

CADENCE DESIGN SYSTEMS INC

Form 10-K

March 02, 2009

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**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 January 3, 2009

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

For the transition period from ____ to ____.

Commission file number 0-15867

CADENCE DESIGN SYSTEMS, INC.
(Exact name of registrant as specified in its charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)
2655 Seely Avenue, Building 5, San Jose, California
(Address of Principal Executive Offices)

77-0148231
(I.R.S. Employer
Identification No.)
95134
(Zip Code)

(408) 943-1234
(Registrant's Telephone Number, including Area Code)

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

Title of Each Class
Common Stock, \$0.01 par value per share

Names of Each Exchange on which Registered
NASDAQ Global Select Market

Securities registered pursuant to Section 12(g) of the Act:
None

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

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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 ☒

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K 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 is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold as of the last business day of the registrant's most recently completed second fiscal quarter ended June 28, 2008 was \$2,638,999,267.

On February 7, 2009, approximately 264,603,479 shares of the Registrant's Common Stock, \$0.01 par value, were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive proxy statement for Cadence Design Systems, Inc.'s 2009 Annual Meeting of Stockholders are incorporated by reference into Part III hereof.

CADENCE DESIGN SYSTEMS, INC.
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FOR THE FISCAL YEAR ENDED JANUARY 3, 2009
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PART I.

Item 1. Business

This Annual Report on Form 10-K and the documents incorporated by reference in this Annual Report on Form 10-K contain forward-looking statements. Certain of such statements, including, but not limited to, statements regarding the extent and timing of future revenues and expenses and customer demand, statements regarding the deployment of our products, statements regarding our reliance on third parties and other statements using words such as anticipates, believes, could, estimates, expects, intends, may, plans, should, will and would, and words of similar import and the negatives thereof, constitute forward-looking statements. These statements are predictions based upon our current expectations about future events. Actual results could vary materially as a result of certain factors, including but not limited to, those expressed in these statements. We refer you to the Proprietary Technology, Competition, Risk Factors, Results of Operations, Quantitative and Qualitative Disclosures About Market Risk and Liquidity and Capital Resources sections contained in this Annual Report on Form 10-K and the risks discussed in our other Securities Exchange Commission, or SEC, filings, which identify important risks and uncertainties that could cause actual results to differ materially from those contained in the forward-looking statements.

We urge you to consider these factors carefully in evaluating the forward-looking statements contained in this Annual Report on Form 10-K. All subsequent written or spoken forward-looking statements attributable to our company or persons acting on our behalf are expressly qualified in their entirety by these cautionary statements. The forward-looking statements included in this Annual Report on Form 10-K are made only as of the date of this Annual Report on Form 10-K. We do not intend, and undertake no obligation, to update these forward-looking statements.

Overview

We develop electronic design automation, or EDA, software and hardware. We license software, sell or lease hardware technology and provide engineering and education services throughout the world to help manage and accelerate electronics product development processes. Our broad range of products and services are used by the world's leading electronics companies to design and develop complex integrated circuits, or ICs, and electronics systems.

We were formed as a Delaware corporation in April 1987. Our headquarters is located at 2655 Seely Avenue, San Jose, California 95134. Our telephone number is (408) 943-1234. Our website can be accessed at www.cadence.com. We use our website at www.cadence.com as a channel for distribution of important information about our company. News releases and financial information regarding our company are posted on and accessible at our investor relations webpage on our website at www.cadence.com. Our website permits investors to subscribe to e-mail alerts when we post new material information on our website. We also make available on our investor relations webpage, free of charge, copies of our SEC filings and submissions as soon as practicable after electronically filing or furnishing such documents with the SEC. Our Corporate Governance Guidelines, Code of Business Conduct and the charters of the Audit Committee, Compensation Committee and Corporate Governance and Nominating Committee of our Board of Directors are also posted on the investor relations webpage on our website at www.cadence.com. Stockholders may also request copies of these documents by writing to our Corporate Secretary at the address above. Information on our website is not incorporated by reference in this Annual Report on Form 10-K unless expressly noted.

Factors Driving the Electronic Design Automation Industry

During fiscal 2008, the semiconductor industry's growth declined as the overall macroeconomic environment deteriorated. Most industry analysts estimate minimal growth for the semiconductor industry for 2008, and these industry analysts are forecasting a significant decline in semiconductor industry revenue for 2009. Since consumer spending on electronics in 2008 was also negatively impacted by higher energy costs and increased unemployment, and corporate spending was impacted by the tight credit market, electronics companies faced financial challenges in fiscal 2008 and may continue to face such challenges in fiscal 2009. Consistent with recent prior years,

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semiconductor unit volumes grew during 2008, but average selling prices declined. These factors, combined with the current macroeconomic environment, impact how electronics companies address the traditional challenges of cost, quality, innovation and time-to-market associated with highly complex electronics systems and IC product development. Electronics companies are currently requiring higher levels of productivity from their design teams, better predictability in their development schedules and higher quality products in order to be competitive in the challenging and price-conscious markets they serve.

Electronics companies respond to demand for increased functionality and miniaturization in markets that are affected by the current macroeconomic environment by combining subsystems such as radio frequency, or RF, wireless communication, video signal processing and microprocessors onto a single silicon chip, creating a system-on-chip, or SoC, or multiple chips into a single chip package in a format referred to as system-in-package, or SiP. These trends toward subsystem integration have required chip makers to find solutions to challenges previously addressed by system companies, such as verifying system-level functionality and hardware-software interoperability.

SoC designs put many more transistors on each chip, increasing the need for tight control over power consumption. This is done not only to increase battery life in portable devices, but also to minimize energy cost for computing and networking equipment. Higher power devices generate more heat, which further increases both system cost as well as operating expenses for cooling. Evolving semiconductor manufacturing processes with smaller features (transistors and wires) and lower supply voltages address both of these issues to some degree, but introduce new challenges of their own. Contemporary portable electronic devices contain chips in which individual features can be as small as 45 nanometers, or 45/1,000,000ths of a millimeter. Because of the electrical characteristics of the materials used to construct the transistors, which are essentially microscopic switches, chips continue to consume power even when transistors in the device are switched off. To overcome these and other power-related issues, specific low power design techniques must be developed and are most effective if they are integrated throughout the design flow, from logic design and verification through physical implementation.

Variability in the processes and materials used to manufacture silicon chips have become so pervasive at 65 nanometers and below that traditional connections between design and manufacturing teams are insufficient to ensure chip performance and yield. Integrating detailed models of the manufacturing process into the chip design environment is desirable so engineers can craft a design to avoid or overcome these manufacturing process variations. Similarly, manufacturing teams can optimize their processes if, along with the design, they are provided with information about the most critical parts of the chip. However, sharing information between design and manufacturing processes is complicated because current data formats used to describe the chip design differ from data formats used to describe the manufacturing process and control the manufacturing equipment. Moreover, design and manufacturing most often involve two or more separate companies, since multiple companies may participate in the design of the chip and in the manufacturing and assembly of the final device.

These trends represent significant new challenges for electronics design processes. Specifically, product performance and size requirements of the mobile consumer electronics market require microelectronic systems to be smaller, consume less power and provide multiple functions all in one SoC or SiP. This requires designers to pay close attention to many electrical, physical and manufacturing effects that were inconsequential in previous generations of chip designs. The design challenge becomes more complex with each new generation of electronics and providers of EDA solutions must deliver products that address these technical challenges while improving the productivity, predictability and reliability of the design process.

Operating Segment

Our chief operating decision maker is our President and Chief Executive Officer, or CEO. Our CEO reviews our consolidated results within only one operating segment.

Products and Product Strategy

Our products are engineered to improve our customers' design productivity and design quality by providing a comprehensive set of EDA tools. Product revenues include all fees earned from granting licenses to use our software and from sales and leases of our hardware products, and exclude revenues derived from maintenance and services.

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We offer customers three license types for our software: perpetual, term and subscription. See Software Licensing Arrangements below for additional discussion of our license types.

We combine our products and technologies into platforms for four major design activities:

- Functional Verification;
- Digital IC Design and Implementation;
- Custom IC Design and Verification; and
- System Interconnect Design.

The four Cadence® design platforms are branded as Incisive® functional verification, Encounter® digital IC design, Virtuoso® custom design and Allegro® system interconnect design. In addition, we augment these platform product offerings with a set of design for manufacturing, or DFM, products that service both the digital and custom IC design flows. These offerings comprise our primary product lines.

The products and technologies that comprise our platforms are combined with services, elements from kits (which assemble technologies from our broad portfolio into ready-to-use packages) and other associated components that provide comprehensive solutions for low power, mixed signal, enterprise verification and advanced node designs. These solutions and their constituent elements are marketed to users who specialize in areas such as system design and verification, functional verification, logic design, digital implementation, custom IC design and printed circuit board, or PCB, and IC package / SiP design.

Our Product revenue was \$516.6 million, or 50% of our total revenue, during fiscal 2008; \$1,104.0 million, or 68% of our total revenue, during fiscal 2007; and \$982.7 million, or 66% of our total revenue, during fiscal 2006. For additional description of our Product revenue, including the current year decrease, see the discussion under the heading Results of Operations under Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, below.

Functional Verification

Our Functional Verification offerings are comprised of two major categories of offerings: Logic Verification and System Design and Verification.

Logic Verification

Our Logic Verification offering consists of the property checking and simulation and environment capabilities within the Incisive functional verification platform. This offering enables our customers to employ enterprise-level verification process automation, including verification planning, process tracking and management that allow the coordination of verification activities across multiple teams and various specialists.

Our Logic Verification offering includes:

- Planning and management that automates and guides the verification process, from specifications to metric-driven functional closure;
- Testbench and simulation that offer Open Verification Methodology, or OVM, multi-language testbench and transaction-level support, assertion checking, low-power and mixed-signal simulation, analysis and a debug environment;
- Formal verification, which provides a mathematical method for verifying RTL functional correctness with assertions before a testbench simulation;

A verification IP portfolio that enables engineers to improve productivity while reducing risks associated with standard protocol development and compliance and provides a broad catalog of standard verification IP equipped with a Compliance Management System allowing metric-driven closure;
Palladium® and Xtreme® series of emulation and acceleration hardware;
SoC Functional Verification Kit, which captures reference examples of verification flows and reduces customers' language, technology and methodology adoption risks; and
Tailored verification services for methodology adoption, environment migration and educational training that provide customized means of addressing customer-specific challenges.

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Our Logic Verification offering also provides methodology-driven and multi-product flows that allow customers to incrementally adopt certain aspects of this offering and to address specific challenges. These flows include:

- Multi-language OVM, which enables productivity and quality gains with reusable and scalable verification environments;
- Metric-driven verification, which enables schedule predictability with a plan- and metric-driven solution and automated functional verification closure;
- Assertion-based verification, which enables productivity and quality gains with block and chip verification of functional intent that are captured via assertions;
- Low power verification, as part of our Low Power Solution, which enables quality and productivity gains associated with the growing need to verify power management logic; and
- Mixed signal verification, which enables risk reduction via integrated verification of designs with both digital and analog content.

System Design and Verification

Our System Design and Verification consists of the acceleration/emulation and system-level design capabilities and includes design and verification hardware and software, verification intellectual property, or IP, services and methodologies that provide customers with system-wide planning and management, design and verification IP reuse automation and system verification. In addition, this offering provides system power exploration, analysis and optimization.

Our System Design and Verification offering targets IP and SoC design and verification planners and architects, transaction-level IP developers and SoC and system-level IP verification and validation engineers. During fiscal 2008, we introduced C-to-Silicon Compiler, Palladium III Dynamic Power Analysis, new system verification IP and new SpeedBridge® adapters.

Our System Design and Verification offering includes:

- SoC estimation software that enables chip architects and planners to evaluate the cost, performance and power of the SoC before initiating a design project;
- System-level verification planning and management that automates and guides the verification process;
- C-to-Silicon Compiler, which provides high-level synthesis with IP reuse automation and architectural analysis and produces register transfer level, or RTL, micro-architectural designs;
- Palladium and Xtreme series of emulation and acceleration hardware;
- Incisive Simulation Analysis, which provides support for transaction-level verification, analysis and mixed-language testbench and full RTL verification;
- Incisive Software eXtension for hardware and software co-verification and co-debug; and
- Verification IP and SpeedBridge adapters that enable chip architect and planners to improve productivity while reducing risks associated with standard protocol compliance and provide a catalogue of standard protocols.

We also offer customers consulting services for verification acceleration and system emulation. Our QuickCycles program allows customers access to our Palladium and Xtreme simulation acceleration and emulation products either on their secure internet site or remotely over a high-speed, secure network connection.

Digital IC Design and Implementation

Our Digital IC offerings include two major categories of offerings: Logic Design and Implementation.

Logic Design

Our Logic Design offering is comprised of equivalency checking, synthesis and test capabilities within the Encounter digital IC design platform and property checking, simulation, and environment capabilities within the Incisive functional verification platform. This offering provides planning, design, verification and test technologies and services to customers across all digital design end markets. Logic Design capabilities are aggregated into

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solutions that address our customers' needs in areas such as power efficiency and advanced process nodes. Our Logic Design offering targets engineers who are tasked with digital chip development planning, functional design, verification, logical implementation and design-for-test, or DFT.

In fiscal 2008, we introduced several new capabilities in our Logic Design offering, such as chip planning technology and a web portal that facilitates IP selection and estimation of chip characteristics.

Our Logic Design offering includes:

- Chip Planning System and Incyte Chip Estimator, which provides users with the ability to perform technical and cost trade-off analyses in the product planning phase of a project;
- Low power capability that enables users to maximize energy efficiency of their designs;
- Engineering change order-, or ECO-, aware products that provide an automated solution for pre-mask and post-mask management of specification changes;
- Logic synthesis, which enables simultaneous, multi-objective optimization for key project attributes;
- Implementation signoff, which extends into areas of low power, constraints and design sign-off rule verification, to provide more accurate results; and
- DFT, automatic test pattern generation and failure diagnosis technologies, which are integrated in the design process, to address the challenges of complex SoC development.

Implementation

Our Implementation offering is comprised of a range of the Encounter digital IC design platform capabilities. The Implementation offering includes timing analysis, signal integrity and place and route capabilities within the Encounter digital IC design platform. This offering enables customers to create a physical representation of logic models, analyze electrical and physical characteristics of a design and prepare a design for manufacturing.

During fiscal 2008, we launched our Encounter Digital Implementation System, or EDI, in our Implementation offering. EDI offers RTL to graphic data system II, or GDSII, design closure solution with end-to-end parallel processing that enables design flow to benefit from current multi-core, multi-processor and multi-computer infrastructure. EDI is based on a single user interface and a unified in-memory data model, and is designed to facilitate chip performance analysis and optimization, power consumption and silicon area and manufacturability throughout the customers' design processes. EDI also supports hierarchical designs, with support for designs containing hundreds of millions of transistors on a single chip. EDI is offered with the L and XL tiers and specific options, depending on the requirements of our customers. Current options include Low Power, Mixed Signal and Advanced Node. These tiers and options are scaled to provide our customers with technologies tailored to specific degrees of design complexity in the digital IC space.

Our Implementation offering includes:

- Silicon virtual prototyping with automated floorplan synthesis and ranking capabilities, which enables designers to explore the design space and plan the complete implementation of a chip before committing to a specific implementation strategy;
- Global RTL and physical synthesis that enables customers to improve the quality of silicon;
- Embedded sign-off-qualified variation analysis and optimization across the design flow, which provides a more predictable design closure at advanced nodes;
- Integrated diagnostic tools for rapid global timing, clock and power analysis and debugging; and
- Interoperability with our Custom IC Design offering to enable implementation of mixed-signal ICs.

