate our products or design around our patents and other intellectual property rights. In addition, it is difficult to monitor compliance with, and enforce, our intellectual property on a worldwide basis in a cost-effective manner. Foreign laws may provide less intellectual property protection than afforded in the United States. Our efforts to protect our intellectual property in the United States and abroad, through lawsuits such as those that have been filed between us and Samsung Electronics Co., Ltd., may be time-consuming and costly. If we cannot adequately protect our technology or other intellectual property rights in the United States and abroad, we may be materially adversely affected.

We may not be able to successfully to negotiate agreements or arrangements with third parties for rights to key intellectual property, which creates a greatly increased risk of patent or other intellectual property infringement claims against us.

We may attempt to negotiate our own agreements and arrangements with third parties for intellectual property and technology that are important to our business. We may also attempt to acquire new patents as our success in negotiating patent cross-license agreements with other industry participants will depend in large part upon the strength of our patent portfolio relative to that of the third party with which we are negotiating. If we are unable to negotiate agreements or arrangements for intellectual property, or to obtain patents, necessary for the success of our business, we may be materially adversely affected.

We are party to intellectual property litigation and may become party to other intellectual property claims or litigation that could cause us to incur substantial costs or pay substantial damages or prohibit us from selling our products.

From time to time, we may be notified, or third parties may bring actions against us based on allegations, that we are infringing the intellectual property rights of others. If any such claims are asserted against us, we may

Table of Contents

seek to obtain a license under the third party s intellectual property rights. We cannot assure you that we will be able to obtain all of the necessary licenses on satisfactory terms, if at all. In the event that we cannot obtain a license, these parties may file lawsuits against us seeking damages (potentially including treble damages) or an injunction against the sale of our products that incorporate allegedly infringed intellectual property or against the operation of our business as presently conducted, which could result in our having to stop the sale of some of our products, increase the costs of selling some of our products, or cause damage to our reputation. The award of damages, including material royalty payments, or the entry of an injunction against the manufacture and sale of some or all of our products, would have a material adverse effect on us. We could decide, in the alternative, to redesign our products or to resort to litigation to challenge or defend such claims, either of which could be expensive and time-consuming and may have a material adverse effect on us. See Item 3 Legal Proceedings.

We provide indemnities relating to non-infringement of patents and other intellectual property indemnities to certain of our customers in connection with the delivery, design, manufacture and sale of our products. If we are required to indemnify companies with whom we do business and we incur substantial costs, our business, results of operations and financial condition could be materially adversely affected.

If essential equipment or adequate supplies of satisfactory materials are not available to manufacture our products, we could be materially adversely affected.

Our manufacturing operations depend upon obtaining deliveries of equipment and adequate supplies of materials on a timely basis. We purchase equipment and materials from a number of suppliers. From time to time, suppliers may extend lead times, limit supply to us or increase prices due to capacity constraints or other factors. Because the equipment that we purchase is complex, it is difficult for us to substitute one supplier for another or one piece of equipment for another. Some raw materials we use in the manufacture of our products are available from a limited number of suppliers or only from a limited number of suppliers in a particular region. In addition, we purchase raw materials such as gold which prices on the world markets have fluctuated significantly during recent periods. Our manufacturing operations also depend upon the quality and usability of the materials we use in our products, including raw materials and wafers we receive from our suppliers. If the materials we receive from our suppliers do not meet our manufacturing requirements or product specifications, are not obtained in a timely manner or if there are significant increases in costs of materials, we may be materially adversely affected.

We also rely on purchasing commercial memory die such as DRAM from third-party suppliers to incorporate these die into multi-chip package products. The availability of these third-party purchased commercial die is subject to market availability, and the process technology roadmaps and manufacturing capacities of our vendors. In addition, some of our suppliers may also be our competitors. Interruption of supply from a competitor that is a supplier or otherwise or increased demand in the industry could cause shortages and price increases in various essential materials. If we are unable to procure these materials, or if the materials we receive from our suppliers do not meet our production requirements or product specifications, we may have to reduce our manufacturing operations or our manufacturing yields may be adversely affected. Such a reduction and yield issues have in the past and could in the future have a material adverse effect on us.

Costs related to defective products could have a material adverse effect on us.

One or more of our products may be found to be defective after the product has been shipped to customers in volume. The cost of product replacements or product returns may be substantial, and our reputation with our customers would be damaged. In addition, we could incur substantial costs to implement modifications to fix defects. Any of these problems could materially adversely affect us.

Unfavorable currency exchange rate fluctuations could adversely affect us.

As a result of our foreign operations, we have sales, expenses, assets and liabilities that are denominated in Japanese yen and other foreign currencies. For example:

- some of our costs are denominated in Japanese yen, Thai baht and Malaysian ringgit;

Table of Contents

- sales of our products to, and purchases from, Spansion Japan are denominated in both US dollars and Japanese yen; and
- some fixed asset purchases are denominated in Japanese yen and European Union euros.

Consequently, movements in exchange rates could cause our net sales and expenses to fluctuate, affecting our profitability and cash flows. We are currently unable to and in the future may not be able to enter into hedging contracts on acceptable terms, if at all.

Worldwide economic and political conditions may adversely affect demand for our products.

We operate in more than ten countries and we derive a majority of our net sales outside the United States. Our business depends on the overall worldwide economic conditions and the economic and business conditions within our customers industries. Our business may also be affected by economic factors that are beyond our control, such as downturns in economic activity in a specific country or region. A further weakening of the worldwide economy or the economy of individual countries or the demand for our customers products may cause a greater decrease in demand for our products, which could materially adversely affect us.

Our consolidated financial results could also be significantly and adversely affected by geopolitical concerns and world events, such as wars and terrorist attacks. Our net sales and financial results have been and could be negatively affected to the extent geopolitical concerns continue and similar events occur or are anticipated to occur. In particular, consequences of military action in the Middle East have in the past, and may in the future, adversely affect demand for our products and our relationship with various third parties with which we collaborate. In addition, terrorist attacks may negatively affect our operations, directly or indirectly, and such attacks or related armed conflicts may directly impact our physical facilities or those of our suppliers or customers. Furthermore, these attacks may make travel and the transportation of our products more difficult and more expensive, which could materially adversely affect us.

The United States has been and may continue to be involved in armed conflicts that could have a further impact on our sales and our supply chain. Political and economic instability in some regions of the world may also result and could negatively impact our business. The consequences of armed conflicts are unpredictable, and we may not be able to foresee events that could have a material adverse effect on us. More generally, any of these events could cause consumer confidence and spending to decrease or result in increased volatility in the U.S. economy and worldwide financial markets. Any of these occurrences could have a material adverse effect on us.

Our operations in foreign countries are subject to political and economic risks, which could have a material adverse effect on us.

A significant portion of our planned wafer fabrication capacity for existing and future products is provided by third parties located in Japan and China, and nearly all final test and assembly of our products is performed at our facilities in Malaysia and Thailand and by third parties in China, Taiwan and Japan. In addition, we have international sales operations and, as part of our business strategy, we are continuing to seek to expand our product sales in high growth markets. The political and economic risks associated with our sales to, and operations in, foreign countries include:

- expropriation;
- changes in political or economic conditions;
- changes in tax laws, trade protection measures and import or export licensing requirements;
- difficulties in protecting our intellectual property;
- difficulties in achieving headcount reductions;

changes in foreign currency exchange rates;

- restrictions on transfers of funds and other assets of our subsidiaries between jurisdictions;
- changes in freight and interest rates;
- disruption in air transportation between the United States and our overseas facilities; and
- loss or modification of exemptions for taxes and tariffs.

Our subsidiary, Saifun, conducts business in Israel, which is affected and surrounded by unstable political, economic and military conditions. We cannot predict the effect of continued or increased violence in Lebanon or Gaza, or the effect of military action elsewhere in the Middle East. Continued armed conflicts or political instability in the region would harm business conditions and could adversely affect the combined company s results of operations. Furthermore, several countries continue to restrict or ban business with Israel and Israeli companies. These restrictive laws and policies may limit the combined company s ability to make sales in those countries, and, as a global company, may limit our own ability to efficiently administer our worldwide resources.

Any conflict or uncertainty in the countries in which we operate, including public health or safety concerns, natural disasters or general economic factors, could have a material adverse effect on our business.

We are subject to a variety of environmental laws that could result in liabilities.

Our properties and many aspects of our business operations are subject to various domestic and international environmental laws and regulations, including those relating to materials used in our products and manufacturing processes; chemical use and handling; waste minimization; discharge of pollutants into the environment; the treatment, transport, storage and disposal of solid and hazardous wastes; and remediation of contamination. Certain of these laws and regulations require us to obtain permits for our operations, including permits related to the discharge of air pollutants and wastewater. From time to time, our facilities are subject to investigation by governmental regulators. Environmental compliance obligations and liability risks are inherent in many of our manufacturing and other activities. Any failure to comply with applicable environmental laws, regulations or permits may subject us to a range of consequences, including fines, suspension of production, alteration of manufacturing processes, sales limitations, and criminal and civil liabilities or other sanctions. We could also be held liable for any and all consequences arising out of exposure to hazardous materials used, stored, released, disposed of by us or located at or under our facilities, or for other environmental or natural resource damage. Certain environmental laws, including the U.S. Comprehensive, Environmental Response, Compensation and Liability Act of 1980, or the Superfund Act, impose joint and several liability on current and previous owners or operators of real property for the cost of removal or remediation of hazardous substances and costs related to damages to natural resources. Liability can attach even if the owner or operator did not know of, or was not responsible for, the release of such hazardous substances. These environmental laws also can result in liability for persons, like us, who arrange for hazardous substances to be sent to disposal or treatment facilities, in the event such facilities are found to be contaminated. Such persons can be responsible for cleanup costs at a disposal or treatment facility, even if they never owned or operated the contaminated facility. One property where we currently conduct research and development operations is listed on the U.S. Environmental Protection Agency s Superfund National Priorities List. However, other parties currently are responsible for all investigation, cleanup and remediation activities. Although we have not been named a responsible party at this site, if we were so named, costs associated with the cleanup of the site could have material adverse effect upon us.

We have not been named a responsible party at any Superfund or other contaminated site. If we were ever so named, costs associated with the cleanup of the site could be material. Additionally, contamination that has not yet been identified could exist at one or more of our facilities, and identification of such contamination could have a material adverse effect on us.

Our business is subject to complex and dynamic environmental regulatory schemes. While we have budgeted for reasonably foreseeable environmental expenditures, we cannot assure you that environmental laws will not change or become more stringent in the future. Future environmental regulations could require us to procure expensive pollution abatement or remediation equipment; to modify product designs; or to incur other expenses associated with compliance with such regulations. For example, the European Union and China recently began imposing stricter requirements regarding reduced lead content in semiconductor packaging. Therefore, we cannot assure you that our costs of complying with current and future environmental and health and safety laws, or liabilities arising from past or future releases of, or exposure to, hazardous substances, will not have a material adverse effect on our business.

Our business, worldwide operations and the operations of our suppliers could be subject to natural disasters and other business disruptions, which could harm our future net sales and financial condition and increase our costs and expenses.

Our worldwide operations and business could be subject to natural disasters and other business disruptions, such as a world health crisis, fire, earthquake, tsunami, volcano eruption, flood, hurricane, power loss, power shortage, telecommunications failure or similar events, which could harm our future net sales and financial condition and increase our costs and expenses. For example, during the first quarter of fiscal 2008, our business was adversely affected by severe weather conditions in China which caused us to experience decreased demand for our products in that region. In addition, our corporate headquarters are located near major earthquake fault lines in California, Spansion Japan s wafer fabrication facilities and Fujitsu s manufacturing facilities are located near major earthquake fault lines in Japan. Also, our assembly and test facilities located in Malaysia and Thailand, and our subcontractors assembly and test facilities in China and other countries in Asia may be affected by tsunamis. In the event of a major earthquake or tsunami, we could experience loss of life of our employees, destruction of facilities or other business interruptions. If such business disruptions result in cancellations of customer orders or contribute to a general decrease in economic activity or demand for our products, or directly impact our marketing, manufacturing, financial, and logistics functions, our results of operations and financial condition could be materially adversely affected.

Furthermore, the operations of our suppliers could be subject to natural disasters and other business disruptions, which could cause shortages and price increases in various essential materials, which are required to manufacture our products or commercial memory die such as DRAMs for incorporation into our MCP products. If we are unable to procure an adequate supply of materials that are required for us to manufacture our products, or if the operations of our other suppliers of such materials are affected by an event that causes a significant business disruption, then we may have to reduce our manufacturing operations. Such a reduction could in the future have a material adverse effect on us.

AMD and Fujitsu may continue to use all of our intellectual property and the intellectual property they have transferred to us.

In connection with our reorganization as Spansion LLC in June 2003, AMD and Fujitsu transferred approximately 400 patents and patent applications to us. In addition, AMD and Fujitsu contributed additional patents to us at the time of our initial public offering. However, both AMD and Fujitsu have retained the rights to use any patents contributed to us for an unlimited period of time. In addition, under their respective patent cross-license agreements with us, AMD and Fujitsu have also obtained licenses to our present and future patents with effective filing dates prior to the later of June 30, 2013, or such date on which they have transferred all of their shares in us, although the scope of patents under license can be impacted by a change in control of the parties or their semiconductor groups. These licenses continue until the last to expire of the patents under license expires and provide AMD and Fujitsu with licenses to all of our present and future patents in existence through such cross-license termination date. Furthermore, we entered into an Amended and Restated Intellectual Property Contribution and Ancillary Matters Agreement with AMD and Fujitsu in connection with our reorganization as Spansion Inc. in December 2005. Pursuant to that agreement, subject to our confidentiality obligations to third parties, and only for so long as AMD s and Fujitsu s ownership interests in us remain above specific minimum levels, we are obligated to identify any of our technology to each of AMD and Fujitsu, and to provide copies of and training with respect to that technology to them. In addition, pursuant to this agreement we have granted a non-exclusive, perpetual, irrevocable fully paid and royalty-free license of our rights, other than patent and trademark rights, in that technology to each of AMD and Fujitsu. Under our non-competition agreement, both AMD and Fujitsu have agreed that they will not directly or indirectly engage in a business, and have agreed to divest any acquired business, that manufactures or supplies standalone semiconductor devices (including single chip, multiple chip or system devices) containing certain Flash memory, which is the business in which we primarily compete. With respect to each of AMD and Fujitsu, this non-competition restriction will last until the earlier of (i) two years from the date such stockholder s ownership in us falls to or below five percent, or (ii) the dissolution of our company. Upon emergence from bankruptcy under the Plan of Reorganization, we expect each of AMD s and Fujitsu s ownership to fall below the five percent threshold. After that time, should they ever decide to re-enter the Flash memory business, AMD or Fujitsu could use our present and future patents and technologies licensed by us to AMD and Fujitsu under the cross licenses and our Amended and Restated Intellectual Property Contribution and Ancillary Matters Agreement to compete against us. If either AMD or Fujitsu were to compete with us, we could be materially adversely affected.

Provisions in our corporate governance documents as well as Delaware law may delay or prevent an acquisition of us that stakeholders may consider favorable.

