
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K

(Mark One)

☒ **Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the fiscal year ended March 31, 2005

☐ **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: 0-21184

MICROCHIP TECHNOLOGY INCORPORATED

(Exact Name of Registrant as Specified in Its Charter)

Delaware
(State of Incorporation)

86-0629024
(IRS Employer Identification No.)

2355 W. Chandler Blvd., Chandler, AZ 85224
(Address of Principal Executive Offices, Including Zip Code)

(480) 792-7200
(Registrant's Telephone Number, Including Area Code)

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

Securities registered pursuant to Section 12(g) of the Act:
Common Stock, \$.001 Par Value Per Share
Preferred Share Purchase Rights

Indicate by checkmark 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 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 Form 10-K or any amendment to this Form 10-K. ☒

Indicate by checkmark whether the Registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2): **Yes** ☒ **No** ☐

The approximate aggregate market value of the voting stock of the Registrant beneficially owned by stockholders, other than directors, officers and affiliates of the Registrant, at **September 30, 2004** was **\$5,431,093,405**.

Number of shares of Common Stock, \$.001 par value, outstanding as of **May 16, 2005**: **208,490,094**.

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Proxy Statement for the 2005 Annual Meeting of Stockholders

Part of Form 10-K
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MICROCHIP TECHNOLOGY INCORPORATED AND SUBSIDIARIES

FORM 10-K

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PART I

This Form 10-K contains certain forward-looking statements that involve risks and uncertainties, including statements regarding our strategy and future financial performance. We use words such as "anticipate," "believe," "plan," "expect," "estimate," "future," "intend" and similar expressions to identify forward-looking statements. Our actual results could differ materially from the results described in these forward-looking statements as a result of certain factors including those set forth under "Item 1 – Business – Additional Factors That May Affect Results of Operations," beginning below at page 12, "Item 7 - Management's Discussion and Analysis of Financial Condition and Results of Operations," beginning below at page 22, and elsewhere in this Form 10-K. Although we believe that the matters reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. You should not place undue reliance on these forward-looking statements. We disclaim any obligation to update information contained in any forward-looking statement.

Item 1. BUSINESS

We develop and manufacture specialized semiconductor products used by our customers for a wide variety of embedded control applications. Our product portfolio comprises our PICmicro[®] field-reprogrammable (Flash) RISC microcontrollers which serve 8-bit and 16-bit embedded control applications, and a broad spectrum of high-performance linear and mixed-signal, power management and thermal management devices. We also offer complementary microperipheral products including interface devices, Serial EEPROMs, and application-specific standard products (ASSPs). Our synergistic product portfolio targets thousands of applications and a growing demand for high-performance designs in the automotive, communications, computing, consumer and industrial control markets. Our quality systems are ISO/TS16949 (2002 version) certified.

Microchip Technology Incorporated was incorporated in Delaware in 1989. In this Form 10-K, "we," "us," and "our" each refers to Microchip Technology Incorporated and its subsidiaries. Our executive offices are located at 2355 West Chandler Boulevard, Chandler, Arizona 85224-6199 and our telephone number is (480) 792-7200.

Our Internet address is www.microchip.com. We post the following filings on our Web site as soon as reasonably practicable after they are electronically filed with or furnished to the Securities and Exchange Commission:

- Our annual report on Form 10-K
- Our quarterly reports on Form 10-Q
- Our current reports on Form 8-K, and
- Any amendments to the above-listed reports filed or furnished pursuant to Sections 13(a) or 15(d) of the Securities Exchange Act of 1934.

All SEC filings on our Web site are available free of charge. The information on our Web site is **not** incorporated into this Form 10-K.

Industry Background

Competitive pressures require manufacturers of a wide variety of products to expand product functionality and provide differentiation while maintaining or reducing cost. To address these requirements, manufacturers often use integrated circuit-based embedded control systems that enable them to:

- differentiate their products
- replace less efficient electromechanical control devices
- reduce the number of components in their system
- add product functionality
- decrease time to market for their products, and
- significantly reduce product cost.

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Embedded control systems have been incorporated into thousands of products and subassemblies in a wide variety of applications and markets worldwide, including:

- automotive comfort, safety and entertainment applications

- remote control devices
- handheld tools
- home appliances
- portable computers
- robotics
- cordless and cellular telephone accessories
- motor controls
- security systems
- educational and entertainment devices, and
- consumer electronics.

Embedded control systems also facilitate the emergence of new classes of products when applications not previously existing become possible. Embedded control systems typically incorporate a microcontroller as the principal active, and sometimes sole, component. A microcontroller is a self-contained computer-on-a-chip consisting of a central processing unit, non-volatile program memory, random access memory for data storage and various input/output peripheral capabilities. In addition to the microcontroller, a complete embedded control system incorporates application-specific software and may include specialized peripheral device controllers, non-volatile memory components such as EEPROMs, and various analog and interface products.

The increasing demand for embedded control has made the market for microcontrollers one of the largest segments of the semiconductor market. Microcontrollers are currently available in 4-bit through 32-bit architectures. Although 4-bit microcontrollers are relatively inexpensive, they generally lack the minimum functionality required in most applications and are typically used in relatively simple applications. While traditional 16-bit and 32-bit microcontrollers provide very high performance and functionality, they are generally too expensive for many high-volume embedded control applications. As a result, many manufacturers of competitive, high-volume products have found 8-bit microcontrollers to be the most cost-effective embedded control solution.

Most microcontrollers shipped today are ROM-based and must be programmed by the semiconductor supplier during manufacturing, resulting in 8-12-week lead times, based on market conditions, for delivery of such microcontrollers. In addition to delayed product introduction, these long lead times can result in potential inventory obsolescence and temporary factory shutdowns when changes in the firmware are required. To address these issues, some suppliers offer programmable microcontrollers that can be configured by the customer in the customer's manufacturing line, thus significantly reducing lead-time and inventory risks when the inevitable firmware changes occur. While these microcontrollers were initially expensive relative to ROM-based microcontrollers, manufacturing technology has evolved over the last several years to the point where reprogrammable microcontrollers are now available for little to no premium over ROM-based microcontrollers, thus providing significant value to microcontroller customers. As a result, reprogrammable microcontrollers are the fastest growing segment of the microcontroller market.

Our Products

Our strategic focus is on embedded control solutions, including:

- microcontrollers
- digital signal controllers
- high-performance linear and mixed-signal devices
- power management and thermal management devices
- patented KEELOQ[®] security ASSPs
- smart battery management ASSPs, and
- Serial EEPROMs

We provide highly cost-effective embedded control solutions that also offer the advantages of small size, high performance, low voltage/power operation and ease of development, enabling timely and cost-effective embedded control product integration by our customers.

Microcontrollers

We offer a broad family of microcontroller products featuring a unique, proprietary architecture marketed under the PIC[®] brand name. We believe that our PIC product family is a price/performance leader in the worldwide microcontroller market. We have shipped over 3 billion PIC microcontrollers to customers worldwide since their introduction in 1990. Our PIC products are designed for applications requiring field-programmability, high performance, low power and cost effectiveness. They feature a variety of memory technology configurations, low voltage and power, small footprint and ease of use. Our performance results from an exclusive product architecture which features dual data and instruction pathways, referred to as a Harvard dual-bus architecture; a Reduced Instruction Set Computer, referred to as RISC; and variable length instructions; all of which provide significant speed advantages over alternative single-bus, Complex Instruction Set Computer architectures, referred to as CISC. With over 260 microcontrollers in our product portfolio, we target the entire performance range of 8-bit microcontrollers. Additionally, our scalable product architecture allows us to successfully target both the entry-level of the 16-bit microcontroller market, as well as the 4-bit microcontroller marketplace, significantly enlarging our addressable market.

We have used our manufacturing experience and design and process technology to bring additional enhancements and manufacturing efficiencies to the development and production of our PIC[®] family of microcontroller products. Our extensive experience base has enabled us to develop our advanced, low cost user programmability feature by incorporating non-volatile memory, such as Flash, EEPROM and EPROM Memory, into the microcontroller, and to be a leader in reprogrammable microcontroller product offerings.

Digital Signal Controllers

We recently began production shipments of our Digital Signal Controller product line. Our family of dsPIC[®] Digital Signal Controllers, currently 19 products, integrates control features of high-performance 16-bit microcontrollers with the processing capabilities of Digital Signal Processors (DSPs). During the last three fiscal years, all of our Digital Signal Controller product development has been focused on reprogrammable (Flash) products. These controllers integrate a wide variety of peripheral functions making them suitable for a large number of embedded control applications.

Our dsPIC product family offers a broad suite of hardware and software development tools, software application libraries, development boards and reference designs to ease and expedite the customer application development cycle. With its field-re-programmability, large selection of peripheral functions, small footprint and ease of use, we believe that our dsPIC controllers will significantly enlarge our addressable market.

We offer a comprehensive set of low-cost and easy-to-learn application development tools. These tools enable system designers to quickly and easily program a PIC microcontroller and dsPIC Digital Signal Controllers for specific applications and are a key factor for obtaining design wins.

Our family of development tools operates in the standard Windows® environment on standard PC hardware. These tools range from entry-level systems, which include an assembler and programmer or in-circuit debugging hardware, to fully configured systems that provide in-circuit emulation hardware. Customers moving from entry-level designs to those requiring real-time emulation are able to preserve their investment in learning and tools as they migrate to future PIC devices since all of our systems share the same integrated development environment.

Many independent companies also develop and market application development tools and systems that support our standard microcontroller product architecture. Currently, there are more than 150 third-party tool suppliers worldwide whose products support our proprietary microcontroller architecture.

We believe that familiarity with and adoption of our, and third-party, development systems by an increasing number of product designers will be an important factor in the future selection of our embedded control products. These development tools allow design engineers to develop thousands of application-specific products from our standard microcontrollers. To date, we have shipped more than 358,000 development systems.

ASSPs

Our application-specific standard products, referred to as ASSPs, are specialized products designed to perform specific end-user applications, compared to our other products that are more general purpose in nature. Our ASSP device families currently include, among others, our KEELOQ® family of secure data transmission products and smart battery management products.

Analog and Interface Products

Our analog and interface products now consist of several families with over 420 power management, linear, mixed-signal, thermal management and interface products. At the end of fiscal 2005, our mixed-signal analog and interface products were being shipped to more than 9,500 end customers.

We continue marketing and selling our analog and interface products into our existing microcontroller customer base, which we refer to as our analog “attach” strategy, as well as to new customers. In addition to our “attach” strategy, we market and sell other products that may not fit our traditional PIC microcontroller and memory products customer base. We market these, and all of our products, based on an application segment approach, targeted to solve different problems in development of our customers’ products.

Memory Products

Our memory products consist primarily of serial electrically erasable programmable read only memory, referred to as EEPROMs. We sell these devices primarily into the embedded control market, and we are one of the largest suppliers of such devices worldwide. EEPROM products are used for non-volatile program and data storage in systems where such data must be either modified frequently or retained for long periods. Serial EEPROMs have a very low I/O pin requirement, permitting production of very small devices.

We address customer requirements by offering products with extremely small package sizes and very low operating voltages for both read and write functions. Our memory products also feature long data retention and high erase/write endurance.

Manufacturing

Our manufacturing operations include wafer fabrication and assembly and test. The ownership of our manufacturing resources is an important component of our business strategy, enabling us to maintain a high level of manufacturing control resulting in us being one of the lowest cost producers in the embedded control industry. By owning our wafer fabrication facilities and much of our assembly and test operations, and by employing proprietary statistical process control techniques, we have been able to achieve and maintain high production yields. Direct control over manufacturing resources allows us to shorten our design and production cycles. This control also allows us to capture the wafer manufacturing and a portion of the assembly and testing profit margin.

Our manufacturing facilities are located in:

- Tempe, Arizona (Fab 2)
- Chandler, Arizona (probe operations)
- Puyallup, Washington (Fab 3) (non-operational)
- Gresham, Oregon (Fab 4), and
- Bangkok, Thailand (assembly and test).

Wafer Fabrication

Fab 2 currently produces 8-inch wafers and supports manufacturing processes between 0.35 and 5.0 microns. During fiscal 2005, Fab 2 operated at approximately 96% of its capacity compared to approximately 91% during fiscal 2004. Operating at higher percentages of capacity has a positive impact on our operating results due to the relatively high fixed costs inherent in wafer fabrication manufacturing.

On June 30, 2003, we completed closure of our Chandler, Arizona (Fab 1) wafer fabrication facility and integrated certain Fab 1 personnel and processes into our Tempe, Arizona (Fab 2) wafer fabrication facility. The facility where Fab 1 is located is an integral part of our overall campus in Chandler, Arizona. Within this same facility resides our wafer probe, mask making and other manufacturing related activities. We have no specific plans for utilizing the space formerly housing the wafer fabrication operations, and intend to leave it in an idle status.

Fab 3 is currently non-operational and being held for future use. See “Item 7 - Management’s Discussion and Analysis of Financial Condition and Results of Operations – Special Charges – Fab 3 Impairment Charge,” below at page 33, for a discussion of the status of Fab 3.

Fab 4 was acquired by us in August 2002 and began production on October 31, 2003. Fab 4 produces 8-inch wafers using 0.5 micron manufacturing processes and is capable of supporting technologies below 0.18 microns. Fab 4 has reached a level of production where costs and efficiencies have met our initial expectations. Fab 4 costs on comparable technologies are in fact lower than those of Fab 2. We have a significant amount of clean room capacity and equipment still to be placed in service at Fab 4 that was acquired in the original acquisition of Fab 4 that we can bring on line in the future to support incremental wafer fabrication capacity needs. We believe the combined capacity of Fab 2, Fab 4 and Fab 3 will provide sufficient capacity to allow us to respond to increases in future demand.

We continue to transition products to more advanced process technologies to reduce future manufacturing costs. We believe that our ability to successfully transition to more advanced process technologies is important for us to remain competitive. Our future operating results could be adversely affected if any such transition is substantially delayed or inefficiently implemented.

We also contract with third-party wafer foundries to fabricate less than 3% of our total production. On a strategic basis, we will continue to use third-party foundries to shorten our product design cycle on certain key technologies and products.

Assembly and Test

We perform product assembly and testing at our facilities located near Bangkok, Thailand. At March 31, 2005, approximately 70% of our assembly requirements were being performed in our Thailand facility. As of March 31, 2005, our Thailand facility was testing substantially all of our wafer production. A 67,000 square foot expansion area that was placed in service in fiscal 2005 provides the Thailand facility with sufficient space for our projected expansion needs in fiscal 2006. We also use third-party assembly and test contractors in several Asian countries for the balance of our assembly and test requirements.

General Matters Impacting Our Manufacturing Operations

We employ proprietary design and manufacturing processes in developing our microcontroller and memory products. We believe our processes afford us both cost-effective designs in existing and derivative products and greater functionality in new product designs. While many of our competitors develop and optimize separate processes for their logic and memory product lines, we use a common process technology for both microcontroller and non-volatile memory products. This allows us to more fully absorb our process research and development costs and to deliver new products to market more rapidly. Our engineers utilize advanced Computer Aided Design tools and software to perform circuit design, simulation and layout, and our in-house photomask and wafer fabrication facilities enable us to rapidly verify design techniques by processing test wafers quickly and efficiently.

Due to the high fixed costs inherent in semiconductor manufacturing, consistently high manufacturing yields have significant positive effects on our gross profit and overall operating results. During fiscal 2005, our focus on manufacturing productivity allowed us to maintain excellent manufacturing yields at our facilities. Our manufacturing yields are primarily driven by a comprehensive implementation of statistical process control, extensive employee training and selective upgrading of our manufacturing facilities and equipment. Maintenance of manufacturing productivity and yields are important factors in the achievement of our operating results. The manufacture and assembly of integrated circuits, particularly non-volatile, erasable CMOS memory and logic devices, such as those that we produce, are complex processes. These processes are sensitive to a wide variety of factors, including the level of contaminants in the manufacturing environment, impurities in the materials used and the performance of our wafer fabrication personnel and equipment. As is typical in the semiconductor industry, we have from time to time experienced lower than anticipated manufacturing yields. Our operating results will suffer if we are unable to maintain yields at approximately the current levels.

Our semiconductor manufacturing operations require raw materials and equipment that must meet exacting standards. We generally have more than one source for these supplies, but there are only a limited number of suppliers capable of delivering various raw materials and equipment that meet our standards. In addition, the raw materials and equipment necessary for our business could become more difficult to obtain as worldwide use of semiconductors in product applications increases. We have experienced supply shortages from time to time in the past, and on occasion our suppliers have told us they need more time than expected to fill our orders. An interruption of any raw materials or equipment sources could harm our business.

Our reliance on third parties for a portion of wafer fabrication and assembly and testing involves some reduction in our level of control over the portions of our business that we subcontract. While we review the quality, delivery and cost performance of these third-party contractors, our future operating results could suffer if any third-party contractor is unable to maintain manufacturing yields, assembly and test yields and costs at approximately their current levels.

The foregoing statements related to the combined capacity of Fab 2, Fab 4 and Fab 3 providing sufficient capacity to allow us to respond to future increases in demand and the transition to more advanced process technologies to reduce future manufacturing costs are forward-looking statements. Actual results could differ materially because of the following factors, among others: changes in utilization of our current manufacturing capacity; unanticipated costs in ramping production at Fab 4; our ability to increase production at Fab 2; the ability to attract and retain qualified personnel in the Portland, Oregon area; changes in demand for products and the products of our customers; supply disruption; absorption of fixed costs, labor and other direct manufacturing costs; fluctuations in production yields; production efficiencies and overall capacity utilization; changes in product mix; competitive pressures on prices; labor unrest; political instability and expropriation; and other general economic conditions.

At the end of fiscal 2005, we owned long-lived assets (consisting of property, plant and equipment and goodwill) in the United States amounting to \$622.3 million and \$102.9 million in other countries, including \$100.6 million in Thailand. At the end of fiscal 2004, we owned long-lived assets in the United States amounting to \$608.3 million and \$113.2 million in other countries, including \$111.7 million in Thailand.

Research and Development (R&D)

We are committed to continuing our investment in new and enhanced products, including development systems, and in our design and manufacturing process technologies. We believe these investments are significant factors in maintaining our competitive position. Our current R&D activities focus on the design of new microcontrollers, digital signal controllers, ASSPs, memory and mixed-signal products, new development systems, software and application-specific software libraries. We are also developing new design and process technologies to achieve further cost reductions and performance improvements in existing products.

In fiscal 2005, our R&D expenses were \$93.0 million, compared to \$85.4 million in fiscal 2004 and \$88.0 million in fiscal 2003.

Sales and Distribution

General

We market our products worldwide primarily through a network of direct sales personnel and distributors.

Our direct sales force focuses primarily on major strategic accounts in three geographical markets: the Americas, Europe and Asia. We currently maintain sales and support centers in major metropolitan areas in North America, Europe and Asia. We believe that a strong technical service presence is essential to the continued development of the embedded control market. The majority of our field sales engineers (FSEs), field application engineers (FAEs), and sales management have technical degrees and have been previously employed in an engineering environment. We believe that the technical knowledge of our sales force is a key competitive advantage in the sale of our products. The primary mission of our FAE team is to provide technical assistance to strategic accounts and to conduct periodic training sessions for FSEs and distributor sales teams. FAEs also frequently conduct technical seminars in major cities around the world, and work closely with our distributors to provide technical assistance and end-user support.

Distribution

Our distributors focus primarily on servicing the product and technical support requirements of a broad base of diverse customers. We believe that distributors provide an effective means of reaching this broad and diverse customer base.

In fiscal 2005, we derived 65% of our net sales from sales through distributors and 35% of our net sales from direct sales to original equipment manufacturers, referred to as OEM customers. Distributors accounted for 64% of our net sales in fiscal 2004 and 60% of our net sales in fiscal 2003. Our largest distributor accounted for approximately 13% of our net sales in fiscal 2005 and fiscal 2004. Our second largest distributor accounted for approximately 12% of our net sales in fiscal 2005 and fiscal 2004. In fiscal 2003, one distributor accounted for 12% of our net sales. No other distributor or end customer accounted for more than 10% of our net sales in fiscal 2005, 2004 or 2003.

Distributors generally have broad-based rights to return product to us. As revenue on distributor shipments is not recognized until the distributors sell our product to their end customers, distributor returns have no impact on our revenue.

We also grant certain credits to our third-party distributors and also offer these distributors price protection. The credits are granted to the distributors on specifically identified pieces of the distributors' business to allow them to earn a competitive gross margin on the sale of our products to their end customers. The credits are on a per unit basis and are not given to the distributor until they provide information regarding the sale to their end customer. The effect of granting these credits establishes the net selling price from us to our distributors for the products and results in the net revenue recognized by us when the product is sold by the distributors to their end customers.

We reduce product pricing through price protection based on market conditions, competitive considerations and other factors. Price protection is granted to third-party distributors on the inventory that they have on hand at the date the price protection is offered. When we reduce the selling price of our products, it allows the distributors to claim a credit against their outstanding accounts receivables balances based on the new price of the inventory they have on hand as of the date of the price reduction. There is no revenue recognition impact from the price protection activity.

We do not offer material incentive programs to our third-party distributors.

We do not have long-term agreements with our distributors and we, or our distributors, may terminate our relationships with each other with little or no advanced notice. The loss of, or the disruption in the operations of, one or more of our distributors could reduce our future net sales in a given quarter and could result in an increase in inventory returns.

Sales by Geography

Sales by geography for fiscal 2005, 2004 and 2003 were as follows (dollars in thousands):

	Year Ended March 31,					
	2005	%	2004	%	2003	%
Americas	\$ 248,881	29.4	\$ 219,641	31.4	\$ 219,504	33.7
Europe	232,493	27.4	194,187	27.8	177,727	27.3
Asia	365,562	43.2	285,432	40.8	254,231	39.0
Total Sales	\$ 846,936	100.0%	\$ 699,260	100.0%	\$ 651,462	100.0%

Sales to customers in Asia have increased as a percentage of sales from fiscal 2003 to fiscal 2004 and from fiscal 2004 to fiscal 2005. We attribute this primarily to many of our customers transitioning their manufacturing operations to Asia.

Sales to foreign customers accounted for approximately 73% of our net sales in fiscal 2005 and 71% of our net sales in fiscal 2004 and fiscal 2003. Our sales to foreign customers have been predominately in Asia and Europe, which we attribute to the manufacturing strength in those areas for automotive, communications, computing, consumer and industrial control products. Americas sales include sales to customers in the United States, Canada, Central America and South America.

Sales to customers in China, including Hong Kong, accounted for approximately 16% of our net sales in fiscal 2005, approximately 14% of our net sales in fiscal 2004 and 13% of our net sales in fiscal 2003. In fiscal 2005, sales to customers in Taiwan accounted for approximately 10% of our net sales. We did not have sales into any other foreign countries that exceeded 10% of our net sales during fiscal 2005, 2004 or 2003.

Our international sales are predominately U.S. dollar denominated. Although foreign sales are subject to certain government export restrictions, we have not experienced any material difficulties as a result of export restrictions to date.

Our foreign operations are subject to a number of risks as described under the heading, "*We are highly dependent on foreign sales and operations, which exposes us to foreign political and economic risks,*" on page 16.

Backlog

As of April 29, 2005, our backlog was approximately \$166.9 million, compared to \$209.9 million as of April 23, 2004. Our backlog includes all purchase orders scheduled for delivery within the subsequent 12 months.

We primarily produce standard products that can be shipped from inventory within a short time after we receive an order. Our business and, to a large extent, that of the entire semiconductor industry, is characterized by short-term orders and shipment schedules. Orders constituting our current backlog are subject to changes in delivery schedules, or to cancellation at the customer's option without significant penalty. Thus, while backlog is useful for scheduling production, backlog as of any particular date may not be a reliable measure of sales for any future period.

Competition

The semiconductor industry is intensely competitive and has been characterized by price erosion and rapid technological change. We compete with major domestic and international semiconductor companies, many of which have greater market recognition and greater financial, technical, marketing, distribution and other resources than we have with which to pursue engineering, manufacturing, marketing and distribution of their products. Emerging companies may also increase their participation in the market for embedded control applications. Furthermore, capacity in the semiconductor industry is generally increasing over time and such increased capacity or improved product availability could adversely affect our competitive position.

We currently compete principally on the basis of the technical innovation and performance of our embedded control products, including the following product characteristics:

- speed
- functionality
- density
- power consumption
- reliability
- packaging alternatives
- price, and
- availability.

We believe that other important competitive factors in the embedded control market include:

- ease of use
- functionality of application development systems
- dependable delivery and quality, and
- technical service and support.

We believe that we compete favorably with other companies on all of these factors, but we may be unable to compete successfully in the future, which could harm our business.

Patents, Licenses and Trademarks

We maintain a portfolio of United States and foreign patents, expiring on various dates between 2005 and 2023. We also have numerous additional United States and foreign patent applications pending. We do not expect that the expiration of any particular patent will have a material impact on our business. While we intend to continue to seek patents on our inventions and manufacturing processes, we believe that our continued success depends primarily on the technological skills and innovative capabilities of our personnel and our ability to rapidly commercialize product developments, rather than on our

patents. Our existing patents and any new patents that are issued may not be of sufficient scope or strength to provide meaningful protection or any commercial advantage to us. In addition, the laws of certain foreign countries do not protect our intellectual property rights to the same extent as the laws of the United States.

We have entered into certain intellectual property licenses and cross-licenses with other companies related to semiconductor products and manufacturing processes. As is typical in the semiconductor industry, we and our customers have from time to time received, and may in the future receive, communications from third parties asserting patent or other intellectual property rights on certain of our products or technologies. We investigate all such notices and respond as we believe is appropriate. Based on industry practice, we believe that in most cases we can obtain any necessary licenses or other rights on commercially reasonable terms, but we cannot assure that licenses would be on acceptable terms, that litigation would not ensue or that damages for any past infringement would not be assessed. Litigation, which could result in substantial cost to us and require significant attention from management, may be necessary to enforce our patents or other intellectual property rights, or to defend us against claimed infringement of the rights of others. The failure to obtain necessary licenses or other rights, or litigation arising out of infringement claims, could harm our business.

Environmental Regulation

We must comply with many different federal, state and local governmental regulations related to the use, storage, discharge and disposal of certain chemicals and gases used in our manufacturing processes. Our facilities have been designed to comply with these regulations and we believe that our activities are conducted in compliance with such regulations. Any changes in such regulations or in their enforcement could require us to acquire costly equipment or to incur other significant expenses to comply with environmental regulations. Any failure by us to control adequately the storage, use and disposal of regulated substances could result in future liabilities.

Increasing public attention has been focused on the environmental impact of electronic manufacturing operations. While we have not experienced any materially adverse effects on our operations from environmental regulations, our business and results of operations could suffer if for any reason we fail to control the use of, or to restrict adequately the discharge of, hazardous substances under present or future environmental regulations.

Employees

As of April 30, 2005, we had 3,943 employees. None of our employees are represented by a labor organization. We have never had a work stoppage and believe that our employee relations are good.

Executive Officers

The following sets forth certain information regarding our executive officers as of April 23, 2005:

Name	Age	Position
Steve Sanghi	49	Chairman of the Board, President and Chief Executive Officer

Steven V. Drehobl	43	Vice President, Security, Microcontroller and Technology Division
David S. Lambert	53	Vice President, Fab Operations
Mitchell R. Little	52	Vice President, Worldwide Sales and Applications
Ganesh Moorthy	45	Vice President, Advanced Microcontroller and Memory Division
Gordon W. Parnell	55	Vice President, Chief Financial Officer
Richard J. Simoncic	41	Vice President, Analog and Interface Products Division

Mr. Sanghi has been President since August 1990, CEO since October 1991, and Chairman of the Board since October 1993. He has served as a director since August 1990. Mr. Sanghi holds an M.S. degree in Electrical and Computer Engineering from the University of Massachusetts and a B.S. degree in Electronics and Communication from Punjab University, India.

Mr. Drehobl has served as Vice President of the Security, Microcontroller, and Technology Division since July 2001. He has been employed by Microchip since August 1989 and has served as a Vice President in various roles since February 1997. Mr. Drehobl holds a Bachelor of Technology degree from the University of Dayton.

Mr. Lambert has served as Vice President, Fab Operations since November 1993. From 1991 to November 1993, he served as Director of Manufacturing Engineering, and from 1988 to 1991, he served as Engineering Manager of Fab Operations. Mr. Lambert holds a B.S. degree in Chemical Engineering from the University of Cincinnati.

Mr. Little has served as Vice President, Worldwide Sales and Applications since July 2000. From April 1998 through July 2000, he served as Vice President, Americas Sales. From November 1995 to April 1998, he served as Vice President, Standard Microcontroller and ASSP Division. Joining Microchip in 1989, Mr. Little also held positions with the Memory Products Division including Vice President of that division. Mr. Little holds a BSET degree from United Electronics Institute.

Mr. Moorthy has served as Vice President, Advanced Microcontroller and Memory Division, since December 2003. From November 2001 to December 2003, he served as Vice President, Advanced Microcontroller and Automotive Division. From August 2000 through November 2001, he served as Chairman and CEO of Cybercilium, Inc., a business intelligence solutions provider for mid-market companies. From 1981 through July 2000, Mr. Moorthy worked at Intel Corporation in various operations and management capacities, including his last assignment as Director of Operations for Intel's Home Products Group. Mr. Moorthy holds an MBA in Marketing from National University, a B.S. degree in Electrical Engineering from the University of Washington and a B.S. degree in Physics from the University of Bombay.

Mr. Parnell has served as Vice President and Chief Financial Officer since May 2000. He served as Vice President, Controller and Treasurer from April 1993 to May 2000. Mr. Parnell holds a finance/accounting qualification with the Association of Certified Accountants from Edinburgh College, Scotland.

Mr. Simoncic has served as Vice President, Analog and Interface Products Division since September 1999. From January 1996 to September 1999, he served as Vice President, Memory and Specialty Products Division. Mr. Simoncic holds a B.S. degree in Electrical Engineering Technology from DeVry Institute of Technology.

Additional Factors That May Affect Our Results of Operations

When evaluating Microchip and its business, you should give careful consideration to the factors listed below, in addition to the information provided elsewhere in this Form 10-K and in other documents that we file with the Securities and Exchange Commission.

Our quarterly operating results may fluctuate due to factors that could reduce our net sales and profitability.