Custom IC Design and Verification

Our Custom IC Design and Verification offering is comprised of a range of Virtuoso custom design platform capabilities and certain DFM product capabilities. The Custom IC Design and Verification offering includes the environment, IC layout and simulation capabilities within the Virtuoso custom design platform. This offering provides designers with an integrated flow for design creation, validation and implementation of silicon-accurate analog, custom digital, mixed-signal, memory and RF designs, while ensuring that these designs are ready for manufacturing through integrated DFM capabilities.

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During fiscal 2008, we released Virtuoso® 6.1.3, which provides a unified design environment by tying together design, layout and verification tasks based on a constraint-driven design methodology that enables customers to improve their productivity. End-to-end simulation and verification technology that we call multi-mode simulation is integrated into the unified environment enabling a complete design-to-verification methodology.

Our Virtuoso Custom IC Design and Verification offering includes:

- Reference flows for analog, mixed-signal, RF and analog-digital integration focused on wireless and analog/mixed-signal market segments;
- Comprehensive specification-driven design environment to analyze designs over a broad set of manufacturing and environmental operating conditions;
- Schematic-capture support and constraint-driven design techniques to secure and retain a designer's intent throughout the design process;
- Automatic analog circuit sizing and optimization including yield optimization;
- Multi-mode simulation for digital, analog, mixed-signal and RF designs; and
- Interactive, assisted or fully automated options for custom layout with advanced floorplanning, chip editing, process node migration and analog/mixed-signal routing technologies.

Our Virtuoso L, XL and GXL offerings also provide designers with the ability to choose the appropriate products that match their needs, ranging from simple entry-level component design to the most complex DFM-aware SoC designs.

System Interconnect Design

Our System Interconnect Design offerings include the following capabilities within the Allegro system interconnect design platform: PCB, IC package, SiP, design management and collaboration. Certain offerings also include the simulation capability within the Virtuoso custom design platform. These offerings enable engineers who are responsible for the capture, layout and analysis of advanced PCB and IC packages to design high-performance electronic products across the domains of IC, IC package and PCB, to increase functional density and to manage design complexity while reducing cost and time to market.

During fiscal 2008, we provided an update to our system interconnect offerings and released Allegro 16.2, which includes technology for High Density Interconnect, or HDI, design that enables design engineers to improve functional density and address design miniaturization. We also enhanced our products to support team-based and geographically dispersed development of large multi-chip designs.

Our System Interconnect Design offering includes:

- Constraint-driven methodology from advanced design capture and authoring, signal integrity and power delivery optimization and analysis through detailed physical implementation and DFM preparation;
- Optimized system level interconnect the electronic signal and power paths across PCBs, IC Packages and ICs through a co-design methodology to reduce hardware costs and the duration of design projects;
- Embedded support for silicon input/output transceiver algorithmic modeling (using Input/Output Buffer Information Specification, or IBIS, 5.0);
- Algorithmic modeling, which enables characterization of the latest serial interface protocols that are being adopted across all markets;
- Million-bit channel analysis, which allows design engineers to verify standards compliance during the design process;
- SiP RF Layout and RF Architect, both of which include a methodology for integrating multiple levels of silicon and discrete functionality in a single performance, cost and size-optimized IC Package; and

SiP integration with our Encounter Digital IC and Virtuoso Custom IC offerings to co-design, streamline and optimize IC Package design.

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Our System Interconnect Design offerings are available as a set of scalable capability-tiered products, including L, XL and GXL, depending on the requirements of our customers. For the mainstream PCB customers, where individual or small team productivity is a focus, we provide the OrCAD® family of offerings that is marketed worldwide through a network of resellers.

Design for Manufacturing

With the advent of silicon manufacturing technologies at geometries of 65 nanometer and below, our customers are increasingly concerned about manufacturability of their designs. The physical layout of each IC requires detailed analysis and optimization to ensure that the design can be manufactured in volume while performing as expected. Our strategy is to integrate DFM awareness into our core design platforms of Encounter Digital IC and Virtuoso Custom IC.

Some of our DFM capabilities include:

- Parasitic extraction products, which take a physical representation of a design and determine the electrical properties to enable additional simulation and timing analysis;
- On-chip power distribution for digital, analog and SoC designs;
- Manufacturing design rule checks to ensure the proposed design meets foundry process requirements; and
- Analytical and design tools for physical and electrical effects, process proximity correction, and yield / failure analysis diagnostics.

Our primary focus in DFM is to address manufacturing effects as early in the product development process as possible. As a result, we are enhancing the DFM awareness of our core Encounter Digital IC and Virtuoso Custom IC product offerings. Where upstream integration is not possible, Cadence offers certain stand alone DFM products. In connection with our cost savings initiatives that were implemented during the fourth quarter of fiscal 2008, we adjusted our roadmaps and investment consistent with our current DFM strategy. The changes in our DFM strategy resulted in an impairment charge of \$42.5 million arising from the abandonment and reduction to net realizable value of certain identifiable intangible assets.

Third Party Programs and Initiatives

In addition to our products, many customers use internally-developed design tools or design tools provided by other EDA companies, as well as IP available from multiple suppliers. We support the use of third-party design products and IP through vehicles such as our Connections® program and through our participation in the OpenAccess Coalition, the Power Forward Initiative and other programs and initiatives. We also contribute to the development and deployment of EDA industry standards.

Maintenance

Customer service and support is critical to the adoption and successful use of our products. We provide our customers with technical support to facilitate their use of our software and hardware solutions.

We offer maintenance to our customers as an integral, non-cancelable component of our subscription license agreements, as a component of our term license agreements subject to annual renewal, or as a separate agreement subject to annual renewal for our perpetual license customers.

Our Maintenance revenue was \$388.5 million, or 37% of our total revenue, during fiscal 2008; \$385.2 million, or 24% of our total revenue, during fiscal 2007; and \$366.3 million, or 25% of our total revenue, during fiscal 2006. For additional description of our Maintenance revenue, see the discussion under the heading "Results of Operations" under Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations," below.

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Services

We offer a number of fee-based services, including engineering and education services. These services may be sold separately or sold and performed in conjunction with the sale, lease or license of our products.

Our Services revenue was \$133.5 million, or 13% of our total revenue, during fiscal 2008; \$125.8 million, or 8% of our total revenue, during fiscal 2007; and \$134.9 million, or 9% of our total revenue, during fiscal 2006. For additional description of our Services revenue, see the discussion under the heading "Results of Operations" under Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations," below.

Engineering Services

We offer engineering services to aid our customers with the design of complex ICs and the implementation of key design capabilities, including low power, IC packaging and board design, mixed-signal design, functional verification, digital implementation, analog/mixed-signal and system-level. The customers for these services primarily consist of semiconductor and systems companies developing products for the consumer, communications, military and aerospace and computing markets. These ICs range from digital SoCs, analog and RF designs to complex mixed-signal ICs.

We offer engineering capabilities to assist customers from product concept to volume manufacturing. We leverage our experience and knowledge of design techniques, leading practices and different design environments to improve the productivity of our own and our customers' engineering teams. Depending on the customers' projects and needs, we work with customers using outsourcing, consultative and collaborative offerings. Our Virtual Computer-Aided Design, or VCAD, offering enables our engineering teams at one or more of our locations to collaborate with our customers' teams located elsewhere in the world during the course of their design and engineering projects through a secure network infrastructure. We also make our design IP portfolio available to customers as part of our technology and services solutions. These reusable design and methodology components enable us to efficiently deliver our services and allow our customers to reduce the design complexity and time to market when developing complex SoCs.

Through collaboration with our customers, we are able to design advanced ICs and gain direct and early visibility to industry design issues that may not be addressed adequately by today's EDA technologies. This enables us to target and accelerate the development of new software technology and products to satisfy current and future design requirements.

Education Services

Our education services offerings can be customized and include training programs that are conducted via the internet or in a classroom setting. The content of these offerings ranges from the latest IC design techniques to methodologies for using the most recent features of our EDA products. The primary focus of education services is to accelerate our customers' path to productivity in the use of our products and increase awareness of the total solution required for engineering success.

Marketing and Sales

We generally market our products and provide maintenance and services to existing and prospective customers through a direct sales force consisting of sales people and applications engineers. Applications engineers provide technical pre-sales and post-sales support for software products. Due to the complexity of many of our EDA products and the electronic design process, the sales cycle is generally long, requiring three to six months or more. During the sales cycle, our direct sales force generally provides technical presentations, product demonstrations and support for

on-site customer evaluation of our solutions. We also use traditional marketing approaches to promote our products and services, including advertising, direct mail, telemarketing, trade shows, public relations and the internet. As EDA products mature and become more widely understood by the marketplace, we selectively utilize value added resellers to broaden our reach and reduce cost of sales. All OrCAD and selected Incisive products are primarily marketed through these channels. With respect to international sales, we generally market and support our

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products and services through our subsidiaries. We also use a third-party distributor to sell our products and services to certain customers in Japan.

Software Licensing Arrangements

We sell software using three license types: subscription, term and perpetual. Customers who prefer to license technology for a specified, limited period of time will choose either a subscription or term license, and customers who prefer to have the right to use the technology continuously without time restriction will choose a perpetual license. Customers who desire to use new technology during the life of the contract will select a subscription license, which allows them limited access to unspecified new technology on a when-and-if-available basis, as opposed to a term or perpetual license, which does not include rights to use new technology. Payment terms for subscription and term licenses generally provide for payments to be made in installments over the license period and payment terms for perpetual licenses generally are net 30 days.

We offer a delivery mechanism for term and subscription licenses called eDA Cards. eDA cards have an overall face value amount that customers draw down against as they select specific products that are priced based on the particular duration of use the customer desires. The selection and licensing of the specific products is accomplished through an automated on-line system. The card expires when all of the face value is consumed, or on the pre-determined expiration date, whichever comes first. There are two types of eDA Cards. An eDA Gold Card is a term license that enables a customer to access a predetermined list of existing products. An eDA Platinum Card is a subscription license that enables a customer to access existing and new technology.

Our revenue recognition depends on a number of contract-specific terms and conditions, including the license type, payment terms, creditworthiness of the customer and other factors. For additional description of our revenue recognition, see the discussion under the heading Critical Accounting Estimates under Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, below. Revenue associated with subscription licenses is recognized over multiple periods during the license term, whereas product revenue associated with term and perpetual licenses is generally recognized upon the later of the effective date of the license or delivery of the product, assuming all other criteria for revenue recognition have been met. The amount of product revenue recognized from backlog varies from quarter to quarter. The amount of product revenue recognized from backlog, as compared to total product revenue, was more than half during fiscal 2008 and approximately two-thirds during both fiscal 2007 and fiscal 2006. We are moving to a license mix that will result in increased ratable revenue and we expect the percentage of product revenue from backlog to increase in future years.

Our revenue and results of operations may miss expectations due to a shortfall in product revenue generated from current transactions or variance in the actual mix of license types executed in any given period, and due to other contract-specific terms and conditions as discussed above. We are subject to greater credit risk on subscription and term licenses, as compared to perpetual licenses because of the installment payment terms generally associated with those license types.

From time to time, we sell receivables generated by our licenses with installment payment terms to third-party financial institutions on a non-recourse or limited-recourse basis.

For a further description of our license agreements, revenue recognition policies and results of operations, please refer to the discussion under the heading Critical Accounting Estimates under Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, below.

Research and Development

Our investment in research and development was \$457.9 million during fiscal 2008, \$494.0 million during fiscal 2007 and \$460.1 million during fiscal 2006.

The primary areas of our research and development include SoC design, the design of silicon devices in the nanometer range, high-performance IC packaging, SiP and PCB design, system-level modeling and verification, high-performance logic verification technology and hardware/software co-verification. The electronics industry combines rapid innovation with rapidly increasing design and manufacturing complexity, so we make significant

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investments in enhancing our current products, as well as creating new products and technologies and integrating those products and technologies together into segmented solutions.

Our future performance depends largely on our ability to maintain and enhance our current product development and commercialization, to develop, acquire or operate with new products from third parties, and to develop solutions that meet increasingly demanding productivity, quality, predictability and cost requirements.

Manufacturing and Distribution

Our software production consists of configuring the customer's order, recording the product electronically or on CD-ROM, and producing unique access keys that allow customers to use licensed products. Software and documentation are primarily distributed to customers by secure electronic delivery. User manuals and other documentation are generally available by secure electronic delivery or on CD-ROM, but are occasionally supplied in hard copy format.

We perform final assembly and test our hardware verification, acceleration and emulation products at our headquarters in San Jose, California. Subcontractors manufacture all major subassemblies, including all individual PCBs and custom ICs, and supply them for qualification and testing before their incorporation into the assembled product.

Proprietary Technology

Our success depends, in part, upon our proprietary technology. We generally rely on patents, copyrights, trademarks and trade secret laws, licenses and restrictive agreements to establish and protect our proprietary rights in technology and products. Many of our products include software or other intellectual property licensed from third parties. We may have to seek new licenses or renew existing licenses for third party software and other intellectual property in the future. As part of performing engineering services for customers, our engineering services business uses certain software and other intellectual property licensed from third parties, including that of our competitors.

Competition

We compete in the EDA market for products and maintenance primarily with three companies: Synopsys, Inc., Mentor Graphics Corporation and Magma Design Automation, Inc. We also compete with numerous smaller EDA companies, with manufacturers of electronic devices that have developed or have the capability to develop their own EDA products, and with numerous electronics design and consulting companies. We generally compete on the basis of product quality, product features, level of integration or compatibility with other tools, price, payment terms and maintenance offerings.

Our maintenance business flows directly from our product business. The competitive issues associated with our maintenance business are substantially similar to those for our product business in that every maintenance contract is the direct result of a product contract, and once we have entered into a product contract, maintenance is generally purchased by the customer to ensure access to bug fixes and service releases, as and when they are made available, and other continued support.

Certain competitive factors in the engineering services business as described herein differ from those of the products and maintenance businesses. While we do compete with other EDA companies in the engineering services business, our principal competitors are independent engineering service businesses. These companies vary greatly in focus, geographic location, capability, cost structure and pricing. In addition, manufacturers of electronic devices may be reluctant to purchase services from independent vendors, including us, because they wish to promote their own internal design departments. We compete with these companies by focusing on the design of complex analog and

digital ICs. It is our strategy to use engineering services as a differentiator to further promote our products and maintenance businesses.

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Backlog

Our backlog as of January 3, 2009 was approximately \$1.8 billion, as compared to approximately \$2.0 billion as of December 29, 2007. Backlog consists of revenue to be recognized in future fiscal periods after January 3, 2009 from a variety of license types which generally include, but are not limited to:

- Subscription licenses for software products;
- Sale or lease of hardware;
- Maintenance contracts on hardware and software products;
- Orders for hardware and software products sold on perpetual and term licenses on which customers have delivery dates after January 3, 2009;
- Licenses with payments that are outside our customary terms; and
- The undelivered portion of engineering services contracts.

The substantial majority of our backlog is generated by our product and maintenance businesses because customer licenses generally include both product and maintenance components. Historically, we have not experienced significant cancellations of our contracts with customers. However, we occasionally reschedule the required completion dates of engineering services contracts, which may defer revenue recognition under those contracts beyond the original expected completion date. Changes in customer license types or payment terms also can impact the timing of revenue recognition.