Our certificate of incorporation and bylaws and Delaware law contain provisions that could make it more difficult for a third party to acquire us without the consent of our board of directors. These provisions include restrictions on the ability of our stockholders to remove directors, a classified board of directors and limitations on action by our stockholders by written consent. In addition, our board of directors has the right to issue preferred stock without stockholder approval, which could be used to make an acquisition of us more difficult. Although we believe these provisions protect our stockholders from coercive or otherwise unfair takeover tactics and thereby provide for an opportunity to receive a higher bid by requiring potential acquirers to negotiate with our board of directors, these provisions apply even if the offer may be considered beneficial by some stakeholders.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

Our principal engineering, manufacturing and administrative facilities as of December 27, 2009, comprise approximately 3.1 million square feet and are located in the United States, Europe, Middle East and Asia. Over 2.8 million square feet of this space is in buildings we own in Sunnyvale, California; Austin, Texas; Kuala Lumpur, Malaysia; Penang, Malaysia; and Bangkok, Thailand. The remainder of this space is leased. We lease approximately 240,000 square feet of office and warehouse space in Europe and Asia. Our Fab 25 facility in Austin, Texas and our facility in Sunnyvale, California are encumbered by liens securing our senior secured term loan facility and our senior secured floating rate notes. See Part II, Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations Contractual Obligations.

Our facility leases have terms of generally one to five years. We currently do not anticipate difficulty in either retaining occupancy of any of our facilities through lease renewals prior to expiration or through month-to-month occupancy or replacing them with equivalent facilities.

ITEM 3. LEGAL PROCEEDINGS

Tessera ITC Action

On April 17, 2007, Tessera, Inc. filed a complaint under section 337 of the Tariff Act of 1930, 19 U.S.C. § 1337, in the United States International Trade Commission (ITC) against respondents ATI Technologies, Inc., Freescale Semiconductor, Inc., Motorola, Inc., Qualcomm, Inc., Spansion Inc., Spansion LLC and STMicroelectronics N.V. Tessera claims that face up and stacked-chip small format laminate Ball Grid

Array (BGA) packages, including the Spansion 5185941F60 chip assembly, infringe certain specified claims of United States Patent Nos. 5,852,326 and 6,433,419 (Asserted Patents). The complaint requests that the ITC institute an investigation into the matter. The complaint seeks a permanent exclusion order pursuant to section 337(d) of the Tariff Act of 1930, as amended, excluding from entry into the United States all semiconductor chips with small format laminate BGA semiconductor packaging that infringe any of the Asserted Patents, and all products containing such infringing small format laminate BGA semiconductor packaged chips. The complaint also seeks a permanent cease and desist order pursuant to section 337(f) of the Tariff Act of 1930, as amended, directing respondents with respect to their domestic inventories to cease and desist from marketing, advertising, demonstrating, sampling, warehousing inventory for distribution, offering for sale, selling, distributing, licensing, or using any semiconductor chips with small format laminate BGA semiconductor packaging that infringe any of the Asserted Patents, and/or products containing such semiconductor chips. On May 15, 2007, the ITC instituted an investigation pursuant to 19 U.S.C. § 1337, entitled *In the Matter of Certain Semiconductor Chips with Minimized Chip Package Size and Products Containing Same*, Inv. No. 337-TA-605, identifying ATI Technologies, ULC, Freescale Semiconductor, Inc., Motorola, Inc., Spansion Inc., Spansion LLC and STMicroelectronics N.V. (Respondents) as respondents. On June 8, 2007, Respondents filed a motion to stay the ITC investigation pending reexamination of the Asserted Patents by the U.S. Patent and Trademark Office. On July 11, 2007, Administrative Law Judge Carl C. Charneski set an Initial Determination date of May 21, 2008 and a target date for completion of the ITC Investigation of August 21, 2008. On October 17, 2007, the ITC investigation was reassigned to Administrative Law Judge Theodore Essex, who set a hearing for February 25, 2008. On February 26, 2008, Judge Essex issued an Initial Determination granting respondents motion for a stay of the ITC investigation pending completion of the re-examination of the Asserted Patents by the U.S. Patent and Trademark Office. On March 4, 2008, Tessera filed, with the ITC, a Petition for Review of the Initial Determination Ordering Stay. On March 27, 2008, the ITC issued an order reversing Judge Essex s Initial Determination, and denying Respondents motion for a stay of the ITC investigation pending reexamination of the Asserted Patents. On May 13, 2008, Judge Essex set an Initial Determination date of October 20, 2008, with a hearing date of July 14, 2008, and a target date for completion of the ITC investigation of February 20, 2009. On July 14, 2008, Judge Essex held an evidentiary hearing in the ITC investigation, and completed the hearing on July 18, 2008. On October 16, 2008, Judge Essex issued an order resetting the Initial Determination date to December 1, 2008, and the target date for completion of the ITC investigation to April 3, 2009. On December 1, 2008, Judge Essex issued an Initial Determination, ruling that the accused small-format BGA packages of Spansion Inc. and Spansion LLC and the other Respondents did not infringe the asserted claims of the Asserted Patents and, therefore, Spansion Inc. and Spansion LLC and the other Respondents were not in violation of section 337 of the Tariff Act of 1930. On December 15, 2008, Tessera filed with the ITC a petition to review the Initial Determination. On January 30, 2009, the ITC issued a notice to review in part Judge Essex s decision finding no violation of section 337. On February 10, 2009, the ITC issued an order resetting the target date for completion of the ITC Investigation to April 14, 2009. On March 31, 2009 the ITC issued an order requesting additional briefing on certain remedy issues and resetting the target date for completion of the ITC Investigation to May 20, 2009. On May 20, 2009 the ITC issued a Final Determination reversing the Initial Determination by finding that there was a violation of 19 U.S.C. § 1337 by Spansion Inc. and Spansion LLC, Qualcomm, Inc., ATI Technologies, Motorola, Inc. STMicroelectronics N.V. and Freescale Semiconductor, Inc., and determined that the appropriate form of relief is (1) a limited exclusion order under 19 U.S.C. § 1337(d)(1) prohibiting the unlicensed entry of semiconductor chips with minimized chip package size and products incorporating these chips that infringe one or more of claims 1, 2, 6, 12, 16-19, 21, 24-26, and 29 of the 326 patent and claims 1-11, 14, 15,19, and 22-24 of the 419 patent, and are manufactured abroad by or on behalf of, or imported by or on behalf of, Spansion, Qualcomm, ATI, Motorola, STMicroelectronics N.V. and Freescale; and (2) cease and desist orders directed to Motorola, Qualcomm, Freescale and Spansion. The cease and desist order directed to Spansion prohibits importing, selling, marketing, advertising, distributing, offering for sale, transferring (except for exportation) and soliciting U.S. agents or distributors for certain semiconductor chips that are covered by the patents asserted in the action. The ITC further determined that the bond for temporary importation during the period of Presidential review which expired 60 days after May 20, 2009 should be in the amount of 3.5 percent of the value of the imported articles that are subject to the order. On June 2, 2009, Spansion and the other respondents to the investigation jointly filed with the ITC a motion to stay the effect of the ITC decision pending appeal to the U.S. Court of Appeals for the Federal Circuit (the Federal Circuit). On July 17, 2009, the ITC denied the motion. On July 20, 2009, Spansion appealed the ITC decision to the Federal Circuit and filed an emergency motion for stay pending appeal and immediate temporary stay. The Federal Circuit denied the stay motions on September 8, 2009. The principal brief in the Federal Circuit appeal was filed on October 30, 2009. No date for oral argument of the appeal has been set.

Fast Memory Erase LLC v. Spansion Inc., et al.

On June 9, 2008, Fast Memory Erase LLC filed a complaint in the U.S. District Court for the Northern District of Texas alleging patent infringement against Spansion Inc., Spansion LLC, Intel Corp., Numonyx B.V., Numonyx, Inc., Nokia Corp., Nokia Inc., Sony Ericsson Mobile Communications AB, Sony Ericsson Mobile Communications (USA), Inc., and Motorola, Inc. The case is styled, Fast Memory Erase, LLC v. Spansion Inc., Spansion LLC, et al., Case No. 3:08-CV-00977-M (N.D. Tex.). Fast Memory Erase s complaint alleges that Spansion s NOR Flash products using floating gate technology infringe one or more claims of U.S. Patent No. 6,236,608 (the 608 patent). Fast Memory Erase has also asserted U.S. Patent No. 6,303,959 (the 959 patent) in its complaint against the products of other defendants, namely Intel and Numonyx, but it has not asserted the 959 patent against any Spansion products. On December 22, 2008, Fast Memory Erase filed an amended complaint. In its amended complaint, Fast Memory Erase added Apple, Inc. as a defendant. Fast Memory Erase in its complaint is seeking: a declaration that the 608 and 959 patents are valid and enforceable; a declaration that Spansion and the other defendants have infringed the 608 and 959 patents; a declaration that the defendant s infringement was willful; an award of damages in an unspecified amount; entry of a preliminary, and thereafter, permanent injunction against the defendants for direct , active inducement, and/or contributory infringement of the 608 and 959 patents; an award of its expenses, costs and attorneys fees pursuant to 35 U.S.C. § 285; an award of increased damages in an amount not less than (3) three times the amount of damages found by the jury or assessed by the court for the defendant s willful infringement; an award of interest on its damages; and such other relief as the Court deems just and proper. Spansion has answered Fast Memory Erase s complaint and amended complaint. Spansion s answers assert that Spansion does not infringe the 608 patent and that the 608 patent is invalid. In its answers, Spansion also asserts counterclaims against Fast Memory Erase for declaratory judgments of non-infringement and invalidity. The case was stayed against Spansion as a result of the Chapter 11 Cases until May 18, 2009. The U.S. Bankruptcy Court preliminarily lifted the stay and set June 23, 2009 as the date for a final determination on the stay. The parties subsequently agreed to lift the stay so that the U.S. District Court could proceed with a Markman hearing to determine the meaning of certain claims, which was held on September 16, 2009. No ruling has yet been issued as a result of the Markman hearing with respect to the 608 patent. On February 2, 2010, the judge issued a Memorandum Opinion and Order construing the claims of the 959 patent. On December 9, 2009 an order was entered staying the case as it relates to the 608 patent pending a reexamination proceeding pending in the U.S. Patent and Trademark Office (the PTO) regarding the 608 patent. The court has asked for an update on the status of the reexamination proceedings in six months, or when the PTO takes action on the reexamination proceeding, whichever is earlier.

LSI, Agere ITC Investigation

On April 18, 2008, LSI Corporation and Agere Systems, Inc. (collectively Complainants) filed a complaint under section 337 of the Tariff Act of 1930, 19 U.S.C. § 1337, in the ITC against respondents United Microelectronics Corporation, Integrated Device Technology, Inc., AMIC Technology Corporation, Elpida Memory, Inc., Freescale Semiconductor, Inc., Grace Semiconductor Manufacturing Corporation, Microchip Technology, Inc., Micromas Semiconductor Holding, AG, National Semiconductor Corporation, Nanya Technology Corporation, NXP B.V., ON Semiconductor Corporation, Powerchip Semiconductor Corporation, ProMOS Technologies, Inc., Spansion, Inc., STMicroelectronics NV and Vanguard International Semiconductor Corporation. The complaint alleges that certain Spansion Flash products, including Spansion s 4 Mb CMOS 3.0 Volt-only Simultaneous Read/Write Flash Memory and 1 G MirrorBit NOR Flash products, infringe at least claim 1 of U.S. Patent No. 5,227,335 (the Asserted Patent). The complaint identifies, under the heading Related Litigations, other lawsuits involving the Asserted Patent, including *Agere Systems, Inc. v. Atmel*

Corporation, Civil Action No. 2:02-CV-864 (E.D. Pa.) (the Atmel case). The complaint requests that the ITC institute an investigation into the matter. The complainant seeks a permanent exclusion order pursuant to section 337(d) of the Tariff Act of 1930, as amended, excluding from entry into the United States all semiconductor IC devices and products containing same, made by a method that infringes one or more claims of the Asserted Patent. The complainant also seeks a permanent cease and desist order pursuant to section 337(1) of the Tariff Act of 1930, as amended, directing respondents to cease and desist from importing, selling, offering for sale, using, demonstrating, promoting, marketing, and/or advertising in the United States, or otherwise transferring outside the United States for sale in the United States, semiconductor IC devices and products containing same made by a method that infringes one or more claims of the Asserted Patent. On May 16, 2008, the ITC instituted an investigation pursuant to 19 U.S.C. § 1337, entitled *In the Matter of Certain Semiconductor Integrated Circuits Using Tungsten Metallization and Products Containing Same* No. 337-TA-648, identifying United Microelectronics Corporation, Integrated Device Technology, Inc., AMIC Technology Corporation, Elpida Memory, Inc., Freescale Semiconductor, Inc., Grace Semiconductor Manufacturing Corporation, Microchip Technology, Inc., Micromas Semiconductor Holding, AG, National Semiconductor Corporation, Nanya Technology Corporation, NXP B.V., ON Semiconductor Corporation, Powerchip Semiconductor Corporation, ProMOS Technologies, Inc., Spansion, Inc., STMicroelectronics NV and Vanguard International Semiconductor Corporation (Respondents) as respondents. On June 5, 2008, respondents Elpida Memory, Inc., Freescale Semiconductor, Inc., Grace Semiconductor Manufacturing Corporation, Integrated Device Technology, Microchip Technology, Inc., Nanya Technology Corp., Powerchip Semiconductor Corp., Spansion Inc. and ST Microelectronics N.V. filed a joint motion for summary determination that Complainant is precluded from re-litigating an invalid patent, based upon the jury finding of invalidity and the court ruling affirming the invalidity finding of the Asserted Patent in the *Atmel* case. On June 27, 2008, Administrative Law Judge Carl L. Charneski set an Initial Determination date of May 21, 2009, with a hearing to be completed by March 13, 2009, and a target date for completion of the ITC investigation of August 21, 2009. On September 18, 2008, Judge Charneski granted Complainants motion to add five respondents, Dongbu HiTek Semiconductor Business; Jazz Semiconductor, Magnachip Semiconductor; Qimonda AG, and Tower Semiconductor, Ltd. On October 30, 2008, Judge Charneski denied Complainants request to add additional claims of infringement against Spansion, and also suspended the current procedural schedule. On November 5, 2008, Judge Charneski issued an order modifying procedural schedule, setting a hearing date of July 20, 2009 and issued a separate order setting an Initial Determination date of September 21, 2009, and a target date for completion of the ITC investigation of January 21, 2010. On December 11, 2008, Judge Charneski issued an Initial Determination denying respondents motion for summary determination that Complainant should be precluded from re-litigating an invalid patent. On February 3, 2009, the ITC issued an opinion affirming the ITC determination that Complainant is not precluded from re-litigating the validity of the patent. A hearing was held July 20, 2009 through July 27, 2009. The initial determination based upon that hearing was issued on September 21, 2009. The judge held that the patent asserted by LSI and Agree is invalid and that Spansion is not a proper party to the action. On September 21, 2009 Judge Charneski issued an Initial Determination ruling that claims 1, 3, and 4 of the 335 patent were invalid due to anticipation in view of certain IBM prior art, and that LSI/Agere had not established that Spansion Inc. imported or sold a product in the U.S. according to an accused process. Consequently, Judge Charneski ruled that Spansion Inc. was not in violation of section 337 of the Tarriff Act as accused by LSI/Agere. On October 5, 2009 LSI/Agere filed with the ITC a petition for review of the Initial Determination. On November 23, 2009 the ITC issued an order remanding the investigation to Judge Charneski to determine whether claim 4 of the 335 patent was also rendered obvious by the IBM prior art in light of the other prior art asserted by the Respondents. On January 14, 2010 Judge Charneski issued a Remand Initial Determination finding that the IBM prior art alone did not render claim 4 of the 335 patent invalid due to obviousness. On January 21, 2010 the ITC issued a notice setting a revised target date for completion of the investigation to March 22, 2010.

We believe that we have meritorious defenses against LSI s and Agere s claims and we intend to defend this proceeding vigorously.