Our quarterly operating results are affected by a wide variety of factors that could reduce our net sales and profitability, many of which are beyond our control. Some of the factors that may affect our quarterly operating results include:

- changes in demand or market acceptance of our products and products of our customers
- the mix of inventory we hold and our ability to satisfy orders from our inventory
- levels of inventories at our customers
- changes in utilization of our manufacturing capacity and fluctuations in manufacturing yields
- our ability to secure sufficient assembly and testing capacity
- competitive developments including pricing pressures
- the level of orders that are received and can be shipped in a quarter
- the level of sell-through of our products through distribution
- changes or fluctuations in customer order patterns and seasonality
- constrained availability from other electronic suppliers impacting our customers' ability to ship their products, which in turn may adversely impact our sales to those customers
- costs and outcomes of any tax audits or any litigation involving intellectual property, customers or other issues
- disruptions in our business or our customers' businesses due to terrorist activity, armed conflict, war, worldwide oil prices and supply, public health concerns or disruptions in the transportation system
- property damage or other losses which are not covered by insurance, and
- general economic, industry or political conditions in the United States or internationally.

We believe that period-to-period comparisons of our operating results are not necessarily meaningful and that you should not rely upon any such comparisons as indications of future performance. In future periods our operating results may fall below our public guidance or the expectations of public market analysts and investors, which would likely have a negative effect on the price of our common stock.

Our operating results will suffer if we ineffectively utilize our manufacturing capacity or fail to maintain manufacturing yields.

The manufacture and assembly of integrated circuits, particularly non-volatile, erasable CMOS memory and logic devices such as those that we produce, are complex processes. These processes are sensitive to a wide variety of factors, including the level of contaminants in the manufacturing environment, impurities in the materials used and the performance of our wafer fabrication personnel and equipment. As is typical in the semiconductor industry, we have from time to time experienced lower than anticipated manufacturing yields. Our operating results will suffer if we are unable to maintain yields at approximately the current levels.

Our operating results are also adversely affected when we operate at less than optimal capacity. Lower capacity utilization results in certain costs being charged directly to expense and lower gross margins.

We are dependent on orders that are received and shipped in the same quarter and therefore limited in our visibility of future product shipments.

Our net sales in any given quarter depend upon a combination of shipments from backlog and orders received in that quarter for shipment in that quarter, which we refer to as turns orders. We measure turns orders at the beginning of a quarter based on the orders needed to meet the shipment targets that we set entering the quarter. Historically, we have proven our ability to respond quickly to customer orders as part of our competitive strategy, resulting in customers placing orders with relatively short delivery schedules. Shorter lead times generally mean that turns orders as a percentage of our business are relatively high in any particular quarter and reduces our backlog visibility on future product shipments. Turns orders correlate to overall semiconductor industry conditions and product lead times. Because turns orders are difficult to predict, varying levels of turns orders make our net sales more difficult to forecast. If we do not achieve a sufficient level of turns orders in a particular quarter relative to our revenue targets, our revenue and operating results may suffer.

Intense competition in the markets we serve may lead to pricing pressures, reduced sales of our products or reduced market share.

The semiconductor industry is intensely competitive and has been characterized by price erosion and rapid technological change. We compete with major domestic and international semiconductor companies, many of which have greater market recognition and substantially greater financial, technical, marketing, distribution and other resources than we do with which to pursue engineering, manufacturing, marketing and distribution of their products. Emerging companies are also increasing their participation in the market for embedded control applications. We may be unable to compete successfully in the future, which could harm our business.

Our ability to compete successfully depends on a number of factors both within and outside our control, including:

- the quality, performance, reliability, features, ease of use, pricing and diversity of our products
- our success in designing and manufacturing new products including those implementing new technologies
- the rate at which customers incorporate our products into their own applications
- product introductions by our competitors
- the number, nature and success of our competitors in a given market
- our ability to obtain adequate supplies of raw materials and other supplies at acceptable prices
- our ability to protect our products and processes by effective utilization of intellectual property rights
- the quality of our customer service and our ability to address the needs of our customers, and
- general market and economic conditions.

Historically, average selling prices in the semiconductor industry decrease over the life of any particular product. The overall average selling prices of our microcontroller and proprietary analog and interface products have remained relatively constant, while average selling prices of our Serial EEPROM and non-proprietary analog and interface products have declined over time.

We have experienced, and expect to continue to experience, modest pricing declines in certain of our more mature proprietary product lines, due primarily to competitive conditions. We have been able to moderate average selling price declines in many of our proprietary product lines by continuing to introduce new products with more features and higher prices. We have experienced in the past and expect to continue to experience in the future varying degrees of competitive pricing pressures in our Serial EEPROM products.

We may be unable to maintain average selling prices for our products as a result of increased pricing pressure in the future, which could adversely impact our operating results.

Our business is highly dependent on selling through distributors.

Sales through distributors accounted for 65% of our net sales in fiscal 2005, 64% of our net sales in fiscal 2004 and 60% of our net sales in fiscal 2003. Our two largest distributors together accounted for approximately 25% of our net sales in fiscal 2005 and fiscal 2004 and approximately 21% of our net sales in fiscal 2003. We do not have long-term agreements with our distributors and our distributors may terminate their relationships with us with little or no advanced notice.

The loss of, or a disruption in the operations of, one or more of our distributors could reduce our net sales in a given quarter and could result in an increase in inventory returns.

Our success depends on our ability to introduce new products on a timely basis.

Our future operating results will depend on our ability to develop and introduce new products on a timely basis that can compete effectively on the basis of price and performance and which address customer requirements. The success of our new product introductions depends on various factors, including:

- proper new product selection
- timely completion and introduction of new product designs
- development of support tools and collateral literature that make complex new products easy for engineers to understand and use, and
- market acceptance of our customers' end products.

Because our products are complex, we have experienced delays from time to time in completing development of new products. In addition, our new products may not receive or maintain substantial market acceptance. We may be unable to design, develop and introduce competitive products on a timely basis, which could adversely impact our future operating results.

Our success also depends upon our ability to develop and implement new design and process technologies. Semiconductor design and process technologies are subject to rapid technological change and require significant R&D expenditures. We and other companies in the industry have, from time to time, experienced difficulties in effecting transitions to advanced process technologies and, consequently, have suffered reduced manufacturing yields or delays in product deliveries. Our future operating results could be adversely affected if any transition to future process technologies is substantially delayed or inefficiently implemented.

We must attract and retain qualified personnel to be successful, and competition for qualified personnel is intense in our market.

Our success depends upon the efforts and abilities of our senior management, engineering and other personnel. The competition for qualified engineering and management personnel is intense. We may be unsuccessful in retaining our existing key personnel or in attracting and retaining additional key personnel that we require. The loss of the services of one or more of our key personnel or the inability to add key personnel could harm our business. We have no employment agreements with any member of our senior management team.

We are dependent on several third-party contractors to perform key manufacturing functions for us.

We use several third-party contractors located in Asia for a portion of the assembly and testing of our products. We also rely on outside wafer foundries for a portion of our wafer fabrication. Although we own the majority of our manufacturing resources, the disruption or termination of any of our third-party contractors could harm our business and operating results.

Our use of third parties involves some reduction in our level of control over the portions of our business that we subcontract. Our future operating results could suffer if any third-party contractor were to experience financial, operations or production difficulties or situations when demand exceeds capacity, or if they were unable to maintain manufacturing yields, assembly and test yields and costs at approximately their current levels, or if due to their locations in foreign countries they were to experience political upheaval or infrastructure disruption. In such case, we may not be able to qualify additional manufacturing sources for our products in a timely manner or at all, and such arrangements, if any, may not be on favorable terms to us. In such event, our business and operating results could be adversely affected.

We may lose sales if our suppliers of raw materials and equipment fail to meet our needs.

Our semiconductor manufacturing operations require raw materials and equipment that must meet exacting standards. We generally have more than one source for these supplies, but there are only a limited number of suppliers capable of delivering various raw materials and equipment that meet our standards. The raw materials and equipment necessary for our business could become more difficult to obtain as worldwide use of semiconductors in product applications increases. We have experienced supply shortages from time to time in the past, and on occasion our suppliers have told us they need more time than expected to fill our orders or that they will no longer support certain equipment with updates or spare and replacements parts. An interruption of any raw materials or equipment sources, or the lack of supplier support for a particular piece of equipment, could harm our business.

Our operating results may be impacted by the wide fluctuations of supply and demand in the semiconductor industry.

The semiconductor industry is characterized by wide fluctuations of supply and demand. The industry has experienced significant economic downturns, characterized by diminished product demand and production over-capacity. We have sought to reduce our exposure to this industry cyclicality by selling proprietary products that cannot be easily or quickly replaced, to a geographically diverse base of customers across a broad range of market segments. However, we have experienced substantial period-to-period fluctuations in operating results and expect, in the future, to experience period-to-period fluctuations in operating results due to general industry or economic conditions.

We are exposed to various risks related to legal proceedings or claims.

We are currently, and in the future may be, involved in legal proceedings or claims regarding patent infringement, intellectual property rights, contracts and other matters. From October 2001 to October 2004, we were involved in patent infringement litigation with Philips Corporation which has since been settled. However, as is typical in the semiconductor industry, we receive notifications from customers from time to time who believe that we owe them indemnification or other obligations related to infringement claims made against the customers by third parties. These legal proceedings and claims, whether with or without merit, could result in substantial cost to us and divert our resources. If we are not able to resolve a claim, negotiate a settlement of a matter, obtain necessary licenses on commercially reasonable terms, and/or successfully prosecute or defend our position, we could incur uninsured liability in any one of them and our business, financial condition or results of operations could be harmed.

It is also possible that from time to time we may be subject to warranty or product liability claims that could lead to significant expenses related to the defense of such claims or any requirement to pay damages claims. We do have product liability insurance, but there is no certainty that insurance will cover all claims or be of a sufficient amount to fully protect against such claims. Costs or payments we may make in connection with warranty or product liability claims may adversely affect the results of our operations.

Failure to adequately protect our intellectual property could result in lost revenue or market opportunities.

Our ability to obtain patents, licenses and other intellectual property rights covering our products and manufacturing processes is important for our success. To that end, we have acquired certain patents and patent licenses and intend to continue to seek patents on our inventions and manufacturing processes. The process of seeking patent protection can be long and expensive, and patents may not be issued from currently pending or future applications. In addition, our existing patents and any new patents that are issued may not be of sufficient scope or strength to provide meaningful protection or any commercial advantage to us. We may be subject to or may initiate interference proceedings in the U.S. Patent and Trademark Office, which can require significant financial and management resources. In addition, the laws of certain foreign countries do not protect our intellectual property rights to the same extent as the laws of the United States. Infringement of our intellectual property rights by a third party could result in uncompensated lost market and revenue opportunities for us.

We do not have long-term contracts with our customers.

We do not typically enter into long-term contracts with our customers and we cannot be certain about future order levels from our customers. When we do enter into customer contracts, the contract is generally cancelable at the convenience of the customer. In the event of any early termination of a contract by one of our major customers, it is unlikely that we would be able to rapidly replace that revenue source which could harm our financial results.

Business interruptions could harm our business.

Operations at any of our manufacturing facilities, or at any of our wafer fabrication or test and assembly subcontractors, may be disrupted for reasons beyond our control, including work stoppages, power loss, incidents of terrorism or security risk, political instability, public health issues, telecommunications, transportation or other infrastructure failure, fire, earthquake, floods, or other natural disasters. If operations at any of our facilities, or our subcontractors' facilities are interrupted, we may not be able to shift production to other facilities on a timely basis. If this occurs, we would likely experience delays in shipments of products to our customers and alternate sources for production may be unavailable on acceptable terms. This could result in reduced revenues and profits and the cancellation of orders or loss of customers. In addition, business interruption

insurance will likely not be enough to compensate us for any losses that may occur and any losses or damages incurred by us as a result of business interruptions could significantly harm our business.

We are highly dependent on foreign sales and operations, which exposes us to foreign political and economic risks.

Sales to foreign customers account for a substantial portion of our net sales. During fiscal 2005, approximately 73% of our net sales were made to foreign customers. During fiscal 2004, approximately 71% of our net sales were made to foreign customers. We purchase a substantial portion of our raw materials and equipment from foreign suppliers. In addition, we own product assembly and testing facilities located near Bangkok, Thailand. We also use various foreign third-party contractors for a portion of our assembly and testing and for a portion of our wafer fabrication requirements. Substantially all of our finished goods inventory is maintained in Thailand.

Our reliance on foreign operations, foreign suppliers, maintenance of substantially all of our finished goods in inventory at foreign locations and significant foreign sales exposes us to foreign political and economic risks, including:

- political, social and economic instability
- public health conditions
- trade restrictions and changes in tariffs
- import and export license requirements and restrictions
- difficulties in staffing and managing international operations
- employment regulations
- disruptions in international transport or delivery
- fluctuations in currency exchange rates
- difficulties in collecting receivables
- economic slowdown in the worldwide markets served by us, and
- potentially adverse tax consequences.

If any of these risks materialize, our sales could decrease and our operating results could suffer.

We are subject to stringent environmental regulations, which may force us to incur significant expenses.

We must comply with many different federal, state and local governmental regulations related to the use, storage, discharge and disposal of toxic, volatile or otherwise hazardous chemicals used in our manufacturing process. Although we believe that our activities conform to presently applicable environmental regulations, our failure to comply with present or future regulations could result in the imposition of fines, suspension of production or a cessation of operations. Any such environmental regulations could require us to acquire costly equipment or to incur other significant expenses to comply with such regulations. Any failure by us to control the use of or adequately restrict the discharge of hazardous substances could subject us to future liabilities. Environmental problems may occur that could subject us to future costs or liabilities.

Further, certain of our customers shipping their products into European markets are also subject to governmental environmental regulations such as the Restriction of Hazardous Substances in Electrical and Electronic Equipment Directive (RoHS) which will be effective July 1, 2006, and the Directive on Waste Electrical and Electronic Equipment. These directives focus on limiting the amounts of certain elements, such as lead, in electrical devices, and providing for the proper disposal of the electrical devices and their components. The inability of this sub-set of our customers to use Microchip products which contain lead after July 2006 may adversely affect our results of operations.

Recently enacted and proposed changes in securities laws and related regulations have resulted in increased costs to us.

Recently enacted and proposed changes in the laws and regulations affecting public companies, including the provisions of the Sarbanes-Oxley Act of 2002 and recent rules enacted and proposed by the SEC, NASDAQ and the NYSE, have resulted in significantly increased costs to us as we respond to their requirements. In particular, complying with the internal control audit requirements of Sarbanes-Oxley Section 404 has resulted in increased internal efforts and significantly higher fees from our independent accounting firm.

This report on Form 10-K contains a report by our management on our internal control over financial reporting including an assessment of the effectiveness of our internal control over financial reporting as of March 31, 2005. This Form 10-K also contains an attestation and report by our auditors with respect to our management's assessment of the effectiveness of internal control over financial reporting under Section 404. While these assessments and reports did not reveal any material weaknesses in our internal control over financial reporting, compliance with Section 404 is an ongoing process and will be required for each future fiscal year. We expect that the ongoing compliance with Section 404 will continue to be both very costly and very challenging and there can be no assurance that material weaknesses with not be identified in future periods. Any adverse results from such ongoing compliance efforts could result in a loss of investor confidence in our financial reports and have an adverse effect on our stock price.

Recent regulations related to equity compensation could adversely affect our earnings and our ability to attract and retain key personnel.

Since our inception, we have used stock options and other long-term equity incentives as a fundamental component of our employee compensation packages and have accounted for them using the intrinsic value method of APB No. 25, "Accounting for Stock Issued to Employees." We believe that stock options and other long-term equity incentives directly motivate our employees to maximize long-term stockholder value and, through the use of vesting, encourage employees to remain with Microchip. In December 2004, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 123 (revised 2004), "Share-Based Payments," (SFAS 123R) which changed U.S. Generally Accepted Accounting Principles in such a way to require us to record a charge to earnings for the fair value of employee stock option grants and other share based compensation beginning in the first quarter of fiscal 2007. This regulation will negatively impact our earnings for those share based awards that vest beginning in fiscal 2007. For example, recording a charge for employee stock options under SFAS 123 would have decreased our net income by \$37.2 million, \$36.8 million and \$36.2 million for fiscal 2005, 2004 and 2003, respectively. The impact on net income of SFAS 123R may differ significantly than the impact as calculated under SFAS 123. Furthermore, adoption of SFAS 123R will require us to make certain assumptions and judgments in the valuation of stock options that we may grant in the future. A change in any of those assumptions or judgments could change the compensation expense that is charged against our earnings and, consequently, adversely affect our results of operations. See also Note 1 to the Consolidated Financial Statements – Significant Accounting Policies: Share-Based Payment.

In addition, recent regulations implemented by The NASDAQ Stock Market requiring shareholder approval for all stock option plans as well as recent regulations implemented by the New York Stock Exchange prohibiting NYSE member organizations from giving a proxy to vote on equity-compensation plans unless the beneficial owner of the shares has given voting instructions could make it more difficult for us to grant equity-based awards to employees in the future. To the extent that these or other new regulations make it more difficult or expensive to grant options to employees, we may incur compensation costs, productivity losses, change our equity compensation strategy or find it difficult to attract, retain and motivate employees, each of which could materially and adversely affect our business.

The future trading price of our common stock could be subject to wide fluctuations in response to a variety of factors.

The market price of our common stock has fluctuated significantly in the past and is likely to fluctuate in the future. The future trading price of our common stock could be subject to wide fluctuations in response to a variety of factors, many of which are beyond our control, including:

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- quarterly variations in our operating results and the operating results of other technology companies
- actual or anticipated announcements of technical innovations or new products by us or our competitors
- changes in analysts' estimates of our financial performance or buy/sell recommendations
- changes in our financial guidance or our failure to meet such guidance
- general conditions in the semiconductor industry, and
- worldwide economic and financial conditions.

In addition, the stock market has experienced significant price and volume fluctuations that have particularly affected the market prices for many high technology companies and that often have been unrelated to the operating performance of such companies. These broad market fluctuations and other factors may harm the market price of our common stock.

Item 2. PROPERTIES

At March 31, 2005, we owned the facilities described below:

Location	Approx. Total Sq. Ft.	Uses
Chandler, Arizona (1)	415,000	Executive and Administrative Offices; Wafer Probe; R&D Center; Sales and Marketing; and Computer and Service Functions
Tempe, Arizona	379,000	Wafer Fabrication (Fab 2); R&D Center; Administrative Offices; and Warehousing
Puyallup, Washington (2)	700,000	Wafer Fabrication (Fab 3); R&D Center; Administrative Offices; and Warehousing (non-operational; held-for-future-use)
Gresham, Oregon (3)	826,500	Wafer Fabrication (Fab 4); R&D Center; Administrative Offices; and Warehousing
Chacherngsao, Thailand (4)	290,000	Test and Assembly; Sample Center; Warehousing; and Administrative Offices

- (1) On June 30, 2003, we closed Fab 1 on our Chandler campus, and integrated certain of the personnel and processes from Fab 1 into Fab 2.
- (2) Currently non-operational and being held-for-future-use. Fab 3 consists of manufacturing buildings and land, with no equipment.
- (3) Acquired in August 2002. Production commenced on October 31, 2003.
- (4) Located in the Alphatechnopolis Industrial Park near Bangkok on land to which we expect to acquire title in accordance with our agreement with the landowner. Progress towards obtaining full title of the land has been delayed due to a complex financial restructuring situation relating to the seller of the land. At this time it is not possible to estimate when, or if, full title transfer will be completed. We have provided reserves that we estimate will be adequate to obtain full title. Such reserves are set at the estimated fair value of the land.

In addition to the facilities we own, we lease several research and development facilities and sales offices in North America, Europe and Asia. Our aggregate monthly rental payment for our leased facilities is approximately \$0.4 million.

We currently believe that our existing facilities will be adequate to meet our production requirements for the next 12 months.

The foregoing statements related to the acquisition of title to the land on which the Thailand facility is situated and the adequacy of existing facilities for the next 12 months are forward-looking statements. Actual results could differ materially because of the following factors, among others: developments in the financial restructuring of the seller of the land where the Thailand facility is situated; demand for our products; fluctuations in production yields, production efficiencies and overall capacity utilization; competitive pressures on prices; political instability and expropriation; and other economic conditions. See also the factors set forth under "Item 1 – Business – Additional Factors That May Affect Results of Operations," beginning at page 12 of this report.

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Item 3. LEGAL PROCEEDINGS

In the ordinary course of our business, we are involved in a limited number of legal actions, both as plaintiff and defendant, and could incur uninsured liability in any one or more of them. Although the outcome of these actions is not presently determinable, we believe that the ultimate resolution of these matters will not harm our business and will not have a material adverse effect on our financial position, cash flows or results of operations. Litigation relating to the semiconductor industry is not uncommon, and we are, and from time to time have been, subject to such litigation. No assurances can be given with respect to the extent or outcome of any such litigation in the future.

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

Not applicable.

PART II

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

Our common stock is traded on the The NASDAQ National Market[®] under the symbol “MCHP.” Our common stock has been quoted on The NASDAQ National Market since our initial public offering on March 19, 1993. The following table sets forth the quarterly high and low closing prices of our common stock as reported by The NASDAQ National Market for the last two years.

<u>Fiscal 2005</u>	<u>High</u>	<u>Low</u>	<u>Fiscal 2004</u>	<u>High</u>	<u>Low</u>
First Quarter	\$ 32.63	\$ 26.80	First Quarter	\$ 24.86	\$ 18.15
Second Quarter	30.61	25.26	Second Quarter	28.19	23.66
Third Quarter	30.63	26.03	Third Quarter	36.03	24.56
Fourth Quarter	28.49	24.28	Fourth Quarter	34.67	25.29

On May 16, 2005, there were approximately 505 holders of record of our common stock. This figure does not reflect beneficial ownership of shares held in nominee names.

We have been declaring and paying quarterly cash dividends since the third quarter of fiscal 2003. Our total cash dividends paid were \$43.0 million, \$23.3 million and \$8.1 million in fiscal 2005, fiscal 2004 and fiscal 2003, respectively. The following table sets forth our quarterly cash dividends per common share and the total amount of the dividend payment each quarter in fiscal 2005 and fiscal 2004 (amounts in thousands, except per share amounts).

<u>Fiscal 2005</u>	<u>Dividends per Common Share</u>	<u>Amount of Dividend Payment</u>	<u>Fiscal 2004</u>	<u>Dividends per Common Share</u>	<u>Amount of Dividend Payment</u>
First Quarter	\$ 0.040	\$ 8,267	First Quarter	\$ 0.024	\$ 4,893
Second Quarter	0.046	9,473	Second Quarter	0.024	4,919
Third Quarter	0.052	10,752	Third Quarter	0.030	6,223
Fourth Quarter	0.070	14,508	Fourth Quarter	0.035	7,284

On April 27, 2005, we declared a quarterly cash dividend of \$0.095 per share, which will be paid on June 3, 2005 to stockholders of record on May 13, 2005 and is estimated to be \$19.8 million. Our Board is free to change its dividend practices at any time and to decrease or increase the dividend paid, or not to pay a dividend, on our common stock on the basis of our results of operations, financial condition, cash requirements and future prospects, and other factors deemed relevant by our Board. Our current intent is to provide for ongoing quarterly cash dividends depending upon market conditions and our results of operations.

The following table sets forth our purchases of our common stock and the information below the table designates the repurchase program that the shares were purchased under:

<u>Period</u>	<u>Total Number of Shares Purchased</u>	<u>Average Price Paid per Share</u>	<u>Total Number of Shares Purchased as Part of Publicly Announced Programs</u>	<u>Maximum Number of Shares that May Yet Be Purchased Under the Programs</u>
January 1, 2005 – January 31, 2005	49,300	\$ 24.395	49,300	1,615,100
February 1, 2005 – February 28, 2005	—	\$ —	—	1,615,100
March 1, 2005 – March 31, 2005	—	\$ —	—	1,615,100

On April 22, 2004, our Board of Directors authorized the repurchase of up to 2,500,000 shares of our common stock in the open market or privately negotiated transactions. As of March 31, 2005, 1,615,100 shares related to this authorization remained available to be purchased under this program.

Please refer to “Item 12, *Security Ownership Of Certain Beneficial Owners And Management And Related Stockholder Matters*,” at page 42 below, for the information required by Item 201(d) of Regulation S-K with respect to securities authorized for issuance under our equity compensation plans at March 31, 2005.

Item 6. SELECTED FINANCIAL DATA

You should read the following selected consolidated financial data for the five-year period ended March 31, 2005 in conjunction with our Consolidated Financial Statements and Notes thereto and, “Management’s Discussion and Analysis of Financial Condition and Results of Operations” included in Item 7 of this Form 10-K. Our consolidated statements of income data for each of the years in the three-year period ended March 31, 2005, and the balance sheet data as of March 31, 2005 and 2004, are derived from our audited consolidated financial statements, included in Item 8 of this Form 10-K (for information below all amounts are in thousands, except per share data).

Statement of Income Data (1):

	<u>Year Ended March 31,</u>				
	<u>2005</u>	<u>2004</u>	<u>2003</u>	<u>2002</u>	<u>2001</u>
Net sales	\$ 846,936	\$ 699,260	\$ 651,462	\$ 571,254	\$ 715,730
Cost of sales	362,961	349,301	299,227	284,518	335,016
Research and development	93,040	85,389	87,963	81,650	78,595
Selling, general and administrative	111,188	92,411	89,355	82,615	102,620
Special charges (2)	21,100	865	50,800	—	17,358
Operating income	258,647	171,294	124,117	122,471	182,141
Interest income (expense), net	16,864	4,639	3,344	4,344	12,741
Other income (expense), net	1,757	1,963	871	376	2,080
Net loss in equity investment (2)	—	—	—	—	(2,190)
Gain on sale of investment (2)	—	—	—	—	1,427
Income before income taxes	277,268	177,896	128,332	127,191	196,199
Income tax provision	63,483	40,634	28,657	32,377	53,363
Income before cumulative effect of change in accounting principle	213,785	137,262	99,675	94,814	142,836
Cumulative effect of change in accounting principle (3)	—	—	11,443	—	—

Net income	\$ 213,785	\$ 137,262	\$ 88,232	\$ 94,814	\$ 142,836
Basic net income per common share	\$ 1.03	\$ 0.67	\$ 0.44	\$ 0.48	\$ 0.74
Diluted net income per common share	\$ 1.01	\$ 0.65	\$ 0.42	\$ 0.45	\$ 0.70
Dividends declared per common share	\$ 0.208	\$ 0.113	\$ 0.040	\$ —	\$ —
Basic common shares outstanding	206,740	206,032	202,483	199,184	193,632
Diluted common shares outstanding	211,962	212,172	210,646	208,907	205,190

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Balance Sheet Data (1):

	Year Ended March 31,				
	2005	2004	2003	2002	2001
Working capital	\$ 768,683	\$ 613,894	\$ 393,979	\$ 381,211	\$ 176,936
Total assets	1,817,554	1,622,143	1,428,275	1,275,600	1,161,349
Long-term obligations, less current portion	—	—	—	—	—
Stockholders' equity	1,485,734	1,320,517	1,178,949	1,075,779	942,848

- (1) On January 16, 2001, we merged with TelCom Semiconductor, Inc. and accounted for the merger as a pooling-of-interests. Accordingly, the selected financial data has been restated to include the operations of TelCom for all periods presented. TelCom had a December 31 fiscal year end, and we have conformed the TelCom financial data to a March 31 year end for the March 31, 2001 fiscal year.
- (2) There were no special charges during the fiscal year ended March 31, 2002. Detailed discussions of the special charges for the fiscal years ended March 31, 2005, 2004 and 2003 are contained in Note 4 to the Consolidated Financial Statements. Detailed explanations of the special charges for the fiscal year ended March 31, 2001 are provided below. The following table presents a summary of special charges for the five-year period ended March 31, 2005:

	Year Ended March 31,				
	2005	2004	2003	2002	2001
Intellectual property settlement	\$ 21,100	\$ —	\$ —	\$ —	\$ —
Contract cancellation, severance and other costs related to Fab 1 closure	—	865	—	—	—
Fab 3 impairment charge	—	—	41,500	—	—
In-process research and development charge	—	—	9,300	—	—
Restructuring charges	—	—	—	—	6,409
TelCom merger charges	—	—	—	—	10,949
Totals	\$ 21,100	\$ 865	\$ 50,800	\$ —	\$ 17,358

- (3) We changed our revenue recognition policy as it relates to Asia regional distributors during fiscal 2003. See "Item 7 – Management's Discussion and Analysis of Financial Condition and Results of Operations – Change in Accounting Principle," beginning at page 36 below, for a discussion of this change.

Fiscal 2001

During the March 2001 quarter, we implemented capacity and cost reduction actions necessitated by adverse business conditions in the semiconductor industry. We reduced cumulative wafer fab capacity at Fabs 1 and 2 by approximately 24%, compared to our December 31, 2000 levels. We also decided to close our Hong Kong test facility, acquired as part of the TelCom transaction, and migrate these test requirements to our Thailand test facility. The capacity reduction at Fabs 1 and 2 was completed by the end of the March 2001 quarter. The closure of the Hong Kong facility was completed by June 30, 2001. These actions resulted in a restructuring charge of \$6.4 million in the March 2001 quarter. These actions were undertaken to reduce both manufacturing capacity and manufacturing costs. The reduction in wafer fab capacity was required due to reduced customer demand. The closure of the Hong Kong facility was undertaken to rationalize our test manufacturing capacity and migrate the test requirements to our more cost-effective test facility in Thailand.

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Included in the restructuring charges resulting from these actions were:

- \$4.0 million related to equipment that was written off
- \$2.1 million related to employee severance costs, and
- \$0.3 million related to other restructuring costs.

On January 16, 2001, we completed our merger with TelCom. Under the terms of the merger agreement, we exchanged each share of TelCom common stock for 0.795 of a share of our common stock. We issued 14,702,184 shares of our common stock and assumed all outstanding TelCom stock options. The transaction was structured as a tax-free reorganization and has been accounted for as a pooling-of-interests.

During the March 2001 quarter, we recognized a special charge of \$10.9 million for costs associated with the TelCom transaction. These costs included:

- \$7.3 million associated with investment banking fees
- \$1.6 million associated with legal and accounting fees
- \$0.9 million of severance costs, and
- \$1.1 million related to other costs.