The challenges currently affecting the economy of the United States and other regions of the world have impacted our customers, who are concentrated in the semiconductor sector, and may cause them to delay or default on their payment obligations, file for bankruptcy or modify or cancel plans to license our products. We have not yet experienced a material level of defaults by customers of payment obligations, but any material payment default by our customers or significant reductions in existing contractual commitments could adversely impact our financial condition and operating results.

Revenue Seasonality

Historically, orders and revenue have been lowest in our first quarter and highest in our fourth quarter, with a material decline between the fourth quarter of one year and the first quarter of the following year. Due to the current economic environment and our previously announced transition to a primarily ratable license mix, we did not see the trend of higher orders and revenue in the fourth quarter of fiscal 2008 and there can be no assurance we will experience it in the future. We still expect the first quarter to remain our lowest quarter for orders and revenue.

International Operations

We have approximately 55 sales offices, design centers and research and development facilities, approximately half of which are located outside of the United States. We consider customer sales and support requirements, the availability of a skilled workforce, and costs and efficiencies, among other relative benefits, when determining what operations to locate internationally. For additional information regarding our international operations, see the discussion under the heading "The effect of foreign exchange rate fluctuations and other risks to our international operations may seriously harm our financial condition" under Item 1A, "Risk Factors" and Note 21 to our Consolidated Financial Statements.

Employees

As of January 3, 2009, we employed approximately 4,900 individuals, with approximately 1,800 in sales, services, marketing, support and manufacturing activities, approximately 2,400 in product research and development and

approximately 700 in management, administration and finance. During fiscal 2008, we initiated a restructuring plan to decrease costs by reducing our workforce across the company. This restructuring plan is expected to reduce our workforce by at least 625 positions. Approximately 300 of the affected employees were still employed by us as of January 3, 2009 due to regulatory requirements in certain jurisdictions in which we operate. For additional description of our restructuring plan, see the discussion under the heading Results of Operations Restructuring and Other Charges under Item 7, Management's Discussion and

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Analysis of Financial Condition and Results of Operations, below. None of our employees is represented by a labor union and we have experienced no work stoppages. We believe that our employee relations are good.

Executive Officers of the Registrant

The following table provides information regarding the executive officers of Cadence as of March 2, 2009:

Name	Age	Positions and Offices
Lip-Bu Tan	49	President, Chief Executive Officer and Director
Thomas A. Cooley	47	Senior Vice President, Worldwide Field Operations
James J. Cowie	44	Senior Vice President, General Counsel and Secretary
Chi-Ping Hsu	53	Senior Vice President, Research and Development
Charlie Huang	45	Senior Vice President and Chief Strategy Officer
Nimish H. Modi	46	Senior Vice President, Research and Development
Kevin S. Palatnik	51	Senior Vice President and Chief Financial Officer

Our executive officers are appointed by the Board of Directors and serve at the discretion of the Board of Directors.

LIP-BU TAN has served as President and Chief Executive Officer of Cadence since January 2009. Mr. Tan has been a member of the Cadence Board of Directors since February 2004 and serves as a member of the Finance and Technology Committees of the Cadence Board of Directors. From October 2008 to January 2009, Mr. Tan also served as Interim Vice Chairman of the Cadence Board of Directors and was a member of the Cadence Interim Office of the Chief Executive. In 1987, Mr. Tan founded Walden International, an international venture capital firm, and since that time has served as its Chairman. Mr. Tan also serves as a director of Flextronics International Ltd., Semiconductor Manufacturing International Corporation and SINA Corporation.

THOMAS A. COOLEY has served as Senior Vice President, Worldwide Field Operations of Cadence since October 2008. From March 1995 to October 2008, Mr. Cooley held several sales related positions at Cadence, most recently as Corporate Vice President of Sales for North America, EMEA and India.

JAMES J. COWIE has served as Senior Vice President and General Counsel of Cadence since April 2008 and Secretary of Cadence since May 2008. From August 2000 to March 2008, Mr. Cowie held several positions at Cadence, most recently as Corporate Vice President Business Development, Associate General Counsel and Assistant Secretary.

CHI-PING HSU has served as Senior Vice President, Research and Development of Cadence since November 2008. From April 2003 to November 2008, Mr. Hsu held several positions at Cadence, most recently as Corporate Vice President, IC Digital and Power Forward. Before joining Cadence, Mr. Hsu served as President and Chief Operating Officer of Get2Chip Inc., a supplier of high-performance system-on-chip synthesis that was acquired by Cadence in April 2003.

CHARLIE HUANG has served as Senior Vice President and Chief Strategy Officer of Cadence since January 2009. From October 2008 to January 2009, Mr. Huang also served as a member and Chief of Staff of the Cadence Interim Office of the Chief Executive. From April 2007 to January 2009, Mr. Huang served as Senior Vice President Business Development of Cadence. Mr. Huang was General Partner at Telos Venture Partners, a venture capital firm, from 2004 to 2005. From 2001 to March 2007, Mr. Huang held several positions at Cadence related to business development. Before joining Cadence, Mr. Huang co-founded and was Chief Executive Officer of CadMOS Design

Technology, Inc., an EDA company that was acquired by Cadence in 2001.

NIMISH H. MODI has served as Senior Vice President, Research and Development of Cadence since November 2008. From August 2006 to November 2008, Mr. Modi served as Corporate Vice President, Front-End Design. Before joining Cadence, from May 1988 to August 2006, Mr. Modi held several positions at Intel Corporation, a semiconductor company, most recently as Vice President in the Enterprise Platforms Group.

KEVIN S. PALATNIK has served as Senior Vice President and Chief Financial Officer of Cadence since April 2008. From October 2008 to January 2009, Mr. Palatnik also served as a member of the Cadence Interim Office of

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the Chief Executive. From January 2002 to April 2008, Mr. Palatnik served in a number of positions at Cadence, including as Corporate Vice President, Technical Field Operations and Corporate Vice President, Field Operations Finance, and most recently as Senior Vice President and Corporate Controller. Before joining Cadence, Mr. Palatnik held several engineering and senior financial positions at International Business Machines Corporation, a computer hardware and software company.

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Item 1A. Risk Factors

Our business faces many risks. Described below are what we believe to be the material risks that we face. If any of the events or circumstances described in the following risks actually occurs, our business, financial condition or results of operations could suffer.

Risks Related to Our Business

We are subject to the cyclical nature of the integrated circuit and electronics systems industries, and any downturn in these industries may reduce our revenue.

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

The IC and electronics systems industries experienced significant challenges in 2008 and may continue to face challenges in 2009 as a result of a decline in the macroeconomic environment. The IC and electronic systems industries also from time to time experience downturns in connection with, or in anticipation of, maturing product cycles of both these industries and their customers' products. As in the past, the current economic downturn is characterized by diminished product demand, production overcapacity, high inventory levels and accelerated erosion of average selling prices. The current economic downturn in the industries we serve has contributed to the substantial reduction in our revenue and could continue to harm our business, operating results and financial condition.

Our failure to respond quickly to technological developments could make our products uncompetitive and obsolete.

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

Migration to nanometer design: the size of features such as wires, transistors and contacts on ICs continuously shrink due to the ongoing advances in the semiconductor manufacturing processes. Process feature sizes refer to the width of the transistors and the width and spacing of interconnect on the IC. Feature size is normally identified by the transistor length, which is shrinking rapidly to 32 nanometers and smaller. This is commonly referred to in the semiconductor industry as the migration to nanometer design. It represents a major challenge for participants in the semiconductor industry, from IC design and design automation to design of manufacturing equipment and the manufacturing process itself. Shrinkage of transistor length to such proportions is challenging the industry in the application of more complex physics and chemistry that is needed to realize advanced silicon devices. For EDA tools, models of each component's electrical properties and behavior become more complex as do requisite analysis, design and verification capabilities. Novel design tools and methodologies must be invented quickly to remain competitive in the design of electronics in the smallest nanometer ranges.

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

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

With the availability of seemingly endless gate capacity, there is an increase in design reuse, or the combining of off-the-shelf design IP with custom logic to create ICs. The unavailability of high-quality design IP that can be reliably incorporated into a customer's design with our IC implementation products and services could reduce demand for our products and services.

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

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

If we are unable to respond quickly and successfully to these trends, we may lose our competitive position, and our products or technologies may become uncompetitive or obsolete. To compete successfully, we must develop or acquire new products and improve our existing products and processes on a schedule that keeps pace with technological developments and the requirements for products addressing a broad spectrum of designers and designer expertise in our industries. We must also be able to support a range of changing computer software, hardware platforms and customer preferences. We cannot guarantee that we will be successful in this effort.

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

We have experienced, and may continue to experience, varied operating results. In particular, we experienced a net loss during fiscal 2008 and we expect to experience a net loss during fiscal 2009. Various factors affect our operating results and some of them are not within our control. Our operating results for any period are affected by the timing of significant orders for our software products because a significant number of licenses for our software products are in excess of \$5.0 million.

Our operating results are also affected by the mix of license types executed in any given period. We license software using three different license types: subscription, term and perpetual. Product revenue associated with term and perpetual licenses is generally recognized at the beginning of the license period, whereas product revenue associated with subscription licenses is recognized over multiple periods during the term of the license. Revenue may also be deferred under term and perpetual licenses until payments become due and payable from customers with nonlinear payment terms or as cash is collected from customers with lower credit ratings. In addition, revenue is impacted by the timing of license renewals, the extent to which contracts contain flexible payment terms, changes in existing contractual arrangements with customers and the mix of license types (i.e., perpetual, term or subscription) for existing customers, which changes could have the effect of accelerating or delaying the recognition of revenue from the timing of recognition under the original contract. Our license mix has changed such that a higher proportion of licenses require ratable revenue recognition and we expect the change in our license mix, combined with the difficult economic environment, will result in a decrease in our revenue for fiscal 2009 as compared to fiscal 2008.

We plan operating expense levels primarily based on forecasted revenue levels. These expenses and the impact of long-term commitments are relatively fixed in the short term. In addition, revenue levels are harder to forecast in a difficult economic environment. A shortfall in revenue could lead to operating results below expectations because we may not be able to quickly reduce these fixed expenses in response to these short-term business changes.

The majority of our contracts are executed in the final few weeks of a fiscal quarter. This makes it difficult to determine with accuracy how much business will be executed in each fiscal quarter. Due to the volume or complexity of transactions that we review at the very end of the quarter, or due to operational matters regarding particular agreements, we may not finish processing or ship products under some contracts that have been signed during that fiscal quarter, which means that the associated revenue cannot be recognized in that particular period.

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

or investors, the trading price of our common stock could decline.

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Our stock price has been subject to fluctuations and has experienced a significant decline, and may continue to be subject to fluctuations and decline.

The market price of our common stock has recently experienced significant fluctuations and may continue to fluctuate in the future, and as a result you could lose the value of your investment. The market price of our common stock may be affected by a number of factors, such as:

- Announcements of our quarterly operating results and revenue and earnings forecasts that fail to meet or are inconsistent with earlier projections or the expectations of our securities analysts or investors;
- Changes in our revenue and earnings estimates;
- Announcements of a restructuring plan;
- Changes in management;
- Accounting charges relating to the impairment of goodwill;
- A gain or loss of a significant customer or market segment share;
- Announcements of new products by us, our competitors or our customers; and
- Market conditions in the electronics systems and semiconductor industries.

In addition, equity markets in general have experienced extreme price and volume fluctuations and the market prices of many technology companies have decreased substantially, particularly electronic systems and semiconductor companies. Such price and volume fluctuations may continue to adversely affect the market price of our common stock for reasons unrelated to our business or operating results.

Litigation could adversely affect our financial condition or operations.

We are currently, and in the future may be, involved in various disputes and litigation that arise in the ordinary course of business. These include disputes and lawsuits related to intellectual property, mergers and acquisitions, licensing, contracts, distribution arrangements and employee relations matters. We are also currently engaged in several securities class actions and derivative lawsuits. For information regarding the litigation matters in which we are currently engaged, please refer to the discussion under Item 3, Legal Proceedings. We cannot provide any assurances that the final outcome of these lawsuits or any other proceedings that may arise in the future will not have a material adverse effect on our business, operating results or financial condition. Litigation can be time-consuming and expensive and could divert management's time and attention from our business, which could have a material adverse effect on our revenues and operating results. The adverse resolution of any specific lawsuit or proceeding could also have a material adverse effect on our business, operating results, financial condition and cash flows.

Matters relating to or arising from our recent restatement and weaknesses in our internal controls could have a material adverse effect on our business, operating results and financial condition.

In connection with the restatement of our previously issued financial statements for the periods ended March 29, 2008 and June 28, 2008 and our reassessment of our disclosure controls and procedures under Item 307 of Regulation S-K, management concluded that as of March 29, 2008, June 28, 2008 and September 27, 2008, our disclosure controls and procedures were not effective and that we had a material weakness in our internal control over financial reporting. Please refer to the discussion under Item 9A, Controls and Procedures for further discussion of the remediation of this material weakness as of January 3, 2009. Should we identify any other material weakness and be unable to remediate any such other material weakness promptly and effectively, such weakness could harm our operating results, result in a material misstatement of our financial statements, cause us to fail to meet our financial reporting obligations or prevent us from providing reliable and accurate financial reports or avoiding or detecting fraud. This, in turn, could result in a loss of investor confidence in the accuracy and completeness of our financial reports, which could have an adverse effect on our stock price. Any litigation or other proceeding or adverse publicity relating to our remediated

material weakness or any future material weakness could have a material adverse effect on our business and operating results.

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Our operating results and revenue could be adversely affected by customer payment delays, customer bankruptcies and defaults or modifications of licenses or supplier modifications in response to the economic environment.

As a result of challenges currently affecting the economy of the United States and other regions of the world, our customers, who are concentrated in the semiconductor sector, have experienced and may continue to experience adverse changes in their business and, as a result, may delay or default on their payment obligations, file for bankruptcy or modify or cancel plans to license our products, and our suppliers may significantly and quickly increase their prices or reduce their output. If our customers are not successful in generating sufficient revenue or are precluded from securing financing, they may not be able to pay, or may delay payment of, accounts receivable that are owed to us, although these obligations are generally not cancelable. Our customers' inability to fulfill payment obligations may adversely affect our revenue and cash flow. Additionally, our customers may seek to renegotiate pre-existing contractual commitments. Though we have not yet experienced a material level of defaults, any material payment default by our customers or significant reductions in existing contractual commitments would have a material adverse effect on our financial condition and operating results. Because of the escalating challenges in the global capital markets and financial institutions, including a tightening in the capital and credit markets, if we were to seek funding from the capital or credit markets in response to any material level of customer defaults, we may not be able to secure funding on terms acceptable to us or at all.

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

Our installed customer base has traditionally generated additional new license, service and maintenance revenues. In future periods, customers may not necessarily license or buy additional products or contract for additional services or maintenance. Maintenance is generally renewable annually at a customer's option, and there are no mandatory payment obligations or obligations to license additional software. If our customers decide not to renew their maintenance agreements or license additional products or contract for additional services, or if they reduce the scope of the maintenance agreements, our revenue could decrease, which could have an adverse effect on our operating results. Our customers, which include large semiconductor companies, often have significant bargaining power in negotiations with us. Mergers or acquisitions of our customers can reduce the total level of purchases of our software and services, and in some cases, increase customers' bargaining power in negotiations with their suppliers, including us.