Table of Contents

Spansion v. Samsung Patent Infringement Litigation

Spansion is currently a party to four, and Spansion Japan Limited is a party to one additional, patent infringement proceedings involving Samsung Electronics Co., Ltd.:

Patent Litigation Settlement Agreement with Samsung Electronics Co., Ltd. (Samsung)

On April 7, 2009, Spansion announced that it had settled its patent litigation lawsuits with Samsung. As part of the settlement, Samsung agreed to pay Spansion $70 million and both parties agreed to exchange rights in their patent portfolios in the form of licenses and covenants subject to a settlement agreement. On June 2, 2009, the U.S. Bankruptcy Court entered an order denying Spansion s motion seeking approval of the settlement agreement. By its terms, the settlement agreement has been terminated automatically as a result of the failure of the U.S. Bankruptcy Court to approve the settlement agreement by June 2, 2009 (sixty days from when Spansion filed a motion seeking U.S. Bankruptcy Court approval). In addition, as a result of the failure of the U.S. Bankruptcy Court to approve the settlement agreement, the lawsuit by Samsung against Spansion Japan Limited is no longer stayed, and the cases in the U.S. District Court and the ITC have resumed.

Samsung ITC Investigation

On November 17, 2008 Spansion Inc. and Spansion LLC filed a complaint under section 337 of the Tariff Act of 1930, 19 U.S.C. § 1337, in the United States International Trade Commission (ITC) against respondents Samsung Electronics Co., Ltd., Samsung Electronics America, Inc., Samsung International, Inc., Samsung Semiconductor, Inc., and Samsung Telecommunications America, LLC and Apple, Inc., Hon Hai Precision Industry Co., Ltd., AsusTek Computer Inc., Asus Computer International, Inc., Kingston Technology Company, Inc., Kingston Technology (Shanghai) Co. Ltd., Kingston Technology Far East Co., Kingston Technology Far East (Malaysia) Sdn. Bhd., Lenovo Group Limited, Lenovo (United States) Inc., Lenovo (Beijing) Limited, Lenovo Information Products (Shenzhen) Co., Ltd., Lenovo (Huiyang) Electronic Industrial Co., Ltd., Shanghai Lenovo Electronic Co., Ltd., PNY Technologies, Inc., Research In Motion, Ltd., Research In Motion Corporation, Sony Corporation, Sony Corporation of America, Sony Ericsson Mobile Communications AB, Sony Ericsson Mobile Communications (USA), Inc., Beijing SE Putian Mobile Communication Co., Ltd., Transcend Information Inc., Transcend Information Inc. (US), Transcend Information Inc. (Shanghai Factory), Verbatim Americas LLC, and Verbatim Corporation (collectively Downstream Respondents). In the ITC Complaint, Spansion alleges that Samsung and Downstream Respondents infringe United States Patent Nos. 6,380,029, 6,080,639, 6,376,877, and 5,715,194 (the Asserted Patents), which are owned by Spansion, through the unlawful importation into the United States of certain Samsung flash memory chips. The complaint seeks a permanent general exclusion order pursuant to section 337(d) of the Tariff Act of 1930, as amended, excluding from entry into the United States the Samsung chips that infringe any of the Asserted Patents, and all products produced by Downstream Respondents that contain such chips. The complaint also seeks a permanent cease and desist order pursuant to section 337(f) of the Tariff Act of 1930, as amended, prohibiting Samsung and Downstream Respondents from importing, selling for importation, using, offering for sale, selling after importation, building inventory for distribution, distributing, licensing, or otherwise transferring within the United States, Samsung chips that the Asserted Patents, and/or products containing such chips. On December 18, 2008 the ITC instituted an investigation pursuant to 19 U.S.C. § 1337, entitled *In the Matter of Certain Flash Memory Chips and Products Containing Same*, Inv. No. 337-TA-664, identifying Samsung and Downstream Respondents (Respondents) as respondents. On December 19, 2008, Administrative Law Judge Charles E. Bullock set a target date for completion of the ITC Investigation of April 19, 2010, and set the hearing to begin July 27, 2009. Subsequently, on February 9, 2009, Judge Bullock extended the target date for the investigation to June 18, 2010, and re-set the hearing to begin on September 28, 2009. Each of the Respondents has entered an appearance and answered the complaint. On January 30, 2009, the parties submitted their respective discovery statements, which included proposed discovery schedules, to Judge Bullock. On March 12, 2009, this action was stayed pending U.S. Bankruptcy Court approval of a settlement agreement between Spansion and Samsung. On June 2, 2009, the U.S. Bankruptcy Court entered an order denying Spansion s motion seeking approval of the settlement agreement. As a result of the failure of the U.S. Bankruptcy Court to approve the settlement agreement, Spansion s case against Samsung in the ITC has resumed. On June 30, 2009, the judge in the ITC investigation entered an order extending to January 18, 2011 the target date for completion of the investigation, setting the trial date for April 19, 2010, and issuing a new procedural schedule. On October 16, 2009 the judge in the ITC investigation entered an order modifying the procedural schedule setting the trial date for May 3, 2010. Discovery in this case is ongoing. A Markman hearing was held on November 10, 2009. No order has been issued as a result of the Markman hearing.

Spansion v. Samsung District Court Action

On November 17, 2008, Spansion LLC filed a complaint, Civil Action No. 08-855-SLR, in the United States District Court for District of Delaware, against defendants Samsung Electronics Co. LTD., and Samsung Electronics America, Inc., Samsung Semiconductor, Inc., Samsung Telecommunications America, LLC, and Samsung Austin Semiconductor, LLC (Samsung U.S.). The complaint alleges that certain Samsung flash memory chips infringe United States Patent Nos. 6,455,888, 6,509,232, 5,831,901, 5,991,202, 6,433,383, and 6,246,610 (the Spansion Patents). The complaint seeks a judgment that Samsung infringes the Spansion Patents, permanent injunctive relief and damages, a trebling of damages for alleged willful conduct, and attorney s fees, costs, and expenses. On January 8, 2009, Samsung U.S. answered the Complaint, and asserted a number of affirmative defenses. Samsung U.S. s answer seeks a judgment of non-infringement as well as attorney s fees, costs, and expenses in connection with defending against Spansion s claims. On January 16, 2009, Samsung answered the Complaint, asserted affirmative defenses and counterclaimed that Spansion infringes United States Patent Nos. 6,930,050, 5,748,531, 5,740,065, 5,567,987, and 5,173,442 (the Samsung Patents), owned by Samsung. Samsung s counterclaim seeks a judgment that Spansion infringes the Samsung Patents, permanent injunctive relief and damages, a trebling of damages for alleged willful conduct, and attorney s fees, costs, and expenses. On March 31, 2009, this action was stayed pending U.S. Bankruptcy Court approval of a settlement agreement between Spansion and Samsung. On June 2, 2009, the U.S. Bankruptcy Court entered an order denying Spansion s motion seeking approval of the settlement agreement. As a result of the failure of the U.S. Bankruptcy Court to approve the settlement agreement, Spansion s case against Samsung in the U.S. District Court for District of Delaware has resumed. On August 3, 2009, Samsung amended its counterclaims to remove Patent Nos. 6,930,050 and 5,740,065, from the action. On August 13, 2009, Spansion responded to Samsung s counterclaims as to the remaining patents asserted by Samsung (i.e., United States Patent Nos., 5,748,531, 5,567,987, and 5,173,442). The action is presently scheduled for trial in May of 2011 and discovery is underway.

Samsung v. Spansion Japan Ltd.

On January 28, 2009, Samsung filed two patent infringement actions in the Tokyo District Court in Japan against Spansion Japan Ltd. (Spansion Japan) alleging that certain flash memory chips manufactured or sold by Spansion Japan infringe certain Japanese patents allegedly owned by Samsung. The actions allege infringement of Japanese patents JP 3834189 and JP 3505324 respectively. The two actions have been consolidated for trial. The complaints seek both injunctive relief and damages. On March 31, 2009, this action by Samsung against Spansion Japan was stayed pending approvals of the U.S. Bankruptcy Court and the Tokyo District Court of a settlement agreement between Spansion and Samsung.

On April 7, 2009, Spansion announced that it had settled its patent infringement litigation with Samsung including the proceedings referenced above. As part of the settlement, Samsung agreed to pay Spansion $70 million and both parties exchanged rights in their patent portfolios in the form of licenses and covenants subject to a confidential settlement agreement. The settlement was subject to Bankruptcy Court approval in both the U.S. and Japan and, if approved, would end the patent disputes between the two companies. On May 18, 2009, the U.S. Bankruptcy Court held a hearing to review Spansion s motion for approval of the settlement. On June 2, 2009, the U.S. Bankruptcy Court entered an order denying Spansion s motion seeking approval of the settlement agreement. By its terms, the settlement agreement has been terminated automatically as a result of the failure of the U.S. Bankruptcy Court to approve the settlement agreement by June 2, 2009 (sixty days from when Spansion filed a motion seeking U.S. Bankruptcy Court approval). In addition, as a result of the failure of the U.S. Bankruptcy Court to approve settlement agreement, the action by Samsung against Spansion Japan is no longer

Table of Contents

stayed, and the cases in the U.S. District Court and the ITC have resumed. A technical hearing was held on December 18, 2009, and a subsequent hearing occurred on January 28, 2010. Additional briefing has been requested by the court, the next of which is due March 1, 2010.

Samsung v. Spansion ITC Investigation

On July 31, 2009, Samsung filed a patent infringement complaint with the ITC against Spansion Inc. and Spansion LLC (collectively, Spansion), Spansion Japan Limited, and the following downstream respondents: Alpine Electronics, Inc., Alpine Electronics of America, Inc., D-Link Corporation, D-Link Systems, inc., Slacker, Inc., Synology, Inc., Synology North America Corp., Shenzhen Egreat Co., Ltd., EGreat USA, and Appro International, Inc. The ITC commissioned its investigation of Samsung s complaint on August 27, 2009. Subsequently, certain of Spansion s creditors sought an order from the U.S. Bankruptcy Court seeking a stay of Samsung s ITC action. On October 1, 2009, the U.S. Bankruptcy Court issued an order granting the motion to stay Samsung s ITC action against Spansion. Both Samsung and the ITC have appealed this order.

Samsung v. Spansion International, Inc.

On July 31, 2009, Samsung Electronics Co., Ltd. commenced an action in the Fourth Civil Division of the Federal Court in Dusseldorf, Germany against Spansion International, Inc. and other third parties alleging patent infringement since March 2, 2009 of German patent DE 693 27 499 T2 (EP 0 591 009 B1). The action seeks damages in the amount of 500,000 (approximately $703,460 as of December 27, 2009). An initial hearing to establish the schedule for the case was set for October 20, 2009. On September 4, 2009, Spansion filed a motion seeking to enforce the automatic stay as to this action, and on November 4, 2009, the U.S. Bankruptcy Court issued an order granting Spansion s motion to stay this action.

Cabreros, et al. v. Spansion LLC, et al.

On March 6, 2009, Wesley Cabreros and David Refuerzo, individually and on behalf of other persons similarly situated, filed a complaint in the U.S. Bankruptcy Court, Adversary Proceeding No. 09-50409, for alleged violations of both the California WARN Act and Federal WARN Act against Spansion LLC and Spansion Inc. In addition to seeking class certification, the complaint seeks damages, costs and attorneys fees. The complaint also seeks payment of 11 U.S.C. § 503 priority claims in favor of the plaintiffs and other similarly situated former employees for their unpaid wages, salary, commissions, bonuses, accrued holiday pay, accrued vacation pay, pension and 401(K) contributions and other ERISA benefits, or a determination that the first $10,950 of the WARN Act claims are entitled to priority status under 11 U.S.C. 507(a)(4) and the remainder are unsecured claims. The plaintiffs also seek to recover attorneys fees and costs as allowed priority claims under 11 U.S.C. § 503. On July 22, 2009, the U.S. Bankruptcy Court certified the class. On October 6, 2009, the parties engaged in a mediation and reached an agreement in principle to settle the litigation conditioned upon U.S. Bankruptcy Court approval. As of December 27, 2009, the Company had accrued the settlement amount of $8.6 million, which was included in liabilities subject to comprise.

Creditor Proceedings

Many creditors initiated proceedings against one or more of the Debtors referred to in the voluntary petitions under Chapter 11 of the U.S. Bankruptcy Code to collect amounts allegedly due those creditors. After the filing date of the petition, all actions to enforce or otherwise effect payment or repayment of liabilities of any Debtor preceding the Petition Date, as well as pending litigation against any Debtor, are stayed as of the Petition Date. Absent further order of the applicable courts and subject to certain exceptions, no party may take any action to recover on pre-petition claims against any Debtor.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of security holders during the fourth quarter of the fiscal year covered by this Report.

Table of Contents

PART II

ITEM 5. MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Market Price of Common Stock

From December 15, 2005 until May 6, 2009, our Common Stock traded on the NASDAQ Global Select Market under the symbol SPSN. As described below, we were delisted from the NASDAQ Stock Market on May 7, 2009. After our delisting, our Common Stock has been quoted on The Pink Sheets under the symbol SPSNQ.PK.

The following table sets forth the high and low per shares sales prices for our Common Stock for fiscal 2009 and fiscal 2008 as reported on the NASDAQ Global Select Market through May 6, 2009, and the high and low bid prices as reported on The Pink Sheets commencing on May 7, 2009. Over the counter market quotations reflect interdealer prices, without retail marked-up, marked-down or commissions and may not necessarily represent actual transactions.

	High	Low
Fiscal Year Ended December 27, 2009		
Fourth Quarter	$ 0.55	$ 0.06
Third Quarter	$ 0.33	$ 0.07
Second Quarter	$ 0.32	$ 0.05
First Quarter	$ 0.23	$ 0.01

	High	Low
Fiscal Year Ended December 28, 2008		
Fourth Quarter	$ 1.69	$ 0.19
Third Quarter	$ 3.05	$ 1.56
Second Quarter	$ 3.70	$ 2.25
First Quarter	$ 4.29	$ 2.10

As of February 8, 2010, there were 21 holders of record of our Common Stock. Because many of our shares are held by brokers and other institutions on behalf of stockholders, we are unable to estimate the total number of stockholders represented by these record holders. The closing sale price of our Common Stock on February 5, 2010 was $0.09 per share.

We currently do not plan to pay dividends on shares of our common stock in the foreseeable future and are currently prohibited from doing so in specific circumstances under agreements governing our borrowing arrangements.

On March 4, 2009, we received notice of a determination of the NASDAQ Listing Qualifications Department to delist our common stock from trading on the NASDAQ Global Select Market because of the Chapter 11 Cases. On March 16, 2009, we received an additional notice of a determination for our failure to timely file our Annual Report on Form 10-K for the fiscal year ended December 28, 2008. On April 16, 2009, we received an additional notice of a determination that our failure to pay certain fees in accordance with NASDAQ Marketplace Rule 5210(d) is an additional basis for delisting our securities from the NASDAQ Global Select Market. On April 23, 2009, we attended a hearing to contest these delisting determinations. On May 5, 2009, NASDAQ denied our request for continued listing on The NASDAQ Stock Market and it suspended trading of shares of our common stock effective at the open of business on Thursday, May 7, 2009, pursuant to an application on Form 25-NSE filed with the Securities and Exchange Commission. We did not request a review of this decision. Since delisting, our common stock has been publicly traded on the Pink Sheets with ticker symbol SPSNQ.PK. However, because trading on the Pink Sheets requires a market maker to quote our common stock, trading on the Pink Sheets is not within our control and could be discontinued at any time if no market maker is willing to offer a quote.

