UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

(Mark One)

☒ **Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the quarterly period ended September 30, 2021

or

☐ **Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the transition period from ______ to ______

Commission File Number 000-23441

POWER INTEGRATIONS, INC.
(Exact name of registrant as specified in its charter)

Delaware	**94-3065014**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
5245 Hellyer Avenue **San Jose, California**	**95138**
(Address of Principal Executive Offices)	(Zip Code)

(408) 414-9200
(Registrant's telephone number, including area code)

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock	**POWI**	The Nasdaq Global Select Market

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

Indicate by check mark whether the registrant submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act:

Large Accelerated Filer	☒	Accelerated Filer	☐
Non-accelerated Filer	☐	Smaller Reporting Company	☐
		Emerging Growth Company	☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Shares Outstanding at October 25, 2021
Common Stock, $0.001 par value	60,331,685

POWER INTEGRATIONS, INC.

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Cautionary Note Regarding Forward-Looking Statements

This Quarterly Report on Form 10-Q includes a number of forward-looking statements that involve many risks and uncertainties. Forward-looking statements are identified by the use of the words “would,” “could,” “will,” “may,” “expect,” “believe,” “should,” “anticipate,” “if,” “future,” “intend,” “plan,” “estimate,” “potential,” “target,” “seek,” or “continue” and similar words and phrases, including the negatives of these terms, or other variations of these terms, that denote future events. These statements reflect our current views with respect to future events and our potential financial performance and are subject to risks and uncertainties that could cause our actual results and financial position to differ materially and/or adversely from what is projected or implied in any forward-looking statements included in this Form 10-Q. These factors include, but are not limited to: the novel coronavirus pandemic (COVID-19), which has disrupted and may again disrupt our operations, including our manufacturing, research and development, and sales and marketing activities, which in turn could have a material adverse impact on our business and has or could exacerbate the risks discussed below; if demand for our products declines in our major end markets, our net revenues will decrease; our products are sold through distributors, which limits our direct interaction with our end customers, therefore reducing our ability to forecast sales and increasing the complexity of our business; we depend on third-party suppliers to provide us with wafers for our products, and if they fail to provide us sufficient quantities of wafers, our business may suffer; intense competition in the high-voltage power supply industry may lead to a decrease in our average selling price and reduced sales volume of our products; if our products do not penetrate additional markets, our business will not grow as we expect; we do not have long-term contracts with any of our customers and if they fail to place, or if they cancel or reschedule orders for our products, our operating results and our business may suffer; if we are unable to adequately protect or enforce our intellectual property rights, we could lose market share, incur costly litigation expenses, suffer incremental price erosion or lose valuable assets, any of which could harm our operations and negatively impact our profitability; and the other risk factors described under the caption “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2020, and in Part I, Item 2 - “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and elsewhere in this Quarterly Report on Form 10-Q. We make these forward-looking statements based upon information available on the date of this Form 10-Q, and we expressly disclaim any obligation to update or alter any forward-looking statements, whether as a result of new information or otherwise, except as required by laws.

In addition, statements that “we believe” and similar statements reflect our beliefs and opinions on the relevant subject. These statements are based upon information available to us as of the date of this Quarterly Report on Form 10-Q, and while we believe such information forms a reasonable basis for such statements, such information may be limited or incomplete, and our statements should not be read to indicate that we have conducted an exhaustive inquiry into, or review of, all potentially available relevant information. These statements are inherently uncertain and investors are cautioned not to unduly rely upon these statements.

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

POWER INTEGRATIONS, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

(In thousands)	September 30, 2021	December 31, 2020
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 262,435	$ 258,874
Short-term marketable securities	286,506	190,318
Accounts receivable, net	38,872	35,910
Inventories	91,814	102,878
Prepaid expenses and other current assets	23,720	13,252
Total current assets	703,347	601,232
PROPERTY AND EQUIPMENT, net	168,498	166,188
INTANGIBLE ASSETS, net	9,807	12,506
GOODWILL	91,849	91,849
DEFERRED TAX ASSETS	3,266	3,339
OTHER ASSETS	28,223	28,225
Total assets	$ 1,004,990	$ 903,339
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 40,390	$ 34,712
Accrued payroll and related expenses	14,064	14,806
Taxes payable	970	902
Other accrued liabilities	10,638	12,106
Total current liabilities	66,062	62,526
LONG-TERM INCOME TAXES PAYABLE	14,644	15,588
OTHER LIABILITIES	15,928	14,814
Total liabilities	96,634	92,928
COMMITMENTS AND CONTINGENCIES (Notes 11, 12 and 13)		
STOCKHOLDERS' EQUITY:		
Common stock	28	28
Additional paid-in capital	189,790	190,920
Accumulated other comprehensive loss	(3,249)	(2,163)
Retained earnings	721,787	621,626
Total stockholders' equity	908,356	810,411
Total liabilities and stockholders' equity	$ 1,004,990	$ 903,339

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

POWER INTEGRATIONS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

(In thousands, except per share amounts)	Three Months Ended September 30, 2021	Three Months Ended September 30, 2020	Nine Months Ended September 30, 2021	Nine Months Ended September 30, 2020
NET REVENUES	$ 176,776	$ 121,129	$ 530,623	$ 337,625
COST OF REVENUES	85,037	61,560	263,160	168,040
GROSS PROFIT	91,739	59,569	267,463	169,585
OPERATING EXPENSES:				
Research and development	21,137	20,868	62,905	59,790
Sales and marketing	15,624	13,658	45,037	40,168
General and administrative	9,386	10,302	28,767	26,867
Total operating expenses	46,147	44,828	136,709	126,825
INCOME FROM OPERATIONS	45,592	14,741	130,754	42,760
OTHER INCOME	206	877	976	4,134
INCOME BEFORE INCOME TAXES	45,798	15,618	131,730	46,894
PROVISION FOR INCOME TAXES	3,764	798	8,017	2,996
NET INCOME	$ 42,034	$ 14,820	$ 123,713	$ 43,898
EARNINGS PER SHARE:				
Basic	$ 0.70	$ 0.25	$ 2.05	$ 0.74
Diluted	$ 0.69	$ 0.24	$ 2.01	$ 0.72
SHARES USED IN PER SHARE CALCULATION:				
Basic	60,319	59,823	60,350	59,582
Diluted	61,363	60,852	61,466	60,668

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

POWER INTEGRATIONS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands)	**2021**	**2020**	**2021**	**2020**
Net income	$ 42,034	$ 14,820	$ 123,713	$ 43,898
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustments, net of $0 tax in each of the three and nine months ended September 30, 2021 and 2020	(154)	(51)	(212)	(364)
Unrealized gain (loss) on marketable securities, net of $0 tax in each of the three and nine months ended September 30, 2021 and 2020	7	(633)	(904)	981
Amortization of defined benefit pension items, net of tax of $6 and $147 in the three and nine months ended September 30, 2021, respectively, and $37 and $92 in the three and nine months ended September 30, 2020, respectively	53	49	30	158
Total other comprehensive income (loss)	(94)	(635)	(1,086)	775
TOTAL COMPREHENSIVE INCOME	$ 41,940	$ 14,185	$ 122,627	$ 44,673

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

POWER INTEGRATIONS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(Unaudited)

(In thousands)	Three Months Ended September 30, 2021	Three Months Ended September 30, 2020	Nine Months Ended September 30, 2021	Nine Months Ended September 30, 2020
Common stock				
Beginning balance	$ 28	$ 28	$ 28	$ 28
Common stock issued under employee stock plans	—	—	1	—
Repurchase of common stock	—	—	(1)	—
Ending balance	28	28	28	28
Additional paid-in capital				
Beginning balance	185,878	168,470	190,920	152,117
Common stock issued under employee stock plans	4,058	3,364	7,709	9,662
Repurchase of common stock	(9,791)	—	(36,164)	(2,636)
Stock-based compensation	9,645	9,358	27,325	22,049
Ending balance	189,790	181,192	189,790	181,192
Accumulated other comprehensive loss				
Beginning balance	(3,155)	(1,720)	(2,163)	(3,130)
Other comprehensive income (loss)	(94)	(635)	(1,086)	775
Ending balance	(3,249)	(2,355)	(3,249)	(2,355)
Retained earnings				
Beginning balance	687,593	592,694	621,626	575,531
Net income	42,034	14,820	123,713	43,898
Payment of dividends to stockholders	(7,840)	(6,582)	(23,552)	(18,497)
Ending balance	721,787	600,932	721,787	600,932
Total stockholders' equity	$ 908,356	$ 779,797	$ 908,356	$ 779,797

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

POWER INTEGRATIONS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

(In thousands)	Nine Months Ended September 30, 2021	Nine Months Ended September 30, 2020
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 123,713	$ 43,898
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	23,400	17,071
Amortization of intangibles	2,699	3,283
Loss on disposal of property and equipment	2,200	311
Stock-based compensation expense	27,325	22,049
Amortization of premium on marketable securities	775	525
Deferred income taxes	(12)	100
Increase in accounts receivable allowance for credit losses	17	155
Change in operating assets and liabilities:		
Accounts receivable	(2,979)	(5,328)
Inventories	11,064	(14,425)
Prepaid expenses and other assets	(4,973)	6,133
Accounts payable	6,633	6,365
Taxes payable and accrued liabilities	(6,157)	(864)
Net cash provided by operating activities	183,705	79,273
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(30,305)	(35,738)
Proceeds from sale of property and equipment	35	331
Purchases of marketable securities	(381,903)	(66,066)
Proceeds from sales and maturities of marketable securities	284,036	86,995
Net cash used in investing activities	(128,137)	(14,478)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Issuance of common stock under employee stock plans	7,710	9,662
Repurchase of common stock	(36,165)	(2,636)
Payments of dividends to stockholders	(23,552)	(18,497)
Net cash used in financing activities	(52,007)	(11,471)
NET INCREASE IN CASH AND CASH EQUIVALENTS	3,561	53,324
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	258,874	178,690
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 262,435	$ 232,014
SUPPLEMENTAL DISCLOSURE OF NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Unpaid property and equipment	$ 4,983	$ 14,180
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid (received) for income taxes, net	$ 16,272	$ (1,927)

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

1. BASIS OF PRESENTATION:

The condensed consolidated financial statements include the accounts of Power Integrations, Inc., a Delaware corporation (the "Company"), and its wholly owned subsidiaries. Significant intercompany accounts and transactions have been eliminated in consolidation.