All reserves relating to the special charges for the fiscal 2001 actions have been fully utilized and there were no reversals of previously provided amounts.

Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Our Management's Discussion and Analysis of Financial Condition and Results of Operations contains certain forward-looking statements that involve risks and uncertainties, including statements regarding our strategy, financial performance and revenue sources. We use words such as "anticipate," "believe," "plan," "expect," "estimate," "future," "intend" and similar expressions to identify forward-looking statements. Our actual results could differ materially from the results anticipated in these forward-looking statements as a result of certain factors including those set forth in this Item 7, and under "Item 1 – Business – Additional Factors That May Affect Our Results of Operations," beginning at page 12, above, and elsewhere in this Form 10-K. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. You should not place undue reliance on these forward-looking statements. We disclaim any obligation to update information contained in any forward-looking statement.

We begin our Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) with a summary of Microchip's overall business strategy to give the reader an overview of the goals of our business and the overall direction of our business and products. This is followed by a discussion of the Critical Accounting Policies and Estimates that we believe are important to understanding the assumptions and judgments incorporated in our reported financial results. In the next section, beginning at page 26, we discuss our Results of Operations for fiscal 2005 compared to fiscal 2004, and for fiscal 2004 compared to fiscal 2003. We then provide an analysis of changes in our balance sheet and cash flows, and discuss our financial commitments in sections titled "Liquidity and Capital Resources," "Contractual Obligations" and "Off-Balance Sheet Arrangements."

This MD&A should be read in conjunction with other sections of this Annual Report on Form 10-K, including "Item 1 – Business"; "Item 6 – Selected Financial Data"; and "Item 8 – Financial Statements and Supplementary Data."

Strategy

Our goal is to be a worldwide leader in providing specialized semiconductor products for a wide variety of embedded control applications. Our strategic focus is on embedded control products, which include microcontrollers, high-performance linear and mixed signal devices, power management and thermal management devices, and complementary microperipheral products including interface devices, Serial EEPROMs, and our patented KEELOQ security devices. We provide highly cost-effective embedded control products that also offer the advantages of small size, high performance, low voltage/power operation and ease of development, enabling timely and cost-effective embedded control product integration by our customers.

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Our manufacturing operations include wafer fabrication and assembly and test. The ownership of our manufacturing resources is an important component of our business strategy, enabling us to maintain a high level of manufacturing control resulting in us being one of the lowest cost producers in the embedded control industry. By owning our wafer fabrication facilities and much of our assembly and test operations, and by employing proprietary statistical process control techniques, we have been able to achieve and maintain high production yields. Direct control over manufacturing resources allows us to shorten our design and production cycles. This control also allows us to capture the wafer manufacturing and a portion of the assembly and test profit margin.

We employ proprietary design and manufacturing processes in developing our embedded control products. We believe our processes afford us both cost-effective designs in existing and derivative products and greater functionality in new product designs. While many of our competitors develop and optimize separate processes for their logic and memory product lines, we use a common process technology for both microcontroller and non-volatile memory products. This allows us to more fully leverage our process research and development costs and to deliver new products to market more rapidly. Our engineers utilize advanced computer-aided design (CAD) tools and software to perform circuit design, simulation and layout, and our in-house photomask and wafer fabrication facilities enable us to rapidly verify design techniques by processing test wafers quickly and efficiently.

We are committed to continuing our investment in new and enhanced products, including development systems, and in our design and manufacturing process technologies. We believe these investments are significant factors in maintaining our competitive position. Our current research and development activities focus on the design of new microcontrollers, digital signal controllers, ASSPs, memory and mixed-signal products, new development systems, software and application-specific software libraries. We are also developing new design and process technologies to achieve further cost reductions and performance improvements in existing products.

We market our products worldwide primarily through a network of direct sales personnel and distributors. Our distributors focus primarily on servicing the product and technical support requirements of a broad base of diverse customers. We believe that distributors provide an effective means of reaching this broad and diverse customer base. Our direct sales force focuses primarily on major strategic accounts in three geographical markets: the Americas, Europe and Asia. We currently maintain sales and support centers in major metropolitan areas in North America, Europe and Asia. We believe that a strong technical service presence is essential to the continued development of the embedded control market. Many of our field sales engineers (FSEs), field application engineers (FAEs), and sales management have technical degrees and have been previously employed in an engineering environment. We believe that the technical knowledge of our sales force is a key competitive advantage in the sale of our products. The primary mission of our FAE team is to provide technical assistance to strategic accounts and to conduct periodic training sessions for FSEs and distributor sales teams. FAEs also frequently conduct technical seminars in major cities around the world, and work closely with our distributors to provide technical assistance and end-user support.

Critical Accounting Policies and Estimates

General

Our discussion and analysis of Microchip's financial condition and results of operations is based upon our Consolidated Financial Statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. We review the accounting policies we use in reporting our financial results on a regular basis. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosure of contingent liabilities. On an ongoing basis, we evaluate our estimates, including those related to revenue recognition, inventories, income taxes, property plant and equipment, impairment of property, plant and equipment and assets held for sale and litigation. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Results may differ from these estimates due to actual outcomes being different from those on which we based our assumptions. We review these estimates and judgments on an ongoing basis. We believe the following critical accounting policies affect our more significant judgments and estimates used in the preparation of our consolidated financial statements. We also have other policies that we consider key accounting policies, such as our policy regarding revenue recognition to OEMs; however, we do not believe these policies require us to make estimates or judgments that are as difficult or subjective as our policies described below.

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Our distributors worldwide have broad rights to return products and price protection rights, so we defer revenue recognition until the distributor sells the product to their customers. We reduce product pricing through price protection based on market conditions, competitive considerations and other factors. Price protection is granted to third-party distributors on the inventory that they have on hand at the date the price protection is offered. When we reduce the price of our products, it allows the distributor to claim a credit against its outstanding accounts receivable balances based on the new price of the inventory it has on hand as of the date of the price reduction. There is no revenue impact from the price protections. We also grant certain credits to our third-party distributors. The credits are granted to the distributors on specially identified pieces of the distributors' business to allow them to earn a competitive gross margin on the sale of our products to their end customers. The credits are on a per unit basis and are not given to the distributor until they provide documentation of the sale to their end customer. The effect of granting these credits establishes the net selling price from us to our distributors for the product and results in the net revenue recognized by us when the product is sold by the distributors to their end customers. Upon shipment, amounts billed to distributors are included as accounts receivable, inventory is relieved, and the sale and the gross margin are deferred and are reflected as a current liability until the product is sold by the distributor to their customers. We changed our revenue recognition policy as it relates to sales to Asia regional distributors during fiscal 2003 as described below at page 36 and in Note 1 to our consolidated financial statements to conform with our revenue recognition policies for our distribution channels in the Americas and Europe.

Inventories

Inventories are valued at the lower of cost or market using the first-in, first-out (FIFO) method. We write down our inventory for estimated obsolescence or unmarketable inventory in an amount equal to the difference between the cost of inventory and the estimated market value based upon assumptions about future demand and market conditions. If actual market conditions are less favorable than those we projected, additional inventory write-downs may be required. Inventory impairment charges establish a new cost basis for inventory and charges are not subsequently reversed to income even if circumstances later suggest that increased carrying amounts are recoverable. In estimating our reserves for obsolescence, we primarily evaluate estimates of demand over a 12-month period and provide reserves for inventory on hand in excess of the estimated 12-month demand.

Income Taxes

As part of the process of preparing our consolidated financial statements, we are required to estimate our income taxes in each of the jurisdictions in which we operate. This process involves estimating our actual current tax exposure together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within our consolidated balance sheet. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income within the relevant jurisdiction and to the extent we believe that recovery is not likely, we must establish a valuation allowance. We have not provided for a valuation allowance because we believe that it is "more likely than not" that our deferred tax assets will be recovered from future taxable income. Should we determine that we would not be able to realize all or part of our net deferred tax asset in the future, an adjustment to the deferred tax asset would be charged to income in the period such determination was made. At March 31, 2005, our gross deferred tax asset was \$105.1 million.

Various taxing authorities in the United States and other countries in which we do business are increasing their scrutiny of various tax structures employed by businesses. Companies of our size and complexity are regularly audited by the taxing authorities in the jurisdictions in which they conduct significant operations. We are currently under audit by the United States Internal Revenue Service (IRS) for our fiscal years ended March 31, 1998, 1999, 2000 and 2001. As part of this ongoing audit, the IRS has proposed certain adjustments related to positions reflected on these returns. The IRS has issued formal assessments for these adjustments. We do not agree with these adjustments and intend to appeal these assessments. We recognize liabilities for anticipated tax audit issues in the United States and other tax jurisdictions based on our estimate of whether, and the extent to which, additional tax payments are probable. We believe that we maintain adequate tax reserves to offset any potential tax liabilities that may arise upon final resolution of the pending audit through either settlement or the appeals process with the IRS. We also believe that we maintain adequate tax reserves to offset any potential tax liabilities that may arise upon other audits in the United States and other countries in which we do business. If such amounts ultimately prove to be unnecessary, the resulting reversal of such reserves would result in tax benefits being recorded in the period the reserves are no longer deemed necessary. If such amounts ultimately prove to be less than an ultimate assessment, a future charge to expense would be recorded in the period in which the assessment is determined.

The foregoing statements regarding the recoverability of our deferred tax asset and the adequacy of our tax reserves are forward-looking statements. Actual results could differ materially because of the following factors, among others: results of any audit conducted by the various taxing authorities in the countries in which we do business; the level of our taxable income and whether our taxable income will be sufficient to realize the benefits available from our deferred tax assets; current and future tax laws and regulations; and taxation rates in geographic regions where we have significant operations.

Property, Plant & Equipment

Property, plant and equipment are stated at cost. Major renewals and improvements are capitalized, while maintenance and repairs are expensed when incurred. At March 31, 2005, the carrying value of our property and equipment totaled \$693.3 million, which represents 38.1% of our total assets. This carrying value reflects the application of our property and equipment accounting policies, which incorporate estimates, assumptions and judgments relative to the useful lives of our property and equipment. Depreciation is provided on a straight-line basis over the estimated useful lives of the related assets, which range from five to seven years on manufacturing equipment and approximately 30 years on buildings.

We began production activities at Fab 4 on October 31, 2003. We began to depreciate the Fab 4 assets as the assets were placed in service for production purposes. As of March 31, 2005, all of the buildings and supporting facilities were being depreciated as well as the manufacturing equipment that had been placed in service. All manufacturing equipment that was not being used in production activities was maintained in projects in process and is not being depreciated until it is placed into service since management believes there is no change to its utility from the present time until it is placed into productive service. The lives to be used for depreciating this equipment at Fab 4 will be evaluated at such time as the assets are placed in service. We do not believe that the temporary idling of such assets has impaired the estimated life or carrying values of the underlying assets.

On March 31, 2005, we changed the classification of Fab 3 from an asset held-for-sale to an asset held-for-future-use. Fab 3 had been on the market for over two years, and we had not received any acceptable offers on the facility. Over that period of time, our business had increased significantly and over the next several years we will need to begin planning for future wafer fabrication capacity as a larger percentage of Fab 4's clean room capacity is utilized. We determined that the appropriate action to take was to stop actively marketing the Fab 3 facility and hold it for our future use. As a result of this change in classification, we had to assess the fair value of the Fab 3 asset to determine if any additional impairment charge was required upon the change in classification from "held-for-sale" to "held-for-future-use" under Statement of Financial Accounting Standards ("SFAS") No. 144. We performed a discounted cash flow analysis of the Fab 3 asset based on various financial projections in developing the fair value estimate given that it was the best available valuation technique for the asset. The discounted cash flow analysis confirmed the carrying value of the Fab 3 asset at March 31, 2005 was not in excess of its fair value. If indicators of impairment for the Fab 3 assets arise in the future, we will determine if the sum of the estimated undiscounted cash flows attributable to the assets in question are less than their carrying value. If less, we would recognize an impairment loss on the excess of the carrying amount of the assets over their respective fair values. We will begin to depreciate the Fab 3 asset in April 2005.

The estimates, assumptions and judgments we use in the application of our property and equipment policies reflect both historical experience and expectations regarding future industry conditions and operations. The use of different estimates, assumptions and judgments regarding the useful lives of our property and equipment and expectations regarding future industry conditions and operations, would likely result in materially different carrying values of assets and results of operations.

We do not currently hold title to the land on which our Thailand facility resides. The land is subject to a complex restructuring situation relating to the seller of the land. We have provided reserves that we estimate will be adequate to obtain full title. Such reserves are set at the estimated fair value of the land. However, timing of the resolution is difficult to predict and the ultimate amount to be paid could change.

Impairment of Property, Plant and Equipment

We assess whether indicators of impairment of long-lived assets are present. If such indicators are present, we determine whether the sum of the estimated undiscounted cash flows attributable to the assets in question is less than their carrying value. If less, we recognize an impairment loss based on the excess of the carrying amount of the assets over their respective fair values. Fair value is determined by discounted future cash flows, appraisals or other methods. If the assets determined to

be impaired are to be held and used, we recognize an impairment loss through a charge to our operating results to the extent the present value of anticipated net cash flows attributable to the asset are less than the asset's carrying value, which we depreciate over the remaining estimated useful life of the asset. We may incur impairment losses, or additional losses on already impaired assets, in future periods if factors influencing our estimates change.

Litigation

Our current estimated range of liability related to certain pending litigation is based on the probable loss of claims for which we can estimate the amount and range of loss. Recorded reserves were not significant at March 31, 2005.

Because of the uncertainties related to both the probability of loss and the amount and range of loss on the remaining pending litigation, we are unable to make a reasonable estimate of the liability that could result from an unfavorable outcome. As additional information becomes available, we will assess the potential liability related to our pending litigation and revise our estimates. Revisions in our estimates of the potential liability could materially impact our results of operation and financial position.

Results of Operations

The following table sets forth certain operational data as a percentage of net sales for the years indicated:

	Year Ended March 31,		
	2005	2004	2003
Net sales	100.0%	100.0%	100.0%
Cost of sales	42.9%	50.0%	45.9%
Gross profit	57.1%	50.0%	54.1%
Research and development	11.0%	12.2%	13.5%
Selling, general and administrative	13.1%	13.2%	13.7%
Special charges	2.5%	0.1%	7.8%
Operating income	30.5%	24.5%	19.1%

Net Sales

We operate in one industry segment and engage primarily in the design, development, manufacture and marketing of semiconductor products. We sell our products to distributors and OEMs in a broad range of market segments, perform ongoing credit evaluations of our customers and generally require no collateral.

Our net sales of \$846.9 million in fiscal 2005 increased by \$147.6 million, or 21.1%, over fiscal 2004, and net sales of \$699.3 million in fiscal 2004 increased by \$47.8 million, or 7.3%, over fiscal 2003. The increases in net sales in fiscal 2005 compared to fiscal 2004 and in fiscal 2004 compared to fiscal 2003 resulted primarily from increased demand, predominantly for our proprietary microcontroller products. Average selling prices for our products were down approximately 4% in fiscal 2005 over fiscal 2004 and 9% in fiscal 2004 over fiscal 2003. The number of units of our products sold was up approximately 26% in fiscal 2005 over fiscal 2004 and 17% in fiscal 2004 over fiscal 2003. The average selling prices and the unit volumes of our sales are impacted by the mix of our products sold. We believe that we have continued to grow our percentage of market share in the embedded control market over the last three fiscal years. Key factors in achieving the amount of net sales during the last three fiscal years include:

- continued market share gains
- increasing semiconductor content in our customers' products
- customers' increasing needs for the flexibility offered by our programmable solutions
- our new product offerings that have increased our served available market, and
- increasing demand for our products.

We recognize revenue from product sales upon shipment to OEMs. Under our shipping terms, legal title passes to the customer upon shipment from Microchip. We have no post shipment obligations. Distributors worldwide generally have broad rights to return products and price protection rights, so we defer revenue recognition until the distributors sell the

product to their customers. Upon shipment, amounts billed to distributors are included in accounts receivable, inventory is relieved, the sale is deferred and the gross margin is reflected as a current liability until the product is sold by the distributors to their customers.

During the quarter ended December 31, 2003, we changed our accounting policy relating to amounts billed to customers for shipping and handling costs to be consistent with EITF 00-10. With this change, we have reclassified amounts billed to customers for shipping and handling costs from a reduction of cost of sales to revenue for the first three quarters of fiscal 2004, and we have continued this treatment in all subsequent periods. This reclassification had no impact on net income and an immaterial impact on revenues and cost of sales. Prior year amounts have not been reclassified, as these amounts were immaterial.

Sales by product line for the fiscal years ended March 31, 2005, 2004 and 2003 were as follows (dollars in thousands):

	Year Ended March 31,					
	2005	%	2004	%	2003	%
Microcontrollers	\$ 674,902	79.7	\$ 556,764	79.6	\$ 516,383	79.3
Memory products	115,120	13.6	91,640	13.1	87,158	13.4
Analog and interface products	56,914	6.7	50,856	7.3	47,921	7.3
Total Sales	\$ 846,936	100.0%	\$ 699,260	100.0%	\$ 651,462	100.0%

Certain prior period amounts have been reclassified to conform to the current period presentation.

Microcontrollers

Our microcontroller product line represents the largest component of our total net sales. Microcontrollers and associated application development systems accounted for approximately 79.7% of our total net sales in fiscal 2005, approximately 79.6% of our total net sales in fiscal 2004 and approximately 79.3% of our total net sales in fiscal 2003.

Net sales of our microcontroller products increased approximately 21.2% in fiscal 2005 compared to fiscal 2004, and increased approximately 7.8% in fiscal 2004 compared to fiscal 2003. The increases in net sales were primarily due to increased demand for our microcontroller products in end markets, driven principally by market share gains and those factors described above under “Net Sales” at page 26. The end markets that we serve include the automotive, communications, computing, consumer and industrial control markets.

Historically, average selling prices in the semiconductor industry decrease over the life of any particular product. The overall average selling prices of our microcontroller products have remained relatively constant over time due to the proprietary nature of these products. We have experienced, and expect to continue to experience, moderate pricing pressure in certain microcontroller product lines, primarily due to competitive conditions. We have in the past been able to, and expect in the future to be able to, moderate average selling price declines in our microcontroller product lines by introducing new products with more features at higher prices. However, we may be unable to maintain average selling prices for our microcontroller products as a result of increased pricing pressure in the future, which could adversely affect our operating results.

Memory Products

Sales of our memory products accounted for approximately 13.6% of our total net sales in fiscal 2005, approximately 13.1% of our total net sales in fiscal 2004 and approximately 13.4% of our total net sales in fiscal 2003.

Net sales of our memory products increased approximately 25.6% in fiscal 2005 compared to fiscal 2004, and increased approximately 5.1% in fiscal 2004 compared to fiscal 2003, driven primarily by customer demand conditions within the Serial EEPROM market, which products comprise substantially all of our memory product net sales.

Serial EEPROM product pricing has historically been cyclical in nature, with steep price declines followed by periods of relative price stability, driven by changes in industry capacity at different stages of the business cycle. During the past three fiscal years, we have experienced several Serial EEPROM product pricing trends, both up and down, due to market

conditions. We have experienced, and expect to continue to experience, varying degrees of competitive pricing pressures in our Serial EEPROM products. We may be unable to maintain the average selling prices of our Serial EEPROM products as a result of increased pricing pressure in the future, which could adversely affect our operating results.

Analog and Interface Products

Sales of our analog and interface products accounted for approximately 6.7% of our total net sales in fiscal 2005, 7.3% of our total net sales in fiscal 2004 and approximately 7.3% of our total net sales in fiscal 2003.

Net sales of our analog and interface products increased approximately 11.9% in fiscal 2005 compared to fiscal 2004 and increased approximately 6.1% in fiscal 2004 compared to fiscal 2003. The increase in net sales of our analog and interface products in these periods were driven primarily by new proprietary design wins, supply and demand conditions within the market and our ability to gain market share.

Analog and interface products can be proprietary or non-proprietary in nature. Currently, we consider more than half of our analog and interface product mix to be proprietary in nature, where prices are relatively stable, similar to the pricing stability experienced in our microcontroller products. The non-proprietary portion of our analog and interface business will experience price fluctuations, driven primarily by the current supply and demand for those products. We may be unable to maintain the average selling prices of our analog and interface products as a result of increased pricing pressure in the future, which could adversely affect our operating results. We anticipate the proprietary portion of our analog and interface products to increase over time.

Turns Orders

Our net sales in any given quarter depend upon a combination of shipments from backlog and orders received in that quarter for shipment in that quarter, which we refer to as turns orders. We measure turns orders at the beginning of a quarter based on the orders needed to meet the shipment targets that we set entering the quarter. Historically, we have proven our ability to respond quickly to customer orders as part of our competitive strategy, resulting in customers placing orders with short delivery schedules. Shorter lead times generally mean that turns orders as a percentage of our business are relatively high in any particular quarter and reduces our backlog visibility on future product shipments. Turns orders correlate to overall semiconductor industry conditions and product lead times. Turns orders are difficult to predict, and we may not experience the combination of turns orders and shipments from backlog in a quarter that would be sufficient to achieve anticipated net sales. If we do not achieve a sufficient level of turns orders in a particular quarter, our net sales and operating results may suffer.

The foregoing statements regarding competitive pricing pressure in our microcontroller, Serial EEPROM and analog and interface product lines, our ability to moderate future average selling price declines in our microcontroller product lines and the proprietary portion of our analog and interface product lines increasing over time are forward-looking statements. Actual results could differ materially because of the following factors, among others: the level of orders that are received and can be shipped in a quarter; changes in demand for our products and the products of our customers; the level and timing at which previous design wins become actual orders and sales; inventory mix and timing of customer orders; customers' inventory levels, order patterns and seasonality; level of sell-through of our products through distribution in any particular fiscal period; our ability to ramp products into volume production; competition and competitive pressures on pricing and product availability; disruptions in commercial activities, or international transport or delivery occasioned by terrorist activity, armed conflict, war or an unexpected increase in the price of, or decrease in the supply of, oil

resulting in reduced end-user purchases relative to expectations; impact of events outside the United States, such as the business impact of fluctuating currency rates or unrest or political instability; the cyclical nature of both the semiconductor industry and the markets addressed by our products; market acceptance of our new products and those of our customers; the financial condition of our customers; fluctuations in production yields, production efficiencies and overall capacity utilization; changes in product mix; absorption of fixed costs, labor and other fixed manufacturing costs; and general industry, economic and political conditions.

Distribution

Distributors accounted for 65% of our net sales in fiscal 2005, 64% of our net sales in fiscal 2004 and 60% of our net sales in fiscal 2003.

Our largest distributor accounted for approximately 13% of our net sales in fiscal 2005 and fiscal 2004 and 12% of our net sales in fiscal 2003. Our two largest distributors accounted for 25% of our net sales in fiscal 2005 and fiscal 2004.

Generally, we do not have long-term agreements with our distributors and we, or our distributors, may terminate their relationships with us with little or no advanced notice. The loss of, or the disruption in the operations of, one or more of our distributors could reduce our future net sales in a given quarter and could result in an increase in inventory returns.

At March 31, 2005, distributors were maintaining an average of approximately 2.3 months of inventory of our products. Over the past three fiscal years, the months of inventory maintained by our distributors have fluctuated between approximately 2.0 months and 2.8 months. Thus, inventory levels at our distributors are at the low to moderate end of the range we have experienced over the last three years. As we recognize revenue based on sell through for all of our distributors, we do not believe that inventory holding patterns at our distributors will materially impact our net sales.

Distributors generally have broad-based rights to return product to us. As revenue on distributor shipments is not recognized until the distributors sell our product on to their end customers, distributor returns have no impact on revenue recognition.

We also grant certain credits to our third-party distributors and also offer these distributors price protection. The credits are granted to the distributors on specifically identified pieces of the distributors' business to allow them to earn a competitive gross margin on the sale of our products to their end customers. The credits are on a per unit basis and are not given to the distributor until they provide information regarding the sale to their end customer. The effect of granting these credits establishes the net selling price from us to our distributors for the products and results in the net revenue recognized by us when the product is sold by the distributors to their end customers.

We reduce product pricing through price protection based on market conditions, competitive considerations and other factors. Price protection is granted to third-party distributors on the inventory that they have on hand at the date the price protection is offered. When we reduce the selling price of our products, it allows the distributors to claim a credit against its outstanding accounts receivables balances based on the new price of the inventory it has on hand as of the date of the price reduction. There is no revenue recognition impact from the price protections.

We do not offer material incentive programs to our third-party distributors.

The foregoing statements regarding our expectation that distributors will increase their current inventory levels and our belief that inventory holding patterns at our distributors will not materially impact our net sales are forward-looking statements. Actual results could differ materially because of the following factors, among others: the rate of recovery in the overall economy and the uncertainty of current economic and political conditions; changes in demand for our products and the products of our customers; the level and timing at which previous design wins become actual orders and sales; inventory mix and timing of customer orders; customers' inventory levels, order patterns and seasonality; the impact on our business and customer order patterns due to major public health concerns, such as the SARS virus; level of sell-through of our products through distribution in any particular fiscal period; disruptions in commercial activities, or international transport or delivery occasioned by terrorist activity, armed conflict, war or an unexpected increase in the price of, or decrease in the supply of, oil resulting in reduced end-user purchases relative to expectations; impact of events outside the United States, such as the business impact of fluctuating currency rates or unrest or political instability; the cyclical nature of both the semiconductor industry and the markets addressed by our products; market acceptance of our new products and those of our customers; and the financial condition of our customers.

Sales by Geography

Sales by geography for the fiscal years ended March 31, 2005, 2004 and 2003 were as follows (dollars in thousands):

	Year Ended March 31,					
	2005	%	2004	%	2003	%
Americas	\$ 248,881	29.4	\$ 219,641	31.4	\$ 219,504	33.7
Europe	232,493	27.4	194,187	27.8	177,727	27.3
Asia	365,562	43.2	285,432	40.8	254,231	39.0
Total Sales	\$ 846,936	100.0%	\$ 699,260	100.0%	\$ 651,462	100.0%

Our sales to foreign customers have been predominately in Asia and Europe, which we attribute to the manufacturing strength in those areas for automotive, communications, computing, consumer and industrial control products. Americas sales include sales to customers in the United States, Canada, Central America and South America. Sales to customers in Asia have increased during the last three fiscal years due to many of our customers transitioning their manufacturing operations to Asia.

Sales to foreign customers accounted for approximately 73% of our net sales in fiscal 2005, and 71% of our net sales in fiscal 2004 and fiscal 2003. Substantially all of our foreign sales are U.S. dollar denominated.

Sales to customers in China, including Hong Kong, accounted for approximately 16% of our net sales in fiscal 2005, approximately 14% of our net sales in fiscal 2004 and approximately 13% of our net sales in fiscal 2003. Sales to customers in Taiwan accounted for approximately 10% of our net sales in fiscal 2005. We did not have sales into any other countries that exceeded 10% of our net sales during the last three fiscal years.

Gross Profit

Our gross profit was \$484.0 million in fiscal 2005, \$350.0 million in fiscal 2004 and \$352.2 million in fiscal 2003. Gross profit as a percent of sales was 57.1% in fiscal 2005, 50.0% in fiscal 2004 and 54.1% in fiscal 2003.

The most significant factors affecting gross profit percentage over the past three fiscal years were:

- Improvements in capacity utilization and product absorption, which positively affected gross margin by \$11.8 million in fiscal 2005 compared to fiscal 2004, and by \$10.4 million in fiscal 2004 compared to fiscal 2003.
- \$31.8 million in accelerated depreciation and other costs associated with the closure of Fab 1, which negatively affected gross margin in fiscal 2004.
- Changes in period cost of sales in Fab 3 and Fab 4, our non-operational facilities at certain times during the last three fiscal years, which negatively impact gross margin. Period cost of sales amounted to \$3.3 million in fiscal 2005, \$18.1 million in fiscal 2004 and \$13.1 million in fiscal 2003.
- A one-week unpaid shutdown negatively affecting gross profit by \$1.7 million in fiscal 2004. The shutdown occurred in the three months ended September 30, 2003 and had a negative impact on gross profit due to the fact that certain fixed costs including depreciation, utilities, property taxes and other ongoing costs continued when the factory was shut down. There were no shutdowns in fiscal 2005 or fiscal 2003.

Other factors that impacted gross profit percentage in the periods covered by this report include:

- continued cost reductions in wafer fabrication and assembly and test manufacturing such as new manufacturing technologies and more efficient manufacturing techniques
- factors impacting the average selling prices of our products
- fluctuations in the product mix of proprietary microcontroller and analog products and related Serial EEPROM products, and
- inventory write-offs and the sale of inventory that was previously written off.

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During fiscal 2005, we operated at approximately 96% of our Fab 2 capacity, which favorably impacted gross margins compared to fiscal 2004. During fiscal 2004, we operated at approximately 91% of our Fab 2 capacity, which favorably impacted gross margins, compared to fiscal 2003. During fiscal 2003, we operated at approximately 85% of our cumulative total Fab 1 and Fab 2 capacity. Our utilization of Fab 4's total capacity is at relatively low levels although we are utilizing all of the installed equipment base. We expect to maintain the current level of capacity utilization at Fab 2 and Fab 4 during the first quarter of fiscal 2006.

The process technologies utilized impact our gross margins. Fab 2 currently utilizes various manufacturing process technologies, but predominantly utilizes our 0.5 to 1.0 micron processes. Fab 4 currently utilizes our 0.5 micron process technology. We continue to transition products to more advanced process technologies to reduce future manufacturing costs. Since the closure of Fab 1 in June 2003, all of our production has been on 8-inch wafers. In fiscal 2003 and the first quarter of fiscal 2004, approximately 80% of our production was on 8-inch wafers.

Our overall inventory levels were \$103.7 million at March 31, 2005, compared to \$94.5 million at March 31, 2004 and \$102.3 million at March 31, 2003. We maintained 107 days of inventory on our balance sheet at March 31, 2005 compared to 101 days of inventory at March 31, 2004 and 128 days at March 31, 2003.

We anticipate that our gross margins will fluctuate over time, driven primarily by the overall product mix of microcontroller, analog and interface and memory products and the percentage of net sales of each of these products in a particular quarter, as well as manufacturing yields, fixed cost absorption, capacity utilization levels, particularly those at Fab 4, and competitive and economic conditions.