Table of Contents

The information under the caption Equity Compensation Plan Information in Part III, Item 12 of this Annual Report on Form 10-K is incorporated herein by reference.

Stock Performance Graph

This performance graph shall not be deemed filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended (the Exchange Act), or incorporated by reference into any filing of Spansion under the Securities Act of 1933, as amended, or the Exchange Act, except as shall be expressly set forth by specific reference in such filing.

The following graph shows a comparison from December 16, 2005 (the date our Common Stock commenced trading) through December 27, 2009 of the cumulative total return for our Common Stock, The Nasdaq Market Index and the S&P 500 Semiconductors Index. Such returns are based on historical results and are not intended to suggest future performance. Data for The Nasdaq Market Index and the S&P 500 Semiconductors Index assume reinvestment of dividends.

ITEM 6. SELECTED FINANCIAL DATA

The following summary historical financial data should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and related notes included elsewhere in this Annual Report on Form 10-K.

Fiscal years in the table below included 52 weeks each, except for fiscal 2006, which included 53 weeks.

	Year Ended December 27, 2009	Year Ended December 28, 2008(1)	Year Ended December 30, 2007(1)	Year Ended December 31, 2006(1)	Year Ended December 25, 2005
	(in thousands, except per share amounts)				
Statement of Operations Data:					
Net sales	$ 1,059,408	$ 1,630,573	$ 1,627,253	$ 1,310,479	$
Net sales to related parties/members	351,245	651,230	873,560	1,268,795	2,002,805
Total net sales	1,410,653	2,281,803	2,500,813	2,579,274	2,002,805
Cost of sales	1,103,757	2,193,345	2,065,143	2,063,639	1,809,929
Gross profit	306,896	88,458	435,670	515,635	192,876
Other expenses:					
Research and development	136,449	431,808	436,785	342,033	292,926
Sales, general and administrative	216,298	253,878	239,317	264,358	184,833
In-process research and development		10,800			
Restructuring charges	46,852	11,161			
Asset impairment charges(3)	12,538	1,652,622			
Operating loss before reorganization items	(105,241)	(2,271,811)	(240,432)	(90,756)	(284,883)
Interest and other income, net	4,038	5,200	32,595	11,681	3,173
Interest expense(5)	(50,976)	(105,536)	(87,460)	(74,156)	(45,032)
Gain on deconsolidation of subsidiary(6)	30,100				
Loss before reorganization items and income taxes	(122,079)	(2,372,147)	(295,297)	(153,231)	(326,742)
Reorganization items	(391,383)				
Loss before income taxes	(513,462)	(2,372,147)	(295,297)	(153,231)	(326,742)
(Provision) benefit for income taxes(4)	(597)	(62,865)	25,144	2,215	22,626
Net loss	$ (514,059)	$ (2,435,012)	$ (270,153)	$ (151,016)	$ (304,116)
Net loss per common share					
Basic and diluted(2)	$ (3.18)	$ (15.69)	$ (2.00)	$ (1.17)	$ (4.15)
Shares used in per share calculation:					
Basic and diluted(2)	161,847	155,162	134,924	128,965	73,311

	December 27, 2009	December 28, 2008(1)	December 30, 2007(1)	December 31, 2006(1)	December 25, 2005
			(in thousands)		
Balance Sheet Data:					
Cash, cash equivalents and marketable securities	$ 425,238	$ 116,387	$ 415,742	$ 885,769	$ 725,816
Working capital (deficit)	553,023	(1,183,337)	592,518	1,085,027	881,902
Total assets	1,437,977	1,773,872	3,813,863	3,547,726	3,301,965
Long-term debt and capital lease obligations, including current portion, short term note, and notes payable to banks under revolving loans	64,150	1,442,782	1,294,189	1,004,036	759,613

Liabilities subject to compromise	987,127				
Total stockholders equity (deficit)	(857,693)	(450,647)	1,737,810	1,957,780	1,921,977

(1) Statement of operations and balance sheet data for these periods have been adjusted to reflect the change in accounting for our Exchangeable Senior Subordinated Debentures as described in Note 4 of Notes to Consolidated Financial Statements.

(2) Diluted net loss per share is computed using the weighted-average number of common shares and excludes potential common shares, as their effect is anti-dilutive.

(3) The asset impairment charge for fiscal 2009 includes pre-tax impairment on an equity investment and loan to an investee. The asset impairment charge for fiscal 2008 includes pre-tax impairment related to long-lived assets held for use of $1.6 billion, and impairment related to goodwill and intangible assets of $20.8 million and $53.5 million, respectively.

(4) The provision for income taxes in fiscal 2009 includes a decrease of $457.9 million in valuation allowances against deferred tax assets in our Japanese subsidiary resulting from the deconsolidation of our Japanese subsidiary in March 2009. However, the decrease in the amount of deferred tax assets had no impact on the provision for income taxes since the deferred tax assets had a full valuation allowance. The provision for income taxes in fiscal 2008 includes an increase of $462.6 million in valuation allowances against deferred tax assets in foreign jurisdictions. This increase occurred because we did not believe it was more likely than not that these deferred tax assets would be realized in these jurisdictions. The increase in valuation allowance resulted in a $64.5 million income tax expense associated with deferred tax assets of Spansion Japan.

(5) Contractual interest expense for the year ended December 27, 2009 was $89.4 million.

(6) The gain on deconsolidation of subsidiary represents the difference between the carrying value of our investment in and receivables from Spansion Japan immediately before deconsolidation and the estimated fair value of our retained non-controlling interest in Spansion Japan, which was zero then and as of December 27, 2009.

Table of Contents

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 consolidated financial statements and related notes as of December 27, 2009 and December 28, 2008 and for the fiscal years ended December 27, 2009, December 28, 2008 and December 30, 2007, which are elsewhere in this Annual Report on Form10-K.

Executive Summary

Historically, one-half or more of our revenues came from the cell phone manufacturers, or the wireless, market. Over the last decade the dynamics of that market changed as a result of increasing feature sets that drove an increased need for data storage that favored an implementation of NAND over NOR architectures, and a consolidation of cell phone manufacturers. At the same time, customers constituting a large portion of demand for NOR flash memory demanded increasing investment in engineering and leading edge wafer manufacturing capability, as well as ever faster decreases in the prices for products. These changes eroded our profitability to unsustainable levels.

Shortly after entering bankruptcy proceedings we began exiting a large portion of the wireless market. While this significantly reduced our revenue, it allowed us to dramatically reduce our engineering spending without impairing our ability to compete in other markets. Our exit from a large portion of the wireless market, related reductions in development spending and capital expenditures, combined with other cost reductions including disposal of manufacturing facilities, enabled us to begin generating significant cash flow. Ultimately, we achieved modest profitability in the later quarters of 2009 even as our revenues contracted approximately forty percent from historical run-rates.

We continue to have leading market share and remain dedicated to, and focused on, the embedded market, i.e., the market for NOR Flash memory used for code storage in industrial, consumer, communications, gaming, and automotive applications. We intend to continue to selectively engage in portions of the wireless market where we can do so advantageously. We believe that though the embedded market is mature and will grow more slowly than some other sectors of the semiconductor industry, we can compete successfully with our continued focus on providing best in class customer service, quality and reliability, and solutions engineering. We believe we can mitigate the historical and anticipated trend of rapid selling price reductions by serving applications with growing unit demand, migrating customers to higher density and more feature-rich devices, capturing market share, and expanding our product offerings.

Creditor Protection Proceedings

During 2008, the macroeconomic environment deteriorated significantly, causing a sharp decline in worldwide demand for consumer goods, and consequently a sharp reduction of demand for our products. Furthermore, continued tightening of credit availability curtailed our ability to execute certain liquidity initiatives launched in the third quarter of 2008, including re-negotiating payment terms with vendors, refinancing our existing short- and long-term debt and lease obligations, or obtaining new financing facilities. As these events unfolded, we intensified our strategic restructuring efforts to include, among other things, pursuing a potential sale of some or all of our assets. The sharp decline in demand, coupled with our inability to execute liquidity initiatives limited our ability to generate sufficient funding for our operations and meet our debt servicing requirements.

On February 10, 2009, Spansion Japan Limited, a wholly-owned subsidiary of Spansion LLC (Spansion Japan), filed a proceeding under the Corporate Reorganization Law (*Kaisha Kosei Ho*) of Japan to obtain protection from Spansion Japan s creditors (the Spansion Japan Proceeding), and the Tokyo District Court approved the filing of the Spansion Japan Proceeding on March 3, 2009 (the Commencement Date), and appointed the incumbent representative director of Spansion Japan as trustee.

Table of Contents

On March 1, 2009 (the Petition Date), Spansion Inc., Spansion Technology LLC, Spansion LLC, Spansion International, Inc. and Cerium Laboratories LLC (the Debtors), each filed a voluntary petition for relief under Chapter 11 of the U. S. Bankruptcy Code in the U. S. Bankruptcy Court for the District of Delaware (the Chapter 11 Cases). The Chapter 11 Cases, together with the Spansion Japan Proceeding are referred to collectively as the Creditor Protection Proceedings.

We continue to operate our businesses as debtors-in-possession under jurisdiction of the U.S. Bankruptcy Court and in accordance with the applicable provisions of the U.S. Bankruptcy Code and orders of the U.S. Bankruptcy Court. Non-U.S subsidiaries that are not included in the Creditor Protection Proceedings continue to operate without the supervision of the U.S. Bankruptcy Court.

Spansion Japan Deconsolidation

As discussed in Note 3 of Notes to Consolidated Financial Statements, in the section entitled, Basis of Presentation and Going Concern, effective March 3, 2009, we are no longer deemed to have control over Spansion Japan for financial reporting purposes. Prior to March 3, 2009, the results of Spansion Japan were included in our condensed consolidated financial statements, and subsequent to March 3, 2009, the results of Spansion Japan are not included in our consolidated financial statements. Accordingly, our operating results and financial position for year ended December 27, 2009 are not fully comparable to prior periods. Furthermore, the deconsolidation resulted in material decrease in reported consolidated cash; inventory; property, plant and equipment and debt as of December 27, 2009 as compared with those consolidated balances at December 28, 2008. As of March 3, 2009, Spansion Japan cash; inventory; property, plant and equipment and debt was approximately $52.1 million, $57.3 million, $253.3 million and $376.8 million, respectively.

Plan of Reorganization

On October 26, 2009, we filed with the U.S. Bankruptcy Court a proposed Plan of Reorganization, together with an accompanying Disclosure Statement. On each of November 25, 2009 and December 9, 2009, we filed an amended proposed Plan of Reorganization together with an accompanying amended Disclosure Statement. On December 17, 2009, we filed a Second Amended Joint Plan of Reorganization Dated December 16, 2009 (as the same may be amended from time to time, the Plan of Reorganization) and accompanying amended Disclosure Statement. The Plan of Reorganization provides for an equitable distribution to holders of allowed claims in certain classes of creditors, preserves the value of the Debtors businesses as going concerns and preserves employment. The Plan of Reorganization, if accepted by the requisite majorities of one or more of the affected class of creditors and approved by the U.S. Bankruptcy Court (and any applicable appellate courts if the order of the U.S. Bankruptcy Court approving the Plan of Reorganization is appealed), would be binding on all creditors within each affected class, including those that did not vote to accept the proposal. The ultimate recovery to creditors will not be determined until the Plan of Reorganization has been effectuated and all claims have been fully adjudicated or resolved.

Under the Plan of Reorganization, the Debtors will be reorganized (Reorganized Debtors) through the consummation of several transactions in which new securities of the Reorganized Debtors will be issued and distributed in accordance with the Plan of Reorganization. These transactions will include:

- the distribution of cash, new senior notes or cash raised through a rights offering and/or debt issuance, providing that such cash is raised no later than the confirmation date for the Plan of Reorganization, to holders of the Company s existing Floating Rate Notes;

- the distribution of new Spansion common stock to holders of general unsecured claims;

- the cancellation of Spansion Inc. s existing equity securities, including all shares of Common Stock and existing options to purchase shares of Common Stock; and

- the retention of the assets of the Debtors in the reorganized Debtors.

Table of Contents

The Plan of Reorganization provides for the treatment of claims of creditors on a waterfall basis that allocates value to the Debtors creditors and stockholders in accordance with the priorities of the Bankruptcy Code. Pursuant to the Plan of Reorganization, allowed administrative claims and priority tax claims would be paid in full in cash or cash equivalents. Other allowed secured claims would be reinstated, paid in full in cash or have the collateral securing such claims returned to the secured creditor. Allowed unsecured convenience claims (in amount equal to, less than or reduced to $2,000) would be paid in full in cash. Any remaining value would be distributed on a pro rata basis, subject to any applicable subordination agreements, to holders of allowed unsecured claims (other than certain claims, including claims based on non-compensatory damages and penalties and intercompany claims) in the form of new Spansion common stock. Under the Plan of Reorganization, our current stockholders will not be entitled to any recovery, making such shares of common stock valueless.

As set forth in the Second Amended Disclosure Statement, the Debtors have assumed that allowed claims will range from approximately $1.6 billion to approximately $2.1 billion after completion of the claims objection, reconciliation and style="margin:0pt;font-family:Times New Roman;font-size: 1pt">

SigmaTron International, Inc.

Condensed Consolidated Statements of Cash Flows

	Six Months Ended October 31, 2017 (Unaudited)	Six Months Ended October 31, 2016 (Unaudited)
Cash flows from operating activities		
Net income	$ 1,118,997	$ 179,892
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	2,560,202	2,515,400
Stock-based compensation	83,659	169,963
Restricted stock expense	-	10,274
Deferred income tax expense (benefit)	(331,312)	152
Amortization of intangible assets	220,075	244,280
Amortization of financing fees	23,757	22,475
Fair value adjustment of contingent consideration	32,201	(96,627)
Loss from disposal or sale of machinery and equipment	191	29,819
Changes in assets and liabilities		
Accounts receivable	42,462	(3,396,989)
Inventories	(7,384,393)	(2,305,356)
Prepaid expenses and other assets	1,458,244	820,534
Refundable income taxes	(219,550)	(118,820)
Income taxes payable	183,537	55,496
Trade accounts payable	609,465	1,308,064
Deferred rent	(117,920)	(100,509)
Accrued expenses and wages	(1,089,676)	(651,825)
Net cash used in operating activities	(2,810,061)	(1,313,777)
Cash flows from investing activities		

Purchases of machinery and equipment	(3,232,111)	(1,901,654)
Net cash used in investing activities	(3,232,111)	(1,901,654)
Cash flows from financing activities		
Advances on notes receivable	(315,000)	-
Proceeds from the exercise of common stock options	42,940	4,320
Proceeds from Employee stock purchases	-	8,347
Proceeds under equipment note	943,136	-
Payments of contingent consideration	(112,151)	(144,154)
Payments under capital lease and sale leaseback agreements	(966,579)	(815,127)
Payments under equipment note	(125,085)	-
Payments under building notes payable	(82,500)	(82,500)
Borrowings under lines of credit	9,298,262	41,780,402
Payments under lines of credit	(3,675,691)	(38,540,132)
Payments of financing fees	(14,632)	-
Net cash provided by financing activities	4,992,700	2,211,156

7

Change in cash and cash equivalents	(1,049,472)	(1,004,275)
Cash and cash equivalents at beginning of period	3,493,324	4,325,268
Cash and cash equivalents at end of period	$ 2,443,852	$ 3,320,993
Supplementary disclosures of cash flow information		
Cash paid for interest	$ 571,537	$ 520,012
Cash paid for income taxes	987,734	212,592
Purchase of machinery and equipment financed under capital leases	2,085,149	1,159,851
Financing of insurance policy	49,500	271,113

8

SigmaTron International, Inc.