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

Our business depends upon the efforts and abilities of our executive officers and other key employees, including key development personnel. From time to time, there may be changes in our management team resulting from the hiring and departure of executive officers. On October 15, 2008, we announced the resignations of our President and Chief Executive Officer, Executive Vice President and Chief Administrative Officer, Executive Vice President - Worldwide Field Operations, Executive Vice President - Products and Technologies Organization and Executive Vice President Corporate Affairs. On January 8, 2009, we announced that Lip-Bu Tan was appointed our new President and Chief Executive Officer. As we undergo this transition, we may experience disruption to our business that may harm our operating results and our relationships with our employees, customers and suppliers may be adversely affected. In addition, our competitors may seek to use this transition and the related potential disruptions to gain a competitive advantage over us.

Competition for highly skilled executive officers and employees can be intense, particularly in geographic areas recognized as high technology centers such as the Silicon Valley area, where our principal offices are located, and the other locations where we maintain facilities. To attract, retain and motivate individuals with the requisite expertise, we may be required to grant large numbers of stock options or other stock-based incentive awards, which may be dilutive to existing stockholders and increase compensation expense, and pay significant base salaries and cash bonuses, which could harm our operating results. The high cost of training new employees, not fully utilizing

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these employees, or losing trained employees to competing employers could also reduce our gross margins and harm our business or operating results.

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

We may not be able to effectively implement our restructuring plans, and our restructuring plans may not result in the expected benefits, which would negatively impact our future results of operations.

During fiscal 2008, we initiated a restructuring plan in an effort to align our cost structure with expected revenue. This restructuring plan is intended to decrease costs throughout our company. We cannot assure you that we will be able to successfully complete and realize the expected benefits of our restructuring plan, such as improvements in operating margins and cash flows, in the restructuring periods contemplated. The restructuring plan may involve higher costs or a longer timetable than we currently anticipate or it may fail to improve our results of operations as we anticipate. Our inability to realize these benefits may result in an inefficient business structure that could negatively impact our results of operations. We also expect our restructuring plan to cause us to incur substantial costs related to severance and other employee-related costs. Our restructuring plan may also subject us to litigation risks and expenses. In addition, our restructuring plan may have other consequences, such as attrition beyond our planned reduction in workforce or a negative impact on employee morale and our competitors may seek to gain a competitive advantage over us. Together with our changes in management, the restructuring plan could also cause our remaining employees to leave or result in reduced productivity by our remaining employees, which in turn may affect our revenue and other operating results in the future.

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

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

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

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

The development by others of competitive EDA products or platforms and engineering services, which could result in a shift of customer preferences away from our products and services and significantly decrease revenue;

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

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The challenges of developing (or acquiring externally-developed) technology solutions that are adequate and competitive in meeting the requirements of next-generation design challenges;
The significant number of current and potential competitors in the EDA industry and the low cost of entry;
Intense competition to attract acquisition targets, which may make it more difficult for us to acquire companies or technologies at an acceptable price or at all; and
The combination of or collaboration among many EDA companies to deliver more comprehensive offerings than they could individually.

We compete in the EDA products market with Synopsys, Inc., Magma Design Automation, Inc. and Mentor Graphics Corporation. We also compete with numerous smaller EDA companies, with manufacturers of electronic devices that have developed or have the capability to develop their own EDA products, and with numerous electronics design and consulting companies. Manufacturers of electronic devices may be reluctant to purchase engineering services from independent vendors such as us because they wish to promote their own internal design departments.

We may need to change our pricing models to compete successfully.

The highly competitive markets in which we compete can put pressure on us to reduce the prices of our products. If our competitors offer deep discounts on certain products in an effort to recapture or gain market segment share or to sell other software or hardware products, we may then need to lower our prices or offer other favorable terms to compete successfully. Any such changes would be likely to reduce our profit margins and could adversely affect our operating results. Any substantial changes to our prices and pricing policies could cause sales and software license revenues to decline or be delayed as our sales force implements and our customers adjust to the new pricing policies. Some of our competitors may bundle products for promotional purposes or as a long-term pricing strategy or provide guarantees of prices and product implementations. These practices could, over time, significantly constrain the prices that we can charge for our products. If we cannot offset price reductions with a corresponding increase in the number of sales or with lower spending, then the reduced license revenues resulting from lower prices could have an adverse effect on our results of operations.

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

We have acquired and expect to acquire other companies and businesses in the future. While we expect to carefully analyze each potential acquisition before committing to the transaction, we may not consummate any particular transaction, which can nevertheless result in significant costs, or if a transaction is consummated, we may not be able to integrate and manage acquired products and businesses effectively. In addition, acquisitions involve a number of risks. If any of the following events occurs after we acquire another business, it could seriously harm our business, operating results or financial condition:

Difficulties in combining previously separate businesses into a single unit;
The substantial diversion of management's attention from day-to-day business when evaluating and negotiating these transactions and integrating an acquired business;
The discovery, after completion of the acquisition, of liabilities assumed from the acquired business or of assets acquired for which we cannot realize the anticipated value and the exposure to such assumed liabilities;
The failure to realize anticipated benefits such as cost savings and revenue enhancements;
The failure to retain key employees of the acquired business;
Difficulties related to integrating the products of an acquired business in, for example, distribution, engineering and customer support areas;
Unanticipated costs;

Customer dissatisfaction with existing license agreements with us, which may dissuade them from licensing or buying products acquired by us after the effective date of the license; and
The failure to understand and compete effectively in markets in which we have limited experience.

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

The specific performance goal levels and amounts and timing of employee bonuses or contingent purchase price payments vary with each acquisition. While we expect to derive value from an acquisition in excess of such contingent payment obligations, our strategy may change and we may be required to make certain contingent payments without deriving the anticipated value. In connection with our acquisitions completed before January 3, 2009, we may be obligated to pay up to an aggregate of \$51.0 million in cash during the next 44 months if certain defined performance goals are achieved in full, which would be expensed as compensation expense in our Consolidated Statements of Operations.

In December 2007, the Financial Accounting Standards Board, or FASB, issued Statement of Financial Accounting Standard, or SFAS, No. 141R, Business Combinations, which will change how business acquisitions are accounted for and will impact financial statements both on the acquisition date and in subsequent periods. SFAS No. 141R is effective for fiscal years beginning after December 15, 2008. Early adoption is not permitted. We are currently evaluating the impact that SFAS No. 141R will have on our Consolidated Financial Statements.

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

Our success depends, in part, upon our proprietary technology. We generally rely on patents, copyrights, trademarks, trade secret laws, licenses and restrictive agreements to establish and protect our proprietary rights in technology and products. Despite precautions we may take to protect our intellectual property, third parties have tried in the past, and may try in the future, to challenge, invalidate or circumvent these safeguards. The rights granted under our patents or attendant to our other intellectual property may not provide us with any competitive advantages and there is no guarantee that patents will be issued on any of our pending applications and future patents may not be sufficiently broad to protect our technology. Furthermore, the laws of foreign countries may not protect our proprietary rights in those countries to the same extent as applicable law protects these rights in the United States. The protection of our intellectual property may require the expenditure of significant financial and managerial resources. Litigation can be time-consuming and expensive and could divert management's time and attention from our business, which could have a material adverse effect on our revenues and operating results. Moreover, the steps we take to protect our intellectual property may not adequately protect our rights or prevent third parties from infringing or misappropriating our proprietary rights. Many of our products include software or other intellectual property licensed from third parties. We may have to seek new or renew existing licenses for such software and other intellectual property in the future. Our engineering services business holds licenses to certain software and other intellectual property owned by third parties, including that of our competitors. Our failure to obtain software or other intellectual property licenses or other intellectual property rights that is necessary or helpful for our business on favorable terms, or the need to engage in litigation over these licenses or rights, could seriously harm our business, operating results or financial condition.

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

There are numerous patents in the EDA industry and new patents are being issued at a rapid rate. It is not always practicable to determine in advance whether a product or any of its components infringes the patent rights of others. As a result, from time to time, we may be compelled to respond to or prosecute intellectual property infringement claims to protect our rights or defend a customer's rights.

Intellectual property infringement claims, regardless of merit, could consume valuable management time, result in costly litigation, or cause product shipment delays, all of which could seriously harm our business, operating results or financial condition. In settling these claims, we may be required to enter into royalty or licensing agreements with the third parties claiming infringement. These royalty or licensing agreements, if available, may not have terms favorable to us. Being compelled to enter into a license agreement with unfavorable terms could seriously harm our business, operating results or financial condition. Any potential intellectual property litigation could compel us to do one or more of the following:

- Pay damages (including the potential for treble damages), license fees or royalties (including royalties for past periods) to the party claiming infringement;
- Stop licensing products or providing services that use the challenged intellectual property;
- Obtain a license from the owner of the infringed intellectual property to sell or use the relevant technology, which license may not be available on reasonable terms, or at all; or
- Redesign the challenged technology, which could be time-consuming and costly, or not be accomplished.

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

If our security measures are breached and an unauthorized party obtains access to customer data, our information systems may be perceived as being insecure and customers may curtail or stop their use of our products and services.

Our products and services involve the storage and transmission of customers' proprietary information, and breaches of our security measures could expose us to a risk of loss or misuse of this information, litigation and potential liability. Because techniques used to obtain unauthorized access or to sabotage information systems change frequently and generally are not recognized until launched against a target, we may be unable to anticipate these techniques or to implement adequate preventive measures. If an actual or perceived breach of our security occurs, the market perception of the effectiveness of our security measures could be harmed and we could lose existing customers and our ability to obtain new customers.

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

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

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

The timing of customers' competitive evaluation processes; or
Customers' budgetary constraints and budget cycles.

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

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The majority of our contracts are executed in the final few weeks of a fiscal quarter. This makes it difficult to determine with accuracy how much business will be executed in each fiscal quarter. Also, because of the timing of large orders and our customers' buying patterns, we may not learn of bookings shortfalls, revenue shortfalls, earnings shortfalls or other failures to meet market expectations until late in a fiscal quarter. These factors may cause our operating results to fluctuate unexpectedly, which can cause significant fluctuations in the trading price of our common stock.

We may not be able to sell certain installment contracts to generate cash, which may impact our operating cash flows for any particular fiscal period.

We sell certain installment contracts to certain financial institutions on a non-recourse or limited-recourse basis to generate cash. Our ability to complete these sales of installment contracts is affected by a number of factors, including the:

- Economic conditions in the securities markets;
- Credit policies of the financial institutions; and
- Credit quality of customers whose installment contracts we wish to sell.

Disruptions in the financial markets have and may continue to adversely impact the availability and cost of financing transactions for the installment contract sales that we have already arranged or may arrange. As a result of the credit losses recorded by banks during 2008 and the current financial challenges experienced by banks, a number of banks have become less willing to purchase assets because of capital constraints and concerns about over-exposure to the technology sector. In addition, the change in our license mix will result in an increased number of subscription licenses and a decrease in the sale of receivables to financial institutions, so we expect a reduced level of Proceeds from the sale of receivables throughout fiscal 2009. If we are unable to sell certain installment contracts, our operating cash flows would be adversely affected. There can be no assurance that funding will be available to us or, if available, that it will be on terms acceptable to us. If sources of funding are not available to us on a regular basis for any reason, including the occurrence of events of default, deterioration in credit quality in the underlying pool of receivables or otherwise, it would have a material adverse effect on our operating cash flows.

The effect of foreign exchange rate fluctuations and other risks to our international operations may seriously harm our financial condition.

We have significant operations outside the United States. Our revenue from international operations as a percentage of total revenue was approximately 58% during fiscal 2008, 54% during fiscal 2007 and 48% during fiscal 2006. We expect that revenue from our international operations will continue to account for a significant portion of our total revenue. We also transact business in various foreign currencies, primarily the Japanese yen. The volatility of foreign currencies in certain regions, most notably the Japanese yen, European Union euro, British pound and Indian rupee have had, and may in the future have, a harmful effect on our revenue or operating results.

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

the same amount of the foreign currency. As we use the foreign currency to pay for payroll costs and other operating expenses in our international operations, this results in an increase in operating expenses.

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

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attempt to reduce the impact of foreign currency fluctuations, significant exchange rate movements may hurt our results of operations as expressed in United States dollars.

Our international operations may also be subject to other risks, including:

- The adoption or expansion of government trade restrictions;
- Limitations on repatriation of earnings;
- Limitations on the conversion of foreign currencies;
- Reduced protection of intellectual property rights in some countries;
- Recessions in foreign economies;
- Longer collection periods for receivables and greater difficulty in collecting accounts receivable;
- Difficulties in managing foreign operations;
- Political and economic instability;
- Unexpected changes in regulatory requirements;
- Tariffs and other trade barriers; and
- United States and other governments' licensing requirements for exports, which may lengthen the sales cycle or restrict or prohibit the sale or licensing of certain products.

We have offices throughout the world, including key research and development facilities outside of the United States. Our operations are dependent upon the connectivity of our operations throughout the world. Activities that interfere with our international connectivity, such as computer hacking or the introduction of a virus into our computer systems, could significantly interfere with our business operations.

Our operating results could be adversely affected as a result of changes in our effective tax rates.

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

- Earnings being lower than anticipated in countries where we are taxed at lower rates as compared to the United States federal and state statutory tax rates;
- An increase in expenses not deductible for tax purposes, including certain stock-based compensation, write-offs of acquired in-process technology and impairment of goodwill;
- Changes in the valuation allowance against our deferred tax assets;
- Changes in tax laws or the interpretation of such tax laws;
- Changes in judgment from the evaluation of new information that results in a recognition, derecognition, or change in measurement of a tax position taken in a prior period;
- Increases to interest expenses classified in the financial statements as income taxes;
- New accounting standards or interpretations of such standards;
- A change in our decision to indefinitely reinvest foreign earnings outside the United States; or
- Results of tax examinations by the Internal Revenue Service, or IRS, and state and foreign tax authorities.

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

We have received an examination report from the IRS proposing deficiencies in certain of our tax returns, and the outcome of current and future tax examinations may have a material adverse effect on our results of operations and cash flows.

The IRS and other tax authorities regularly examine our income tax returns. In July 2006, the IRS completed its field examination of our federal income tax returns for the tax years 2000 through 2002 and issued a Revenue Agents

Report, or RAR, in which the IRS proposed to assess an aggregate tax deficiency for the three-year period of approximately \$324.0 million. In November 2006, the IRS revised the proposed aggregate tax deficiency for the three-year period to be approximately \$318.0 million. The IRS is contesting our qualification for deferred recognition of certain proceeds received from restitution and settlement in connection with litigation during the period. The proposed tax deficiency for this item is approximately \$152.0 million. The remaining proposed tax deficiency of approximately \$166.0 million is primarily related to proposed adjustments to our transfer pricing

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arrangements with foreign subsidiaries and to our deductions for foreign trade income. The IRS may make similar claims against our transfer pricing arrangements and deductions for foreign trade income in future examinations. We have filed a timely protest with the IRS and are seeking resolution of the issues through the Appeals Office of the IRS, or the Appeals Office.

We believe that the proposed IRS adjustments are inconsistent with applicable tax laws and we are vigorously challenging these proposed adjustments. The RAR is not a final Statutory Notice of Deficiency but the IRS imposes interest on the proposed deficiencies until the matters are resolved. Interest is compounded daily at rates published and adjusted quarterly by the IRS and have been between 4% and 10% since 2001. The IRS is currently examining our federal income tax returns for the tax years 2003 through 2005.