While the financial information furnished is unaudited, the condensed consolidated financial statements included in this report reflect all adjustments (consisting only of normal recurring adjustments) that the Company considers necessary for the fair presentation of the results of operations for the interim periods covered and the financial condition of the Company at the date of the interim balance sheet in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP"). The results for interim periods are not necessarily indicative of the results for the entire year. The condensed consolidated financial statements should be read in conjunction with the Company's consolidated financial statements and the notes thereto for the year ended December 31, 2020, included in its Form 10-K filed on February 5, 2021, with the Securities and Exchange Commission.

2. SIGNIFICANT ACCOUNTING POLICIES AND RECENT ACCOUNTING PRONOUNCEMENTS:

Significant Accounting Policies and Estimates

No material changes have been made to the Company's significant accounting policies disclosed in Note 2, *Significant Accounting Policies and Recent Accounting Pronouncements*, in its Annual Report on Form 10-K, filed on February 5, 2021, for the year ended December 31, 2020.

Recent Accounting Pronouncements

The Company has considered all recent accounting pronouncements issued, but not yet effective, and does not expect any to have a material effect on the Company's condensed consolidated financial statements.

3. COMPONENTS OF THE COMPANY'S CONDENSED CONSOLIDATED BALANCE SHEETS:

Accounts Receivable

(In thousands)	September 30, 2021	December 31, 2020
Accounts receivable trade	$ 91,299	$ 66,703
Allowance for ship and debit	(46,056)	(26,435)
Allowance for stock rotation and rebate	(5,927)	(3,931)
Allowance for credit losses	(444)	(427)
Total	$ 38,872	$ 35,910

The Company maintains an allowance for estimated credit losses resulting from the inability of customers to make required payments. This allowance is established using estimates formulated by the Company's management based upon factors such as the composition of the accounts receivable aging, historical losses, changes in payments patterns, customer creditworthiness, and current economic trends. Receivables determined to be uncollectible are written off and deducted from the allowance.

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands)	2021	2020	2021	2020
Beginning balance	$ (518)	$ (609)	$ (427)	$ (763)
Provision for credit loss expense	(325)	(309)	(902)	(309)
Receivables written off	74	—	74	154
Recoveries collected	325	—	811	—
Ending balance	$ (444)	$ (918)	$ (444)	$ (918)

POWER INTEGRATIONS, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Inventories

(In thousands)	September 30, 2021	December 31, 2020
Raw materials	$ 27,087	$ 32,131
Work-in-process	36,338	39,469
Finished goods	28,389	31,278
Total	$ 91,814	$ 102,878

Intangible Assets

	September 30, 2021			December 31, 2020		
(In thousands)	Gross	Accumulated Amortization	Net	Gross	Accumulated Amortization	Net
Domain name	$ 1,261	$ —	$ 1,261	$ 1,261	$ —	$ 1,261
Developed technology	37,960	(31,051)	6,909	37,960	(29,126)	8,834
Customer relationships	16,700	(16,277)	423	16,700	(15,687)	1,013
Technology licenses	1,926	(712)	1,214	1,926	(528)	1,398
Total intangible assets	$ 57,847	$ (48,040)	$ 9,807	$ 57,847	$ (45,341)	$ 12,506

The estimated future amortization expense related to finite-lived intangible assets at September 30, 2021, is as follows:

Fiscal Year	Estimated Amortization (In thousands)
2021 (remaining three months)	$ 795
2022	2,415
2023	2,173
2024	1,279
2025	832
Thereafter	1,052
Total	$ 8,546

Accumulated Other Comprehensive Loss

Changes in accumulated other comprehensive loss for the three and nine months ended September 30, 2021 and 2020, were as follows:

	Unrealized Gains and Losses on Marketable Securities		Defined Benefit Pension Items		Foreign Currency Items		Total	
	Three Months Ended September 30,		Three Months Ended September 30,		Three Months Ended September 30,		Three Months Ended September 30,	
(In thousands)	2021	2020	2021	2020	2021	2020	2021	2020
Beginning balance	$ (21)	$ 2,197	$ (1,664)	$ (2,375)	$ (1,470)	$ (1,542)	$ (3,155)	$ (1,720)
Other comprehensive income (loss) before reclassifications	7	(633)	—	—	(154)	(51)	(147)	(684)
Amounts reclassified from accumulated other comprehensive loss	—	—	53 (1)	49 (1)	—	—	53	49
Net-current period other comprehensive income (loss)	7	(633)	53	49	(154)	(51)	(94)	(635)
Ending balance	$ (14)	$ 1,564	$ (1,611)	$ (2,326)	$ (1,624)	$ (1,593)	$ (3,249)	$ (2,355)

(1) This component of accumulated other comprehensive income (loss) is included in the computation of net periodic pension cost for the three months ended September 30, 2021 and 2020.

	Unrealized Gains and Losses on Marketable Securities		Defined Benefit Pension Items		Foreign Currency Items		Total	
	Nine Months Ended September 30,		Nine Months Ended September 30,		Nine Months Ended September 30,		Nine Months Ended September 30,	
(In thousands)	**2021**	**2020**	**2021**	**2020**	**2021**	**2020**	**2021**	**2020**
Beginning balance	$ 890	$ 583	$ (1,641)	$ (2,484)	$ (1,412)	$ (1,229)	$ (2,163)	$ (3,130)
Other comprehensive income (loss) before reclassifications	(904)	981	—	—	(212)	(364)	(1,116)	617
Amounts reclassified from accumulated other comprehensive loss	—	—	30 (1)	158 (1)	—	—	30	158
Net-current period other comprehensive income (loss)	(904)	981	30	158	(212)	(364)	(1,086)	775
Ending balance	$ (14)	$ 1,564	$ (1,611)	$ (2,326)	$ (1,624)	$ (1,593)	$ (3,249)	$ (2,355)

(1) This component of accumulated other comprehensive income (loss) is included in the computation of net periodic pension cost for the nine months ended September 30, 2021 and 2020.

4. FAIR VALUE MEASUREMENTS:

The FASB established a three-tier value hierarchy, which prioritizes the inputs used in measuring fair value as follows: (Level 1) observable inputs such as quoted prices for identical assets in active markets; (Level 2) inputs other than the quoted prices in active markets that are observable either directly or indirectly; and (Level 3) unobservable inputs in which there is little or no market data, which requires the Company to develop its own assumptions. This hierarchy requires the Company to use observable market data, when available, and to minimize the use of unobservable inputs when determining fair value.

The Company’s cash equivalents and short-term marketable securities are classified within Level 1 or Level 2 of the fair-value hierarchy because they are valued using quoted market prices, broker or dealer quotations, or alternative pricing sources with reasonable levels of price transparency.

The fair-value hierarchy of the Company’s cash equivalents and marketable securities at September 30, 2021, and December 31, 2020, was as follows:

	Fair Value Measurement at September 30, 2021		
(In thousands)	**Total Fair Value**	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**
Commercial paper	$ 282,192	$ —	$ 282,192
Corporate securities	178,067	—	178,067
Money market funds	22,028	22,028	—
Total	$ 482,287	$ 22,028	$ 460,259

	Fair Value Measurement at December 31, 2020		
(In thousands)	**Total Fair Value**	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**
Commercial paper	$ 253,855	$ —	$ 253,855
Corporate securities	146,658	—	146,658
Money market funds	1,634	1,634	—
Total	$ 402,147	$ 1,634	$ 400,513

The Company did not transfer any investments between Level 1 and Level 2 of the fair-value hierarchy in the nine months ended September 30, 2021, and the twelve months ended December 31, 2020.

5. MARKETABLE SECURITIES:

Amortized cost and estimated fair market value of marketable securities classified as available-for-sale (excluding cash equivalents) at September 30, 2021, were as follows:

	Amortized	Gross Unrealized		Estimated Fair
(In thousands)	**Cost**	**Gains**	**Losses**	**Market Value**
Investments due in 3 months or less:				
Commercial paper	$ 69,079	$ —	$ —	$ 69,079
Corporate securities	13,285	12	(1)	13,296
Total	82,364	12	(1)	82,375
Investments due in 4-12 months:				
Commercial paper	40,500	—	—	40,500
Corporate securities	15,361	—	(4)	15,357
Total	55,861	—	(4)	55,857
Investments due in 12 months or greater:				
Corporate securities	148,295	51	(72)	148,274
Total	148,295	51	(72)	148,274
Total marketable securities	$ 286,520	$ 63	$ (77)	$ 286,506

Accrued interest receivable was $1.0 million at September 30, 2021 and was recorded within prepaid expenses and other current assets on the condensed consolidated balance sheet.

Amortized cost and estimated fair market value of marketable securities classified as available-for-sale (excluding cash equivalents) at December 31, 2020, were as follows:

	Amortized	Gross Unrealized		Estimated Fair
(In thousands)	**Cost**	**Gains**	**Losses**	**Market Value**
Investments due in 3 months or less:				
Commercial paper	$ 43,660	$ —	$ —	$ 43,660
Corporate securities	19,846	44	—	19,890
Total	63,506	44	—	63,550
Investments due in 4-12 months:				
Corporate securities	125,922	846	—	126,768
Total	125,922	846	—	126,768
Total marketable securities	$ 189,428	$ 890	$ —	$ 190,318

Accrued interest receivable was $0.8 million at December 31, 2020 and was recorded within prepaid expenses and other current assets on the condensed consolidated balance sheet.

POWER INTEGRATIONS, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table summarizes marketable securities classified as available-for-sale (excluding cash equivalents) in a continuous unrealized loss position for which an allowance for credit losses was not recorded at September 30, 2021:

(In thousands)	Less Than 12 Months		12 Months or Longer		Total	
	Estimated Fair Market Value	Gross Unrealized Losses	Estimated Fair Market Value	Gross Unrealized Losses	Estimated Fair Market Value	Gross Unrealized Losses
Corporate securities	$ 93,255	$ (77)	$ —	$ —	$ 93,255	$ (77)
Total marketable securities	$ 93,255	$ (77)	$ —	$ —	$ 93,255	$ (77)

In the three and nine months ended September 30, 2021 and 2020, no unrealized losses on marketable securities were recognized in income.

The Company does not intend to sell and it is unlikely that it will be required to sell the securities prior to their anticipated recovery. The issuers are high quality (investment grade) and the decline in fair value is largely due to changes in interest rates and other market conditions. Additionally, the issuers continue to make timely interest payments on the marketable securities with the fair value expected to recover as they reach maturity.