October 31, 2017

Notes to Condensed Consolidated Financial Statements

(Unaudited)

Note A - Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of SigmaTron International, Inc. (“SigmaTron”), SigmaTron’s wholly-owned subsidiaries Standard Components de Mexico S.A., AbleMex, S.A. de C.V., Digital Appliance Controls de Mexico, S.A. de C.V., Spitfire Controls (Vietnam) Co. Ltd., Spitfire Controls (Cayman) Co. Ltd. and wholly-owned foreign enterprises Wujiang SigmaTron Electronics Co., Ltd. and SigmaTron Electronic Technology Co., Ltd. (“SigmaTron China”) and international procurement office SigmaTron Taiwan branch (collectively, the “Company”) have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X.

Accordingly, the condensed consolidated financial statements do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the three and six month periods ended October 31, 2017 are not necessarily indicative of the results that may be expected for the year ending April 30, 2018. For further information, refer to the condensed consolidated financial statements and footnotes thereto included in the Company’s Annual Report on Form 10-K for the year ended April 30, 2017.

Note B - Inventories, net

The components of inventory consist of the following:

	October 31, 2017	April 30, 2017
Finished products	$ 21,213,051	$ 20,291,768
Work-in-process	1,642,188	1,795,852
Raw materials	59,342,433	52,748,542
	82,197,672	74,836,162
Less excess and obsolescence reserve	(1,242,041)	(1,264,924)
	$ 80,955,631	$ 73,571,238

SigmaTron International, Inc.

October 31, 2017

Notes to Condensed Consolidated Financial Statements

(Unaudited)

Note C - Earnings Per Share and Stockholders' Equity

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

	Three Months Ended October 31,		Six Months Ended October 31,	
	2017	2016	2017	2016
Net income	$ 736,115	$ 33,295	$ 1,118,997	$ 179,892
Weighted-average shares				
Basic	4,201,442	4,185,752	4,198,714	4,184,854
Effect of dilutive stock options	125,412	40,122	104,263	40,990
Diluted	4,326,854	4,225,874	4,302,977	4,225,844
Basic earnings per share	$ 0.18	$ 0.01	$ 0.27	$ 0.04
Diluted earnings per share	$ 0.17	$ 0.01	$ 0.26	$ 0.04

Options to purchase 359,763 and 366,763 shares of common stock were outstanding at October 31, 2017 and 2016, respectively. There were no options granted during the six month periods ended October 31, 2017 and 2016, respectively. The Company recognized $0 and $82,731 in stock option expense for the three month periods ended October 31, 2017 and 2016, respectively. The Company recognized $83,659 and $166,404 in stock option expense for the six month periods ended October 31, 2017 and 2016, respectively. The balance of unrecognized compensation expense related to the Company's stock option plans was $0 and $246,479 at October 31, 2017 and 2016, respectively. There were no anti-dilutive common stock equivalents outstanding during the three and six month periods ended October 31, 2017. There were 35,067 and 29,500 anti-dilutive common stock equivalents outstanding during the three and six month periods ended October 31, 2016 which were excluded from the calculation of diluted earnings per share.

On October 1, 2016, the Company issued 11,250 shares of restricted stock pursuant to the 2013 Non-Employee Director Restricted Stock Plan, which fully vested on April 1, 2017. The Company recognized no compensation expense with respect to such shares for the three and six month periods ended October 31, 2017. The Company recognized $10,274 in compensation expense for the three and six month periods ended October 31, 2016.

The Company implemented an employee stock purchase plan ("ESPP") for all eligible employees on February 1, 2014. The ESPP reserved 500,000 shares of common stock for issuance to employees. In addition, the number of shares of common stock reserved for issuance under the plan automatically increases on the first day of the Company's fiscal years by 25,000 shares. The ESPP was terminated effective August 15, 2016. Final purchases under the ESPP were completed on August 31, 2016. The Company recorded $0 and $1,677 in compensation expense for the three months ended October 31, 2017 and 2016 respectively. The Company recorded $0 and $3,559 in compensation expense for the six months ended October 31, 2017 and 2016 respectively. During the three months ended October 31, 2017 and 2016, the Company recorded $0 and $1,472, respectively, to stockholders'

10

SigmaTron International, Inc.

October 31, 2017

Notes to Condensed Consolidated Financial Statements

(Unaudited)

Note C - Earnings Per Share and Stockholders' Equity - Continued

equity relating to purchases under the ESPP. During the six months ended October 31, 2017 and 2016, the Company recorded $0 and $8,347, respectively, to stockholders' equity relating to purchases under the ESPP.

Note D - Long-term Debt

Notes Payable – Banks

On March 31, 2017, the Company entered into a $35,000,000 senior secured credit facility with U.S. Bank, N.A., which expires on March 31, 2022. The credit facility is collateralized by substantially all of the Company's domestically located assets. The facility allows the Company to choose among interest rates at which it may borrow funds: the fixed rate of four percent or LIBOR plus one and one half percent (effectively 2.775% at October 31, 2017). Interest is due monthly. Under the senior secured credit facility, the Company may borrow up to the lesser of (i) $35,000,000 or (ii) an amount equal to a percentage of the eligible receivable borrowing base plus a percentage of the inventory borrowing base. Deferred financing costs of $14,632 and $207,647 were capitalized in the first quarter of fiscal 2018 and the fourth quarter of fiscal 2017, respectively, which are amortized over the term of the agreement. There were no deferred financing costs capitalized in the second quarter of fiscal 2018. As of October 31, 2017 and April 30, 2017 the unamortized amount included in other assets was $196,346 and $204,186, respectively. As of October 31, 2017, there was $28,801,000 outstanding and $6,199,000 of unused availability under the credit facility agreement compared to an outstanding balance of $23,178,429 and $11,821,571 of unused availability at April 30, 2017. At October 31, 2017, the Company was in compliance with its financial covenant and other restricted covenants under the credit facility.

On August 4, 2015, the Company's wholly-owned subsidiary, Wujiang SigmaTron Electronics Co., Ltd., entered into a credit facility with China Construction Bank. Under the agreement Wujiang SigmaTron Electronics Co., Ltd. could borrow up to 5,000,000 Renminbi and the facility was collateralized by Wujiang SigmaTron Electronics Co., Ltd.'s manufacturing building. Interest was payable monthly and the facility had a fixed interest rate of 6.67%. The facility was due to expire on August 3, 2017. The credit facility was closed as of March 1, 2017. There was no outstanding balance under the facility at October 31, 2017 or April 30, 2017.

On March 24, 2017, the Company's wholly-owned subsidiary, SigmaTron Electronic Technology Co., Ltd., entered into a credit facility with China Construction Bank. Under the agreement SigmaTron Electronic Technology Co., Ltd. can borrow up to 9,000,000 Renminbi and the facility is collateralized by Wujiang SigmaTron Electronics Co., Ltd.'s manufacturing building. Interest is payable monthly and the facility bears a fixed interest rate of 6.09%. The term of the facility extends to February 7, 2018. There was no outstanding balance under the facility at October 31, 2017 or April 30, 2017.

Notes Payable – Buildings

The Company entered into a mortgage agreement on January 8, 2010, in the amount of $2,500,000, with Wells Fargo, N.A. to refinance the property that serves as the Company's corporate headquarters and its Illinois manufacturing facility. On November 24, 2014, the Company refinanced the mortgage

SigmaTron International, Inc.

October 31, 2017

Notes to Condensed Consolidated Financial Statements

(Unaudited)

Note D - Long-term Debt - Continued

agreement with Wells Fargo, N.A. The note requires the Company to pay monthly principal payments in the amount of $9,500, bears an interest rate of LIBOR plus two and one-quarter percent (effectively 3.625% at October 31, 2017) and is payable over a sixty month period. A final payment of approximately $2,289,500 is due on or before November 8, 2019. The outstanding balance was $2,517,500 and $2,574,500 at October 31, 2017 and April 30, 2017, respectively.

The Company entered into a mortgage agreement on October 24, 2013, in the amount of $1,275,000, with Wells Fargo, N.A. to finance the property that serves as the Company's engineering and design center in Elgin, Illinois. The Wells Fargo, N.A. note requires the Company to pay monthly principal payments in the amount of $4,250, bears interest at a fixed rate of 4.5% per year and is payable over a sixty month period. A final payment of approximately $1,030,000 is due on or before October 2018. The outstanding balance was $1,071,000 and $1,096,500 at October 31, 2017 and April 30, 2017, respectively.

Note Payable – Equipment

On November 1, 2016, the Company entered into a secured note agreement with Engencap Fin S.A. DE C.V. to finance the purchase of equipment in the amount of $596,987. The term of the agreement extends to November 1, 2021 with average quarterly payments of $35,060 beginning on February 1, 2017 and a fixed interest rate of 6.65%. The balance outstanding under this note agreement was $507,439 and $567,138 at October 31, 2017 and April 30, 2017, respectively.

On February 1, 2017, the Company entered into a secured note agreement with Engencap Fin S.A. DE C.V. to finance the purchase of equipment in the amount of $335,825. The term of the agreement extends to February 1, 2022 with average quarterly payments of $20,031 beginning on May 1, 2017 and a fixed interest rate of 7.35%. The balance outstanding under this note agreement was $302,243 and $335,825 at October 31, 2017 and April 30, 2017, respectively.

On June 1, 2017, the Company entered into a secured note agreement with Engencap Fin S.A. DE C.V. to finance the purchase of equipment in the amount of $636,100. The term of the agreement extends to June 1, 2022 with average quarterly payments of $37,941 beginning on September 1, 2017 and a fixed interest rate of 7.35%. The balance outstanding under this note agreement was $604,295 at October 31, 2017.

On October 1, 2017, the Company entered into a secured note agreement with Engencap Fin S.A. DE C.V. to finance the purchase of equipment in the amount of $307,036. The term of the agreement extends to November 1, 2022 with average quarterly payments of $18,314 beginning on February 1, 2018 and a fixed interest rate of 7.35%. The balance outstanding under this note agreement was $307,036 at October 31, 2017.

Capital Lease and Sales Leaseback Obligations

From October 2013 through June 2017, the Company entered into various capital lease and sales leaseback agreements with Associated Bank, National Association to purchase equipment totaling $6,893,596. The terms of the lease agreements extend to September 2018 through May 2022 with monthly installment payments ranging from $1,455 to $40,173 and a fixed interest rate ranging from

12

SigmaTron International, Inc.

October 31, 2017

Notes to Condensed Consolidated Financial Statements

(Unaudited)

Note D - Long-term Debt - Continued

3.75% to 4.90%. The balance outstanding under these capital lease agreements was $3,612,558 and $3,627,760 at October 31, 2017 and April 30, 2017, respectively. The net book value of the equipment under these leases was $5,083,596 and $4,713,044 at October 31, 2017 and April 30, 2017, respectively.

From April 2014 through July 2015, the Company entered into various capital lease agreements with CIT Finance LLC to purchase equipment totaling $2,512,051. The terms of the lease agreements extend to March 2019 through July 2020 with monthly installment payments ranging from $1,931 to $12,764 and a fixed interest rate ranging from 5.65% through 6.50%. The balance outstanding under these capital lease agreements was $1,219,552 and $1,448,269 at October 31, 2017 and April 30, 2017, respectively. The net book value of the equipment under these leases was $1,841,357 and $1,946,026 at October 31, 2017 and April 30, 2017, respectively.

From September 2017 through October 2017, the Company entered into various capital sales leaseback agreements with First American Equipment Finance to purchase equipment totaling $1,432,114. The terms of the lease agreements extend to August 2021 through September 2021 with monthly installment payments ranging from $12,912 to $20,093 and a fixed interest rate ranging from 5.82% through 6.37%. The balance outstanding under these capital lease agreements was $1,362,487 at October 31, 2017. The net book value of the equipment under these leases was $1,374,731 at October 31, 2017.

SigmaTron International, Inc.

October 31, 2017

Notes to Condensed Consolidated Financial Statements

(Unaudited)

Note E - Goodwill and Other Intangible Assets

Goodwill

There were no changes in the carrying amount of tax-deductible goodwill in the amount of $3,222,899 for the three and six months ended October 31, 2017 and 2016, respectively.

Other Intangible Assets

Intangible assets subject to amortization are summarized as of October 31, 2017 as follows:

	Weighted Average Remaining Amortization Period (Years)	Gross Carrying Amount	Accumulated Amortization
Other intangible assets – Able	-	$ 375,000	$ 375,000
Customer relationships – Able	-	2,395,000	2,395,000
Spitfire:			
Non-contractual customer relationships	9.58	4,690,000	1,422,770
Backlog	-	22,000	22,000
Trade names	14.58	980,000	265,395
Non-compete agreements	1.58	50,000	38,675
Patents	-	400,000	400,000
Total		$ 8,912,000	$ 4,918,840

14

SigmaTron International, Inc.

October 31, 2017

Notes to Condensed Consolidated Financial Statements

(Unaudited)

Note E - Goodwill and Other Intangible Assets - Continued

Intangible assets subject to amortization are summarized as of April 30, 2017, as follows:

	Weighted Average Remaining Amortization Period (Years)	Gross Carrying Amount	Accumulated Amortization
Other intangible assets – Able	-	$ 375,000	$ 375,000
Customer relationships – Able	-	2,395,000	2,395,000
Spitfire:			
Non-contractual customer relationships	10.08	4,690,000	1,237,410
Backlog	-	22,000	22,000
Trade names	15.08	980,000	240,897
Non-compete agreements	2.08	50,000	35,105
Patents	0.08	400,000	393,353
Total		$ 8,912,000	$ 4,698,765

Estimated aggregate amortization expense for intangible assets, which becomes fully amortized in 2032, for the remaining periods is as follows:

For the remaining 6 months of the fiscal year ending April 30:	2018	$ 214,968
For the fiscal years ending April 30:	2019	423,721

2020	411,406
2021	403,199
2022	395,578
Thereafter	2,144,288
	$ 3,993,160

Amortization expense was $107,484 and $122,865 for the three months ended October 31, 2017 and 2016, respectively. Amortization expense was $220,075 and $244,280 for the six months ended October 31, 2017 and 2016, respectively.

15

SigmaTron International, Inc.

October 31, 2017

Notes to Condensed Consolidated Financial Statements

(Unaudited)

Note E - Goodwill and Other Intangible Assets - Continued

In conjunction with the May 2012 acquisition of Spitfire, an estimate of the fair value of the contingent consideration, $2,320,000, was recorded based on expected operating results through fiscal 2019 and the specific terms of when such consideration would be earned. Those terms provide for additional consideration to be paid based on a percentage of sales and pre-tax profits over those years in excess of certain minimums. Payments are made quarterly each year and adjusted after each year-end audit. The Company made payments totaling $342,162 during fiscal year 2016. The Company made payments totaling $273,672 during fiscal year 2017. During fiscal year 2017 the Company decreased the estimated remaining payments expected to be paid under the agreement, which resulted in a decrease of $353,591 to the contingent consideration liability. Any change in the Company's estimate is reflected as a change in the contingent consideration liability and as additional charges or credits to selling and administrative expenses. The Company made one payment in the quarter ended July 31, 2017 in the amount of $45,875 and one payment in the quarter ended October 31, 2017 in the amount of $66,276. As of October 31, 2017, the contingent consideration liability was $443,868 compared to $523,818 at April 30, 2017.