Significant judgment is required in applying the principles of FASB Interpretation, or FIN, No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 and SFAS No. 109, Accounting for Income Taxes. The calculation of our provision for income taxes involves dealing with uncertainties in the application of complex tax laws and regulations. In determining the adequacy of our provision for income taxes, we regularly assess the potential settlement outcomes resulting from income tax examinations. However, the final outcome of tax examinations, including the total amount payable or the timing of any such payments upon resolution of these issues, cannot be estimated with certainty. In addition, we cannot be certain that such amount will not be materially different than that which is reflected in our historical income tax provisions and accruals. Should the IRS or other tax authorities assess additional taxes as a result of a current or a future examination, we may be required to record charges to operations in future periods that could have a material impact on the results of operations, financial position or cash flows in the applicable period or periods.

Forecasting our estimated annual effective tax rate is complex and subject to uncertainty, and material differences between forecasted and actual tax rates could have a material impact on our results of operations.

Forecasts of our income tax position and resultant effective tax rate are complex and subject to uncertainty because our income tax position for each year combines the effects of estimating our annual income or loss, the mix of profits and losses earned by us and our subsidiaries in tax jurisdictions with a broad range of income tax rates, as well as benefits from available deferred tax assets, the impact of various accounting rules and changes to these rules and results of tax audits. To forecast our global tax rate, pre-tax profits and losses by jurisdiction are estimated and tax expense by jurisdiction is calculated. If our estimate of the pre-tax profit and losses, the mix of our profits and losses, our ability to use deferred tax assets, the results of tax audits, or effective tax rates by jurisdiction is different than those estimates, our actual tax rate could be materially different than forecasted, which could have a material impact on our results of operations.

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

We must comply with regulations of the United States and of certain other countries in shipping our software products and transferring our technology outside the United States and to foreign nationals. Although we have not had any significant difficulty complying with such regulations so far, any significant future difficulty in complying could harm our business, operating results or financial condition.

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

Our customers use our products and services in designing and developing products that involve a high degree of technological complexity, each of which has its own specifications. Because of the complexity of the systems and products with which we work, some of our products and designs can be adequately tested only when put to full use in

the marketplace. As a result, our customers or their end users may discover errors or defects in our software or the systems we design, or the products or systems incorporating our design and intellectual property may not operate as expected. Errors or defects could result in:

- Loss of customers;
- Loss of market segment share;

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Failure to attract new customers or achieve market acceptance;
Diversion of development resources to resolve the problem;
Loss of or delay in revenue;
Increased service costs; and
Liability for damages.

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

Companies in our industry whose employees accept positions with competitors frequently claim that these competitors have engaged in unfair hiring practices or that the employment of these persons would involve the disclosure or use of trade secrets. These claims could prevent us from hiring employees or cause us to incur liability for damages. We could also incur substantial costs in defending ourselves or our employees against these claims, regardless of their merits. Defending ourselves from these claims could also divert the attention of our management away from our operations.

Our business is subject to the risk of earthquakes.

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

We maintain research and development and other facilities in parts of the world that are not as politically stable as the United States, and as a result we may face a higher risk of business interruption from acts of war or terrorism than businesses located only or primarily in the United States.

We maintain international research and development and other facilities, some of which are in parts of the world that are not as politically stable as the United States. Consequently, we may face a greater risk of business interruption as a result of terrorist acts or military conflicts than businesses located domestically. Furthermore, this potential harm is exacerbated given that damage to or disruptions at our international research and development facilities could have an adverse effect on our ability to develop new or improve existing products as compared to other businesses which may only have sales offices or other less critical operations abroad. We are not insured for losses or interruptions caused by acts of war or terrorism.

Risks Related to Our Securities and Indebtedness

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

We have a substantial level of debt. As of January 3, 2009, we had \$500.2 million of outstanding indebtedness as follows:

\$250.0 million related to our 1.375% Convertible Senior Notes Due 2011, or the 2011 Notes;
\$250.0 million related to our 1.500% Convertible Senior Notes Due 2013, or the 2013 Notes and, together with the 2011 Notes, the Convertible Senior Notes; and
\$0.2 million related to our Zero Coupon Zero Yield Senior Convertible Notes Due 2023, or the 2023 Notes.

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

Make it difficult for us to satisfy our payment obligations on our debt as described below;
Make us more vulnerable in the event of a downturn in our business;
Reduce funds available for use in our operations;
Make it difficult for us to incur additional debt or obtain any necessary financing in the future for working capital, capital expenditures, debt service, acquisitions or general corporate purposes;

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Impose operating or financial covenants on us;
Limit our flexibility in planning for or reacting to changes in our business; or
Place us at a possible competitive disadvantage relative to less leveraged competitors and competitors that have greater access to capital resources.

While we are not currently a party to any loans that would prohibit us from making payment on our outstanding convertible notes, we are not prevented by the terms of the convertible notes from entering into other loans that could prohibit such payments. If we are prohibited from paying our outstanding indebtedness, we could try to obtain the consent of the lenders under those arrangements to make such payment, or we could attempt to refinance the borrowings that contain the restrictions. If we do not obtain the necessary consents or refinance the borrowings, we may be unable to satisfy our outstanding indebtedness. Any such failure would constitute an event of default under our indebtedness, which could, in turn, constitute a default under the terms of any other indebtedness then outstanding.

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

We have in the past and may in the future attempt to access the capital or credit markets in order to obtain funding to meet particular liquidity needs. Because of the escalating challenges in the global capital markets and financial institutions, including a tightening in the capital and credit markets, compounded by the increasingly challenging and price-conscious economic environment and our lower levels of business, we may not be able to secure additional funding on terms acceptable to us or at all, which could adversely impact our business and operating results.

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

In May 2008, the FASB issued FASB Staff Position, or FSP, Accounting Principles Board Opinion, or APB 14-1, Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement), which will require us to recognize additional non-cash interest expense related to our Convertible Senior Notes in our Consolidated Statements of Operations. FSP APB 14-1 is effective for fiscal 2009 and is required to be applied retrospectively for all periods for which our Convertible Senior Notes were outstanding before the date of adoption. FSP APB 14-1 will have an adverse effect on our operating results and financial condition, particularly with respect to interest expense ratios commonly referred to by lenders, and could potentially hinder our ability to raise capital through the issuance of debt or equity securities.

Conversion of the Convertible Senior Notes will dilute the ownership interests of existing stockholders.

The terms of the Convertible Senior Notes permit the holders to convert the Convertible Senior Notes into shares of our common stock. The terms of the Convertible Senior Notes stipulate a net share settlement, which upon conversion of the Convertible Senior Notes requires us to pay the principal amount in cash and the conversion premium, if any, in shares of our common stock based on a daily settlement amount, calculated on a proportionate basis for each day of the relevant 20 trading-day observation period. The initial conversion rate for the Convertible Senior Notes is 47.2813 shares of our common stock per \$1,000 principal amount of Convertible Senior Notes, equivalent to a conversion price of approximately \$21.15 per share of our common stock. The conversion price is subject to adjustment in some events but will not be adjusted for accrued interest, except in limited circumstances. The

conversion of some or all of the Convertible Senior Notes will dilute the ownership interest of our existing stockholders. Any sales in the public market of the common stock issuable upon conversion could adversely affect prevailing market prices of our common stock.

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Each \$1,000 of principal of the Convertible Senior Notes is initially convertible into 47.2813 shares of our common stock, subject to adjustment upon the occurrence of specified events. Holders of the Convertible Senior Notes may convert their notes at their option on any day before the close of business on the scheduled trading day immediately preceding December 15, 2011 in the case of the 2011 Notes and December 15, 2013 in the case of the 2013 Notes, in each case only if:

The price of our common stock reaches \$27.50 during certain periods of time specified in the Convertible Senior Notes;
Specified corporate transactions occur; or
The trading price of the Convertible Senior Notes falls below 98% of the product of (i) the last reported sale price of our common stock and (ii) the conversion rate on that date.

On and after November 2, 2011, in the case of the 2011 Notes, and November 1, 2013, in the case of the 2013 Notes, until the close of business on the scheduled trading day immediately preceding the maturity date of such Convertible Senior Notes, holders may convert their Convertible Senior Notes at any time, regardless of the foregoing circumstances. As of January 3, 2009, none of the conditions allowing holders of the Convertible Senior Notes to convert had been met.

Although the conversion price of the Convertible Senior Notes is currently \$21.15 per share, concurrent with the issuance of the Convertible Senior Notes, we entered into hedge and separate warrant transactions to reduce the potential dilution from the conversion of the Convertible Senior Notes. However, we cannot guarantee that such hedges and warrant instruments will fully mitigate the dilution. In addition, the existence of the Convertible Senior Notes may encourage short selling by market participants because the conversion of the Convertible Senior Notes could depress the price of our common stock.

At the option of the holders of the Convertible Senior Notes, under certain circumstances we may be required to repurchase the Convertible Senior Notes in cash or shares of our common stock.

Under the terms of the Convertible Senior Notes, we may be required to repurchase the Convertible Senior Notes following a fundamental change in our corporate ownership or structure, such as a change of control in which substantially all of the consideration does not consist of publicly traded securities, prior to maturity of the Convertible Senior Notes. The repurchase price for the Convertible Senior Notes in the event of a fundamental change must be paid solely in cash. This repayment obligation may have the effect of discouraging, delaying or preventing a takeover of our company that may otherwise be beneficial to investors.

Hedge and warrant transactions entered into in connection with the issuance of the Convertible Senior Notes may affect the value of our common stock.

We entered into hedge transactions with various financial institutions, at the time of issuance of the Convertible Senior Notes, with the objective of reducing the potential dilutive effect of issuing our common stock upon conversion of the Convertible Senior Notes. We also entered into separate warrant transactions with the same financial institutions. In connection with our hedge and warrant transactions, these financial institutions purchased our common stock in secondary market transactions and entered into various over-the-counter derivative transactions with respect to our common stock. These entities or their affiliates are likely to modify their hedge positions from time to time prior to conversion or maturity of the Convertible Senior Notes by purchasing and selling shares of our common stock, other of our securities or other instruments they may wish to use in connection with such hedging. Any of these transactions and activities could adversely affect the value of our common stock and, as a result, the number of shares and the value of the common stock holders will receive upon conversion of the Convertible Senior Notes. In addition, subject to movement in the price of our common stock, if the hedge transactions settle in our favor, we could be

exposed to credit risk related to the other party with respect to the payment we are owed from such other party. If the financial institutions with which we entered into these hedge transactions were to fail or default, our ability to settle on these transactions could be harmed or delayed.

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Rating agencies may provide unsolicited ratings on the Convertible Senior Notes that could reduce the market value or liquidity of our common stock.

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

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

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

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

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

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

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

We own land and buildings at our headquarters, which is located in San Jose, California. We also own buildings in India. As of January 3, 2009, the total square footage of our owned buildings was approximately 950,000, which includes our newly constructed building located at our headquarters. During the first quarter of fiscal 2009, we occupied all of the approximately 208,000 square feet available in our new building.

In January 2007, we completed the sale of certain of our land and buildings in San Jose, California. Concurrently with the sale, we leased back from the purchaser all available space in the buildings for two years. The lease term ended in January 2009, and we have vacated the leased buildings.

We lease additional facilities in the United States and various other countries. We sublease certain of these facilities where space is not fully utilized or has been involved in restructuring plans.

We believe that these facilities, including our newly constructed building located at our headquarters, are adequate for our current needs and that suitable additional or substitute space will be available as needed to accommodate any expansion of our operations.

Item 3. Legal Proceedings

From time to time, we are involved in various disputes and litigation that arise in the ordinary course of business. These include disputes and lawsuits related to intellectual property, mergers and acquisitions, licensing,

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contracts, distribution arrangements and employee relations matters. At least quarterly, we review the status of each significant matter and assess its potential financial exposure. If the potential loss from any claim or legal proceeding is considered probable and the amount or the range of loss can be estimated, we accrue a liability for the estimated loss in accordance with SFAS No. 5, Accounting for Contingencies. Legal proceedings are subject to uncertainties, and the outcomes are difficult to predict. Because of such uncertainties, accruals are based only on the best information available at the time. As additional information becomes available, we reassess the potential liability related to pending claims and litigation matters and may revise estimates.

During fiscal 2008, three complaints were filed in the United States District Court for the Northern District of California, or District Court, all alleging violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, as amended, or Exchange Act, and Rule 10b-5 promulgated thereunder, on behalf of a purported class of purchasers of our common stock. The plaintiffs in these actions allege that the company and the individual defendants made statements during the class period regarding our financial results that were false and misleading because we had recognized revenue that should have been recognized in subsequent quarters. The plaintiffs requested certification of the actions as a class action, unspecified damages and interest, the plaintiffs' reasonable costs, including attorneys' and experts' fees, and unspecified equitable or injunctive relief. The first such complaint was filed on October 29, 2008, captioned *Hu v. Cadence Design Systems, Inc., Michael J. Fister, William Porter and Kevin S. Palatnik*; the second such complaint was filed on November 4, 2008, captioned *Vyas v. Cadence Design Systems, Inc., Michael J. Fister, and Kevin S. Palatnik*; and the third such complaint was filed on November 21, 2008, captioned *Collins v. Cadence Design Systems, Inc., Michael J. Fister, John B. Shoven, Kevin S. Palatnik and William Porter*. Various plaintiffs have filed motions seeking to be named lead plaintiff, and to have these complaints consolidated. Those motions are set to be heard by the Court on March 6, 2009. We intend to vigorously defend these and any other securities lawsuits that may be filed.

During fiscal 2008, two derivative complaints were filed in Santa Clara County Superior Court. The first was filed on November 20, 2008, and captioned *Ury Priel*, derivatively on behalf of nominal defendant Cadence Design Systems, Inc. v. John B. Shoven, Lip-Bu Tan, Alberto Sangiovanni-Vincentelli, Donald L. Lucas, Sr., Roger Siboni, George Scalise, Michael J. Fister, and Doe Defendants 1-15. The second was filed on December 1, 2008, and captioned *Mark Levine*, derivatively on behalf of nominal defendant Cadence Design Systems, Inc. v. John B. Shoven, Lip-Bu Tan, Alberto Sangiovanni-Vincentelli, Donald L. Lucas, Sr., Roger Siboni, George Scalise, Michael J. Fister, John Swainson and Doe Defendants 1-10. These complaints purport to bring suit derivatively, on behalf of Cadence, against certain of our current and former directors for alleged breach of fiduciary duty, abuse of control, gross mismanagement, waste of corporate assets and unjust enrichment. Many of the allegations underlying these claims are similar or identical to the allegations in the securities class action lawsuits described above, and further allege that the individual defendants approved compensation based on inflated financial results. The plaintiffs request unspecified damages, restitution, equitable relief and their reasonable attorneys' fees, experts' fees, costs and expenses on behalf of us against the individual defendants. A motion to consolidate these complaints was granted on January 20, 2009. We are analyzing these derivative complaints and will respond to them appropriately.

In light of the preliminary status of these lawsuits, we cannot predict the claims, allegations, class period (in the case of the class actions), or outcome of these matters. We cannot provide any assurances that the final outcome of these lawsuits or any other lawsuits or proceedings that may arise in the future will not have a material adverse effect on our business, operating results or financial condition. Litigation can be time-consuming and expensive and could divert management's time and attention from our business, which could have a material adverse effect on our revenues and operating results.

While the outcome of these disputes and litigation matters cannot be predicted with any certainty, management does not believe that the outcome of any current matters will have a material adverse effect on our consolidated financial position, liquidity or operating results.