6. STOCK-BASED COMPENSATION:

The following table summarizes the stock-based compensation expense recognized in accordance with ASC 718-10 for the three and nine months ended September 30, 2021 and 2020:

(In thousands)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2021	2020	2021	2020
Cost of revenues	$ 664	$ 602	$ 1,935	$ 1,250
Research and development	3,055	2,976	8,605	7,436
Sales and marketing	2,201	1,900	5,540	4,550
General and administrative	3,725	3,880	11,245	8,813
Total stock-based compensation expense	$ 9,645	$ 9,358	$ 27,325	$ 22,049

Stock-based compensation expense in the three months ended September 30, 2021, was approximately $9.6 million, comprising approximately $5.0 million related to restricted stock unit (RSU) awards, $4.2 million related to performance-based (PSU) awards and long-term performance-based (PRSU) awards and $0.4 million related to the Company's employee stock purchase plan. Stock-based compensation expense in the nine months ended September 30, 2021, was approximately $27.3 million, comprising approximately $15.0 million related to RSUs, $10.9 million related to PSUs and PRSUs and $1.4 million related to the Company's employee stock purchase plan.

Stock-based compensation expense in the three months ended September 30, 2020, was approximately $9.4 million, comprising approximately $4.7 million related to RSUs, $4.2 million related to PSUs and PRSUs and $0.5 million related to the Company's employee stock purchase plan. Stock-based compensation expense in the nine months ended September 30, 2020, was approximately $22.0 million, comprising approximately $14.1 million related to RSUs, $6.6 million related to PSUs and PRSUs and $1.3 million related to the Company's employee stock purchase plan.

POWER INTEGRATIONS, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Stock Options

A summary of stock options outstanding as of September 30, 2021, and activity during the nine months ended, is presented below:

	Shares (In thousands)	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (In years)	Aggregate Intrinsic Value (In thousands)
Outstanding at January 1, 2021	92	$ 20.63		
Granted	—	—		
Exercised	(80)	$ 20.50		
Forfeited or expired	—	—		
Outstanding at September 30, 2021	12	$ 21.44	0.60	$ 931
Vested and exercisable at September 30, 2021	12		0.60	$ 931

PSU Awards

Under the performance-based awards program, the Company grants awards in the performance year in an amount equal to twice the target number of shares to be issued if the maximum performance metrics are met. The number of shares that are released at the end of the performance year can range from zero to 200% of the target number depending on the Company's performance. The performance metrics of this program are annual targets consisting of a combination of net revenue, non-GAAP operating income and strategic goals.

As the net revenue, non-GAAP operating income and strategic goals are considered performance conditions, expense associated with these awards, net of estimated forfeitures, is recognized over the service period based on an assessment of the expected achievement of the performance targets. The fair value of these PSUs is determined using the fair value of the Company's common stock on the date of the grant, reduced by the discounted present value of dividends expected to be declared before the awards vest. If the performance conditions are not achieved, no compensation cost is recognized and any previously recognized compensation is reversed.

In January 2021, it was determined that approximately 150,000 shares subject to the PSUs granted in 2020 vested in aggregate; the shares were released to the Company's employees and executives in the first quarter of 2021.

A summary of PSUs outstanding as of September 30, 2021, and activity during the nine months ended, is presented below:

	Shares (In thousands)	Weighted-Average Grant Date Fair Value Per Share	Weighted-Average Remaining Contractual Term (In years)	Aggregate Intrinsic Value (In thousands)
Outstanding at January 1, 2021	150	$ 46.27		
Granted	105	$ 84.40		
Vested	(150)	$ 46.27		
Forfeited	(1)	$ 85.01		
Outstanding at September 30, 2021	104	$ 84.39	0.25	$ 10,342
Outstanding and expected to vest at September 30, 2021	104		0.25	$ 10,342

PRSU Awards

The Company's PRSU program provides for the issuance of PRSUs which will vest based on the Company's performance measured against the PRSU program's established performance targets. PRSUs are granted in an amount equal to twice the target number of shares to be issued if the maximum performance metrics are met. The actual number of shares the recipient receives is determined at the end of a three-year performance period based on results achieved versus the Company's performance goals, and may range from zero to 200% of the target number. The performance goals for PRSUs granted in fiscal 2019 were based on the Company's annual revenue growth, while the PRSUs granted in 2020 and 2021 were based on the Company's compound annual growth rate ("CAGR") of revenue as measured against the revenue CAGR of the analog semiconductor industry, in each case over the respective three-year performance period. Expense associated with these awards, net of estimated forfeitures, is recorded throughout the year based on an assessment of the expected achievement of the performance targets. If the performance conditions are not achieved, no compensation cost is recognized and any previously recognized compensation is reversed.

In January 2021 it was determined that approximately 6,000 shares subject to the PRSUs granted in 2018 vested in aggregate; the shares were released to the Company's executives in the first quarter of 2021.

A summary of PRSUs outstanding as of September 30, 2021, and activity during the nine months ended, is presented below:

	Shares (In thousands)	Weighted-Average Grant Date Fair Value Per Share	Weighted-Average Remaining Contractual Term (In years)	Aggregate Intrinsic Value (In thousands)
Outstanding at January 1, 2021	301	$ 41.90		
Granted	103	$ 82.92		
Vested	(6)	$ 29.95		
Forfeited	(15)	$ 40.05		
Outstanding at September 30, 2021	383	$ 53.14	1.17	$ 37,871
Outstanding and expected to vest at September 30, 2021	383		1.17	$ 37,871

RSU Awards

A summary of RSUs outstanding as of September 30, 2021, and activity during the nine months ended, is presented below:

	Shares (In thousands)	Weighted-Average Grant Date Fair Value Per Share	Weighted-Average Remaining Contractual Term (In years)	Aggregate Intrinsic Value (In thousands)
Outstanding at January 1, 2021	1,518	$ 35.51		
Granted	262	$ 83.27		
Vested	(538)	$ 34.89		
Forfeited	(84)	$ 38.38		
Outstanding at September 30, 2021	1,158	$ 46.42	1.48	$ 114,544
Outstanding and expected to vest at September 30, 2021	1,081		1.43	$ 107,057

7. SIGNIFICANT CUSTOMERS AND GEOGRAPHIC NET REVENUES:

Segment Reporting

The Company is organized and operates as one reportable segment, the design, development, manufacture and marketing of integrated circuits and related components for use primarily in the high-voltage power-conversion market. The Company's chief operating decision maker, the Chief Executive Officer, reviews financial information presented on a consolidated basis for purposes of making operating decisions and assessing financial performance.

Customer Concentration

The Company's top ten customers accounted for approximately 76% and 79% of net revenues for the three and nine months ended September 30, 2021, respectively, and approximately 65% and 56%, respectively in the corresponding periods of 2020. A significant portion of these revenues are attributable to sales of the Company's products to distributors of electronic components. These distributors sell the Company's products to a broad, diverse range of end users, including original equipment manufacturers, or OEMs, and merchant power supply manufacturers. Sales to distributors were $127.3 million and $397.9 million in the three and nine months ended September 30, 2021, respectively, and $85.3 million and $256.1 million, respectively, for the corresponding periods of 2020. Direct sales to OEMs and power-supply manufacturers accounted for the remainder.

The following customers represented 10% or more of the Company's net revenues for the respective periods:

	Three Months Ended September 30,		Nine Months Ended September 30,	
Customer	**2021**	**2020**	**2021**	**2020**
Avnet	27 %	18 %	29 %	14 %
Honestar Technologies Co., Ltd.	15 %	14 %	17 %	*

* Total customer revenue was less than 10% of net revenues.

No other customers accounted for 10% or more of the Company's net revenues in the periods presented.

Concentration of Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash investments and trade receivables. The Company does not have any off-balance-sheet credit exposure related to its customers. As of September 30, 2021, and December 31, 2020, 84% and 90%, respectively, of accounts receivable were concentrated with the Company's top ten customers.

The following customers represented 10% or more of accounts receivable:

Customer	**September 30, 2021**	**December 31, 2020**
Avnet	40 %	50 %
Powertech Distribution Ltd.	*	10 %

* Total customer accounts receivable was less than 10% of accounts receivable.

No other customers accounted for 10% or more of the Company's accounts receivable in the periods presented.

Geographic Net Revenues

The Company markets its products globally through its sales personnel and a worldwide network of independent sales representatives and distributors. Geographic net revenues, based on "bill to" customer locations, for the three and nine months ended September 30, 2021 and 2020, were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands)	**2021**	**2020**	**2021**	**2020**
United States of America	$ 5,054	$ 2,380	$ 12,973	$ 8,028
Hong Kong/China	103,937	76,549	344,790	202,642
Taiwan	7,629	4,133	20,432	17,811
Korea	17,508	12,121	43,702	29,762
Western Europe (excluding Germany)	11,418	7,535	27,268	25,565
Japan	6,959	4,303	16,758	12,606
Germany	9,402	5,755	24,064	17,169
Other	14,869	8,353	40,636	24,042
Total net revenues	$ 176,776	$ 121,129	$ 530,623	$ 337,625

8. STOCKHOLDERS' EQUITY:

Common Stock Shares Outstanding

POWER INTEGRATIONS, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands)	**2021**	**2020**	**2021**	**2020**
Beginning balance	60,344	59,752	59,910	58,862
Common stock issued under employee stock plans	104	103	873	1,057
Repurchased	(120)	—	(455)	(64)
Ending balance	60,328	59,855	60,328	59,855

Common Stock Repurchases

As of December 31, 2020, the Company had $41.3 million remaining under its stock-repurchase program. In April 2021, the Company's board of directors authorized the use of an additional $50.0 million for the repurchase of the Company's common stock, with repurchases to be executed according to pre-defined price/volume guidelines. In the nine months ended September 30, 2021 the Company purchased approximately 455,000 shares for $36.2 million. As of September 30, 2021, the Company had $55.1 million remaining under its current repurchase program, which has no expiration date. In October 2021, the Company's board of directors authorized the use of an additional $50.0 million for the repurchase of the Company's common stock, with repurchases to be executed according to pre-defined price/volume guidelines. Authorization of future repurchase programs is at the discretion of the board of directors and will depend on the Company's financial condition, results of operations, capital requirements, business conditions and other factors.