The foregoing statements relating to our expectation to maintain the current level of capacity utilization at Fab 2 and Fab 4 during the first quarter of fiscal 2006, our transition to more advanced process technologies to reduce future manufacturing costs and the fluctuation of gross margins over time are forward-looking statements. Actual results could differ materially because of the following factors, among others: changes in demand for our products and the products of our customers; fluctuations in production yields, production efficiencies and overall capacity utilization; absorption of fixed costs, labor and other direct manufacturing costs; competition and competitive pressure on pricing; disruptions in commercial activities, or international transport or delivery occasioned by terrorist activity, armed conflict, war or an unexpected increase in the price of, or decrease in the supply of, oil resulting in reduced end-user purchases relative to expectations; impact of events outside the United States, such as the business impact of fluctuating currency rates or unrest or political instability; our ability to increase manufacturing capacity as needed; cost and availability of raw materials; changes in product mix; and other general industry, economic and political conditions.

At March 31, 2005, approximately 70% of our assembly requirements were being performed in our Thailand facility, compared to approximately 71% as of March 31, 2004 and approximately 77% at March 31, 2003. Third-party contractors located in Asia perform the balance of our assembly operations. Substantially all of our test requirements were being performed in our Thailand facility over the last three fiscal years. We believe that the assembly and test operations performed at our Thailand facility provide us with significant cost savings when compared to third-party contractor assembly and test costs, as well as increased control over these portions of the manufacturing process.

We rely on outside wafer foundries for a small portion of our wafer fabrication requirements.

Our use of third parties involves some reduction in our level of control over the portions of our business that we subcontract. While we review the quality, delivery and cost performance of our third-party contractors, our future operating results could suffer if any third-party contractor is unable to maintain manufacturing yields, assembly and test yields and costs at approximately their current levels.

Research and Development (R&D)

R&D expenses for fiscal 2005 were \$93.0 million, or 11.0% of sales, compared to \$85.4 million, or 12.2% of sales, for fiscal 2004 and \$88.0 million, or 13.5% of sales, for fiscal 2003. We are committed to investing in new and enhanced products, including development systems software, and in our design and manufacturing process technologies. We believe these investments are significant factors in maintaining our competitive position. We expense all R&D costs as incurred. R&D expenses include expenditures for labor, depreciation, masks, prototype wafers, and expenses for the development of process technologies, new packages, and software to support new products and design environments.

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R&D expenses increased \$7.6 million, or 9.0%, for fiscal 2005 over fiscal 2004. The primary reasons for the dollar increase in R&D costs in fiscal 2005 compared to fiscal 2004 was higher labor costs as a result of expanding our technical resources and increases in bonuses. R&D expenses decreased \$2.6 million, or 3.0%, for fiscal 2004

over fiscal 2003. The primary reasons for the dollar decrease in R&D costs in fiscal 2004 compared to fiscal 2003 were reductions in professional services and lower costs associated with product prototyping which were partially offset by increases in labor costs.

Selling, General and Administrative

Selling, general and administrative expenses for fiscal 2005 were \$111.2 million, or 13.1% of sales, compared to \$92.4 million, or 13.2% of sales, for fiscal 2004, and \$89.4 million, or 13.7% of sales, for fiscal 2003. Selling, general and administrative expenses include salary expenses related to field sales, marketing and administrative personnel, advertising and promotional expenditures and legal expenses. Selling, general and administrative expenses also include costs related to our direct sales force and field applications engineers who work in sales offices worldwide to stimulate demand by assisting customers in the selection and use of our products.

Selling, general and administrative expenses increased \$18.8 million, or 20.3% for fiscal 2005 over fiscal 2004. The primary reasons for the dollar increases in selling, general and administrative expenses in fiscal 2005 over fiscal 2004 were higher labor costs as a result of expanding our internal resources, increases in bonuses, increases in travel expenses and increases in audit and legal services. Selling, general and administrative expenses increased \$3.0 million, or 3.4%, for fiscal 2004 over fiscal 2003. The primary reasons for the dollar increase in selling, general and administrative expenses in fiscal 2004 over fiscal 2003 were increases in labor costs and travel expenses.

Selling, general and administrative expenses fluctuate over time, primarily due to revenue and operating expense investment levels.

Special Charges

The following table presents a summary of special charges for the fiscal years ended March 31, 2005, 2004 and 2003 (dollars in thousands).

	Year Ended March 31,		
	2005	2004	2003
Patent license settlement	\$ 21,100	\$ —	\$ —
Contract cancellation, severance and other costs related to Fab 1 closure	—	865	—
Fab 3 impairment charge	—	—	41,500
In-process research & development charge	—	—	9,300
Totals	\$ 21,100	\$ 865	\$ 50,800

Fiscal 2005

Settlement with U.S. Philips Corporation

We reached an agreement with U.S. Philips Corporation and Philips Electronics North America Corp. (together “Philips”) regarding patent license litigation between Philips and ourselves which had been ongoing from October 2001 to October 2004. The agreement includes dismissal of the then pending litigation and the cross-license of certain patents between Philips and Microchip. We recorded a special charge of \$21.1 million in the quarter ended June 30, 2004 associated with this matter. As part of the settlement, we licensed certain of our patents related to 8-pin microcontrollers to Philips, and Philips licensed its patents related to I²C serial communications to us, each on fully-paid up, non-royalty bearing worldwide licenses. The definitive agreement related to this matter was finalized and executed and the cash payment was made by us to Philips during our fiscal quarter ending September 30, 2004.

Fiscal 2004

Fab 1 Closure and Special Charges

On April 7, 2003, we announced our intention to close our Chandler, Arizona (Fab 1) wafer fabrication facility and integrate certain Fab 1 personnel and processes into our Tempe, Arizona (Fab 2) wafer fabrication facility. We completed this integration process during the three-month period ended June 30, 2003. The closure of Fab 1 and the integration of certain Fab 1 personnel into Fab 2 operations resulted in a reduction in force of 207 employees who were either directly involved in our manufacturing operations or provided support to Fab 1. The detail of the charges incurred related to the closure of Fab 1 that were included in cost of sales for the three-month period ended June 30, 2003 is as follows (amounts in thousands):

Accelerated depreciation for Fab 1	\$ 30,608
Fab 1 related charges including severance, material and other costs	1,147
Total charges in cost of sales	\$ 31,755

For the quarter ended June 30, 2003, operating expense included \$1,612,000 of special charges recorded principally for contract cancellation, severance and other costs related to the closure of Fab 1 and other actions. We incurred \$865,000 of such expenditures during fiscal 2004. We reversed \$747,000 of the special charges recorded in the quarter ended June 30, 2003 in the quarter ended December 31, 2003 as a result of a favorable outcome in the settlement of a contract cancellation.

The facility where Fab 1 is located is an integral part of our overall campus in Chandler, Arizona. Within this same facility resides our wafer probe, mask making and other manufacturing related activities. The accelerated depreciation that was taken only related to assets used in the wafer fabrication operations at the facility. We have no specific plans for utilizing the space formerly housing the wafer fabrication operations, and intend to leave it in an idle status. The property, plant and equipment that was subject to the accelerated depreciation is reflected in the gross and accumulated depreciation carrying values in the property, plant and equipment section of our balance sheet and related footnote disclosures.

Fiscal 2003

Fab 3 Impairment Charge

We recorded a \$41.5 million asset impairment charge during the quarter ended September 30, 2002, as described below.

We acquired Fab 3, a semiconductor manufacturing facility in Puyallup, Washington, in July 2000. The original purchase consisted of semiconductor manufacturing facilities and real property. It was our intention to bring Fab 3 to productive readiness and commence volume production of 8-inch wafers using our 0.7 and 0.5 micron process technologies by August 2001. We delayed our production start up at Fab 3 due to deteriorating business conditions in the semiconductor industry during fiscal 2002. Fab 3 has never been brought to productive readiness.

On August 23, 2002, we acquired Fab 4, a semiconductor manufacturing facility in Gresham, Oregon. See Note 2 to the Consolidated Financial Statements on page F-12, below. We decided to purchase Fab 4 instead of bringing Fab 3 to productive readiness because, among other things, the cost of the manufacturing equipment needed to ramp production at Fab 3 over the next several years was significantly higher than the total purchase price of Fab 4, and the time to bring Fab 4 to productive readiness was significantly less than the time required to bring Fab 3 to productive readiness.

After the acquisition of Fab 4 was completed, we undertook an analysis of the potential production capacity at Fab 4. The results of the production capacity analysis led us to determine that Fab 3's capacity would not be needed in the foreseeable future and during the September 2002 quarter we committed to a plan to sell Fab 3. At that time, we retained a third-party broker to market Fab 3 on our behalf. Accordingly, Fab 3 was classified as an asset held-for-sale as of September 30, 2002 and maintained that classification until the end of fiscal 2005.

Management determined the value assigned to the assets through various methods including assistance from a third-party appraisal. The independent third party used the market approach and considered sales of comparable properties in determining the fair value of Fab 3. The comparable sales included eight properties, including our purchases of Fab 3 in July 2000 and Fab 4 in August 2002. Based on the results of this appraisal, we recorded an asset impairment charge on Fab 3 of

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\$36.9 million, including estimated costs to sell. The remaining value of \$60.2 million was classified as an asset held-for-sale and was included as a component of other current assets until March 31, 2005.

During the quarter ended September 30, 2002, we also recorded an asset impairment charge of \$4.6 million to write-down certain excess manufacturing equipment located at Fab 3 to its net realizable value of \$0.2 million. This manufacturing equipment became "excess" as a result of duplicate equipment acquired in the purchase of Fab 4. The net realizable value for the excess manufacturing equipment was determined based on management estimates. Substantially all of the other manufacturing equipment located at Fab 3 has been transferred to and will be used in our other wafer fabrication facilities located in Tempe, Arizona (Fab 2) and Gresham, Oregon (Fab 4).

At March 31, 2005, we changed the classification of Fab 3 from an asset held-for-sale to an asset held-for-future use. Fab 3 consists of manufacturing buildings and land, with no equipment. Fab 3 had been on the market for over two years, and we had not received any acceptable offers on the facility. Over that period of time, our business has increased significantly and over the next several years we need to begin planning for future wafer fabrication capacity as a larger percentage of Fab 4's clean room capacity is utilized. We determined that the appropriate action to take was to stop actively marketing the Fab 3 facility and hold it for our future use. As a result of this change in classification, we had to assess the fair value of the Fab 3 asset to determine if any additional impairment charge was required upon the change in classification from "held-for-sale" to "held-for-future-use" under SFAS 144. We performed a discounted cash flow analysis of the Fab 3 asset based on various financial projections in developing the fair value estimate given that it was the best available valuation technique for the asset. The discounted cash flow analysis confirmed the carrying value of the Fab 3 asset at March 31, 2005 was not in excess of its fair value. We will begin to depreciate the Fab 3 asset in the first quarter of fiscal 2006.

PowerSmart In-Process Research and Development Charge

During the quarter ended June 30, 2002, purchased in-process research and development of \$9.3 million associated with our acquisition of PowerSmart, Inc. was written off at the date of the acquisition (June 5, 2002) in accordance with FASB Interpretation No. 4, "Applicability of FASB Statement No. 2, Business Combinations Accounted for by the Purchase Method" ("FIN 4"). PowerSmart delivered a battery management whole product solution that improves system runtimes with a lower system cost for the user. Included in the whole product solution is an application tools suite designed to speed up implementation during the user's development and production. The acquisition was intended to strengthen our position in battery management applications such as laptop computers, personal digital assistants, cellular telephones, digital cameras and camcorders.

The assets acquired included in-process research and development for which there is no alternative future use. Management determined the value assigned to this asset through various methods including assistance from third party appraisal firms in valuing the PowerSmart business. As of the valuation date, there were 15 projects that were considered to be in process. The values of the projects were determined based on analyses of estimated cash flows to be generated by the products that are expected to result from the in-process projects. These cash flows were estimated by forecasting total revenues expected from these products then deducting appropriate operating expenses, cash flow adjustments and contributory asset returns to establish a forecast of the net return on the in-process technology. These net returns were substantially reduced to take into account the time value of money and the risks associated with the inherent difficulties and uncertainties in achieving commercial readiness. The above analysis resulted in \$9.3 million of value assigned to acquired in-process research and development, which was expensed on the acquisition date. We believe the assumptions used in valuing in-process research and development are reasonable, but are inherently uncertain.

Other Income (Expense)

Interest income in fiscal 2005 increased from interest income in fiscal 2004 as our average invested cash balances were at higher levels in fiscal 2005 compared to fiscal 2004, and we extended the average maturity term of our invested cash balances and thus earned a higher interest rate on our invested balances. Interest income in fiscal 2004 increased from interest income in fiscal 2003 as our average invested cash balances were at higher levels in fiscal 2004 compared to fiscal 2003.

Provision for Income Taxes

Provisions for income taxes reflect tax on our foreign earnings and federal and state tax on our U.S. earnings. Our effective tax rate was 22.9% in fiscal 2005, 22.8% in fiscal 2004 and, 22.3% in fiscal 2003, and is lower than statutory rates in the United States due primarily to lower tax rates at our foreign locations and R&D tax credits.

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As part of the process of preparing our consolidated financial statements, we are required to estimate our income taxes in each of the jurisdictions in which we operate. This process involves estimating our actual current tax exposure, together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within our consolidated balance sheet. We must then assess the likelihood that our deferred tax asset will be recovered from future taxable income within the relevant jurisdiction and, to the extent we believe that recovery is not likely, we must establish a valuation allowance. We have not provided for a valuation allowance because we believe that our deferred tax asset will be recovered from future taxable income. Should we determine that we would not be able to realize all or part of our net deferred tax asset in the future, an adjustment to the deferred tax asset would be charged to income in the period such determination was made. At March 31, 2005 our gross deferred tax asset was \$105.1 million.

Various taxing authorities in the United States and other countries in which we do business are increasing their scrutiny of various tax structures employed by businesses. Companies of our size and complexity are regularly audited by the taxing authorities in the jurisdictions in which they conduct significant operations. We are currently under audit by the United States Internal Revenue Service (IRS) for our fiscal years ended March 31, 1998, 1999, 2000 and 2001. As part of this ongoing audit, the IRS has proposed certain adjustments related to positions reflected on these returns. The IRS has issued formal assessments for these adjustments. We do not agree with these adjustments and intend to appeal these assessments. We believe that we maintain adequate tax reserves to offset any potential tax liabilities that may arise upon final resolution of the pending audit through either settlement or the appeals process with the IRS. We also believe that we maintain adequate tax reserves to offset any potential tax liabilities that may arise upon other audits in the United States and other countries in which we do business. If such amounts ultimately prove to be unnecessary, the resulting reversal of such reserves would result in tax benefits being recorded in the period the reserves are no longer deemed necessary. If such amounts ultimately prove to be less than an ultimate assessment, a future charge to expense would be recorded in the period in which the assessment is determined.

Our Thailand manufacturing operations currently benefit from numerous tax holidays that have been granted to us by the Thailand government based on our investments in property, plant and equipment in Thailand. Although our tax holidays in Thailand partially expired in October 2003, our manufacturing operations in Thailand are being predominantly conducted using equipment that was invested pursuant to tax holidays that do not begin to expire until September 2006. The expiration of a portion of our tax holiday in Thailand did not have a material impact on our effective tax rate in fiscal 2004.

The American Jobs Creation Act of 2004 (the "Jobs Act"), enacted on October 22, 2004, provides for a temporary deduction of 85% of dividends received on certain foreign earnings repatriated during a one-year period. The deduction would result in an approximate 5.25% federal tax rate on the repatriated earnings. To qualify for the deduction, the earnings must be reinvested in the United States pursuant to a domestic reinvestment plan established by a company's chief executive officer and approved by the company's board of directors. Certain other criteria in the Jobs Act must be satisfied as well. The maximum amount of our foreign earnings that qualify for the temporary deduction is \$500 million. The one-year period for which we are considering the qualifying distribution is fiscal 2006.

We are in the process of evaluating whether we will repatriate foreign earnings under the repatriation provisions of the Jobs Act, and if so, the amount that will be repatriated. The range of reasonably possible amounts that we are considering for repatriation, which would be eligible for the temporary deduction, is zero to \$500 million. We are in the process of analyzing and evaluating the recently issued regulatory guidance and statutory technical corrections associated with the Jobs Act to determine the amount, if any, we will repatriate. We expect to determine the amounts and sources of foreign earnings to be repatriated, if any, during fiscal 2006.

We are not yet in a position to determine the impact of a qualifying repatriation, should we choose to make one, on our income tax expense for fiscal 2006 or the amount of our indefinitely reinvested foreign earnings. If we were to plan to repatriate the maximum amount eligible for the temporary deduction, which is \$500 million, from foreign earnings which were previously indefinitely reinvested, we estimate we would incur additional tax expense in fiscal 2006 of between \$26.3 million and \$28.7 million.

The foregoing statements regarding the recoverability of our deferred tax asset from our future taxable income, the adequacy of our tax reserves to offset any potential tax liabilities that may arise upon audit, the range of possible repatriation amounts and the estimated amount of additional tax expense are forward-looking statements. Actual results could differ materially because of the following factors, among others: current and future tax laws and regulations; taxation rates in geographic regions where we have significant operations; results of any current or future audit conducted by the

U.S. Internal Revenue Service or other taxing authorities in the countries in which we do business; and the level of our taxable income and whether our taxable income will be sufficient to utilize our deferred tax asset.

Change in Accounting Principle

We had historically recognized revenue from sales to our Americas, European and multinational Asian distributors at Point of Sale (POS), or when those distributors sell our products to their customers, and, prior to fiscal 2003, we recognized revenue on sales to regional Asian distributors at Point of Purchase (POP), or when we shipped product to these distributors. Upon shipment, amounts billed to distributors at POS are included as accounts receivable, inventory is relieved, the sale is deferred and the gross margin is reflected as a current liability until the product is sold by the distributor to its customers.

On March 18, 2003, we announced that we would change our revenue recognition policy relating to regional Asian distributors from POP to POS. We believe that revenue recognition at POS for sales to distributors as our sole revenue recognition policy worldwide is a more reflective measure of end customer demand for our products. To implement the change in revenue recognition, we recorded the cumulative effect of a change in accounting principle of \$11.4 million (net of income taxes of \$6.6 million) as of April 1, 2002, the beginning of fiscal 2003. The cumulative effect of this change in accounting principle was calculated by multiplying the quantity of our inventory that the regional Asia distributors maintained as of April 1, 2002 by the gross margin we would realize on those sales, net of related income tax.

Liquidity and Capital Resources

We had \$734.6 million in cash, cash equivalents and short-term investments at March 31, 2005, an increase of \$260.1 million from the March 31, 2004 balance. The increase in cash, cash equivalents and short-term investments over this time period is primarily attributable to our cash flows generated from operations.

During fiscal 2005, we maintained an unsecured short-term line of credit with various financial institutions in Asia, which at March 31, 2005 totaled \$5 million (U.S. dollar equivalent). There were no borrowings under the foreign line of credit as of March 31, 2005, but an allocation of approximately \$0.4 million of the available line was made, relating to import guarantees associated with our business in Thailand. There are no covenants related to the foreign line of credit.

Net cash provided from operating activities was \$352.7 million for fiscal 2005, \$343.1 million for fiscal 2004 and \$260.2 million for fiscal 2003. The increase in cash flow from operations was primarily due to increases in net income.

Net cash used in investing activities was \$370.7 million for fiscal 2005, \$267.6 million for fiscal 2004 and \$376.8 million in fiscal 2003. The increase in cash used in investing activities in fiscal 2005 over fiscal 2004 was due to changes in our net purchases, sales and maturities of short-term investments. The decrease in cash used in investing activities in fiscal 2004 over fiscal 2003 was primarily due to the purchases of Fab 4 and PowerSmart that occurred in fiscal 2003.

We enter into hedging transactions from time to time in an attempt to minimize our exposure to currency rate fluctuations. Although none of the countries in which we conduct significant foreign operations have had a highly inflationary economy in the last five years, there is no assurance that inflation rates or fluctuations in foreign currency rates in countries where we conduct operations will not adversely affect our operating results in the future. There were no hedges outstanding as of March 31, 2005.

Our level of capital expenditures varies from time to time as a result of actual and anticipated business conditions. Capital expenditures were \$63.2 million in fiscal 2005, \$63.5 million in fiscal 2004 and \$265.1 million in fiscal 2003. The primary reason for the dollar decrease in capital expenditures in fiscal 2004 compared to fiscal 2003 was a reduced need for additional capital equipment as a result of our purchase of Fab 4 during fiscal 2003. We currently intend to spend approximately \$55 to \$60 million during the next 12 months to invest in equipment and facilities to maintain, and selectively increase, capacity to meet our currently anticipated needs.

We expect to finance capital expenditures through our existing cash balances and cash flows from operations. We believe that the capital expenditures anticipated to be incurred over the next 12 months will provide sufficient manufacturing capacity to meet our currently anticipated needs.

Net cash used in financing activities was \$18.6 million for fiscal 2005, \$24.0 million for fiscal 2004 and \$3.1 million for fiscal 2003. Proceeds from the sale of stock, the exercise of stock options and employee purchases under our employee stock purchase plan were \$47.2 million for fiscal 2005, \$53.2 million for fiscal 2004 and \$31.5 million for fiscal 2003. Cash

expended for the repurchase of our common stock was \$68.3 million in fiscal 2005, \$53.9 million in fiscal 2004 and \$26.5 million in fiscal 2003. We had short-term borrowings of \$45.5 million at March 31, 2005. The short-term debt is a result of repurchase agreements that are in place with two investment firms.

On March 11, 2004, our Board of Directors authorized the repurchase of 2,500,000 shares of our common stock in the open market or in privately negotiated transactions. As of March 31, 2005, we had repurchased the entire 2,500,000 common shares under this authorization for a total of \$66.1 million. On April 22, 2004, our Board of Directors authorized the repurchase of up to an additional 2,500,000 shares of our common stock in the open market or in privately negotiated transactions. As of March 31, 2005, we had repurchased 884,900 common shares under this authorization for a total of \$23.3 million. As of March 31, 2005, all but 818,332 of the purchased shares under both authorizations had been reissued to fund stock option exercises and purchases under our employee stock purchase plan. The timing and amount of any future repurchases will depend upon market conditions and corporate considerations.

On October 28, 2002, we announced that our Board of Directors had approved and instituted a quarterly cash dividend on our common stock. The initial quarterly dividend of \$0.02 per share was paid on December 6, 2003 in the amount of \$4.0 million. We have continued to pay quarterly dividends and have increased the amount of such dividends on a regular basis. During fiscal 2004, we paid dividends in the amount of \$0.113 per share for a total dividend payment of \$23.3 million. During fiscal 2005, we paid dividends in the amount of \$0.208 per share for a total dividend payment of \$43.0 million. On April 27, 2005, we declared a quarterly cash dividend of \$0.095 per share, which will be paid on June 3, 2005 to stockholders of record on May 13, 2005 and is estimated to be \$19.8 million. Our Board is free to change its dividend practices at any time and to decrease or increase the dividend paid, or not to pay a dividend, on our common stock on the basis of our results of operations, financial condition, cash requirements and future prospects, and other factors deemed relevant by our Board. Our current intent is to provide for ongoing quarterly cash dividends depending upon market conditions and our results of operations.

We believe that our existing sources of liquidity combined with cash generated from operations will be sufficient to meet our currently anticipated cash requirements for at least the next 12 months. However, the semiconductor industry is capital intensive. In order to remain competitive, we must constantly evaluate the need to make significant investments in capital equipment for both production and research and development. We may seek additional equity or debt financing from time to time to maintain or expand our wafer fabrication and product assembly and test facilities, or for other purposes. The timing and amount of any such financing requirements will depend on a number of factors, including demand for our products, changes in industry conditions, product mix, and competitive factors. There can be no assurance that such financing will be available on acceptable terms, and any additional equity financing would result in incremental ownership dilution to our existing stockholders.

The foregoing statements regarding our anticipated level of capital expenditures over the next 12 months, the nature of such expenditures, the financing and sufficiency of our capital expenditures and our belief that existing sources of liquidity will be sufficient to meet our requirements are forward-looking statements. Actual results could differ materially because of the following factors, among others: changes in demand for our products and those of our customers; changes in utilization of current manufacturing capacity; unanticipated costs in continuing to ramp production at Fab 4; market acceptance of our products and of our customers' products; the cyclical nature of the semiconductor industry and the markets addressed by our products; the availability and cost of raw materials, equipment and other supplies; actual levels of capital expenditures; the costs and outcome of any tax audit or any litigation involving intellectual property, customer or other issues; the financial condition of our customers and vendors; uninsured losses; and the economic, political and other conditions in the worldwide markets served by us.

Contractual Obligations

The following table summarizes our significant contractual obligations at March 31, 2005, and the effect such obligations are expected to have on our liquidity and cash flows in future periods. This table excludes amounts already recorded on our balance sheet as current liabilities at March 31, 2005 (dollars in thousands):

	Payments Due by Period				
	Total	Less than 1 year	1 – 3 years	3 – 5 years	More than 5 years
Operating lease obligations	\$ 10,127	\$ 4,183	\$ 4,986	\$ 929	\$ 29
Capital purchase obligations (1)	15,547	15,547	—	—	—
Other purchase obligations and commitments (2)	5,521	2,950	2,281	290	—
Long-term debt obligations	—	—	—	—	—
Total contractual obligations (3)	\$ 31,195	\$ 22,680	\$ 7,267	\$ 1,219	\$ 29

(1) Capital purchase obligations represent commitments for construction or purchases of property, plant and equipment. They are not recorded as liabilities on our balance sheet as of March 31, 2005, as we have not yet received the related goods or taken title to the property.

(2) Other purchase obligations and commitments include payments due under various types of licenses.

(3) Total contractual obligations do not include contractual obligations recorded on the balance sheet as current liabilities, or certain purchase obligations as discussed below.

Purchase orders or contracts for the purchase of raw materials and other goods and services are not included in the table above. We are not able to determine the aggregate amount of such purchase orders that represent contractual obligations, as purchase orders may represent authorizations to purchase rather than binding agreements. For the purpose of this table, contractual obligations for purchase of goods or services are defined as agreements that are enforceable and legally binding on Microchip and that specify all significant terms, including: fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction. Our

purchase orders are based on our current manufacturing needs and are fulfilled by our vendors with short time horizons. We do not have significant agreements for the purchase of raw materials or other goods specifying minimum quantities or set prices that exceed our expected requirements for three months. We also enter into contracts for outsourced services; however, the obligations under these contracts were not significant and the contracts generally contain clauses allowing for cancellation without significant penalty.

The expected timing of payment of the obligations discussed above is estimated based on current information. Timing of payments and actual amounts paid may be different depending on the time of receipt of goods or services or changes to agreed-upon amounts for some obligations.

Off-Balance Sheet Arrangements

As of March 31, 2005, we are not involved in any off-balance sheet arrangements, as defined in Item 3(a)(4)(ii) of SEC Regulation S-K.

Recently Issued Accounting Pronouncements

During December 2004, the FASB issued SFAS No. 123R which requires companies to measure and recognize compensation expense for all share-based payments at fair value. Share-based payments include stock option grants. We grant options to purchase common stock to some of our employees and directors under our stock option plan at prices equal to the market value of the stock on the dates the options were granted. SFAS No. 123R is effective for us beginning April 1, 2006. Early adoption of the provisions of SFAS No. 123R is encouraged, but not required. We have not yet adopted this pronouncement and are currently evaluating the expected impact that the adoption of SFAS No. 123R will have on our consolidated financial position and results of operations. We expect the adoption of SFAS No. 123R will have an unfavorable impact on our consolidated results of operations and net income per common share. SFAS No. 123R also requires the benefits of tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as an operating cash flow as required under current literature. This requirement will reduce net operating cash flows and increase net financing cash flows in periods after adoption. We cannot estimate what those amounts will be in the future because they depend on, among other things, when employees exercise stock options.

FASB Staff Position ("FSP") No. 109-2, "Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004" ("FSP 109-2"), provides guidance under FASB Statement No. 109, "Accounting for Income Taxes," ("SFAS 109") with respect to recording the potential impact of the repatriation provisions of the American Jobs Creation Act of 2004 (the "Jobs Creation Act") on enterprises' income tax expense and deferred tax liability. The Jobs Creation Act was enacted on October 22, 2004. FSP 109-2 states that an enterprise is allowed time beyond the financial reporting period of enactment to evaluate the effect of the Jobs Act on its plan for reinvestment or repatriation of foreign earnings for purposes of applying SFAS 109. As of March 31, 2005, we are in the process of evaluating whether we will repatriate any foreign earnings under the Act and, if so, the amount that we will repatriate. However, we do not expect to be able to complete this evaluation until later in fiscal 2006. Accordingly, as provided for in FSP 109-2, we have not adjusted our tax expense or deferred tax liability to reflect the repatriation provisions of the Jobs Creation Act. The Jobs Creation Act also provides a deduction for income from qualified domestic production activities, to be phased in from 2005 through 2010, which is intended to replace the existing extra-territorial income exclusion for foreign sales. In FSP 109-1, the FASB decided the deduction for qualified domestic production activities should be accounted for as a special deduction under SFAS 109, rather than as a rate reduction. Accordingly, any benefit from the deduction will be reported in the period in which the deduction is claimed on the tax return and no adjustment to deferred taxes at March 31, 2005 is required.

In March 2004, the FASB approved the consensus reached on the Emerging Issues Task Force (EITF) Issue No. 03-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments" ("EITF 03-1"). The Issue's objective is to provide guidance for identifying other-than-temporarily impaired investments. EITF 03-1 also provides new disclosure requirements for investments that are deemed to be temporarily impaired. In September 2004, the FASB issued a FSP EITF 03-1-1 that delays the effective date of the measurement and recognition guidance in EITF 03-1 until further notice. The disclosure requirements of EITF 03-1 are effective with this annual report for fiscal 2005. Once the FASB reaches a final decision on the measurement and recognition provisions, we will evaluate the impact of the adoption of the accounting provisions of EITF 03-1.