Item 4. Submission of Matters to a Vote of Security Holders

None.

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Our common stock is traded on the NASDAQ Global Select Market under the symbol CDNS. We have never declared or paid any cash dividends on our common stock in the past, and we do not plan to pay cash dividends in the foreseeable future. As of February 7, 2009, we had approximately 1,001 registered stockholders and approximately 24,218 beneficial owners of our common stock.

The following table sets forth the high and low sales prices for Cadence common stock for each fiscal quarter in the two-year period ended January 3, 2009:

	High	Low
<u>2008</u>		
First Quarter	\$ 17.18	\$ 9.89
Second Quarter	11.73	10.02
Third Quarter	10.64	6.74
Fourth Quarter	6.93	2.42
<u>2007</u>		
First Quarter	\$ 21.23	\$ 17.65
Second Quarter	24.90	20.94
Third Quarter	22.99	19.53
Fourth Quarter	22.45	15.96

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The following graph compares the cumulative 5-year total stockholder return on our common stock relative to the cumulative total return of the S&P 500 index, the S&P Information Technology index, the NASDAQ Composite index and the S&P 400 Information Technology index. We plan to replace the S&P 500 index with the S&P 400 Information Technology index as a comparative index going forward because we believe that a comparison of our performance against the S&P 400 Information Technology index is a more appropriate performance measure for Cadence, as this index is focused on mid-cap technology companies. We will retain the NASDAQ Composite index going forward rather than the S&P 500 index as a broadly market focused index because Cadence is listed on the NASDAQ Global Select Market.

The graph below assumes that the value of the investment in our common stock and in each index (including reinvestment of dividends) was \$100 on January 3, 2004 and tracks it through January 3, 2009.

COMPARISON OF 5 YEAR CUMULATIVE TOTAL RETURN*

Among Cadence Design Systems, Inc., The S&P 500 Index,
The NASDAQ Composite Index, The S&P Information Technology Index
And S&P 400 Information Technology Index

* \$100 invested on 1/3/04 in stock & 12/31/03 in index-including reinvestment of dividends.

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	1/3/04	1/1/05	12/31/05	12/30/06	12/29/07	1/3/09
Cadence Design Systems, Inc.	100.00	75.63	92.66	98.08	93.26	21.03
S&P 500	100.00	110.88	116.33	134.70	142.10	89.53
NASDAQ Composite	100.00	110.08	112.88	126.51	138.13	80.47
S&P Information Technology	100.00	102.56	103.57	112.29	130.61	74.26
S&P 400 Information Technology	100.00	104.44	105.81	122.57	125.94	75.85

The stock price performance included in this graph is not necessarily indicative of future stock price performance

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In February 2008, our Board of Directors authorized a program to repurchase shares of our common stock in the open market with a value of up to \$500.0 million in the aggregate. In August 2008, our Board of Directors authorized a new program to repurchase shares of our common stock in the open market with a value of up to an additional \$500.0 million in the aggregate. The following table sets forth the repurchases we made during the three months ended January 3, 2009:

Period	Total Number of Shares Purchased *	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Dollar Value of Shares that May Yet Be Purchased Under Publicly Announced Plans or Programs * (In millions)
September 28, 2008				
November 1, 2008	111,572	\$ 3.54	----	\$ 854.4
November 2, 2008				
November 29, 2008	22,543	\$ 3.75	----	\$ 854.4
November 30, 2008				
January 3, 2009	236,722	\$ 3.99	----	\$ 854.4
Total	370,837	\$ 3.84	----	

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

Table of Contents**Item 6. Selected Financial Data Unaudited**

The following selected consolidated financial data should be read in conjunction with our Consolidated Financial Statements and the Notes thereto and the information contained in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations. Historical results are not necessarily indicative of future results. The notes below the table are provided for comparability purposes due to adoptions of recently issued accounting pronouncements on a prospective basis from the date of adoption.

	2008	Five fiscal years ended January 3, 2009			2004
		2007	2006	2005	
		(In millions, except per share amounts)			
Revenue	\$ 1,038.6	\$ 1,615.0	\$ 1,483.9	\$ 1,329.2	\$ 1,197.5
Income (loss) from operations					
+*	(1,573.3)	317.9	224.6	118.8	104.1
Other income (expense), net	(16.8)	58.5	70.4	15.1	(11.5)
Net income (loss) + * u	(1,854.0)	296.3	142.6	49.3	74.5
Net income (loss) per share assuming dilution + *u	(7.29)	1.01	0.46	0.16	0.25
Total assets +u	1,678.7	3,871.2	3,442.8	3,401.3	2,989.8
Convertible notes	500.2	730.4	730.4	420.0	420.0
Other long-term debt	----	----	----	128.0	----
Stockholders' equity +u	102.0	2,080.1	1,699.3	1,844.7	1,700.0

+ During the quarter ended January 3, 2009, we recorded a \$1,317.2 million impairment of goodwill, a \$47.1 million impairment of intangible and tangible assets and a \$332.9 million valuation allowance against our deferred tax assets. For additional description of the goodwill impairment, see the discussion under the heading Results of Operations Impairment of Goodwill under Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, below. For additional description of the impairment of intangible and tangible assets, see the discussion under the heading Results of Operations Impairment of Intangible and Tangible Assets under Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, below. For additional description of the valuation allowance, see the discussion under the heading Results of Operations Provision for Income Taxes under Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, below.

* We adopted SFAS No. 123R, Share-Based Payment, on January 1, 2006 using the modified prospective transition method. Using the modified prospective transition method, we began recognizing compensation expense for equity-based awards granted on or after January 1, 2006 and unvested awards granted prior to January 1, 2006.

u We adopted the provisions of FIN No. 48 on December 31, 2006, which was the first day of fiscal 2007. FIN No. 48 prescribes the recognition threshold and measurement attribute for financial statement recognition and measurement of an income tax position taken or expected to be taken in a tax return. The cumulative effect of applying the provisions of FIN No. 48 have been reported as an adjustment to our opening balance of retained earnings or other appropriate components of equity or net assets in our Consolidated Balance Sheet as of the beginning of fiscal 2007.

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

The following discussion should be read in conjunction with the Consolidated Financial Statements and Notes thereto included elsewhere in this Annual Report on Form 10-K. Certain of such statements, including, but not limited to, statements regarding the extent and timing of future revenues and expenses and customer demand, statements regarding the deployment of our products, statements regarding our reliance on third parties and other statements using words such as anticipates, believes, could, estimates, expects, intends, may, plans, should, will and would, and words of similar import and the negatives thereof, constitute forward-

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looking statements. These statements are predictions based upon our current expectations about future events. Actual results could vary materially as a result of certain factors, including but not limited to, those expressed in these statements. We refer you to the Competition, Proprietary Technology, Risk Factors, Results of Operations, Quantitative and Qualitative Disclosures About Market Risk and Liquidity and Capital Resources sections contained in this Annual Report on Form 10-K and the risks discussed in our other SEC filings, which identify important risks and uncertainties that could cause actual results to differ materially from those contained in the forward-looking statements.

We urge you to consider these factors carefully in evaluating the forward-looking statements contained in this Annual Report on Form 10-K. All subsequent written or spoken forward-looking statements attributable to our company or persons acting on our behalf are expressly qualified in their entirety by these cautionary statements. The forward-looking statements included in this Annual Report on Form 10-K are made only as of the date of this Annual Report on Form 10-K. We do not intend, and undertake no obligation, to update these forward-looking statements.

Overview

Business Overview

We develop electronic design automation, or EDA, software and hardware. We license software, sell or lease hardware technology, provide maintenance for our software and hardware and provide engineering and education services throughout the world to help manage and accelerate product development processes for electronics. Our broad range of products and services are used by the world's leading electronics companies to design and develop complex integrated circuits, or ICs, and electronics systems.

We primarily generate revenue from licensing our EDA software, selling or leasing our hardware technology, providing maintenance for our software and hardware and providing engineering services. In the past, our revenue recognition has been significantly affected by the mix of license types executed in any given period. Our revenue may also be deferred until payments become due and payable or cash is received from certain customers and for certain contracts. For additional description of our revenue recognition, see the discussion under the heading Critical Accounting Estimates Revenue Recognition, below. Substantially all of our revenue is generated from IC manufacturers and designers and electronics systems companies and is dependent upon their commencement of new design projects. As a result, our revenue is significantly influenced by our customers' business outlook and investment in the introduction of new products and the improvement of existing products.

The IC, electronics systems and semiconductor industries are currently experiencing significant challenges, primarily due to a deteriorating macroeconomic environment, which is characterized by diminished product demand, production overcapacity, high inventory levels and accelerated erosion of average selling prices. As a result of this downturn, some of our customers faced financial challenges in fiscal 2008 and may continue to face such challenges in fiscal 2009. It is unclear when the macroeconomic environment may improve. We are seeing increasing pressures on our customers' research and development budgets, and therefore our customers are looking for more flexibility in the type of software and hardware products they purchase and how and when they purchase them. The current economic downturn in our customers' industries has contributed to the substantial reduction in our revenue and could continue to harm our business, operating results and financial condition.

Facing uncertainty and cost pressures in their own businesses, some of our customers are waiting to purchase our products and are increasingly seeking purchasing terms and conditions that are less favorable to us. As a result of this trend, we experienced lower business levels for fiscal 2008 and we have forecasted lower business levels for fiscal 2009. We recognized a net loss for fiscal 2008 and we expect to recognize a net loss for fiscal 2009. To enable us to keep our focus on the value of our technology and to assist with customer demands, we are transitioning to a license

mix that will provide our customers with greater flexibility and will result in a higher portion of our revenue being recognized ratably.

Our customers may also experience adverse changes in their business and, as a result, may delay or default on their payment obligations, file for bankruptcy or modify or cancel plans to license our products. If our customers are not successful in generating sufficient revenue or are precluded from securing financing, they may not be able to

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pay, or may delay payment of, accounts receivable that are owed to us, although these obligations are generally not cancelable. Additionally, our customers may seek to renegotiate existing contractual commitments. Though we have not yet experienced a material level of defaults, any material payment default by our customers or significant reductions in existing contractual commitments could have a material adverse effect on our financial condition and operating results.

Due to the decline in our stock price and market capitalization, our fiscal 2008 net loss, expected future net losses, reduced future cash flow estimates and slower growth rates in our industry, we recorded impairment charges totaling \$1,317.2 million in fiscal 2008, representing all of our acquired goodwill, and we recorded an additional valuation allowance on our deferred tax assets of \$332.9 million.

We plan operating expense levels primarily based on forecasted revenue levels. To offset some of the impact of our expected decrease in revenue, we have implemented cost savings initiatives, including reducing headcount, decreasing employee bonuses and reducing other discretionary spending. During fiscal 2008, we initiated a restructuring plan to improve our operating results and to align our cost structure with expected revenue. This restructuring plan is intended to decrease costs by reducing our workforce throughout the company by at least 625 positions. We expect ongoing annual savings of approximately \$150.0 million related to this restructuring plan.

Product performance and size specifications of the mobile and other consumer electronics market are requiring electronic systems to be smaller, consume less power and provide multiple functions in one system-on-chip, or SoC, or system-in-package, or SiP. The design challenge is also becoming more complex with each new generation of electronics because providers of EDA solutions are required to deliver products that address these technical challenges and improve the efficiency and productivity of the design process in a price-conscious environment.

With the addition of emerging nanometer design considerations to the already burgeoning set of traditional design tasks, complex SoC or IC design can no longer be accomplished using a collection of discrete design tools. What previously consisted of sequential design activities must be merged and accomplished nearly simultaneously without time-consuming data translation steps. We combine our design technologies into platforms addressing four major design activities: functional verification, digital IC design, custom IC design and system interconnect design. The four Cadence design platforms are Incisive functional verification, Encounter digital IC design, Virtuoso custom design and Allegro system interconnect design platforms. In addition, we augment these platform product offerings with a set of DFM products that service both the digital and custom IC design flows. These four platforms, together with our DFM products, comprised our primary product lines during fiscal 2008. In connection with our cost savings initiatives that were implemented during the fourth quarter of fiscal 2008, we made certain changes to our DFM product strategy, including focusing on integrating DFM awareness into our core design platforms of Encounter and Virtuoso. The changes in our DFM strategy resulted in an impairment charge of \$42.5 million arising from the abandonment and reduction to net realizable value of certain identifiable intangible assets.

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

Management

On October 15, 2008, we announced the resignation of Michael J. Fister, our President and Chief Executive Officer and member of our Board of Directors, and four other executive officers, and in connection with Mr. Fister's resignation, our Board of Directors formed an Interim Office of the Chief Executive, or the IOCE, to oversee the day-to-day running of our operations. On January 8, 2009, we announced the appointment of Lip-Bu Tan as our new President and Chief Executive Officer and the dissolution of the IOCE.

Critical Accounting Estimates

In preparing our Consolidated Financial Statements, we make assumptions, judgments and estimates that can have a significant impact on our revenue, operating income and net income, as well as on the value of certain assets and liabilities on our Consolidated Balance Sheets. We base our assumptions, judgments and estimates on historical

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experience and various other factors that we believe to be reasonable under the circumstances. Actual results could differ materially from these estimates under different assumptions or conditions. At least quarterly, we evaluate our assumptions, judgments and estimates and make changes accordingly. We believe that the assumptions, judgments and estimates involved in the accounting for revenue recognition, accounting for income taxes and valuation of goodwill and other long-lived assets have the greatest potential impact on our Consolidated Financial Statements; therefore, we consider these to be our critical accounting estimates.

Historically, our assumptions, judgments and estimates relative to our critical accounting estimates have not differed materially from actual results. For further information on our significant accounting policies, see Note 2 to our Consolidated Financial Statements.

Revenue Recognition

We apply the provisions of Statement of Position, or SOP, 97-2, Software Revenue Recognition, as amended by SOP 98-9, Modification of SOP 97-2, Software Revenue Recognition, With Respect to Certain Transactions, to all software licensing transactions and to all product revenue transactions where the software is not incidental. We also apply the provisions of SFAS No. 13, Accounting for Leases, to all hardware lease transactions. We recognize revenue when persuasive evidence of an arrangement exists, the product has been delivered, the fee is fixed or determinable, collection of the resulting receivable is probable, and vendor-specific objective evidence of fair value, or VSOE, exists.

We license software using three different license types:

Subscription licenses;
Term licenses; and
Perpetual licenses.

For many of our term and subscription license arrangements, we use our proprietary internet-based delivery mechanism, eDA-on-tap, to facilitate the delivery of our software products. To maximize the efficiency of this delivery mechanism, we created what we refer to as eDA Cards, of which there are two types. Subscription license customers may purchase what we refer to as an eDA Platinum Card, which provides the customer access to and use of all software products delivered at the outset of the arrangement and the ability to use additional unspecified software products that may become commercially available during the term of the arrangement. Term license customers may purchase what we refer to as an eDA Gold Card, which provides the customer access to and use of all software products delivered at the outset of the arrangement. Overall, the eDA Cards provide greater flexibility for our customers in how and when they deploy and use our software products.

Subscription licenses Our subscription license arrangements offer our customers the right to:

Access and use all software products delivered at the outset of an arrangement throughout the entire term of the arrangement, generally two to four years, with no rights to return;
Use unspecified additional software products that become commercially available during the term of the arrangement; and
Remix among the software products delivered at the outset of the arrangement, as well as the right to remix into other unspecified additional software products that may become available during the term of the arrangement, so long as the cumulative value of all products in use does not exceed the total license fee determined at the outset of the arrangement. These remix rights may be exercisable multiple times during the term of the arrangement. The right to remix all software products delivered pursuant to the license agreement is not considered an exchange or return of software because all software products have been

delivered and the customer has the continuing right to use them.