Cash Dividends

In October 2019, the Company's board of directors declared four quarterly cash dividends of $0.095 per share to be paid to stockholders of record at the end of each quarter in 2020. In April 2020, the Company's board of directors raised the cash dividends with the declaration of three cash dividends of $0.105 per share (in lieu of the $0.095 per share previously announced in October 2019) to be paid to stockholders of record at the end of each of the second, third and fourth quarter in 2020. In July 2020, the Company's board of directors raised the cash dividends further with the declaration of two cash dividends of $0.11 per share (in lieu of the $0.105 per share announced in April 2020) to be paid to stockholders of record at the end of each of the third and fourth quarter in 2020.

In January 2021, the Company's board of directors raised the quarterly cash dividend by an additional $0.02 per share with the declaration of four cash dividends of $0.13 per share to be paid to stockholders of record at the end of each quarter in 2021. In October 2021, the Company's board of directors raised the quarterly cash dividend again with the declaration of five cash dividends of $0.15 per share (in lieu of the $0.13 per share announced in January 2021) to be paid to stockholders of record at the end of the fourth quarter in 2021 and at the end of each quarter in 2022.

For the three and nine months ended September 30, 2021 and 2020, cash dividends declared and paid were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands, except per share amounts)	**2021**	**2020**	**2021**	**2020**
Dividends declared and paid	$ 7,840	$ 6,582	$ 23,552	$ 18,497
Dividends declared per common share	$ 0.13	$ 0.11	$ 0.39	$ 0.31

9. EARNINGS PER SHARE:

Basic earnings per share are calculated by dividing net income by the weighted-average shares of common stock outstanding during the period. Diluted earnings per share are calculated by dividing net income by the weighted-average shares of common stock and dilutive common equivalent shares outstanding during the period. Dilutive common equivalent shares included in this calculation consist of dilutive shares issuable upon the assumed exercise of outstanding common stock options, the assumed vesting of outstanding restricted stock units, the assumed issuance of awards under the stock purchase plan and contingently issuable performance-based awards, as computed using the treasury stock method.

A summary of the earnings per share calculation is as follows:

(In thousands, except per share amounts)	Three Months Ended September 30, 2021	Three Months Ended September 30, 2020	Nine Months Ended September 30, 2021	Nine Months Ended September 30, 2020
Basic earnings per share:				
Net income	$ 42,034	$ 14,820	$ 123,713	$ 43,898
Weighted-average common shares	60,319	59,823	60,350	59,582
Basic earnings per share	$ 0.70	$ 0.25	$ 2.05	$ 0.74
Diluted earnings per share: (1)				
Net income	$ 42,034	$ 14,820	$ 123,713	$ 43,898
Weighted-average common shares	60,319	59,823	60,350	59,582
Effect of dilutive awards:				
Employee stock plans	1,044	1,029	1,116	1,086
Diluted weighted-average common shares	61,363	60,852	61,466	60,668
Diluted earnings per share	$ 0.69	$ 0.24	$ 2.01	$ 0.72

(1) The Company includes the shares underlying performance-based awards in the calculation of diluted earnings per share if the performance conditions have been satisfied as of the end of the reporting period and excludes such shares when the necessary conditions have not been met. The Company has excluded the shares underlying the outstanding performance-based awards in the 2021 and 2020 calculations as the shares were not contingently issuable as of the end of the reporting periods.

In the three and nine months ended September 30, 2021 and 2020, no stock awards were determined to be anti-dilutive and therefore excluded from the computation of diluted earnings per share.

10. PROVISION FOR INCOME TAXES:

Income-tax expense includes a provision for federal, state and foreign taxes based on the annual estimated effective tax rate applicable to the Company and its subsidiaries, adjusted for certain discrete items which are fully recognized in the period they occur. Accordingly, the interim effective tax rate may not be reflective of the annual estimated effective tax rate.

The Company’s effective tax rates for the three and nine months ended September 30, 2021, were 8.2% and 6.1%, respectively, and 5.1% and 6.4%, respectively, in the corresponding periods of 2020. In the three and nine months ended September 30, 2021 and 2020, the effective tax rate was lower than the statutory federal income-tax rate of 21% due to the geographic distribution of the Company’s world-wide earnings in lower-tax jurisdictions, federal research tax credits and the recognition of excess tax benefits related to share-based payments. Additionally, in the nine months ended September 30, 2021, the Company’s effective tax rate was favorably impacted by a discrete item associated with the release of an unrecognized tax benefit. These benefits were partially offset by foreign income subject to U.S. tax, known as global intangible low-taxed income. The Company’s primary jurisdiction where foreign earnings are derived is the Cayman Islands, which is a non-taxing jurisdiction. Income earned in other foreign jurisdictions was not material. The Company has not been granted any incentivized tax rates and does not operate under any tax holidays in any jurisdiction.

As of September 30, 2021, the Company maintained a valuation allowance on its California deferred tax assets, New Jersey deferred tax assets, and capital losses for federal purposes, and a valuation allowance with respect to its deferred tax assets relating to tax credits in Canada.

Determining the consolidated provision for income-tax expense, income-tax liabilities and deferred tax assets and liabilities involves judgment. The Company calculates and provides for income taxes in each of the tax jurisdictions in which it operates, which involves estimating current tax exposures as well as making judgments regarding the recoverability of deferred tax assets in each jurisdiction. The estimates used could differ from actual results, which may have a significant impact on operating results in future periods.

11. COMMITMENTS:

Supplier Agreements

Under the terms of the Company's wafer-supply agreements with Seiko Epson Corporation ("Epson"), and ROHM Lapis Semiconductor Co., Ltd. ("Lapis") the wafers purchased from these suppliers are priced in U.S. dollars, with mutual sharing of the impact of fluctuations in the exchange rate between the Japanese yen and the U.S. dollar on future purchases. Each year, the Company's management and these two suppliers review and negotiate future pricing; the negotiated pricing is denominated in U.S. dollars but is subject to contractual exchange rate provisions. The fluctuation in the exchange rate is shared equally between the Company and each of these suppliers on future purchases.

12. LEGAL PROCEEDINGS AND CONTINGENCIES:

From time to time in the ordinary course of business, the Company becomes involved in lawsuits, or customers and distributors may make claims against the Company. In accordance with ASC 450-10, *Contingencies*, the Company makes a provision for a liability when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated.

On April 1, 2016, Opticurrent, LLC filed a complaint against the Company in the United States District Court for the Eastern District of Texas alleging that the Company infringed one patent pertaining to transistor switch devices and seeking damages for the alleged infringement. The Company filed a motion to transfer the case to the Northern District of California, which the Court granted, and the case was assigned to a new judge in San Francisco following the transfer. On December 21, 2018, the Court granted the Company's challenge to Opticurrent's damages expert but denied the Company's motion for summary judgment. Following a trial in February 2019, a jury issued a finding of direct infringement by the Company but found that the Company did not induce infringement, and awarded Opticurrent damages of $6.7 million. The Company challenged those findings in post-trial proceedings, and the Court granted one of the Company's post-trial motions, reducing the damages award to $1.2 million. The Court of Appeals affirmed the original findings and the reduced damages award, but the Company believes Opticurrent made key disclaimers during reexamination proceedings after the original trial, giving rise to a motion to set aside the original judgment in view of a disclaimer, an issue that is currently on appeal to the Federal Circuit. Briefing and oral argument on the Company's appeal are completed, with a ruling expected in the coming months. The District Court has issued an order staying execution on the original judgment pending the Company's appeal, and the Federal Circuit rejected Opticurrent's challenge to the order staying execution pending appeal. As such, the Company continues to believe it has strong defenses, and intends to continue to vigorously defend itself against Opticurrent's claims.

On June 19, 2019, Opticurrent, LLC filed a follow-on lawsuit in the United States District Court for the Northern District of California accusing more of the Company's products of infringement and seeking damages for the alleged infringement of the same claim of the same patent asserted in the parties' prior litigation, as described above. Limited discovery has taken place, but proceedings are currently stayed for all but written discovery, and no schedule has yet been set for expert discovery, dispositive motions, or trial. The Company believes it has strong defenses, independent of the issue on appeal in the first case, and intends to vigorously defend itself against Opticurrent's claims, with appeals to follow if necessary.

On May 10, 2021, Opticurrent, LLC filed another follow-on lawsuit in the United States District Court for the Eastern District of Texas accusing one of the Company's customers of infringement based on the use of the Company's products and seeking damages for the alleged infringement of the same claim of the same patent asserted in the parties' prior litigation, as described above. The case is at the pleadings stage, and no schedule has been set for discovery, dispositive motions, or trial. The Company believes it has strong defenses, independent of the issue on appeal in the parties' first case, and intends to vigorously defend against Opticurrent's claims against the Company's technology, with appeals to follow if necessary.

On January 6, 2020, the Company filed a complaint against CogniPower LLC in the United States District Court for the District of Delaware for infringement of two of the Company's patents and seeking a declaration of non-infringement with respect to patents that CogniPower had charged the Company's customers with infringing, based on customer use of the Company's products. In response, CogniPower filed a motion to dismiss the Company's declaratory judgment claims on the basis that CogniPower had not threatened the Company directly with suit. That motion was granted, so CogniPower's claims for infringement initially went forward separately in their lawsuit against the Company's customers in the District of Delaware, but the Company filed a motion to intervene in that lawsuit and received a ruling allowing the Company to intervene in CogniPower's customer lawsuit on February 1, 2021. The Company believes it has strong claims and defenses, and intends to vigorously defend itself against CogniPower's claims against the Company's technology, with appeals to follow if necessary. Moreover, given the United States Patent and Trademark Office's institution of inter partes review (IPR) proceedings against every independent claim CogniPower asserted in the litigation, the parties have agreed to stay the associated District Court litigation pending resolution of the IPRs.

The Company is unable to predict the outcome of legal proceedings with certainty, and there can be no assurance that the Company will prevail in the above-mentioned unsettled litigations. These litigations, whether or not determined in the Company's favor or settled, will be costly and will divert the efforts and attention of the Company's management and technical personnel from normal business operations, potentially causing a material adverse effect on the business, financial condition and operating results. Currently, the Company is not able to estimate a loss or a range of loss for the ongoing litigation disclosed above, however adverse determinations in litigation could result in monetary losses, the loss of proprietary rights, subject the Company to significant liabilities, require the Company to seek licenses from third parties or prevent the Company from licensing the technology, any of which could have a material adverse effect on the Company's business, financial condition and operating results.