In December 2004, the FASB also issued SFAS No. 151, "Inventory Costs, an amendment of ARB No. 43, Chapter 4," ("SFAS 151") which will become effective for us beginning January 1, 2006. This standard clarifies that abnormal amounts of idle facility expense, freight, handling costs and wasted material should be expensed as incurred and not included in overhead. In addition, this standard requires that the allocation of fixed production overhead costs to inventory be based on the normal capacity of the production facilities. We are currently evaluating the potential impact of this standard on our financial position and results of operations, but do not believe the impact of the change will be material.

Item 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our investment portfolio, consisting of fixed income securities that we hold on an available-for-sale basis, was \$728.7 million as of March 31, 2005, and \$462.9 million as of March 31, 2004. These securities, like all fixed income instruments, are subject to interest rate risk and will decline in value if market interest rates increase. We have the ability to hold our fixed income investments until maturity and, therefore, we would not expect to recognize any material adverse impact in income or cash flows if market interest rates increase. The following table provides information about our available-for-sale securities that are sensitive to changes in interest rates. We have aggregated our available-for-sale securities for presentation purposes since they are all very similar in nature (dollars in thousands):

	Financial instruments mature during the fiscal year ended March 31,					
	2006	2007	2008	2009	2010	Thereafter
Available-for-sale securities	\$ 76,116	\$ 81,421	\$ 94,711	\$ 169,237	\$ 231,215	\$ 13,174
Weighted-average yield rate	2.31%	2.74%	3.01%	3.50%	4.02%	3.14%

We have international operations and are thus subject to foreign currency rate fluctuations. To date, our exposure related to exchange rate volatility has not been significant. Approximately 99% of our sales are denominated in U.S. dollars. At times we maintain hedges of foreign currency exposure of a net investment in a foreign operation. There were no hedges outstanding as of March 31, 2005. The amounts of the hedges outstanding as of March 31, 2004 were immaterial. If foreign currency rates fluctuate by 15% from the rates at March 31, 2005 and March 31, 2004, the effect on our financial position and results of operation would not be material.

During the normal course of business we are routinely subjected to a variety of market risks, examples of which include, but are not limited to, interest rate movements and foreign currency fluctuations, as we discuss in this Item 7A, and collectability of accounts receivable. We continuously assess these risks and have established policies and

procedures to protect against the adverse effects of these and other potential exposures. Although we do not anticipate any material losses in these risk areas, no assurance can be made that material losses will not be incurred in these areas in the future.

Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The Consolidated Financial Statements listed in the index appearing under Item 15(a)(1) hereof are filed as part of this Form 10-K. See also Index to Financial Statements, below.

Item 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

Not applicable.

Item 9A. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures.

As of the end of the period covered by this Annual Report on Form 10-K, as required by paragraph (b) of Rule 13a-15 or Rule 15d-15 under the Securities Exchange Act of 1934, as amended, we evaluated under the supervision of our Chief Executive Officer and our Chief Financial Officer, the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) or 15d-15(e) of the Securities Exchange Act of 1934, as amended). Based on this evaluation, our Chief Executive Officer and our Chief Financial Officer have concluded that our disclosure controls and procedures are effective to ensure that information we are required to disclose in reports that we file or submit under the Securities Exchange Act of 1934 (i) is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms, and (ii) is accumulated and communicated to our management, including our Chief Executive Officer and our Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. Our disclosure controls and procedures are designed to provide reasonable assurance that such information is accumulated and communicated to our management. Our disclosure controls and procedures include components of our internal control over financial reporting. Management's assessment of the effectiveness of our internal control over financial reporting is expressed at the level of reasonable assurance because a control system, no matter how well designed and operated, can provide only reasonable, but not absolute, assurance that the control system's objectives will be met.

Management Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting to provide reasonable assurance regarding the reliability of our financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements.

Management assessed our internal control over financial reporting as of March 31, 2005, the end of our fiscal year. Management based its assessment on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Management's assessment included evaluation of such elements as the design and operating effectiveness of key financial reporting controls, process documentation, accounting policies, and our overall control environment. This assessment is supported by testing and monitoring performed by our finance organization.

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Based on our assessment, management has concluded that our internal control over financial reporting was effective as of the end of the fiscal year to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external reporting purposes in accordance with generally accepted accounting principles. We reviewed the results of management's assessment with the Audit Committee of our Board of Directors.

Our independent registered public accounting firm, Ernst & Young LLP, who also audited the Company's consolidated financial statements, audited management's assessment and independently assessed the effectiveness of our internal control over financial reporting. Ernst & Young LLP has issued their attestation report, which is included in Part II, Item 8 of this Form 10-K.

Changes in Internal Control over Financial Reporting.

During the three months ended March 31, 2005, there was no change in our internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Rule 13a-15 or Rule 15d-15 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Item 9B. OTHER INFORMATION

None.

PART III

Item 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

Information on the members of our Board of Directors is incorporated herein by reference to our proxy statement for the 2005 annual meeting of stockholders under the captions "The Board of Directors," and "Proposal One – Election of Directors."

Information on the composition of our audit committee and the members of our audit committee, including information on our audit committee financial experts, is incorporated by reference to our proxy statement for our 2005 annual meeting of stockholders under the caption "The Board of Directors – Committees of the Board of Directors – Audit Committee."

Information on our executive officers is provided in Item I, Part I of this Form 10-K under the caption "Executive Officers" at page 11, above.

Information with respect to compliance with Section 16(a) of the Securities Exchange Act of 1934, as amended, is incorporated herein by reference to our proxy statement for our 2005 annual meeting of stockholders under the caption "Section 16(a) Beneficial Ownership Reporting Compliance."

Information with respect to our code of ethics that applies to our directors, executive officers (including our principal executive officer and our principal financial and accounting officer) and employees is incorporated by reference to our proxy statement for our 2005 annual meeting of stockholders under the caption "Code of Ethics." A copy of the Code of Ethics is available on our website at the Investor Relations section under Mission Statement/Corporate Governance on www.microchip.com.

Item 11. EXECUTIVE COMPENSATION

Information with respect to executive compensation is incorporated herein by reference to the information under the caption "Executive Compensation" in our proxy statement for our 2005 annual meeting of stockholders.

Information with respect to director compensation is incorporated herein by reference to the information under the caption "The Board of Directors – Director Compensation" in our proxy statement for our 2005 annual meeting of stockholders.

Information with respect to compensation committee interlocks and insider participation in compensation decisions is incorporated herein by reference to the information under the caption "The Board of Directors – Compensation Committee Interlocks and Insider Participation" in our proxy statement for our 2005 annual meeting of stockholders.

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Our Board compensation committee report on executive compensation is incorporated herein by reference to the information under the caption "Executive Compensation – Compensation Committee Report on Executive Compensation" in our proxy statement for our 2005 annual meeting of stockholders.

Information with respect to changes in our cumulative shareholder return on our common stock is incorporated herein by reference to the information under the caption "Performance Graph" in our proxy statement for our 2005 annual meeting of stockholders.

Item 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

Information with respect to securities authorized for issuance under our equity compensation plans is incorporated herein by reference to the information under the caption "Executive Compensation – Equity Compensation Plan Information" in our proxy statement for our 2005 annual meeting of stockholders.

Information with respect to security ownership of certain beneficial owners and management is incorporated herein by reference to the information under the caption "Security Ownership of Principal Stockholders, Directors and Executive Officers" in our proxy statement for our 2005 annual meeting of stockholders.

Item 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Not applicable.

Item 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information required by this Item related to principal accountant fees and services as well as related pre-approval policies is incorporated by reference to the information under the caption "Independent Registered Public Accounting Firm" contained in our proxy statement for our 2005 annual meeting of stockholders.

[The area below is left blank intentionally.]

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PART IV

Item 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES.

(a) The following documents are filed as part of this Form 10-K:

(1) Financial Statements:

[Reports of Ernst & Young LLP, Independent Registered Public Accounting Firm](#)

[Consolidated Balance Sheets as of March 31, 2005 and 2004](#)

[Consolidated Statements of Income for each of the years in the three-year period ended March 31, 2005](#)

[Consolidated Statements of Cash Flows for each of the years in the three-year period ended March 31, 2005](#)

[Consolidated Statements of Stockholders' Equity for each of the years in the three-year period ended March 31, 2005](#)

[Notes to Consolidated Financial Statements](#)

(2) [Financial Statement Schedules – Applicable schedules have been omitted because information is included in the footnotes to the Financial Statements.](#)

(3) [The Exhibits filed with this Form 10-K or incorporated herein by reference are set forth in the Exhibit Index appearing on page E-1 hereof, which Exhibit Index is incorporated herein by this reference.](#)

(b) See Item 15(a)(3) above.

(c) See "Index to Financial Statements" included under Item 8 to this Form 10-K.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

MICROCHIP TECHNOLOGY INCORPORATED
(Registrant)

By : /s/ Steve Sanghi
Steve Sanghi
President and Chief Executive Officer

Date: May 23, 2005

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Name and Signature	Title	Date
/s/ Steve Sanghi Steve Sanghi	Director, President and Chief Executive Officer	May 23, 2005
/s/ Albert J. Hugo-Martinez Albert J. Hugo-Martinez	Director	May 23, 2005
/s/ L.B. Day L.B. Day	Director	May 23, 2005
/s/ Matthew W. Chapman Matthew W. Chapman	Director	May 23, 2005
/s/ Wade F. Meyercord Wade F. Meyercord	Director	May 23, 2005
/s/ Gordon W. Parnell Gordon W. Parnell	Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)	May 23, 2005

Exhibit Number	Exhibit Description	Incorporated by Reference			Filing Date	Filed Herewith
		Form	File Number	Exhibit		
2.1	Purchase and Sale Agreement, dated as of July 18, 2002 between Registrant and Fujitsu Microelectronics, Inc.	8-K	000-21184	2.1	7/18/02	
3.1	Restated Certificate of Incorporation of Registrant	10-Q	000-21184	3.1	11/12/02	
3.2	Amended and Restated By-Laws of Registrant, as amended through August 16, 2002	10-Q	000-21184	3.2	11/12/02	
3.3	Certificate of Ownership and Merger Merging ASIC Technical Solutions, Inc. into Microchip Technology Incorporated	10-K	000-21184	3.3	5/15/01	
3.4	Certificate of Ownership and Merger Merging TelCom Semiconductor, Inc. with and into Microchip Technology Incorporated	10-K	000-21184	3.4	5/15/01	
4.1	Amended and Restated Preferred Shares Rights Agreement, dated as of October 11, 1999, between Registrant and Norwest Bank Minnesota, N.A., including the Amended Certificate of Designations, the form of Rights Certificate and the Summary of Rights, attached as exhibits thereto	8-K	000-21184	4.1	10/12/99	
10.1	Form of Indemnification Agreement between Registrant and its directors and certain of its officers	S-1	33-57960	10.1	2/5/93	
10.2	*Microchip Technology 2004 Equity Incentive Plan, effective October 2, 2004	S-8	333-119939	4.4	10/25/04	
10.3	*Form of Notice of Grant for 2004 Equity Incentive Plan (including Exhibit A Stock Option Agreement)	S-8	333-119939	4.5	10/25/04	
10.4	*Form of Notice of Grant (foreign) for 2004 Equity Incentive Plan (including Exhibit A Stock Option Agreement (foreign))					

10.5	*Form of Notice of Grant of Restricted Stock Units for 2004 Equity Incentive Plan (including Exhibit A Restricted Stock Units Agreement)					X
10.6	*1993 Stock Option Plan, as Amended through August 16, 2002	10-Q	000-21184	10.1	11/12/02	
10.7	*Form of Notice of Grant For 1993 Stock Option Plan, with Exhibit A thereto, Form of Stock Option Agreement; and Exhibit B thereto, Form of Stock Purchase Agreement	S-8	333-872	10.6	1/23/96	
10.8	*2001 Employee Stock Purchase Plan as Amended through August 16, 2002	S-8	333-99655	10.3	9/17/02	
10.9	*Form of Executive Officer Severance Agreement	S-8	333-872	10.7	1/23/96	
10.10	Development Agreement dated as of August 29, 1997 by and between Registrant and the City of Chandler, Arizona	10-Q	000-21184	10.1	2/13/98	
10.11	Development Agreement dated as of July 17, 1997 by and between Registrant and the City of Tempe, Arizona	10-Q	000-21184	10.2	2/13/98	

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Exhibit Number	Exhibit Description	Incorporated by Reference			Filing Date	Filed Herewith
		Form	File Number	Exhibit		
10.12	Addendum to Development Agreement by and between Registrant and the City of Tempe, Arizona, dated May 11, 2000	10-K	000-21184	10.14	5/15/01	
10.13	*1997 Nonstatutory Stock Option Plan, as Amended Through March 3, 2003	10-K	000-21184	10.13	6/5/03	
10.14	Form of Notice of Grant For 1997 Nonstatutory Stock Option Plan, with Exhibit A thereto, Form of Stock Option Agreement	10-K	000-21184	10.17	5/27/98	
10.15	*International Employee Stock Purchase Plan as Amended Through March 3, 2003	S-8	333-103764	4.1	3/12/03	
10.16	Microchip Technology Inc. International Employee Stock Purchase Plan, as amended through August 20, 2004	S-8	333-119939	4.1	10/25/04	
10.17	Microchip Technology Inc. Stock Purchase Agreement for the International Employee Stock Purchase Plan (including attached Form of Enrollment Form)	S-8	333-119939	4.2	10/25/04	
10.18	Form of Change Form for Microchip Technology Inc. International Employee Stock Purchase Plan	S-8	333-119939	4.3	10/25/04	
10.19	*Description of Registrant's Management Incentive Compensation Plan	10-Q	000-21184	10.1	8/9/02	
10.20	TelCom Semiconductor, Inc. 1994 Stock Option Plan and forms of agreements thereunder	S-8	333-53876	4.1	1/18/01	
10.21	TelCom Semiconductor, Inc. 2000 Nonstatutory Stock Option Plan and forms of agreements used thereunder	S-8	333-53876	4.4	1/18/01	
10.22	Strategic Investment Program Contract dated as of August 15, 2002 by and between Registrant, Multnomah County, Oregon and City of Gresham, Oregon	8-K	000-21184	2.2	8/23/02	
10.23	PowerSmart, Inc. 1998 Stock Incentive Plan, Including Forms of Incentive Stock Option Agreement and Nonqualified Stock Option Agreement	S-8	333-96791	4.1	7/19/02	
10.24	*Microchip Technology Incorporated Supplemental Retirement Plan	S-8	333-101696	4.1.1	12/6/02	
10.25	*Amendment dated August 29, 2001 to the Microchip Technology Incorporated Supplemental Retirement Plan	S-8	333-101696	4.1.2	12/6/02	
10.26	*Adoption Agreement to the Microchip Technology Incorporated Supplemental Retirement Plan dated January 1, 1997	S-8	333-101696	4.1.3	12/6/02	
10.27	*Amendment Dated December 9, 1999 to the Adoption Agreement to the Microchip Technology Incorporated Supplemental Retirement Plan	S-8	333-101696	4.1.4	12/6/02	

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Exhibit Number	Exhibit Description	Incorporated by Reference			Filing Date	Filed Herewith
		Form	File Number	Exhibit		
10.28	*February 3, 2003 Amendment to the Adoption Agreement to the Microchip Technology Incorporated Supplemental Retirement Plan	10-K	000-21184	10.28	6/5/03	
21.1	Subsidiaries of Registrant					X
23.1	Consent of Ernst & Young LLP, Independent Registered Public Accounting Firm					X
24.1	Power of Attorney re: Microchip Technology Incorporated, the Registrant	10-K	000-21184	24.1	6/7/00	
31.1	Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended (the Exchange Act)					X
31.2	Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended (the Exchange Act)					X
32	Certifications Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002					X

* Compensation plans or arrangements in which directors or executive officers are eligible to participate

Annual Report on Form 10-K
Item 8, Item 15(a)(1) and (2), (c) and (d)

INDEX TO FINANCIAL STATEMENTS

CONSOLIDATED FINANCIAL STATEMENTS

EXHIBITS

YEAR ENDED MARCH 31, 2005

MICROCHIP TECHNOLOGY INCORPORATED
AND SUBSIDIARIES

CHANDLER, ARIZONA

MICROCHIP TECHNOLOGY INCORPORATED AND SUBSIDIARIES

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[Consolidated Statements of Stockholders' Equity for each of the years in the three-year period ended March 31, 2005](#)

[Notes to Consolidated Financial Statements](#)

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders of Microchip Technology Incorporated and subsidiaries

We have audited the accompanying consolidated balance sheets of Microchip Technology Incorporated and subsidiaries as of March 31, 2005 and 2004, and the related consolidated statements of income, stockholders' equity, and cash flows for each of the three years in the period ended March 31, 2005. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Microchip Technology Incorporated and subsidiaries at March 31, 2005 and 2004, and the consolidated results of their operations and their cash flows for each of the three years in the period ended March 31, 2005, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Microchip Technology Incorporated's internal control over financial reporting as of March 31, 2005, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated May 17, 2005 expressed an unqualified opinion thereon.

/s/ ERNST & YOUNG LLP

Phoenix, Arizona
May 17, 2005

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders of Microchip Technology Incorporated and subsidiaries

We have audited management's assessment, included in the accompanying Management Report on Internal Control Over Financial Reporting, that Microchip Technology Incorporated and subsidiaries maintained effective internal control over financial reporting as of March 31, 2005, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Microchip Technology Incorporated's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that Microchip Technology Incorporated maintained effective internal control over financial reporting as of March 31, 2005, is fairly stated, in all material respects, based on the COSO criteria. Also, in our opinion, Microchip Technology Incorporated maintained, in all material respects, effective internal control over financial reporting as of March 31, 2005, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the March 31, 2005 consolidated financial statements of Microchip Technology Incorporated and our report dated May 17, 2005 expressed an unqualified opinion thereon.

/s/ ERNST & YOUNG LLP

Phoenix, Arizona
May 17, 2005

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MICROCHIP TECHNOLOGY INCORPORATED AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS

(in thousands, except share amounts)

	March 31,	
	2005	2004
ASSETS		
Cash and cash equivalents	\$ 68,730	\$ 105,334
Short-term investments	665,874	369,216
Accounts receivable, net	113,088	107,890
Inventories	103,728	94,514
Prepaid expenses	10,828	6,884
Deferred tax assets	105,097	126,046
Other current assets	8,003	74,061
Total current assets	1,075,348	883,945
Property, plant and equipment, net	693,302	689,206
Goodwill	31,886	32,346
Intangible assets, net	9,289	9,698
Other assets	7,729	6,948
Total assets	\$ 1,817,554	\$ 1,622,143
LIABILITIES AND STOCKHOLDERS' EQUITY		
Short-term debt	\$ 45,454	\$ —
Accounts payable	34,328	61,184
Accrued liabilities	135,153	124,051
Deferred income on shipments to distributors	91,730	84,816
Total current liabilities	306,665	270,051
Pension accrual	599	871
Deferred tax liability	24,556	30,704
Stockholders' equity:		
Preferred stock, \$.001 par value; authorized 5,000,000 shares; no shares issued or outstanding.	—	—

Common stock, \$.001 par value; authorized 450,000,000 shares; issued 208,556,546 and outstanding 207,738,214 shares at March 31, 2005; issued 208,556,546 and outstanding 206,589,038 shares at March 31, 2004	208	207
Additional paid-in capital	532,666	558,354
Accumulated other comprehensive (loss) income	(9,718)	733
Retained earnings	984,095	813,307
Less shares of common stock held in treasury at cost; 818,332 shares at March 31, 2005 and 1,967,508 shares at March 31, 2004.	(21,517)	(52,084)
Net stockholders' equity	<u>1,485,734</u>	<u>1,320,517</u>
Total liabilities and stockholders' equity	<u>\$ 1,817,554</u>	<u>\$ 1,622,143</u>

See accompanying notes to consolidated financial statements

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MICROCHIP TECHNOLOGY INCORPORATED AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME

(in thousands, except per share amounts)

	Year Ended March 31,		
	2005	2004	2003
Net sales	\$ 846,936	\$ 699,260	\$ 651,462
Cost of sales	362,961	349,301	299,227
Gross profit	<u>483,975</u>	<u>349,959</u>	<u>352,235</u>
Operating expenses:			
Research and development	93,040	85,389	87,963
Selling, general and administrative	111,188	92,411	89,355
Special charges	21,100	865	50,800
	<u>225,328</u>	<u>178,665</u>	<u>228,118</u>
Operating income	258,647	171,294	124,117
Other income (expense):			
Interest income	17,804	4,888	3,837
Interest expense	(940)	(249)	(493)
Other, net	1,757	1,963	871
	<u>277,268</u>	<u>177,896</u>	<u>128,332</u>
Income before income taxes	277,268	177,896	128,332
Income tax provision	63,483	40,634	28,657
Income before cumulative effect of change in accounting principle	213,785	137,262	99,675
Cumulative effect of change in accounting principle, net of income tax benefit of \$6,645	—	—	11,443
Net income	<u>\$ 213,785</u>	<u>\$ 137,262</u>	<u>\$ 88,232</u>
Basic income per common share:			
Income before cumulative effect of change in accounting principle	\$ 1.03	\$ 0.67	\$ 0.49
Cumulative effect of change in accounting principle	—	—	(0.05)
Basic income per common share	<u>\$ 1.03</u>	<u>\$ 0.67</u>	<u>\$ 0.44</u>
Diluted income per common share:			
Income before cumulative effect of change in accounting principle	\$ 1.01	\$ 0.65	\$ 0.47
Cumulative effect of change in accounting principle	—	—	(0.05)
Diluted income per common share	<u>\$ 1.01</u>	<u>\$ 0.65</u>	<u>\$ 0.42</u>
Dividends declared per common share	\$ 0.208	\$ 0.113	\$ 0.040
Weighted average common share outstanding	<u>206,740</u>	<u>206,032</u>	<u>202,483</u>
Weighted average common and potential common shares outstanding	<u>211,962</u>	<u>212,172</u>	<u>210,646</u>

See accompanying notes to consolidated financial statements

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MICROCHIP TECHNOLOGY INCORPORATED AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

Year ended March 31,

	2005	2004	2003
Cash flows from operating activities:			
Net income	\$ 213,785	\$ 137,262	\$ 88,232
Adjustments to reconcile net income to net cash provided by operating activities:			
Gain on sale of fixed assets	(1,224)	(1,097)	(555)
Loss on write-down of fixed assets	—	—	2,165
Cumulative effect of change in accounting principle	—	—	11,443
Special charges:			
Accelerated depreciation – Fab 1	—	30,608	—
Fab 1 severance and shutdown charges	—	598	—
Special charges – operating expenses	—	645	—
In-process research and development	—	—	9,300
Fab 3 impairment charge	—	—	41,500
Depreciation and amortization	120,466	111,627	111,076
Deferred income taxes	16,869	(12,188)	(17,101)
Tax benefit from exercise of stock options	15,296	37,639	17,951
Changes in operating assets and liabilities:			
Increase in accounts receivable	(5,198)	(12,503)	(13,520)
(Increase) decrease in inventory	(9,214)	7,357	(13,230)
Increase in deferred income on shipments to distributors	6,914	13,828	12,100
Increase in accounts payable and accrued liabilities	1,178	30,901	13,129
Change in other assets and liabilities	(6,162)	(1,597)	(2,303)
Net cash provided by operating activities	352,710	343,080	260,187
Cash flows from investing activities:			
Purchases of short-term investments	(1,061,237)	(1,291,676)	(1,078,925)
Sales and maturities of short-term investments	752,060	1,085,934	1,023,373
Investment in other assets	—	(700)	(6,032)
Proceeds from sale of assets	1,659	2,329	608
Purchase of Fab 4	—	—	(184,717)
PowerSmart acquisition, net of cash acquired	—	—	(50,674)
Capital expenditures	(63,211)	(63,507)	(80,387)
Net cash used in investing activities	(370,729)	(267,620)	(376,754)
Cash flows from financing activities:			
Payment of cash dividend	(42,997)	(23,321)	(8,129)
Repurchase of common stock	(68,276)	(53,864)	(26,520)
Proceeds from short-term borrowings	45,454	—	—
Proceeds from sale of common stock	47,234	53,150	31,528
Net cash used in financing activities	(18,585)	(24,035)	(3,121)
Net (decrease) increase in cash and cash equivalents	(36,604)	51,425	(119,688)
Cash and cash equivalents beginning of year	105,334	53,909	173,597
Cash and cash equivalents end of year	\$ 68,730	\$ 105,334	\$ 53,909

See accompanying notes to consolidated financial statements

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MICROCHIP TECHNOLOGY INCORPORATED AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(in thousands)

	Common Stock and Additional Paid-in Capital		Common Stock held in Treasury		Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Net Stockholders' Equity
	Shares	Amount	Shares	Amount			
Balance at March 31, 2002	200,803	\$ 459,504	173	\$ (2,979)	\$ —	\$ 619,254	\$ 1,075,779
Net and comprehensive income	—	—	—	—	—	88,232	88,232
Exercise of stock options and assumption of stock options in connection with PowerSmart acquisition	3,565	23,588	—	—	—	—	23,588
Employee stock purchase plan	503	8,511	—	—	—	—	8,511
Purchase of treasury stock	—	—	1,265	(27,063)	—	—	(27,063)
Treasury stock used for new issuances	(1,126)	(23,107)	(1,126)	23,107	—	—	—
Tax benefit from exercise of stock options	—	17,951	—	—	—	—	17,951
Acquisition-related unearned stock compensation, net of \$59 of amortization	—	71	—	—	—	—	71
Cash dividend	—	—	—	—	—	(8,120)	(8,120)
Balance at March 31, 2003	203,745	486,518	312	(6,935)	—	699,366	1,178,949
Components of comprehensive income:							
Net Income	—	—	—	—	—	137,262	137,262
Net unrealized gains on available-for-sale investments, net of \$139 of tax	—	—	—	—	733	—	733
Total comprehensive income	—	—	—	—	—	—	137,995
Exercise of stock options	5,114	44,986	—	—	—	—	44,986
Employee stock purchase plan	477	8,154	—	—	—	—	8,154
Purchase of treasury stock	—	—	2,435	(63,931)	—	—	(63,931)
Treasury stock used for new issuances	(780)	(18,782)	(780)	18,782	—	—	—
Tax benefit from exercise of stock options	—	37,639	—	—	—	—	37,639
Unearned compensation amortization	—	46	—	—	—	—	46

Cash dividend	—	—	—	—	—	(23,321)	(23,321)
Balance at March 31, 2004	208,556	558,561	1,967	(52,084)	733	813,307	1,320,517
Components of comprehensive income:							
Net Income	—	—	—	—	—	213,785	213,785
Net unrealized losses on available-for-sale investments, net of \$2,068 of tax	—	—	—	—	(10,451)	—	(10,451)
Total comprehensive income	—	—	—	—	—	—	203,334
Exercise of stock options	2,882	36,831	—	—	—	—	36,831
Employee stock purchase plan	452	10,403	—	—	—	—	10,403
Purchase of treasury stock	—	—	2,185	(57,666)	—	—	(57,666)
Treasury stock used for new issuances	(3,334)	(88,233)	(3,334)	88,233	—	—	—
Tax benefit from exercise of stock options	—	15,296	—	—	—	—	15,296
Unearned compensation amortization	—	16	—	—	—	—	16
Cash dividend	—	—	—	—	—	(42,997)	(42,997)
Balance at March 31, 2005	208,556	\$ 532,874	818	\$ (21,517)	\$ (9,718)	\$ 984,095	\$ 1,485,734

See accompanying notes to consolidated financial statements

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MICROCHIP TECHNOLOGY INCORPORATED AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. SIGNIFICANT ACCOUNTING POLICIES

Nature of Business

Microchip develops and manufactures specialized semiconductor products used by its customers for a wide variety of embedded control applications. Microchip's product portfolio comprises the PICmicro[®] field-programmable (FLASH) RISC microcontrollers, which serve 8-bit and 16-bit embedded control applications, and a broad spectrum of high-performance linear and mixed-signal, power management and thermal management devices. Microchip also offers complementary microperipheral products including interface devices, Serial EEPROMs, and application-specific standard products (ASSPs). This synergistic product portfolio targets thousands of applications and a growing demand for high-performance designs in the automotive, communications, computing, consumer and industrial control markets.

Principles of Consolidation

The consolidated financial statements include the accounts of Microchip Technology Incorporated and its wholly-owned subsidiaries ("Microchip" or the "Company"). The Company does not have any subsidiaries in which it does not own 100% of the outstanding stock. All of the Company's subsidiaries are included in the consolidated financial statements. All significant intercompany accounts and transactions have been eliminated in consolidation.

Change in Accounting Principle

On March 18, 2003, the Company announced that it would change its revenue recognition policy relating to regional Asian distributors from Point of Purchase (POP), or when the Company ships product to these distributors, to Point of Sale (POS), or when those distributors sell the Company's products to their customers. The change in accounting principle is preferable because: (i) it better reflects the substance of end customer demand for the Company's products, and will better focus the Company on, and allow investors to better understand, end user demand trends for its products; (ii) it provides uniformity in the revenue recognition policy of the Company; and (iii) the new accounting method is consistent with other companies in the semiconductor industry and, therefore, provides greater comparability in the presentation of financial results among the Company and its peers. To implement the change in revenue recognition, the Company recorded a cumulative effect of change in accounting principle charge of \$11.4 million (net of income taxes of \$6.6 million) as of April 1, 2002.

Revenue Recognition

The Company recognizes revenue when the earnings process is complete, as evidenced by an agreement with the customer, transfer of title as well as fixed pricing and probable collectability. The Company recognizes revenue from product sales to OEMs upon shipment and records reserves for estimated customer returns. Distributors worldwide generally have broad price protection and product return rights, so the Company defers revenue recognition until the distributor sells the product to their customer. The Company reduces product pricing through price protection based on market conditions, competitive considerations and other factors. Price protection is granted to third-party distributors on the inventory they have on hand at the date the price protection is offered. When the Company reduces the price of its products, it allows the distributor to claim a credit against its outstanding accounts receivable balances based on the new price of the inventory it has on hand as of the date of the price reduction. There is no revenue impact from the price protections. The Company also grants certain credits to its third-party distributors. The credits are granted to the distributors on specially identified pieces of the distributors' business to allow them to earn a competitive gross margin on the sale of the Company's products to their end customers. The credits are on a per unit basis and are not given to the distributor until they provide information regarding the sale to their end customer. The effect of granting these credits establishes the net selling price from the Company to its distributors for the product and results in the net revenue recognized by the Company when the product is sold by the distributors to their end customers. Upon shipment, amounts billed to distributors are included as accounts receivable, inventory is relieved, the sale and the gross margin are deferred and reflected as a current liability until the product is sold by the distributor to its customers. Shipping charges billed to customers are included in net sales, and the related shipping costs are included in cost of sales.