Note F - Commitments and Contingencies

From time to time the Company is involved in legal proceedings, claims or investigations that are incidental to the conduct of the Company's business. In future periods, the Company could be subjected to cash cost or non-cash charges to earnings if any of these matters are resolved on unfavorable terms. However, although the ultimate outcome of any legal matter cannot be predicted with certainty, based on present information, including management's assessment of the merits of any particular claim, the Company does not expect that these legal proceedings or claims will have any material adverse impact on its future consolidated financial position or results of operations.

Note G - Critical Accounting Policies

Management Estimates and Uncertainties - The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates made in preparing the consolidated financial statements include depreciation and amortization periods, the allowance for doubtful accounts, reserves for inventory and valuation of long-lived assets and goodwill, deferred taxes, contingent consideration and other commitments and litigation. Actual results could materially differ from these estimates.

Revenue Recognition - Revenues from sales of the Company's electronic manufacturing services business are recognized when the finished good product is shipped to the customer. In general, and except for consignment inventory, it is the Company's policy to recognize revenue and related costs when the finished goods have been shipped from its facilities, which is also the same point in time that title passes under the terms of the purchase order and control passes to the customer. Finished goods inventory for certain customers is shipped from the Company to an independent warehouse for storage or shipped directly to the customer and stored in a segregated part of the customer’s own facility.

SigmaTron International, Inc.

October 31, 2017

Notes to Condensed Consolidated Financial Statements

(Unaudited)

Note G - Critical Accounting Policies - Continued

Upon the customer's request for finished goods inventory, the inventory is shipped to the customer if the inventory was stored off-site, or transferred from the segregated part of the customer's facility for consumption or use by the customer. The Company recognizes revenue upon such shipment or transfer. The Company does not earn a fee for such arrangements. The Company from time to time may ship finished goods from its facilities, which is also the same point in time that title passes under the terms of the purchase order, and invoice the customer at the end of the calendar month. This is done only in special circumstances to accommodate a specific customer. Further, from time to time customers request the Company hold finished goods after they have been invoiced to consolidate finished goods for shipping purposes. The Company generally provides a warranty for workmanship, unless the assembly was designed by the Company, in which case it warrants assembly/design. The Company does not have any installation, acceptance or sales incentives (although the Company has negotiated longer warranty terms in certain instances). The Company assembles and tests assemblies based on customers' specifications. Historically, the amount of returns for workmanship issues has been de minimis under the Company's standard or extended warranties.

Inventories - Inventories are valued at cost. Cost is determined by an average cost method and the Company allocates labor and overhead to work-in-process and finished goods. In the event of an inventory write-down, the Company records expense to state the inventory at lower of cost or market. The Company establishes inventory reserves for valuation, shrinkage, and excess and obsolete inventory. The Company records provisions for inventory shrinkage based on historical experience to account for unmeasured usage or loss. The Company records provisions for excess and obsolete inventories for the difference between the cost of inventory and its estimated realizable value based on assumptions about future product demand and market conditions. For convenience, the Company records these inventory reserves against the inventory cost through a contra asset rather than through a new cost basis. Upon a subsequent sale or disposal of the impaired inventory, the corresponding reserve is relieved to ensure the cost basis of the inventory reflects any reductions. Actual results differing from these estimates could significantly affect the Company's inventories and cost of products sold as the inventory is sold or otherwise relieved.

Goodwill - Goodwill represents the purchase price in excess of the fair value of assets acquired in business combinations. Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 350, "Intangibles – Goodwill and Other," requires the Company to assess goodwill and other indefinite-lived intangible assets for impairment at least annually in the absence of an indicator of possible impairment and immediately upon an indicator of possible impairment. The Company is permitted the option to first assess qualitative factors to determine whether the existence of events and circumstances indicates that it is more likely than not that the fair value of any reporting unit is less than its corresponding carrying value. If, after assessing the totality of events and circumstances, the Company concludes that it is not more likely than not that the fair value of any reporting unit is less than its corresponding carrying value, then the Company is not required to take further action. However, if the Company concludes otherwise, then it is required to perform a quantitative impairment test, including computing the fair value of the reporting unit and comparing that value to its carrying value. If the fair value is less than its carrying value, a second step of the test is required to determine if recorded goodwill is impaired. The Company also has the option to bypass the qualitative assessment for goodwill in any period and proceed directly to performing the quantitative impairment test. The Company will be able to resume performing the qualitative assessment in any subsequent period. The Company performed its annual goodwill impairment test as

SigmaTron International, Inc.

October 31, 2017

Notes to Condensed Consolidated Financial Statements

(Unaudited)

Note G - Critical Accounting Policies - Continued

of February 1, 2017 and determined no impairment existed as of that date. The step one analysis was performed using a combination of a market approach and an income approach based on a discounted cash flow approach. The Company did not note any triggering events that might indicate an impairment during the three and six month periods ended October 31, 2017.

Intangible Assets - Intangible assets are comprised of finite life intangible assets including patents, trade names, backlog, non-compete agreements, and customer relationships. Finite life intangible assets are amortized on a straight line basis over their estimated useful lives of 5 years for patents, 20 years for trade names, 1 year for backlog and 7 years for non-compete agreements except for customer relationships which are amortized on an accelerated basis over their estimated useful life of 15 years.

Impairment of Long-Lived Assets - The Company reviews long-lived assets, including amortizable intangible assets, for impairment. Property, machinery and equipment and finite life intangible assets are reviewed whenever events or changes in circumstances occur that indicate possible impairment. If events or changes in circumstances occur that indicate possible impairment, the Company first performs an impairment review based on an undiscounted cash flow analysis at the lowest level at which cash flows of the long-lived assets are largely independent of other groups of its assets and liabilities. This analysis requires management judgment with respect to changes in technology, the continued success of product lines, and future volume, revenue and expense growth rates. If the carrying value exceeds the undiscounted cash flows, the Company records an impairment, if any, for the difference between the estimated fair value of the asset group and its carrying value. The Company further conducts annual reviews for idle and underutilized equipment, and reviews business plans for possible impairment. As of October 31, 2017, there were no indicators of possible impairment of long-lived assets.

Income Tax - The Company’s income tax expense, deferred tax assets and liabilities and reserves for unrecognized tax benefits reflect management’s best assessment of estimated future taxes to be paid. The Company is subject to income taxes in both the U.S. and several foreign jurisdictions. Significant judgments and estimates by management are required in determining the consolidated income tax expense assessment.

Deferred income tax assets and liabilities are determined based on differences between financial reporting and tax basis of assets and liabilities, and are measured using the enacted tax rates and laws that are expected to be in effect when the differences are expected to reverse. In evaluating the Company's ability to recover its deferred tax assets within the jurisdiction from which they arise, the Company considers all available positive and negative evidence, including scheduled reversals of deferred tax liabilities, projected future taxable income, tax planning strategies and recent financial operations. In projecting future taxable income, the Company begins with historical results and changes in accounting policies, and incorporates assumptions including the amount of future state, federal and foreign pre-tax operating income, the reversal of temporary differences, and the implementation of feasible and prudent tax planning strategies. These assumptions require significant judgment and estimates by management about the forecasts of future taxable income and are consistent with the plans and estimates the Company uses to manage the underlying businesses. In evaluating the objective evidence that historical results provide, the Company considers three years of cumulative operating income and/or loss. Valuation allowances are established when necessary to reduce deferred

SigmaTron International, Inc.

October 31, 2017

Notes to Condensed Consolidated Financial Statements

(Unaudited)

Note G - Critical Accounting Policies - Continued

income tax assets to an amount more likely than not to be realized. The Company established a valuation allowance of $78,100 related to its foreign tax credit carry-forward at April 30, 2017. The Company did not change the previous valuation allowance or establish any new valuation allowances at October 31, 2017.

The calculation of the Company's tax liabilities involves dealing with uncertainties in the application of complex tax laws and regulations in a multitude of jurisdictions across its global operations. Changes in tax laws and rates could also affect recorded deferred tax assets and liabilities in the future. Management is not aware of any such changes that would have a material effect on the Company's results of operations, cash flows or financial position.

A tax benefit from an uncertain tax position may only be recognized when it is more likely than not that the position will be sustained upon examination, including resolutions of any related appeals or litigation processes, based on the technical merits.

The Company adjusts its tax liabilities when its judgment changes as a result of the evaluation of new information not previously available. Due to the complexity of some of these uncertainties, the ultimate resolution may result in a payment that is materially different from its current estimate of the tax liabilities. These differences will be reflected as increases or decreases to income tax expense in the period in which they are determined.

Reclassifications - Certain reclassifications have been made to the previously reported 2017 financial statements to conform to the 2018 presentation. There was no change to net income.

New Accounting Standards:

In May 2014, the FASB issued Accounting Standards Update ("ASU") No. 2014-09, "Revenue from Contracts with Customers" (Topic 606) which supersedes the revenue recognition requirements in ASC 605, "Revenue Recognition". This ASU is based on the principle that revenue is recognized to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The ASU also requires additional disclosure about the nature, amount, timing and uncertainty of revenue. In August 2015, the FASB amended the effective date to be annual reporting periods beginning after December 15, 2017, including interim periods within that year (effective the first quarter of the Company's fiscal year ending April 30, 2019), with early adoption permitted for annual reporting periods beginning after December 15, 2016 including the interim period within that year. The FASB issued several amendments clarifying various aspects of the ASU, including revenue transactions that involve a third party, goods or services that are immaterial in the context of the contract and licensing arrangements. ASC 606 may be adopted on either a full retrospective or modified retrospective basis. The Company plans to adopt the ASU effective the first quarter of fiscal year ending April 30, 2019. As the new standard will supersede all existing revenue guidance affecting the Company, it could impact the timing and amounts of revenue and costs recognized from customer contracts. The Company, along with its third-party advisor, is currently performing an analysis to determine the impact the new standard will have on its consolidated financial statements. This includes reviewing the terms and conditions included in its contracts with customers and evaluating which, if any, practical expedients the Company will elect upon adoption. The Company expects that the disclosures in the notes to its

SigmaTron International, Inc.

October 31, 2017

Notes to Condensed Consolidated Financial Statements

(Unaudited)

Note G - Critical Accounting Policies - Continued

consolidated financial statements related to revenue recognition will be expanded under the new standards. Companies have the option of using either a full or modified retrospective approach in applying this standard. The Company has not yet concluded upon its selection of the transition method but plans to select a transition method by the end of the third quarter of the current fiscal year.

In July 2015, the FASB issued ASU No. 2015-11, "Inventory (Topic 330): Simplifying the Measurement of Inventory". ASU No. 2015-11 requires an entity that determines the cost of inventory by methods other than last-in, first-out (LIFO) and the retail inventory method (RIM) to measure inventory at the lower of cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation. This amendment applies to all inventory that is measured using the average cost or first-in first-out (FIFO) methods. This supersedes prior guidance which allowed entities to measure inventory at the lower of cost or market, where market could be replacement cost, net realizable value or net realizable value less an approximately normal profit margin. ASU No. 2015-11 is effective for annual reporting periods, and interim periods therein, beginning after December 15, 2016 and prospective application is required. The Company adopted the ASU on May 1, 2017 and the adoption did not have an impact on its consolidated financial position or results of operations.

In February 2016, the FASB issued ASU No. 2016-02, "Leases". The new standard establishes a right-of-use (ROU) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. A modified retrospective transition approach is required for capital leases and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. While the Company is still evaluating the impact of its pending adoption of the new standard on its consolidated financial statements, the Company expects that upon adoption in the fiscal year ending April 30, 2020, it will recognize ROU assets and lease liabilities and that the amounts could be material.

In March 2016, the FASB issued ASU No. 2016-09, "Compensation—Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting", a new accounting standard update intended to simplify several aspects of the accounting for share-based payment transactions including: income tax consequences, classification of awards as either equity or liabilities and classification on the statement of cash flows. Specifically, the update requires that excess tax benefits and tax deficiencies (the difference between the deduction for tax purposes and the compensation cost recognized for financial reporting purposes) be recognized as income tax expense or benefit in the Consolidated Statements of Income, introducing a new element of volatility to the provision for income taxes. This update is effective for fiscal years beginning after December 15, 2016. Early adoption is permitted. The Company adopted the ASU on May 1, 2017. Effective with the adoption of the ASU all share-based awards continue to be accounted for as equity awards, excess tax benefits recognized on stock-based compensation expense are reflected in the consolidated statements of income as a component of the provision for income taxes on a prospective basis, excess tax benefits recognized on stock-based compensation expense are classified as an operating activity in the consolidated statements of cash flows on a prospective basis and the Company has elected to continue

SigmaTron International, Inc.

October 31, 2017

Notes to Condensed Consolidated Financial Statements

(Unaudited)

Note G - Critical Accounting Policies - Continued

to estimate expected forfeitures over the course of a vesting period. The adoption of the ASU had no impact on the retained earnings, other components of equity or net assets as of the beginning of the period of adoption.

In June 2016, the FASB issued ASU No. 2016-13, "Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments." ASU 2016-13 introduces a new forward-looking approach, based on expected losses, to estimate credit losses on certain types of financial instruments, including trade receivables. The estimate of expected credit losses will require entities to incorporate considerations of historical information, current information and reasonable and supportable forecasts. This ASU also expands the disclosure requirements to enable users of financial statements to understand the entity's assumptions, models and methods for estimating expected credit losses. For public business entities, ASU 2016-13 is effective for annual and interim reporting periods beginning after December 15, 2019, and the guidance is to be applied using the modified-retrospective approach. Earlier adoption is permitted for annual and interim reporting periods beginning after December 15, 2018. The Company is currently evaluating the new guidance and has not determined the impact this ASU may have on its consolidated financial statements.

In August 2016, the FASB issued ASU Update No. 2016-15, "Statement of Cash Flows- Classification of Certain Cash Receipts and Cash Payments," which is intended to reduce diversity in practice in how certain transactions are classified in the statements of cash flows. This update will be effective for fiscal years beginning after December 15, 2017 (the Company's fiscal year ending April 30, 2019), and interim periods within those fiscal years. Early adoption is permitted, provided that all of the amendments are adopted in the same period. The guidance requires application using a retrospective transition method. The Company plans to adopt the ASU in its fiscal year ending April 30, 2019 using the retrospective transition method. The Company does not expect the impact of the adoption of this ASU to have a material impact on the Company's Consolidated Statements of Cash Flows.

In January 2017, the FASB issued ASU No. 2017-04, "Intangibles-Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment," which removes the step 2 requirement to perform a hypothetical purchase price allocation to measure goodwill impairment. Goodwill impairment will now be the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the recorded amount of goodwill. This guidance is effective for public companies for annual or any interim goodwill impairment tests in fiscal years beginning after December 15, 2019, and early adoption is permitted. The Company does not expect this guidance to have a significant impact on its financial statements and plans to adopt ASU No. 2017-04 in its fiscal year ending April 30, 2018.

In January 2017, the FASB issued ASU No. 2017-01, “Business Combinations (Topic 805): Clarifying the Definition of a Business,” which clarifies the definition of a business when evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. For public companies, this ASU is effective for annual periods beginning after December 15, 2017, including interim periods within those periods. The Company plans to adopt this ASU in the first quarter of its fiscal year ending April 30, 2019. The Company will apply the clarified definition of a business, as applicable, from the period of adoption.

SigmaTron International, Inc.

October 31, 2017

Notes to Condensed Consolidated Financial Statements

(Unaudited)

Note H - Related Parties

In March, 2015, two of the Company's executive officers invested in a start-up customer. The executive officers' investments constitute less than 2% (individually and in aggregate) of the outstanding beneficial ownership of the customer, according to information provided by the customer to the executive officers. As of October 31, 2017, the Company had an outstanding note receivable and account receivable from that customer of approximately $1,200,000 and $1,356,000, respectively, compared to an outstanding note receivable and account receivable of approximately $888,000 and $1,271,000, respectively, at April 30, 2017. As of October 31, 2017, inventory on hand related to this customer approximated $208,000 compared to $310,000 at April 30, 2017. Sales to this customer have not been material for the three and six months ended October 31, 2017 or during fiscal year 2017.