13. INDEMNIFICATIONS:

The Company sells products to its distributors under contracts, collectively referred to as Distributor Sales Agreements ("DSA"). Each DSA contains the relevant terms of the contractual arrangement with the distributor, and generally includes certain provisions for indemnifying the distributor against losses, expenses, and liabilities from damages that may be awarded against the distributor in the event the Company's products are found to infringe upon a patent, copyright, trademark, or other proprietary right of a third party ("Customer Indemnification"). The DSA generally limits the scope of and remedies for the Customer Indemnification obligations in a variety of industry-standard respects, including, but not limited to, limitations based on time and geography, and a right to replace an infringing product. The Company also, from time to time, has granted a specific indemnification right to individual customers.

The Company believes its internal development processes and other policies and practices limit its exposure related to such indemnifications. In addition, the Company requires its employees to sign a proprietary information and inventions agreement, which assigns the rights to its employees' development work to the Company. To date, the Company has not had to reimburse any of its distributors or customers for any losses related to these indemnifications and no material claims were outstanding as of September 30, 2021. For several reasons, including the lack of prior indemnification claims and the lack of a monetary liability limit for certain infringement cases, the Company cannot determine the maximum amount of potential future payments, if any, related to such indemnifications.

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

The following discussion and analysis of our financial condition and our results of operations should be read in conjunction with the condensed consolidated financial statements and the notes to those statements included elsewhere in this Quarterly Report on Form 10-Q, and with the consolidated financial statements and management's discussion and analysis of our financial condition and results of operations in our Annual Report on Form 10-K for the year ended December 31, 2020, filed with the SEC on February 5, 2021. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those contained in these forward-looking statements due to a number of factors, including those discussed under the caption "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2020, and in Part II, Item 1A - "Risk Factors" and elsewhere in this report. See also "Cautionary Note Regarding Forward-Looking Statements" at the beginning of this report.

Overview

We design, develop and market analog and mixed-signal integrated circuits (ICs) and other electronic components and circuitry used in high-voltage power conversion. Our products are used in power converters that convert electricity from a high-voltage source to the type of power required for a specified downstream use. In most cases, this conversion entails, among other functions, converting alternating current (AC) to direct current (DC) or vice versa, reducing or increasing the voltage, and regulating the output voltage and/or current according to the customer's specifications.

A large percentage of our products are ICs used in AC-DC power supplies, which convert the high-voltage AC from a wall outlet to the low-voltage DC required by most electronic devices. Power supplies incorporating our products are used with all manner of electronic products including mobile phones, computing and networking equipment, appliances, electronic utility meters, battery-powered tools, industrial controls, and "home-automation," or "internet of things" applications such as networked thermostats, power strips and security devices. We also supply high-voltage LED drivers, which are AC-DC ICs specifically designed for lighting applications that utilize light-emitting diodes, and motor-driver ICs addressing brushless DC (BLDC) motors used in refrigerators, HVAC systems, ceiling fans and other consumer-appliance and light commercial applications.

We also offer high-voltage gate drivers—either standalone ICs or circuit boards containing ICs, electrical isolation components and other circuitry—used to operate high-voltage switches such as insulated-gate bipolar transistors (IGBTs) and silicon-carbide (SiC) MOSFETs. These combinations of switches and drivers are used for power conversion in high-power applications (i.e., power levels ranging from a few kilowatts up to gigawatts) such as industrial motors, solar- and wind-power systems, electric vehicles (EVs) and high-voltage DC transmission systems.

Our products bring a number of important benefits to the power-conversion market compared with less advanced alternatives, including reduced component count and design complexity, smaller size, higher reliability and reduced time-to-market. Our products also reduce the energy consumption of power converters during normal use and in "standby" operation, when the end product is not in use. In addition to the environmental benefits of reduced energy usage, our energy-saving technologies provide a number of benefits to our customers; these include helping them meet the increasingly stringent efficiency standards now in effect for many electronic products, and enabling the elimination of bulky heatsinks used to dissipate heat produced by wasted electricity.

While the size of our addressable market fluctuates with changes in macroeconomic and industry conditions, the market has generally exhibited a modest growth rate over time as growth in the unit volume of power converters has been offset to a large degree by reductions in the average selling price of components in this market. Therefore, the growth of our business depends largely on increasing our penetration of the markets that we serve and on further expanding our addressable market. Our growth strategy includes the following elements:

- *Increase our penetration of the markets we serve.* We currently address AC-DC applications with power outputs up to approximately 500 watts, gate-driver applications ranging from a few kilowatts up to gigawatts, and motor-drive applications up to approximately 400 watts. Through our research and development efforts, we seek to introduce more advanced products for these markets offering higher levels of integration and performance compared to earlier products. We also continue to expand our sales and application-engineering staff and our network of distributors, as well as our offerings of technical documentation and design-support tools and services to help customers use our products. These tools and services include our PI Expert™ design software, which we offer free of charge, and our transformer-sample service.

Our market-penetration strategy also includes capitalizing on the importance of energy efficiency and renewable energy in the power conversion market. For example, our EcoSmart™ technology drastically reduces the amount of energy consumed by electronic products when they are not in use, helping our customers comply with regulations that seek to curb this so-called “standby” energy consumption. Also, our gate-driver products are critical components in energy-efficient DC motor drives, high-voltage DC transmission systems, solar and wind energy systems and electric transportation applications.

- *Increase the size of our addressable market.* Prior to 2010 our addressable market consisted of AC-DC applications with up to about 50 watts of output, a served available market (SAM) opportunity of approximately $1.5 billion. Since that time we have expanded our SAM to more than $4 billion through a variety of means. These include the introduction of products that enable us to address higher-power AC-DC applications (such as our Hiper™ product families), the introduction of LED-driver products, and our entry into the gate-driver market through the acquisition of CT-Concept Technologie AG in 2012. In 2016 we introduced the SCALE-iDriver™ family of ICs, broadening the range of gate-driver applications we can address, and in 2018 we introduced our BridgeSwitch™ motor-driver ICs, addressing BLDC motors, as described above. We have recently introduced a series of automotive-qualified versions of our products, including SCALE-iDriver, InnoSwitch™ and LinkSwitch™ ICs, targeting the EV market; we expect to introduce additional products targeting EVs in the future, and expect automotive applications to become a significant portion of our SAM over time.

  Also contributing to our SAM expansion has been the emergence of new applications within the power ranges that our products can address. For example, applications such as “smart” utility meters, battery-powered lawn equipment and bicycles, and USB power receptacles (often installed alongside traditional AC wall outlets) can incorporate our products. The increased use of electronic intelligence and connectivity in consumer appliances has also enhanced our SAM. Finally, we have enhanced our SAM through the development of new technologies that increase the value (and therefore the average selling prices) of our products. For example, our InnoSwitch™ ICs integrate circuitry from the secondary, or low-voltage, side of AC-DC power supplies, whereas earlier product families integrated circuitry only on the primary, or high-voltage side. In 2019, we began incorporating proprietary gallium-nitride (GaN) transistors in some products, enabling a higher level of energy efficiency than ICs with traditional silicon transistors.

  We intend to continue expanding our SAM in the years ahead through all of the means described above.

Our quarterly operating results are difficult to predict and subject to significant fluctuations. We plan our production and inventory levels based on internal forecasts of projected customer demand, which are highly unpredictable and can fluctuate substantially. Customers typically may cancel or reschedule orders on short notice without significant penalty and, conversely, often place orders with very short lead times to delivery. Also, external factors such as global economic conditions and supply-chain dynamics can cause our operating results to be volatile. In particular, the severe economic disruption caused by the global novel coronavirus pandemic (COVID-19) may affect the supply of and demand for our products and make our results more difficult to forecast. Furthermore, because our industry is intensely price-sensitive, our gross margin (gross profit divided by net revenues) is subject to change based on the relative pricing of solutions that compete with ours. Variations in product mix, end-market mix and customer mix can also cause our gross margin to fluctuate. Because we purchase a large percentage of our silicon wafers from foundries located in Japan, our gross margin is influenced by fluctuations in the exchange rate between the U.S. dollar and the Japanese yen. Changes in the prices of raw materials used in our products, such as copper and gold, can also affect our gross margin. Although our wafer fabrication and assembly operations are outsourced, as are most of our test operations, a portion of our production costs are fixed in nature. As a result, our unit costs and gross margin are impacted by the volume of units we produce.

Recent Results

Our net revenues were $176.8 million and $121.1 million for the three months ended September 30, 2021 and 2020, respectively, and $530.6 million and $337.6 million for the nine months ended September 30, 2021 and 2020, respectively. The increase in revenues reflects the strong demand conditions currently prevalent across the semiconductor industry, as well as market-share gains for our products in a broad range of applications including consumer appliances, advanced chargers for mobile devices such as smartphones, tablets and notebook computers and a range of industrial applications including home-and-building automation, electronic utility meters, battery-operated tools and broad-based industrial applications.

Our top ten customers, including distributors that resell to original equipment manufacturers, or OEMs, and merchant power supply manufacturers, accounted for 76% and 79% of net revenues in the three and nine months ended September 30, 2021, and 65% and 56% of net revenues in the corresponding periods of 2020. In the three and nine months ended September 30, 2021, two customers, distributors of our products, each accounted for more than 10% of our net revenues. These customers each accounted for more than 10% of our net revenues in the corresponding three-month period of 2020, while only one accounted for more than 10% in the corresponding nine-month period of 2020. International sales accounted for 97% and 98% of our net revenues in the three and nine months ended September 30, 2021, respectively, and 98% of our net revenues in each of the corresponding periods of 2020.

Our gross margin was 51.9% and 49.2% in the three months ended September 30, 2021 and 2020, respectively, and 50.4% and 50.2% in the nine months ended September 30, 2021 and 2020, respectively. Our gross margin increased in the three-month period due primarily to a favorable change in end-market mix, with a greater percentage of revenues coming from higher-margin end markets, as well as manufacturing efficiencies, partially offset by increased equipment-related charges. Our gross margin increased slightly in the nine-month period as manufacturing efficiencies were mostly offset by an unfavorable change in end-market mix and increased equipment-related expenses.

Total operating expenses were $46.1 million and $44.8 million for the three months ended September 30, 2021 and 2020, respectively, and $136.7 million and $126.8 million for the nine months ended September 30, 2021 and 2020, respectively. The increases in operating expenses for the three- and nine-month periods were due primarily to higher salary and related expenses driven by increased headcount and annual merit increases, higher stock-based compensation expense related to performance-based awards, as well as increased materials engineering and equipment-related expenses in support of our product development efforts.