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Product Warranty

The Company generally sells products with a limited warranty related to product quality and a limited indemnification of customers against intellectual property infringement claims related to the Company's products. Due to comprehensive product testing, the short time between product shipment and the detection and correction of product failures, and a low historical rate of payments on indemnification claims, the accrual based on historical activity and the related expense were not significant as of and for the fiscal years presented.

Advertising Costs

The Company expenses all advertising costs as incurred. Advertising costs were not material in the years ended March 31, 2005, 2004 and 2003.

Research and Development

Research and development costs are expensed as incurred. Research and development expenses include expenditures for labor, masks, prototype wafers, and expenses for development of process technologies, new packages, and software to support new products and design environments.

Foreign Currency Translation and Forward Contracts

The Company's foreign subsidiaries are considered to be extensions of the U.S. Company and any translation gains and losses related to these subsidiaries are included in other income and expense. As the U.S. dollar is utilized as the functional currency, gains and losses resulting from foreign currency transactions (transactions denominated in a currency other than the subsidiaries' functional currency) are also included in income. Gains and losses associated with currency rate changes on forward contracts are recorded currently in income. These gains and losses have historically been immaterial to the Company's financial statements.

Income Taxes

As part of the process of preparing its consolidated financial statements, the Company is required to estimate its income taxes in each of the jurisdictions in which it operates. This process involves estimating the Company's actual current tax exposure together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within the Company's consolidated balance sheet. The Company must then assess the likelihood that its deferred tax assets will be recovered from future taxable income and to the extent it believes that recovery is not likely, it must establish a valuation allowance. The Company has not provided for a valuation allowance because management currently believes that it is "more likely than not" that its deferred tax assets will be recovered from future taxable income.

Cash and Cash Equivalents

All highly liquid investments, including marketable securities purchased with a remaining maturity of three months or less when acquired are considered to be cash equivalents.

Short-Term Investments

The Company's investments are classified as available-for-sale. The Company defines short-term investments as income yielding securities, which can be readily converted to cash. Short-term investments consist of government agency bonds, municipal bonds, corporate preferred stock, state student loan bonds and fixed rate annuity contracts. These investments are carried at fair value with unrealized gains and losses reported in stockholders' equity. Realized gains and losses are included in interest income. The cost of securities sold is based upon the specific identification method.

Allowance for Doubtful Accounts

The Company maintains an allowance for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments, which is included in bad debt expense. The Company determines the adequacy of this allowance by regularly reviewing the composition of its accounts receivable aging and evaluating individual customer receivables, considering such customer's financial condition, credit history and current economic conditions.

Inventories

Inventories are valued at the lower of cost or market using the first-in, first-out (FIFO) method. The Company writes down its inventory for estimated obsolescence or unmarketable inventory in an amount equal to the difference between the cost of inventory and the estimated market value based upon assumptions about future demand and market conditions. If actual market conditions are less favorable than those projected by the Company, additional

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inventory write-downs may be required. Inventory impairment charges establish a new cost basis for inventory and charges are not subsequently reversed to income even if circumstances later suggest that increased carrying amounts are recoverable. In estimating reserves for obsolescence, the Company primarily evaluates estimates of demand over a 12-month period and provides reserves for inventory on hand in excess of the estimated 12-month demand.

Property, Plant and Equipment

Property, plant and equipment are stated at cost. Major renewals and improvements are capitalized, while maintenance and repairs are expensed when incurred. The Company's property and equipment accounting policies incorporate estimates, assumptions and judgments relative to the useful lives of its property and equipment. Depreciation is provided for assets placed in service on a straight-line basis over the estimated useful lives of the relative assets, which range from 3 to 30 years. The Company evaluates the carrying value of its property and equipment when events or changes in circumstances indicate that the carrying value of such assets may be impaired. Asset impairment evaluations are, by nature, highly subjective.

Litigation

The Company's estimated range of liability related to certain pending litigation is based on claims for which management believes a loss is probable and it can estimate the amount or range of loss. Because of the uncertainties related to both the amount and range of the loss on the remaining pending litigation, the Company is unable to make a reasonable estimate of the liability that could result from an unfavorable outcome. As additional information becomes available, the Company will assess the potential liability related to its pending litigation and revise its estimates, if necessary.

Goodwill

Goodwill is recorded when the purchase price paid for an acquisition exceeds the estimated fair value of the net identified tangible and intangible assets acquired. The Company is required to perform an annual impairment review, and more frequently under certain circumstances. The goodwill is subjected to this test during the fourth quarter of the Company's fiscal year. The Company engages primarily in the design, development, manufacture and marketing of semiconductor products and, as a result, the Company concluded there is one reporting unit. The impairment review process compares the fair value of the reporting unit to its carrying value. If the Company determines through the impairment process that goodwill has been impaired, the Company will record the impairment charge in the statement of income. As of March 31, 2005, there was no impairment charge related to goodwill. There can be no assurance that future goodwill impairment tests will not result in a charge to earnings.

Impairment of Long-Lived Assets

The Company assesses whether indicators of impairment of long-lived assets are present. If such indicators are present, the Company determines whether the sum of the estimated undiscounted cash flows attributable to the assets in question is less than their carrying value. If less, the Company recognizes an impairment loss based on the excess of the carrying amount of the assets over their respective fair values. Fair value is determined by discounted future cash flows, appraisals or other methods. If the assets determined to be impaired are to be held and used, the Company recognizes an impairment loss through a charge to operating results to the extent the present value of anticipated net cash flows attributable to the asset are less than the asset's carrying value. The Company would depreciate the remaining value over the remaining estimated useful life of the asset.

Share-Based Payment

The Company grants stock options for a fixed number of shares to certain employees and directors with an exercise price equal to the fair market value of the shares at the date of grant. The Company accounts for stock option grants in accordance with Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees" and related Interpretations, and, accordingly, recognizes no compensation expense for the stock option grants.

The following table represents the effect on net income and earnings per share (shown in thousands, except for per share amounts) if the Company had applied the fair value based method and recognition provisions of SFAS No. 123, "Accounting for Stock-Based Compensation," to share-based employee and director compensation. For purposes of this pro forma disclosure, the value of the options is estimated using a Black-Scholes option pricing model and amortized ratably to expense over the options' vesting periods. Because the estimated value is determined as of the date of grant, the actual value ultimately realized by the employee may be significantly different.

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	Year Ended March 31,		
	2005	2004	2003
Net income, as reported	\$ 213,785	\$ 137,262	\$ 88,232
Deduct: Total share-based employee compensation expense determined under fair value methods for all awards, net of related tax effects	37,211	36,821	36,151
Pro forma net income	\$ 176,574	\$ 100,441	\$ 52,081
Net income per common share:			
Basic, as reported	\$ 1.03	\$ 0.67	\$ 0.44
Basic, pro forma	\$ 0.85	\$ 0.49	\$ 0.26
Diluted, as reported	\$ 1.01	\$ 0.65	\$ 0.42
Diluted, pro forma	\$ 0.83	\$ 0.47	\$ 0.25
Weighted average shares used in computation:			
Basic	206,740	206,032	202,483
Diluted	211,962	212,172	210,646

See Note 17 for further discussion of the Company's equity incentive plan.

At a meeting held on February 17, 2005, the Compensation Committee of the Board of Directors and the Board of Directors of the Company approved the acceleration of the vesting of certain Company stock options with an option price of \$27.153 per share or greater. The purpose of the accelerated vesting was to enable the Company to avoid recognizing in its income statement compensation expense associated with these options in future periods, upon adoption of SFAS No. 123R (Share-Based Payment) in April 2006. The pre-tax charge to be avoided amounts to approximately \$13.7 million and represents the fair of the unvested awards as of the date of the acceleration as determined under SFAS No. 123. This amount would otherwise have been required to be recognized as compensation expense over the vesting period upon adoption of SFAS No. 123R. As a result of the accelerated vesting, approximately 2.3 million option shares or 25.4% of the total number of the outstanding unvested option shares with varying remaining vesting schedules became immediately exercisable. In order to help avoid unintended personal benefits to the holders of the accelerated options, any shares received through the exercise of accelerated options may not be sold by the option holder until the first to occur of the original vesting date of the accelerated option or the termination of the employment of the option holder. In connection with the accelerated vesting, each option agreement underlying such options was amended. As of the date of the acceleration, the fair market value of the Company's common stock was below the option price of the accelerated options in all material respects, so no APB 25 charges were incurred and future potential charges are immaterial.

Concentrations of Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of investments in debt securities and trade receivables. The Company generally places its investments with high-credit quality counterparties. Investments in debt securities with original maturities of greater than six months consist primarily of AAA rated financial instruments and counterparties. The Company's investments are primarily in direct obligations of the United States government or its agencies.

Concentrations of credit risk with respect to accounts receivable are generally not significant due to the diversity of the Company's customers and geographic sales areas. The Company sells its products primarily to OEMs and distributors in the Americas, Europe and Asia. The company performs ongoing credit evaluations of its customers' financial condition and requires collateral, primarily letters of credit, as deemed necessary. No single end customer accounted for 10% or more of the Company's net sales or accounts receivable balances during the years ended March 31, 2005, 2004 and 2003. The Company had two distributors that accounted for more than 10% of its net sales in the year ended March 31, 2005. See Note 19, Geographic Information, for additional information on the Company's largest distributors.

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Use of Estimates

The Company has made a number of estimates and assumptions relating to the reporting of assets, liabilities, revenues and expenses and the disclosure of contingent assets and liabilities to prepare the consolidated financial statements in conformity with accounting principles generally accepted in the U.S. Actual results could differ from those estimates.

Recently Issued Accounting Pronouncements

During December 2004, the FASB issued SFAS No. 123R, which requires companies to measure and recognize compensation expense for all share-based payments at fair value. Share-based payments include stock option grants. The Company grants options to purchase common stock to some of our employees and directors under our stock option plan at prices equal to the market value of the stock on the dates the options were granted. SFAS No. 123R is effective for the Company beginning April 1, 2006. Early adoption of the provisions of SFAS No. 123R is encouraged, but not required. The Company has not yet adopted this pronouncement and is currently evaluating the expected impact that the adoption of SFAS No. 123R will have on our consolidated financial position and results of operations. The adoption of SFAS No. 123R is expected to have an unfavorable impact on the consolidated results of operations and net income per common share. SFAS No. 123R also requires the benefits of tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as an operating cash flow as required under current literature. This requirement will reduce net operating cash flows and increase net financing cash flows in periods after adoption. The Company cannot estimate what those amounts will be in the future because they depend on, among other things, when employees exercise stock options.

FASB Staff Position (“FSP”) No. 109-2, “Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004” (“FSP 109-2”), provides guidance under FASB Statement No. 109, “Accounting for Income Taxes,” (“SFAS No. 109”) with respect to recording the potential impact of the repatriation provisions of the American Jobs Creation Act of 2004 (the “Jobs Creation Act”) on enterprises’ income tax expense and deferred tax liability. The Jobs Creation Act was enacted on October 22, 2004. FSP 109-2 states that an enterprise is allowed time beyond the financial reporting period of enactment to evaluate the effect of the Jobs Act on its plan for reinvestment or repatriation of foreign earnings for purposes of applying SFAS No. 109. As of March 31, 2005, the Company is in the process of evaluating whether it will repatriate any foreign earnings and, if so, the amount that it will repatriate. However, the Company does not expect to be able to complete this evaluation until later in fiscal 2006. Accordingly, as provided for in FSP 109-2, the Company has not adjusted our tax expense or deferred tax liability to reflect the repatriation provisions of the Jobs Creation Act. The Jobs Creation Act also provides a deduction for income from qualified domestic production activities, to be phased in from 2005 through 2010, which is intended to replace the existing extra-territorial income exclusion for foreign sales. In FSP 109-1, the FASB decided the deduction for qualified domestic production activities should be accounted for as a special deduction under SFAS No. 109, rather than as a rate reduction. Accordingly, any benefit from the deduction will be reported in the period in which the deduction is claimed on the tax return and no adjustment to deferred taxes at March 31, 2005, is required.

In March 2004, the FASB approved the consensus reached on the Emerging Issues Task Force (EITF) Issue No. 03-1, “The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments” (“EITF 03-1”). The Issue’s objective is to provide guidance for identifying other-than-temporarily impaired investments. EITF 03-1 also provides new disclosure requirements for investments that are deemed to be temporarily impaired. In September 2004, the FASB issued FSP EITF 03-1-1 that delays the effective date of the measurement and recognition guidance in EITF 03-1 until further notice. The disclosure requirements of EITF 03-1 are effective with this annual report for fiscal 2005. Once the FASB reaches a final decision on the measurement and recognition provisions, the Company will evaluate the impact of the adoption of the accounting provisions of EITF 03-1.

In December 2004, the FASB also issued SFAS No. 151, “Inventory Costs, an amendment of ARB No. 43, Chapter 4,” which will become effective for the Company beginning January 1, 2006. This standard clarifies that abnormal amounts of idle facility expense, freight, handling costs and wasted material should be expensed as incurred and not included in overhead. In addition, this standard requires that the allocation of fixed production overhead costs to inventory be based on the normal capacity of the production facilities. The Company is currently evaluating the potential impact of this standard on its financial position and results of operations, but does not believe the impact of the change will be material.

Reclassifications

Certain prior year amounts have been reclassified to conform with the current period presentation.

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2. ACQUISITION OF GRESHAM, OREGON WAFER FABRICATION FACILITY

On August 23, 2002, the Company completed its acquisition of a semiconductor manufacturing complex in Gresham, Oregon. The Company acquired the facility for \$183.5 million in cash plus direct acquisition costs of approximately \$1.2 million. The facility is situated on an approximately 140-acre campus east of Portland and comprises approximately 826,500 square feet. The facility came equipped with approximately 350 process tools and 170 support tools. The Company is currently producing 8-inch wafers on its 0.5 micron process technology at the Gresham facility. The facility also houses offices, meeting rooms and support functions. The Company began production activities on October 31, 2003 at this facility. As of March 31, 2005, all of the buildings and supporting facilities were being depreciated as well as the manufacturing equipment that had been placed in service. All manufacturing equipment that was not being used in production activities was maintained in projects in process since the Company believes there is no change to their utility from the present time until they are placed into productive service. The lives to be used for depreciating this equipment at this facility will be evaluated at such time as the assets are placed in service. The temporary idling of such assets has not impaired the estimated life or carrying values of the underlying assets.

3. ACQUISITION OF POWERSMART, INC.

On June 5, 2002, the Company completed the acquisition of PowerSmart, Inc. in which the Company acquired all of PowerSmart’s outstanding capital stock and assumed certain stock options for consideration of \$54.0 million in cash plus other acquisition-related costs of \$1.2 million. The acquisition was accounted for as a purchase business combination in accordance with SFAS No. 141, *Business Combinations*, and accordingly, the results of PowerSmart’s operations are included in the Company’s consolidated results from the date of the acquisition. The acquisition was not considered significant under the rules and regulations of the SEC (Rule 3-05 of Regulation S-X).

The purchase price was allocated among PowerSmart’s tangible and intangible assets, in-process research and development and goodwill. Management determined the value assigned to the assets acquired through various methods including assistance from a third-party appraisal. An allocation of \$9.3 million of the purchase price was assigned to in-process research and development and was written off at the date of the acquisition. The amount paid in excess of the fair value of the net tangible assets has been allocated to separately identifiable intangible assets based upon an independent valuation analysis. An allocation of \$5.6 million of the purchase price was made to core technology and other identifiable intangible assets and is being amortized over an estimated useful life of seven years. An allocation of approximately \$32.3 million of the purchase price was made to goodwill. None of the goodwill is deductible for tax purposes. The goodwill related to the PowerSmart acquisition was reduced by \$0.4 million to \$31.9 million in the year ended March 31, 2005 due to a favorable settlement of a liability that was recorded as of the original acquisition date.

The Company records acquisition-related purchase consideration as unearned stock-based compensation. During the year ended March 31, 2003, the Company recorded unearned stock-based compensation of \$130,000. The unearned stock-based compensation includes the intrinsic value of stock options assumed in connection with the acquisition of PowerSmart that is earned as the employees provide future services. The compensation is being recognized over the period earned, and the expense is included in the amortization of acquisition-related intangibles and costs. Amortization of unearned stock compensation was \$16,000 in fiscal 2005, \$46,000 in fiscal 2004 and \$59,000 in fiscal 2003.

4. SPECIAL CHARGES

The components of special charges are (in thousands):

	Year Ended March 31,		
	2005	2004	2003
Patent license settlement	\$ 21,100	\$ —	\$ —
Contract cancellation, severance and other costs related to Fab 1 closure	—	865	—
Fab 3 impairment charge	—	—	41,500
In-process research and development	—	—	9,300
Totals	\$ 21,100	\$ 865	\$ 50,800

Fiscal 2005

Settlement with U.S. Philips Corporation

The Company reached an agreement with U.S. Philips Corporation and Philips Electronics North America Corp. (together "Philips") regarding patent license litigation with Philips which was ongoing from October 2001 to October 2004. The agreement included dismissal of the then pending litigation and the cross-license of certain patents between Philips and the Company. The Company recorded a special charge of \$21.1 million in the quarter that ended June 30, 2004 associated with this matter. Pursuant to this cross-license, the Company licensed certain of its patents related to 8-pin microcontrollers to Philips, and Philips licensed its patents related to I²C serial communications to the Company, each on fully-paid up, non-royalty bearing worldwide licenses. The Company finalized and executed the definitive settlement agreement related to this matter and made the cash payment to Philips during the fiscal quarter ending September 30, 2004.

Fiscal 2004

Closure of Fab 1

On April 7, 2003, the Company announced its intention to close its Chandler, Arizona (Fab 1) wafer fabrication facility and integrate certain Fab 1 personnel and processes into its Tempe, Arizona (Fab 2) wafer fabrication facility. The Company completed this integration process during the three-month period ended June 30, 2003. The closure of Fab 1 and the integration of certain Fab 1 personnel into Fab 2 operations resulted in a reduction in force of 207 employees who were either directly involved in the Company's manufacturing operations or provided support functions to Fab 1. The detail of the charges incurred related to the closure of Fab 1 that were included in cost of sales for the three-month period ended June 30, 2003 is as follows (amounts in thousands):

Accelerated depreciation for Fab 1	\$ 30,608
Fab 1 related charges including severance, material and other costs	1,147
Total charges in cost of sales	\$ 31,755

The facility where Fab 1 was located is an integral part of the Company's overall campus in Chandler, Arizona. Within this same facility resides the Company's wafer probe, mask making and other manufacturing related activities. Consequently it is not possible to abandon or otherwise dispose of this facility. The accelerated depreciation that was taken only related to assets used in the wafer fabrication operations at the facility. The Company has no specific plans for utilizing the space formerly housing the wafer fabrication operations, and intends to leave it in an idle state. The property, plant and equipment that was subject to the accelerated depreciation is reflected in the gross and accumulated depreciation carrying values in the property, plant and equipment section of the Company's balance sheet and related footnote disclosures.

The Company incurred \$865,000 of special charges recorded principally for contract cancellation, severance and other costs related to the closure of Fab 1 and other actions.

Fiscal 2003

Fab 3 Impairment Charge

The Company recorded a \$41.5 million asset impairment charge during the quarter ended September 30, 2002, as described below.

The Company acquired a semiconductor manufacturing facility in Puyallup, Washington, referred to as Fab 3, in July 2000. The original purchase consisted of semiconductor manufacturing facilities and real property. It was the Company's intention to bring Fab 3 to productive readiness and commence volume production of 8-inch wafers using its 0.7 and 0.5 micron process technologies by August 2001. The Company delayed its intended production start up at Fab 3 due to deteriorating business conditions in the semiconductor industry during fiscal 2002. Fab 3 has never been brought to productive readiness.

As is described in Note 2, in August 2002 the Company acquired a semiconductor manufacturing facility in Gresham, Oregon, referred to as Fab 4. After the acquisition of Fab 4 was completed, the Company undertook an analysis of the potential production capacity at Fab 4. The results of the production capacity analysis at that time led the Company to determine that Fab 3's capacity would not be needed in the foreseeable future and during the second quarter of fiscal 2003 the Company committed to a plan to sell Fab 3. The Company subsequently retained a third-party broker to market Fab 3 on its behalf and began actively seeking potential buyers. Accordingly, Fab 3 was classified as an asset held-for-sale as of September 30, 2002 and maintained that classification until March 31, 2005.

Management determined the value assigned to the Fab 3 assets through various methods including assistance from a third-party appraisal. The independent third party used the market approach and considered sales of comparable properties in determining the fair value of Fab 3. The comparable sales included eight properties, including the Company's purchases of Fab 3 in July 2000 and Fab 4 in August 2002. Based on the results of this appraisal, the Company recorded an asset impairment

charge on Fab 3 of \$36.9 million, including estimated costs to sell. The remaining value of \$60.2 million was classified as an asset held-for-sale and was included as a component of other current assets until March 31, 2005.

During the quarter ended September 30, 2002, the Company recorded an asset impairment charge of \$4.6 million to write-down certain excess manufacturing equipment located at Fab 3 to its net realizable value of \$0.2 million. This manufacturing equipment became “excess” as a result of duplicate equipment acquired in the purchase of Fab 4. The net realizable value for the excess manufacturing equipment was determined based on management estimates. Substantially all of the other manufacturing equipment located at Fab 3 has been transferred to and will be used in the Company’s other wafer fabrication facilities located in Tempe, Arizona (Fab 2) and Gresham, Oregon (Fab 4).

At March 31, 2005, the Company changed the classification of Fab 3 from an asset held-for-sale to an asset held-for-future-use. Fab 3 had been on the market for over two years, and the Company had not received any acceptable offers on the facility. Over that period of time, the Company’s business had increased significantly and over the next several years the Company will need to begin planning for future wafer fabrication capacity as a larger percentage of Fab 4’s clean room capacity is utilized. The Company determined that the appropriate action to take was to stop actively marketing the Fab 3 facility and hold it for its future use. As a result of this change in classification, the Company had to assess the fair value of the Fab 3 asset to determine if any additional impairment charge was required upon the change in classification from “held-for-sale” to “held-for-future-use” under SFAS 144. The Company performed a discounted cash flow analysis of the Fab 3 asset based on various financial projections in developing the fair value estimate given that it was the best available valuation technique for the asset. The discounted cash flow analysis confirmed the carrying value of the Fab 3 asset at March 31, 2005 was not in excess of its fair value. The Company will begin to depreciate the Fab 3 asset in April 2005.

PowerSmart In-Process Research and Development Charge

As described in Note 3, an allocation of \$9.3 million of the purchase price was assigned to in-process research and development and was written off at the date of the acquisition in accordance with FASB Interpretation No. 4, “Applicability of FASB Statement No. 2, *Business Combinations Accounted for by the Purchase Method*.”

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5. **SHORT-TERM INVESTMENTS**

The Company’s short-term investments are intended to establish a high-quality portfolio that preserves principal, meets liquidity needs, avoids inappropriate concentrations and delivers an appropriate yield in relationship to the Company’s investment guidelines and market conditions. Short-term investments consist of corporate and various government agency and municipal debt securities. Management classifies the Company’s short-term investments as available-for-sale. Available-for-sale securities are carried at fair value with unrealized gains and losses reported in stockholders’ equity. Realized gains and losses and declines in value judged to be other than temporary, if any, are included in operations. A decline in the market value of any available-for-sale security below cost that is deemed to be other than temporary, results in an impairment in the fair value of the investment. The impairment is charged to earnings and a new cost basis for the security is established. Premiums and discounts are amortized or accreted over the life of the related available-for-sale security. Dividend and interest income are recognized when earned. The cost of security sold is calculated using the specific identification method. The following is a summary of available-for-sale securities at March 31, 2005 (amounts in thousands):

	Adjusted Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Government agency bonds	\$ 639,720	\$ —	\$ 11,601	\$ 628,119
Municipal bonds	3,626	—	46	3,580
Corporate preferred stock	34,175	—	—	34,175
	<u>\$ 677,521</u>	<u>\$ —</u>	<u>\$ 11,647</u>	<u>\$ 665,874</u>

The following is a summary of available-for-sale securities at March 31, 2004 (amounts in thousands):

	Adjusted Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
State student loan bonds	\$ 15,600	\$ —	\$ —	\$ 15,600
Government agency bonds	338,491	872	—	339,363
Municipal bonds	3,706	—	—	3,706
Corporate preferred stock	3,000	—	—	3,000
Fixed rate annuity contracts	7,547	—	—	7,547
	<u>\$ 368,344</u>	<u>\$ 872</u>	<u>\$ —</u>	<u>\$ 369,216</u>

The Company’s unrealized losses of \$11.6 million were due to fluctuations in interest rates. Management does not believe any of the unrealized losses represented an other-than-temporary impairment based on its evaluation of available evidence as of March 31, 2005.

During the year ended March 31, 2005, the Company did not have any gross realized gains or losses on sales of available-for-sale securities. During the year ended March 31, 2004, the Company had a gross realized gain of \$8,000 on sales of available-for-sale securities.

The amortized cost and estimated fair value of the available-for-sale securities at March 31, 2005, by maturity, are shown below (amounts in thousands). Expected maturities can differ from contractual maturities because the issuers of the securities may have the right to prepay obligations without prepayment penalties, and the Company views its available-for-sale securities as available for current operations.

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	Adjusted Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-sale				
Due in one year or less	\$ 76,646	\$ —	\$ 531	\$ 76,115
Due after one year and through five years	566,700	—	11,116	555,584

Due after five years through ten years	—	—	—	—
Due after ten years	34,175	—	—	34,175
	<u>\$ 677,521</u>	<u>\$ —</u>	<u>\$ 11,647</u>	<u>\$ 665,874</u>

6. ACCOUNTS RECEIVABLE

Accounts receivable consists of the following (amounts in thousands):

	March 31,	
	2005	2004
Trade accounts receivable	\$ 116,689	\$ 111,548
Other	216	152
	<u>116,905</u>	<u>111,700</u>
Less allowance for doubtful accounts	<u>3,817</u>	<u>3,810</u>
	<u>\$ 113,088</u>	<u>\$ 107,890</u>

7. INVENTORIES

The components of inventories are as follows (amounts in thousands):

	March 31,	
	2005	2004
Raw materials	\$ 4,852	\$ 9,169
Work in process	73,295	57,589
Finished goods	25,581	27,756
	<u>\$ 103,728</u>	<u>\$ 94,514</u>

Inventory impairment charges establish a new cost basis for inventory and charges are not subsequently reversed to income even if circumstances later suggest that increased carrying amounts are recoverable.

8. OTHER CURRENT ASSETS

Other current assets consists of the following (amounts in thousands):

	March 31,	
	2005	2004
Assets held-for-sale	\$ —	\$ 60,414
Income tax receivable	—	6,862
Accrued interest receivable	6,273	1,341
Other current assets	1,730	5,444
	<u>\$ 8,003</u>	<u>\$ 74,061</u>

The assets held-for-sale at March 31, 2004 of \$60.4 million related primarily to Fab 3. These assets were reclassified to held-for-future-use at March 31, 2005 and are included in property, plant and equipment. See discussion of "Fab 3 Impairment Charge" in Footnote 4.

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9. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consists of the following (amounts in thousands):

	March 31,	
	2005	2004
Land	\$ 45,641	\$ 33,494
Building and building improvements	356,233	293,230
Machinery and equipment	938,261	852,087
Projects in process	84,846	145,070
	<u>1,424,981</u>	<u>1,323,881</u>
Less accumulated depreciation and amortization	<u>731,679</u>	<u>634,675</u>
	<u>\$ 693,302</u>	<u>\$ 689,206</u>

Property, plant and equipment at March 31, 2005 includes \$12.1 million in land and \$48.1 million in buildings and building improvements related to Fab 3. These assets were included in other current assets at March 31, 2004 since they were classified as assets held-for-sale prior to the Company's recent decision to retain them for future use (see Note 4).

Depreciation and amortization expense attributed to property, plant and equipment was \$119.0 million, \$109.8 million and \$109.6 million for the years ending March 31, 2005, 2004 and 2003, respectively. In addition to depreciation and amortization expense, accelerated depreciation charges of \$30.6 million in the year ended March 31, 2004, related to the Company's Fab 1 shutdown, are included in cost of sales.

10. INTANGIBLE ASSETS

The table below summarizes the gross carrying amounts and accumulated amortization of the Company's intangible assets (amounts in thousands):

		March 31, 2005	
	Gross Amount	Accumulated Amortization	Net Amount
Developed technology	\$ 14,566	\$ (8,793)	\$ 5,773
Distribution rights	4,804	(1,288)	3,516
	<u>\$ 19,370</u>	<u>\$ (10,081)</u>	<u>\$ 9,289</u>

		March 31, 2004	
	Gross Amount	Accumulated Amortization	Net Amount
Developed technology	\$ 13,566	\$ (7,846)	\$ 5,720
Distribution rights	4,804	(826)	3,978
	<u>\$ 18,370</u>	<u>\$ (8,672)</u>	<u>\$ 9,698</u>

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The Company amortizes intangible assets over their expected useful lives, which range between 1 and 10 years. The weighted average total amortization period for the Company's intangible assets at March 31, 2005 was 7 years, consisting of 6 years for developed technology and 10 years for distribution rights. The following is an expected amortization schedule for the intangible assets for the fiscal years March 31, 2006 through March 31, 2010, absent any future acquisitions or impairment charges (amounts in thousands):

Year Ending March 31,	Projected Amortization Expense
2006	\$ 1,403
2007	1,545
2008	1,646
2009	1,645
2010	978

The Company has not recorded any impairment losses associated with the intangible assets acquired.

11. SHORT-TERM DEBT

The Company had short-term debt of \$45.5 million as of March 31, 2005. The short-term debt is a result of repurchase agreements that are in place with two of the Company's investment brokerages. The short-term debt is collateralized with \$47.5 million of the Company's short-term investments. The short-term debt had a weighted average interest rate of 2.71% as of March 31, 2005. The Company used these borrowings to fund the activity under its stock repurchase programs beginning in the second quarter of the year ended March 31, 2005.