On January 29, 2016, the Company entered into a memorandum of understanding with this customer. Under the subsequent agreement, effective January 29, 2016, the then outstanding account receivable of approximately $888,000 was converted into a short-term promissory note. The promissory note bears interest at the rate of 8% per annum, payable at the maturity of the promissory note. The promissory note was scheduled to mature at the earlier of October 31, 2016, or within 10 days after the customer obtains certain equity financing, or at the closing of a sale of substantially all of the customer's stock or assets. As additional consideration, the Company received warrants under the agreement. The warrants are ten years in duration and may be exercised at an exercise price of $0.01 per share and for a number of shares determined pursuant to the warrant, expected to be, at a minimum, approximately 1% of the customer's then – outstanding equity securities. The Company believes the warrants have nil value. Further, the Company was granted a security interest in the customer's accounts receivable and authority to access and be a signatory on the customer's deposit accounts.

On December 6, 2016, the Company extended the maturity of the promissory note to July 31, 2017. The promissory note continues to bear interest at the rate of 8% per annum, payable monthly. As consideration, the Company received additional warrants under the agreement, which the Company currently believes have nil value.

On August 25, 2017, effective as of July 31, 2017, the Company and the customer entered into a new forbearance agreement. The Company agreed to extend the maturity of the promissory note and forbear exercising its remedies until the earliest of a capital raise, the sale of the customer, or October 31, 2017, and to fund the customer's operations while the customer explores its options by advancing a maximum of $315,000 through October 31, 2017, pursuant to a new promissory note that bears interest at 8% per annum. Additionally, should the customer's business be sold at a price exceeding $5,000,000 and the amount necessary to pay its creditors, the Company would receive a fee in addition to the debt owed to the Company. The forbearance period and maturity date of the notes expired on the earliest of a capital raise, the sale of the customer or October 31, 2017, but the Company has a unilateral right to extend the forbearance period and maturity of the notes and to make additional advances.

On October 27, 2017, while the preparation of a private placement memorandum for the sale of the customer was underway, the Company extended the forbearance period and maturity of the notes until November 30, 2017. The Company advanced the customer $315,000 in the second fiscal quarter and

SigmaTron International, Inc.

October 31, 2017

Notes to Condensed Consolidated Financial Statements

(Unaudited)

Note H - Related Parties - Continued

$105,000 to fund working capital through the month of November, 2017. On December 1, 2017 the Company extended the forbearance period and maturity of the notes to December 31, 2017 and advanced the customer $105,000 to fund working capital through the month of December, 2017.

Management continues to assess whether the recorded accounts receivable, notes receivable and inventory are recoverable and whether reserves are necessary. The Company is primarily relying on an assessment of the value of the customer by an investment banker with significant experience in the customer's industry. The Company retains its priority position as a secured creditor in a potential sale, liquidation or bankruptcy filing by or against the customer. Based on these factors, the Company believes the accounts receivable, notes receivable and inventory are recoverable. However, in the event that the customer fails to sell its business or raise additional capital in the short term, the Company may not receive payment in full of the obligations owed by the customer or payments by the customer to the Company may be further delayed. The Company will continue to monitor and assess any need to record a reserve against this obligation.

SigmaTron International, Inc.

October 31, 2017

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

In addition to historical financial information, this discussion of the business of SigmaTron International, Inc. ("SigmaTron"), its wholly-owned subsidiaries Standard Components de Mexico S.A., AbleMex, S.A. de C.V., Digital Appliance Controls de Mexico, S.A. de C.V., Spitfire Controls (Vietnam) Co. Ltd., Spitfire Controls (Cayman) Co. Ltd., wholly-owned foreign enterprises Wujiang SigmaTron Electronics Co., Ltd. and SigmaTron Electronic Technology Co., Ltd. (collectively, "SigmaTron China") and international procurement office SigmaTron Taiwan branch (collectively, the "Company") and other Items in this Quarterly Report on Form 10-Q contain forward-looking statements concerning the Company's business or results of operations. Words such as "continue," "anticipate," "will," "expect," "believe," "plan," and similar expressions identify forward-looking statements. These forward-looking statements are based on the current expectations of the Company. Because these forward-looking statements involve risks and uncertainties, the Company's plans, actions and actual results could differ materially. Such statements should be evaluated in the context of the risks and uncertainties inherent in the Company's business including, but not necessarily limited to, the Company's continued dependence on certain significant customers; the continued market acceptance of products and services offered by the Company and its customers; pricing pressures from the Company's customers, suppliers and the market; the activities of competitors, some of which may have greater financial or other resources than the Company; the variability of the Company's operating results; the results of long-lived assets and goodwill impairment testing; the collection of aged account receivables; the variability of the Company's customers' requirements; the availability and cost of necessary components and materials; the ability of the Company and its customers to keep current with technological changes within its industries; regulatory compliance, including conflict minerals; the continued availability and sufficiency of the Company's credit arrangements; changes in U.S., Mexican, Chinese, Vietnamese or Taiwanese regulations affecting the Company's business; the turmoil in the global economy and financial markets; the stability of the U.S., Mexican, Chinese, Vietnamese and Taiwanese economic, labor and political systems and conditions; currency exchange fluctuations; and the ability of the Company to manage its growth. These and other factors which may affect the Company's future business and results of operations are identified throughout the Company's Annual Report on Form 10-K, and as risk factors, may be detailed from time to time in the Company's filings with the Securities and Exchange Commission. These statements speak as of the date of such filings, and the Company undertakes no obligation to update such statements in light of future events or otherwise unless otherwise required by law.

SigmaTron International, Inc.

October 31, 2017

Overview:

The Company operates in one business segment as an independent provider of EMS, which includes printed circuit board assemblies and completely assembled (box-build) electronic products. In connection with the production of assembled products, the Company also provides services to its customers, including (1) automatic and manual assembly and testing of products; (2) material sourcing and procurement; (3) manufacturing and test engineering support; (4) design services; (5) warehousing and distribution services; and (6) assistance in obtaining product approval from governmental and other regulatory bodies. The Company provides these manufacturing services through an international network of facilities located in the United States, Mexico, China, Vietnam and Taiwan.

The Company relies on numerous third-party suppliers for components used in the Company's production process. Certain of these components are available only from single-sources or a limited number of suppliers. In addition, a customer's specifications may require the Company to obtain components from a single-source or a small number of suppliers. The loss of any such suppliers could have a material impact on the Company's results of operations. Further, the Company could operate at a cost disadvantage compared to competitors who have greater direct buying power from suppliers. The Company does not enter into long-term purchase agreements with major or single-source suppliers. The Company believes that short-term purchase orders with its suppliers provides flexibility, given that the Company's orders are based on the changing needs of its customers.

Sales can be a misleading indicator of the Company's financial performance. Sales levels can vary considerably among customers and products depending on the type of services (turnkey versus consignment) rendered by the Company and the demand by customers. Consignment orders require the Company to perform manufacturing services on components and other materials supplied by a customer, and the Company charges only for its labor, overhead and manufacturing costs, plus a profit. In the case of turnkey orders, the Company provides, in addition to manufacturing services, the components and other materials used in assembly. Turnkey contracts, in general, have a higher dollar volume of sales for each given assembly, owing to inclusion of the cost of components and other materials in net sales and cost of goods sold. Variations in the number of turnkey orders compared to consignment orders can lead to significant fluctuations in the Company's revenue and gross margin levels. Consignment orders accounted for less than 1% of the Company's revenues for the three and six months ended October 31, 2017 and 2016, respectively.

The Company's international footprint provides our customers with flexibility within the Company to manufacture in China, Mexico, Vietnam or the U.S. We believe this strategy will continue to serve the Company well as its customers continuously evaluate their supply chain strategies.

The Company had a good quarter in terms of both revenue growth and bottom line growth. Revenues increased modestly and net income increased significantly from the first quarter of 2018. However, the Company continues to encounter shortages in the component marketplace, primarily with semiconductor products. These shortages negatively affected the Company's revenue in the second fiscal quarter and the Company anticipates these shortages will continue during the third fiscal quarter. The shortages have not only negatively impacted the Company's ability to assemble and ship finished goods, but in some cases there were price increases which required customer approval and slowed down production. The Company is heading into what has historically been a slower quarter, driven by the calendar year end, holidays and customers adjusting inventory for their year-end. While the third fiscal quarter may reflect some slowing in the short-term, the Company has landed several new significant customers and their business is projected to start during the Company's fourth fiscal

SigmaTron International, Inc.

October 31, 2017

quarter. The Company continues to see positive trends going forward and is optimistic for the balance of this fiscal year.

Results of Operations:

The following table sets forth selective financial data as a percentage of net sales for the periods indicated.

	Three Months Ended October 31, 2017 (Unaudited)	Three Months Ended October 31, 2016 (Unaudited)	Six Months Ended October 31, 2017 (Unaudited)	Six Months Ended October 31, 2016 (Unaudited)
Net sales	100.0%	100.0%	100.0%	100.0%
Operating expenses:				
Cost of products sold	90.3	91.2	90.4	90.8
Selling and administrative expenses	7.7	8.4	8.0	8.7
Total operating expenses	98.0	99.6	98.4	99.5
Operating income	2.0%	0.4%	1.6%	0.5%

Net Sales

Net sales increased for the three month period ended October 31, 2017 to $72,959,074 from $66,159,586 for the three month period ended October 31, 2016. Net sales increased for the six month period ended October 31, 2017 to $144,183,367 from $125,344,917 for the same period in the prior year. Sales volume increased for the three and six month periods ended October 31, 2017 as compared to the prior year in the industrial electronics, fitness, gaming, auto and medical/life science marketplaces. During the three and six month periods ended October 31, 2017, sales in the appliance and telecommunications marketplaces decreased compared to the same period in the prior year. Sales in the first six months increased due to increasing demand from existing and new customers.

Gross Profit

Gross profit increased during the three month period ended October 31, 2017 to $7,103,568 or 9.7% of net sales compared to $5,818,669 or 8.8% of net sales for the same period in the prior fiscal year. Gross profit increased for the six month period ended October 31, 2017 to $13,860,622 or 9.6% of net sales compared to $11,589,259 or 9.2% of net sales for the same period in the prior fiscal year. The increase in gross profit for the six month period ended October 31, 2017 was primarily the result of increased sales in the majority of marketplaces the Company serves compared to the same period in the prior year and product mix.

Selling and Administrative Expenses

Selling and administrative expenses increased to $5,642,273 or 7.7% of net sales for the three month period ended October 31, 2017 compared to $5,555,385 or 8.4% of net sales for the same period in the prior fiscal year. The net increase in selling and administrative expenses for the three month period

SigmaTron International, Inc.

October 31, 2017

ended October 31, 2017 was driven by increases in general office salaries and bonus expenses. The increase in the foregoing selling and administrative expenses was partially offset by a decrease in accounting professional fees and other general administrative expenses. Selling and administrative expenses increased to $11,554,419 or 8.0% of net sales for the six month period ended October 31, 2017 compared to $10,915,276 or 8.7% of net sales for the same period in the prior fiscal year. This increase was primarily due to an increase in general office salaries.

Interest Expense

Interest expense increased to $345,656 for the three month period ended October 31, 2017 compared to $276,538 for the same period in the prior fiscal year. Interest expense for the six month period ended October 31, 2017 was $654,070 compared to $519,781 for the same period in the prior fiscal year. The increase in interest expense for the three and six month periods ended October 31, 2017 was due to increased loan obligations and higher interest rates compared to the same period in the prior year. Interest expense for future quarters may fluctuate depending on interest rates and borrowings levels.

Income Tax Expense

The income tax expense was $415,339 for the three month period ended October 31, 2017 compared to an income tax benefit of $6,679 for the same period in the prior fiscal year. The increase in income tax expense for the three month period ended October 31, 2017 compared to the same period in the previous year is the result of significantly higher pretax income recognized in the U.S. The Company's effective tax rate was 36.07% and negative 25.1% for the quarters ended October 31, 2017 and 2016, respectively. The effective tax rate is higher for the quarter ended October 31, 2017 than the quarter ended October 31, 2016 due to more income recognized in high tax rate jurisdictions for the period ended October 31, 2017. The income tax expense was $613,302 for the six month period ended October 31, 2017 compared to income tax expense of $73,582 for the same period in the prior year. The Company's effective tax rate was 35.4% and 29.0% for the six months ended October 31, 2017 and 2016, respectively. The effective tax rate is higher for the six month period ended October 31, 2017 compared to the same period in the previous year due to more income recognized in high tax rate jurisdictions for the period ended October 31, 2017.

The Company has not recorded U.S. income taxes on the undistributed earnings of the Company's foreign subsidiaries. The earnings of the foreign subsidiaries have been, and under fiscal year 2018 plans will continue to be, indefinitely reinvested, and as a result, no deferred tax liability was recorded at October 31, 2017. The cumulative amount of unremitted earnings for which U.S. income taxes have not been recorded is $10,273,000 as of October 31,

2017. The amount of U.S. income taxes on these earnings is impractical to compute due to the complexities of the hypothetical calculation.

Net Income

Net income increased to $736,115 for the three month period ended October 31, 2017 compared to net income of $33,295 for the same period in the prior fiscal year. Net income increased to $1,118,997 for the six month period ended October 31, 2017 compared to net income of $179,892 for the same period in the prior fiscal year. Basic and diluted earnings per share for the second quarter of 2018 were $0.18 and $0.17 each, respectively, compared to basic and diluted earnings per share of $0.01 each for the same period in the prior fiscal year. Basic and diluted earnings per share for the six month period ended October 31, 2017 were $0.27 and $0.26, respectively, compared to basic and diluted earnings

---

SigmaTron International, Inc.

October 31, 2017

per share of $0.04 each for the same period in the prior fiscal year. The increases in net income and earnings per share are due to the results of operations described above, mainly from an increase in net sales.

Liquidity and Capital Resources:

Operating Activities.

Cash flow used in operating activities was $2,810,061 for the six months ended October 31, 2017. During the first six months of fiscal year 2018, cash flow used in operating activities was primarily the result of an increase in inventory in the amount of $7,384,393 and a decrease in accrued expenses and wages of $1,089,676. The increase in inventory is the result of an increase in customer orders and in some cases orders being pushed out. Further, capacity issues in the component industry are making it difficult to obtain some components to complete assemblies for shipping. Cash flow used in operating activities was partially offset by the result of an increase in accounts payable, decrease in prepaid expenses and other, net income and the non-cash effects of depreciation and amortization.

Cash flow used in operating activities was $1,313,777 for the six months ended October 31, 2016. During the first six months of fiscal year 2017, cash flow used in operating activities was primarily the result of an increase in inventory of $2,305,356 and accounts receivable of $3,396,989. Cash flow used in operating activities was partially offset by net income, an increase in accounts payable of $1,308,064 and the non-cash effects of depreciation and amortization. The increase in inventory was the result of slower than expected demand for customer orders based on forecast. The increase in accounts receivable was due to the timing of customer payments in the ordinary course of business.

Investing Activities.

During the first six months of fiscal year 2018, the Company purchased $3,232,111 in machinery and equipment to be used in the ordinary course of business. The Company has received forecasts from current customers for increased business that would require additional investment in capital equipment and facilities. To the extent that these forecasts come to fruition, the Company anticipates that it will make additional machinery and equipment purchases in fiscal year 2018.   The Company anticipates purchases will be funded by lease transactions and its senior secured credit facility.