COVID-19 Pandemic

The COVID-19 pandemic has disrupted everyday life and markets worldwide, and governments around the world have imposed restrictions aimed at controlling the spread of the virus, including shelter-in-place orders, travel restrictions, business shutdowns and border closures. Beginning March 16, 2020 our San Jose headquarters location was subject to a shelter-in-place order, under which most of our employees were required to work from home; other locations around the world have also been subject to such restrictions. With high employee-vaccination rates and an ease in restrictions, we have begun a phased reopening of our San Jose headquarters. Our employee health and well-being is a top priority. We are actively monitoring the situation and expect most employees to return to the office as restrictions are further lifted. Some of our employees in other locations around the world have also returned to the office under a phased reopening plan. We have implemented a variety of measures to protect the health and safety of our employees, including the provision of masks, gloves and sanitizers, social-distancing rules, and regular deep cleaning of our facilities.

While we have been able to conduct our day-to-day operations effectively in spite of the restrictions caused by the pandemic, the pandemic has caused disruptions in our supply chain. While our supply of wafers from our foundry partners has not been interrupted, government-mandated closures in China, Malaysia, Sri Lanka and the Philippines have caused temporary shutdowns at our assembly and test sub-contractors at various times. These disruptions have not materially affected our results due to a variety of mitigation measures including higher-than-normal inventories of wafers and finished goods in the early stages of the pandemic, safety stocks of certain key inputs, and multiple sources for components for most of our products. Although there are signs of improvement in many areas around the world, the potential for new lockdowns and other mitigation efforts to deal with an increase in infection rates in certain areas remains a key risk for our supply chain and the results of our business.

While the continuing pandemic brings a greater-than-normal level of uncertainty with respect to the demand for our products, we believe our business is fundamentally sound with strong, long-term growth prospects. We have increased headcount and intend to continue investing in research and development and other functions necessary to support our future growth. We also intend to continue our cash dividend and stock-repurchase programs; however, if the economy deteriorates or our business outlook changes, our board of directors may choose to suspend or alter these programs at its discretion. For additional discussion regarding COVID-19 business risks refer to Part I, Item 1A “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2020.

Critical Accounting Policies and Estimates

The preparation of financial statements and related disclosures in conformity with accounting principles generally accepted in the United States of America (“U.S. GAAP”) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. On an ongoing basis, we evaluate our estimates, including those listed below. We base our estimates on historical facts and various other assumptions that we believe to be reasonable at the time the estimates are made. Actual results could differ from those estimates.

Our critical accounting policies are as follows:

- revenue recognition; and
- income taxes.

Our critical accounting policies are important to the portrayal of our financial condition and results of operations, and require us to make judgments and estimates about matters that are inherently uncertain. There have been no material changes to our critical accounting policies and estimates disclosed in “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations - Critical Accounting Policies and Estimates” and Note 2, *Significant Accounting Policies and Recent Accounting Pronouncements*, in each case in our Annual Report on Form 10-K for the year ended December 31, 2020, filed with the SEC on February 5, 2021.

Results of Operations

The following table sets forth certain operating data as a percentage of net revenues for the periods indicated.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2021	**2020**	**2021**	**2020**
Net revenues	100.0 %	100.0 %	100.0 %	100.0 %
Cost of revenues	48.1	50.8	49.6	49.8
Gross profit	51.9	49.2	50.4	50.2
Operating expenses:				
Research and development	12.0	17.2	11.9	17.7
Sales and marketing	8.8	11.3	8.5	11.9
General and administrative	5.3	8.5	5.4	8.0
Total operating expenses	26.1	37.0	25.8	37.6
Income from operations	25.8	12.2	24.6	12.6
Other income	0.1	0.7	0.2	1.2
Income before income taxes	25.9	12.9	24.8	13.8
Provision for income taxes	2.1	0.7	1.5	0.9
Net income	23.8 %	12.2 %	23.3 %	12.9 %

Comparison of the Three and Nine Months Ended September 30, 2021 and 2020

Net revenues. Net revenues consist of revenues from product sales, which are calculated net of returns and allowances. Net revenues for the three and nine months ended September 30, 2021 were $176.8 million and $530.6 million, respectively, and $121.1 million and $337.6 million, respectively, for the corresponding periods of 2020.

The increase in revenues reflects the strong demand conditions currently prevalent across the semiconductor industry, as well as market-share gains for our products in a broad range of applications including consumer appliances, advanced chargers for mobile devices such as smartphones, tablets and notebook computers and a range of industrial applications including home-and-building automation, electronic utility meters, battery-operated tools and broad-based industrial applications.

Our revenue mix by end market for the three and nine months ended September 30, 2021 and 2020 was as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
End Market	**2021**	**2020**	**2021**	**2020**
Communications	25 %	32 %	33 %	28 %
Computer	11 %	9 %	9 %	6 %
Consumer	34 %	31 %	31 %	34 %
Industrial	30 %	28 %	27 %	32 %

International sales, consisting of sales outside of the United States of America based on "bill to" customer locations, were $171.7 million and $517.7 million in the three and nine months ended September 30, 2021, respectively, and $118.7 million and $329.6 million, respectively, in corresponding periods of 2020. Although power converters using our products are distributed to end markets worldwide, most are manufactured in Asia. As a result, sales to this region represented 80% and 83% of our net revenues in the three and nine months ended September 30, 2021, and 82% and 80%, respectively, in the corresponding periods of 2020. We expect international sales, and sales to the Asia region in particular, to continue to account for a large portion of our net revenues in the future.

Sales to distributors accounted for 72% and 75% in the three and nine months ended September 30, 2021, respectively, and 70% and 76%, respectively, in the corresponding periods of 2020. Direct sales to OEMs and power-supply manufacturers accounted for the remainder.

The following customers represented 10% or more of our net revenues for the respective periods:

	Three Months Ended September 30,		Nine Months Ended September 30,	
Customer	**2021**	**2020**	**2021**	**2020**
Avnet	27 %	18 %	29 %	14 %
Honestar Technologies Co., Ltd.	15 %	14 %	17 %	*

* Total customer revenue was less than 10% of net revenues.

No other customers accounted for 10% or more of our net revenues in these periods.

Gross profit. Gross profit is net revenues less cost of revenues. Our cost of revenues consists primarily of costs associated with the purchase of wafers from our contracted foundries, the assembly, packaging and testing of our products by sub-contractors, product testing performed in our own facilities, amortization of acquired intangible assets, and overhead associated with the management of our supply chain. Gross margin is gross profit divided by net revenues. The table below compares gross profit and gross margin for the three and nine months ended September 30, 2021 and 2020:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(dollars in millions)	**2021**	**2020**	**2021**	**2020**
Net revenues	$ 176.8	$ 121.1	$ 530.6	$ 337.6
Gross profit	$ 91.7	$ 59.6	$ 267.5	$ 169.6
Gross margin	51.9 %	49.2 %	50.4 %	50.2 %

Our gross margin increased in the three-month period due primarily to a favorable change in end-market mix, with a greater percentage of revenues coming from higher-margin end markets, as well as manufacturing efficiencies, partially offset by increased equipment-related expenses. Our gross margin increased slightly in the nine-month period as manufacturing efficiencies were mostly offset by an unfavorable change in end-market mix and increased equipment-related expenses.

Research and development expenses. Research and development ("R&D") expenses consist primarily of employee-related expenses, including stock-based compensation, and expensed material and facility costs associated with the development of new technologies and new products. We also record R&D expenses for prototype wafers related to new products until such products are released to production. The table below compares R&D expenses for the three and nine months ended September 30, 2021 and 2020:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(dollars in millions)	**2021**	**2020**	**2021**	**2020**
Net revenues	$ 176.8	$ 121.1	$ 530.6	$ 337.6
R&D expenses	$ 21.1	$ 20.9	$ 62.9	$ 59.8
Percentage of net revenues	12.0 %	17.2 %	11.9 %	17.7 %

R&D expenses increased for the three and nine months ended September 30, 2021, as compared to the corresponding periods of 2020, primarily due to higher salary and related expenses driven by increased headcount and annual merit increases, higher stock-based compensation expense related to performance-based awards and increased equipment-related expenses partially offset by lower outside-service expenses.

Sales and marketing expenses. Sales and marketing ("S&M") expenses consist primarily of employee-related expenses, including stock-based compensation, commissions to sales representatives, amortization of intangible assets and facilities expenses, including expenses associated with our regional sales and support offices. The table below compares S&M expenses for the three and nine months ended September 30, 2021 and 2020:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(dollars in millions)	**2021**	**2020**	**2021**	**2020**
Net revenues	$ 176.8	$ 121.1	$ 530.6	$ 337.6
Sales and marketing expenses	$ 15.6	$ 13.7	$ 45.0	$ 40.2
Percentage of net revenues	8.8 %	11.3 %	8.5 %	11.9 %

S&M expenses increased in the three and nine months ended September 30, 2021, as compared to the corresponding periods of 2020, due primarily to increased commission expense driven by increased sales, higher salary and related expenses stemming from annual merit increases, and higher stock-based compensation expense primarily related to performance-based awards.

General and administrative expenses. General and administrative ("G&A") expenses consist primarily of employee-related expenses, including stock-based compensation expenses, for administration, finance, human resources and general management, as well as consulting, professional services, legal and audit expenses. The table below compares G&A expenses for the three and nine months ended September 30, 2021 and 2020:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(dollars in millions)	**2021**	**2020**	**2021**	**2020**
Net revenues	$ 176.8	$ 121.1	$ 530.6	$ 337.6
G&A expenses	$ 9.4	$ 10.3	$ 28.8	$ 26.9
Percentage of net revenues	5.3 %	8.5 %	5.4 %	8.0 %

G&A expenses decreased for the three months ended September 30, 2021, as compared to the corresponding period of 2020, due to lower patent-litigation and bad-debt expenses. G&A expenses increased for the nine months ended September 30, 2021, as compared to the corresponding period of 2020, primarily due to higher stock-based compensation expense related to performance-based awards, partially offset by lower patent-litigation expenses.