Customers that purchase an eDA Platinum Card have the ability during the term of the arrangement to use software products delivered at the outset of the arrangement, and to use other unspecified additional software products that may become commercially available during the term of the arrangement, until the fees have been depleted.

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In general, revenue associated with subscription licenses is recognized ratably over the term of the license commencing upon the later of the effective date of the arrangement or delivery of the software product. Subscription license revenue is allocated to product and maintenance revenue. The allocation to maintenance revenue is based on vendor specific objective evidence, or VSOE, of fair value of the undelivered maintenance that was established in connection with the sale of our term licenses.

In the event that a subscription license arrangement is terminated by mutual agreement and a new term license arrangement is entered into either concurrently with or after the termination of the subscription license arrangement, the revenue associated with the new term license arrangement is recognized upon the later of the effective date of the arrangement or delivery of the software product, assuming all other criteria in SOP 97-2 have been met.

Term licenses Our term license arrangements offer our customers the right to:

Access and use all software products delivered at the outset of an arrangement throughout the entire term of the arrangement, generally two to four years, with no rights to return; and
Remix among the software products delivered at the outset of the arrangement, so long as the cumulative value of all products in use does not exceed the total license fee determined at the outset of the arrangement. These remix rights may be exercisable multiple times during the term of the arrangement. The right to remix all software products delivered pursuant to the license agreement is not considered an exchange or return of software because all software products have been delivered and the customer has the continuing right to use them.

Customers that purchase an eDA Gold Card have the ability during the term of the arrangement to use software products delivered at the outset of the arrangement until the fees relating to the arrangement have been depleted.

In general, revenue associated with term licenses is recognized upon the later of the effective date of the arrangement or delivery of the software product.

Perpetual licenses Our perpetual licenses consist of software licensed on a perpetual basis with no right to return or exchange the licensed software. In general, revenue associated with perpetual licenses is recognized upon the later of the effective date of the license or delivery of the licensed product.

Persuasive evidence of an arrangement Generally, we use a contract signed by the customer as evidence of an arrangement for subscription and term licenses and hardware leases. If a contract signed by the customer does not exist, we have historically used a purchase order as evidence of an arrangement for perpetual licenses, hardware sales, maintenance renewals and small fixed-price service projects, such as training classes and small methodology service engagements of approximately \$10,000 or less. For all other service engagements, we use a signed professional services agreement and a statement of work to evidence an arrangement. In cases where both a signed contract and a purchase order exist, we consider the signed contract to be the most persuasive evidence of the arrangement. Sales through our distributors are evidenced by a master agreement governing the relationship, together with binding purchase orders from the distributor on a transaction-by-transaction basis.

Product delivery Software and the corresponding access keys are generally delivered to customers electronically. Electronic delivery occurs when we provide the customer access to the software. Occasionally, we will deliver the software on a compact disc with standard transfer terms of free-on-board, or F.O.B., shipping point. Our software license agreements generally do not contain conditions for acceptance. With respect to hardware, delivery of an entire system is deemed to occur upon its successful installation. For certain hardware products, installation is the responsibility of the customer, as the system is fully functional at the time of shipment. For these products, delivery is deemed to be complete when the products are shipped with freight terms of F.O.B. shipping point.

For customers who purchase eDA Gold or eDA Platinum Cards, delivery occurs when the customer has been provided with access codes that allow the customer to download the software pursuant to the terms of the software license agreement.

Fee is fixed or determinable We assess whether a fee is fixed or determinable at the outset of the arrangement, primarily based on the payment terms associated with the transaction. We have established a history of collecting

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under the original contract without providing concessions on payments, products or services. For our installment contracts that do not include a substantial up front payment, we only consider that a fee is fixed or determinable if the arrangement has payment periods that are equal to or less than the term of the licenses and the payments are collected in equal or nearly equal installments, when evaluated over the entire term of the arrangement. We have a history of collecting receivables under installment contracts of up to five years.

Significant judgment is involved in assessing whether a fee is fixed or determinable. We must also make these judgments when assessing whether a contract amendment to a term arrangement (primarily in the context of a license extension or renewal) constitutes a concession. Our experience has been that we are able to determine whether a fee is fixed or determinable for term licenses. While we do not expect that experience to change, if we no longer were to have a history of collecting under the original contract without providing concessions on term licenses, revenue from term licenses would be required to be recognized when payments under the installment contract become due and payable. Such a change could have a material impact on our results of operations.

Collection is probable We assess the probability of collecting from each customer at the outset of the arrangement based on a number of factors, including the customer's payment history and its current creditworthiness. We have concluded that collection is not probable for license arrangements executed with customers in certain countries. If in our judgment collection of a fee is not probable, we defer the revenue until the uncertainty is removed, which generally means revenue is recognized upon receipt of cash payment. Our experience has been that we are able to estimate whether collection is probable. While we do not expect that experience to change, if we were to determine that collection is not probable for any license arrangement, particularly those with installment payment terms, revenue from such license would be recognized generally upon the receipt of cash payment. Such a change could have a material impact on our results of operations.

Multiple element arrangement A multiple element arrangement, or MEA, is any arrangement that includes or contemplates rights to a combination of software or hardware products, software license types, services, training or maintenance in a single arrangement. From time to time, we may include individual deliverables in separately priced and separately signed contracts with the same customer. We obtain and evaluate all known relevant facts and circumstances in determining whether the separate contracts should be accounted for individually as distinct arrangements or whether the separate contracts are, in substance, a MEA. Significant judgment can be involved in determining whether a group of contracts might be so closely related that they are, in effect, part of a single arrangement.

Vendor-specific objective evidence of fair value Our VSOE for certain product elements of an arrangement is based upon the pricing in comparable transactions when the element is sold separately. VSOE for maintenance is generally based upon the customer's stated annual renewal rates. VSOE for services is generally based on the price charged when the services are sold separately. For multiple element arrangements, VSOE must exist to allocate the total fee among all delivered and undelivered elements of a term or perpetual license arrangement. If VSOE does not exist for all elements to support the allocation of the total fee among all delivered and undelivered elements of the arrangement, revenue is deferred until such evidence does exist for the undelivered elements, or until all elements are delivered, whichever is earlier. If VSOE of all undelivered elements exists but VSOE does not exist for one or more delivered elements, revenue is recognized using the residual method. Under the residual method, the VSOE of the undelivered elements is deferred, and the remaining portion of the arrangement fee is recognized as revenue as the elements are delivered. Our experience has been that we are able to determine VSOE for maintenance and time-based services, but not for product.

Finance fee revenue Finance fees result from discounting to present value the product revenue derived from our installment contracts in which the payment terms extend beyond one year from the effective date of the contract. Finance fees are recognized using a method that approximates the effective interest method over the relevant license

term and are classified as product revenue. Finance fee revenue represented approximately 3% of total revenue for fiscal 2008 and 2% for each of fiscal 2007 and fiscal 2006. Upon the sale of an installment contract, we recognize the remaining finance fee revenue associated with the installment contract.

Services revenue Services revenue consists primarily of revenue received for performing engineering services. These services are not related to the functionality of the products licensed. Revenue from service contracts is recognized either on the time and materials method, as work is performed, or on the percentage-of-

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completion method. For contracts with fixed or not-to-exceed fees, we estimate on a monthly basis the percentage-of-completion, which is based on the completion of milestones relating to the arrangement. We have a history of accurately estimating project status and the costs necessary to complete projects. A number of internal and external factors can affect our estimates, including labor rates, utilization and efficiency variances and specification and testing requirement changes. If different conditions were to prevail such that accurate estimates could not be made, then the use of the completed contract method would be required and the recognition of all revenue and costs would be deferred until the project was completed. Such a change could have a material impact on our results of operations.

Accounting for Income Taxes

We provide for the effect of income taxes in our Consolidated Financial Statements in accordance with SFAS No. 109 and FIN No. 48.

Under SFAS No. 109, income tax expense or benefit is recognized for the amount of taxes payable or refundable for the current year, and for deferred tax assets and liabilities for the tax consequences of events that have been recognized in an entity's financial statements or tax returns. We must make significant assumptions, judgments and estimates to determine our current provision for income taxes, our deferred tax assets and liabilities and any valuation allowance to be recorded against our deferred tax assets. Our judgments, assumptions and estimates relating to the current provision for income taxes include the geographic mix and amount of income (loss), our interpretation of current tax laws, and possible outcomes of current and future audits conducted by foreign and domestic tax authorities. Our judgments also include anticipating the tax positions we will take on tax returns before actually preparing and filing the tax returns. Changes in our business, tax laws or our interpretation of tax laws, and developments in current and future tax audits, could significantly impact the amounts provided for income taxes in our results of operations, financial position or cash flows.

Deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to tax benefit carryforwards and to differences between the financial statement amounts of assets and liabilities and their respective tax basis. We regularly review our deferred tax assets for recoverability and establish a valuation allowance if it is more likely than not that some portion or all of the deferred tax assets will not be realized. To make this assessment, we take into account predictions of the amount and category of taxable income from various sources and all available positive and negative evidence about these possible sources of taxable income. As required under SFAS No. 109, the weight given to the potential effect of negative and positive evidence is commensurate with the extent to which the strength of the evidence can be objectively verified. For example, a company's current or previous losses are given more weight than its future outlook. For the year ended January 3, 2009, we concluded that a significant increase in valuation allowance was required based on our evaluation and weighting of the positive and negative evidence. If, in the future, we determine that these deferred tax assets are more likely than not to be realized, a release of all or part, of the related valuation allowance could result in a material income tax benefit in the period such determination is made. For additional description of the fiscal 2008 valuation allowance, see the discussion under the heading "Results of Operations - Provision for Income Taxes," below.

Under FIN No. 48, we may only recognize an income tax position in our financial statements that we judge is more likely than not to be sustained solely on its technical merits in a tax audit, including resolution of any related appeals or litigation processes. To make this judgment, we must interpret the application of complex and sometimes ambiguous tax laws, regulations and practices. If an income tax position meets the more likely than not recognition threshold, then we must measure the amount of the tax benefit to be recognized by determining the largest amount of tax benefit that has a greater than a 50% likelihood of being realized upon effective settlement with a taxing authority that has full knowledge of all of the relevant facts. It is inherently difficult and subjective to estimate such amounts, as this requires us to determine the probability of various possible settlement outcomes. To determine if a tax position is

effectively settled, we must also estimate the likelihood that a taxing authority would review a tax position after a tax examination had otherwise been completed. We must also determine when it is reasonably possible that the amount of unrecognized tax benefits will significantly increase or decrease in the 12 months after each fiscal year-end. These judgments are difficult because a taxing authority may change its behavior as a result of our disclosures in our financial statements that are based on the requirements of FIN No. 48. We must re-evaluate our income tax positions on a quarterly basis to consider factors such as changes in facts or circumstances, changes

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in tax law, effectively settled issues under audit, and new audit activity. Such a change in recognition or measurement would result in recognition of a tax benefit or an additional charge to the tax provision.

We are also required to assess whether the earnings of our foreign subsidiaries will be indefinitely reinvested outside the United States. Given the escalating challenges in the global capital markets during fiscal 2008, we decided to repatriate \$250.0 million of earnings from a foreign subsidiary to the United States that had previously been considered to be indefinitely reinvested outside the United States and for which deferred taxes had not been previously provided. We currently expect that an additional \$67.2 million of previously untaxed earnings from foreign subsidiaries will not be indefinitely reinvested outside of the United States. As a result, we have accrued a tax expense of \$101.1 million during fiscal 2008 to provide for the potential federal, state and foreign income taxes on these repatriations. To calculate this tax expense, we were required to estimate the geographic mix of profits and losses earned by us and our subsidiaries in tax jurisdictions with a broad range of income and dividend withholding tax rates, the impact of foreign exchange rate fluctuations, and the potential outcomes of current and future tax audits. Changes in our actual or projected operating results, tax laws or our interpretation of tax laws, foreign exchange rates and developments in current and future tax audits could significantly impact the amounts provided for income taxes in our results of operations, financial position or cash flows.

Valuation of Goodwill and Other Long-lived Assets

Goodwill

Costs in excess of the fair value of tangible and other intangible assets acquired and liabilities assumed in a purchase business combination are recorded as goodwill. SFAS No. 142, Goodwill and Other Intangible Assets, requires that companies not amortize goodwill, but instead test for impairment at least annually. We have evaluated goodwill on an annual basis since our adoption of SFAS No. 142 and whenever events and changes in circumstances suggest that the carrying amount may not be recoverable.

Impairment of goodwill is tested at the reporting unit level by comparing the reporting unit's carrying amount, including goodwill, to the fair value of the reporting unit. The fair values of the reporting units are estimated using a combination of the income, or discounted cash flows, approach and the market approach, which utilizes comparable companies' data. If the carrying amount of the reporting unit exceeds its fair value, goodwill is considered to be impaired and a second step is performed to measure the amount of the impairment loss.

The preparation of the goodwill impairment analysis requires management to make significant estimates and assumptions with respect to the determination of fair values of reporting units and tangible and intangible assets. These estimates and assumptions, which include future values, are complex and often subjective and may differ significantly from period to period based on changes in the overall economic environment, changes in our industry and changes in our strategy or our internal forecasts. Estimates and assumptions with respect to the determination of the fair value of our reporting unit include:

- Control premium assigned to our market capitalization;
- Our operating forecasts;
- Revenue growth rates;
- Risk-commensurate discount rates and costs of capital; and
- Market multiples of revenue and earnings.

These estimates and assumptions, along with others, are used to estimate the fair value of our reporting unit as well as tangible and intangible assets. While we believe the estimates and assumptions we used are reasonable, different assumptions may materially impact the resulting fair value of the reporting unit, tangible assets and intangible assets,

the amount of impairment we record in any given period and our results of operations.

We engage independent valuation experts to assess the reasonableness of our assumptions and to perform certain portions of our goodwill impairment analysis.

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Other Long-lived Assets

We review long-lived assets, including certain identifiable intangibles, for impairment whenever events or changes in circumstances indicate that we will not be able to recover an asset's carrying amount in accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. In addition, we assess our long-lived assets for impairment if they are abandoned.

For long-lived assets to be held and used, including acquired intangibles, we initiate our review whenever events or changes in circumstances indicate that the carrying amount of a long-lived asset may not be recoverable. Recoverability of an asset is measured by comparing its carrying amount to the expected future undiscounted cash flows expected to result from the use and eventual disposition of that asset, excluding future interest costs that would be recognized as an expense when incurred. Any impairment to be recognized is measured by the amount by which the carrying amount of the asset exceeds its fair market value. Significant management judgment is required in:

- Identifying a triggering event that arises from a change in circumstances;
- Forecasting future operating results; and
- Estimating the proceeds from the disposition of long-lived or intangible assets.

In future periods, material impairment charges could be necessary should different conditions prevail or different judgments be made.

Results of Operations

As noted above, we saw increasing pressures on the research and development budgets in our customer base due to the deceleration of growth in the electronics systems and semiconductor industries and the deteriorating macroeconomic environment. In addition, the escalating challenges in the global capital markets made it important to keep cash available and held in short-term, low-risk investments.