During the six months of fiscal year 2017, the Company purchased $1,901,654 in machinery and equipment used in the ordinary course of business. The Company made additional machinery and equipment purchases of $1,603,832 during the balance of fiscal year 2017.

Financing Activities.

Cash provided by financing activities was $4,992,700 for the six months ended October 31, 2017. Cash provided by financing activities was primarily the result of net borrowings under the line of credit and proceeds under equipment notes.

Cash provided by financing activities was $2,211,156 for the six months ended October 31, 2016. Cash provided by financing activities was primarily the result of net borrowings under the line of credit.

SigmaTron International, Inc.

October 31, 2017

Financing Summary.

Notes Payable – Banks

On March 31, 2017, the Company entered into a $35,000,000 senior secured credit facility with U.S. Bank, N.A., which expires on March 31, 2022. The credit facility is collateralized by substantially all of the Company's domestically located assets. The facility allows the Company to choose among interest rates at which it may borrow funds: the fixed rate of four percent or LIBOR plus one and one half percent (effectively 2.775% at October 31, 2017). Interest is due monthly. Under the senior secured credit facility, the Company may borrow up to the lesser of (i) $35,000,000 or (ii) an amount equal to a percentage of the eligible receivable borrowing base plus a percentage of the inventory borrowing base. Deferred financing costs of $14,632 and $207,647 were capitalized in the first quarter of fiscal 2018 and the fourth quarter of fiscal 2017, respectively, which are amortized over the term of the agreement. There were no deferred financing costs capitalized in the second quarter of fiscal 2018. As of October 31, 2017 and April 30, 2017 the unamortized amount included in other assets was $196,346 and $204,186, respectively. As of October 31, 2017, there was $28,801,000 outstanding and $6,199,000 of unused availability under the credit facility agreement compared to an outstanding balance of $23,178,429 and $11,821,571 of unused availability at April 30, 2017. At October 31, 2017, the Company was in compliance with its financial covenant and other restricted covenants under the credit facility.

On August 4, 2015, the Company's wholly-owned subsidiary, Wujiang SigmaTron Electronics Co., Ltd., entered into a credit facility with China Construction Bank. Under the agreement Wujiang SigmaTron Electronics Co., Ltd. could borrow up to 5,000,000 Renminbi and the facility was collateralized by Wujiang SigmaTron Electronics Co., Ltd.'s manufacturing building. Interest was payable monthly and the facility had a fixed interest rate of 6.67%. The facility was due to expire on August 3, 2017. The credit facility was closed as of March 1, 2017. There was no outstanding balance under the facility at October 31, 2017 or April 30, 2017.

On March 24, 2017, the Company's wholly-owned subsidiary, SigmaTron Electronic Technology Co., Ltd., entered into a credit facility with China Construction Bank. Under the agreement SigmaTron Electronic Technology Co., Ltd. can borrow up to 9,000,000 Renminbi and the facility is collateralized by Wujiang SigmaTron Electronics Co., Ltd.'s manufacturing building. Interest is payable monthly and the facility bears a fixed interest rate of 6.09%. The term of the facility extends to February 7, 2018. There was no outstanding balance under the facility at October 31, 2017 or April 30, 2017.

Notes Payable – Buildings

The Company entered into a mortgage agreement on January 8, 2010, in the amount of $2,500,000, with Wells Fargo, N.A. to refinance the property that serves as the Company's corporate headquarters and its Illinois manufacturing facility. On November 24, 2014, the Company refinanced the mortgage agreement with Wells Fargo, N.A. The note requires the Company to pay monthly principal payments in the amount of $9,500, bears an interest rate of LIBOR plus two and one-quarter percent (effectively 3.625% at October 31, 2017) and is payable over a sixty month period. A final payment of approximately $2,289,500 is due on or before November 8, 2019. The outstanding balance was $2,517,500 and $2,574,500 at October 31, 2017 and April 30, 2017, respectively.

The Company entered into a mortgage agreement on October 24, 2013, in the amount of $1,275,000, with Wells Fargo, N.A. to finance the property that serves as the Company's engineering and design

29

SigmaTron International, Inc.

October 31, 2017

center in Elgin, Illinois. The Wells Fargo, N.A. note requires the Company to pay monthly principal payments in the amount of $4,250, bears interest at a fixed rate of 4.5% per year and is payable over a sixty month period. A final payment of approximately $1,030,000 is due on or before October 2018. The outstanding balance was $1,071,000 and $1,096,500 at October 31, 2017 and April 30, 2017, respectively.

Note Payable – Equipment

On November 1, 2016, the Company entered into a secured note agreement with Engencap Fin S.A. DE C.V. to finance the purchase of equipment in the amount of $596,987. The term of the agreement extends to November 1, 2021 with average quarterly payments of $35,060 beginning on February 1, 2017 and a fixed interest rate of 6.65%. The balance outstanding under this note agreement was $507,439 and $567,138 at October 31, 2017 and April 30, 2017, respectively.

On February 1, 2017, the Company entered into a secured note agreement with Engencap Fin S.A. DE C.V. to finance the purchase of equipment in the amount of $335,825. The term of the agreement extends to February 1, 2022 with average quarterly payments of $20,031 beginning on May 1, 2017 and a fixed interest rate of 7.35%. The balance outstanding under this note agreement was $302,243 and $335,825 at October 31, 2017 and April 30, 2017, respectively.

On June 1, 2017, the Company entered into a secured note agreement with Engencap Fin S.A. DE C.V. to finance the purchase of equipment in the amount of $636,100. The term of the agreement extends to June 1, 2022 with average quarterly payments of $37,941 beginning on September 1, 2017 and a fixed interest rate of 7.35%. The balance outstanding under this note agreement was $604,295 at October 31, 2017.

On October 1, 2017, the Company entered into a secured note agreement with Engencap Fin S.A. DE C.V. to finance the purchase of equipment in the amount of $307,036. The term of the agreement extends to November 1, 2022 with average quarterly payments of $18,314 beginning on February 1, 2018 and a fixed interest rate of 7.35%. The balance outstanding under this note agreement was $307,036 at October 31, 2017.

Capital Lease and Sales Leaseback Obligations

From October 2013 through June 2017, the Company entered into various capital lease and sales leaseback agreements with Associated Bank, National Association to purchase equipment totaling \$6,893,596. The terms of the lease agreements extend to September 2018 through May 2022 with monthly installment payments ranging from \$1,455 to \$40,173 and a fixed interest rate ranging from 3.75% to 4.90%. The balance outstanding under these capital lease agreements was \$3,612,558 and \$3,627,760 at October 31, 2017 and April 30, 2017, respectively. The net book value of the equipment under these leases was \$5,083,596 and \$4,713,044 at October 31, 2017 and April 30, 2017, respectively.

From April 2014 through July 2015, the Company entered into various capital lease agreements with CIT Finance LLC to purchase equipment totaling \$2,512,051. The terms of the lease agreements extend to March 2019 through July 2020 with monthly installment payments ranging from \$1,931 to \$12,764 and a fixed interest rate ranging from 5.65% through 6.50%. The balance outstanding under these capital lease agreements was \$1,219,552 and \$1,448,269 at October 31, 2017 and April 30, 2017, respectively. The net book value of the equipment under these leases was \$1,841,357 and \$1,946,026 at October 31, 2017 and April 30, 2017, respectively.

30

SigmaTron International, Inc.

October 31, 2017

From September 2017 through October 2017, the Company entered into various capital sales leaseback agreements with First American Equipment Finance to purchase equipment totaling $1,432,114. The terms of the lease agreements extend to August 2021 through September 2021 with monthly installment payments ranging from $12,912 to $20,093 and a fixed interest rate ranging from 5.82% through 6.37%. The balance outstanding under these capital lease agreements was $1,362,487 at October 31, 2017. The net book value of the equipment under these leases was $1,374,731 at October 31, 2017.

Operating Leases

In September 2010, the Company entered into a real estate lease agreement in Union City, CA, to rent approximately 117,000 square feet of manufacturing and office space. Under the terms of the lease agreement, the Company receives incentives over the life of the lease, which extends through March 2021. The amount of the deferred rent income recorded for the three and six month periods ended October 31, 2017 was $25,383 and $50,765, respectively. The amount of the deferred rent income recorded for the three and six month periods ended October 31, 2016 was $19,395 and $38,790, respectively. In addition, the landlord provided the Company tenant incentives of $418,000, which are being amortized over the life of the lease. The balance of deferred rent at October 31, 2017 was $499,907 compared to $550,672 at April 30, 2017.

On May 31, 2012, the Company entered into a lease agreement in Tijuana, MX, to rent approximately 112,000 square feet of manufacturing and office space. Under the terms of the lease agreement, the Company receives incentives over the life of the lease, which extends through November 2018. The amount of the deferred rent income for the three and six month periods ended October 31, 2017 was $33,577 and $67,154, respectively. The amount of the deferred rent income for the three and six month periods ended October 31, 2016 was $30,860 and $61,719, respectively. The balance of deferred rent at October 31, 2017 was $157,809 compared to $224,964 at April 30, 2017.

Other

The Company provides funds for salaries, wages, overhead and capital expenditure items as necessary to operate its wholly-owned Mexican, Vietnam and Chinese subsidiaries and the Taiwan international procurement office. The Company provides funding, as needed, in U.S. dollars, which are exchanged for Pesos, Dong, Renminbi, and New Taiwan dollars. The fluctuation of currencies from time to time, without an equal or greater increase in inflation, could have a material impact on the financial results of the Company. The impact of currency fluctuation for the six month period ended October 31, 2017 resulted in a foreign currency transaction gain of $78,503 compared to a foreign currency transaction loss of approximately $197,614 for the same period in the prior year. Foreign currency gains or losses are recorded in the cost of products sold. During the first six months of fiscal year 2018, the Company's U.S. operations paid approximately $25,770,000 to its foreign subsidiaries for services provided.

The Company has not recorded U.S. income taxes on the undistributed earnings of the Company's foreign subsidiaries. The earnings of the foreign subsidiaries have been, and under fiscal April 30, 2018 plans, will continue to be indefinitely reinvested, and as a result, no deferred tax liability was recorded at October 31, 2017. The cumulative amount of unremitted earnings for which U.S. income taxes have not been recorded is $10,273,000 as of October 31, 2017. The amount of U.S. income taxes on these earnings is impractical to compute due to the complexities of the hypothetical calculation.

SigmaTron International, Inc.

October 31, 2017

The Company anticipates that its credit facilities, cash flow from operations and leasing resources are adequate to meet its working capital requirements and capital expenditures for fiscal year 2018. In addition, in the event the Company desires to expand its operations, its business grows more rapidly than expected, the current economic climate deteriorates, customers delay payments, or the Company desires to consummate an acquisition, additional financing resources may be necessary in the current or future fiscal years. There is no assurance that the Company will be able to obtain equity or debt financing at acceptable terms, or at all, in the future. There is no assurance that the Company will be able to retain or renew its credit agreements in the future, or that any retention or renewal will be on the same terms as currently exist.

The impact of inflation on the Company's net sales, revenues and income from operations for the past two fiscal years has been minimal.

Off-balance Sheet Transactions:

The Company has no off-balance sheet transactions.

Tabular Disclosure of Contractual Obligations:

As a smaller reporting company, as defined in Item 10(f)(1) of Regulation S-K under the Exchange Act, the Company is not required to provide the information required by this item.

Item 3.Quantitative and Qualitative Disclosures About Market Risks.

As a smaller reporting company, as defined in Item 10(f)(1) of Regulation S-K under the Exchange Act, the Company is not required to provide the information required by this item.

Item 4.Controls and Procedures.

Disclosure Controls:

The Company's management, including its President and Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of its disclosure controls and procedures (as defined under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), Rules 13a-15(e) and 15(d)-15(e)) as of October 31, 2017. The Company's disclosure controls and procedures are designed to provide reasonable assurance of achieving their objectives and its President and Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective at the reasonable assurance level as of October 31, 2017.

Internal Controls:

There has been no change in the Company's internal control over financial reporting during the three months ended October 31, 2017, that has materially affected or is reasonably likely to materially affect, its internal control over financial reporting. The Company's internal controls over financial reporting are designed to provide reasonable assurance regarding the reliability of financial reporting and preparation of financial statements for external purposes in accordance with U.S. GAAP.

On May 14, 2013, the Committee of Sponsoring Organizations of the Treasury Commission ("COSO") issued an updated version of its Internal Control - Integrated Framework (the "2013 Framework") which officially superseded COSO's earlier Internal Control-Integrated Framework

32

(1992) (the "1992 Framework") on December 15, 2014. Originally issued in 1992, the framework helps organizations design, implement and evaluate the effectiveness of internal control concepts and simplify their use and application. None of COSO, the Securities and Exchange Commission or any other regulatory body has mandated adoption of the 2013 Framework by a specified date. We are currently performing an analysis to evaluate what changes to our control environment, if any, would be needed to successfully implement the 2013 Framework. Until such time as such analysis and any related transition to the 2013 Framework is complete, we will continue to use the 1992 Framework in connection with our assessment of internal control. The Company anticipates the transition will be completed in fiscal year 2018.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings.

From time to time the Company is involved in legal proceedings, claims, or investigations that are incidental to the Company's business. In future periods, the Company could be subjected to cash cost or non-cash charges to earnings if any of these matters are resolved on unfavorable terms. However, although the ultimate outcome of any legal matter cannot be predicted with certainty, based on present information, including management's assessment of the merits of any particular claim, the Company does not expect these legal proceedings or claims will have any material adverse impact on its future consolidated financial position or results of operations.

Item 1A. Risk Factors.

As a smaller reporting company, as defined in Item 10(f)(1) of Regulation S-K under the Exchange Act, the Company is not required to provide the information required by this item.

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

None.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Mine Safety Disclosures.

Not applicable.

Item 5. Other Information.

None.

SigmaTron International, Inc.

October 31, 2017

Item 6.Exhibits.

10.1	Lease No. 1, entered into September 13, 2017, is an attachment to Master Lease No. 2017389 dated August 15, 2017 by and between First American Commercial Bancorp, Inc. and SigmaTron International, Inc.
10.2	Lease No. 2, entered into October 9, 2017, is an attachment to Master Lease No. 2017389 dated August 15, 2017 by and between First American Commercial Bancorp, Inc. and SigmaTron International, Inc.
10.3	Promissory Note, entered into October 12, 2017, by and between ENGENCAP FIN, S.A. DE C.V., SOFOM, E.N.R. "HOLDER") and SigmaTron International, Inc. ("The Maker").
31.1	Certification of Principal Executive Officer of the Company Pursuant to Rule 13a-14(a) under the Exchange Act, as adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. 1350).
31.2	Certification of Principal Financial Officer of the Company Pursuant to Rule 13a-14(a) under the Exchange Act, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. 1350).
32.1	Certification by the Principal Executive Officer of SigmaTron International, Inc. Pursuant to Rule 13a-14(b) under the Exchange Act and Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. 1350).
32.2	Certification by the Principal Financial Officer of SigmaTron International, Inc. Pursuant to Rule 13a-14(b) under the Exchange Act and Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. 1350).
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Scheme Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

34

SigmaTron International, Inc.

October 31, 2017

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.

SIGMATRON INTERNATIONAL, INC.

/s/ Gary R. Fairhead	December 12, 2017
Gary R. Fairhead President and CEO (Principal Executive Officer)	Date
/s/ Linda K. Frauendorfer	December 12, 2017
Linda K. Frauendorfer Chief Financial Officer, Secretary and Treasurer (Principal Financial Officer and Principal Accounting Officer)	Date

35