Other income. Other income consists primarily of interest income earned on cash and cash equivalents, marketable securities and other investments, and the impact of foreign exchange gains or losses. The table below compares other income for the three and nine months ended September 30, 2021 and 2020:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(dollars in millions)	**2021**	**2020**	**2021**	**2020**
Net revenues	$ 176.8	$ 121.1	$ 530.6	$ 337.6
Other income	$ 0.2	$ 0.9	$ 1.0	$ 4.1
Percentage of net revenues	0.1 %	0.7 %	0.2 %	1.2 %

Other income decreased for the three and nine months ended September 30, 2021, as compared to the corresponding periods of 2020, due primarily to lower interest income, as lower yields on our cash and investments more than offset the impact of higher cash and investment balances.

Provision for income taxes. Provision for income taxes represents federal, state and foreign taxes. The table below compares income-tax expense for the three and nine months ended September 30, 2021 and 2020:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(dollars in millions)	**2021**	**2020**	**2021**	**2020**
Income before income taxes	$ 45.8	$ 15.6	$ 131.7	$ 46.9
Provision for income taxes	$ 3.8	$ 0.8	$ 8.0	$ 3.0
Effective tax rate	8.2 %	5.1 %	6.1 %	6.4 %

Income-tax expense includes a provision for federal, state and foreign taxes based on the annual estimated effective tax rate applicable to us and our subsidiaries, adjusted for certain discrete items which are fully recognized in the period in which they occur. Accordingly, the interim effective tax rate may not be reflective of the annual estimated effective tax rate.

Our effective tax rates for the three and nine months ended September 30, 2021 were 8.2% and 6.1%, respectively, and 5.1% and 6.4%, respectively, for the corresponding periods of 2020. The effective tax rate in these periods was lower than the statutory federal income-tax rate of 21% due to the geographic distribution of our world-wide earnings in lower-tax jurisdictions, the impact of federal research tax credits and the recognition of excess tax benefits related to share-based payments. Additionally, in the nine months ended September 30, 2021, our effective tax rate was favorably impacted by a discrete item associated with the release of an unrecognized tax benefit. These benefits were partially offset by U.S. tax on foreign income, known as global intangible low-taxed income. The primary jurisdiction from which our foreign earnings are derived is the Cayman Islands, which is a non-taxing jurisdiction. Income earned in other foreign jurisdictions was not material. We have not been granted any incentivized tax rates and do not operate under any tax holidays in any jurisdiction.

Liquidity and Capital Resources

As of September 30, 2021, we had $548.9 million in cash, cash equivalents and short-term marketable securities, an increase of approximately $99.7 million from $449.2 million as of December 31, 2020. As of September 30, 2021, we had working capital, defined as current assets less current liabilities, of $637.3 million, an increase of approximately $98.6 million from $538.7 million as of December 31, 2020.

We have a Credit Agreement with Wells Fargo Bank, National Association (the "Credit Agreement") that provides us with a $75.0 million revolving line of credit to use for general corporate purposes with a $20.0 million sub-limit for the issuance of standby and trade letters of credit. The Credit Agreement was amended on June 7, 2021, to provide an alternate borrowing rate as a replacement for LIBOR and extend the termination date from April 30, 2022, to June 7, 2026, with all other terms remaining the same. Our ability to borrow under the revolving line of credit is conditioned upon our compliance with specified covenants, including reporting and financial covenants, primarily a minimum liquidity measure and a debt to earnings ratio, with which we are currently in compliance. The Credit Agreement terminates on June 7, 2026; all advances under the revolving line of credit will become due on such date, or earlier in the event of a default. No advances were outstanding under the agreement as of September 30, 2021.

Cash From Operating Activities

Operating activities generated cash of $183.7 million in the nine months ended September 30, 2021. Net income for this period was $123.7 million; we also incurred non-cash stock-based compensation expense, depreciation and amortization of $27.3 million, $23.4 million and $2.7 million, respectively. Sources of cash also included an $11.1 million decrease in inventory reflecting strong demand for the period and a $6.6 million increase in accounts payable (excluding payables related to property and equipment) due to the timing of payments. These sources of cash were partially offset by a $6.2 million decrease in taxes payable and accrued liabilities, a $5.0 million increase in prepaid expenses and other assets, primarily due to prepaid income taxes, and a $3.0 million increase in accounts receivable due to increased customer shipments.

Operating activities generated cash of $79.3 million in the nine months ended September 30, 2020. Net income for this period was $43.9 million; we also incurred non-cash stock-based compensation expense, depreciation, amortization and deferred income taxes of $22.0 million, $17.1 million, $3.3 million and $0.1 million, respectively. Sources of cash also included an $6.4 million increase in accounts payable (excluding payables related to property and equipment) due primarily to the timing of payments and a $6.1 million decrease in prepaid expenses and other assets, primarily driven by taxes refunded. These sources of cash were partially offset by a $14.4 million increase in inventories in order to support the demand environment, a $5.3 million increase in accounts receivable due to the increase and timing of customer shipments and a $0.9 million decrease in taxes payable and accrued liabilities.

Cash From Investing Activities

Our investing activities in the nine months ended September 30, 2021, resulted in a $128.1 million net use of cash, primarily consisting of $97.8 million for the purchase of marketable securities, net of sales and maturities, and $30.3 million for purchases of property and equipment, primarily production-related machinery and equipment as well as construction of a new office building in Switzerland.

Our investing activities in the nine months ended September 30, 2020, resulted in a $14.5 million net use of cash, primarily consisting of $35.7 million for purchases of property and equipment, primarily production-related machinery and equipment as well as construction of our offices in Switzerland and Germany, partially offset by $20.9 million from sales and maturities of marketable securities, net of purchases.

Cash From Financing Activities

Our financing activities in the nine months ended September 30, 2021, resulted in a $52.0 million net use of cash, consisting of $36.2 million for the repurchase of our common stock and $23.5 million for the payment of dividends to stockholders, partially offset by $7.7 million from the issuance of common stock from the exercise of employee stock options and the issuance of shares through our employee stock purchase plan.

Our financing activities in the nine months ended September 30, 2020, resulted in an $11.5 million net use of cash, consisting of $18.5 million for the payment of dividends to stockholders and $2.6 million for the repurchase of our common stock. These uses of cash were offset in part by $9.7 million from the issuance of common stock from the exercise of employee stock options and the issuance of shares through our employee stock purchase plan.

Credit Agreement

On July 27, 2016, we entered into the Credit Agreement with Wells Fargo Bank, National Association that provides us with a $75.0 million revolving line of credit to use for general corporate purposes with a $20.0 million sub-limit for the issuance of standby and trade letters of credit. We amended the Credit Agreement on April 30, 2018, to extend the termination date from July 26, 2019, to April 30, 2022, with all other terms remaining the same. On June 7, 2021, we signed the second amendment to the Credit Agreement to provide an alternate borrowing rate as a replacement for LIBOR and extend the termination date from April 30, 2022, to June 7, 2026, with all other terms remaining the same. Our ability to borrow under the revolving line of credit is conditioned upon our compliance with specified covenants, including reporting and financial covenants, primarily a minimum liquidity measure and a debt to earnings ratio, with which we are currently in compliance. The Credit Agreement terminates on June 7, 2026; all advances under the revolving line of credit will become due on such date, or earlier in the event of a default. No advances were outstanding under the agreement as of September 30, 2021.

Dividends

In October 2019, our board of directors declared four quarterly cash dividends of $0.095 per share to be paid to stockholders of record at the end of each quarter in 2020. In April 2020, our board of directors raised the cash dividend with the declaration of three cash dividends of $0.105 per share (in lieu of the $0.095 per share previously announced in October 2019) to be paid to stockholders of record at the end of each of the second, third and fourth quarter in 2020. In July 2020, our board of directors raised the cash dividends further with the declaration of two cash dividends of $0.11 per share (in lieu of the $0.105 per share announced in April 2020) to be paid to stockholders of record at the end of each of the third and fourth quarter in 2020.

In January 2021, our board of directors raised the quarterly cash dividend by an additional $0.02 per share with the declaration of four cash dividends of $0.13 per share to be paid to stockholders of record at the end of each quarter in 2021. In October 2021, our board of directors raised the quarterly cash dividend again with the declaration of five cash dividends of $0.15 per share (in lieu of the $0.13 per share announced in January 2021) to be paid to stockholders of record at the end of the fourth quarter in 2021 and at the end of each quarter in 2022.

Dividends payouts of $7.8 million, $7.9 million and $7.8 million occurred on March 31, 2021, June 30, 2021 and September 30, 2021, respectively. The declaration of any future cash dividend is at the discretion of the board of directors and will depend on our financial condition, results of operations, capital requirements, business conditions and other factors, as well as a determination that cash dividends are in the best interests of our stockholders.

Stock Repurchases

As of December 31, 2020, we had approximately $41.3 million remaining under our stock-repurchasing program. In April 2021, our board of directors authorized the use of an additional $50.0 million for the repurchase of our common stock, with repurchases to be executed according to pre-defined price/volume guidelines. In the nine months ended September 30, 2021, we repurchased approximately 455,000 shares of our common stock for $36.2 million. As of September 30, 2021, we had approximately $55.1 million remaining under our stock-repurchase program, which has no expiration date. In October 2021, our board of directors authorized the use of an additional $50.0 million for the repurchase of our common stock, with repurchases to be executed according to pre-defined price/volume guidelines. Authorization of future repurchase programs is at the discretion of the board of directors and will depend on our financial condition, results of operations, capital requirements, business conditions and other factors.

Contractual Commitments

As of September 30, 2021 we had a contractual obligation related to income tax, which consisted primarily of unrecognized tax benefits of approximately $20.9 million. A portion of the tax obligation is classified as long-term income taxes payable and a portion is recorded in deferred tax assets in our condensed consolidated balance sheet.

As of September 30, 2021, there were no material changes in our contractual commitments from those reported in our Annual Report on Form 10-K for the year ended December 31, 2020.

Other Information

Our cash, cash equivalents and investment balances may change in future periods due to changes in our planned cash outlays, including changes in incremental costs such as direct and integration costs related to future acquisitions. Current U.S. tax laws generally allow companies to repatriate accumulated foreign earnings without incurring additional U.S. federal taxes. Accordingly, as of September 30, 2021, our worldwide cash and marketable securities are available to fund capital allocation needs, including capital and internal investments, acquisitions, stock repurchases and/or dividends without incurring additional U.S. federal income taxes.

If our operating results deteriorate in future periods, either as a result of a decrease in customer demand or pricing pressures from our customers or our competitors, or for other reasons, our ability to generate positive cash flow from operations may be jeopardized. In that case, we may be forced to use our cash, cash equivalents and short-term investments, use our current financing or seek additional financing from third parties to fund our operations. We believe that cash generated from operations, together with existing sources of liquidity, will satisfy our projected working capital and other cash requirements for at least the next 12 months.