Fiscal 2008 financial results reflected the following:

- Lower business levels due to the challenges in the current macroeconomic environment and the timing of our contract renewals with existing customers;
- Lower business levels and up-front revenue recognized due to our transition to a ratable license mix, which began in the third quarter of fiscal 2008;
- Initiation of a restructuring plan, resulting in \$46.4 million of expense during fiscal 2008;
- Impairment of all of our \$1,317.2 million of goodwill and \$47.1 million of intangible and tangible assets;
- Repatriation of earnings that had previously been considered to be indefinitely reinvested outside the United States and for which deferred taxes had not been previously provided, resulting in additional provisions for income taxes of \$101.1 million;
- Additional valuation allowance of \$332.9 million against our deferred tax assets; and
- Resignations of five executive officers resulting in severance expense of \$16.4 million, \$7.1 million of which was stock-based compensation.

Revenue

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

The right to access new technology;
The duration of the license; and
Payment timing.

Customer decisions regarding these aspects of license transactions determine the license type, timing of revenue recognition and potential future business activity. For example, if a customer chooses a fixed duration of use, this will result in either a subscription or term license. A business implication of this decision is that, at the expiration of the license period, the customer must decide whether to continue using the technology and therefore

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renew the license agreement. Because larger customers generally use products from two or more of our five product groups, rarely will a large customer completely terminate its relationship with us at expiration of the license. See the discussion under the heading **Critical Accounting Estimates Revenue Recognition** above for additional description of license types and timing of revenue recognition.

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

- Competitiveness of our new technology;
- Timing of contract renewals with existing customers;
- Length of our sales cycle; and
- Size, duration, terms and type of:
 - Contract renewals with existing customers;
 - Additional sales to existing customers; and
 - Sales to new customers.

A substantial portion of our total revenue is recognized over multiple periods. In the past, a significant portion of our product revenue has been recognized upon delivery of licensed software, which generally occurs upon the later of the effective date of the arrangement or delivery of the software product. We are moving to a license mix that will result in increased ratable revenue and we expect the percentage of product revenue from backlog to increase in future years.

The value and duration of contracts, and consequently product revenue recognized, is affected by the competitiveness of our products. Product revenue recognized in any period is also affected by the extent to which customers purchase subscription, term or perpetual licenses, and the extent to which contracts contain flexible payment terms. The timing of revenue recognition is also affected by changes in the extent to which existing contracts contain flexible payment terms and by changes in contractual arrangements with existing customers (e.g., customers transitioning from subscription license arrangements to term license arrangements).

Revenue Mix

We analyze our software and hardware businesses by product group, combining revenues for both product and maintenance because of their interrelationship. During fiscal 2008, fiscal 2007 and fiscal 2006, our product groups were as follows:

Functional Verification: Products in this group, which include the Incisive functional verification platform, are used to verify that the high level, logical representation of an IC design is functionally correct.

Digital IC Design: Products in this group, which include the Encounter digital IC design platform, are used to accurately convert the high-level, logical representation of a digital IC into a detailed physical blueprint and then detailed design information showing how the IC will be physically implemented. This data is used for creation of the photomasks used in chip manufacture.

Custom IC Design: Our custom design products, which include the Virtuoso custom design platform, are used for ICs that must be designed at the transistor level, including analog, radio frequency, memories, high performance digital blocks and standard cell libraries. Detailed design information showing how an IC will be physically implemented is used for creation of the photomasks used in chip manufacture.

System Interconnect Design: This product group consists of our PCB and IC package design products, including the Allegro and OrCAD products. The Allegro system interconnect design platform enables consistent co-design of interconnects across ICs, IC packages and PCBs, while the OrCAD line focuses on cost-effective, entry-level PCB solutions.

Design for Manufacturing: Included in this product group are our physical verification and analysis products. These products are used to analyze and verify that the physical blueprint of the IC has been constructed correctly and can be manufactured successfully. In connection with our cost savings initiatives that were implemented during the fourth quarter of fiscal 2008, we made certain changes to our DFM product

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strategy, including focusing on integrating DFM awareness into our core design platforms of Encounter and Virtuoso. The changes in our DFM strategy resulted in an impairment charge of \$42.5 million arising from the abandonment and reduction to net realizable value of certain identifiable intangible assets.

For additional description of our current product strategy, see the discussion under the heading *Products and Product Strategy* under Item 1, *Business*, above.

Revenue by Year

The following table shows our revenue for fiscal 2008, fiscal 2007 and fiscal 2006 and the dollar change in revenue between years:

	2008	2007	2006	Change 2008 vs. 2007	2007 vs. 2006
			(In millions)		
Product	\$ 516.6	\$ 1,104.0	\$ 982.7	\$ (587.4)	\$ 121.3
Services	133.5	125.8	134.9	7.7	(9.1)
Maintenance	388.5	385.2	366.3	3.3	18.9
Total revenue	\$ 1,038.6	\$ 1,615.0	\$ 1,483.9	\$ (576.4)	\$ 131.1

Product revenue decreased during fiscal 2008, as compared to fiscal 2007, primarily because of lower business levels due to the challenges in the current macroeconomic environment, the timing of our contract renewals with existing customers, our transition to a ratable license mix and a longer sales cycle. As a result, product revenue decreased for all product groups, and particularly for Digital IC Design, Custom IC Design and Functional Verification products during fiscal 2008. Due to the lower business levels and the change in the license mix in the second half of fiscal 2008, we expect to recognize decreased revenue during fiscal 2009, as compared to fiscal 2008.

Product revenue was higher during fiscal 2007, as compared to fiscal 2006, primarily because of increased revenue from licenses for Digital IC Design, Functional Verification and Custom IC Design products, partially offset by a small decrease in revenue from licenses for DFM products.

Revenue by Product Group

The following table shows the percentage of product and related maintenance revenue contributed by each of our five product groups and Services and other during fiscal 2008, fiscal 2007 and fiscal 2006:

	2008	2007	2006
Functional Verification	22%	24%	24%
Digital IC Design	24%	27%	24%
Custom IC Design	24%	27%	27%
System Interconnect Design	11%	8%	9%
Design for Manufacturing	6%	6%	7%

Services and other	13%	8%	9%
Total	100%	100%	100%

As described under the heading **Critical Accounting Estimates** above, certain of our licenses allow customers the ability to remix among software products. Additionally, we have licensed a combination of our products to customers with the actual product selection and number of licensed users to be determined at a later date. For these arrangements, we estimate the allocation of the revenue to product groups based upon the expected usage of our products by these customers. The actual usage of our products by these customers may differ and, if that proves to be the case, the revenue allocation in the above table would differ.

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Although we believe the methodology of allocating revenue to product groups is reasonable, there can be no assurance that such allocated amounts reflect the amounts that would result had the customer individually licensed each specific software solution at the onset of the arrangement.

Revenue by Geography

	2008	2007	2006	2008 vs. 2007	Change 2007 vs. 2006
	(In millions)				
United States	\$ 435.1	\$ 741.9	\$ 765.1	\$ (306.8)	\$ (23.2)
Other Americas	33.0	34.8	31.3	(1.8)	3.5
Europe, Middle East and Africa	230.8	296.9	284.4	(66.1)	12.5
Japan	204.1	342.6	247.9	(138.5)	94.7
Asia	135.6	198.8	155.2	(63.2)	43.6
Total revenue	\$ 1,038.6	\$ 1,615.0	\$ 1,483.9	\$ (576.4)	\$ 131.1

Revenue by Geography as a Percentage of Total Revenue

	2008	2007	2006
United States	42%	46%	52%
Other Americas	3%	2%	2%
Europe, Middle East and Africa	22%	19%	19%
Japan	20%	21%	17%
Asia	13%	12%	10%

The rate of revenue change varies geographically primarily due to differences in the timing and size of term licenses in those regions. No single customer accounted for 10% or more of total revenue during fiscal 2008, fiscal 2007 or fiscal 2006.

Changes in foreign currency exchange rates caused our revenue to increase by \$24.5 million during fiscal 2008 compared to fiscal 2007, primarily due to a decrease in the valuation of the United States dollar when compared to the Japanese yen and the European Union euro, partially offset by an increase in the valuation of the United States dollar when compared to the British pound. Changes in foreign currency exchange rates caused our revenue to increase by \$2.9 million in 2007 compared to 2006, primarily due to a decrease in the valuation of the United States dollar when compared to the European Union euro and the British pound, partially offset by an increase in the valuation of the United States dollar when compared to the Japanese yen. Additional information about revenue and other financial information by geography can be found in Note 21 to our Consolidated Financial Statements.

Table of Contents**Stock-based Compensation Expense Summary**

Stock-based compensation expense is reflected throughout our costs and expenses during fiscal 2008, fiscal 2007 and fiscal 2006 as follows:

	2008	2007 (In millions)	2006
Cost of product	\$ 0.2	\$ 0.2	\$ 0.2
Cost of services	4.3	3.9	4.0
Cost of maintenance	2.8	2.5	2.5
Marketing and sales	17.4	22.2	23.9
Research and development	36.7	46.3	50.9
General and administrative	19.9	26.3	22.5
Total	\$ 81.3	\$ 101.4	\$ 104.0

Stock-based compensation expense decreased \$20.1 million during fiscal 2008, as compared to fiscal 2007, and \$2.6 million during fiscal 2007, as compared to fiscal 2006, due to the following:

	2008 vs. 2007	Change 2007 vs. 2006 (In millions)
Restricted stock and stock bonuses	\$ (16.2)	\$ 6.0
Stock options	(7.2)	(10.5)
Employee stock purchase plan	3.3	1.9
	\$ (20.1)	\$ (2.6)

Stock-based compensation expense related to restricted stock awards and restricted stock units, collectively referred to as restricted stock, and stock bonuses decreased during fiscal 2008, as compared to fiscal 2007, primarily due to the reversal of \$6.5 million of stock-based compensation expense related to the modification of certain performance-based restricted stock awards, new grants of restricted stock being valued at a lower stock price and a decrease in stock bonuses. Stock-based compensation expense related to restricted stock and stock bonuses increased during fiscal 2007, as compared to fiscal 2006, as we issued more restricted stock in place of stock options and due to our increased stock price during fiscal 2007.

Stock-based compensation expense related to stock options decreased in each of fiscal 2008, as compared to fiscal 2007, and fiscal 2007, as compared to fiscal 2006, primarily due to our increased use of restricted stock instead of stock options, partially offset by an increase in stock option expense during fiscal 2008 due to the acceleration of vesting for the five executive officers that resigned during fiscal 2008.

We expect stock-based compensation expense to continue to decrease during fiscal 2009, primarily due to lower fair values at grant dates for both restricted stock and stock options, and due to the cancellation of restricted stock and stock options due to our restructuring plan and other attrition.

Expected Effects of Restructuring Plans

We plan operating expense levels primarily based on forecasted revenue levels. To offset some of the impact of our expected decrease in revenue, we have implemented cost savings initiatives, including reducing headcount, decreasing employee bonuses and reducing other discretionary spending. During fiscal 2008, we initiated a restructuring plan to improve our operating results and to align our cost structure with expected revenue. This restructuring plan is intended to decrease costs by reducing our workforce throughout the company by at least 625 positions. We expect ongoing annual savings of approximately \$150.0 million related to this restructuring plan.

Table of Contents**Cost of Revenue**

	2008	2007	2006	2008 vs. 2007	Change 2007 vs. 2006
	(In millions)				
Product	\$ 50.3	\$ 60.1	\$ 66.8	\$ (9.8)	\$ (6.7)
Services	103.3	93.4	96.5	9.9	(3.1)
Maintenance	55.8	61.1	63.8	(5.3)	(2.7)

The following table shows cost of revenue as a percentage of related revenue for fiscal 2008, fiscal 2007 and fiscal 2006:

	2008	2007	2006
Product	10%	5%	7%
Services	77%	74%	72%
Maintenance	14%	16%	17%

Cost of Product

Cost of product includes costs associated with the sale or lease of our hardware and licensing of our software products. Cost of product primarily includes the cost of employee salary, benefits and other employee-related costs, including stock-based compensation expense, amortization of acquired intangibles directly related to our products, the cost of technical documentation and royalties payable to third-party vendors. Cost of product associated with our hardware products also includes materials, assembly and overhead. These additional manufacturing costs make our cost of hardware product higher, as a percentage of revenue, than our cost of software product. Cost of product as a percentage of product revenue increased during fiscal 2008, as compared to fiscal 2007, primarily due to decreased software product revenue during fiscal 2008.

A summary of Cost of product during fiscal 2008, fiscal 2007 and fiscal 2006 is as follows:

	2008	2007	2006
	(In millions)		
Product related costs	\$ 33.0	\$ 37.8	\$ 33.6
Amortization of acquired intangibles	17.3	22.3	33.2
Total Cost of product	\$ 50.3	\$ 60.1	\$ 66.8

Cost of product decreased \$9.8 million during fiscal 2008, as compared to fiscal 2007, and \$6.7 million during fiscal 2007, as compared to fiscal 2006, due to the following:

	Change	
	2008 vs. 2007	2007 vs. 2006
	(In millions)	
Hardware costs	\$ (5.8)	\$ 5.0
Amortization of acquired intangibles	(5.1)	(10.9)
Other individually insignificant items	1.1	(0.8)
	\$ (9.8)	\$ (6.7)

Hardware costs decreased during fiscal 2008, as compared to fiscal 2007, primarily due to a decrease in hardware sales, partially offset by a write-off of obsolete inventory during fiscal 2008. Hardware costs increased during fiscal 2007, as compared to fiscal 2006, primarily due to an increase in hardware sales.

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Amortization of acquired intangibles decreased in each of fiscal 2008, as compared to fiscal 2007, and during fiscal 2007, as compared to fiscal 2006, because certain acquired intangible assets became fully amortized during the related periods. We expect the amortization of acquired intangibles component of Cost of product to decrease during fiscal 2009 due to the impairment of certain acquired intangibles during fiscal 2008.

Cost of product depends primarily upon the extent to which we acquire intangible assets, acquire licenses and incorporate third-party technology in our products that are licensed or sold in any given period, and the actual mix of hardware and software product sales in any given period.

Cost of Services

Cost of services primarily includes employee salary, benefits and other employee-related costs, costs to maintain the infrastructure necessary to manage a services organization and provisions for contract losses, if any. Cost of services increased \$9.9 million during fiscal 2008, as compared to fiscal 2007, and decreased \$3.1 million during fiscal 2007, as compared to fiscal 2006, due to the following:

	Change	
	2008 vs. 2007	2007 vs. 2006
	(In millions)	
Salary, benefits and other employee-related costs	\$ 3.3	\$ 2.4
Computer equipment lease costs and maintenance costs associated with third-party software	2.2	(1.4)
Facilities and other infrastructure costs	1.9	----
Portion of the gain on the sale of land and building that relates to Cost of services expense	1.1	(1.3)
Professional services costs	0.3	(1.2)
Other individually insignificant items	1.1	(1.6)
	\$ 9.9	\$ (3.1)

Cost of Maintenance

Cost of maintenance includes the cost of customer services, such as hot-line and on-site support, employee salary, benefits and other employee-related costs, and documentation of maintenance updates. Cost of maintenance decreased \$5.3 million during fiscal 2008, as compared to fiscal 2007, and decreased \$2.7 million during fiscal 2007, as compared to fiscal 2006, due to the following:

	Change	
	2008 vs. 2007	2007 vs. 2006
	(In millions)	
Salary, benefit and other employee-related costs	\$ (4.6)	\$ (0.9)
Other individually insignificant items	(0.7)	(1.8)
	\$ (5.3)	\$ (2.7)

Operating Expenses