The Company has an unsecured line of credit with a financial institution in Asia for up to \$5.0 million (U.S. dollar equivalent). There were no borrowings against this line of credit as of March 31, 2005, but an allocation of \$0.4 million of the available line was made, relating to import guarantees associated with the Company's business in Thailand. There are no covenants associated with the foreign line of credit. The foreign line of credit is due to expire in July 2005.

12. ACCRUED LIABILITIES

Accrued liabilities consists of the following (amounts in thousands):

	March 31,	
	2005	2004
Income taxes	\$ 101,406	\$ 91,771
Other accrued expenses	33,747	32,280
	<u>\$ 135,153</u>	<u>\$ 124,051</u>

13. INCOME TAXES

The provision for income taxes is as follows (amounts in thousands):

	Year Ended March 31,		
	2005	2004	2003
Current expense:			
Federal	\$ 34,320	\$ 37,580	\$ 32,602
State	3,436	3,268	2,835
Foreign	8,858	11,974	10,321
Total current	<u>46,614</u>	<u>52,822</u>	<u>45,758</u>
Deferred expense (benefit):			
Federal	5,908	(3,795)	(19,892)
State	591	(330)	(1,730)
Foreign	10,370	(8,063)	(2,124)
Total deferred	<u>16,869</u>	<u>(12,188)</u>	<u>(23,746)</u>

Less: deferred tax benefit allocated to cumulative effect of accounting method	—	—	6,645
	<u>\$ 63,483</u>	<u>\$ 40,634</u>	<u>\$ 28,657</u>

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The tax benefit associated with the exercise of employee stock options reduced taxes currently payable by \$15.3 million, \$37.6 million and \$18.0 million for the years ended March 31, 2005, 2004 and 2003, respectively. These amounts were credited to additional paid-in capital in each of the three fiscal years.

The provision for income taxes differs from the amount computed by applying the statutory federal tax rate to income before income taxes. The sources and tax effects of the differences in the total income tax provision for income before cumulative effect of change in accounting principle are as follows (amounts in thousands):

	Year Ended March 31,		
	2005	2004	2003
Computed expected provision	\$ 97,044	\$ 62,264	\$ 44,916
State income taxes, net of federal benefits	2,738	1,424	554
Foreign export sales benefit	(1,111)	(96)	(2,278)
Research and development tax credits	(4,750)	(4,000)	(2,959)
Foreign income taxed at lower than the federal rate	(30,438)	(18,958)	(11,576)
	<u>\$ 63,483</u>	<u>\$ 40,634</u>	<u>\$ 28,657</u>

Pretax income from foreign operations was \$199.0 million, \$136.3 million and \$108.2 million for the years ended March 31, 2005, 2004 and 2003, respectively. Unremitted foreign earnings that are considered to be permanently invested outside the United States, and on which no deferred taxes have been provided, amounted to approximately \$766.0 million at March 31, 2005. Should the Company elect in the future to repatriate a portion of the foreign earnings so invested, the Company would incur income tax expense on such repatriation, net of any available deductions and foreign tax credits. This would result in additional income tax expense beyond the computed expected provision in such periods.

In December 2004, the FASB issued Financial Staff Position (FSP) No. FAS 109-2, "Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004" (FSP 109-2). On October 22, 2004, the American Jobs Creation Act of 2004 (the "Act") was signed into law. The Act creates a temporary incentive for U.S. corporations to repatriate accumulated income earned abroad by including an 85 percent deduction for certain foreign earnings that are repatriated, as defined in the Act, at an effective tax cost of 5.25 percent. FSP 109-2 is effective immediately and provides accounting and disclosure guidance for the repatriation provision. FSP 109-2 allows companies additional time to evaluate the effects of the law on its unremitted earnings for the purpose of applying the "indefinite reversal criteria" under APB 23, "Accounting for Income Taxes – Special Areas," and requires explanatory disclosures from companies that have not yet completed the evaluation.

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The Company is in the process of evaluating whether it will repatriate any foreign earnings under the Act and, if so, the amount that it will repatriate. However, the Company does not expect to be able to complete this evaluation until later in fiscal 2006. Based on our preliminary analysis, the range of possible amounts that the Company is considering for repatriation under this provision is between zero and \$500 million. The related potential range of income tax is between zero and approximately \$28.7 million. The Company expects to determine the amounts and sources of foreign earnings to be repatriated, if any, during fiscal year 2006.

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities are as follows (amounts in thousands):

	March 31,	
	2005	2004
Deferred tax assets:		
Intercompany profit in inventory	\$ 11,616	\$ 10,887
Deferred income on shipments to distributors	22,699	34,500
Inventory valuation	8,020	1,987
Net operating loss carryforward	5,942	12,531
Tax credit carryforward	47,337	29,944
Fab 3 impairment	—	15,977
Fab 1 closure and impairment charges	—	10,421
Accrued expenses and other	9,483	9,799
Gross deferred tax assets	<u>105,097</u>	<u>126,046</u>
Deferred tax liabilities:		
Property, plant and equipment, principally due to differences in depreciation	(23,258)	(28,958)
Other	(1,298)	(1,746)
Gross deferred tax liability	<u>(24,556)</u>	<u>(30,704)</u>
Net deferred tax asset	<u>\$ 80,541</u>	<u>\$ 95,342</u>

The Fab 3 asset changed classifications from an asset held-for-sale at March 31, 2004 to an asset held-for-future-use at March 31, 2005. At March 31, 2005, any tax effects of temporary differences related to Fab 3 are included in the deferred tax liability related to depreciation on property, plant and equipment.

Management believes that the results of future operations will generate sufficient taxable income such that it is “more likely than not” that deferred tax assets will be realized.

On June 5, 2002, the Company acquired all of the outstanding stock of PowerSmart Inc. in a taxable stock acquisition. As a result of the PowerSmart acquisition, \$6.7 million of net deferred tax assets were acquired consisting of a deferred tax asset of \$8.8 million relating primarily to net operating loss carryforwards and a deferred tax liability of \$2.1 million relating to intangible assets acquired.

At March 31, 2005, the Company had a net operating loss carryforward for federal income tax purposes of approximately \$15.4 million, which begins to expire in varying amounts in the years 2018 through 2022. The net operating loss carryforward is attributable to the acquisition of PowerSmart. An analysis of the annual limitation on the utilization of the PowerSmart net operating losses was performed in accordance with Internal Revenue Code Section 382. It was determined that Section 382 will not limit the use of the PowerSmart net operating losses in full over the carryover period.

At March 31, 2005, the Company had recorded credit carryforwards of approximately \$19.7 million for foreign tax credits, \$22.9 million for research and development credits, and \$4.7 million for alternative minimum tax credits.

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The foreign tax credits begin to expire in varying amounts in the years ending March 31, 2006 through March 31, 2010, the research and development credits begin to expire in varying amounts in the years ending March 31, 2011 through March 31, 2025 and the alternative minimum tax credits have no expiration date. The Company believes that all of its credit carryforwards will be utilized in future periods.

The Company’s Thailand manufacturing operations currently benefit from numerous tax holidays granted to the Company based on its investment in property, plant and equipment in Thailand. Although the Company’s tax holidays in Thailand partially expired in October 2003, the Company’s manufacturing operations in Thailand are being conducted using primarily equipment that was invested pursuant to tax holidays that do not begin to expire until September 2006. The aggregate dollar benefits derived from these tax holidays approximated \$11.5 million, \$45.3 million and \$31.4 million for the years ended March 31, 2005, 2004 and 2003, respectively. The benefit the tax holiday had on net income per share approximated \$0.05, \$0.21 and \$0.15 for the years ended March 31, 2005, 2004 and 2003, respectively. The reduction in the benefits derived from the Company’s tax holiday in Thailand in the year ended March 31, 2005 compared to the year ended March 31, 2004 was a result of changes in the Company’s overall international tax structure. These changes did not have a material impact on the Company’s overall effective tax rate.

The Company is currently under audit by the United States Internal Revenue Service (IRS) for its fiscal years ended March 31, 1998, 1999, 2000 and 2001. The IRS has proposed certain adjustments related to positions reflected on these tax returns. The IRS has issued formal assessments for these adjustments. The Company does not agree with these adjustments and intends to appeal these assessments. The Company believes that it maintains adequate tax reserves to offset the potential liabilities that may arise upon final resolution of the audit through either settlement or the appeals process with the IRS. If such amounts ultimately prove to be unnecessary, the resulting reversal of such reserves would result in tax benefits being recorded in the period the reserves are no longer deemed necessary. If such amounts ultimately prove to be less than the ultimate assessment, a future charge to expense would result. The Company has included in income taxes payable reserves for potential losses. Should such losses occur, they would result in the reduction of deferred tax assets or payments of amounts accrued.

14. CONTINGENCIES

The Company’s assembly and test facility in Thailand is located in Alphatechnopolis Industrial Park near Bangkok on land to which the Company expects to acquire title in accordance with its agreement with the landowner. Progress towards obtaining full title of the land has been delayed due to a complex financial restructuring situation relating to the seller of the land. At this time it is not possible to estimate when, or if, full title will be completed. The Company has provided reserves that it estimates will be adequate to obtain full title. Such reserves are set at the estimated fair value of the land.

In the ordinary course of its business, the Company is involved in a limited number of legal actions, both as plaintiff and defendant, and could incur uninsured liability in any one or more of them. Although the outcome of these actions is not presently determinable, the Company believes that the ultimate resolution of these matters will not harm its business. Litigation relating to the semiconductor industry is not uncommon, and the Company is, and from time to time has been, subject to such litigation. In the Company’s opinion, based on consultation with legal counsel, as of March 31, 2005, the effect of such matters will not have a material adverse effect on the Company’s financial position, cash flows or results of operations.

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15. STOCKHOLDERS’ EQUITY

Stockholder Rights Plan. Effective October 11, 1999, the Company adopted an Amended and Restated Preferred Shares Rights Agreement (the “Amended Rights Agreement”). The Amended Rights Agreement amends and restates the Preferred Share Rights Agreement adopted by the Company as of February 13, 1995 (the “Prior Rights Agreement”). Under the Prior Rights Agreement, on February 13, 1995, the Company’s Board of Directors declared a dividend of one right (a “Right”) to purchase one one-hundredth of a share of the Company’s Series A Participating Preferred Stock (“Series A Preferred”) for each outstanding share of common stock, \$0.01 par value, of the Company. The dividend was payable on February 24, 1995 to stockholders of record as of the close of business on that date. The Amended Rights Agreement supersedes the Prior Rights Agreement as originally executed. Under the Amended Rights Agreement, each Right enables the holder to purchase from the Company one one-hundredth of a share of Series A Preferred at a purchase price of seventy four dollars and seven cents (\$74.07) (the “Purchase Price”), subject to adjustment. Under the Amended Rights Agreement, the rights will become exercisable upon the earlier of (i) 10 days following a public announcement that a person or a group of affiliated or associated persons has acquired, or obtained the right to acquire, beneficial ownership of 15% or more of the Company’s outstanding common shares, or (ii) 10 days (or such later date as may be determined by action of the Company’s Board of Directors) following the commencement of, or announcement of an intention to make, a tender offer or exchange offer the consummation of which would result in a beneficial ownership by a person or group of 15% or more of the Company’s outstanding common shares.

Stock Repurchase Activity. On August 7, 2002, the Company’s Board of Directors authorized the Company to repurchase up to 2,500,000 shares of its common stock in the open market or in privately negotiated transactions. As of March 31, 2005, the Company had repurchased the entire 2,500,000 common share authorization for \$59.3 million. On March 11, 2004, the Company’s Board of Directors authorized the repurchase of an additional 2,500,000 shares of its common stock in the open market or in privately negotiated transactions. As of March 31, 2005, the Company had repurchased the entire 2,500,000 common share authorization for \$66.1 million. On April 22, 2004, the Company’s Board of Directors authorized the repurchase of an additional 2,500,000 shares of its common stock in the open market or in privately negotiated transactions. As of March 31, 2005, the Company had repurchased 884,900 shares under this authorization for \$23.3 million. As of March 31, 2005, all but 818,332 of the purchased shares under the authorizations had been reissued to fund stock option exercises and purchases under the Company’s employee

stock purchase plan. During the twelve months ended March 31, 2003, the Company purchased 1,264,700 shares of its common stock for \$27.1 million. During the twelve months ended March 31, 2004, the Company purchased 2,435,400 shares of its common stock for \$63.9 million, of which \$10.6 million was not paid until April 2004 and is reflected in the March 31, 2004 accounts payable balance. During the twelve months ended March 31, 2005, the Company purchased 2,184,800 shares of its common stock for \$57.7 million.

16. EMPLOYEE BENEFIT PLANS

The Company maintains a contributory profit-sharing plan for its domestic employees meeting certain eligibility and service requirements. The plan qualifies under Section 401(k) of the Internal Revenue Code of 1986, as amended, and allows employees to contribute up to 60% of their base salary, subject to maximum annual limitations prescribed by the Internal Revenue Service. The Company shall make a matching contribution of up to 25% of the first 4% of the participant's eligible compensation and may award up to an additional 25% under the discretionary match. All matches are provided on a quarterly basis and require the participant to be an active employee at the end of each quarter. For the fiscal years ended March 31, 2005, 2004 and 2003, the Company contributions to the plan totaled \$1.4 million, \$1.1 million and \$0.8 million, respectively.

The Company's 2001 Employee Stock Purchase Plan (the "2001 Purchase Plan") became effective on March 1, 2002. The Board of Directors approved the 2001 Purchase Plan in May 2001 and the stockholders approved it in August 2001. Under the 2001 Purchase Plan, eligible employees of the Company may purchase shares of common stock at semi-annual intervals through periodic payroll deductions. The purchase price in general will be 85% of the lower of the fair market value of the common stock on the first day of the participant's entry date into the offering period or 85% of the fair market value on the semi-annual purchase date. Depending upon a participant's entry date into the 2001 Purchase Plan, purchase periods under the 2001 Purchase Plan consist of overlapping periods of either 24, 18, 12 or 6 months in duration. 2,450,000 shares of common stock have been previously reserved for issuance under the 2001 Purchase Plan. In May 2003, the Board of Directors reserved an additional 975,000 shares of common stock for issuance under the 2001 Purchase Plan, which was approved by the stockholders in August 2003.

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In May 2003 and August 2003, the Company's Board and stockholders, respectively, each approved an annual automatic increase in the number of shares reserved under the 2001 Purchase Plan. The automatic increase took effect on January 1, 2005, and on each January 1 thereafter during the term of the plan, and is equal to the lesser of (i) 1,500,000 shares, (ii) one half of one percent (0.5%) of the then outstanding shares of the Company's common stock, or (iii) such lesser amount as is approved by the Company's Board of Directors. On January 1, 2005, 1,035,863 additional shares were reserved under the 2001 Purchase Plan based on the automatic increase.

During fiscal 1995, a purchase plan was adopted for employees in non-U.S. locations. Such plan allows for the purchase price per share to be 100% of the lower of the fair market value of the common stock on the beginning or end of the semi-annual purchase plan period. Since the inception of this purchase plan, 348,593 shares of common stock have been reserved for issuance and 232,254 shares have been issued under this purchase plan.

Effective January 1, 1997, the Company adopted a non-qualified deferred compensation arrangement. This plan is unfunded and is maintained primarily for the purpose of providing deferred compensation for a select group of highly compensated employees as defined in ERISA Sections 201, 301 and 401. There are no Company matching contributions made under this plan.

The Company has a management incentive compensation plan which provides for bonus payments, based on a percentage of base salary, from an incentive pool created from operating profits of the Company, at the discretion of the Board of Directors. During the years ended March 31, 2005 and March 31, 2004, \$10.2 million and \$1.8 million was charged against operations for this plan, respectively. The Company did not make any payments under its management incentive compensation plan during fiscal 2003.

The Company also has a plan that, at the discretion of the Board of Directors, provides a cash bonus to all employees of the Company based on the operating profits of the Company. During the years ended March 31, 2005, 2004 and 2003, \$4.9 million, \$2.4 million and \$1.8 million, respectively, were charged against operations for this plan.

17. EQUITY INCENTIVE PLANS

Under the Company's equity incentive plans (the "Plans"), eligible participants may be granted different types of equity incentive awards. No awards other than stock options have been awarded under our equity incentive plans as of March 31, 2005. Officers, key employees, non-employee directors and consultants may be granted non-statutory stock options to purchase shares of common stock at a price not less than 100% of the fair value of the option shares on the grant date. Options granted under the Plans vest over the period determined by the Board of Directors at the date of grant, at periods ranging from one year to four years. The maximum term of options granted under the Plans is 10 years. The Company did not make any stock option grants to consultants during the years ended March 31, 2005, 2004 and 2003. At March 31, 2005, there were 15,122,075 shares available for grant under the Plans. The per share weighted average fair value of stock options granted under the Plans for the years ended March 31, 2005, 2004 and 2003 was \$15.82, \$12.06 and \$15.00, respectively, based on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions:

	Year Ended March 31,		
	2005	2004	2003
Expected life (years)	5.30	5.19	5.00
Risk-free interest rate	3.78%	2.90%	2.80%
Volatility	67%	70%	71%
Dividend yield	0.97%	0.48%	0.48%

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Under the Plans, 105,281,645 shares of common stock had been reserved for issuance since the inception of the Plans.

The stock option activity is as follows:

	Options Outstanding	
	Shares	Weighted Average Exercise Price
Outstanding at March 31, 2002	24,666,811	\$ 12.12

Granted	5,126,899	25.76
Exercised	(3,564,895)	6.47
Canceled	(993,899)	18.11
Outstanding at March 31, 2003	25,234,916	15.45
Granted	4,186,351	20.68
Exercised	(5,114,292)	8.79
Canceled	(947,047)	21.53
Outstanding at March 31, 2004	23,359,928	17.60
Granted	2,693,824	27.35
Exercised	(2,881,830)	12.78
Canceled	(801,236)	23.34
Outstanding at March 31, 2005	22,370,686	\$ 19.19

The following table summarizes information about the stock options outstanding at March 31, 2005:

Range Exercise Price	Number Outstanding	Weighted Average Remaining Life	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
\$ 0.009 — \$ 6.370	2,475,899	2.33	\$ 5.74	2,475,114	\$ 5.74
\$ 6.525 — \$ 10.037	2,941,161	3.22	\$ 9.30	2,941,161	\$ 9.30
\$ 10.407 — \$ 15.917	2,858,854	5.81	\$ 15.62	1,263,084	\$ 15.24
\$ 16.167 — \$ 17.846	192,097	5.45	\$ 17.24	190,676	\$ 17.25
\$ 18.480 — \$ 18.480	2,420,121	8.02	\$ 18.48	855,142	\$ 18.48
\$ 18.649 — \$ 23.389	3,130,839	5.57	\$ 22.31	2,885,073	\$ 22.33
\$ 23.700 — \$ 26.250	2,317,374	7.74	\$ 25.04	1,588,151	\$ 24.86
\$ 26.600 — \$ 27.050	1,814,983	8.88	\$ 27.04	62,295	\$ 26.79
\$ 27.153 — \$ 27.153	2,618,266	7.01	\$ 27.15	2,607,672	\$ 27.15
\$ 27.170 — \$ 35.080	1,601,092	7.42	\$ 29.29	1,145,702	\$ 29.15
\$ 0.009 — \$ 35.080	22,370,686	5.99	\$ 19.19	16,014,070	\$ 18.09

At March 31, 2005 and 2004, the number of option shares exercisable was 16,014,070 and 11,583,715, respectively, and the weighted-average exercise price of those options was \$18.09 and \$13.26, respectively.

The Company received a tax benefit of \$15.3 million, \$37.6 million and \$18.0 million for the years ended March 31, 2005, 2004 and 2003, respectively, from the exercise of non-qualified stock options and the disposition of stock acquired with incentive stock options or through the Company's employee stock purchase plan. For financial reporting purposes, the tax effect of this deduction is accounted for as a credit to additional paid-in capital rather than as a reduction of income tax expense.

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18. LEASE COMMITMENTS

The Company leases office space, transportation and other equipment under operating leases, which expire at various dates through March 31, 2010. The future minimum lease commitments under these leases are payable as follows (amounts in thousands):

Year Ending March 31,	Operating Leases
2006	\$ 4,183
2007	3,081
2008	1,522
2009	522
2010	195
Total minimum payments	\$ 9,503

Rental expense under operating leases totaled \$5.9 million, \$5.4 million and \$5.7 million for the years ended March 31, 2005, 2004 and 2003, respectively.

19. GEOGRAPHIC INFORMATION

The Company operates in one operating segment and engages primarily in the design, development, manufacture and marketing of semiconductor products. The Company sells its products to distributors and original equipment manufacturers (OEMs) in a broad range of market segments, performs on-going credit evaluations of its customers and generally requires no collateral. The Company's operations outside the United States consist of product assembly and final test facilities in Thailand, and sales and support centers and design centers in certain foreign countries. Domestic operations are responsible for the design, development and wafer fabrication of all products, as well as the coordination of production planning and shipping to meet worldwide customer commitments. The Thailand assembly and test facility is reimbursed in relation to value added with respect to assembly and test operations and other functions performed, and certain foreign sales offices receive compensation for export sales within their territory. Accordingly, for financial statement purposes, it is not meaningful to segregate sales or operating profits for the assembly and test and foreign sales office operations. Identifiable long-lived assets (consisting of property, plant and equipment and goodwill) by geographic area are as follows (amounts in thousands):

March 31,	
2005	2004

United States	\$	622,287	\$	608,343
Thailand		100,622		111,730
Various		2,279		1,479
Total long-lived assets	\$	725,188	\$	721,552

Sales to unaffiliated customers located outside the United States, primarily in Asia and Europe, aggregated approximately 73%, 71% and 71% of consolidated net sales for the years ended March 31, 2005, 2004 and 2003, respectively. Sales to customers in Europe represented 27%, 28% and 27% of consolidated net sales for the years ended March 31, 2005, 2004 and 2003, respectively. Sales to customers in Asia represented 43%, 41% and 39% of consolidated net sales for the years ended March 31, 2005, 2004 and 2003, respectively. Sales into China, including Hong Kong, represented 16%, 14% and 13% of consolidated net sales for the years ended March 31, 2005, 2004 and 2003, respectively. Sales into Taiwan represented 10% of consolidated net sales for the year ended March 31, 2005. Sales into any other individual foreign country did not exceed 10% of the Company's net sales for any of the years presented.

The Company had two distributors who represented more than 10% of its net sales during fiscal 2005 and fiscal 2004. The Company's largest distributor accounted for approximately 13% of its net sales and its second largest distributor accounted for approximately 12% of net sales in fiscal 2005. The Company's largest distributor accounted for approximately 13% of its net sales and its second largest distributor accounted for approximately 12%

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of its net sales in fiscal 2004. In fiscal 2003, the Company had one distributor that accounted for approximately 12% of its net sales.

20. FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying amount of cash equivalents approximates fair value because their maturity is less than three months. The carrying amount of short-term investments approximates fair value because the longer-term instruments have interest rate reset features that regularly adjust to current market rates. The carrying amount of accounts receivable, accounts payable and accrued liabilities approximates fair value due to the short-term maturity of the amounts. The fair value of capital lease obligations, long-term debt and lines of credit approximate their carrying value as they are estimated by discounting the future cash flows at rates currently offered to the Company for similar debt instruments.

The Company has entered into certain financial instruments in the normal course of business to reduce its exposure to fluctuations in foreign exchange rates. These financial instruments include standby letters of credit and foreign currency forward contracts. When engaging in forward contracts, risks arise from the possible inability of counterparties to meet the terms of their contracts and from movements in securities values, interest rates and foreign exchange rates. At March 31, 2005, there were no foreign currency forward contracts outstanding. At March 31, 2004, the Company held contracts with nominal amounts totaling \$3.2 million, which were entered into and hedged the Company's foreign currency risk. The value of the contracts is based on quoted market prices. The contracts matured in June 2004. Unrealized gains and losses as of the balance sheet dates and realized gains and losses for the years ending March 31, 2005, 2004 and 2003 were not material.

21. NET INCOME PER COMMON SHARE

The following table sets forth the computation of basic and diluted net income per share (in thousands except per share amounts):

	Year Ended March 31,		
	2005	2004	2003
Net income	\$ 213,785	\$ 137,262	\$ 88,232
Weighted average common shares outstanding	206,740	206,032	202,483
Dilutive effect of stock options	5,222	6,140	8,163
Weighted average common and common equivalent shares outstanding	211,962	212,172	210,646
Basic net income per common share	\$ 1.03	\$ 0.67	\$ 0.44
Diluted net income per common share	\$ 1.01	\$ 0.65	\$ 0.42

Weighted average common shares exclude the effect of antidilutive options. As of March 31, 2005, 2004 and 2003, the number of options that were antidilutive were 1,310,018, 4,532,872 and 4,282,029, respectively.

22. QUARTERLY RESULTS (UNAUDITED)

The following table presents the Company's selected unaudited quarterly operating results for eight quarters ended March 31, 2005. The Company believes that all necessary adjustments have been made to present fairly the related quarterly results (in thousands, except per share amounts):

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	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total
Fiscal 2005					
Net sales	\$ 212,775	\$ 220,694	\$ 205,384	\$ 208,083	\$ 846,936
Gross profit	121,459	126,377	116,788	119,351	483,975
Operating income	49,854	75,051	65,622	68,120	258,647
Net income	43,799	60,443	53,140	56,403	213,785
Diluted net income per common share	0.21	0.29	0.25	0.27	1.01
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total

Fiscal 2004

Net sales	\$	161,283	\$	168,486	\$	177,967	\$	191,524	\$	699,260
Gross profit		55,521		91,194		97,019		106,225		349,959
Operating income		10,512		47,594		53,852		59,336		171,294
Net income		13,470		36,104		40,843		46,845		137,262
Diluted net income per common share		0.06		0.17		0.19		0.22		0.65

Refer to Note 4, Special Charges, for an explanation of the unusual and infrequent items that occurred in the applicable fiscal quarters that materially impacted the Company's operating results.

23. SUPPLEMENTAL FINANCIAL INFORMATION

Cash paid for income taxes amounted to \$15.6 million, \$4.6 million and \$5.2 million during the years ended March 31, 2005, 2004 and 2003, respectively. Cash paid for interest amounted to \$0.8 million, \$0.2 million and \$0.5 million during the years ended March 31, 2005, 2004 and 2003, respectively. Included in the special charge for the year ended March 31, 2003 was a non-cash amount of \$41.5 million, which pertained to the write-down of the Fab 3 fixed assets.

Treasury stock purchases for which settlement has not occurred are included as treasury stock repurchased in shareholders' equity and accounts payable and amounted to \$10.6 million and \$0.5 million as of March 31, 2004 and 2003, respectively.

A summary of additions and deductions related to the allowance for doubtful accounts for the years ended March 31, 2005, 2004 and 2003 follows (amounts in thousands):

	Balance at beginning of year	Charged to costs and expenses	Deductions (1)	Balance at end of year
Allowance for doubtful accounts:				
2005	\$ 3,810	\$ 7	\$ 0	\$ 3,817
2004	3,768	250	(208)	3,810
2003	3,937	60	(229)	3,768

(1) Deductions represent uncollectible accounts written off, net of recoveries.

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24. DIVIDENDS

On October 28, 2002, the Company announced that its Board of Directors had approved and instituted a quarterly cash dividend on its common stock. The initial quarterly dividend of \$0.02 per share was paid on December 6, 2003 in the amount of \$4.1 million. The Company has continued to pay quarterly dividends and has increased the amount of such dividends on a regular basis. During the year ended March 31, 2005, the Company paid dividends totaling \$0.208 per share for a total dividend payment of \$43.0 million. During the year ended March 31, 2004, the Company paid dividends totaling \$0.113 per share for a total dividend payment of \$23.3 million.

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MICROCHIP TECHNOLOGY INCORPORATED
2004 EQUITY INCENTIVE PLAN
NOTICE OF STOCK OPTION GRANT

Unless otherwise defined herein, the terms used in this Notice of Stock Option Grant ("Grant Notice") shall have the same meanings as those defined in the 2004 Equity Incentive Plan (the "Plan").

Name of Optionee: _____

Optionee has been granted an option to purchase Common Stock of the Company, subject to the terms and conditions of this Grant Notice, the Plan and the Stock Option Agreement attached as Exhibit A hereto ("Agreement"), as follows:

Grant Number: _____

Grant Date: _____

Date Vesting Begins: _____

Vesting Period: _____

Exercise Price per Share: \$ _____

Total Number of Shares Granted: _____

Total Exercise Price: \$ _____

Type of Option: **Nonstatutory Stock Option**

Term/Expiration Date: _____

Vesting Schedule. This Option shall be exercisable, in whole or in part, in accordance with the following schedule: If the Grant Date and the Date Vesting Begins are the same, then the monthly installments for the first year of the Vesting Period will vest only in a lump sum upon the Optionee's completion of twelve months as an employee of [Name of Subsidiary], measured from the Grant Date, and the balance will vest over the remainder of the Vesting Period on a monthly basis subject to Optionee remaining an employee of [Name of Subsidiary] continuously through the applicable vesting dates. However, if the Date Vesting Begins is not the same as the Grant Date, then the Option Shares will vest in equal monthly installments (12 x the number of years in the Vesting Period) over Optionee's period of continuous employment with [Name of Subsidiary] beginning one month after the Date Vesting Begins subject to Optionee continuously remaining an employee of [Name of Subsidiary] through the applicable vesting dates.

Termination Period. This Option shall automatically terminate and Optionee's rights are forfeited with respect to any Option Shares unvested on the date Optionee ceases to be employed by [Name of Subsidiary]. In no event will the Option Shares vest following the Optionee's cessation of employment with [Name of Subsidiary], even in the event that Optionee is employed by the Company, a different subsidiary of the Company, or is re-employed by [Name of Subsidiary]. In no event shall this Option be exercised later than the Term/Expiration Date above.

Choice of Languages For Employees of Canadian Locations. The undersigned agrees that it is his or her express wish that this form and all documents relating to his participation in the scheme be drawn in the English language only. Le soussigné convient que sa volonté expresse est que ce formulaire ainsi que tous les documents se rapportant à sa participation au régime soient rédigés en langue anglaise seulement.