Off-Balance-Sheet Arrangements

As of September 30, 2021, we did not have any off-balance-sheet arrangements or relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which are typically established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

Recent Accounting Pronouncements

Information with respect to this item may be found in Note 2, *Significant Accounting Policies and Recent Accounting Pronouncements,* in our Notes to Unaudited Condensed Consolidated Financial Statements included in Part I, Item 1, of this Quarterly Report on Form 10-Q, which information is incorporated herein by reference.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There has not been a material change in our exposure to foreign currency exchange and interest rate risks from that described in our Annual Report on Form 10-K for the year ended December 31, 2020.

Interest Rate Risk. Our exposure to market risk for changes in interest rates relates primarily to our investment portfolio. We consider cash invested in highly liquid financial instruments with a remaining maturity of three months or less at the date of purchase to be cash equivalents. Investments in highly liquid financial instruments with maturities greater than three months at the date of purchase are classified as short-term investments. We generally hold securities until maturity; however, they may be sold under certain circumstances, including, but not limited to, when necessary for the funding of acquisitions and other strategic investments, and therefore we classify our investment portfolio as available-for-sale. We invest in high-credit quality issuers and, by policy, limit the amount of credit exposure to any one issuer. As stated in our policy, we seek to ensure the safety and preservation of our invested principal funds by limiting default risk, market risk and reinvestment risk. We mitigate default risk by investing in safe and high-credit quality securities and by constantly positioning our portfolio to respond appropriately to a significant reduction in a credit rating of any investment issuer, guarantor or depository. Our portfolio includes only marketable securities with active secondary or resale markets to facilitate portfolio liquidity. At September 30, 2021, and December 31, 2020, we held primarily cash equivalents and short-term investments with fixed interest rates.

Our investment securities are subject to market interest rate risk and will vary in value as market interest rates fluctuate. We monitor our investments per our above-mentioned investment policy; therefore, if market interest rates were to increase or decrease by 10% from interest rates as of September 30, 2021, or December 31, 2020, the increase or decrease in the fair market value of our portfolio on these dates would not have been material. We monitor our investments for impairment on a periodic basis. Refer to Note 5, *Marketable Securities*, in our Notes to Unaudited Condensed Consolidated Financial Statements, for a tabular presentation of our available-for-sale investments and the expected maturity dates.

Foreign Currency Exchange Risk. As of September 30, 2021, our primary transactional currency was U.S. dollars; in addition, we hold cash in Swiss francs and euro. We maintain cash denominated in Swiss francs and euro to fund the operations of our Swiss subsidiary. The foreign exchange rate fluctuation between the U.S. dollar versus the Swiss franc and euro is recorded in other income in our condensed consolidated statements of income.

We have sales offices in various other foreign countries in which our expenses are denominated in the local currency, primarily Asia and Western Europe. Cash balances held in foreign countries are subject to local banking laws and may bear higher or lower risk than cash deposited in the United States. From time to time we may enter into foreign currency hedging contracts to hedge certain foreign currency transactions. As of September 30, 2021, and December 31, 2020, we did not have an open foreign currency hedge program utilizing foreign currency forward exchange contracts.

Two of our major suppliers, Epson and Lapis, have wafer supply agreements based in U.S. dollars; however, our agreements with Epson and Lapis also allow for mutual sharing of the impact of the exchange rate fluctuation between Japanese yen and the U.S. dollar on future purchases. Each year, our management and these two suppliers review and negotiate future pricing; the negotiated pricing is denominated in U.S. dollars but is subject to contractual exchange rate provisions. The fluctuation in the exchange rate is shared equally between us and each of these suppliers on future purchases. Nevertheless, as a result of these supplier agreements, our gross margin is influenced by fluctuations in the exchange rate between the U.S. dollar and the Japanese yen. All else being equal, a 10% change in the value of the U.S.

dollar compared to the Japanese yen would result in a corresponding change in our gross margin of approximately 1.0%; this sensitivity may increase or decrease depending on the percentage of our wafer supply that we purchase from some of our Japanese suppliers and could subject our gross profit and operating results to the potential for material fluctuations.

ITEM 4. CONTROLS AND PROCEDURES

Limitation on Effectiveness of Controls

Any control system, no matter how well designed and operated, can provide only reasonable assurance as to the tested objectives. The design of any control system is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions, regardless of how remote. The inherent limitations in any control system include the realities that judgments related to decision-making can be faulty, and that reduced effectiveness in controls can occur because of simple errors or mistakes. Due to the inherent limitations in a cost-effective control system, misstatements due to error may occur and may not be detected.

Evaluation of Disclosure Controls and Procedures

Management is required to evaluate our disclosure controls and procedures, as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the “Exchange Act”). Disclosure controls and procedures are controls and other procedures designed to provide reasonable assurance that information required to be disclosed in our reports filed under the Exchange Act, such as this Quarterly Report on Form 10-Q, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms. Disclosure controls and procedures include controls and procedures designed to provide reasonable assurance that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer as appropriate to allow timely decisions regarding required disclosure. Based on our management’s evaluation (with the participation of our principal executive officer and principal financial officer), our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) were effective as of the end of the period covered by this report.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting during the quarter ended September 30, 2021, that have materially affected or are reasonably likely to materially affect our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Information with respect to this item may be found in Note 12, *Legal Proceedings and Contingencies,* in our Notes to Unaudited Condensed Consolidated Financial Statements included in Part I, Item 1, of this Quarterly Report on Form 10-Q, which information is incorporated herein by reference.

ITEM 1A. RISK FACTORS

As of the date of this filing, the risk factors have not changed substantively from those disclosed in Part I Item 1A in our Annual Report on Form 10-K for the year ended December 31, 2020, which risk factors are incorporated by reference in this report.

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

As of December 31, 2020, we had approximately $41.3 million available for future repurchases to be executed according to predefined price/volume guidelines. In April 2021, our board of directors authorized the use of an additional $50.0 million for the repurchase of our common stock, which was announced on April 29, 2021.

In the nine months ended September 30, 2021, we repurchased approximately 455,000 of our shares for approximately $36.2 million. As of September 30, 2021, we had approximately $55.1 million remaining in our repurchase program, which has no expiration date. In October 2021, our board of directors authorized the use of an additional $50.0 million for the repurchase of our common stock, with repurchases to be executed according to pre-defined price/volume guidelines.

Issuer Purchases of Equity Securities

The following table summarizes repurchases of our common stock during the third quarter of fiscal 2021:

Period	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value that May Yet be Repurchased Under the Plans or Program (In millions)
July 1, 2021 to July 31, 2021	120,002	$ 81.54	120,002	$ 55.1
August 1, 2021 to August 31, 2021	—	—	—	$ 55.1
September 1, 2021 to September 30, 2021	—	—	—	$ 55.1
Total	120,002		120,002	

All of the shares repurchased were pursuant to our publicly announced repurchase program.

ITEM 6. EXHIBITS

EXHIBIT NUMBER	Exhibit Description	Incorporation by Reference				Filed Herewith
		Form	File Number	Exhibit/Other Reference	Filing Date	
3.1	Restated Certificate of Incorporation	10-K	000-23441	3.1	2/29/2012	
3.2	Amended and Restated Bylaws	8-K	000-23441	3.1	4/26/2013	
4.2	Reference is made to Exhibits 3.1 to 3.2					
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002					X
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002					X
32.1**	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002					X
32.2**	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002					X
101.INS	XBRL Instance Document - The instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document.					X
101.SCH	Inline XBRL Taxonomy Extension Schema Document					X
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document					X
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document					X
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase Document					X
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase Document					X
104	Cover Page Interactive Data File (formatted as inline XBRL and contained in Exhibit 101)					

All references in the table above to previously filed documents or descriptions are incorporating those documents and descriptions by reference thereto.

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† Portions of this exhibit (indicated by asterisks) have been omitted as being immaterial and is the type of information that Power Integrations, Inc. treats as private or confidential.

** The certifications attached as Exhibits 32.1 and 32.2 accompanying this Form 10-Q, are not deemed filed with the SEC, and are not to be incorporated by reference into any filing of Power Integrations, Inc. under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, whether made before or after the date of this Form 10-Q, irrespective of any general incorporation language contained in such filing.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

POWER INTEGRATIONS, INC.

Dated: October 28, 2021

By: /s/ SANDEEP NAYYAR

Sandeep Nayyar
Chief Financial Officer
(Duly Authorized Officer, Principal Financial Officer and Principal Accounting Officer)

Exhibit 31.1

CERTIFICATION OF CHIEF EXECUTIVE OFFICER

I, Balu Balakrishnan certify that:

1. I have reviewed this Form 10-Q of Power Integrations, Inc.;

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.

Dated: October 28, 2021

By: /s/ BALU BALAKRISHNAN

Balu Balakrishnan
Chief Executive Officer

Exhibit 31.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER

I, Sandeep Nayyar, certify that:

1. I have reviewed this Form 10-Q of Power Integrations, Inc.;

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.

Dated: October 28, 2021

By: /s/ SANDEEP NAYYAR

Sandeep Nayyar
Chief Financial Officer

Exhibit 32.1

CERTIFICATION OF CHIEF EXECUTIVE OFFICER

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

In connection with the Quarterly Report of Power Integrations, Inc. (the "Company") on Form 10-Q for the quarter ended September 30, 2021, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Balu Balakrishnan, Chief Executive Officer of the Company, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 ("Section 906"), certify to the best of my knowledge that:

(1) The Report fully complies with the requirements of Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: October 28, 2021

By: /s/ BALU BALAKRISHNAN

Balu Balakrishnan
Chief Executive Officer

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to the Registrant and will be retained by the Registrant and furnished to the Securities and Exchange Commission or its staff upon request.

Exhibit 32.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER

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

In connection with the Quarterly Report of Power Integrations, Inc. (the "Company") on Form 10-Q for the quarter ended September 30, 2021, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Sandeep Nayyar, Chief Financial Officer of the Company, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 ("Section 906"), certify to the best of my knowledge that:

(1) The Report fully complies with the requirements of Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: October 28, 2021

By: /s/ SANDEEP NAYYAR

Sandeep Nayyar
Chief Financial Officer

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to the Registrant and will be retained by the Registrant and furnished to the Securities and Exchange Commission or its staff upon request.