Binding Agreements. By signature of the Optionee and Company representative below, Optionee and the Company agree that this Grant Notice, the Agreement, and the Plan constitute Optionee's entire agreement with respect to this Option and agree to be bound by the terms therein. Optionee hereby agrees to accept as binding, conclusive and final all decisions or interpretations of the Administrator upon any questions relating to the Plan, the Agreement, and/or this Option. In accordance with Section 21(c) of the Plan, this Grant Notice may not be modified adversely to Optionee's interest except by means of a writing signed by the Company and Optionee. The Company will administer the Plan from the United States of America. The internal laws of the State of Arizona, United States of America, but not its choice of law principles, will govern this Option.

OPTIONEE

MICROCHIP TECHNOLOGY INCORPORATED

Optionee Signature: _____

By: _____

Address: _____

Steve Sanghi, President and CEO

Dated: _____

EXHIBIT A

MICROCHIP TECHNOLOGY INCORPORATED
2004 EQUITY INCENTIVE PLAN
STOCK OPTION AGREEMENT

1. **Grant of Option.** The Company hereby grants to the optionee (the "Optionee") named in the Notice of Stock Option Grant (the "Grant Notice"), to which this Agreement is attached as Exhibit A, an option (the "Option") to purchase the number of Shares, as set forth in the Grant Notice, at the exercise price per share set forth in the Grant Notice (the "Exercise Price"), subject to the terms and conditions of the Plan, which is incorporated herein by reference. Subject to Section 21(c) of the Plan, in the event of a conflict between the terms and conditions of the Plan and the terms and conditions of this Agreement, the terms and conditions of the Plan shall prevail.

2. Exercise of Option.

(a) Right to Exercise. This Option is exercisable during its term in accordance with the Vesting Schedule set out in the Grant Notice and the applicable provisions of the Grant Notice, the Plan and this Agreement.

(b) Method of Exercise. This Option is exercisable by delivery of an exercise notice, in the form attached as Exhibit A-1 (the "Exercise Notice") or in written or electronic form as designated by the Company, which shall state the election to exercise the Option, the number of Shares in respect of which the Option is being exercised (the "Exercised Shares"), and such other representations and agreements as may be required by the Company pursuant to the provisions of the Plan. The Exercise Notice shall be completed by the Optionee and delivered to the Stock Administrator of the Company. The Exercise Notice shall be accompanied by payment of the aggregate Exercise Price as to all Exercised Shares. This Option shall be deemed to be exercised upon receipt by the Company of such fully executed Exercise Notice accompanied by such aggregate Exercise Price.

No Shares shall be issued pursuant to the exercise of this Option unless such issuance and exercise complies with Applicable Laws. Assuming such compliance, for income tax purposes the Exercised Shares shall be considered transferred to the Optionee on the date the Option is exercised with respect to such Exercised Shares.

3. Method of Payment. Payment of the aggregate Exercise Price shall be by any of the following, or a combination thereof, at the election of the Optionee:

(a) cash;

(b) check; or

(c) to the extent permitted by the Administrator, delivery of a properly executed exercise notice together with such other documentation as the Administrator and the broker, if applicable, shall be required to effect an exercise of the Option and delivery to the Company of the sale proceeds required to pay the Exercise Price.

4. Term of Option. This Option may be exercised only within the term set out in the Grant Notice, and may be exercised during such term only in accordance with the Plan and the terms of this Agreement; provided, however that notwithstanding any contrary provision of the Plan if a Subsidiary is expressly named in the Grant Notice then this Option shall terminate with respect to any then unvested shares immediately upon cessation of employment with the named subsidiary, but if no such subsidiary is expressly named in the Grant Notice then this Option shall terminate with respect to any then unvested shares immediately upon Optionee ceasing to be a Service Provider.

5. Grant is not Transferable. Unless determined otherwise by the Administrator, this Option may not be sold, pledged, assigned, hypothecated, transferred, or disposed of in any manner other than by will or by the laws of descent or distribution and may be exercised, during the lifetime of the recipient, only by the recipient. If the Administrator makes this Option transferable, the Grant Notice shall contain this additional terms and conditions as the Administrator deems appropriate.

6. No Privilege of Stock Ownership. Neither the holder of the option granted hereunder nor any person claiming under or through the Optionee shall have any of the rights of a stockholder with respect to the Optioned Shares until such Optionee shall have exercised the option, paid the Exercise Price, and received a stock certificate for the purchased shares of Stock, or had the Shares electronically transferred into Optionee's account.

7. Withholding Taxes. Optionee agrees to make appropriate arrangements with the Company (or the Parent or Subsidiary employing or retaining Optionee) for the satisfaction of all Federal, state, local and foreign income and minimum required employment tax withholding requirements applicable to the Option exercise. Optionee acknowledges and agrees that the Company may refuse to honor the exercise and refuse to deliver Shares if such withholding amounts are not delivered at the time of exercise.

8. Acknowledgments. The Optionee expressly acknowledges the following:

(a) The Company (whether or not Optionee's employer) is granting the Option. That the grant of the Option, future grants of Options, and benefits and rights provided under the Plan are at the complete discretion of the Company and do not constitute regular or periodic payments. No grant of Options will be deemed to create any obligation to grant any further Options, whether or not such a reservation is explicitly stated at the time of such a grant. The benefits and rights provided under the Plan are not to be considered part of Optionee's salary or compensation for purposes of calculating any severance, resignation, redundancy or other end of service payments, vacation, bonuses, long-term service awards, indemnification, pension or retirement benefits, or any other payments, benefits or rights of any kind. Optionee waives any and all rights to compensation or damages as a result of the termination of employment with the Company or its subsidiaries for any reason whatsoever insofar as those rights result or may result from:

(i) the loss or diminution in value of such rights under the Plan, or

(ii) Optionee ceasing to have any rights under, or ceasing to be entitled to any rights under the Plan as a result of such termination.

(b) The Company has the right, at any time to amend, suspend or terminate the Plan. The Plan will not be deemed to constitute, and will not be construed by Optionee to constitute, part of the terms and conditions of employment, and that the Company will not incur any liability of any kind to Optionee as a result of any change or amendment, or any cancellation, of the Plan at any time.

(c) The Grantee's employment with the Company and its Subsidiaries is not affected at all by any Award and is agreed by the Grantee not to create an entitlement. Accordingly, the terms of the Grantee's employment with the Company and its Subsidiaries will be determined from time to time by the Company or the Subsidiary employing the Grantee (as the case may be), and the Company or the Subsidiary will have the right, which is hereby expressly reserved, to terminate or change the terms of the employment of the Grantee at any time for any reason whatsoever, with or without good cause or notice, except as may be expressly prohibited by the laws of the jurisdiction in which the Grantee is employed.

(d) By entering into this Agreement, and as a condition of the grant of the Option, Optionee consents to the collection, use, and transfer of personal data as described in this subsection to the full extent permitted by and in full compliance with Applicable Law.

(i) Optionee understands that the Company and its Subsidiaries hold certain personal information about the Optionee, including, but not limited to, name, home address and telephone number, date of birth, social insurance number, salary, nationality, job title, any Shares or directorships held in the Company, details of all Options or other entitlement to Shares awarded, canceled, exercised, vested, unvested, or outstanding in Optionee's favor, for the purpose of managing and administering the Plan ("Data").

(ii) Optionee further understands that the Company and/or its Subsidiaries will transfer Data among themselves as necessary for the purposes of implementation, administration, and management of Optionee's participation in the Plan, and that the Company and/or its Subsidiary may each further transfer Data to any third parties assisting the Company in the implementation, administration, and management of the Plan ("Data Recipients").

(iii) Optionee understands that these Data Recipients may be located in Optionee's country of residence or elsewhere, such as the United States. Optionee authorizes the Data Recipients to receive, possess, use, retain, and transfer Data in electronic or other form, for the purposes of implementing, administering, and managing Optionee's participation in the Plan, including any transfer of such Data, as may be required for Plan administration and/or the subsequent holding of Shares on Optionee's behalf, to a broker or third party with whom the Shares acquired on exercise may be deposited.

(iv) Optionee understands that Optionee may, at any time, review the Data, request that any necessary amendments be made to it, or withdraw Optionee's consent herein in writing by contacting the Company. Optionee further understands that withdrawing consent may affect Optionee's ability to participate in the Plan.

(e) Choice of Language.

(i) For Employees of Canadian Locations: The undersigned agrees that it is his or her express wish that this form and all documents relating to his participation in the scheme be drawn in the English language only. Le soussigné convient que sa volonté expresse est que ce formulaire ainsi que tous les documents se rapportant à sa participation au régime soient rédigés en langue anglaise seulement.

(ii) For Employees of Locations Other than Canada: Optionee has received this Agreement and any other related communications and consents to having received these documents solely in English.

9. Binding Agreement. Subject to the limitation on the transferability of this grant contained herein, this Agreement will be binding upon and inure to the benefit of the heirs, legatees, legal representatives, successors and assigns of the parties hereto.

10. Additional Conditions to Issuance of Stock. If at any time the Company will determine, in its discretion, that the listing, registration or qualification of the Shares upon any securities exchange or under any state or federal law, or the consent or approval of any governmental regulatory authority is necessary or desirable as a condition to the issuance of Shares to the Optionee (or his or her estate), such issuance will not occur unless and until such listing, registration, qualification, consent or approval will have been effected or obtained free of any conditions not acceptable to the Company. The Company will make all reasonable efforts to meet the requirements of any such state or federal law or securities exchange and to obtain any such consent or approval of any such governmental authority.

11. Administrator Authority. The Administrator has the power to interpret the Plan, the Grant Notice and this Agreement and to adopt such rules for the administration, interpretation and application thereof as are consistent therewith and to interpret or revoke any such rules (including, but not limited to, the determination of

whether or not any Options have vested). All actions taken and all interpretations and determinations made by the Administrator in good faith will be final and binding upon Optionee, the Company and all other interested persons. No member of the Administrator will be personally liable for any action, determination or interpretation made in good faith with respect to the Plan, the Grant Notice or this Agreement.

12. Notice Requirement. Where there is a legal requirement for any notice or document to be sent to any person by any other person, it shall be considered sent if an electronic transmission of the relevant information is sent in a form previously determined as being acceptable to the Administrator. For the avoidance of doubt, the Administrator may dispense with the requirement to tender a certificate on the issuance of Shares under an Option where the Administrator authorizes any system permitting electronic notification.

13. Address for Notices. Any notice to be given to the Company under the terms of this Agreement will be addressed to the Company at 2355 West Chandler Boulevard, Chandler AZ 85224, Attn: Stock Administration, or at such other address as the Company may hereafter designate in writing or electronically.

14. Entire Agreement; Governing Law. The Plan and Grant Notice are incorporated herein by reference. The Plan, Grant Notice and this Agreement constitute the entire agreement of the parties with respect to the subject matter hereof and supersede in their entirety all prior undertakings and agreements of the Company and Optionee with respect to the subject matter hereof, and may not be modified adversely to the Optionee's interest except by means of a writing signed by the Company and Optionee. The Company will administer the Plan from the United States of America. The internal laws of the State of Arizona, United States of America, but not its choice of laws principles, will govern this Agreement, the Grant Notice, and all Options granted under the Plan.

By your signature, you agree that this Option is granted under and governed by the terms and conditions of the Plan, the Grant Notice and this Option Agreement. Optionee has reviewed the Plan, the Grant Notice and this Agreement in their entirety, has had an opportunity to obtain the advice of counsel prior to executing this Agreement and fully understands all provisions of the Plan, the Grant Notice and Agreement. Optionee hereby agrees to accept as binding, conclusive and final all decisions or interpretations of the Administrator upon any questions relating to the Plan and Agreement. Optionee further agrees to notify the Company upon any change in the residence address indicated below.

OPTIONEE

MICROCHIP TECHNOLOGY INCORPORATED

Signature

By:

Print Name

Title

Date

Address:

EXHIBIT A-1**MICROCHIP TECHNOLOGY INCORPORATED****2004 EQUITY INCENTIVE PLAN****EXERCISE NOTICE**

Microchip Technology Incorporated
Human Resources, Stock Administration

Exercise of Option. Effective as of today, _____, 20__ (date you sign this Exercise Notice), the undersigned ("Purchaser") hereby elects to purchase _____ number of shares (the "Shares") of the Common Stock of Microchip Technology Incorporated (the "Company") under and pursuant to the 2004 Equity Incentive Plan (the "Plan"), the Grant Notice (Grant No. _____), and associated Stock Option Agreement (the "Agreement"). Subject to adjustment in accordance with Section 19 of the Plan, the purchase price for the Shares shall be \$_____, as required by the Agreement.

Delivery of Payment. Purchaser herewith delivers to the Company the full purchase price for the Shares in accordance with Section 3 of the Agreement.

Representations of Purchaser. Purchaser acknowledges that Purchaser has received, read and understood the Plan, the Grant Notice and the Agreement and agrees to abide by and be bound by their terms and conditions.

Rights as Shareholder. Until the issuance (as evidenced by the appropriate entry on the books of the Company or of a duly authorized transfer agent of the Company) of the Shares, no right to vote or receive dividends or any other rights as a shareholder shall exist with respect to the Optioned Stock, notwithstanding the exercise of the Option. The Shares so acquired shall be issued to the Optionee as soon as practicable after exercise of the Option. No adjustment will be made for a dividend or other right where the record date precedes the date of issuance, except as provided in Section 19 of the Plan.

Tax Consultation. Purchaser understands that Purchaser may suffer adverse tax consequences as a result of Purchaser's purchase or disposition of the Shares. Purchaser represents that Purchaser has had the opportunity to consult with any tax consultants Purchaser deems advisable in connection with the purchase or disposition of the Shares and that Purchaser is not relying on the Company for any tax advice.

Entire Agreement; Governing Law. The Plan, Grant Notice, and Agreement are incorporated herein by reference and in conjunction with this Exercise Notice constitute the entire agreement of the parties with respect to the subject matter hereof and supersede in their entirety all prior undertakings and agreements of the Company and Purchaser with respect to the subject matter hereof. This agreement is governed by the internal substantive laws, but not the choice of law rules, of the state of Arizona, U.S.A.

Submitted by:

Accepted by:

PURCHASER

MICROCHIP TECHNOLOGY INCORPORATED

Signature

By

Print Name

Its

Date

Address:

Date Received (by Stock Administrator)

MICROCHIP TECHNOLOGY INCORPORATED

2004 EQUITY INCENTIVE PLAN

NOTICE OF GRANT OF RESTRICTED STOCK UNITS

Unless otherwise defined herein, the terms used in this Notice of Grant of Restricted Stock Units ("Grant Notice") shall have the same meanings as those defined in the 2004 Equity Incentive Plan (the "Plan").

Grantee: _____

You have been granted an Award of Restricted Stock Units ("RSU/s") subject to and in accordance with the express terms and conditions of the Plan and the Restricted Stock Unit Agreement attached hereto as Exhibit A ("Agreement"). Each such RSU is equivalent to the right to receive one share of Common Stock of the Company ("Share") for purposes of determining the number of Shares subject to this Award. No Shares will be issued until the vesting conditions of the Award described below are satisfied and the restrictions lapse. This Award does not entitle Grantee to any stockholder rights with respect to the underlying Shares until the vesting conditions of the Award described below are satisfied and the restrictions lapse. Additional terms of this Award are as follows:

Grant Number: _____

Grant Date: _____

Date Vesting Begins: _____

Vesting Period: _____

Purchase Price Per RSU: _____

Total Number of RSUs Granted: _____

Vesting Schedule. The RSUs vest and all restrictions lapse in a lump sum upon the Grantee's completion of twelve months continuous service as a Service Provider measured from the Grant Date.

Termination Period. This Award automatically terminates and Grantee's rights are forfeited with respect to any portion of the RSUs unvested on the date Grantee ceases to be a Service Provider. In no event shall this Award vest later than the Vesting Period above.

Choice of Languages For Employees of Canadian Locations Only. The undersigned agrees that it is his or her express wish that this form and all documents relating to his participation in the scheme be drawn in the English language only. Le soussigné convient que sa volonté expresse est que ce formulaire ainsi que tous les documents se rapportant à sa participation au régime soient rédigés en langue anglaise seulement.

Binding Agreements. By signature of Grantee and Company's representative below, the parties agree that this Grant Notice, the Agreement, and the Plan constitute Grantee's entire agreement with respect to this Award and agree to be bound by the terms therein. Grantee hereby agrees to accept as binding, conclusive and final all decisions or interpretations of the Administrator upon any questions relating to the Plan, the Agreement, and/or this Award. This Award may be modified by the Company, but in accordance with Section 21(c) of the Plan, it may not be modified adversely to Grantee's interest except by means of a writing signed by the Company and Grantee. The Company will administer the Plan from the United States of America. The internal laws of the State of Arizona, United States of America, but not its choice of law principles, will govern this Award.

GRANTEE

MICROCHIP TECHNOLOGY INCORPORATED

Signature: _____

By: _____

Address: _____

Steve Sanghi, President and CEO

Dated: _____

EXHIBIT A

MICROCHIP TECHNOLOGY INCORPORATED

2004 EQUITY INCENTIVE PLAN

RESTRICTED STOCK UNITS AGREEMENT

1. **Grant of Restricted Stock Units.** The Company hereby grants to the Grantee named in the Notice of Grant of Restricted Stock Units ("Grant Notice") an Award of Restricted Stock Units ("RSU/s"), as set forth in the Grant Notice and subject to the terms and conditions in this Restricted Stock Unit Agreement ("Agreement") and the Company's 2004 Equity Incentive Plan (the "Plan"). Unless otherwise defined herein, the terms defined in the Plan shall have the same defined meanings in this Agreement.

2. **Company's Obligation.** Each RSU represents the right to receive a Share in accordance with the Vesting Period in the Grant Notice. Unless and until the RSUs vest, the Grantee will have no right to receive Shares underlying such RSUs. Prior to actual distribution of Shares pursuant to any vested RSUs, such RSUs will represent an unsecured obligation of the Company, payable (if at all) only from the general assets of the Company.

3. **Vesting Schedule.** Subject to paragraph 4 of this Agreement, the RSUs awarded by this Agreement will vest and all restrictions lapse according to the vesting schedule specified in the Grant Notice.

4. Forfeiture upon Termination as a Service Provider. Notwithstanding any contrary provision of this Agreement or the Grant Notice, if the Grantee terminates service as an Service Provider for any or no reason prior to vesting, the unvested RSUs awarded by this Agreement will thereupon be forfeited at no cost to the Company.
5. Payment after Vesting. Any RSUs that vest in accordance with paragraph 3 of this Agreement will be paid to the Grantee (or in the event of the Grantee's death, to his or her estate) in Shares, provided that to the extent determined appropriate by the Company, any federal, state and local withholding taxes with respect to such RSUs will be paid by the Grantee in the manner allowed by the Company.
6. Payments after Death. Any distribution or delivery to be made to the Grantee under this Agreement will, if the Grantee is then deceased, be made to the administrator or executor of the Grantee's estate. Any such administrator or executor must furnish the Company with (a) written notice of his or her status as transferee, and (b) evidence satisfactory to the Company to establish the validity of the transfer and compliance with any laws or regulations pertaining to said transfer.
7. Grant is Not Transferable. Except to the limited extent provided in paragraph 6 of this Agreement, this grant and the rights and privileges conferred hereby will not be transferred, assigned, pledged or hypothecated in any way (whether by operation of law or otherwise) and will not be subject to sale under execution, attachment or similar process. Upon any attempt to transfer, assign, pledge,

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hypothecate or otherwise dispose of this grant, or any right or privilege conferred hereby, or upon any attempted sale under any execution, attachment or similar process, this grant and the rights and privileges conferred hereby immediately will become null and void.

8. Rights as Stockholder. Neither the Grantee nor any person claiming under or through the Grantee will have any of the rights or privileges of a stockholder of the Company in respect of any Shares deliverable hereunder unless and until certificates representing such Shares will have been issued, recorded on the records of the Company or its transfer agents or registrars, and delivered to the Grantee or Grantee's broker or had the Shares electronically transferred to Grantee's account.
9. Tax Obligations. Grantee agrees to make appropriate arrangements with the Company (or the Parent or Subsidiary employing or retaining Grantee) in accordance with the procedures offered by the Company for the satisfaction of all Federal, state, local and foreign income and employment tax withholding requirements applicable to the issuance of Shares pursuant to an RSU Award. The Administrator may in its sole discretion determine whether the minimum required withholding taxes with respect to such RSUs will be paid by selling a portion of vested shares or by direct payment from the Grantee to the Company, by some other method, or by some combination thereof.

The Grantee grants to the Company the irrevocable authority, as agent of Grantee and on his behalf, to sell or procure the sale of sufficient Shares subject to this Award so that the net proceeds receivable by the Company are as far as possible equal to but not less than the amount of any tax the Grantee is liable for and the Company shall account to Grantee for any balance.

Grantee acknowledges and agrees that the Company may refuse to deliver Shares if Grantee has not made appropriate arrangements with the Company to satisfy the minimum tax withholding requirements.

10. Acknowledgments. The Grantee expressly acknowledges the following:
- (a) The Company (whether or not Grantee's employer) is granting the Award. That the grant of the Award, future grants of Awards, and benefits and rights provided under the Plan are at the complete discretion of the Company and do not constitute regular or periodic payments. No grant of Awards will be deemed to create any obligation to grant any further Awards, whether or not such a reservation is explicitly stated at the time of such a grant. The benefits and rights provided under the Plan are not to be considered part of Grantee's salary or compensation for purposes of calculating any severance, resignation, redundancy or other end of service payments, vacation, bonuses, long-term service awards, indemnification, pension or retirement benefits, or any other payments, benefits or rights of any kind. Grantee waives any and all rights to compensation or damages as a result of the termination of employment with the Company or its subsidiaries for any reason whatsoever insofar as those rights result or may result from:
 - (i) the loss or diminution in value of such rights under the Plan, or
 - (ii) Grantee ceasing to have any rights under, or ceasing to be entitled to any rights under the Plan as a result of such termination.
 - (b) The Company has the right, at any time to amend, suspend or terminate the Plan. The Plan will not be deemed to constitute, and will not be construed by Grantee to constitute, part of the terms and conditions of employment, and that the Company will not incur any liability of any kind to Grantee as a result of any change or amendment, or any cancellation, of the Plan at any time.

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- (c) The Grantee's employment with the Company and its Subsidiaries is not affected at all by any Award and it is agreed by the Grantee not to create an entitlement. Accordingly, the terms of the Grantee's employment with the Company and its Subsidiaries will be determined from time to time by the Company or the Subsidiary employing the Grantee (as the case may be), and the Company or the Subsidiary will have the right, which is hereby expressly reserved, to terminate or change the terms of the employment of the Grantee at any time for any reason whatsoever, with or without good cause or notice, except as may be expressly prohibited by the laws of the jurisdiction in which the Grantee is employed.
- (d) By entering into this Agreement, and as a condition of the grant of the Award, Grantee consents to the collection, use, and transfer of personal data as described in this subsection to the full extent permitted by and in full compliance with Applicable Law.
 - (i) Grantee understands that the Company and its Subsidiaries hold certain personal information about the Grantee, including, but not limited to, name, home address and telephone number, date of birth, social insurance number, salary, nationality, job title, any Shares or directorships held in the Company, details of all Awards or other entitlement to Shares awarded, canceled, exercised, vested, unvested, or outstanding in Grantee's favor, for the purpose of managing and administering the Plan ("Data").
 - (ii) Grantee further understands that the Company and/or its Subsidiaries will transfer Data among themselves as necessary for the purposes of implementation, administration, and management of Grantee's participation in the Plan, and that the Company and/or its Subsidiary may each further transfer Data to any third parties assisting the Company in the implementation, administration, and management of the Plan ("Data Recipients").
 - (iii) Grantee understands that these Data Recipients may be located in Grantee's country of residence or elsewhere, such as the United States. Grantee authorizes the Data Recipients to receive, possess, use, retain, and transfer Data in electronic or other form, for the purposes of implementing, administering, and

managing Grantee's participation in the Plan, including any transfer of such Data, as may be required for Plan administration and/or the subsequent holding of Shares on Grantee's behalf, to a broker or third party with whom the Shares acquired on exercise may be deposited.

- (iv) Grantee understands that Grantee may, at any time, review the Data, request that any necessary amendments be made to it, or withdraw Grantee's consent herein in writing by contacting the Company. Grantee further understands that withdrawing consent may affect Grantee's ability to participate in the Plan.

(e) Choice of Language.

- (i) For Employees of Canadian Locations: The undersigned agrees that it is his or her express wish that this form and all documents relating to his participation in the scheme be drawn in the English language only. Le soussigné convient que sa volonté expresse est que ce formulaire ainsi que tous les documents se rapportant à sa participation au régime soient rédigés en langue anglaise seulement.
- (ii) For Employees of Locations Other than Canada: Grantee has received this Agreement and any other related communications and consents to having received these documents solely in English.

11. **Binding Agreement.** Subject to the limitation on the transferability of this grant contained herein, this Agreement will be binding upon and inure to the benefit of the heirs, legatees, legal representatives, successors and assigns of the parties hereto.

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12. **Additional Conditions to Issuance of Stock.** If at any time the Company will determine, in its discretion, that the listing, registration or qualification of the Shares upon any securities exchange or under any state or federal law, or the consent or approval of any governmental regulatory authority is necessary or desirable as a condition to the issuance of Shares to the Grantee (or his or her estate), such issuance will not occur unless and until such listing, registration, qualification, consent or approval will have been effected or obtained free of any conditions not acceptable to the Company. The Company will make all reasonable efforts to meet the requirements of any such state or federal law or securities exchange and to obtain any such consent or approval of any such governmental authority.

13. **Administrator Authority.** The Administrator has the power to interpret the Plan, the Grant Notice and this Agreement and to adopt such rules for the administration, interpretation and application thereof as are consistent therewith and to interpret or revoke any such rules (including, but not limited to, the determination of whether or not any RSUs have vested). All actions taken and all interpretations and determinations made by the Administrator in good faith will be final and binding upon Grantee, the Company and all other interested persons. No member of the Administrator will be personally liable for any action, determination or interpretation made in good faith with respect to the Plan, the Grant Notice or this Agreement.

14. **Notice Requirement.** Where there is a legal requirement for any notice or document to be sent to any person by any other person, it shall be considered sent if an electronic transmission of the relevant information is sent in a form previously determined as being acceptable to the Administrator. For the avoidance of doubt, the Administrator may dispense with the requirement to tender a certificate on the issuance of Shares under an RSU Award where the Administrator authorizes any system permitting electronic notification.

15. **Address for Notices.** Any notice to be given to the Company under the terms of this Agreement will be addressed to the Company at 2355 West Chandler Boulevard, Chandler AZ 85224, Attn: Stock Administration, or at such other address as the Company may hereafter designate in writing or electronically.

16. **Entire Agreement; Governing Law.** The Plan and Grant Notice are incorporated herein by reference. The Plan, Grant Notice and this Agreement constitute the entire agreement of the parties with respect to the subject matter hereof and supersede in their entirety all prior undertakings and agreements of the Company and Grantee with respect to the subject matter hereof, and may not be modified adversely to the Grantee's interest except by means of a writing signed by the Company and Grantee. The Company will administer the Plan from the United States of America. This Agreement, the Grant Notice and all Awards are governed by the internal substantive laws, but not the choice of law principles, of the State of Arizona, United States of America.

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By Grantee's signature, Grantee agrees that this Award is granted under and governed by the terms and conditions of the Plan, the Grant Notice and this Agreement. Grantee has reviewed the Plan, the Grant Notice and this Agreement in their entirety, has had an opportunity to obtain the advice of counsel prior to executing this Agreement and fully understands all provisions of the Plan, the Grant Notice and this Agreement. Grantee hereby agrees to accept as binding, conclusive and final all decisions or interpretations of the Administrator upon any questions relating to the Plan, the Grant Notice and this Agreement.

GRANTEE

MICROCHIP TECHNOLOGY INCORPORATED

Signature

By _____
Steve Sanghi, President and CEO

Print Name

Date

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MICROCHIP TECHNOLOGY INCORPORATED

LIST OF SIGNIFICANT SUBSIDIARIES

Microchip Technology (Thailand) Co., Ltd.
14 Moo 1, T. Wangtakien
A. Muang Chacherngsao
Chacherngsao 24000
Thailand

Microchip Technology (Barbados) Incorporated
Hastings Business Services Limited
Hastings, Christ Church
Barbados

CONSENT OF ERNST & YOUNG LLP, INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We consent to the incorporation by reference in the Registration Statements (Form S-8 Nos. 33-59686, 33-80072, 33-81690, 33-83196, 333-872, 333-40791, 333-67215, 333-93571, 333-51322, 333-53876, 333-73506, 333-96791, 333-99655, 333-101696, 333-103764, 333-109486 and 333-119939) of Microchip Technology Incorporated of our reports dated May 17, 2005 with respect to the consolidated financial statements of Microchip Technology Incorporated, Microchip Technology Incorporated management's assessment of the effectiveness of internal control over financial reporting, and the effectiveness of internal control over financial reporting of Microchip Technology Incorporated, included in this Annual Report (Form 10-K) for the year ended March 31, 2005.

/s/ Ernst & Young LLP

Phoenix, Arizona
May 20, 2005

CERTIFICATION

I, Steve Sanghi, certify that:

1. I have reviewed, this Form 10-K of Microchip Technology Incorporated;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 23, 2005

/s/ Steve Sanghi
Steve Sanghi
President and CEO

CERTIFICATION

I, Gordon Parnell, certify that:

1. I have reviewed, this Form 10-K of Microchip Technology Incorporated;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 23, 2005

/s/ Gordon Parnell
Gordon Parnell
Vice President and CFO

CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER
PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

I, Steve Sanghi, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Annual Report of Microchip Technology Incorporated on Form 10-K for the period ended March 31, 2005 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Form 10-K fairly presents, in all material respects, the financial condition and results of operations of Microchip Technology Incorporated.

By: /s/ Steve Sanghi
Name: Steve Sanghi
Title: President and Chief Executive Officer
Date: May 23, 2005

I, Gordon W. Parnell, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Annual Report of Microchip Technology Incorporated on Form 10-K for the period ended March 31, 2005 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Form 10-K fairly presents, in all material respects, the financial condition and results of operations of Microchip Technology Incorporated.

By: /s/ Gordon W. Parnell
Name: Gordon W. Parnell
Title: Vice President and Chief Financial Officer
Date: May 23, 2005
